

# Dutch Disease: The Case of The Republic of Kosovo

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## Abstract

This study examines whether the economy of Kosovo displays symptoms indicative of Dutch Disease, a phenomenon associated with adverse economic effects typically stemming from natural resource discoveries, and in our case from large inflows of foreign exchange. Firstly, the theoretical frameworks surrounding worker remittances, foreign aid, and Dutch Disease are explored, drawing upon a review of relevant literature. Subsequently, an analysis is conducted to ascertain whether Kosovo's economy exhibits key symptoms of Dutch Disease, including inflation, contraction of the manufacturing sector, positive wage growth, and a persistent trade deficit. Finally, the implications of a form of Dutch Disease for Kosovo's long-term economic prospects are discussed.

**Keywords:** Dutch Disease, Worker Remittances, Foreign Aid

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# 1 Introduction

Dutch Disease is a phenomenon historically caused by natural resource discoveries or large inflows of foreign aid. It exhibits characteristics such as the appreciation of the real exchange rate, the prioritization of consumption over investment, the skewing of production towards the sector of non-traded goods, and trade deficit (Corden & Neary, 1982). Some have defined Dutch Disease to be an adverse state of the economy resulting exclusively from a natural resource boom (Rutherford, 1992). Others, on the other hand, have advanced a broader definition that, in addition to natural resources, associates Dutch Disease with foreign exchange inflows involving official international aid or worker remittances (Younger, 1992). Both of these forms of foreign exchange inflows are rather important components of Kosovo's economy. Thus, one might ask, understood in light of the broader definition, is the phenomenon of Dutch Disease present in the economy of Kosovo and what are its implications?

Kosovo is one of the countries with the highest rate of remittance inflows as a percentage of real GDP in Western Balkans. The World Bank (2022) estimates that in 2020 personal remittances received in Kosovo amounted to 1.44 billion US dollars or around 18% of its real GDP. Accordingly, in 2020, the respective values for worker remittances received as a percentage of real GDP were 9.7% for Albania, 12.6% for Montenegro, 7.3% for Serbia, 3.4% for North Macedonia, and 9.6% for Bosnia and Herzegovina. That is to say, Kosovo experiences much higher rates compared to other countries in Southeast Europe. In addition, based on Bujupi (2018), the levels of remittances in Kosovo were comparable with and at times higher than total exports until 2008. Similarly, net official development assistance and official aid received in 2020 was 544 million US dollars, which is an amount considerably higher than in the neighboring countries (World Bank, 2022). Such high levels of official development assistance (ODA) have been persistent throughout the entire postwar period. Total external inflows in postwar Kosovo have at times climbed as high as 35% of GDP (Lemay-Hébert & Murshed, 2016). In Kosovo, therefore, worker remittances and ODA are

crucial aspects of the economy since they represent an extremely large share of the real GDP. As much as they can have positive macroeconomic effects, they can also significantly distort the long run trajectory of the economy.

This paper makes a valuable contribution to the ongoing discourse by conducting a theoretical analysis to determine whether Kosovo's economy demonstrates indicators of the Dutch Disease phenomenon. Notably, it fills a gap in the existing literature pertaining to Kosovo, as no prior studies of comparable scope and focus have been identified. Most of the relevant work focuses solely on a country's economic dependence on remittances – excluding the possibility for additional effects arising from a triggered Dutch Disease. This paper initiates discourse surrounding the Dutch Disease phenomenon and establishes a theoretical connection with worker remittances and ODA for the case of Kosovo. Proper statistical methods of isolating the casual effect, however, are beyond its scope. Nonetheless, it presents an alternative interpretation for the observed elevated inflation, trade deficit, and rent-seeking behavior in Kosovo's economy.

Thus, in the first part we delve into the theoretical underpinnings of a) worker remittances, b) official development aid, and c) Dutch Disease, providing a comprehensive review of the respective literature. Subsequently, in the second part, utilizing sectoral time series data from Kosovo Agency of Statistics, we assess whether Kosovo's economy displays symptoms associated with the Dutch Disease phenomenon, including rising inflation rates, manufacturing sector contraction, higher wages, and trade imbalances.

Our analysis reveals that Kosovo's economy manifests all these characteristics. The causal link itself between worker remittances, ODA, and Dutch Disease, nevertheless, remains an open area for research. Any sufficiently large source of passive income is susceptible to causing Dutch Disease outcomes, if it fundamentally triggers the same economic conduct and processes that natural resource booms do; thus, it remains to see whether Kosovo's high rates of worker remittances and foreign aid can be understood as a form of Dutch Disease.

## 2 Literature Review

### Explaining Worker Remittances

We commonly distinguish between three categories of private foreign inflows, depending on the macroeconomic effects that they induce. Workers' remittances, for example, are private and unrequited transfers of money from migrants to their family members in the country of origin. Employee compensations are salaries or benefits earned by individuals in countries in which they are not residents but work for and are paid for by their residents. The third category, migrants' transfers, are entries that arise from individuals' change of residency. In Kosovo, both employee compensations and migrants' transfers show much lower levels than worker remittances. They are, however, significant insofar as the net migration balance for 2021 in Kosovo was -38,606 persons and there is a rising trend of young people working remotely for other countries and spending their salaries back home (BQK, 2022). However, for the purposes of this paper, our focus will be mostly worker remittances and official development aid.

