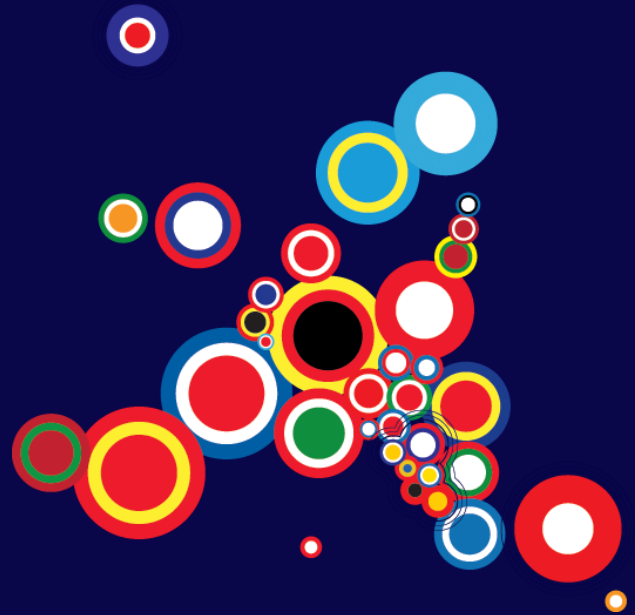




INSTRUMENT FOR PRE-ACCESSION ASSISTANCE (IPA II) 2014-2020

Kosovo*

Support to enhance Kosovo
competitiveness



Action summary

The main aim of this action is to support Kosovo's micro, as well as small and medium enterprises (MSMEs and SMEs) in accessing finance and know-how to increase their competitiveness and sustainability leading to growth in (M)SMEs' output and new job creation. Support will be provided through grants and a credit facility to blend funds of the European Bank for Reconstruction and Development (EBRD) with IPA funding in order to facilitate access to finance for development projects of Kosovo enterprises that have potential for export promotion, import substitution and job creation.

The assistance will be provided, but not limited to the following sectors: Wood processing including furniture, ICT, Tourism, Textiles and leather processing, Metal works and metal processing, and services.

*This designation is without prejudice to positions on status, and is in line with UNSCR 1244/1999 and the ICJ Opinion on the Kosovo declaration of independence

Action Identification	
Action Programme Title	Action Programme for Kosovo for the Year 2016 – Part I
Action Title	Support to enhance Kosovo competitiveness
Action ID	IPA 2016/039 745/ 04 / Kosovo/Competitiveness)
Sector Information	
IPA II Sector	6. Competitiveness and innovation
DAC Sector	43010
Budget	
Total cost	EUR 30.5 million
EU contribution	EUR 10 million
Budget line(s)	22.02.01.02
Management and Implementation	
Management mode	Direct and indirect management
<i>Direct management:</i> EU Delegation	European Union Office in Kosovo
<i>Indirect management:</i> Entrusted entity	European Bank for Reconstruction and Development
Implementation responsibilities	European Union Office in Kosovo
Location	
Zone benefiting from the action	Kosovo
Specific implementation area(s)	Kosovo
Timeline	
Final date for concluding Financing Agreement(s) with IPA II beneficiary	31 December 2017
Final date for concluding delegation agreements under indirect management	N/A
Final date for concluding procurement and grant contracts	3 years following the date of conclusion of the Financing Agreement, with the exception of cases listed under Article 189(2) of the Financial Regulation
Final date for operational implementation	6 years following the conclusion of the Financing Agreement
Final date for implementing the Financing Agreement (date by which this	12 years following the conclusion of the Financing Agreement

programme should be de-committed and closed)			
Policy objectives / Markers (DAC form)			
General policy objective	Not targeted	Significant objective	Main objective
Participation development/good governance	<input type="checkbox"/>	x	<input type="checkbox"/>
Aid to environment	x	<input type="checkbox"/>	<input type="checkbox"/>
Gender equality (including Women In Development)	x	<input type="checkbox"/>	<input type="checkbox"/>
Business Development	<input type="checkbox"/>	<input type="checkbox"/>	x
Reproductive, Maternal, New born and child health	x	<input type="checkbox"/>	<input type="checkbox"/>
RIO Convention markers	Not targeted	Significant objective	Main objective
Biological diversity	x	<input type="checkbox"/>	<input type="checkbox"/>
Combat desertification	x	<input type="checkbox"/>	<input type="checkbox"/>
Climate change mitigation	x	<input type="checkbox"/>	<input type="checkbox"/>
Climate change adaptation	x	<input type="checkbox"/>	<input type="checkbox"/>

1. RATIONALE

The development of a sound business environment which can stimulate growth and employment generation is one of the key priorities for Western Balkan countries, also in line with their European perspective. Small and Medium Enterprises are the backbone of the economies of EU Enlargement candidates and potential candidates in the region and their increased competitiveness is one of the main priorities for Governments.

Within the framework of the EU Enlargement Policy, the European Commission supports the development of MSMEs in the Western Balkans. Access to affordable sources of finance is a key priority of the EU support as it would allow MSMEs the possibility to grow and compete at all levels including regional and international markets.

Despite a well-established financial sector in Kosovo, especially the banking sector, MSMEs access to bank loans is limited by the high interest rates, requests for high collateral and also as there is no or limited financing willingness by banks for financing business expansion and new project undertakings by MSMEs.

