Global Economic Crisis and Its Reflection in Kosovo Financial System

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Abstract

This paper intends to analyse the impact of global economic crisis on the economy of Kosovo with the focus on the impact of crisis on financial system of the country. For the purpose of analysing the global crisis impact on specific sectors of the economy of Kosovo, this paper begins by explain the roots of the global crisis, and the impact of the crisis in the region of Western Balkan by identifying and analysing fluctuations of major macroeconomic indicator of the economy, which is the GDP of Kosovo and Western Balkan countries for comparative analysis. In this regard the paper furthermore analyses the trends of macroeconomics indicators that reflect the development and macroeconomic balances of Kosovo economy in period of 2007-2012, such as GDP, Trade Balance, CPI, Unemployment Rates, Remittances, and FDI. Furthermore, specifically analysis the reflection of global crisis in financial system by analysing the main developments of banking sector and pensions fond as major pillars of financial system .Additionally this paper by considering reports, academic journals, and different studies in view of economic development of Kosovo during the global economic crisis, presents applied fiscal policies of government during that period and the respond of financial system itself toward crisis.

Keywords: *Global Crisis, Effect, Kosovo Financial System, Financial Indicators*

1. Introduction and Background

The existing world open economy has been hugely affected by the last financial crisis triggered by “Housing Bubble” of financial institutions in Wall Street in 2007. Due to Globalization, sophisticated banking products and financial engineering, the crisis has hit fast and wide all major players of world economy like U.S., European Union countries, Japan, Far East and later with different nuances other emerging and developing countries.

The crisis primarily has included the banking Sector and Capital markets on the U.S. but since financial institution are main source of founding, it had a chain effect to other economic activities and was spread to real economy soon to reach the peak in 2009, while global economy experienced the deepest economic recession since the Great Depression (1929-33).

Roots of the last financial crisis entitled to be the application of the system of risky mortgage loans, known as “”*sub-prime*” initially by U.S. financial institution, based on which they issued securities, and sold them to big financial institution, other banks and insurance companies through packing in complex financial arrangements (Tmava and Peci et al., 2013).The sources of the crisis that let to “Housing Bubble” in U.S. through sub-prime loans according to Ramosaj lies in the three pillars of the functioning of banking institutions: “the inadequate management of credit risk and liberalization of excessive lending policies, inadequate capitalization of the banking institutions and inadequate management of their liquidity”(2010, p.3).Furthermore, he described the following metalized factors that caused the crisis:

- “Rapid rise for years of assessment of real property disproportionate to incomes and other economic factors (inflation, growth) known as the Housing Bubble in the U.S.
- The emergence of different types of loans in real estate sector known as subprime;
- Undervalued credit risk due to the intensification of competition in financial markets; Creation of more complex financial instruments, where many banks were unable to adequately manage risk, - and regulations and instruments that have not fit properly because of excessive deregulation failed to understand the challenge” (Ramosaj, 2010, p.4)

According to the majority of financial analysts the above mention factors were the origins of the crisis which resulted in slowdown of economy, consequently in 2009 world GDP and the economic slowdown was global and growth slowed in every region of the world. Whereas the developed economies, central and southern Europe, the former Soviet countries, as well as Latin America and the Caribbean experienced actual recession, the rest of the world experienced lower, but still positive growth including some countries of South Eastern Europe (Gamberoni and Uexkull et al., 2010).

Crisis has slowdown real sector of economy, by shrinking the final output produced that was reflected globally on countries' GDP, which is the main macroeconomic indicator that purelyshows the sum of market price value of all final goods and services produced by each country(Schiller, 2008).The table number 1. below shows growth of GDP impacted by the crisis and the disparity between advanced economies and emerging economies.