Indicators such as ODA and employee's compensations tend to be procyclical; that is, when the domestic economy experiences growth, employment compensation, and direct foreign investment also increase, given the prospect of a more stable economy abroad. Worker remittances, on the other hand, usually tend to be countercyclical (Frankel, 2009). Giuliano and Ruiz-Arranz (2006), nevertheless, differentiate between altruistic remittances, which tend to be countercyclical, and self-interested remittances, which are usually procyclical. In the case of Kosovo, worker remittances are usually countercyclical to the business cycles of the domestic economy; that is, altruistically motivated (Bujupi, 2018).

This was evident in the 2008 global financial crisis, in which case Kosovo's economy remained immune to global shocks because there was a massive increase in worker remittances mitigating the potential adverse effects of this global crisis (Pula, 2014). Furthermore, during Covid19 pandemic, worker remittances increased to unprecedented levels (more than doubled), smoothing consumption and reducing potential poverty (Central Bank of Kosovo,

2022). Worker remittances, thus, do improve social welfare in the short term as they increase leisure and consumption levels and smooth income volatility (Acosta, Lartey, and Mandelman, 2009).

Worker remittances, nonetheless, can cause what is known as a moral hazard. That is because they induce rent-seeking behavior on the side of receiving agents, affect labor supply, and distort the productive channeling of savings (Ratha, 2013). They affect labor supply by increasing the reservation wage of remittance recipients, who are then pushed out of the labor market. The decline in labor supply causes an increase in wages, which leads to more expensive (thus less internationally competitive) production, shrinking the respective economic sector (usually, this sector will tend to be the manufacturing one, for reasons that we will explain later). In addition, remittances act like 'rents'. These rents distort agents' economic conduct, causing what is typically known as rent-seeking behavior, which commonly entails the act of advancing personal benefits (governments or individuals), through unproductive channels, at the expense of consumers' benefits.

Some argue that remittances may bring about economic growth, but only in countries with good policies with respect to property rights and contract enforcement (Driffield & Jones, 2013). On the other hand, other authors find that worker remittances might in fact, contribute to the declining quality in institutions due to a lower necessity for governmental accountability and transparency, which is caused by a false sense of remittance "security" (Abdih et al., 2008). As alluded to, the reliance of Kosovo's economy on remittances is indeed concerning, and yet essential, without which, as Korovilas (2010) emphasizes, "Kosovo would be unable to meet the costs of vital imports." However, if the importance of worker remittances is that essential, but they give rise to consequences that are consistent with our understanding of the Dutch Disease, the future trajectory of Kosovo's economy must be navigated with careful consideration as it pertains to these foreign exchange inflows.

## Explaining Foreign Aid

The fundamental role of ODA is to promote economic growth in developing countries. In addition to alleviating poverty, ODA finances investment or increases worker productivity by improving health, education, and technology (Steven Radelet, Michael Clemens, & Rikhil Bhavnani, 2005). Another way through which ODA promotes growth was prescribed by Barron (1990), who suggested that aid could reduce fiscal policy distortions in the receiving countries – which policymakers tend to adopt to generate governmental revenues – by offering a different alternative to finance public expenditures. On the contrary, Boone (1995) argues that policymakers will not adjust distortionary policies even upon receiving foreign aid, as it is not an optimal solution for them to do so and that poverty is not caused solely by long run capital deficiency. Along the same lines, Bauer and Friedman insist that politicians repeatedly fail to allocate ODA properly and that only some groups of people tend to be beneficiaries of it.

According to the Solow model (1956) for growth accounting, stagnant economic growth in the long run is caused by a low total factor of productivity rather than long-run capital or labor deficiency. Institutions, instead, play a crucial role in the long run economic growth of a country, as found by Acemoglu, Johnson, and Robinson (2004).

Contrary to expectations, Alesina and Weder (1999) find that foreign aid allocation decisions are largely unaffected by policymakers' behavior or institutional quality in the recipient country. Their findings suggest that even countries with corrupt governments do not necessarily receive reduced aid. Moreover, their study reveals a positive correlation between foreign aid recipients and countries with higher levels of corruption, challenging conventional assumptions about aid's impact on curbing corruption, or its relevance to it altogether.

Pushed even further, Easterly (2014) and Moyo (2010) suggest that such a correlation is in fact casual – meaning that official aid itself generates dependency, corruption, and currency overvaluation, practically isolating these countries from the global economy.

Similarly, Boone (1996) goes so far as to show that aid only benefits the elite class of

an emerging market economy and that foreign aid indeed fails to achieve its objective for improving the basic indicators of economic development in poorer countries. In his framework, the corrupt elite is continuously subsidized through aid and its bad, but perpetuated, governance only strengthens poverty.

Burnside and Dollar (2000) present a more nuanced perspective, suggesting that the positive impact of aid is contingent upon the presence of sound monetary, fiscal, and trade policies in developing economies. Their findings emphasize the crucial role of institutional quality in determining aid effectiveness. Consequently, they advocate for a systematic and conditional approach to aid distribution, emphasizing the need to align assistance with the institutional context of recipient countries.

