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## Youth unemployment in Kosovo and situation on the labor market before the declaration of Kosovo's independence

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Faculty of Business, Management and Economics

**Youth unemployment in Kosovo and situation on the labor market  
before the declaration of Kosovo's independence**

Bachelor Degree

Uran Zhubi

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Prishtinë



Faculty of Management, Business and Economics

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**Youth unemployment in Kosovo and situation on the labor market  
before the declaration of Kosovo's independence**

Supervisor: Prof. Dr. Edmond Hajrizi

September 2010

This thesis is submitted in partial fulfillment of the requirements for a  
Bachelor Degree

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## ABBREVIATIONS

CIS	Commonwealth of Independent States
ESI	European Stability Initiative
EU	European Union
FDI	Foreign Direct Investment
GDP	Gross Domestic Product
ILO	International Labor Organization
IMF	International Monetary Fund
IOM	International Organization for Migration
KEDP	Kosovo Education Development Program
KFOR	NATO-led Kosovo Force
MEST	Ministry of Education, Science and Technology in Kosovo
MLSW	Ministry of Labor and Social Welfare in Kosovo
MTI	Ministry of Trade and Industry
NATO	North Atlantic Treaty Organization
NGO	Non-government organization
OECD	Organization for Economic Cooperation and Development
PISG	Provisional Institutions of Self-Government
POE	Public owned enterprise
SAP	Stabilization and Association Process
SEE	South East Europe
SME	Small and Medium Sized Enterprises
SOE	State owned enterprise
SOK	Statistical Office of Kosovo
SRSG	Special Representative of the United Nations-Secretary General
STM	Stabilization and Association Process Tracking Mechanism
UN	United Nations
UNESCO	United Nations Educational, Scientific and Cultural Organization
UNMIK	United Nations Interim Administration Mission in Kosovo
UNSCR	United Nations Security Council Resolution 1244
USAID	United States Agency for International Development
WB	World Bank

## 1. INTRODUCTION

Youth employment-related issues became the number one problem for Kosovo and potentially a main destabilizing factor. In order to overcome the problem, it would be necessary to increase the number of jobs (Kosovo Outlook 2004, 2004, p. 11). High unemployment in general and high youth unemployment in particular have been one of the most pressing problems of Kosovo's economy. The youth unemployment rate in 2005 was alarmingly high at 70.5% and the overall unemployment rate was 41.4%, with both rates being some of the highest in Europe (Labor Market Statistics 2005, 2006, p. 3). In addition the ratio of youth unemployment to adult unemployment rate was 3.1 which further reveals the seriousness of the youth unemployment problem (Kolev, Saget, 2006, p. 13).

During the presentation by Kosovo's Ex- Prime Minister Agim Çeku at the Business Conference in Portoroz in 2006, I realized that in spite of United Nations' initiatives and others, the Kosovo economy is still very unstable. When searching for the reasons for this, the unemployment rate seemed alarmingly high. More than discovering the reasons for the present economic situation, I became interested in the reasons for the serious unemployment. Considering the many problems facing the labor market I will attempt to propose some ways to reduce unemployment there. Since youth unemployment is the most pressing problem, it will be studied more closely. The objective of the diploma paper is to outline the reasons for high unemployment in general and youth unemployment in particular and to try to evaluate whether certain further actions can help cut unemployment.

In my thesis I will use secondary sources that are mainly reports from international organizations since it is even difficult for them to acquire data. I also use information from two authentic Kosovo sources in Slovenia and one in Kosovo that have showed great deal of cooperation in both acquiring data and giving a critical view. Kosovo and especially the labor market has not yet been analysed much, therefore my diploma paper will contribute to the awareness of Kosovo's problems and propose some suggestions for solving them.

I start off with some facts about Kosovo, its population and the economic situation which is relevant for the further analysis of unemployment. Then i analyse the labor market and the reasons underlying unemployment in Kosovo and, based on that, propose some further steps for limiting unemployment. In the conclusion I present a short outline of the situation and some related proposals.

## 2. WHY THE INTEREST IN KOSOVO?

Kosovo is a province of 1.1 million hectares in the southern part of Serbia, bordering with Montenegro, Albania, and the Republic of Macedonia. The population of around two million is predominately Albanian with smaller populations of Serbs, Turks, Bosniaks, Romani people and other ethnic groups. Administration and economic activity is driven from the capital Prishtina.

### 2.1. Unique recent history

Kosovo was part of Yugoslavia when, during the 1989-1999 period, ethnic tensions emerged, resulting in an armed conflict in 1999. The international community intervened and ended the war on 10 June 1999 with the Serbian and Yugoslav governments signing the Kumanovo agreement to transfer governance of the province of Kosovo to the United Nations. Based on United Nations Security Council Resolution 1244 (UNSCR 1244) an interim civil administration was subsequently established and named the United Nations Mission in Kosovo ('UNMIK'), headed by a Special Representative of the United Nations-Secretary General ('SRSG'). In May 2001, the UNMIK announced the Constitutional Framework which established Kosovo's Provisional Institutions of Self-Government ('PISG'). Since 2001, the UNMIK has gradually been transferring ever more governing competencies to the PISG, while reserving some strategic powers (e.g., foreign affairs) (UNMIKonline, 2007).

In December 2003 'Standards for Kosovo' were published and endorsed by the UN Security Council (Standards for Kosovo, 2004, p. 2). The aim was to identify a series of standards and associated actions documented in the 'Kosovo Standards Implementation Plan' that were to be undertaken by the PISG and other institutions to realise a 'multi-ethnic, stable and democratic Kosovo, which is approaching European standards'. Progress in achieving these standards has been taken into consideration for the start of negotiations on Kosovo's final status.

In co-operation with the European Union ('EU') Kosovo participates in the Stabilisation and Association Process (SAP), the EU's policy framework regarding the Western Balkans, by following the guidelines of the European Partnership. The SAP steers Kosovo's reform process according to EU best practice and European legislation. The Partnership document outlines the main priorities that Kosovo needs to fulfill, thereby also taking into account the requirements of the Standards for Kosovo into account (Kosovo In October 2006, 2006, p.3).

An UN-led process in late 2005 initiated the determination of Kosovo's future status, namely whether the province should be independent or remain part of the state of Serbia. And 17<sup>th</sup> of February 2008 Kosovo declared independence. But in my diploma paper I will analyse unemployment and labor market before independence 2008.



## 2.2. The population of Kosovo

Kosovo's population has been ethnically diverse over the years and today predominately comprises Albanians with minority communities of Serbs, Turks, Bosniaks, Romani and other ethnic groups (Kosovo Report, 2006, p. 5). Estimates of the size of its population vary from 1.8 million to 2 million. The last population census was carried out in 1981 and revealed a population of 1,584,000; however, since then much migration has followed. An International Labor Organisation ('ILO') press release from 1999 noted that while it was extremely difficult to obtain reliable data, due to many official records proving either unreliable or data having been destroyed, the population of Kosovo in 1999 was estimated at some 1.8 to 1.9 million people, down from 2.3 million in 1997 (ILO Press Release, 1999). The population has been growing since 1999 and amounted to 2,100,000 Kosovars in 2007 (Statistical Office of Kosovo, 2007).

Detailed population figures are presented in Appendix 1.

During the 1990s huge distortions were observed in the demographic profile, due to the high level of migration. They reached their peak in 1997 and 1998 because of the armed conflicts that had occurred. The population in Kosovo has decreased by around 22% (see Appendix 1), while most of the emigrated people were 18 to 35 years old (ILO Press Release, 1999).

Kosovo has the youngest population in Europe. Over half of its people are under the age of 25, and about 21% of the population is between the ages of 15 and 25. UN and PISG standards consider people aged from 15 up to and including 24 as the young population.

**Table 1:** Structure of the population in Kosovo in 2002

Age range	Percent	Cumulative percent
0-6	12,6%	12,6%
7-14	17,5%	30,1%
15-18	9,0%	39,1%
19-24	12,4%	51,5%
25-30	11,4%	63,0%
31-40	13,6%	76,5%
41-50	9,5%	86,0%
51-60	7,2%	93,3%

61-64	2,0%	95,3%
65 and over	4,7%	100%
<b>Total</b>	100%	

Source: Labour market and unemployment in Kosova, 2003, p. 18.

### 2.3. Macroeconomic situation

Kosovo was always the poorest part of Yugoslavia. In 1988, for example, GDP per capita in Kosovo was just 67% of the average in Yugoslavia as a whole and just 44% of the average in Slovenia, the federation's richest region, and only 74% of the average of Serbia.

When Yugoslavia broke apart, Kosovo became even poorer; per capita income in 1995 was just 400USD (Domadenik, Mulaj, Redek, 2006, pp. 363-378).

With starting on the course of transition some profound institutional and structural changes associated with the economic transition – economic liberalisation, privatisation, hard budget constraints, the emergence of market competition and the disintegration of existing economic ties – led to a substantial drop in output. This gave rise to unemployment and a fall in labor force participation. After a decade of economic decay, impoverishment, the huge immigration of refugees and emigration of young qualified labor, increased investment risk as well as unfavorable economic, social and regional changes, the economy has gradually started to take off with the help of international intervention.

Kosovo has experienced a post-conflict boom, with positive economic growth being seen since 2000. The economic growth has been attributed to high levels of public and private sector investment. This has primarily been financed by official aid flows, amounting to EUR 1.96 billion during 1999-2003 alone, and remittances estimated at EUR 550 million per year. Kosovo adopted the euro as its domestic legal currency which has resulted in a stable exchange rate and low inflation levels (Kosovo Report, 2006, p. 4).

In 2006 real output grew by an estimated 3.8% (see Appendix 2). Interestingly enough, consumption as one of the four components of GDP since 2001 to date is higher than GDP itself. Imports are several times greater than exports causing a very large trade deficit which is currently running at around 44%. The main source of financing this economic paradox is foreign assistance and the remittances of Kosovo's emigrants that encourage production and investment in countries that export consumption goods to Kosovo (CBAK Annual Report, 2006, p. 16).

Foreign assistance and remittances have been decreasing since 2004, while in 2006 the level of foreign assistance dropped from 21% of GDP in 2005 to 18% in 2006 and private capital transfers were substantial (around 20% of GDP in 2006). Donor-financed investment shrank by 15% and, as a consequence, its share in total investment fell to 11% in 2006, down from 14% in 2005. On the contrary, private investment continued to grow at a brisk pace – by 32% in 2006, up from 24% in 2005 (Kosovo under UNSCR 1244 2007 Progress Report, 2007, pp. 25 - 27).

Foreign direct investment ('FDI') inflows, together with the accelerated privatisation activity, rose to around 10% of GDP in 2006 after a figure of just 3.5% in 2005.

Kosovo is facing a decline in donor support, weak economic growth, a fragile fiscal position, extensive poverty, environmental pollution and contamination, and pervasive governance problems. There is a clear need to develop new sources of economic growth for Kosovo and to ensure macroeconomic stability, particularly fiscal and external sustainability.

### 3. THE LABOR MARKET IN KOSOVO

It seems that Kosovo has already commenced and will further accelerate the implementation of comprehensive structural reforms, including fiscal reform, financial sector reform and the faster privatisation of public enterprises. These factors have had direct and indirect implications for the labor market<sup>1</sup>. There has been considerable interest in employment adjustment by firms during the transition in order for them to restructure from a relatively inflexible (centrally planned) mode to a more flexible (market) mode of operation which is a key element of the transition and employment adjustment (Svejnar, 1999, p. 8). The changed macroeconomic performance and household welfare highlight the need for a labor market study.