Table 1. GDP growth in (%), constant prices of country groups for period of 2008-12

Country Group Name	2008	2009	2010	2011	2012
World	2.698	-0.38	5.192	3.905	3.177
Advanced economies	0.1	-3.434	3.043	1.688	1.467
Euro area	0.376	-4.404	1.965	1.549	-0.641
Major advanced economies (G7)	-0.301	-3.779	2.828	1.557	1.747
European Union	0.588	-4.414	1.983	1.706	-0.302
Emerging market and developing economies	5.845	3.099	7.537	6.231	4.915
Central and eastern Europe	3.163	-3.614	4.613	5.41	1.418
Developing Asia	7.329	7.702	9.794	7.812	6.409
ASEAN-5	4.741	1.772	6.972	4.53	6.161
Latin America and the Caribbean	4.234	-1.223	5.994	4.593	2.934
Middle East and North Africa	5.043	2.99	5.515	3.899	4.608
Sub-Saharan Africa	5.702	2.636	5.614	5.489	4.855

Source: International Monetary Fund, World Economic Outlook Database, October 2013

This financial crisis has been manifested globally and due to high degree of integration the effect of recession emerged in real sectors of economies that are not directly affected by financial crisis (Thaci, 2012). Therefore countries like Kosovo and Western Balkan in general are affected later and indirectly by the crisis, whereas for analysing the effects of this economic crisis for Kosovo and the Western Balkan, this paper is consisted of three main sections. The first section intends to illustrate through main macroeconomics indicators the impact of the last global economic crisis in Kosovo and the Region. The second section aims to explain the refection of global crisis to Kosovo financial system, particular in banking system, while in the third section, is conducted a quantitative analysis of Kosovo government policy and financial sector strategy in order to deal with the crisis and finally, the paper's brief conclusions are presented.

1.1 Research Method

Main objective of this paper is to theoretically explain the effects of global financial crises in Kosovo emerging economy with the focus on its financial system, and suggest future reforms in this sector. Therefore, to provide answer for this research objective a comprehensive and up-to dated literature review is conducted on the impact of the crisis in the region of Western Balkan, including Kosovo. However, since Kosovo financial system is underdeveloped and mostly is consider to be isolated the selection methodology for materials and publication is based on materials that provide data to identifying and analysing fluctuations of major macroeconomic indicator of the economy, which indirectly have affected finical system in Kosovo. In this regard materials and publications selected for analyse tend to present the trends of macroeconomics indicators that reflect the development and macroeconomic balances of Kosovo economy in immediate period during and after the crises. Findings and conclusion of this paper are based on analysis of those selected materials and analysis of financial system data provided by public institution of Kosovo.

2. Main Macroeconomic Developments

Advanced economy indisputably have been impacted by the global financial crisis, moreover in many developing countries the crisis has manifested itself mainly in terms of trade and investment links, including a drop in commodity prices, exports, remittances and foreign direct investment (Koro, 2009).Kosovo with an emerging economy is still consider to be the poorest country in Europe, but just like most of Western Balkan countries*(including; Albania, Bosnia and Herzegovina, Croatia, Kosovo, FYR Macedonia, Serbia and Montenegro)* is characterized as a developing country that has relatively lower openness to world economy, with stable banking system that have been minimally affected by financial crisis (Pere and Hashorva, 2012).

Therefore, the effect of crisis in Western Balkan including Kosovo, in contrast with other countries in Europe was first felt in 2009 (Uvalic, 2014**)** when most of developing countries in Balkan have been faced with negative growth of GDP (Eid and Khawasek, 2013)with exclusion of Kosovo and Albania that had positive GDP growth, but lower than the previous years. Even though immediately next year all of Western Balkan countries moved to positive increase of GDP with lone exception of Croatia, the impact of the crisis have been evident and the continuity of Euro Crises, impacted the downturn of economy the flowing years particularly in 2012. Accordingly, to GDP indicators the impact of the U.S. financial crisis has been prolonged and reached later to Western Balkan Countries but the effects are lasting.

Table 2. GDP growth percent (%) for Western Balkan Countries

Country	2008	2009	2010	2011(est)	2012(est)
Albania	7.536	3.315	3.8	2.8	1.6
Bosnia and Herzegovina	5.582	-2.911	0.722	1.264	-0.7
Croatia	2.084	-6.947	-2.272	-0.047	-1.976
Kosovo	7.223	3.469	3.211	5.186	2.346
FYR Macedonia	5	-0.92	2.895	2.861	-0.267
Montenegro	6.9	-5.7	2.464	3.222	-0.545
Serbia	3.819	-3.506	1.007	1.567	-1.746

Source: International Monetary Fund, World Economic Outlook Database, October 2013

The low impact of global crisis in developing economies raised the multi-polar world (Bank Negara Malaysia, 2012, pp. 85-90), and is related to several factors, among these factors are: the integration of these economies to the global economy; increasing of the prices during the crisis in the global economy, partially reducing of remittances from emigrants as result of the crisis in host countries, decline of the direct foreign aids; the difficulties of borrowing from banks, decrease of consumption, etc (Lubrani, 2009;Koro, 2009*;* Pere and Hashorva, 2012). For example Croatia which is a European Union Country has higher economic openness index has been affected much more from Euro Crises, as results their GDP is negative during the whole period of 2009-12.