Steven Radelet, Michael Clemens, and Mr. Rikhil Bhavnani (2005), find that foreign aid exhibits a positive relationship with economic growth in most countries, but not all. Foreign aid, according to them, can finance investments or improve the accumulation of human capital, whereby it directly results in economic growth. However, they also assert that aid exhibits diminishing marginal returns in the medium to long run course.

Jeffrey Sachs, Joseph Stiglitz, and Nicholas Stern, among others, argue that despite a few cases of failure, in general, aid has assisted in the reduction of poverty; that is, even if it has not necessarily supported economic growth, it has certainly impeded worse economic performance in developing countries, thereby being of great humanitarian importance. But 23 years after the war, one might ask, is Kosovo in a position for humanitarian need? I would argue it is not.

## Explaining Dutch Disease

Dutch Disease occurs when the discovery of natural resources leads to negative economic consequences. This phenomenon is often referred to as a "resource curse," though some academics question this relationship (Sachs, Warner, Oomes, & Kalcheva, 1995, 2001, 2007). Dutch Disease typically leads to long run lower economic growth. As disposable incomes

increase due to observed growth in foreign exchange, stemming from natural resource booms, domestic aggregate demand increases for both traded and non-traded goods.

Non-traded goods demand can only be satisfied by domestic production (e.g., hotel services). The demand for traded goods, on the other hand, can be satisfied by increasing imports. As a result, when aggregate demand increases due to a resource boom, within the non-traded goods sector prices and wages increase faster, attracting more labor supply from the tradable sector to the non-tradable one. On the other hand, prices in the tradable sector converge to those abroad, as import levels become higher. Therefore, most of the manufacturing firms (corresponding to the tradable sector) have to correspondingly increase wages and simultaneously compete with the prices of imported and substitutable goods, which results in lower profits, and subsequent downsizing of the domestic firms. This causes, in other words, the tradable sector to shrink and renders it unable to compete in the international market (through the appreciation of the real exchange rate).

One could argue, however, that such a transition from the tradable sector to the non-tradable one is consistent with the theory that open economies and trade bring about specialization and, in fact, increase the overall utility of the economy. That is, if one sector of the economy has a comparative advantage, then it is expected for the economy to focus its resources in that sector, making consumers better off. There are two problems with this argument. First, in countries like Kosovo, the expansion of the non-traded sector did not occur because it exhibited comparative advantage per se, but rather because of an externally induced new equilibrium through foreign assistance. Secondly, the tradable sector, including industries like manufacturing, is characterized by more competition, innovation, and technological spillovers than any other economic sector (Oomes and Kalcheva, 2007). Therefore, the contraction of the manufacturing sector diminishes the long run utility of Kosovo's economy and the service sector can not provide enough to mitigate losses in competition, quality, innovation, etc.

The process, often termed "deindustrialization" (Corden and Neary, 1982), reflects a



shift between economic sectors, with implications for production factors. This structural transformation impacts labor transitions, aligning with the framework of the Lewis model. Extending the Solow model (1956), the Lewis model introduces two additional sectors: a traditional, less productive sector (commonly agriculture) and a modern, highly productive one (like manufacturing). It emphasizes the significance of reallocating labor from the former to the latter as a crucial driver of industrialization and economic advancement. In the case of Dutch Disease it appears that such a reallocation of labor manifests an inverse direction. The labor is moved from the manufacturing sector – which is more productive in the long run – to the service one - which is less productive. This inverse transition causes direct deindustrialization of the economy – a well-known symptom of Dutch Disease.

There are four noticeable channels through which Dutch Disease negatively impacts an economy: i) the appreciation of the real exchange rate, ii) the contraction of the traded goods sector, iii) wage growth, and iv) trade deficit. In the following section, we will examine each of these indicators in relation to the economy of Kosovo, aiming to ascertain whether Kosovo's economy exhibits symptoms consistent with Dutch Disease.

The appreciation of the real exchange rate occurs when the value of the domestic currency increases relative to other currencies. This makes exports less competitive in international markets, leading to a decline in export-oriented industries, but even further, directly affects domestic production in an open economy. This brings us to the contraction of the traded goods sector. Industries involved in producing goods either for export or domestic use, may shrink as a result of factors like reduced competitiveness due to currency appreciation or resource sector dominance. Thirdly, the influx of wealth from the natural resource boom leads to increased wages across the economy. While this may initially seem positive, it often causes inflation and reduces competitiveness in all other sectors. Lastly, Dutch Disease can cause an imbalance between imports and exports, where a country imports more than it exports. This can occur because usually resource exports generate significant revenue, and with higher revenues, reliance on imported goods increases, while incentives to produce

domestically fall.