To identify the main problems and provide a broader context for the study, this chapter provides an overview of trends and outcomes in the Kosovo labor market. It describes trends in Kosovo labor market in general, analyses the education of the population, continues with migration and the sector-structure of supply and demand and concludes with some remarks about the labor market.

#### 3.1. Trends and the Kosovo labor market

To obtain a dynamic, all-encompassing picture of the Kosovo labor market, one should observe trends in labor force participation, unemployment and employment rates, as well as other indicators revealing the state of the labor market.

##### 3.1.1. Labor force participation rate

The indicator of the labor force participation rate plays a central role in the study of factors that determine the size and composition of a country's human resources and in making projections about the future supply of labor. The level and pattern of labor force participation depend on employment opportunities and the demand for income, which may differ from one category of persons to another (KILM 1: Labor force participation rate, 2007, p. 2).

##### **Box 1:** Labor force participation rate

**The labor force participation rate** is a measure of the proportion of a country's working age population that engages actively in the labor market, either by working or looking for work; it provides an indication of the relative size of the supply of labor available to be engaged in the production of goods and services.

Source: KILM 1: Labor force participation rate, 2007, pp. 2, 9.

<sup>1</sup> In abstract terms, a labor market may be said to be a relatively self-contained market where the factors determining the supply and demand of labor are common (Raines, 2000, p. 3). Labor markets function through the interaction of workers and employers or through labor suppliers (workers) and labor demanders (employers).

Kosovo's working age population (15-64 years) accounts for 63% of the entire Kosovo population. The labor force participation rate in 2005 was 49.2% (Labor Market Statistics 2005, 2006, p. 4), which is very low compared to the world level of 65.5% and the figure of 59% for Central and South-east Europe with CIS (KILM 1: Labor force participation rate, 2007, p.5). This shows that Kosovo is far from being a developed country because, at higher levels of development, the trend tends to reverse and labor force participation rates increase as employment opportunities for all grow. This also points to the province's scarce employment opportunities (KILM 1: Labor force participation rate, 2007, p. 10).

Occasionally low labor force participation rate indicate that large proportion of working age population is still in education and do not look for jobs. Given young population in Kosovo one would assume that this might be the reason, however later on it will be shown that is not the case.

### **3.1.2. Inactivity rate**

#### **Box 2: Inactivity rate**

Individuals are considered to be outside the labor force, or inactive, if they are neither employed nor unemployed, that is, not actively seeking work. There is a variety of reasons why some individuals do not participate in the labor force; such people may be occupied with caring for family members; they may be retired, sick or disabled or attending school; they may believe no jobs are available; or they may simply not want to work. The inactivity rate is the proportion of the working-age population that is not in the labor force.

Source: KILM 13: Inactivity rate, 2007, p. 2.

The inactivity rate in Kosovo was 50.9% in 2005. The reason for the high inactivity rate in Kosovo might be a subgroup of the inactive labor force that comprises those known as discouraged workers, defined as persons not in the labor force who are available for work but no longer looking for work because they think they will not find any. This is typically for personal reasons associated with their perception of the lack of jobs. Regardless of their reasons for being discouraged, these potential workers are generally considered underutilised.

The informal sector also contributes to the high inactivity rate as workers engaged in informal activities usually do not register as unemployed. Therefore, the increasing unemployment presented in the next chapter might be also due to the enforcement of laws to restrain the informal sector. In addition, while formally employed in SOEs some workers are actually working in the informal sector.

### 3.1.3. Unemployment rate

The unemployment rate is a key indicator of labor market conditions. The first reason for this is that the unemployment rate is an indicator of the overall health of an economy. High and persistent unemployment usually points to unresolved structural problems. Second, unemployment is very costly from both the individual and social perspectives. Job losses are associated with a loss of income and often lead to poverty. Prolonged unemployment leads to the erosion of skills and morale, and often to social marginalisation. To help the unemployed cope with joblessness the state provides income support and services intended to put the unemployed back into jobs. Such programmes are costly and raise the burden of taxation. Finally, high unemployment can be politically costly as in the opinion of voters the government is responsible for ensuring job opportunities and good employment prospects (Rutkowski, 2006, p. 19).

#### **Box 3:** Unemployment rate

The unemployment rate tells us the proportion of the labor force that does not have a job but is available and actively looking for work. The unemployment rate is mathematically defined as the quotient resulting from dividing the total number of unemployed (for a country or a specific group of workers) by the corresponding labor force, which itself is the sum of all employed and unemployed people in the group. It should be emphasised that it is the labor force or economically active portion of the population that serves as the basis for this statistic, not the total population.

Source: KILM 8: Unemployment, 2007, p. 2.

In spite of some economic growth, the unemployment rate in Kosovo was very high – 41.2% in 2005 (Labor Market Statistics 2005, 2006, p. 4) and ranked at the very top of unemployment rates in the region. The difference between males and females amounted to 28 percentage points (32.9% vs. 60.5%). In comparison, in recent years the world unemployment rate decreased from 6.6% in 2002 to 6.3% in 2006 and developed economies and the European Union also saw continuous declines in their unemployment rates over the last decade (KILM 8: Unemployment, 2007, p. 7). What is more, the trend in Kosovo runs in the opposite direction as the number of registered job-seekers continues to rise steadily. Measuring the unemployment rate is very difficult. Related figures of various organisations range from 30% to 70% as the unemployment rate depends on classifications, definitions, methodologies and others (Appendix 3: Different unemployment rates).

The latest Kosovo Progress Report issued in November 2007 stated that the number of registered unemployed persons at the end of 2006 had increased by 2.4% compared to 2005, and rose

further in 2007 (Kosovo under UNSCR 1244 2007 Progress Report, 2007, p. 5). According to the labor force survey, unemployment stood at 44.9% of the active labor force in 2006. Yet a large number of the registered unemployed may be active in the informal economy. Overall, registered unemployment remains high and has been growing steadily. However, partly due to the estimated size of the grey economy, registered unemployment does not yet systematically reflect the dynamics of the economy.

It must be said that the number of the registered unemployed is not an accurate indicator of unemployment as it is not unusual for individuals to register as unemployed in order to receive social benefits, even though they are working in the informal sector. On the other hand, according to the Ministry of Labor and Social Welfare ('MLSW') there are cases of individuals who fail to register as unemployed when jobless and looking for work. There is no estimate of the number of persons in either of the two groups (Kosovo under UNSCR 1244 2007 Progress Report, 2007, p. 5).

#### **3.1.4. Youth unemployment**

Young women and men are the world's greatest asset for the present and future, yet they also represent a group that is seriously vulnerable when it comes to employment. Youth unemployment is generally viewed as an important policy issue for many countries, regardless of their stage of development. A failure to successfully integrate young people into the labor market has broader consequences for the country at large.

#### **Box 4: Youth unemployment**

Youth unemployment indicator consists of four distinct measurements, with each representing a different aspect of the youth unemployment problem. The four measurements are: (a) the youth unemployment rate (youth unemployment as a percentage of the youth labor force); (b) the ratio of the youth unemployment rate to the adult unemployment rate; (c) youth unemployment as a proportion of total unemployment; and (d) youth unemployment as a proportion of the population of youth. The youth unemployment rate is defined as the proportion of the unemployed young population (15 to 24 years old) divided by the labor force in the same group.

Source: KILM 9: Youth unemployment, 2007, p. 1.

The youth currently constitute a quarter of the working-age population worldwide (Kolev, Saget, 2005, p. 13). According to estimates by the ILO (Youth, training and employment, 2004), the global unemployment rate for youth increased steadily from 11.7% in 1993 to 14.4% in 2003.

What is more, youth unemployment is an issue of concern for all transition countries.

Unemployment rates for those below 25 years of age in Balkan countries are routinely twice or even three times higher than those of the total working-age population, and range from 18% and

20.8% in Slovenia and Romania to 68.6% in the FYR Macedonia. In recent years unemployed youth have accounted for more than 50% of all unemployed in some countries (see Appendix 4). In Albania 58% of all registered unemployed are below 31 years of age, whereas in Croatia the rate is 53.9% of all unemployed (Labor market and unemployment in Kosova, 2003, p. 28).

When the transition process started in the early 1990s, it was thought that the high unemployment among young people was only a temporary problem. Later on, it was shown that this was related to the education, training and retraining systems at the national level, which were insufficient. Given the nature of the labor market and the time that any reform of an education and training system takes, youth unemployment became a serious problem and many young unemployed became long-term unemployed. The link between youth unemployment and social exclusion has been clearly established; an inability to find a job creates a sense of vulnerability, uselessness and idleness among young people and can heighten the attraction to get involved in illegal activities (Fares, Tiongson, 2007, p. 11).

The youth unemployment rate in Kosovo that was alarmingly high in 2005 (70.5%) can serve as a useful proxy for the health of the labor market vis-à-vis this group. Apparently youth labor market disadvantages that are defined as a lack of decent work, encompassing joblessness and the holding of low-quality jobs are strongly present in Kosovo. This is shown as the unequally distributed of unemployment with the ratio of the youth unemployment rate to the adult unemployment rate. In addition to the high youth unemployment rate, the proportion of youth unemployment in total unemployment is high. In response, employment policies might be usefully directed towards easing the entry of young people into the world of work.

**Table 2:** Selected indicators of youth unemployment in Kosovo

Indicator of youth unemployment	Value
Youth unemployment rate in 2005	70,5%
Teen (aged 15-19) unemployment rate	79,8%
Young adult (aged 20-24) unemployment rate	64,7%
Ratio of youth unemployment to adult unemployment	2.1 (3.1*)
Youth unemployment as a proportion of total unemployment	40,6 %
Youth unemployment as a proportion of the population of youth	n.a.

\* based on Living Standard Measurement Surveys ('LSMS') conducted September to December 2000 (published in Kolev, Saget, 2005, p.10).

Source: Kolev, Saget, 2005, p. 10.

Kosovo's economic reforms have not been directed enough at decreasing youth unemployment.



Besides unemployment, the emergence of large pools of jobless youth who do not even look for work is a worrying trend. Table 3 provides some recent evidence of youth discouragement and idleness in Kosovo. The proportion of jobless youth who do not report looking for work is particularly important and indicates that the grey economy seems to be widespread.

**Table 3:** Selected Indicators of Youth Discouragement and Idleness

Indicator of youth discouragement and idleness	Value
Share of youth neither in education nor in employment ( %)	46.0
Share of teenagers aged 15-19 not in education nor in employment ( %)	32.6
Share of teenagers aged 20-24 not in education nor in employment ( %)	57.7
Share of youth not in education nor in the labor force ( %)	38.4

Living Standard Measurement Surveys, conducted September – December 2000 (published in Kolev, Saget, 2005, p.15).

Source: Kolev, Saget, 2005, p. 15.

What is the most worrying is the large proportion (46%) of idle youths, as measured by the share of the population of youth that is not in school nor in employment. Further, the percentage of those youth is higher in the age class 20 to 24 years, which means that youth of that age mostly do not enroll or go to university which is hindering the possibility of getting a job. What is also remarkable is that a large majority of jobless and out-of-school youth (not in school nor in employment) were not looking for a job, which shows the share of youth not in education nor in the labor force (38.4%). Those young people who are neither in education nor in employment and even not looking for a job represent a group that warrants special attention. Often they are engaged in the grey economy which means they are not covered by satisfactory working conditions, occupational safety or benefits in case of illness, a job loss or retirement. There are also some who are at risk of becoming involved in the illicit economy, including the sex and drug industry.

Perhaps the most positive way youth have responded to poor labor market conditions in the region is by staying longer in education in order to delay their entry to the labor market and to increase their chances of finding a job. This will be examined in later on.