The effect of these factors are certainly diverse in different countries, sometimes even contradictor and are related to their characteristics especially in Kosovo case, which main macroeconomic indicators hugely differ from the rest of neighbour countries with exception of Albania which has more similar trends.

Tabel 3. Kosovo Main Economic Indicators

	2008	2009	2010	2011	2012	2013 proj.
GDP (millions of Euros)	3,851	3,912	4,216	4,637	4,885	5,169
GDP (in %)	6.9	2.9	3.9	5	2.7	3.2
CPI, period average (in %)	9.4	-2.4	3.5	7.3	2.5	2.2
Revenues, incl. int. in % of GDP	24.5	29.3	27.6	28.1	27.8	27.6
Primary expenditures in % of GDP	24.7	29.9	30	29.8	30.3	30.7
Overall balance in % of GDP	-0.2	-0.7	-2.6	-1.9	-2.7	-3.5
Exports (mill euro)	218	177	305	322	289	307
Imports (mill euro)	1,886	1,851	2,081	2,412	2,474	2,566
Trade balance (mill euro)	-1,669	-1,673	-1,776	-2,090	-2,185	-2,259
FDI, net (in mill euro)	342	277	358	371	321	674
C/A balance (% of GDP)	-15	-15	-17	-20	-21	-21
Worker remittances (in mill euro)	535	506	512	548	557	568
Official transfers (in mill euro)	289	401	361	273	273	201

Source: IMF Kosovo Main Indicators, 2008-14Annex to the Assessment letter for the World Bank, 2012

The table above shows that effects of crisis can be noticed mostly in 2009 and partially to some indicators in 2012, because most of trends deviation occurredon those two years. Growth of real GDP slowed from 6.9%in 2008 to 3.9-4.2%in 2009-10, with an increase of 4.68 -4.88% in 2011-12. High trade deficit of Kosovo during this period has been negatively influenced the GDP growth.

However, both import and exports are increased during 2007-2012 period, with the exception of 2009 that the volume of both exports and imports of imported goods and services was negative, imports decreased -2.5% in 2009, while for other years the demand for imports as well as export's also increased with exception 2012 which results in decrease of volume of exported goods and services, which is e direct reflection of economy crisis in Europe. Initially the declining of exports was a result of considerable declining of demand, and declining the prices of basic metals in metal stock exchange, because basic metals covered approximately 2/3 of the total exported goods of Kosovo, which also explains the huge growth of demand in 2010 of exports.

Kosovo's budget revenues consist mainly of border taxes constantly increased, but even that the traded volume has been smaller in 2009 Kosovo's state budget revenues increased during that period. Additional indicator of growth of Kosovo economy has been an increase in government expenditures that reaches 29.7% GDP in 2010 mostly in infrastructure that influenced the structure of imported goods to shift from consumer goods to equipment and machinery.

Figure number 1. Shows the fluctuation of CPI percentage during the period of 2007-11, were there was very high inflation percentage in 2008 with an average 9.4%, while in 2009 was recorded -2.41% deflation due to effects of crisis, but immediately in the following two years was recorded a staidly increases of CPI to again follow with decrease in 2012.

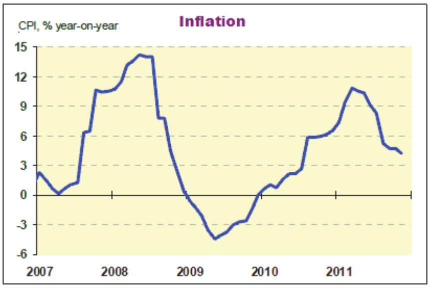

Figure 1. Consumer Price Index (CPI) % fluctuation during 2007-11
Source: EU Candidate and Pre-Accession Countries' Economies Quarterly Reports – CCEQ, 2012

Another indicator that can show the impact of the crisis is the unemployment ration which has been even before the crisis a concern for Western Balkan Countries and especially Kosovo with around 45 % unemployed of total labour force for 2010, while data's of International monetary Fund-IMF for World Economic Outlook(2013),for Western Balkan countries recorded the highest unemployment ration in 2012 and not 2009, since the Euro crises influenced more directly Western Balkan Countries in that period. In 2012 *Results of the Kosovo 2012 Labour Force Survey* (2013) conducted by Kosovo Statistic Agency shows unemployment rate in Kosovo to bereduce to 36.9%, which is another factor that indicates that Kosovo has been less severely impacted country in Balkans by the crisis.