According to the World Bank/EBRD Business Environment and Enterprise Survey (BEEPS), access to finance was one of the main obstacles for the surveyed enterprises. Some 45% of enterprises in Kosovo have identified access to finance as one of the most severe obstacles to doing business. This is the highest rate compared to other countries in the region. Furthermore, the OECD growth diagnostics also concluded that access to finance is one of the binding constraints to growth (see Economic Reform Program 2016). Based on further research and analysis, it is apparent that the most affected category is small and medium enterprises. Lending to women is another big obstacle according to the EBRD as in 2013 only 3% of bank lending went to women-lead enterprises.

The 2015 Kosovo report (progress report) states that access to finance is being a major obstacle for business development and the market entry of the businesses. This has also been identified as an obstacle in the previous progress reports (2014, 2013, and 2012).

Firstly, the majority of MSMEs only pass a fraction of their business through the banking system and pay only the minimum salary for their employees into banks. Secondly, a large portion of MSME owners/managers lacks capabilities to run their businesses in a professional manner. Thirdly, there is very little focus on the financial aspects of the businesses.

According to the Riinvest Report on Business Climate in Kosovo performed in 2014, a range of different obstacles contribute to the unfavourable picture of the private sector such as limited access to finance and high cost of finance. Furthermore the same study surveyed 1,000 businesses across Kosovo to indicate the severity of 23 potential barriers to business entry and development in past (2009), present 2013 and future 2017. In addition, the high cost to finance was identified as the main barrier, the indicators were marked from 20 to 100 and the high cost of finance/borrowing was 83.7 in 2013, 84.2 in 2009 and 71.2 was foreseen to be in 2017.

Moreover, Kosovo's financial sector and instruments for financing are not diversified. The sector is dominated by the traditional commercial banks. Capital markets are underdeveloped according to the OECD analysis. According to the Banking Association of Kosovo (see The Banker), the combined portfolios of leasing companies, non-bank financial institutions and microfinance institutions account for less than 10% of total assets. Despite the fact that there is a regulatory framework in place for leasing, the financial institutions currently use this instrument only for financing household needs for vehicles and apartments. Factoring is not offered at all by the banking system. There are no specialised banks, for instance investment banks which could have been provided usually offer longer term loans or equity markets which have proven to be very effective growth financing vehicles for small and medium enterprises globally.

PROBLEM AND STAKEHOLDER ANALYSIS

Problem description

Despite the GDP growth rates of 2.7-3.3% registered over the past five years, Kosovo is the poorest economy in the region. Growth path is largely dependent on remittances from Kosovars living abroad (mainly Germany, Switzerland and Scandinavian countries), on public investments and donor funding. The

official unemployment rate is over 35% with youth unemployment reaching up to the highest rate in the region (60, 2%).

The productive system is largely made by Micro Small and Medium Enterprises (almost 99% of the total of registered companies) working in traditional sectors and which are the main source of employment. The economy is dominated by the trade and service sector with a large number of micro and small companies importing goods to be resold in the internal market.

The very limited access to innovation in local production and processes is a key determinant of the low competitiveness of Kosovar productions. The majority of businesses are family owned with no distinction between ownership and management and very limited involvement of external skilled managers. The very low level of financial literacy is another key factor hampering the establishment and growth of MSME. Informal/shadow economy is quite spread and financial information provided by companies is not aligned to international standards. The habit of keeping several financial books to be used according to purpose (revenue declaration for tax purpose rather than for credit demand or for every day company management) is quite common among local companies and this makes very difficult to understand the real financial position of individual MSMEs.

All these elements largely explain the great difficulties faced by Kosovar MSMEs in accessing affordable sources of finance.

Such a business environment affects also companies which may have the capacity and skills to improve the quality and quantity of productions in some sectors, but in reality struggle to obtain adequate financial resources to implement the investments they need.

Despite the importance role in economic development MSMEs growth continues to be hampered by a number of obstacles. Unfavourable business environment, informal economy and difficult access to finance with high interest rates and high collateral on loans are holding back MSMEs from growing their operations. Banks due to market imperfection have often been reluctant on their lending activity. This has limited the financial sources and would serve the growth of MSMEs that depend strongly on funds to finance their activities.

MSMEs in countries in transition usually finance their activity through their internal funds, borrowing from family or friends, grants, bank loan or other investors. Most small and medium enterprises start up with their own funds and take loans only later because other external sources of finance does not exist in the market of Kosovo.

Difficulties arise when businesses go to the bank to ask for a loan, due to various obstacles set by creditors. Banks require from the borrower MSMEs to fulfil a number of criteria if they want to get access to bank loan. In order to overcome these obstacles, businesses sometimes present unreliable data to creditors leading to a stricter bank decision-making process with regard to lending. Due to existing asymmetric information from businesses and due to other reasons, banks impose unfavourable lending conditions to businesses such as difficult procedures for loan approval, high interest rates, requirement for collateral in a value that is nearly twice as much as the value of the loan in order to avoid the risk of borrowing (236,436 average value of the loan compared to 518,265 average value of collateral requirement, BSCK 2011). There are a number of microfinance institutions which aim to provide source of finance to the businesses and entrepreneurs however those credits are characterised with even higher interest rates than banks, thus making them extremely unfavourable for businesses.

Data from the Kosovo Business Registration agency show that 2,199 businesses were closed in 2015 and 1,663 in 2014, limited access to finance may have been one of the reasons of their sustainability.

