



CONGRESSIONAL NOTIFICATION TRANSMITTAL SHEET

This congressional notification outlines the Millennium Challenge Corporation's intent to negotiate a Millennium Challenge Compact with the Government of Kosovo.

The transmission of this notification to Congress on April 13, 2022, affirms negotiations concerning the proposed Kosovo Compact may begin on or after 15 days from the date of this notice.

Please find enclosed the notification with supplemental information regarding the proposed compact.

If you or your staff would like to arrange a meeting to discuss the proposed negotiations with the Government of Kosovo, please contact Brian Forni at (202) 521-2631 or ForniBJ@mcc.gov.

Sincerely,

/s/

Aysha House
Vice President
Congressional and Public Affairs

Enclosure: As stated

MILLENNIUM CHALLENGE CORPORATION
CONGRESSIONAL NOTIFICATION

April 13, 2022

Pursuant to Division F, Title III under the heading “Millennium Challenge Corporation” of the Consolidated Appropriations Act, 2019 (P.L.116-6); Division K, Title III under the heading “Millennium Challenge Corporation” of the Consolidated Appropriations Act, 2021 (P.L.116-260); Division K, Title III under the heading “Millennium Challenge Corporation” of the Consolidated Appropriations Act, 2022 (P.L. 117-103); and section 610(a) of the Millennium Challenge Act of 2003, as amended, this notification is (1) to advise you that the Millennium Challenge Corporation (MCC) intends to start negotiations with the Government of Kosovo for a Millennium Challenge Compact and (2) to initiate Congressional consultation before the start of negotiations.

The proposed \$202,000,000 compact seeks to assist the Government of Kosovo in addressing one of the country’s binding constraints to economic growth: the unreliable supply of electricity. The compact aims to address this constraint through two projects: the Energy Storage Project and the Just and Equitable Transition Acceleration (JETA) Project. In addition, the compact includes an American Catalyst Facility for Development (ACFD) Project to be conducted in collaboration with the U.S. International Development Finance Corporation (DFC).

Projected Economic Justification for the Compact

In recent years, demand for electricity in Kosovo has far exceeded supply—a problem that is expected to worsen over the next few years. Forty percent of households in Kosovo experience energy poverty, the highest rate among five regional neighbors for which data exists. The unreliable supply of electricity results in frequent supply disruptions, which then require Kosovo to import costly emergency energy supply. Kosovo’s electricity supply options are highly constrained due to limited installed renewable energy capacity, aging and unreliable lignite-fired generation plants, the lack of flexible generators, supply shortages in neighboring countries, and an absence of any natural gas resources or infrastructure to import gas. Kosovo’s unusually heavy reliance on coal-fired electricity generation, particularly for heating in the winter, contributes significantly to this energy constraint.

The compact will address these constraints through two projects: the Energy Storage Project and the JETA Project. The ACFD Project will leverage DFC tools and authorities to support financing that may support or complement the objectives of the Energy Storage Project.

At the compact-level, approximately 1.8 million people will benefit from MCC’s investment. This estimate is based on the scope of the Energy Storage Project, which intends to reach all households connected to the electric grid (reported to be 100 percent of the country’s households). The JETA Project aims to benefit women, but detailed project design is required to conduct cost-benefit analysis (CBA) and clearly define and count intended beneficiaries for both its activities. The JETA Project’s CBA and beneficiary analysis will be completed before the compact’s entry into force (EIF). As the entire population may benefit from the Energy Storage Project, while those that benefit from the JETA Project would be considered only at the project-level to avoid double counting.

Energy Storage Project

The Economic Return Rate (ERR) for the Energy Storage Project is preliminarily estimated at 8.7 percent. However, new data that will allow further refinement and the inclusion of currently unquantified benefits (see below) indicate the ERR will plausibly be higher and ultimately above MCC's hurdle rate. The project aims to increase Kosovo's energy capacity to balance scheduled power and actual power between neighboring countries with the establishment of a battery storage entity with a capacity of approximately 250MWh. This should reduce costly energy purchases during periods of energy imbalance and support the longer-term capability of the transmission grid to accommodate renewable energy generation that is intermittent and benefits from storage capacity to smooth system use. These benefits should lead to the principal objective of the project, which is to support energy security, including the use of energy storage, battery availability, and the reduced cost of securing adequate electricity as Kosovo transitions towards clean energy. The core benefits that are captured in the ERR include avoided capacity and activation payments, net revenues from energy arbitrage, and benefits of carbon reduction. Some benefits that are not yet quantified include savings from potential additional ancillary services, voltage regulation, and local air quality benefits with associated health benefits, which may be sizeable. MCC expects to be able to add to the current list of quantified benefits and it is plausible that the final ERR will exceed MCC's hurdle rate.

JETA Project

While an ERR is not available for the JETA Project at this time, MCC anticipates that this will be available before entry into force of the compact. The JETA Project aims to support Kosovo's future ability to address the unreliable electricity supply constraint by supporting new technical training programs or building from existing programs to provide the skills demanded by employers in the energy and adjacent sectors. This is expected to facilitate the Government of Kosovo's energy transition, incentivize gender equitable practices within companies, support networking and mentoring opportunities for women, and provide technical assistance to energy and adjacent sector employers to help increase female representation in the energy sector.