### 3.1.5. Employment-to-population ratio

The employment-to-population ratio provides information about the ability of an economy to create employment.

#### **Box 5:** Employment-to-population ratio

The employment-to-population ratio is defined as the proportion of a country's working-age population that is employed. Employment is defined in the resolution adopted by the 13th International Conference of Labor Statisticians ('ICLS') as persons above a specified age (15 years) who have performed any work at all in the reference period for pay or profit (or pay in kind), or who were temporarily absent from a job for reasons such as illness, maternity or parental leave, holiday, training or an industrial dispute.

Source: KILM 2: Employment-to-population ratio, 2007, p. 2.

The employment-to-population ratio in Kosovo in 2005 was 28.9%, which is low compared to the world's employment-to-population ratio that in 2006 amounted to 60.5%. A low ratio means that a large share of the population is not directly involved in market-related activities because they are either unemployed or (more likely) out of the labor force altogether. While almost 46% of Kosovo males of working age were actually employed in 2005, the applicable figure for females was about 12%, with the overall rate hovering around 29%. The overall data show that Kosovo has an insufficient ability to create employment (Labor Market Statistics 2005, 2006, p. 14).

### 3.1.6. Long-term unemployment

While short periods of joblessness are of less concern, especially when the unemployed persons involved are covered by unemployment insurance schemes or similar forms of support, prolonged periods of unemployment bring many undesirable effects, particularly a loss of income and diminishing employability. The indicator on long-term unemployment looks at the duration of unemployment, that is, the length of time an unemployed person has been without work and looking for a job.

#### **Box 6:** Long-term unemployment

Long-term unemployment covers all unemployed persons with continuous periods of unemployment extending for a year or longer (52 weeks and over). It is expressed as a percentage of the overall labor force (long-term unemployment rate) or of total unemployment (incidence of long-term unemployment).

Source: KILM 10: Long-term unemployment, p.2.

Reducing the duration of periods of unemployment is a key element of many strategies to reduce overall unemployment. Long-duration unemployment is undesirable, especially in circumstances where unemployment results from difficulties in matching supply and demand because of a demand deficiency. The longer someone is unemployed, the lower is their chance of finding a job.

Long-term unemployment as a proportion of total unemployment in Kosovo in 2005 was 87.9% (Labor Market Statistics 2005, 2006, p. 4). Almost one-third of the countries with available data show incidences of long-term unemployment of approximately 50% (KILM 10: Long-term unemployment, p. 4), in addition long-term unemployment in transition countries ranges from 50% to 70%. Moreover, the share of youth in total long-term unemployment in Kosovo is 43% (Kolev, Saget, 2005, p. 9). Usually long-term unemployment leads to poverty and social exclusion and these tend to further undermine future chances of finding work. A long duration of unemployment indicates a stagnant labor market in which chances to escape unemployment are limited. Information on the incidences of long-term unemployment among young people is urgently needed so that policy-makers can target the particularly vulnerable youth experiencing long-term unemployment and help them re-enter productive society (Global Employment Trends for Youth, 2004, p. 16).

### **3.2. The education and unemployment**

It can be safely stated that the high unemployment rate in Kosovo is largely attributable to the lack of opportunities and inadequate skills and education of the working-age population (Kosovo under UNSCR 1244 2007 Progress Report, 2007, p.5). Therefore, high unemployment rates can be related to the low educational enrolment rates, high drop-out rates and overall level of education. Econometric studies conducted in transition countries have revealed that less educated people have greater probabilities of being unemployed. This probability differs across and within countries but it seems that this tendency prevails in all countries and regions (Labor Market and Unemployment in Kosovo, 2003, p. 23). Kosovo is not an exception; as higher the education as higher the employment rate and as lower the unemployment rate. Table 4 (p. 17) shows that the employment rate for Kosovars who have a tertiary education is 61.8 percentage points higher than the employment rate for Kosovars who possess no education or an education up to primary school level. Further, in Appendix 5 we can observe the 12-month inflow and outflow labor force numbers by skills. They indicate that less people with a high school education registered as unemployed than those people with a high school education who got a job. This clearly indicates the need for urgent education in order to decrease unemployment.

**Table 4:** Employment and unemployment rates in Kosovo by education

Education	Employment rate (%)	Unemployed rate (%)
< Upper secondary	14,4	50,2
Upper secondary	38,1	43,4
tertiary	76,2	12,6

**<Upper secondary:** no school, 1-4 grades of elementary school, 5-7 grades of elementary school,

elementary school (completed); **upper secondary:** secondary school; **tertiary:** high-school, university, academy, master's and doctorate.

Source: Labour Market Statistics 2005, 2006, pp. 34, 35.

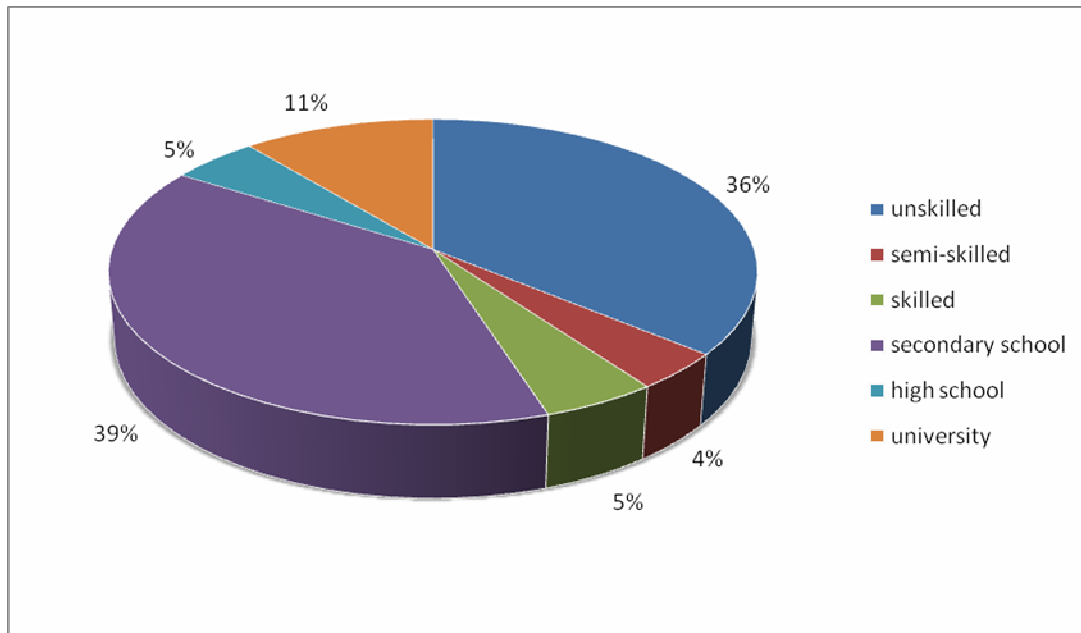
Enrolment levels at the compulsory level are relatively high. In 2003 more than 95% of the applicable age group population was enrolled in at least primary school (for a comparison the World Bank reported that in the EU the figure is 100%) and the number of the enrolled was increasing until school-year 2004/2005 and then dropped by 3.5% (Appendix 6) (Strategy for the Development of Preuniversity Education in Kosovo 2007-2017, 2006, p. 18). However, enrolment levels at the secondary level are much lower and especially low at the level of high education. Most European countries have secondary enrolment rates of between 85-95% but there are not enough data to calculate the secondary enrolment rate in Kosovo. Based on estimations it is between 45 to 55% .

There are many reasons for the decline in further education after compulsory schooling, including the difficult economic situation in general, the lack of motivation to learn, substandard learning conditions, the long distances from home to school in some areas, and traditional family customs (in the case of young women). With poor education being one of the reasons for youth unemployment a well-performing education system must therefore be in place. The education system's reform in Kosovo has been hindered by numerous complications. A rapid reduction of the donor support which previously financed education was not followed by an increase in support from the Kosovo Consolidated Budget. The lion's share of expenditure in the education system goes to salaries, which helps explain why the budget is more operational than sector developmental in nature (Kosovo Human Development Report, 2006 p. 39).

Data on vacancies by education or skills is needed to examine if the low education level is one of the reasons for the high youth unemployment. There is a high share of unemployed with a secondary school education. However, 39% of the total demand of all new vacancies from July 2005 until June 2006, similar to previous time periods, was addressed to the unemployed on the

secondary school skills-level, followed by the unskilled skills-level (Appendix 8) (Employment Promotion - Performance report 2005/2006, 2006, pp. 16, 17).

**Picture 1:** Proportion of vacancies offered by skills from 06/2005 to 05/2006 in Kosovo



Source: Employment Promotion - Performance report 2005/2006, 2006, p. 16.

### 3.3. Migration and its impact on the labor market

Throughout the 20<sup>th</sup> century rural Kosovo households survived and occasionally prospered by sending their men abroad as migrant laborers. They became construction workers, agricultural laborers or ice-cream vendors. In the socialist era men mainly migrated to Zagreb or Belgrade.

In the late 1960s, the migration route went further west, to serve the needs of growing European economies for ‘guest workers’. The remittances sent by these guest workers helped generate the cash the rural families needed. By the mid-1990s, it was estimated that as many as half a million Kosovars (20% to 25% of the total population) were living abroad, mainly in Germany and Switzerland, with smaller percentages in Austria and Sweden (Cutting the Lifeline, Migration, Families and the Future of Kosovo, 2006, p. 6).

In March 1992 the Kosovar ‘government in exile’ made the first effort to estimate the total number of Kosovo Albanians abroad, arriving at a figure of 217,000. The study located the largest communities in Germany (82,348), Switzerland (72,448), Sweden (15,652) and Austria (12,300). Germany and Switzerland remained the two most popular destinations for Kosovars throughout the 1990s (Cutting the Lifeline, Migration, Families and the Future of Kosovo, 2006, p. 8). Based on Labor market and unemployment in Kosova (2003, p.15) the estimates of those who had emigrated were around 450,000 Kosovars.

With NATO's intervention in 1999 and the end of the Serbian control of Kosovo, the toleration of Kosovar refugees and guest workers came to an end. More than 200,000 Kosovars were returned from Germany alone and as much as 77% of all those who returned home were from 16 to 64 years old and represented the working population. All of a sudden, Kosovo involuntarily began to re-import migrant laborers and its migration flows went into reverse. Not only was the economic lifeline that had kept rural Kosovo afloat cut but this created huge labor inflows which were too massive for Kosovo's destroyed economy (Cutting the Lifeline, Migration, Families and the Future of Kosovo, 2006, p. 9).

The return of these migrants was supported in the Standards for Kosovo by the need to achieve freedom of movement. Further objectives were established so that returnees to Kosovo could participate in the economy and job market without discrimination and limitations based on the freedom of movement (Standards for Kosovo, 2004, p. 9). The Standards also demand that health care, social services, education and public utilities be available to returnees on a level equal to that for the rest of the population, which encouraged returnees to come back to Kosovo.

In the last couple of years the return of emigrated Kosovars has had tremendous implications for youth unemployment, also in terms of major labor inflows. In addition, remittances have declined and I therefore expect this has provided a motivation for families to search for extra income. Logically young people have needed to search for jobs. The number of registered unemployed has increased yet it is difficult to claim that this is only a result of the decline in remittances and being forced to actively search for job as a substitute for the lower remittances.

From this point of view, the decline in remittances has had a positive effect of forcing youth to get a job. However, 46 % of youth is still not in education nor in employment (Table 3, p.14). Yet it is important to recognise another consequence of the labor migration. On the economic front, while lowly qualified migrants were usually forced to return to Kosovo the most educated were allowed to stay in their adopted new countries.