Annual Report of Central Bank of Kosovo (CBK)in 2008 indicates that remittances inflows in Kosovo count on total of around 14%ofcountry's GDP, while in 2012remittancesmade around 11.4 % of GDP. This negative shift of percentage of remittances in relation with GDP is not significant because around 64% of remittance inflows come from euro countries mainly from Germany which has been not impacted severely by crisis."Impulse models" developed by IMF Country Report No. 223 (2013)Kosovo impulse response functions confirm dependence on—and vulnerability to—developments in host countries of emigrants. Hosting country of most of Kosovo emigrants Germany, Switzerland and UK, in2011 accounted for over half of remittance transfers to Kosovo, and have over the years contributed to about 40 percent of overall yearly Foreign Direct Investments(FDI) inflows since 2007 (*Country Report nr.223*, 2013).Those countries especially Germany and Switzerland were less affected by the crisis and the reduction of amount of remittances in Kosovo were non-significant in comparison withthe manner those remittances has been spend. Consumption preferences shifted to basic commodities, resulting that the impact of remittances mostly to be felt by construction industry and capital investments in general, because during crises periods most of remittances inflows were spend for basic goods and services, but not capital investments.

The decrease of remittances reflected in decrease in consumption and particular in capital investments, meanwhile Kosovo's economy is also significantly dependent on donor funds that have been drastically reduced in that period, and in combination with lower Foreign Direct Investments (FDI)and structure of the economy, directly influenced lower economy growth and lower economic activity of Kosovo.

3. Reflection of Global Crisis in Kosovo Financial System

Financial sector of Kosovo is the newest in the region since it began to function in early 2000 and is underdeveloped comparing to with the Western Europe countries and to some extend is less developed to region countries too. It consist of banking sector which includes 9 privately owned commercial banks represented around 72.6 percent of total assets with 89% foreign equity ownership, the insurance companies which make up 3.4% of total financial sector assets counting13 insurance companies with majority of foreign equity ownership, 18 microfinance institution with 2.9% of total assets and 2 pension funds also participate by around 21.1 percent of the total financial sector assets (*Financial Report - CBK*, 2013)

Financial Structure in Kosovo is dominated by banking sector which is the main pillar of financial system and has been one of the driving forces of Kosovo continuous economic development, therefore, the focus of analysing and evaluating of this paper will be on banking sector.

Fortunately for Kosovo the banking sector greatly avoided the possible impact of the last financial crisis, mainly due to low exposal to high risk instruments, because Commercial Banks in Kosovo have been offering basic products and mainly was concentrated in lending and borrowing within domestic market, rather than seeking financial sources outside Kosovo. This made Commercial Banks to have low exposure to the negative flows of international financial market and the rates of loaned have been self-regulated and not reliant on international finance.

Thus, in spite of continues development of banking sector in Kosovo, Commercial Banks in crises period still have been offering simple products that are not volunteer to the effect of international financial turbulence. However, this risk will be less inevitable in the future since in the last years financial system in Kosovo has been developing significantly more complex voluntary products and financial instruments that are more related to the international finance such as health, property and professional liability insurance, mortgage loans, private pensions funds, goods and services insurance, etc.

Whereas, on the beginning of the crisis only a part of financial assets of banking and insurance sector were deposited in foreign correspondent banks and only for their needs to perform daily banking transactions, and there were no investments in financial derivative instruments, which were affected by crisis(*Annual Report - CBK*, 2013).Exposure of the banking sector to the external sector remains low both within the assets, as well as obligations. In June 2013, 19.1 percent (%) of total banking sector assets and 5.4 percent (%) of total banking sector liabilities were invested in the external sector. Therefore, the only unsafe sector has been Kosovo Pension and Savings Trust (the Trust) that the impact of the crisis was noticed, due to the fact that most of its financial assets were invested in foreign financial markets. As a result of this, by the end of 2008 and the beginning of 2009 the value of shares invested in foreign markets, declined over 30 percent (%).