Stakeholder analysis

The financial sector in Kosovo is largely made of private commercial banks with a wide predominance of foreign owned institutions (eight out of nine registered financial institutions). Trade loans and short term loans are the most used funding instrument for MSMEs while other debt (leasing) and equity schemes are very limited.

The last bulletin issued by the Central Bank of Kosovo shows a very solid and liquid structure of the overall commercial banks, according to international safety standards (ref. *International regulatory framework for banks – Basel III*). The average loan/deposit ratio (76%) and, most of all, the impressively high return on average equity ratio (17,1%) testify the excellent profitability and stability of the sector as a

whole. The level of Non-Performing Loans (NPL) is the lowest of the region (6.1% according to the last figures of the Central Bank of Kosovo). The main source of funding for commercial banks are medium/long term deposits on which the nine institutions offer with average an interest rate around 1%.

The credit supply has not increased in the recent years as the financial institutions preferably lend funds to well-known clients rather than addressing new segments. Their loan portfolios are extensively made of short term loans to MSME mainly for trade related products.

The majority of businesses are family owned characterised with limited financial literacy. The financial information provided by companies is not aligned to international standards. The habit of keeping several financial books to be used according to purpose (revenue declaration for tax purpose, rather than for credit demand or for every day company management) is quite common among local companies and this makes very difficult to understand the real financial position of individual MSMEs.

Collateral and guarantee requirements remain very high (on average 200-250% of the loan amount). The main reasons for this are related to: the remaining uncertainty on the property rights and land registration, although the establishment of the Kosovo cadastre has improved the situation; the weak legal mechanism in place for collateral enforcement, although progress in this sense have been made in the recent years; and the difficulty of reselling sized properties on the market. These elements lead banks to heavily discount the value of proposed collaterals with additional burdens for MSMEs.

Even if the high liquidity detained by banks has been leading in the last year to a progressive decrease in actual interest rates on loans to MSMEs, it has not impacted the existing risk-adverse credit policies of the main financial institutions.

All these elements largely explain the great difficulties faced by Kosovar MSMEs in accessing affordable sources of finance.

The Central Bank of Kosovo (as a regulator and overseeing body) is in charge of overseeing the banking sector, the institution reports to the Assembly while the Ministry of Finance is in charge of relevant policy making. Licensed commercial banks operating in Kosovo are also key stakeholders to this Action.

The Ministry of Trade and Industry is in charge for policy making, while the Kosovo Investment and Enterprise Support Agency (KIESA) is the main institutional body that is in charge for implementing the policy and legislation relating to MSMEs and private sector development.

The Kosovo Credit Guarantee Fund (KCGF) has been established in April 2016 and it is fully operational. This marks the establishment of an independent, local, and sustainable institution that will issue portfolio loan guarantees to financial institutions thereby increasing access to finance for the Micro, Small, and Medium Enterprises (MSMEs) in Kosovo. The Kosovo Credit Guarantee Fund (KCGF) will provide a guarantee for eligible business loans to qualified borrowers, it will cover up to 50% of the risk of the loans with the aim to facilitate the private sector development and increase access to finance for MSMEs. KCGF guaranteed loans will help especially farmers, entrepreneurs, women-owned businesses, and minority-businesses to expand, increase domestic production, create jobs, and improve the trade balance.

Important stakeholder in this project will be European Bank for Reconstruction and Development.

OUTLINE OF IPA II ASSISTANCE

With the aim of supporting Kosovar MSMEs in improving their competitiveness, the proposed assistance will enhance the management and production capacities of SMEs with a substantial number of job creation by setting up a credit and advisory facility which would be implemented by EBRD together with direct grants for MSMEs.

Similarly to the results foreseen in this action document, the planned activities aim at:

- Supporting domestic companies to become more competitive through an increase in their share of trade with the EU and the region,
- Developing sound economic governance policies,
- Establishing an enabling and efficient institutional, economic and legal business-friendly environment (inductive to private investments, enabled to implement relevant legislation).

The implementation of activities foreseen in this document will produce both immediate results and changes in the current situation, as well as, long-term sustainable results to be introduced in the form of systemic and policy change, improved performance of relevant institutions and overall increased competitiveness of the target audiences within the private sector.

RELEVANCE WITH THE IPA II STRATEGY PAPER AND OTHER KEY REFERENCES

The relevance of proposed interventions is closely linked to the objectives and results foreseen in the IPA Indicative Strategy Paper (ISP) 2014-2020 for Kosovo. IPA II support to Competitiveness is expected to be essential both for increasing the competitiveness of Kosovo's private sector, especially MSMEs, and promoting private investments. Similarly to ISP objectives, the proposed interventions aim at increasing the competitiveness of Kosovo's private sector, especially MSMEs, and promoting private investments including technological upgrade and innovation capacity*.

The need for intervention and support to MSMEs is highly relevant. Improving access to finance for Kosovo MSMEs is a priority measure identified in the Kosovo's Economic Reform Program 2016 as reform measure number 12. This measure aims to expand the credit guarantees and to improve information on business and individual lending history. Furthermore, improving access to finance for MSMEs is also identified as a priority in the Small Business Act for Europe (SBA). In March 2016 the Ministry of Trade and Industry together with engagement of several donors established the Credit guarantee scheme, which will provide partial coverage for collateral requirements on MSME loan portfolios of banks participating in the scheme. Preliminary negotiations held by KIESA with private commercial banks have confirmed the interest of the financial market in the instrument.