### 3 Data and Results

#### Real Exchange Rate Appreciation and Inflation

Kosovo has unilaterally adopted the Euro in 2002 and therefore employs a fixed exchange rate regime. As the country becomes richer and the level of prices increases, under the fixed exchange rate regime, the economy experiences inflation because it is incapable of devaluing its currency. Furthermore, where flexible exchange rate regimes face appreciation of real exchange rate, fixed exchange rate regimes face inflation (Oomes and Kalcheva, 2007). Indeed, both inflation and economic growth tend to be more volatile under a fixed exchange rate regime (IMF, 2017). Analysis of data from the Kosovo Agency of Statistics (2022) reveals a concerning trend: since 2003, Kosovo has experienced both high and fluctuating levels of inflation, as depicted in Figure 1. Despite the strategic decision to adopt the Euro and relinquish monetary autonomy, aiming to ensure a regime of low and consistent inflation, these desired outcomes have frequently proven unachievable.

During the first two trimesters of 2022, Kosovo, alongside Montenegro that has also adopted the Euro currency, faced the highest inflation rates in the Western Balkans, largely attributed to disruptions in the global supply chain caused by the Covid-19 pandemic. But to identify this economic issue as attributable to Dutch Disease, we need to focus on long-lasting factors, not just temporary effects from recessions. On the other hand, we have to avoid wrongly labeling Kosovo's economy as always in recession or constantly facing shocks, if inflation and other indicators are persistent.

Figure 2 illustrates a significant price disparity between traded goods and non-tradables, indicating a potential reliance on imports to meet domestic demand for traded goods, influenced by foreign market prices. This then causes domestic inflation in Kosovo. Alternatively,

this could signify an increase in wages within the tradable sector, which as we saw earlier is a common effect of Dutch Disease. However, these observations alone do not definitively suggest the presence of Dutch Disease, which here we would associate with high levels of remittances and foreign aid inflow. A comprehensive study, accounting for factors such as government consumption, net international reserves, productivity differentials, and corruption levels, is necessary to establish causation accurately, but that is beyond the scope of what we aim to establish here.

## Contraction of the Manufacturing Sector

To test whether there has been a decline in the manufacturing sector and an expansion of the service sector, we use sectoral data from the Central Bank of Kosovo (2022). We first observe whether output in respective sectors has shrunk or expanded as a share of the real GDP. We find that the manufacturing sector has had a relatively small output decrease as a share of GDP, whereas the service sector has marginally increased (Figure 3). That is, the percentage share of the non-tradable sector was 52.5% in 2008 and 54.3% in 2021, exhibiting volatility in between.

The absence of consistent absolute growth or decline in both sectors suggests that absolute deindustrialization has not occurred. However, in line with Oomes and Kalcheva (2007), we cannot definitively dismiss the potential presence of Dutch Disease in Kosovo's economy. According to the Dutch Disease framework, a country typically experiences either a modest decline in its manufacturing sector or sluggish growth, indicative of relative deindustrialization. Therefore, the evidence presented here can only be disregarded after considering other factors that may have contributed to the relative decline in manufacturing. One such factor could be transitional effects, particularly relevant to Kosovo's transition from a socialist entity within Yugoslavia to a liberal democracy. Any future investigation in this domain must account for the potential economic distortions stemming from transition-induced externali-

ties in post-war Kosovo.

Upon analyzing the sectoral employment distribution provided by the Kosovo Agency for Statistics (2022), we observe a significant gap in employment levels between the service and manufacturing sectors. Specifically, employment in the service sector surpasses that in manufacturing by more than threefold. Furthermore, while the service sector has seen consistent employment growth since 2008, the manufacturing sector has experienced a modest decline in employment growth over the same period (refer to Figure 4). This disparity in sectoral employment can be understood as a potential outcome of Dutch Disease, aligning with the theory that it prompts a shift in production factors from the traded goods sector to the non-traded goods sector, particularly in terms of labor concentration. Nevertheless, here too we must allow for the possibility of omitted variables that might have caused the skewing of labor towards the service sector.

## Wage Price Increase

As depicted in Figures 5 and 6, we identify another indication of the Dutch Disease within Kosovo's economy. Driven by significant inflows of remittances and foreign aid, alongside overall GDP growth, the average wage level demonstrates an upward trajectory. This trend aligns with the spending effect and external income inflows described by Oomes and Kalcheva (2007), which elevate the wage reservation level and alter the production structure within the economy. However, three additional explanations merit consideration regarding the observed wage growth in Kosovo, as outlined by Oomes and Kalcheva (2007) in the context of Russia.

Firstly, the wage increase could stem from the documentation of previously unrecorded wage levels, reflecting a mere distortion resulting from the formalization of the economy – a phenomenon termed de-shadowization by these authors. This observation aligns with Kosovo's socio-economic history, where documentation of economic data was limited before 1999 when it was part of Yugoslavia. The lack of comprehensive records prior to this period

underscores the potential for distortions in wage data resulting from the formalization of the economy in more recent years. Secondly, given the suspension of most economic activities during the war, the subsequent wage growth may primarily signify the economic rebound of Kosovo. Lastly, global wage growth over the past decade due to overall productivity advancements offers another plausible explanation for our findings.