### **3.4. Sector-structure supply and demand in the labor market**

In this chapter I examine important labor market issues that have arisen during the transition from a centrally planned to a market economy. Economic liberalisation, privatisation, hard budget constraints, and the emergence of product market competition as well as the disintegration of existing economic ties brought major profound institutional and structural changes associated with the economic transition that led to a substantial drop in output, especially in the early stages. This gave rise to unemployment and a fall in labor force participation. Generally, in European transition economies the burden of restructuring led to 20% to 30% lower employment than before the transition (Rutkowski, 2006, pp. 3 and 4).

### **3.4.1. Restructuring the economy**

The removal of state subsidies and associated hardening of budget constraints as well as encountering new market-oriented principles pushed many state-owned enterprises to close down in the 1990s, including the mass shedding of labor. Based on that, large inflows of redundant workers jointly entered the labor market. In the public sector jobs were cut from 245,400 (1988) to 126,000 (2002), or by 52% (Labor market and unemployment in Kosova, 2003, p. 44). Job security was largely lost and, in addition, employers have increasingly turned to fixed-term or temporary employment contracts to facilitate their workforce adjustment. The proportion of regular secure jobs has gone down and this changing nature of jobs has been associated with growth of the informal sector, which by definition provides less protected jobs with fewer benefits. On top of this, many workers who lost (or were unable to find) employment turned to self-employment (Rutkowski, 2006, pp. 19, 20).

The extent of progress in enterprise restructuring affected labor market outcomes and explains some of the reasons for youth unemployment in most South-east European regions (Kosovo Economic Memorandum, 2004, p. 66). It is often believed that countries in the region which failed to restructure rapidly may have temporarily managed to preserve existing jobs and the welfare of senior workers, but often this may have been at the expense of young people who may find greater difficulty entering the labor market and who may thus constitute a disproportionately high share of the unemployed. In Kosovo labor restructuring problems are not of the same magnitude as those experienced elsewhere in Eastern Europe and the former Soviet Union. However, as mentioned the delays in SOE and POE restructuring mean that the issues of overstaffing in many of these remain to be addressed. At the same time, intensive restructuring is likely to generate large job reallocation and thus create structural unemployment that may affect youth and adults equally (Kosovo Economic Memorandum, 2004, p. 67).

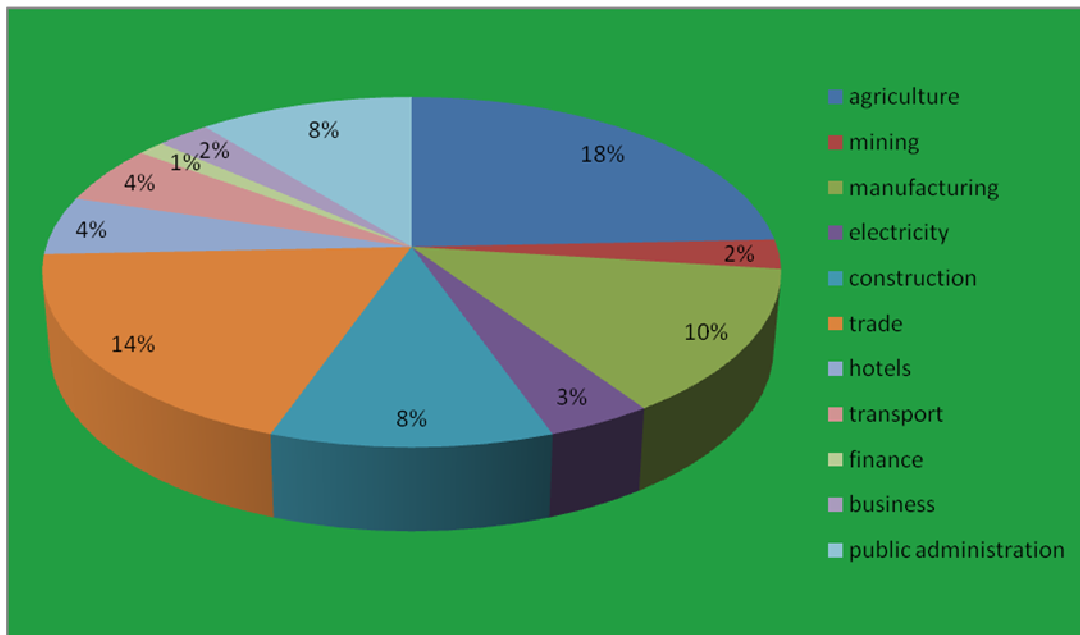
### **3.4.2. Labor adjustments to reflect the changed production structure**

Beside employment reductions in medium and large enterprises, another reason for the high unemployment is slow adjustment of labor to the changed production structure and the lack of mobility. The extent of unemployment due to structural shifts that caused structural imbalances can be analysed by unemployment by economic activity in a given time interval. In Appendix 9 the proportion of employment in enterprises by economic activity in 2002 and 2005 can be observed. In comparison to the pre-war years employment shifted away from manufacturing. In contrast to other sectors, employment in manufacturing fell by 20.4 percentage points. Moreover, according to official data (Labor Market Statistics 2005, 2006, p. 34) show that the three sectors with the highest proportion of employment were agriculture (18.8% of all employed), followed

by trade (13.8%) and education (10.8%) substituted manufacturing (35%) and electricity (22%) from 2002. These structural shifts are also some of the reasons for the high unemployment as people were used to becoming skilled for the traditional occupations. Youth were no exception. According to an authentic Kosovar, it has been perceived that a son should continue the occupation their father was qualified for. However, the companies that once existed have closed or been sold or some have even changed their production range for which other skills are required.

Evidence of structural shifts as one reason for both general and youth unemployment is given in Picture 2 (p. 22) where it can be observed that, due to the decrease in employment in manufacturing from 35% in 2002 to 9.6% in 2005, 29% of all unemployed had their last job in the manufacturing sector.

**Picture 2:** Unemployment by economic activity according to last job in 2005



Source: Labour Market Statistics 2005, 2006, p. 31

Nearly 70% of those employed work in the private sector – agriculture, trade, services and construction (Labor market and unemployment in Kosova, 2003, p. 38). Private business is also providing employment for those who lost their jobs in socially-owned enterprises (‘SOEs’) in the 1990s. This shows the aim of further developing of the private sector for which proposals will be given in chapter 5. Nevertheless, employment in SOEs and in government institutions still constitutes a significant part of total employment; together they account for 30% of total employment. What is interesting is that the UNMIK employs approximately 3,250 Kosovars and



mainly young ones who are flexible and can speak a foreign language, usually English (according to an anonymous Kosovo source).

### **Vacancies in the labor market**

Regarding the traditional classification of economic sectors, most vacancies offered in the 12 months up until June 2006 referred to the tertiary sector (services; 68%), followed by the secondary sector (production; 23%) and the primary sector (agriculture; 9%) (Employment Promotion – Performance Report 2005/2006, p. 15). In comparison to the 12-month results for 06/2005, both the primary and secondary sector showed an increasing share of all vacancies reported, while the share of all vacancies in the tertiary sector significantly decreased (by 9%).

Based on this, it can be perceived that youth needs to get qualified for the primary and secondary sector and it provides controversial evidence regarding education. In 3.2. it was shown that levels of education and unemployment are negatively correlated, which means that in the case of higher education one has fewer chances of being unemployed. However, Appendix 10 reveals that vacancies have increased in the primary and secondary sectors. Here we have to take into consideration the fact that the tertiary sector still dominates in vacancy demand and that there are less people educated to work in the tertiary sector and they have better chances of getting a job.

It also needs to be mentioned that some vacancies in agriculture and production on offer might be for educated Kosovars.

A look at the sectors regarding owners reveals a tremendous increase in 12-month cumulative private sector demand for new employees in recent years. 06/2006 compared to the 12-month results for 06/2005 shows the proportional share of private sector demand grew from 42% to 60%, while the cumulative labor demand of the private sector rose by almost 74%. Vice versa, public sector demand declined to 40%, representing a decrease of about -12% in the 12-month cumulative number of vacancies offered (Employment Promotion – Performance Report 2005/2006, p. 16).

### **3.4.3. Has privatisation influenced the labor market conditions?**

While there is growing evidence of the benefits of privatisation the unwillingness to privatise appears to be associated with a relatively negative perception of the privatisation process with respect to the labor force. A particular concern is that privatisation leads to layoffs and a worsening of labor conditions in divested firms (Ryan, 2002, p. 9). On the contrary, a survey by Brown and Earle (2006) shows the example of Hungary, Romania, Russia and Ukraine where privatisation has increased employment in all four countries and wages in three of them (Brown, Earle, 2006, pp. 13, 14). Privatisation can generate jobs.

The transition process in Kosovo resulted in mass job destruction and the low level of created new jobs despite the fact that some new owners were obliged to employ a certain amount of

workers. Consequently, privatisation resulted in modest sectoral changes and insignificant employment opportunities. In 2007 so far 3,500 new vacancies have been created due to privatisation (UNMIK Kosovo under UNSCR 1244 2007 Progress Report, 2007, p. 15). In addition to external shocks and low levels of FDI, the privatisation process did not contribute to job generation. As a result, low paid, low quality jobs in the informal economy have also been created together with low-skilled private sector jobs in manufacturing and agriculture. But the question remains: where can new jobs come from?

#### **3.4.4. The influence of Small and Medium Sized Enterprises on Labor Market Conditions**

Today, the small and medium sized enterprise (SME) sector is the main source of new-job generation and income growth and is a major force for growth and transformations into market economies. In all market economies, small and medium sized enterprises (SMEs) are a dynamic and active sector where significant capital is invested. SMEs promote economic development and as a result they contribute to employment growth and productivity improvement as well as the growth of gross domestic product (GDP). SMEs are particularly crucial for Kosovo since they have a strong economic impact (Peritt, 2004, pp. 11-13).

Currently Kosovo is undergoing a transitional period in which SMEs will play a crucial role in its economic reactivation and development and will be creating jobs that are missing due to the insufficiency of the privatisation process in terms of creating them. This can be illustrated by the fact that many family businesses have experienced a rapid recent expansion (especially in the trade sector). This is not due to favourable conditions and an appropriate enabling environment but is more a result of action taken by Kosovar employers in the sector, making small investments and turning capital around quickly to realise profits (The Status and Activity of Small and Medium Enterprises in Kosovo, 2005, p. 5)

In spite of the less than optimal enabling environment during the transition period, the SME sector has shown continual growth. At the end of 2003, 27,920 businesses were registered, of which 26,399 were sole traders or single owner businesses. By the end of 2004, this figure had increased to 39,257 and at the end of 2005 there were 65,051 registered businesses (The Status and Activity of Small and Medium Enterprises in Kosovo, 2005, p. 7). 18.3% of SMEs operate in the service sector, 32.2% in manufacturing and 49.5% in trade. Micro enterprises provide jobs for 68.9% of the entire employment of registered businesses, small enterprises provide jobs for 9.4% of the total employed in registered businesses, medium enterprises provide jobs for 6.4%, while large businesses employ 15.2% of the total employed in registered businesses. Micro enterprises make the biggest contribution to employment; however it is still unsatisfactory (The Status and Activity of Small and Medium Enterprises in Kosovo, 2005, p. 21). The largest number (98%) of private enterprises in Kosovo represent those that employ up to nine workers.

Those with 10-49 workers represent 1.7% of enterprises and those with 50 to 249 workers represent just 0.2% of enterprises. This demonstrates that micro-enterprises (i.e. those that employ 1-9 workers) are the main providers of employment in Kosovo and in the entire region.