LESSONS LEARNED AND LINK TO PREVIOUS FINANCIAL ASSISTANCE

This Action will build upon the following past and current projects listed in the below summary:

Micro, Small and Medium Enterprise Grants project supported by the EU Office in Kosovo, co-financed by Ministry of Trade and Industry. The project provided 36 grants to MSMEs with the potential to export and import substitution. Grants were provided across different sectors such as metal processing, wood processing, textile, food processing, ICT, glass processing and automotive industry etc. As a result around 12 businesses are exporting, over 200 jobs have been created; 93% declared their increase in sales, profit, production quality and competitiveness, while 87% experienced an increase in efficiency and range of products as a result of support by the grant. The selected enterprises were well established MSMEs, and all of them contributed with a co-funding through own capital or borrowed funds to the financing of the proposed investment. In relation to access to finance, these beneficiaries continue to have the same constraints as before, as there are no financial products which fit with the requirements of their respective stage of growth and related investments (for expansion, capital increase, differentiation) etc.

Previous projects implemented such as “**Aid for Trade,**” “**Enterprise Growth Project/BAS-EBRD (TAM/BAS)**” have enhanced the performance and competitiveness of assisted beneficiaries and continue to support the development and sustainability of local MSMEs. The recommendations extracted from the project imply that assistance should focus on increasing management performance, upgrading production techniques and developing new products to add value and efficiency.

The successful inclusion of a vast number of stakeholders in legal reform efforts, development of the SME Strategy, implementation of Small Business Days 2011, numerous studies (“Training Needs Analysis 2012”, “Access to Finance” and “Social Business Incubation”) and various communication/visibility activities – within the on-going EU-funded “**SME Support through MTI**” project – present positive learned lesson for the SME Support Agency, shaping its future support to the SME sector in Kosovo.

The Kosovo **SME Promotion Program (KOSME)** is co-financed from ADA, SDC and MTI. The project is ongoing and has to finish in March 2016. The project has 3 components. The first component is KIESA capacity building. The second component is the Voucher Counselling Scheme and the third component is

*From the Indicative Strategy Paper

to assist MTI to create the Credit Guarantee Scheme. Within the Voucher Scheme component we build the new mechanism to provide the consultancy to SME, in partnership with Business Consultants Council. From begging to now the project provided services for 145 Enterprise and around the 30 SME are in process for Voucher Implementation.

Grant subsidies provided by **USAID, EMPOWER Project** provide financial support to businesses for increasing and improving production, expanding buyer connections, specific training and internship programmes.

2. INTERVENTION LOGIC

LOGICAL FRAMEWORK MATRIX

Overall objective	Objectively verifiable indicators (OVI)	Sources of Verification	
To support Kosovo MSMEs in accessing finance and know-how to start/ grow their businesses and increase their competitiveness and sustainability leading to growth in MSMEs' output and new job creation.	Doing Business - Distance to frontier (score)	World Bank – Doing Business	
Specific objectives	Objectively verifiable indicators (OVI)	Sources of Verification	Assumptions
<p>Specific Objective 1 :</p> <p>To improve access to finance for MSMEs</p>	<ul style="list-style-type: none"> ▪ Number of MSMEs receiving support services ▪ Volume of new investments by Kosovo MSMEs ▪ Number of loans provided by PFIs and value of financing mobilised. 	<ul style="list-style-type: none"> • Ministry of Trade and Industry, periodic reports • Kosovo Report • Small Business Act for Europe (SBA) Index • World Bank Doing Business Report • Ministry of Finance, periodic reports • KIESA, periodic reports • Kosovo Customs data • Central Bank of Kosovo, periodic 	<ul style="list-style-type: none"> ▪ Effective government measures for improvement of business environment in Kosovo ▪ Efficient institutional capacities for business advisory services ▪ Improvement of access to finance for MSMEs

		<ul style="list-style-type: none"> reports • Periodic reports form the Agency of statistics of Kosovo 	
<p>Specific Objective 2:</p> <p>To increase the selected enterprise's, outputs, export capacities, and employment levels</p>	<p>Number of new jobs created within supported MSMEs</p>	<ul style="list-style-type: none"> ▪ Ministry of Trade and Industry, periodic reports ▪ Kosovo Report ▪ Small Business Act for Europe (SBA) Index ▪ World Bank Doing Business Report ▪ Ministry of Finance, periodic reports ▪ KIESA, periodic reports ▪ Kosovo Customs data ▪ Central Bank of Kosovo, periodic reports ▪ Periodic reports form the Agency of statistics of Kosovo ▪ Tax Administration of Kosovo 	<ul style="list-style-type: none"> ▪ Number of Kosovo MSMEs with improved competitiveness as a result of innovation and technology transfer ▪ Trade balance improved
Results	Objectively verifiable indicators (OVI)	Sources of Verification	Assumptions
<p>Result 1:</p> <ul style="list-style-type: none"> ▪ Kosovo MSMEs access finance through Investment Incentives for Enterprises. 	<ul style="list-style-type: none"> ▪ Number of eligible MSMEs supported by EU assistance ▪ Total amount of finance provided to eligible MSMEs 	<ul style="list-style-type: none"> ▪ KIESA, periodic reports ▪ EBRD, project implementation periodic reports ▪ Periodic reports form the Agency of statistics of Kosovo 	<ul style="list-style-type: none"> ▪ Number of Kosovo MSMEs with improved competitiveness as a result of innovation and technology transfer ▪ Trade balance improved