ACFD Project

The ACFD Project is designed to leverage DFC financing to support one or more blended finance transactions that will catalyze private investment in Kosovo's energy sector, supporting the goals of MCC's energy investments. MCC funds will be used to de-risk DFC-led investments in the private sector and DFC will be responsible for the appraisal and oversight of the overall investment. The ERR assessment and CBA excludes the ACFD Project because DFC will lead the identification of potential investments. MCC will coordinate with DFC and the accountable entity in Kosovo to help identify potential investments that align with the constraint to growth identified in Kosovo, as well as the compact timeline. While details are still being defined, MCC anticipates that DFC will assess and report the benefits of ACFD-supported investments using its new Impact Quotient system for measuring development impact. In addition, MCC will work with DFC to consider ways to assess and quantify the benefits of ACFD.

PROPOSED KOSOVO COMPACT

SUPPLEMENTAL INFORMATION

Overview

The proposed compact with the Government of Kosovo seeks to address a binding constraint to economic growth in the country: the unreliable supply of electricity. The compact will address this constraint through two projects: the Energy Storage Project and the Just and Equitable Transition Acceleration Project (JETA). The American Catalyst Facility for Development (ACFD) Project constitutes a third project leveraging U.S. International Development Finance Corporation (DFC) that will support or complement the objectives of the Energy Storage Project.

Background and Context

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 kilometers, 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 ethnic Serbs (5 percent). Kosovo is one of the world's newest countries, having declared independence in 2008. Kosovo is 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 38.3 percent in 2020. Similarly, the unemployment rate remained stagnant at 25.9 percent in 2020. Kosovo's population is one of the youngest in Europe with a median age of 27 years. The unemployment rate of 49.1 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 14.1 percent is the lowest in the region and among the lowest in the world. Women's unemployment rates are high and entrepreneurship rates are lower than comparators, with women in Kosovo accounting 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. For much of the past decade, annual flows of foreign direct investment have remained below levels received by comparable countries due in part to questions on the legal status of the country.

Kosovo is a services-oriented economy with services contributing 54 percent of value added to the 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 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 economic growth, and ultimately reduce the high rates of poverty and unemployment, including specifically among youth and women.

Selection and Eligibility Overview

MCC's Board initially selected Kosovo as eligible to develop a compact in December 2015, when it passed the MCC scorecard for the first time, following years of Government of Kosovo engagement with MCC regarding the eligibility requirements for MCC programs. During compact development, however, Kosovo failed the Control of Corruption "hard hurdle" indicator, and the scorecard. In December 2016, the Board selected Kosovo for a threshold program. Kosovo is currently in the final stages of implementing its \$49 million threshold program focused on promoting reliable energy and enabling transparent and accountable governance.

During threshold program implementation, Kosovo improved its performance on the Control of Corruption indicator and passed the scorecard two years in a row. As a result, in December 2018, MCC's Board selected Kosovo as eligible to develop a compact while it continued to implement its threshold program.

The year following its selection, Kosovo was reclassified by the World Bank as an upper middle-income country and exited MCC's candidate country pool. It has, therefore, not received an MCC scorecard since its graduation. MCC's Board has repeatedly affirmed its support for Kosovo continuing to develop a compact with MCC, and Kosovo has continued to demonstrate its commitment to the principles of democratic governance that underpin MCC's eligibility criteria and the scorecard.

Compact Proposal Overview and Budget

The proposed compact is summarized in the budget table below. The anticipated compact budget is \$236,670,607 which includes up to \$202,000,000 funded by MCC and a contribution from the Government of Kosovo of \$34,670,607 million.

Table 1 presents an approximate budget for the proposed compact based on initial due diligence and appraisal.

Table 1: Kosovo Compact Budget (in US\$)

Compact Component	Amount
1. Energy Storage Project	\$180,629,587
1.1 Frequency Restoration Response Activity	\$46,181,274
1.2 Multi-functional Energy Storage Activity	\$124,822,312
1.3 Energy and Climate Policy Support Activity	\$9,626,000
2. Just and Equitable Transition Acceleration Project	\$16,000,000
2.1 Energy Skills for the Future Activity	\$8,000,000
2.2 Inclusive Energy Sector Workforce Activity	\$8,000,000
3. American Catalyst Fund for Development Project	\$2,000,000
4. Monitoring and Evaluation	\$3,265,000
5. Program Administration and Oversight	\$34,476,020
Total MCC Funding	\$202,000,000
Total Government of Kosovo Contribution	\$34,670,607
Total Compact	\$236,670,607

Proposed Projects

- 1. Energy Storage Project:** The objective of the Energy Storage Project is to support energy security and transition to a cleaner energy future, as reflected by (1) usage of energy storage systems, (2) availability of the energy storage system, and (3) reduced cost of securing adequate electricity for Kosovo.