## Trade Deficit

Lemay-Hébert and Murshed (2016) were among the first to highlight that the substantial trade deficit in Kosovo mirrors a classic symptom of Dutch Disease, a finding consistent with our own research shown in Figure 7. Since 2001, Kosovo has consistently maintained a positive trade deficit, indicating that imports have consistently exceeded exports in the post-war era. This surge in imports could stem from either the domestic economy's inability to meet growing demand or the lack of competitiveness in domestically produced goods.

Moreover, stagnant export growth over the past two decades suggests that production levels have failed to meet both domestic and international demand. Specifically, manufacturing production has been absent to a degree that would have had meaningful economic impact. As Kosovo receives significant inflows of remittances and foreign aid, it relies on imported goods rather than developing domestic industries. This in effect contributes to trade deficit.

## 4 Discussions

Lemay-Hébert and Murshed (2016) assert that the economy of Kosovo shows Dutch Disease due to its continued reliance on emigration and worker remittances, as a form of passive revenues, analogous to natural resource booms. However, our focus in this paper was not to

confirm this causal link. Rather, we sought to identify and confirm the presence of Dutch Disease symptoms themselves. By doing so, we have paved the way for further statistical studies to test whether a relationship indeed exists between worker remittances and the Dutch Disease in Kosovo. This nuanced approach allows for a more comprehensive understanding of the economic dynamics at play, through a theoretical perspective, and sets the stage for future research to delve deeper into this potential relationship.

While we may not necessarily call the phenomenon as Dutch Disease, the similarities in the effects of foreign aid inflows and remittances, as opposed to natural resource booms, offer valuable insights. In fact, the paper's primary focus is not on exploring the connection between remittances or foreign inflows and Dutch Disease itself. If these effects resemble those traditionally associated with Dutch Disease, then there is much to be learned from studying its mechanisms and implications, and we are sufficed by that. By understanding how foreign aid and remittances impact the economy in a manner akin to Dutch Disease, we can better comprehend the challenges and opportunities they present. This encourages us to draw lessons from Dutch Disease theory while remaining open to the unique dynamics of Kosovo's economic context.

This paper explores the literature surrounding worker remittances and their potential impact on the economy. While opinions and findings vary, there is strong evidence advocating for the thorough examination of worker remittances and the precise identification of their consequences to avoid economic distortions, making it a priority for policymakers.

We discuss the theory surrounding Official Development Assistance (ODA). Aid, in general, is often viewed as having an adverse effect on long term growth, with a historically low success rate. Similar to worker remittances, aid distribution requires careful allocation and supervision to mitigate unintended externalities, such as perpetuating corruption in developing countries.

We examine the concept of Dutch Disease and find that its symptoms could be applicable to Kosovo's economy. However, whether worker remittances or other variables are

responsible for these symptoms remains undetermined. This theoretical exploration lays the groundwork for the rest of the paper.

We identified four indicators of Dutch Disease in Kosovo. Firstly, we observed real exchange rate appreciation, evident through inflation. Specifically, there was higher inflation in traded goods sector compared to non-traded goods one, possibly due to domestic market limitations in meeting demand and imported commodity prices. Given the multitude of factors contributing to inflation, such as government spending, supply chain shocks, or demand fluctuations, we could not attribute it solely to increasing worker remittances or Dutch Disease itself, irrespective of its origins.

Secondly, an examination of various sectoral indicators reveals a gradual decline in the manufacturing sector, juxtaposed with a relative increase in the service sector. This trend has contributed to a relative deindustrialization of Kosovo's economy, aligning with the Dutch Disease theory. However, it is plausible that other omitted variables may have contributed to this sectoral shift. One such factor could be the transitional effect experienced by Kosovo's economy in recent years. Nevertheless, this classic adverse symptom of Dutch Disease requires further investigation in Kosovo to fully understand its prevalence and implications.

Thirdly, we observed the dynamics of wage growth in Kosovo. We utilized sectoral data to assess the distribution of employment and their respective wage levels. The results strongly indicate that there has been positive wage growth in both the manufacturing and service sector. However, this phenomenon could be due to other reasons, such as the de-shadowization of the economy, global productivity growth, or postwar revival.

The fourth indicator – trade deficit – is highly suggestive of the presence of the Dutch Disease. By analyzing time series on trade provided by the Central Bank of Kosovo (2022), we find that export levels have been extremely low in Kosovo, whereas imports have boomed. Consumption relative to production is much higher, and this points to our second analysis above – that of manufacturing sector's contraction. Since 2001, exports in Kosovo have seen

only marginal growth. This could be attributed to large external inflows financing imports, thereby diminishing the imperative for a robust export sector in the economy.

If remittances and foreign aid are indeed contributing to symptoms akin to Dutch Disease in Kosovo, policymakers face a critical task in regulating these inflows. Firstly, they should implement measures to ensure that remittances and aid are channeled towards productive investments that stimulate economic growth and development, rather than exacerbating inflation or currency appreciation. Secondly, they must strengthen oversight and transparency mechanisms to prevent mismanagement or corruption associated with the influx of remittances and aid. In addition, policymakers should explore strategies to diversify the economy and reduce dependency on remittances and foreign aid. This would eradicate rent-seeking behavior and secure Kosovo's long run economy.