<p>Result 2:</p> <ul style="list-style-type: none"> ▪ Number of women entrepreneurs supported 	<ul style="list-style-type: none"> ▪ Number of grants/loans to women entrepreneurs 	<ul style="list-style-type: none"> ▪ KIESA, periodic reports ▪ EU commission, project implementation, periodic reports ▪ Periodic reports form the Agency of EUO Kosovo and EBRD Kosovo 	<ul style="list-style-type: none"> ▪ Number of Kosovo MSMEs with improved competitiveness as a result of innovation and technology transfer ▪ Trade balance improved

DESCRIPTION OF ACTIVITIES

Support to Kosovar MSMEs (Micro, Small and Medium Enterprises) for improvement of their competitiveness through:

1. A credit and advisory facility to be implemented by EBRD (EU funding 5 million EUR)
2. A grant facility targeting MSMEs in 6 priority sectors (wood processing including furniture, ICT, textiles and leather processing, metal works and metal processing, services, tourism) to be implemented by EUO in Kosovo (EU funding 5 million EUR)

1. Credit facility to be implemented by EBRD

The first activity (Facility) that will be implemented by the European Bank for Reconstruction and Development (EBRD) comprises the following elements:

- a. **Long-term financing for Enterprises** to facilitate access to long-term funding for eligible investments that will enhance SMEs' competitiveness. The funding will be provided by the EBRD and channelled to the SMEs through Kosovar Banks and Micro Finance Institutions, jointly referred to as Partner Financial Institutions ("PFIs");
- b. **Investment Incentives for Enterprises** to blend EBRD funding and incentivise investments by SMEs. This component will be funded by the European Union (EU) contribution under IPA II.
- c. **Technical Assistance to PFIs** to build their capacity, develop systems and tools to provide appropriate and dedicated services in support of SMEs' competitiveness. This component will be funded by the EU contribution under IPA II
- d. **Advisory services to Enterprises** to provide access to know-how for the enterprises in order to facilitate access to finance, growing their businesses and enhance their competitiveness. This component will be funded by the EU contribution under IPA II

The Facility is expected to work with the proportion of 5:1, which mobilises EUR 25 million of EBRD lending for eligible investments to SMEs through PFIs.

Therefore, the EU contribution requested is EUR 5.0 million to be provided in the form of: (i) investment incentives/grants; (ii) technical assistance to PFIs and (iii) advisory service to enterprises benefiting from the facility.

The overall objective of the Facility is to support Kosovar enterprises in accessing finance and know-how to grow their businesses and enhance competitiveness via improved productivity and adoption of innovative practices leading to increased output and new job creation. The facility will support small and medium enterprises active in all the sectors of Kosovo economy. This activity will facilitate access to finance for all businesses that have problems when dealing only with commercial banks, as the commercial banks will be able to use the TA to PFI facility in order to help them assess the loan applications of the potential beneficiaries. The technical assistance component, in particular, will reduce the transaction costs for the banks when analysing a SME request. Furthermore, the proposed technical assistance for the banks will be aimed at supporting the institutions in designing and launching new and more SME oriented long term financial products, thus responding to the need of local companies in terms of finance for investments and innovation.

The activity will also use advisory services for enterprises who are beneficiaries of the loan in order to help them with access to finance, tailor made advice for growing their business and enhancing their competitiveness.

Through the proposed structure, the Facility takes a holistic approach to enterprise development by enabling each enterprise to access blended instruments tailored to their needs and the stage of their growth. The availability of EBRD long-term financing and associated grant funding will enable the Kosovar enterprises to make investments to upgrade production capacities, enhance processes and improve product quality. The EBRD Advice for Small Businesses component, through its advisory services, will provide access to know-how for SMEs that will help them assess their investment and

business needs, as well as raise the awareness of the Facility. Hence, the enterprises will gain access to both know-how and finance in order to improve their competitiveness.

The Facility is proposed to be implemented by means of a Pillar Assessed Delegation Agreement with the EBRD, which will be responsible for the overall management and implementation.

The Facility will be implemented in Kosovo, but this project will be coordinated at the regional level and within the framework of the Enterprise Development and Innovation Facility (EDIF), where the EBRD will be reporting on progress. This Facility is already being rolled out in Bosnia and Herzegovina and in the former Yugoslav Republic of Macedonia. Regional coordination will help the absorption of the Facility because EDIF offers a series of technical assistance and advisory services (including the Small Business Support also provided by EBRD) that works in complementarity to improve business conditions and facilitate access to finance in the Western Balkans.

The minimum size of loans provided to businesses is EUR 250.000, whereas the maximum size is EUR 750,000.

2. A grant facility targeting MSMEs in 6 priority sectors to be implemented by EUO in Kosovo (EU funding 5 million EUR)

This activity will provide capital intensive investments to key MSMEs in priority sectors with an incentive to offer also sub-grants to their related suppliers (value chain approach).

The main goal of this activity is to increase competitiveness, substitute imports and increase exports and facilitate job creation. The aim of this component is also to develop the micro business in the value chain and support them through sub-granting.