A wide consensus has been reached between Kosovo institutions, the UNMIK and the international community that the stable economic development of Kosovo should be based on private sector development. In order to achieve SME development, the conditions for effective legal and institutional structures should be created to support the private sector. Although much effort has been made in this direction much remains to be done. The self-governmental institutions of Kosovo should pay particular attention to this. Completion of the legal system combined with institutional strengthening will encourage and contribute to the development and expansion of the SME sector (Kosovo under UNSCR 1244 2007 Progress Report, 2007, 2007, p. 14).

An important factor in the effective and efficient development of the private sector is the provision of financial resources from abroad. Currently in Kosovo there is a limited number of financial institutions and instruments. The SME financing system, in spite of huge effort, is still immature. Financing for SMEs remains a constant struggle. Currently there are seven licensed commercial banks operating in Kosovo. This has influenced the continual improvement of SME financing conditions as a result of the enhanced competition between commercial banks. Macroeconomic policy is a determining factor of an effective enabling environment for SMEs' development.

Is the growth in self-employment observed in transition economies a positive phenomenon? On the one hand, it is an indication of a developing entrepreneurial spirit, and a springboard to starting a small business. Self-employment can be a source of an 'entrepreneurship premium' and as such offer above-average earning opportunities. On the other hand, the growth in self-employment may be a symptom of a depressed labor market where firms create few jobs and employment opportunities are scarce (Rutkowski, 2006, p. 15), which is the case of Kosovo.

### **3.5. Remarks on Labor market**

The labor market in Kosovo has some distinctive characteristics compared to other transition countries. The population of Kosovo is one of the youngest in Europe: one-third is under 15 years of age and about half is under 25, representing the supply of youth available in the labor market and the huge inflows entering it every year when people turn 15. However, the youth unemployment rate is the highest in transition countries and so is the national employment rate.

What is even more daunting is the fact that the ratio of youth unemployment to adult unemployment is 3.1 which indicates the seriousness of the troubled employment opportunities.

After the conflict and beginning of United Nations' control over Kosovo the return of emigrant Kosovars followed and had tremendous implications for the labor market in terms of major labor inflows. Youth who also entered the labor market were faced with stiff competition for the rare vacancies on offer. Inflows into Kosovo's devastated economy have therefore been too massive. In addition, the low labor participation rate and high inactivity rate indicate serious problems for the economy as a whole that has failed to create job opportunities for the unemployed. Consequently, labor inflows are leading mostly toward the unemployment pool and there are considerable labor outflows from unemployment to inactivity.

After the conflict Kosovo entered a transition process. The main goal of this transition process was the restructuring of the economy aiming to increase the efficiency of production and the level of its competitiveness in the global economy. In this process the reallocation of production factors was mainly occurring through dislodgement from the state sector, which traditionally employ surplus labor in order to achieve certain long-run and macro-economic goals. The main negative effect of the transition process was unemployment due to the laying off of redundant workers as a consequence of economic restructuring<sup>2</sup>. The redundant workers ought to seek jobs in the newly emerging private sector (Bošković, Ognjanov, 2006, pp. 91 - 95).

In spite of some growth of private sector the generation of jobs is still not sufficient. In addition, the unemployed are also confronted with mismatch of the sector labor demand and their skills.

For example employment shifted away from manufacturing into service sector, mainly in trade and employment in manufacturing fell from 2002 to 2005 by 20.4 percentage points.

High unemployment rate in Kosovo is largely attributable to a lack of inadequate skills and education of the working age population and also lack of job opportunities. Moreover less educated people have higher probabilities of being unemployed which is also the case in Kosovo, where the majority (59 %) of all the unemployed are unskilled and possess no or poor education and according to the lowest vacancy-registration rate they have rare chances of getting a job.

What is more, difficult economic situation in general, lack of motivation to learn, substandard learning conditions, long distances from home to school in some areas, and traditional family customs contributed to failure of the youth to recognise that education enhance their chances of getting a job. They do not continue with education after compulsory education in the sufficient

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<sup>2</sup> Comparing the speed of disengaging redundant labor in the state sector and the speed of employment in the private sector led to the development of the well-known »optimal speed of transition« (OST) model in the transition literature (Aghion and Blanchard, 1994, pp. 283-320). But in answering the question of which factors are causing unemployment in transition and how it can be restrained more efficiently the new literature offers much more complex suggestions than the OST model did some ten years ago (Jovičić, 2006, pp. 49-51).

range. Above all 38.4 % of youth are not in education nor in the labor force which means that they remain idle.

General feature of the Kosovo's labor market is relatively flexible labor market. On average dynamic labor market might be understood as encourages businesses to create jobs and contribute to higher employment to population ratios. Therefore active and passive labor market policies are not relevant especially due to low level of offered jobs whatsoever (Fretwell, 2004, p. 4).

## 4. PROPOSALS

There is no other way to achieve relevant progress concerning Kosovo's employment situation than the substantial development of the Kosovo economy. In order to achieve this, Kosovo needs to economically transform from low-productivity activities to higher-productivity. This transformation can be achieved through investment, private sector development, improved education and a solid institutional framework. The government has the key role to play by ensuring that private sector development and investment not only remain on its agenda but also become the centerpiece of its programme. Many governments under the influence of the international policy community, often referred to as the Washington Consensus, have tried to boost efficiency in developing countries by pursuing a number of key reforms, including the privatisation of state-owned enterprises, stimulating the entry of new firms, encouraging foreign direct investment with the assistance of institutional development (Sabirianova, Svejnar and Terrell, 2005, p. 4). Kosovo lacks initiatives and sufficient capital to foster development. As discussed before, it is important for the development of the economy to cut unemployment. During the transition process jobs were destroyed and only limited new jobs were created, resulting in few job opportunities. In addition, Kosovo seems to lack initiatives to create new jobs so now I will make some relevant proposals.

The proposals to cut unemployment are divided into five groups. Job generation is the first group of proposals as a vital part of achieving higher employment. All other groups are correlated with job creation and a reduction of unemployment.

### 4.1. Job generation

#### **Proposal 1: Establishing strategically important sectors for job creation**

With the encouragement of several ministers (PISG) and under the supervision of international organisations (UNMIK) the revival of strategic sectors could create many job occupancies. Kosovo has abundant mineral deposits, low transport costs to Western European markets and fertile land, which are competitive advantages for the development of the energy, mining and agriculture sectors, which are believed to be the pillars of economic growth in Kosovo (Fuelling Kosovo's Growth Engines, 2005, p. 17). However, there is a lack of institutional capacity to attract and retain qualified, strategic investors. In addition, the revitalising of past strategically important sectors is considered not to be risky. Kosovo has a comparative advantage in both mining and energy which used to generate the majority of jobs that need to be revitalised and put back into business to generate more jobs.

### **Proposal 2: The encouragement of non-traditional sectors**

Discovering possible non-traditional sectors that could be relevant to Kosovo, such as IT technology, financial industry, tourism, should be one of the government's key roles. When identifying non-traditional sectors it needs to be noted that services have the highest added value and therefore the development of the service industry should be a priority.

### **Proposal 3: Development of the private sector by encouraging the establishment of SMEs**

The Kosovo Economic Memorandum recognised the development of the private sector in the South-east European region as the major factor contributing to job creation. Because of an apparent negative association between the share of services in total employment and youth unemployment further forms of encouragement should be introduced. Development in private sector would reduce unemployment, especially for youth, whose attitudes may be more oriented to the needs of the new private sector (Kosovo Economic Memorandum, 2004, p. 29). Small businesses are the key source of jobs, business dynamism and innovation for the European economy and they are one of the primary concerns of public policies in the context of the renewed Lisbon Strategy for Growth and Jobs. Stimulating the creation of new companies is the key to growth and job creation throughout Europe (European Charter for Small Enterprises, 2007, p. 7).

The Bologna Charter on SME Policies<sup>3</sup> is the most applicable for the economic situation Kosovo and serves as a basis for further proposals. The Bologna Charter recognised that entrepreneurship and a dynamic SME sector are important for restructuring economies and for combating poverty (Bologna Charter on SME Policies, 2000). There were 65,051 SMEs registered in Kosovo in 2004 (Ministry of Trade and Industry, 2005, p. 7) and they employed 79,057 people which is not nearly sufficient for the more than 600,000 Kosovars who make up the labor force.

Kosovo needs the equivalent of the American Small Business Administration with local offices, including Internet and paper publications with titles such as How to Start your Own Business (Perrit, 2004). The Bologna Charter on SME Policies recognises that for SME creation a regulatory environment that does not impose undue burdens on SMEs, education that fosters an innovative and entrepreneurial culture and effective access to financial services is essential.

### **Proposal 4: Fostering a favorable business environment**

It is generally believed that a favorable business environment is essential for the creation of SMEs and for combating Kosovo's widespread informal sector. According to the World Bank Investment Climate Assessment, the business environment in Kosovo is considered relatively favorable for SMEs. The tax system is simple and transparent and does not put a heavy burden

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<sup>3</sup> The Bologna Charter 2000 on SME Policies was adopted by representatives of 47 countries meeting under the sponsorship of the Organisation for Economic Co-operation and Development (OECD).

on enterprises with 15% VAT. In addition, basic economic legislation has been formulated and the institutional infrastructure has been created and is being maintained. Kosovo boasts relatively low red tape levels (bureaucracy), low regulatory requirements, no restrictive and costly labor rules and easy access to land (Fuelling Kosovo's Growth Engine, 2005, p. 15). In addition, during the last four years a range of new commercial laws has been promulgated, all of which are oriented to EU standards and new public and private institutions have been established to support implementation of these laws and this should be further encouraged.

**Proposition 5: Encouragement Kosovars for self-employment**

Particularly in circumstances where there are relatively few job opportunities, like in Kosovo, attention turns to initiatives designed to promote self-employment. ILO Recommendation no. 189 on Job Creation in Small and Medium Sized Enterprises suggests a series of measures to facilitate and improve the environment for small business start-ups to promote self-employment (Recommendation no. 189, 1998). The unemployed should be aware of the possibilities to start up a business by themselves. In order to achieve this, a special agency should provide training in business skills, consulting and matching with potential investors. Within specific countries Local Economic Development (LED) and SME promotion projects have been implemented in Bosnia & Herzegovina and Serbia & Montenegro and Kosovo should not be an exception (ILO, 1998).

**4.2. Development of education**

Inadequate education and skills are a crucial problem of employing Kosovo people in privatized and restructured enterprises. Even though young people are getting education, we have to take into consideration that even higher education would increase their employment opportunities.

**Proposition 1: Focusing on education**

Youth Employment Network's high-level panel recommendations suggest achieving employability by investing in education and vocational training for young people – and improving the impact of these investments (Global employment trends for youth, 2004, p. 5).

Kosovo's government introduced in 2005 the 'Platform of 3 Es' with Education as a key component. In 2005 the government allocated 4.3% (EUR 30.4 million) of Kosovo's budget to the Ministry of Education, Science and Technology; however, that includes expenditure on the ministry and all public workers (teachers). The governments' commitment is reflected in the 2007 budget where education funds increased by EUR 7 million. Government initiatives should be further extended (Kosovo Human Development Report 2006, 2007, p. 19).

**Proposal 2: The education system should be based on labor market needs**

The need to reform and improve the education systems arises so as to provide young people with skills which are useful once they leave school. The rapid industrial restructuring that ran parallel



to the transition also changed the demand for workers' education levels. The slowness of the education systems caused an insufficient adaptation to the rapid industrial change.