## 5 Conclusion

Through a study of inflation trends, manufacturing sector performance, wage growth trends, and trade deficits, we have identified compelling evidence suggestive of Dutch Disease manifestations in Kosovo. This analysis aims to emphasize the importance of understanding and addressing the potential impacts of large inflows of foreign exchange, such as worker remittances and foreign aid, on economic stability and long-term growth.

While our findings estimate that there is a presence of Dutch Disease symptoms in Kosovo, it is essential to acknowledge the complexities involved in attributing causality and the need for further research to explain the precise mechanisms at play.

Moving forward, policymakers in Kosovo must thus prioritize strategies to manage the impacts of foreign exchange inflows effectively, including implementing measures to promote diversification, enhance productivity, and become less dependent on remittances and aid. By addressing the challenges posed by Dutch Disease and leveraging the benefits of foreign exchange inflows, Kosovo can plan a sustainable economic growth in the years to come.



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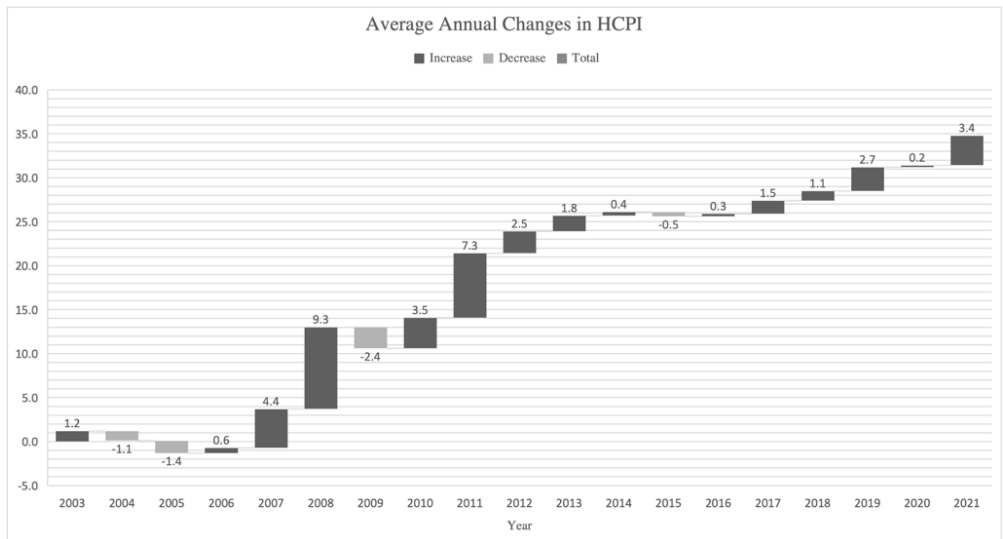