While the lending facility is open to all manufacturing sectors, the proposed grant component will be restricted to the mentioned 6 priority sectors:

- wood processing including furniture
- ICT
- textiles and leather processing
- metal works and metal processing
- services, and
- tourism

The identified priority sectors have different needs in terms of capital investments. Some of them need high amounts of funds (wood processing, metal processing and tourism) while others (mainly ICT, services and textile) are not capital intensive. For this reason a flexible approach in the administration of the grant component and the establishment of different thresholds and eligibility criteria for MSME and related investments is applied in this activity. In accordance with different needs of sectors the implementation is proposed through two lots with different sizes of grants:

Lot 1, EUR 1.5 million will include three sectors: ICT, Service and Textile and leather processing with grants between EUR 60.000 and EUR 100.000

Lot 2, EUR 3.5 million will include three sectors: Wood Processing (including furniture and bio-mass products), Tourism and Metal works and processing with grants between EUR 60.000 and EUR 250.000.

Support should include expanding and improving production or services, certification process for companies, preparation and implementation of activities for exporting, business advisory and development services tackling specific needs of the enterprise, development of skills needed through specific and tailored made trainings, support to further development of the value chain through inclusion of sub-granting.

During the implementation the beneficiaries of the grant scheme will be able to benefit through business advice from TA assistance to KIESA on preparation of export promotion policy and activities, IPA 2008 Project "Increase of Enterprise Competitiveness and Export Promotion".

A new financing facility for enterprises will assist selected enterprises in priority sectors to take concrete steps to improve their competitiveness in both domestic and international markets and generate employment. Through these measures the project aims to achieve significantly better business and economic results with those enterprises taking part in the scheme, while demonstrating and disseminating new models of approach to other businesses that will help Kosovo's enterprises more generally to better realise their potential.

The proposed project will tackle directly, and in a new way, some of the most persistent problems of company competence and behaviour that have resulted in Kosovo under-performing in business and economic development in relation to its potential.

The financial envelope for this activity is proposed EUR 5 million, which will be distributed through grants and sub-grants to micro, small and medium enterprises.

Co-funding will have to be provided by the grant beneficiaries. The size of co-funding will be included in the Guidelines of CfP.

Past recipient of competitiveness/MSME grants under IPA are not eligible when applying under this activity, however they are encouraged to apply for the support under the Activity 1. Recipients of **Investment Incentives for Enterprises** outlined under 1(ii) of this sub-paragraph are not eligible to apply for this activity (**Grant facility for enterprises**).

RISKS

The potential risks that may arise are the following:

- Possible limited SMEs absorption capacity for the loan facility with EBRD. The risk is that due to the limited absorption capacity of the SMEs, the available amount is not disbursed or not disbursed in sufficient amounts to (fully) achieve the objectives of the action.
- No interest of commercial banks to participate in the lending facility.
- Liquidity risk: high liquidity managed by the PFI in Kosovo might lead to difficulty of "marketing" the credit facility implemented by EBRD which, in turn, might not be attractive to local banks

In order to limit the above mentioned risks, EBRD will work with all banks in Kosovo to attract the banks to participate in the Activity 1 and will also offer to them support through point (iii) TA to PFIs.

Under the Activity 1, EBRD has to report to the Western Balkans Enterprise Development & Innovation Facility (WB EDIF), and its WB EDIF Platform Advisory Group (PAG) about the implementation of the project. PAG convenes at least twice per calendar year in order to discuss relevant key matters of the WBEDIF, to give strategic direction and to decide on certain matters in relation to the management of the WBEDIF.

The Western Balkans Enterprise Development & Innovation Facility (WB EDIF), funded by the EU, aims at improving access to finance for small and medium-sized enterprises (SMEs) in the Western Balkans.

In regard to possible overlapping of the activities with those implemented by other donors MTI will have regular meetings with the relevant donors regarding their projects in order to make sure that activities are well coordinated between projects.

CONDITIONS FOR IMPLEMENTATION

Absorption capacity of the MSMEs is the main condition required for implementation of this project. This means that there should be "appetite" within MSMEs for expansion, need for funds and the MSMEs should be able to satisfy the prerequisites set by the PFIs for obtaining loans.

3. IMPLEMENTATION ARRANGEMENTS

ROLES AND RESPONSIBILITIES

The final beneficiaries of the project are Micro, Small, Medium Enterprises in Kosovo.

Indirect beneficiary is Kosovo Agency of Investment Promotion and Enterprise Support (KIESA). KIESA is an institution operating under the Ministry of Trade and Industry and is responsible for protection and promotion of investments, supports application of public policies and programmes for Micro, Small and Medium enterprises and develops policies related to establishment and development of economic zones.

The credit facility will be implemented by the EBRD which will also co-finance the project. The direct grants for enterprises will be prepared and implemented by the EU Office in Kosovo. EUO will also monitor the implementation of the grant contracts as well as the achievement of the objectives of the action.

As this action is aimed at improving access to finance and boosting the competitiveness of Kosovo MSMEs, there will be limited involvement of the Kosovo administration in the implementation of the action (KIESA being a notable exception).