Kosovo's education system is not producing graduates with appropriate skills (Labor market and unemployment in Kosovo, 2003 p. 11) because educational programmes are based on past needs. More reforms based on demands of the labor market are a must. Further more education programmes need to be flexible to incorporate an assessment of labor market needs. There is a number of channels through which the harmonising of labor market demands and education may be achieved. On the one hand, the involvement of workers' and employers' organisations on local education boards is a step in the right direction. Here I would also propose scholarships for education programmes that are strategically important for Kosovo like university engineers, programmers and electrical engineers. Later on the involvement of all social partners in the development of curricula should be ensured. As O'Higgins (2004, p. 33) also proposed, at local levels where the policies are being implemented the social partners and workers' organisations in particular should be involved in adopting policies to local needs and their implementation. Indeed, the collaboration of employers' representatives is also encouraged by the ILO.

### **Proposal 3: Enhancing the quality of education**

In the 2002-2005 period, after the shift of responsibility to provide school infrastructure from various donors to local institutions and the local budget, the MEST financed the renovation of 39 school buildings in a total amount of EUR 1,793,001 and the construction of 28 new school facilities in the amount of EUR 8,192,425 (Strategy for the Development of Preuniversity Education in Kosovo 2007-2017, 2007, p. 15). After the education infrastructure has mainly been provided, Kosovo needs more teachers with up-to-date economics knowledge not only to be in charge of policy-making but also to create a critical mass of professors teaching in line with international standards. Based on that, resources need to be concentrated in a few of the most promising institutions in the country; these programmes could become models for other programmes throughout the country. Other important recommendations include supporting Internet access and upgrading libraries. The Open Society Institute has already greatly improved Internet connectivity in the region.

### **Proposal 4: Further co-operation in education with international organisations**

To encourage youth to either enrol or stay in school, international organisations provided huge financial injections for Kosovo's education system. The School Development Grant ('SDG'), based on the World Bank's Transitional Support Strategy<sup>4</sup> ('TSS'), was introduced to support

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<sup>4</sup> The World Bank prepared the Transitional Support Strategy (TSS) in 2002. The programme aimed to support postconflict reconstruction, economic recovery, poverty alleviation and human development, fiscal sustainability, good governance, peace-building and stabilisation of the region as part of a broader international effort led by the United Nations' Interim Administration Mission in Kosovo.

educational institution-building, reconstruction and financing. A project worth USD 4.5 million regarding improving education participation followed that focused on increasing educational enrolments, attendances, and retention at primary and secondary education levels by grants and enhancing the access of vulnerable groups to education.

A positive effect of foreign organisations' presence has led to the strong motivation of the local education leadership and administration. They made local educators and officers highly open and receptive to the new training programmes offered by foreign organisations. This in return boosted the effectiveness of education and training programmes and, at the same time, improved efficiency and management in education institutions in general. Training programmes in education leadership were initially organised and/or co-ordinated by the Canadian Kosovo Educator Development Programme ('KEDP'). To conclude, foreign organisations bring necessary improvements to education and further co-operation is essential.

#### **Proposal 5: Stressing the importance of MEST**

Immediately after the Ministry of Education, Science, and Technology (MEST) was established in 2002 a mixed working group consisting of local and international experts and officials was set up to start the process of drafting a short-term strategic plan for development of Kosovo's education system. This group produced the first strategic plan for moving Kosovar education from its emergency phase to consolidation phase and, at the same time, for retaining the unity of the system and foreseeing measures for its integration into relevant European education processes. They focused on the development of new curricula and on drafting new school textbooks for implementing the same subject curricula. However, in 2007 the system has not functioned as it should. I propose further engagement in the process of implementing the strategies. The government did allocate EUR 30.4 million to the MEST in 2005. However, more money should be spent on implementing strategies rather than on planning them.

#### **Proposal 6: Scholarships**

Scholarships are vital for young talented Kosovars to them to afford continuing their education at foreign, well-established universities. For example, in September 2007 11 young people from Kosovo were awarded European Commission funded scholarships to study master's degrees in European Studies at some of Europe's most prominent universities. However, Kosovo needs to be alert to limit any brain drain which would also represent a lost investment in education. Mainly scholarships should be made available to Kosovars to keep them in Kosovo and to enable them to receive a proper education (Quarterly report to the European Parliament, 2007)

#### **4.3. Further restructuring**

The transition in Kosovo resulted in major labor shedding and a slow pace of creating new jobs.

Since during the restructuring as much as 50% of all employees in SOEs and POEs lost their jobs a massive inflow into the labor market followed.

#### **Proposal 1: Continue with the special privatisation method**

In order to limit the termination of employees during the privatisation process, more SOEs should be privatised through the so-called special spin-off method which demands employment guarantees. According to this method, a new owner must employ a certain number of old and sometimes even new Kosovar people. The advantage of this method is that the ethnic structure of the region is taken into account to avoid discrimination. In addition to the generation of new jobs, this method also signals to Kosovo people that privatisation can be beneficial to them. This method was only used for 19 out of the 311 privatised SOEs because it is limited to large enterprises and strategic sectors; however, it should be noted that further encouragement of this method is necessary (Shala, 2007).

#### **Proposal 2: Preserve and generate jobs in high-tech sectors**

Although restructuring is necessary in Kosovo it needs to ensure the preserving of as many jobs as possible while at the same time generating new jobs for higher educated Kosovars. Restructuring also needs to be towards high-tech and value added enterprises that are able to compete with European ones. Doing this would also allow youth to get educated for such occupations and prevent a brain drain of those who are already educated. In 2005 there were 2,406 registered unemployed with a university education alone and 2,315 with a high school education, which indicates an adequate supply for newly privatised enterprises (Labour Market Statistics 2005, 2006, p. 31). Given that a lot of youth remains idle and many do not enrol at the unemployment office there seems to be enough human capital in Kosovo to take steps leading towards enterprise reform.

#### **4.4. Investment**

Kosovo's low domestic savings are insufficient to finance the required investment in restructuring (Kosovo: gearing policies towards growth and development, 2005, p. 14). Since Kosovo's own resources are insufficient, foreign direct investment ('FDI') should be attracted. As factor endowments-based trade theory argues that FDI is drawn to countries with lower wages and more abundant natural resources (Barrell, Pain, 1999, pp. 925-934) this makes Kosovo an investment opportunity. Also Mauro (1995, 681-712) argued that economic growth and job creation can be achieved through greater investment and higher educational attainment. The Washington Consensus also advocated FDI as a vehicle for this (Sabirianova, Svejnar and Terrell, 2005, p. 35).

### **Proposal 1: Recognising the need to attract FDI**

Kosovo's enterprises suffer from a lack of capital to finance investments to support a shift towards market-oriented enterprises (restructuring) and to purchase the new equipment required for high value-added production. FDI represents an alternative to Kosovo's financing of its development. In the transition economies of Central and Eastern Europe during the last ten years FDI had beneficial effects on prospects for sustainable development. The sharp growth in percapita GDP and labour productivity seen in countries like Poland, Hungary and Estonia has been driven by the large amounts of FDI that these countries have attracted. FDI is largely acknowledged as an engine of development, progress and a job creator (Foreign Direct Investment in Transition Economies: Challenges, Policies and Good Practices, 2003). Kosovo should follow the steps of the biggest FDI receivers and provide a favourable environment to attract investors.

### **Proposal 2: Creating an attractive environment for FDI**

Kosovo's environment has been hindering the activity of FDI mainly through its political instability. Much has already been done here and on 10 December 2007 the political status of Kosovo promises to be determined. Foreign investors, among others, face insufficient infrastructure, few opportunities for external financing, weak law enforcement, corruption, and disputes over property rights as well as problems with electricity distribution. In addition, disagreements between the PISG and UNMIK have undermined investors' confidence. Much effort needs to be channelled into removing these obstacles.

The government should promote the comparative advantages of Kosovo's economy that are attractive to FDI such as: the euro as the currency and a stable monetary policy, growth of the financial sector and the presence of foreign, well-established banks, the young population, developing border countries, export encouragement and an unsaturated market (Fuelling Kosovo's Growth Engine, 2005, p. 15).

### **Proposal 3: Efficiency Spillovers from FDI**

Foreign firms may bring efficiency and other 'spillover' effects that are broadly defined as the transfer of technology and managerial practices, production methods, marketing techniques or any other knowledge embodied in a product or service to local competition (horizontal spillovers) as well as to upstream and downstream domestic firms (vertical spillovers). A spillover may occur through a number of channels. Local firms may, for instance, learn to imitate a new process or improve the quality of their products or services through observation, or find better processes or marketing methods through interaction with foreign managers in business chambers or former employees. Local firms may also benefit from the entry of new professional services or suppliers. Foreign firms may act as catalysts for domestic suppliers to

improve quality or time efficiency by demanding higher standards (Gorodnichenko, Svejnar, Terrell, 2007, pp. 6, 7).

#### **Proposal 4: Prudent investment of remittances**

A large part of investment flows, especially remittances, has not been channeled into productive activities such as the rebuilding of destroyed infrastructure and trade and has been used for consumption instead of investment. The suggestion is that, despite the present trend of declining remittances, they should be invested in starting up new businesses to reduce unemployment, education and training.

#### **Proposal 5: An investment Fund for SMEs**

Around two-thirds of respondents in an opinion poll identified the lack of capital as a major obstacle to the creation and development of SMEs (The Status and Activity of Small and Medium Enterprises in Kosovo, 2005, p. 24). An investment fund is necessary to encourage this. Presently the pension fund cannot invest in new SMEs or in privatised SOEs because the risk is too high. On the contrary, an Investment Fund for SMEs could manage risk through diversification. An investment fund would perform three important economic functions: providing maturity intermediation; reducing risk through diversification; and reducing the costs of searching, contracting and information-processing associated with finding attractive investments, negotiating appropriate relationships and monitoring management.

An SME investment fund would also provide outside financing because SMEs are very reluctant to obtain financing from Kosovo's banks. The main problem of the banks is that the difference between the deposit and credit interest rate is around 10% and this is obviously too high to finance SMEs (CBAK Annual Report, 2006, p. 25).

#### **Proposal 6: Investing in manufacturing**

The manufacturing sector has been identified as a strategic engine of growth (Kosovo: gearing policies towards growth and development, 2005, p. 6). The traditional manufacturing sector (such as the production of construction materials) is not particularly mobile and so has much stronger ties with the domestic economy. 28.8% of all unemployed in 2005 were qualified to work in the manufacturing sector (Labor Market Statistics 2005, 2006, p. 31) so Kosovo should promote this sector to foreign investors as there is an available labor supply.

#### **Proposal 7: Investing in other sectors**

While the manufacturing sector usually has a certain primacy in the economy, other sectors also have a role to play in national competitiveness. Manufacturing activities require many inputs from the service sector. The agricultural sector provides inputs to the food and drink sub-sectors of manufacturing. The public sector is responsible for the provision of health, education and infrastructure, while fiscal policy has an impact on domestic demand through tax gathering and

expenditure programmes. Therefore, investment in other sectors is also vital. Sectors appealing to investors are telecommunications, as lately explored by Telekom Slovenia, the energy sector, transportation and tourism.

## 5. CONCLUSION

There is a range of challenges which the post-conflict Kosovo labor market has to accommodate. The labor market has yet to absorb the systemic changes associated with the transition to a market economy. Kosovo has one of the highest unemployment rates in CEE transition countries and the highest youth unemployment rate. It can be safely stated that the high unemployment rate in Kosovo is largely attributable to the lack of job opportunities and inadequate skills and education of the working-age population. The immediate cause of the high rates of unemployment is the small and sluggishly growing private sector. However the main constraint on the growth of the private sector is the quality of education and skills of Kosovo's labor force. The vast majority of the registered unemployed (59%) are classified as unskilled, while only 1% of the unemployed has a university degree. Consequently, education and vocational training policies ought to be at the core of Kosovo's development planning (Kosovo Economic Outlook 2007, 2007, pp. 5, 6).