 - Frequency Restoration Response Activity:** This activity will support the transmission system operator to own and operate approximately 90 megawatt hours (MWh) of energy reserves to cost-effectively smooth out unexpected imbalances in the electricity grid.
 - Multi-functional Energy Storage (MFES) Activity:** This activity will support a new public or public-private partnership battery storage entity to own and operate approximately 250MWh of energy storage that could be used for frequency restoration reserves, energy arbitrage, or other potential ancillary services, filling in gaps of longer-scale, unexpected outages or shifting energy to cover peak demand.
 - Energy and Climate Policy Support Activity:** This activity supports technical and administrative capacity building for energy and climate regulators and the policy and institutional reforms required to ensure the operating environment for energy storage in Kosovo is well defined and regulated through Kosovo's laws and supported by good planning, maintenance, and cost-reflective tariffs. It will also support cross-cutting measures on female employment and entrepreneurship across projects, and

policy and institutional reform around pro-poor and gender-inclusive planning in the sector.

2. ***Just and Equitable Transition Acceleration Project:*** The objectives of the JETA Project are (1) that trained graduates are hired in relevant jobs in the energy and adjacent sectors; and (2) increased employment of women in participating employers.
 - **Energy Skills for the Future Activity:** This activity establishes new technical training programs and build from existing programs to provide the skills demanded by employers in the energy and adjacent sectors, aiming to facilitate the Government of Kosovo’s just energy transition and increasing women’s participation in such programs.
 - **Inclusive Energy Sector Workforce Activity:** This activity aims to incentivize gender equitable practices among energy sector employers, support networking and mentoring opportunities for women, and provide technical assistance to help increase female representation in energy companies in Kosovo.
3. ***ACFD Project:*** The objective of the ACFD Project is to facilitate DFC investments in Kosovo. The project aims to leverage DFC financing to support one or more blended finance transaction that will catalyze private investment in Kosovo that could include (1) complementing MCC’s funding to deliver a public private partnership focused transaction for energy storage in lieu of a public entity for the MFES Activity; (2) leveraging private sector participation to scale a successful energy storage public entity launch via additional private sector delivered storage systems and services (i.e., additionally leased energy storage capacity); and (3) catalyzing complementary renewable energy investments that bolster generation capacity and strengthen the energy storage entity business case.

Policy Reform and the Compact

The compact program will require passage of several new laws. Energy storage, for instance, is not defined in Kosovo law and must allow the transmission system operator to own the storage resources.

The benefits of the Energy Storage Project depend on the broader investment in private renewable energy generation. To ensure this type of investment is encouraged, the compact may include a set of policy conditions that seek to ensure that the full benefits of the program can be achieved and focus on assisting the Government of Kosovo to facilitate its renewable generation goals.

There are no major conditions or reforms required for the JETA Project, although MCC will seek to secure a contribution from the Government of Kosovo on subsidies, such as travel or housing stipends, that would help students, particularly women, facing barriers to attend trainings. The Inclusive Energy Sector Workforce Activity aims to incentivize companies to institute gender-

equitable practices and policies into their organizations. This would support the operationalization of existing but unfulfilled national legal requirements.

Specific reforms include:

- Passing the relevant laws and reforms to incentivize renewable independent power generators to enter the market.
- Legal and administrative steps to define battery systems in Kosovo energy policy and define potential ownership structures.
- Government of Kosovo adoption of a vulnerable customers program, which has been previously developed by the World Bank, to ensure that means-tested, lower income customers can access more affordable electricity.

Update 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 develop 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 threshold program is expected to close in September 2022.

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. All major procurements for this project are complete and in implementation.
2. **Transparent and Accountable Governance:** This project supports the implementation of a case management information system to make judicial information publicly available and improves the collection of reporting of environmental data to the public. An open innovation competition will let the Government of Kosovo 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 major procurements for this project are complete and in implementation.

The threshold program's Women in Energy initiative, which is a sub-activity in the Reliable Energy Landscape Project, provides scholarships, internships, and entrepreneurship grants and

training for women. These activities create opportunities for women to participate in the energy sector as both employees and entrepreneurs.

As of March 2022, the threshold program reports the following milestones and achievements:

- 692 grant agreements for household retrofits have been approved in the first two application windows, with a third window ongoing. 350 household retrofits are complete. Apartment-level retrofits will cover at least 600 households by the end of the program.
- 26 women scholarship recipients graduated from Millennium Foundation Kosovo-Des Moines Area Community College energy degree program in May 2021; 88 percent are employed, continuing education, or interning in the energy sector.
- 124 women interns placed in internships in the energy sector and 400 beneficiaries have been awarded grants as part of the Women Entrepreneurs in Energy program.
- All windows of the Open Data Challenge have now closed, with 21 small grants having been awarded over the course of four challenges.

The proposed compact builds upon lessons learned in the threshold program, with the JETA Project moving beyond a compliance approach to enhancing female employment by incorporating specific and dedicated outreach and additional measures to reach minority group participation. Through the Energy Storage Project, the proposed compact aims to encourage the energy sector to collect consumer data that is disaggregated by gender, income, and other key variables such as ethnicity, improve pro-poor planning, and integrate gender considerations into energy sector policy.