In the other hand, dependence of the banking sector to foreign financial resources unlike Kosovo Pension and Savings Trust (the Trust) remained limited, while deposits of non-residents continue to have the highest participation in total liabilities to external sector (51.2 percent in June 2013) compared obtained credit lines from abroad (45.6 percent in June 2013),(*Financial Report - CBK*, 2013).

If we observe the average of credit and deposits growth before 2009 deposit in the commercial banks in Kosovo have had increasing trends and since 2009 the trend was decreasing, the same could be said about loans with the exception of year 2011 there is positive growth trend. This means that the effects of global financial crisis has impacted trends in financial sector especially in 2009, but even during this period the financial sector continued to expanded.

Table 4. Financial indicators of Kosovo banking sector

Financial indicators	2007	2008	2009	2010	2011	2012
Interest rate (3-12 months)	15.25	16.61	14.11	18.24	18.13	16.3
Credit growth (Ann. % ch)	29.7	38.7	17.4	10.1	15.4	8.9
Deposit growth (Ann. % ch)	19.3	25.6	20.3	14.8	12.2	8
Non-performing loans	n/a	3.7	3.9	4.5	5.9	6.5

Source: Financial Report, Central Bank of Kosovo, 2012

The banking sector has supported an increase in loans and deposits with slower rates after the crisis. Interest rates have fluctuated during this period; a decrease was recorded in 2009 from 16.1 % of previous to 14.11%, followed with and increase 18 % in 2010 and 2011reflecting more conservative interest rates started to decrease in 2012 to 16.3 % but still remain higher than in neighbour and European countries.

The increase of interest rates in 2010-11 result in slowness of the lending for economy needs. This slowness in lending by banks happened as prevention since they lead a more conservative policy of issuing loans than in the past, which resulted in the declining of loan portfolio, in particular for SME loans, which now have more difficulties to get the loans. This had a direct negative impact also on the financing of needs for working capital and needs for additional investments (Bartlett and Monastiriotis, 2010).

Another indicator that reflects the impact of crisis to real sector economy in Kosovo is fast increase of growth rate of Non-Performing Loans (NPL). In June 2010, the share of Non-Performing Loans (NPL) to total loans of the banking sector amounted at 4.5 percent. Central Bank of Kosovo in Annual Report (2013)during the period 2008-2012, reported an annual growth average rate of NPL value to 26.8 percent (%), while the average rate of growth of total credit was 22percent(%) and in June of 2011 it reached to 30.6%.

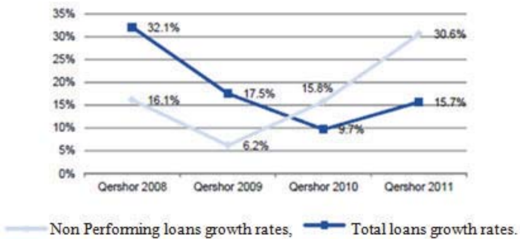

Figure 2. Percentage of growth rates of Loans in total and NPL for of 2008-2011
Source: Financial Report, Central Bank of Kosovo, 2011

The graph above, on Figure number 2, shows growth rates of NLP overlapping the growth rate of loans in the beginning of 2010, mainly due to the fact that Banks have been adopting more conservative policy's for high risky loans that affected the ability of some sector mostly SME to finance their business needs. That in combination with lower economic activity caused by reduced demand due to crisis, increased NPL over the years and the same trend has continued in June 2013 when NPL reached 7.8% of total.

In this context, the increase in NPL to some extent can be attributed to construction sector because of collapse of property market of Kosovo due to downfall demand for new apartments, which to some extent can be attributed to the decline of purchases from Kosovo immigrants. Also, the reduction of demand for exports Kosovo may have negatively affected the ability of manufacturing industry to repay the loans, thus affecting the growth of NPL in this sector.

4. Government Response to Externalities

Kosovo Government during the 2007 – 2013even though used market based policies for corrective taxes and subsidies to internalize the externality by taxing activities that have negative externalities and subsidizing activities that have positive externalities(Mankiw, 2012), did not immediately follow any particular fiscal policies or take direct steps to prevent or react towards global crises.

