



## CONGRESSIONAL NOTIFICATION TRANSMITTAL SHEET

We wish to notify you that the Millennium Challenge Corporation (MCC) intends to provide assistance to the Government of Kosovo to facilitate the development and implementation of a MCC Compact.

If you or your staff would like to arrange a meeting to discuss this assistance, please contact Dan Petrie at (202) 521-3583 or [PetrieDB@mcc.gov](mailto:PetrieDB@mcc.gov).

The attached notification is being sent to the Congress on October 3, 2019. The assistance may be provided and funds obligated on or after 15 days from the date of this notification.

In addition to the enclosed notification, we have attached supplemental information regarding the planned assistance.

Sincerely,

Sean Cairncross  
Chief Executive Officer  
Millennium Challenge Corporation

Enclosure: As stated

**MILLENNIUM CHALLENGE CORPORATION  
CONGRESSIONAL NOTIFICATION**

October 3, 2019

PROGRAM:	Eligible Countries
APPROPRIATIONS CATEGORY:	Fiscal Year 2019 Program Funds
OBLIGATION AMOUNT:	\$6,925,000

Pursuant to section 7015(c) of the Department of State, Foreign Operations, and Related Programs Appropriations Act, 2019, and section 610(a) of the Millennium Challenge Act of 2003, as amended (the "Act"), this is to advise that the Millennium Challenge Corporation ("MCC") intends to obligate up to \$6,925,000 of fiscal year 2019 funds under section 609(g) of the Act to provide assistance to the Government of Kosovo for the purpose of facilitating the development and implementation of a Millennium Challenge Compact with MCC.

The funds are expected to finance activities necessary for MCC to assess the expected impact of the proposed compact, further design activities, and develop implementation strategies.

## **SUPPLEMENTAL INFORMATION - MCC 609(G) ACTIVITIES FOR KOSOVO**

### **Background**

Kosovo is a small developing country on the Balkan Peninsula in Southeastern Europe. With a population of 1.8 million people spread across 10,908 km, it is among the most densely populated countries in the region. Ethnic Albanians make up the majority of the population (92 percent), while the largest minority is represented by ethnic Serbs (5 percent). Kosovo is one of the world's newest countries, having declared independence in 2008.

Kosovo is also one of the poorest countries in Europe. The 2015 Household Budget Survey estimates that 17.6 percent of Kosovo's population lives below the poverty line, with 5.2 percent of the population living in extreme poverty. Kosovo's labor force participation rate remains extremely low and fell to 40.9 in 2017. Similarly, the unemployment rate remains stagnant at 29.6 percent in 2018.

Kosovo's population is one of the youngest in Europe with a median age of 27 years. This represents both a promising source of future growth as well as an increasing cause for concern. The unemployment rate of 52.6 percent for 15 to 24-year-olds indicates an economy that has not created sufficient employment opportunities for the country's youth. Furthermore, the country's female labor force participation rate of 18 percent is the lowest in the region and among the lowest in the world. Female labor force participation percentage rates in neighboring countries such as Serbia, Albania, Montenegro, or Macedonia are in the low to mid-50s. Additionally, women's unemployment rates are high and entrepreneurship rates lower than for comparators. Women in Kosovo account for just eight percent of individual entrepreneurs, compared to approximately 33 percent globally and in the region.

While growth in Kosovo has not been fast enough to reach the level of wealth of comparators, it has been remarkably stable. Kosovo is one of only four countries in Europe to record positive growth rates in the years following the global financial crisis in 2008, with average annual growth around three percent since 2010. Private consumption was the main driver of growth and was fueled by remittances, public sector wages, and social transfers. The inflows of remittances have enhanced the stability of the economy and financed most of the country's trade deficit. Investment, which lags behind savings, has flowed mainly into residential and commercial construction. Annual flows of foreign direct investment remain below levels received by comparable countries due in part to the uncertain legal status of the country.

Kosovo is a services-oriented economy with services contributing 54 percent of value added to gross domestic product from 2009 to 2017. Kosovo's main trading partners continue to be the western Balkan and European Union countries. Kosovo's export sector is dominated by mining commodities, but high-value agriculture is a growing contributor.

Key challenges for Kosovo continue to be implementing reforms aimed at strengthening public administration to increase the quality of and access to public services, improve the business climate, and upgrade public infrastructure, including the country's current electricity system. Through reforms to these institutions, Kosovo can attract direct investments of the scale, scope,



and quality necessary to increase productivity in key sectors of the economy, generate growth, and ultimately reduce the high rates of unemployment and poverty.

### **Compact Eligibility and Constraints Analysis**

Kosovo was initially selected as eligible to develop a compact in fiscal year 2016 after passing the MCC scorecard for the first time with 13 out of 20 indicators, including the Control of Corruption and Democratic Rights indicators. In fiscal year 2017, however, after MCC and the Government of Kosovo conducted a constraints analysis and root cause analysis, Kosovo failed the MCC scorecard and the MCC Board of Directors selected Kosovo to develop a threshold program. In September 2017, MCC signed a \$49 million Threshold Program Grant Agreement with Kosovo that focused on two key constraints to Kosovo's economic growth: an unreliable supply of electricity and real and perceived weakness in rule of law. In fiscal year 2019, Kosovo passed the scorecard and was selected to develop a compact.

MCC and the Government of Kosovo conducted a constraints analysis in 2016 that identified three binding constraints to growth in Kosovo: (1) lack of reliable electricity supply; (2) perception and reality of weak rule of law; and (3) poor environmental services. In addition, the constraints analysis identified the low participation of women in the labor market as a critical, cross-cutting concern that could limit the equitable distribution of the benefits of MCC assistance. This constraints analysis has been used to inform and guide current compact development. In May 2019, MCC conducted its first technical mission to refresh the root cause analysis and stakeholder consultations conducted in October 2016.