Despite massive reconstruction assistance and humanitarian aid, economic output still lags well behind its pre-war levels and so does employment as a large share of employment has moved into the informal sector, and unemployment has been very high. As a result, labor force participation has been very low by international standards. Given these worrying facts, a thorough analysis of the labor market and its links with the economy is increasingly important and present in this diploma paper.

As the privatisation has not created enough jobs and even though the development of private sector did some still restructuring has caused major labor shedding. Consequently youth need to compete for few vacancies offered with all that lost their job due to restructuring. In addition due to return of Kosovo's migrants the situation got worse. Concerning education, youth need to accept that the higher education the possibility of finding a job. Kosovo needs to take more steps in order to achieve the job generation so desperately needed for reconstruction of the economy as a whole. First, strategically important sectors which would be the main job generators need to be identified. Then it should continue with establishing the non-strategically important sectors so as to set the economy as a whole in motion. What is probably the most important generator in all transition economies are micro, small and medium enterprises so their establishment should be widely addressed in Kosovo. Along with promotion and setting up an encouraging institutional environment for SMEs, financing needs to be made available in order to promote selfemployment among youth. If there are no jobs then young people need to generate them.

In addition, to drive privatisation and restructuring investments are needed and, as Kosovo does not have sufficient investment capabilities, attracting foreign investment is necessary. In doing

so a favourable environment for FDI has to be created and FDI has to be wisely channelled into those sectors and companies that hold the biggest potential for Kosovo's economy as a whole and for job generation in particular.

As enterprises are restructured privatised demand for a well-educated labor force will follow.

Kosovo needs to set education in general and its quality as one of the main objectives. Chances for youth to get jobs will thereby be enhanced. Education reforms need to be in tune with the European education system and in line with the economy. Kosovo's education system needs to produce workers with applicable knowledge for the newly restructured and privatized companies.

Kosovo has an opportunity to resolve all the problems it faces however steps must be cautiously taken so that its population can ultimately become same as citizens of the European Union.



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## Appendix 1: Population in Kosovo from 1981 to 2006

**Table 1:** Population in Kosovo from 1981 to 2006

Year	Population
1981(registration)	1,584,000**
1991(estimation)	1,982,000-2,030,000**
1997(estimation)	2,300,000*
1998(estimation)	1,800,000-1,900,000*
2001(estimation)	1,868,000***
2002(estimation)	1,900,000***
2003(estimation)	1,932,000***
2004(estimation)	1,965,000***
2005(estimation)	1,999,000***
2006(estimation)	2,100,000****

Source: \*ILO Press Release, 1999, \*\*Labour market and unemployment in Kosova, 2003, p. 11., \*\*\* Kosovo Report, 2006, p. 7., \*\*\*\*SOK, 2007.

## Appendix 2: Basic economic indicators from 2001 – 2005

**Table 2:** Basic economic indicators from 2001-2005

Economic indicator	2001	2002	2003	2004	2005	EU-25 (2005)
Population, total (1000)	1,868	1,900	1,932	1,965	1,999	459,488
Surface area (sq km )			11,000			3,975,043
Population density (No per sq km)	170	172	175.6	178.6	181.7	115.6
GDP (current Mio.Euro)	1,625	1,735	1,797	1,895	1,999	2,697,935
GDP per capita(current Euro)	870	913	930	964	1000	22,600
Exports of goods and services (% of GDP)	16.5%	12.51%	10.91%	10.66%	10.26%	9.3*
Real GDP development (growth rate)		1.2	3.1	3.2	1.7	1.6
Imports of goods and services (% of GDP)	75.38%	60.81%	55.82%	54.09%	52.28%	9.9*
Inflation, GDP deflator (annual %)	21.6	5.5	0.5	2.2	3.7	2.2

\*2004 data

Source: Kosovo Report, 2006, p. 4.

### Appendix 3: Different Unemployment Rates in Kosovo

Table 3: Different Unemployment Rates

Source	Reference year	Unemployment Rate
IOM 05/2000	2000	50 %
SOK 03/2004	2001	57%
UNDP 2002	2001	50-55 %
SOK 03/2004	2002	55 %
Riinvest 01/2003	2002	39-49 %
SOK 03/2004a	2003	53 %
SOK 2005	2003	50 %
UNDP 2004	2003	44 %
MLSW 03/2004	2003	43 %
SOK 2005a	2004	40 %
MLSW 03/2005	2004	42 %
MLSW 03/2006	2005	42-44 %

Source: Employment Promotion – Performance Report 2005/2006, 2006, 31 p.

### Appendix 4: Youth unemployment in Kosovo and other selected transition countries

Table 4: Youth unemployment in Kosovo and other transition countries

Country	National Unemployment rate	Youth Unemployment rate	Ratio of youth unemployment to adult unemployment rate	Share of unemployed youth to total unemployed (%)
Kosovo	49.0	71.6	3.1*	40.2
Bulgaria	14.1	32.6	2.5	23.5
Croatia	13.5	29.8	N/A	38.6
Romania	6.8	19.5	3.8	38.5
Czech Rep.	8.7	17.0	2.4	29.4
Hungary	7.0	12.4	2.1	27.6
Poland	12.5	30.0	2.9	26.4
Slovenia	7.4	18.2	3.1	31.1

N/A – not available

\* based on Living Standard Measurement Survey

Source: Riinvest 2003, p. 29; Kolev, Saget, 2005, p. 13



**Appendix 5:** Unemployment by skills in Kosovo in 2006**Table 5:** Unemployment by skills in Kosovo in 2006

Skills	ISCED	Registered unemployed	% of all unemployed	12 month inflow	12 month outflow	Inflow-outflow
Unskilled	0-2	191893	59.3	15744	9078	6666
Semi-skilled	3	13636	4.2	1000	471	529
Skilled	3a	29229	9.0	2385	1367	1018
Secondary school	3c	83943	26.	11196	8096	3100
High school	4	2315	0.7	378	460	-82
University	5a+	2406	0.7	921	683	238

**International Standard Classification of Education (ISCED Classification)**

Skill Groups (proprietary educational classification / old):

- Unskilled (ISCED 1 or 2): No school, not completed elementary school.
- Semi-skilled (ISCED 3): Elementary school completed, 3-6 months in-service training.
- Skilled (ISCED 3A): 2nd. School not completed, 3-6 months technical training.
- Secondary school (ISCED 3C): 2nd. School completed, 4 years tech. gymnasium.
- High School (ISCED 4): Not completed university, engineer graduation.
- University (ISCED 5A or 6): completed faculty, graduates, post-graduates.

Source: Employment promotion, Performance report 2005/2006, p. 10, own calculations

**Appendix 6:** Number of students in Kosovo in pre-university education by year**Table 6:** Number of students in Kosovo in pre-university education by year

Education level	Number of students for each school year			
	2001/2002	2002/2003	2003/2004	2004/2005
Mandatory	307,517	315,089	339,680	327,618
Secondary	93,502	86,830	72,635	70,183
Total	401,019	401,919	412,315	397,801

Source: Strategy for the Development of Preuniversity Education in Kosovo 2007-2017, 2006, p.19.

**Appendix 7:** Vacancies offered from July 2005 to June 2006 in Kosovo by skills

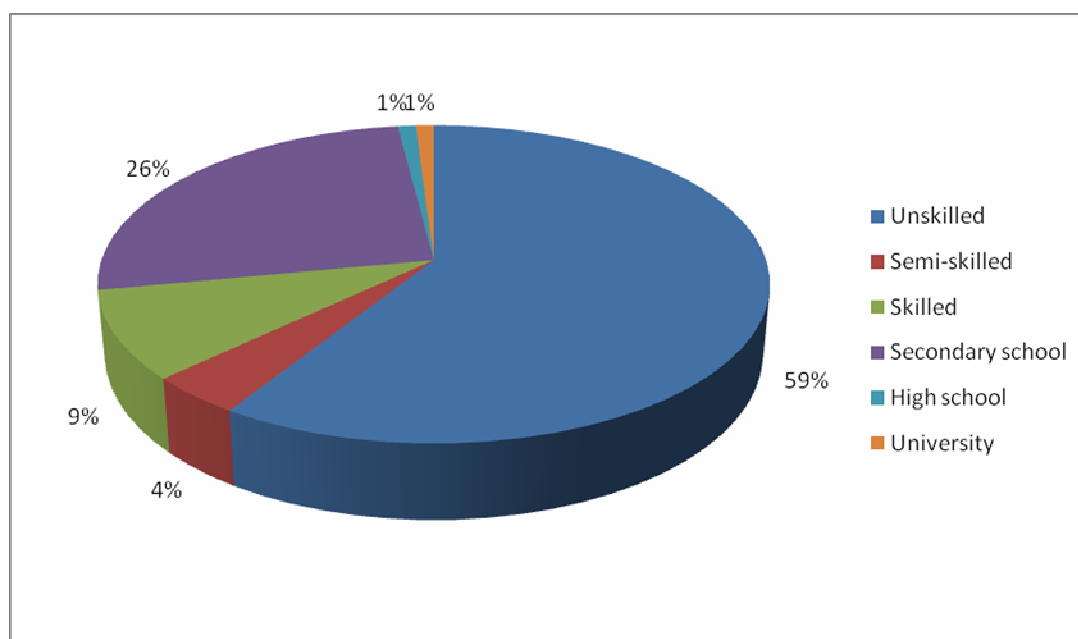
**Table 7:** Vacancies offered from July 2005 to July 2006

Skills	ISCED	Comulated vacancies	% of all Vacancies offered	Registered unemployed	% of all unemployed	VRR 06/2006
Unskilled	0-2	3260	36%	191893	59.3	1,7%
Semi-skilled	3	364	4%	13636	4.2	2,7%
Skilled	3a	467	5%	29229	9.0	1,6%
Secondary school	3c	3521	39%	83943	26.0	4,2%
High school	4	449	5%	2315	0.7	19,4%
University	5a+	983	11%	2406	0.7	40,8%
Total		9044	100%	323422		2,8%

Source: Performance report 2005/2006, 2006, p. 15.