IMPLEMENTATION METHOD(S) AND TYPE(S) OF FINANCING

Implementation of the project will be divided into two components:

1. A credit facility which is foreseen to provide loan subsidisation for businesses and technical assistance to commercial banks and SMEs. The facility would be implemented through **indirect management – a pillar assessed delegation agreement with EBRD**.
2. A facility that foresees grants for Micro and Small Enterprises as described under the section 'Description of Activities'. The facility is to be implemented through **calls for proposals managed by the EU Office in Kosovo (direct management)**. Depending on the needs for detailed information in specific sectors, the sector specific associations will be consulted when developing the CfP. It should be emphasized once again that recipients of Investment Incentives for Enterprises under the Credit facility will not be eligible to apply for grants under the Grant Facility for Enterprises.

Before starting the grant facility Call for proposals the EU Office will coordinate with the EBRD Office in Kosovo on the beneficiaries of the credit facility in order to ensure that there is no overlap of support. The same will be repeated on a monthly basis until the Call for proposals is concluded and grant contracts with beneficiaries have been signed. Afterwards, the coordination meetings will continue in order for EBRD to have the information on the projects supported through the grant facility Performance measurement.

METHODOLOGY FOR MONITORING (AND EVALUATION)

In line with the IPA II Implementing Regulation 447/2014, an IPA II beneficiary who has been entrusted budget implementation tasks of IPA II assistance shall be responsible for conducting evaluations of the programmes it manages.

The European Commission may carry out a mid-term, a final or an ex-post evaluation for this Action or its components via independent consultants, through a joint mission or via an implementing partner. In case a mid-term or final evaluation is not foreseen, the European Commission may, during implementation, decide to undertake such an evaluation for duly justified reasons either on its own decision or on the initiative of the partner. The evaluations will be carried out as prescribed by the DG NEAR guidelines for evaluations. In addition, the Action might be subject to external monitoring in line with the European Commission rules and procedures set in the Financing Agreement.

During the implementation of Activity 1 the Contracting Authority will monitor the implementation of the entire action through contacts with EBRD. Further to this the EBRD will monitor the projects implemented by final beneficiaries as per the contract agreement.

The beneficiaries of the Activity 2 will be monitored by the Contracting Authority.

INDICATOR MEASUREMENT

Indicator	Baseline (value + year) (2)	Target 2020 (3)	Final Target (2025) (4)	Source of information
Doing Business - Distance to frontier (score)	54,35			
Volume of new investments by Kosovo MSMEs	(2016) 0	33 million EUR	33 million EUR	EUO Kosovo and EBRD Kosovo
Number of MSMEs receiving support services	(2016) 0	20 Micro 30 Small 30 Medium	20 Micro 30 Small 30 Medium	EUO Kosovo and EBRD Kosovo
Number of loans provided by PFIs and value of financing mobilised.	Newly established facility	20 million EUR credit lines for 3 to 5 banks for 80 sub-loans (assuming average sub-loan size of EUR 250,000) Grant of 5 million EUR (used for Incentives, TAs to Banks and TAs for SMEs)	A cumulative 40 million EUR assuming the same level of grants as for the previous period Additional 20 million EUR credit lines for 3 to 5 banks for 80 sub-loans (assuming average sub-loan size of EUR 250,000) Grant of 5 million EUR (used for Incentives, TAs to	EBRD Resident Office and Financial Institutions Team

			Banks and TAs for SMEs)	
Number of new jobs created within supported MSMEs	(2016) 0	120	160	EUO Kosovo
Number of eligible MSMEs supported by EU assistance	(2016) 0	80	80	EUO Kosovo
Total amount of finance provided to eligible MSMEs	(2016) 0	30 million EUR	30 million EUR	EUO Kosovo
Number of grants/loans to women entrepreneurs ²	(2016) 0	10	10	EUO Kosovo

² Out of 80 MSMEs, 10 of them (12.5 %), will be to the benefit of women; It is considered that this AD contributes to Gender Equality.

5. SECTOR APPROACH ASSESSMENT

Private Sector Development Strategy - The Strategy of the Ministry of Trade and Industry for the Private Sector Development represent the key sector document an effort to increase employment and reduce poverty, aims to create a globally competitive private sector. The strategy provides a framework for possible interventions by central and local government, the private sector and non-governmental organizations. These interventions will foster changes necessary for achieving social welfare, modern infrastructure, sustainable economic development, as well as providing efficient public services. This strategy aims to fulfil the entire legal environment in order to create the right conditions that would stimulate investments and removal of administrative barriers with an end result of increasing investments in the private sector. The private sector development strategy is being amended to 2016-2021.

Concept of the Industrial Policy 2020 – This Concept represents a platform of relevant theories, and links them with sector specific policies with imperative of NDS 2020. It comprises of sector based analysis, out of which particular shared and sector-specific needs have been identified. In particular, industry modernization and supporting development of cluster have been foreseen as immediate areas of intervention for achieving higher and sustainable economic growth and creation of new jobs in Kosovo.

Ministry of Labour and Social Welfare Draft Sector Strategy 2014 – 2020- The mission of this Strategy is the development, implementation and coordination of policies, laws and other instruments to ensure social protection and inclusion, skills and employment opportunities for all the citizens of Kosovo.

The project proposal is well in line with the **Sectorial Strategy 2014-2020** which determines four (4) strategic objectives that cover vital segments of the sector and include: a) employment and vocational training, b) social welfare, c) pension system and d) social dialogue and labour.