In June 2019, MCC assessed the Government of Kosovo's proposed concepts, which focused on the lack of reliable electricity as a binding constraint. MCC identified two concepts focused on the energy sector for further analysis: (1) strengthening energy supply and (2) energy demand management. MCC, in partnership with the Government of Kosovo, undertook a series of missions between May and July 2019 to hold discussions with key stakeholders in the public, private, and donor sectors to further develop projects and activities within these two concepts.

As noted in the constraints analysis, a key factor impeding robust growth in Kosovo is inadequate infrastructure, particularly energy infrastructure. While the Government of Kosovo has undertaken a series of important reforms in the power sector, the unreliability of the current supply of coal-fired electricity increases operating costs for companies and limits their competitiveness. Frequent power outages disrupt manufacturing and other income-generating activities, imposing costs to businesses and households and hindering investment. The proposed interventions below aim to alleviate the root causes of this binding constraint.

### **Summary of Proposed Project Interventions**

Potential compact projects may focus on the following concepts:

1. A **Gas Sector Development Project** would give energy users a more efficient thermal energy option, support Kosovo's energy transition, and contribute to improved air quality. The project would include a collection of transmission and distribution pipeline, technical assistance to establish the management of the sector, as well as a connection fund to enable poorer consumers to benefit from the program.



2. A **Reserves for Power System Balancing Project** would deliver more reliable electricity to consumers, thereby reducing the significant cost to businesses of mitigating unreliable supply on their own. This project would build both the reserve infrastructure required to stabilize the system as well as the institutional capacity to procure and manage the reserves.
3. A **Distribution Network Improvement Project** would improve the continuity and quality of the electricity supply and reduce the technical losses in the system that drive up system costs for ratepayers and reduce the shock of future tariff increases. To do so, this project would upgrade the medium voltage power network, regularize transformers, and install hardware and software to more effectively meter and monitor the electrical network and isolate faults.
4. An **Energy Sector Strengthening Project** would build the Government of Kosovo's capacity to deliver the most cost-effective energy future for Kosovo, implement regulations, and meet the demands of the private sector to stimulate economic growth and prosperity. It would also establish mechanisms for workforce development that will give women and youth opportunities to meet the sustainability needs of the energy sector.

Together, the proposed projects focus on alleviating root causes of Kosovo's energy constraint while providing complementary assistance to the energy sector that addresses the other binding constraints of rule of law and environmental services. While not a binding constraint, lack of women's participation in the economy is also addressed in these projects and is critical to the ability of women to benefit from an MCC compact. MCC will work with the Government of Kosovo to more fully develop these projects. MCC currently projects that the MCC Board of Directors will consider a fully-developed compact program for Kosovo in 2020.

#### **Assistance to Develop the Compact Proposal**

The proposed assistance, in addition to funds previously notified on July 17, 2019, will be used to assist the Government of Kosovo in further developing the proposed compact. Specifically, funds would be used to support the rapid acquisition of pre-feasibility, feasibility, and design work, including environmental and social impact assessments, resettlement policy frameworks, gender and social inclusion analysis, and trafficking-in-persons risk assessments. These funds would also be used to further design and develop the gender and social inclusion-focused components of the projects given the significant opportunities across the proposed projects to support women's economic empowerment through interventions focused on women's employment and entrepreneurship. Lastly, funds would be used to collect baseline data for monitoring and evaluation purposes, as well as to fund the fiscal and procurement agents, the hiring of a recruitment firm, and the administrative costs required for the accountable entity. Funding these activities reflects MCC's commitment to preparing projects in a comprehensive manner in order to reduce implementation risk and increase confidence in the economic justification and technical feasibility of the proposed projects. The timing of the proposed assistance is driven by the need to procure key feasibility studies expeditiously in order to maintain efficient progress in compact development.

### **Update on and Sustainability of the Kosovo Threshold Program**

Kosovo's \$49 million threshold program addresses two constraints to Kosovo's economic growth: (1) an unreliable supply of electricity and (2) the real and perceived weakness of rule of law. MCC's assistance is designed to strengthen the power sector by fostering a market-driven approach to lowering energy costs for households and businesses, encouraging energy efficiency, and developing new sources for electricity generation. The program also supports the Government of Kosovo's efforts to improve decision-making and accountability by increasing accessibility and use of judicial, environmental, and labor force data.

The Government of Kosovo has been dedicated to working with MCC throughout its engagement on both the threshold program and compact development, and has committed over \$1.8 million to development team salaries, data collection, and office space since 2015. There has been high-level Government of Kosovo cooperation and interest in the partnership with MCC.

The Kosovo Threshold program is comprised of two projects:

1. **Reliable Energy Landscape:** This project encourages greater household energy efficiency and facilitates the switch to non-electric sources of heating through a pilot activity. MCC's assistance also works to bolster private-sector participation in the power sector by exploring barriers to finance for independent power producers and creating opportunities for women to participate in the energy sector through employment and entrepreneurship. Most major procurements for this project are complete and in early implementation.
2. **Transparent and Accountable Governance:** This project supports the implementation of a case management information system to make judicial information publicly available and improvements to the collection and reporting of environmental data to the public. An open innovation competition will let the government pose its challenges to civil society and private sector stakeholders to propose creative, data-grounded solutions, which can be a model for more productive partnerships between government and civil society. All activities except the judicial information activity are under way, with the last activity to be procured in fall 2019.

The program is expected to continue implementation through September 2021.