**Appendix 8:** Proportion of registered unemployed from 06/2005 to 06/2006

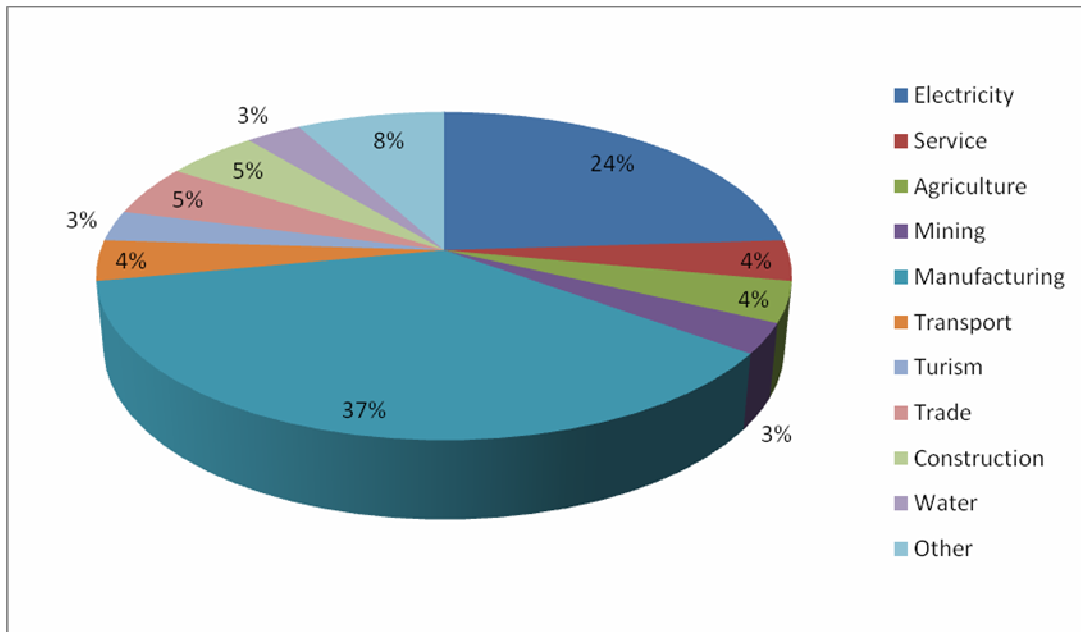
**Picture 1:** Proportion of registered unemployed from 06/2005 to 06/2006



Source: Employment promotion - Performance report 2005/2006, 2006, p. 10, own calculations

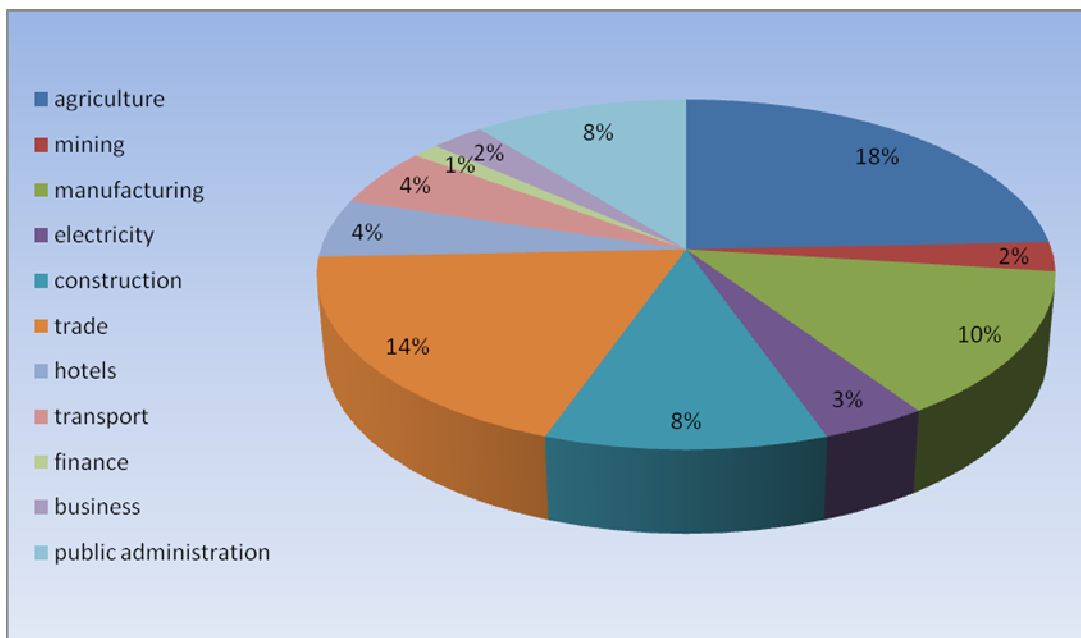
**Appendix 9:** Employment in enterprises by economic activity in 2002 and 2005

**Picture 2:** Employment in enterprises by economic activity in 2002



Source: Research on the General Data for Socially Owned Enterprises, 2002, p. 10.

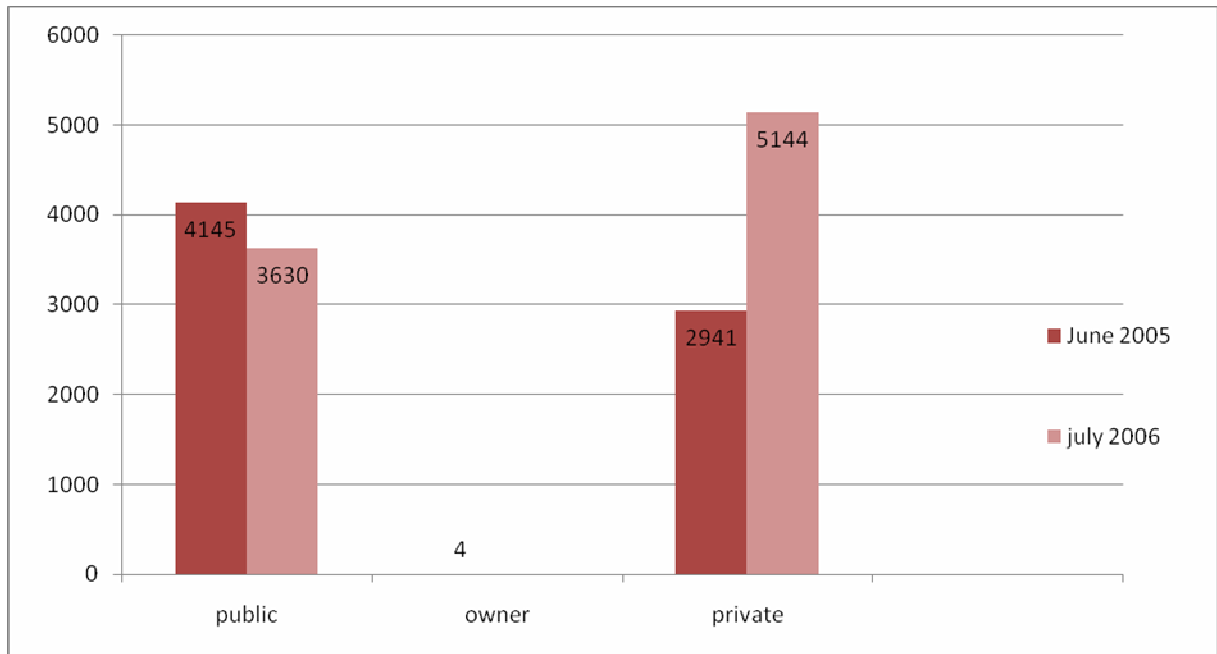
**Picture 3:** Employment in enterprises by economic activity in 2005



Source: Labour Market Statistics 2005, 2006, p. 30.

**Appendix 10:** Months cumulated vacancies by owner in 2005 and 2006

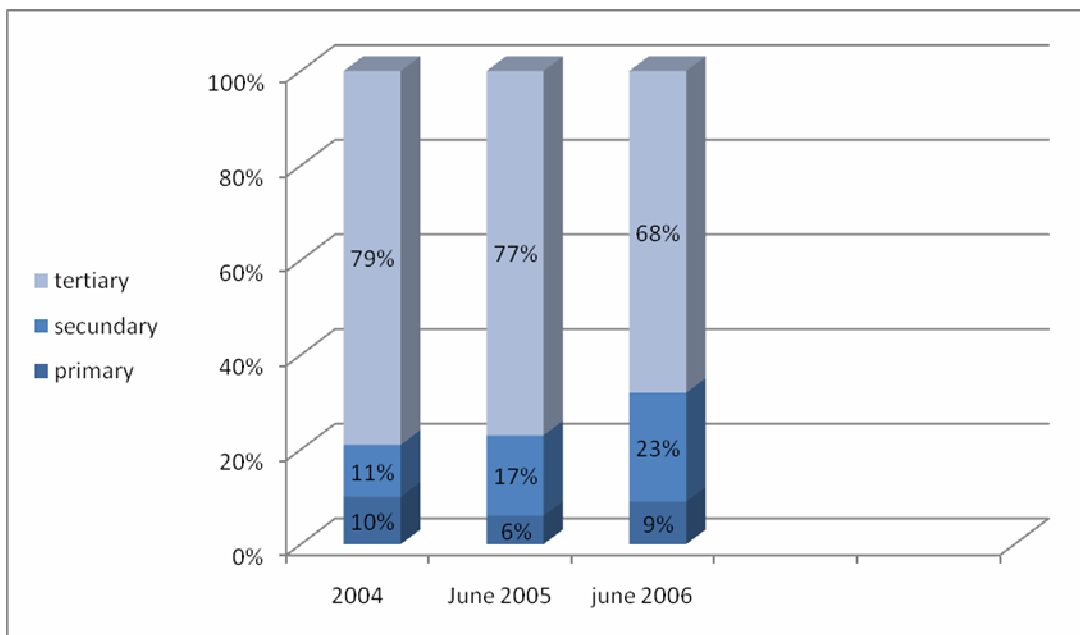
**Picture 4:** Number of vacancies offered in public and private sector in 2005 and 2006



Source: Employment Promotion – Performance Report 2005/2006, p. 16.

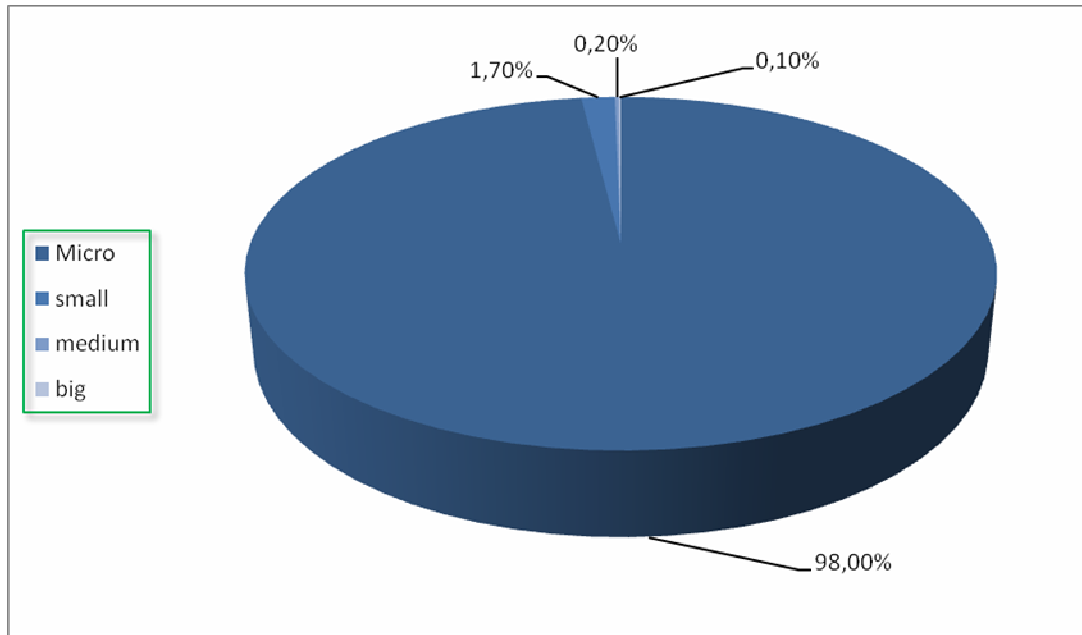
**Appendix 11:** Vacancies offered by sector in 2004, 2005 and 2006

**Picture 5:** Vacancies offered by sector in 2004, 2005 and 2006



Source: Employment Promotion – Performance Report 2005/2006, p. 15.

**Appendix 12:** Enterprise structure according to their size in Kosovo in 2004  
**Picture 6:** Enterprise structure according to their size in Kosovo in 2004



Source: Observatory of SME-s: The Status and Activity of Small and Medium Enterprises in Kosovo, 2005, p. 11.