Sector and Donor Coordination - Donor Coordination is the responsibility the respective beneficiary institutions, which hosts regular meetings of thematic sub-working groups, as a means of coordinating donor project planning in various sectors. On the project implementation level, project coordination is taking place through the monthly meetings of donor project managers, exchanging experiences and ideas, in an effort to achieve synergies and avoid over-lapping of activities.

Medium Term Expenditure Framework (MTEF 2017-2019)³ represents the main document on the basis of which the budget of Government of Kosovo is being developed. The main purpose of MTEF is to provide an analysis based on the macroeconomic environment and to set the basis for budget planning for the coming years in accordance with the strategic priorities of the Government.

In early 2015, the Government's Programme for Kosovo was developed and approved, where policy priorities for the coming years were presented. The programme was the document on the basis of which the National Development Strategy was drafted together with the Economic Reform Programme.

The main pillars of the government's program are economic development, employment and the welfare of the population. One of the priority sectors identified in these strategic documents is the support to young and existing entrepreneurs, as well as potential foreign investors. This support will be accompanied by a new and innovative approach of which will enable businesses to develop more solid and better access finance.

6. CROSS-CUTTING ISSUES

GENDER MAINSTREAMING

Even though the gender gaps remain in many areas and in the labour market, women will be supported through different projects and programs and encouraged to participate in activities of EU funded projects. Their equal rights in Kosovo are guaranteed with the Law No. 05/L -020. on gender equality. Businesses owned by women will be prioritised in getting the benefits from this project; in addition, women being

³ <http://mf.rks-gov.net/desk/inc/media/711403B5-C840-4CDD-8518-0CF67F169DE5.pdf>

employees of businesses will be treated in priority while being selected to attend trainings provided by this project.

EQUAL OPPORTUNITIES

Equal opportunity will be taken into account in the preparation of all tender documents and in the recruitment of personnel through the placement of appropriate wording, equal opportunity will be granted while in the implementation of the project.

MINORITIES AND VULNERABLE GROUPS

Minorities are to be treated equally, as guaranteed by Amendment No. 59 to the Constitution of Kosovo.

ENGAGEMENT WITH CIVIL SOCIETY (AND IF RELEVANT OTHER STAKEHOLDERS)

Civil society/stakeholder involvement will be taken into consideration in all aspects of EU-funded activities in order to support civil society organisations to strengthen their capacities and professionalism, allowing them to engage in an effective dialogue with public and private actors and to monitor developments in different areas including free movement of goods.

ENVIRONMENT AND CLIMATE CHANGE (AND IF RELEVANT DISASTER RESILIENCE)

The environment will be highly considered within this project, in addition to specific actions dedicated to environment, in particular as concerns environment impact assessments. Disaster resilience and risk prevention and management should be integrated in the planning, preparation and implementation of projects. In addition, the action will aim to support green investments (energy saving equipment, energy efficiency measures and investment in renewables).

The action will have indirect environmental impact as the final beneficiaries will have to include elements related to environment protection and energy efficiency when implementing the projects. The budgeting at the current moment is not possible as the action will not support specifically environment and climate change.

7. SUSTAINABILITY

The Ministry of Trade and Industry commits itself to transferring the knowledge gained during the implementation of the action to the private sector. The relevant unit in KIESA which deals with the business advisory will be available for offering constant consultancy to businesses. The coordination between the relevant institutions will be continuously improved.

The past IPA projects have demonstrated the need of companies in Kosovo for easier and better access to finance along with easy access to business advisory services. The combination of the two will increase financial and professional capacities for business development and increase entrepreneurship. The action will also complement the activities of the MTI, such as credit guarantee facility, and support to exporting companies. The business advisory services will assist in ensuring sustainability of the action as it will provide the entrepreneurs with better knowledge on conducting business.

8. COMMUNICATION AND VISIBILITY

Communication and visibility will be given high importance during the implementation of the Action. The implementation of the communication activities shall be the responsibility of the IPA II beneficiary, and shall be funded from the amounts allocated to the Action.

All necessary measures will be taken to publicise the fact that the Action has received funding from the EU in line with the Communication and Visibility Manual for EU External Actions. Additional Visibility Guidelines developed by the European Commission (DG NEAR) will have to be followed.

Visibility and communication actions shall demonstrate how the intervention contributes to the agreed programme objectives. Actions shall be aimed at strengthening general public awareness and support of interventions financed and the objectives pursued. The actions shall aim at highlighting to the relevant

target audiences the added value and impact of the EU's interventions and will promote transparency and accountability on the use of funds.

The European Union Office in Kosovo has developed clear visibility guidelines and ensures that all projects which are implemented in Kosovo are fully in line with these guidelines. Project visibility is also clearly stipulated in all contractual documents whereby the contractors/implementers are obliged to adhere to all EU visibility requirements. Awareness campaigns are included within the project activities with clear information for the public and for the final recipients that the financing is EU support. The EU Office will be present in opening events and inaugurations and will publish successful stories in social media.

In the case of first activity (implemented by EBRD), the visibility materials which will be produced (brochure, leaflets, newsletters) will have clear indications on the support provided by the EU to the final beneficiaries.

In addition, the EU Office will be present in opening events and inaugurations and will publish successful stories in social media.

It is the responsibility of the beneficiary to keep the European Union Office fully informed of the planning and implementation of the specific visibility and communication activities.

The beneficiary shall report on its visibility and communication actions in the report submitted to the IPA monitoring committee and the sectoral monitoring committees.