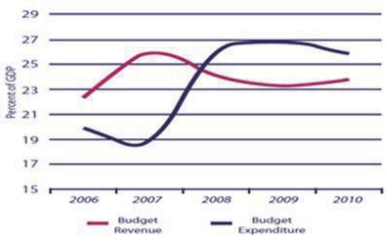

Figure 3. Kosovo Budged Revenue and Budget Expenditure 2006-10
Source: Kosovo Midterm Expenditure Framework 2008-2010, Ministry of Finance, 2009

This lethargic or indirect government reaction was primarily instigated, due to the fact that the effects of the crisis in Kosovo economy have been minor because of few transmitting channels or was in shadow of internal economic problems that have ever been present in Kosovo.

However, through "Keynesian"fiscal policies (Schiller, 2008)of new elected government, that started to be implemented in 2007 before the impact of economic crisis in Kosovo (see figure number 3.),influenced growth in both fronts revenues and expenditures, especially huge investments in public infrastructure helped greatly to maintain macro-fiscal stability and influenced growth of Kosovo GDP.

The Figure number 4.below shows the huge difference of government expenditures between year 2007 to 2011. During a period of five years the government capital expenditures have increase for 269%, over 70% of them have been allocated to finance infrastructures development mainly road and education system infrastructure. Goods and services of government expenditures were increased 27% the majority of supplies came from domestic companies, subventions and transfers an increase of 78%, together with wages and allowances that have been increased for 83%, supplemented cash flow in the market and influenced consumption. In total government expenditures from 662 million euro have been increased to 1,411 million euro equalling 113 % growth, that is a huge influence to the Kosovo economy and GDP growth.

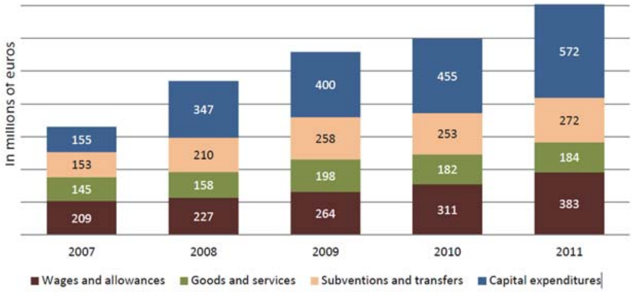

Figure 4. Government Expenditures during 2007-2011
Source: Kosovo Midterm Expenditure Framework 2012-2014, Ministry of Finance, 2011

Continues increase of budged revenues has been as result of; improvement of the performance of collection agencies such as TAX Administration of Kosovo (TAK) and Customs, increase of public expenditures of government, International Monetary Fund soft loans through Stabilisation and Association Agreement (KMF, 2012), and government treasury bonds starting from 2012 used aslong term debt instruments (Shaber K.P., 2011).Both collection agencies TAK and Customs have had a key role in budget increase by doing reforms and installing new information systems, targeting full fiscal functions of all business to prevent and lower the gap of informal economy. More efficient government agencies together with implementation of tax system reforms in 2009, allowed government to increase the revenues in yearly bases through tax collection.

More revenues in combination with sufficient budged reserves in 2007, new source for funds, and a chain effect of growth tax base from year to year by economic growth, made possible to government to adopt those fiscal policies that maintained economic stability and stimulated growth in 2007-2012.

5. Essential Future Reforms for Financial Sector

Banking sector of Kosovo has virtually been intact by global crises due to the fact that is not exposed to external borrowing and has very low financial integration that can affect financial outflows. The real sector of economy has affected the banking sector through lower trade volume, lower demand, and in the other hand lower supply by banks with more conservative policies. However, there are some other features of the banking sector that are worth mentioning that request necessary protective measures that should be taken to improve this sector and mean time to boost economic development.

Primarily, one of the important drawbacks of the banking sector in Kosovo is its high level of concentration. Nine banks are operational, and around 80 percent of the assets are managed by three major banks, however, after 2012 some new merging banks incline lowering this concentration. The high level of concentration and the lack of competition have pushed interest rates to uncompetitive levels because of inelastic demand of market for banking products and price matching strategy through collusive agreements of major players of banking industry (Baye, 2010).

Secondly, the sector has high percent of shares owned by foreign, should change, especially three major commercial banks that are 100 % foreign owned, and that in a time of economic crisis can transmit its effects in Kosovo economy.