Figure 1: Average Annual Changes in Inflation

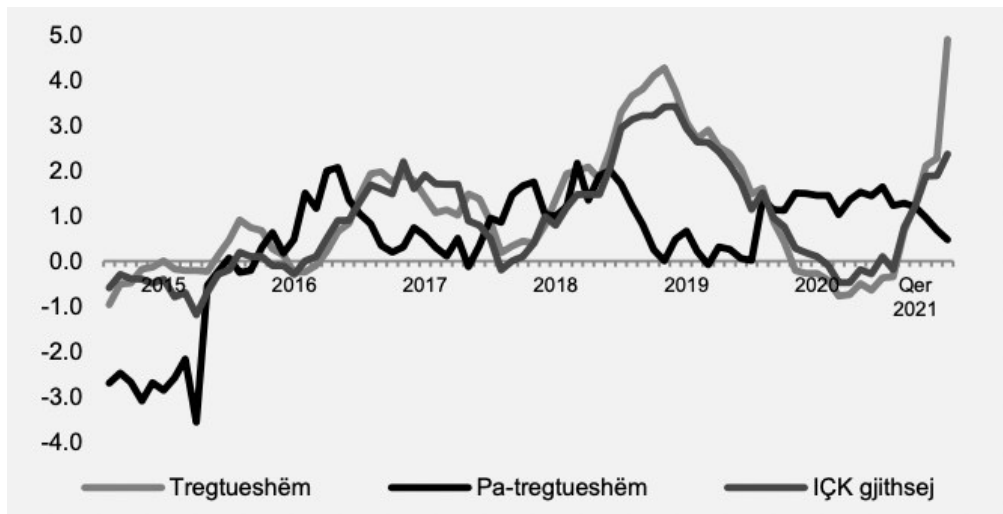


Figure 2: Price levels of traded and non-traded goods

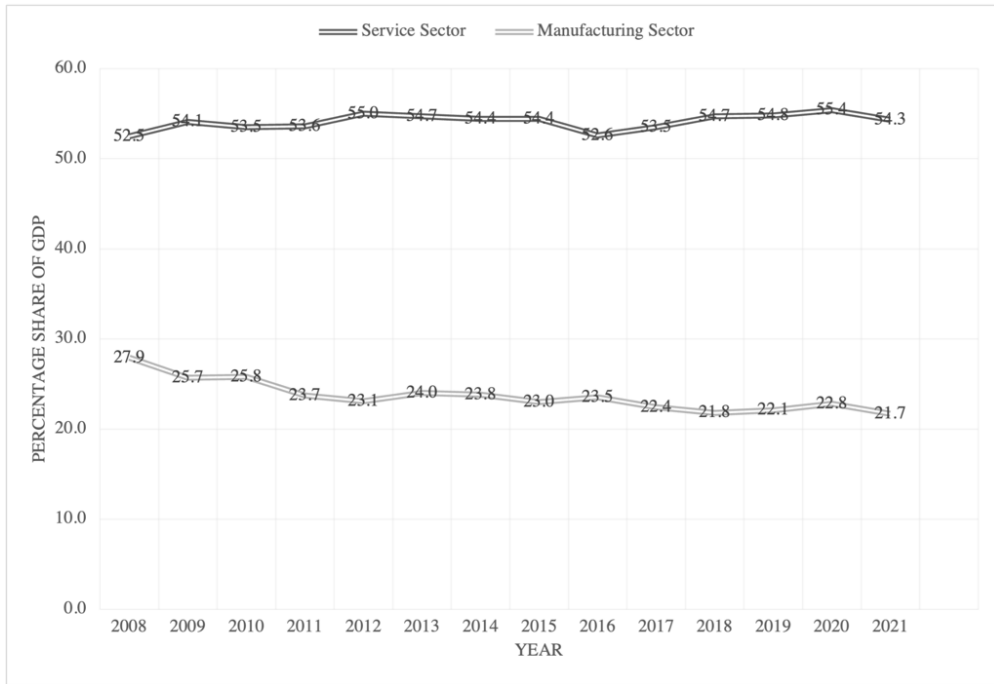


Figure 3: Share of the economic output by sector: manufacturing and service

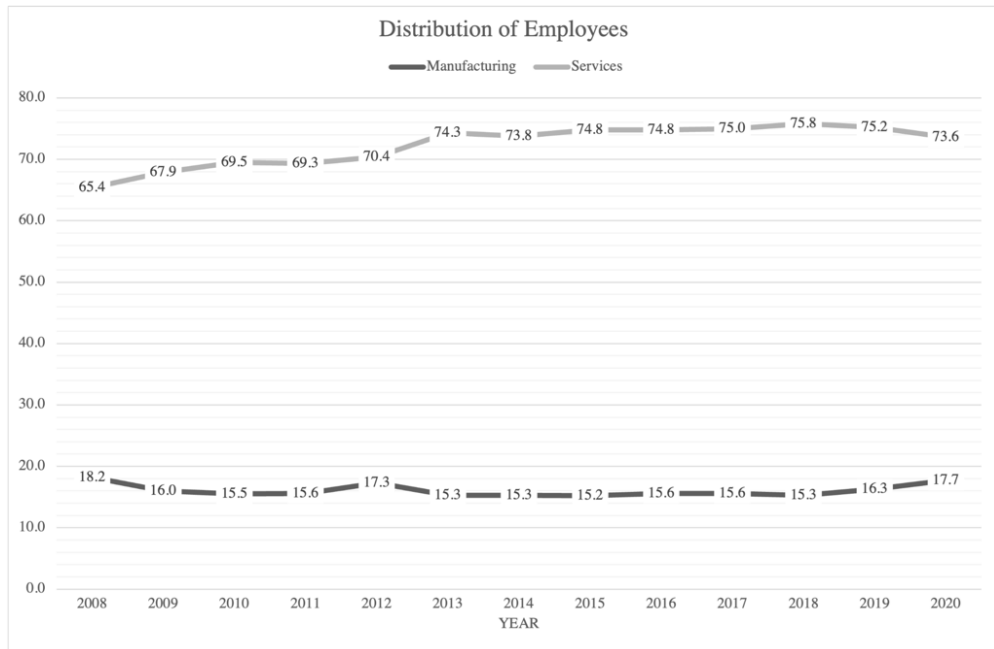


Figure 4: Distribution of employees in different sectors