And finally, the ratio of bank assets and liabilities to GDP (an indicator of financial integration) is very low compared to the SEE average, an advantage for Kosovo in this time of economic crisis, but a hindrance for economic development, because the high level of financial integration has been a powerful driver of growth in the undeveloped countries (Bartlett and Monastiriotis, 2010).

Therefore, for financial integration of traditional Kosovo Banking sector is more than necessary to create additional mechanisms that will enable advancements in the development of Kosovo's financial sector. Primary Financial market development with special focus in the field of investment on securities which would enable companies, governments and other organizations to trade securities can raise long term funds (Ramosaj, 2010).

Whereas for the Pension Fund as an integral component of financial system of Kosovo, during this years the practice proves that such financial assets would be safer and more profitable if they were invested or deposited in the Kosovo market partially or totally (Tmava and Peci et al., 2013). The risk of impacted by global financial crises would be lower and the cash inflow would boost Kosovo economy, which would increase availability of funds, increasing the supply would result in lower interest rates. The investment within Kosovo economy can be made staidly and deposit could be spread in domestic market and partially to international financial market to minimazed the risk of concentrating within one economy. This suggestion is supported by the fact that the Kosovo Pension Trust starting from the beginning of 2010 has deposited some amounts of its fund in Commercial Banks in Kosovo.

6. Conclusion

Brief analysis of world GDP shows that the last global financial crisis has been evident all over the world, but with different intervals and magnitudes in advanced and emerging economies. Macroeconomic indicators shows that the global economic crisis of 2007 rooted in U.S. have interrupted the positive trend of the development of the Western Balkan Countries, including Kosovo, by shrinking economic growth. Kosovo as an developing country in most emerging economic growth period, have been affected by the crisis 9 - 12 months later than what was reflected in the developed European countries, because of fewer direct transmitting channels of global financial crisis. Though, it could not escape unscathed, the impacts has affected the reduction of investments in private sector, reduction of consumption, lessening economic activity and trade volume resulted in reduction of exports, and imports in 2009, declining of remittances and foreign direct investments, declining of level of lending to corporate consumers, either because of more conservative lending policies applied by banks, or because of the declining of private/corporate capital investments. Decline of growth rate of GDP was one of most significant macroeconomic indicator that could be measured as indicator of crisis impact in Kosovo economy.

Additionally, considering financial system of Kosovo especially banking sector that is more isolated to international finance instruments, did not have symptoms of being directly affected by financial crisis, but have been indirectly affected by real sectors economy, meaning their clientele. Financial sector expanded during the period of crisis, but commercial banks in Kosovo took preventive measures for more efficient risk management and more moderate growth of banking sector. They became more reserved by applying more conservative loan policy, especially when providing loans to SME or new enterprises.

In the other hand structure of the Kosovo economy enhanced more competitive market in this period lowering profit margins, besides that the decline of investments, decline of overall turnover, resulted in fewer profits and recapitalization of corporate consumers of banking products. Therefore, as a result their loan ability has decreased, which caused in fact the reduction of their ability to payback bank debts, consequently the percentage of non-performing loans (NPL) in Kosovo commercial banks continuously resulted in growing trends during that period, which can cause a series of negative consequences for Kosovo economy.

Key findings of this paper that are in line with other similar domestic papers is that Kosovo although its financial system especially banking sector is considered to be isolated to international finance instruments, could not avoid indirect impacts of the financial crisis in domestic market. Moreover, on a final note, based on material and data analyzed an explanation can be drawn that new fiscal policies of Kosovo government elected in the end of 2007, fortuitously coincided with the onset of the crisis. New policies consist of high level of public investments in infrastructure and increase of public employees' wages, helped significantly to mitigate the impact of the crisis, maintaining aggregate demand and continuing the growth trend of GDP, achieved in Kosovo during the period of crisis.

To conclude, there appears to have been two fundamental factors which have offset the impact of the crisis in the case of Kosovo: the low level of economic integration, particular the financial sector, that in time of prosperity is a barrier for economic growth, but in time of crisis is fortunate circumstance, and the other factor is shifting of the government priorities towards capital investments. Taking in consider those factors and post-crisis structural changes in global growth trends, for mid to long term run, the determining factor of growth for Kosovo economy is the level of economic integration, which Kosovo should enhance greatly for further economic development.

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