Figure 5: Wage levels in the manufacturing sector

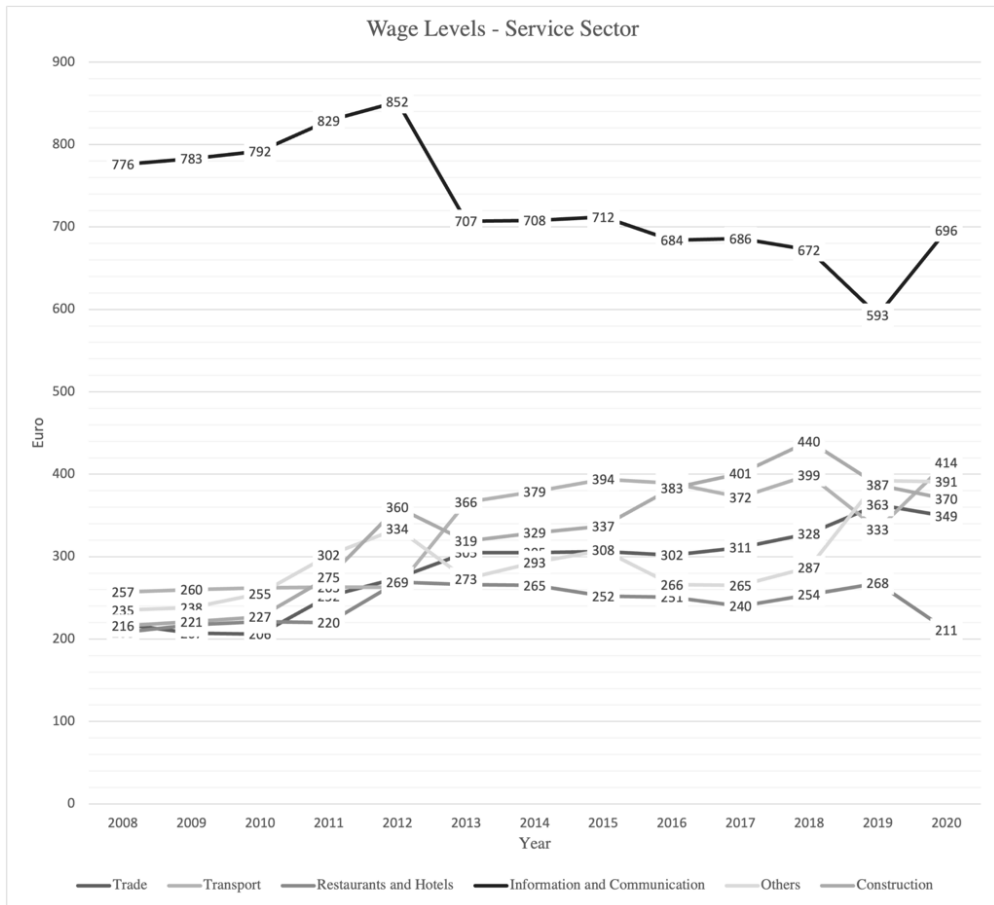


Figure 6: Wage levels in the service sector observed in six sub-categories

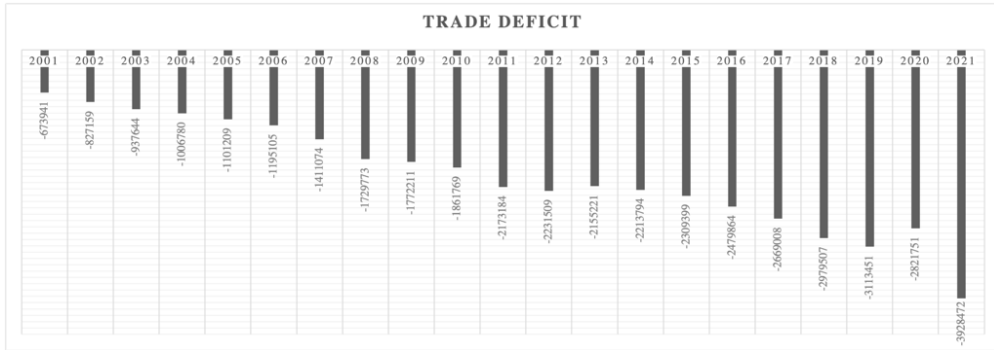


Figure 7: Trade Deficit by year in Kosovo from 2001 to 2021

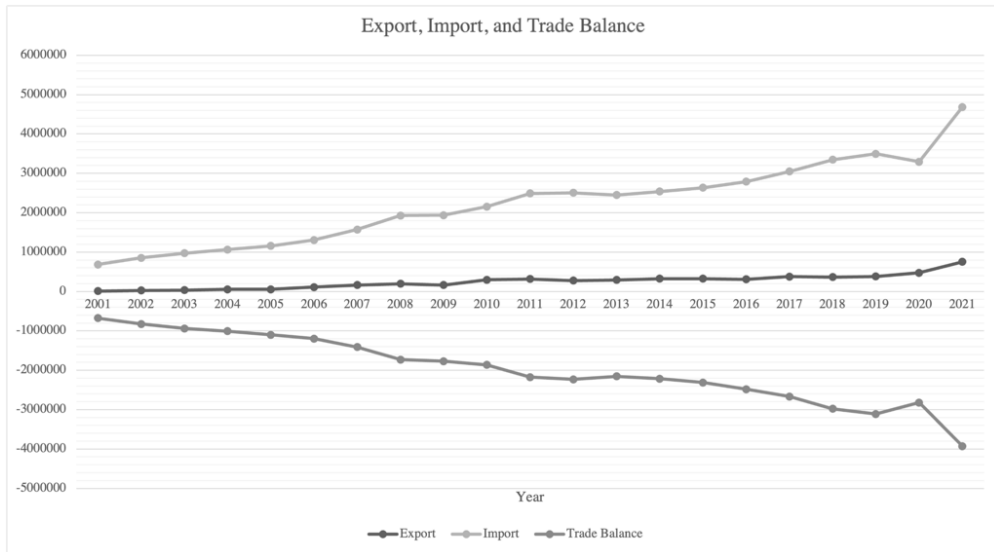


Figure 8: Levels of Export, Imports and Trade Balance in Kosovo from 2001 to 2021