FOREIGN DIRECT INVESTMENT IN KOSOVO

AMERICAN CHAMBER OF COMMERCE IN KOSOVO

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*Study: FDI in Kosovo*

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This Study seeks to provide an introduction of Foreign Direct Investment (FDI) and highlight the investment environment in the Republic of Kosovo. To achieve this, the Study will impart a legal and regional analysis, using both quantitative and qualitative data. The American Chamber of Commerce produces such studies in order to supply their target audience, in this case foreign investors and those who analyze FDIs, with up to date information.

Disclaimer

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FDI is “an investment involving a long-term relationship and reflecting a lasting interest and control by a resident entity in one economy (foreign direct investor or parent enterprise) in an enterprise resident in an economy other than that of the foreign direct investor.” They contribute to economic growth by enhancing human capital accumulation, technological innovation, foreign trade, and incentivizing domestic investment. Kosovo’s Law on Investment aims to incentivize Foreign Direct Investment (FDI) by providing articles that ensure equitable, non-discriminatory treatment to foreign investors. However, due to structural issues, the value of FDI over time has decreased (neglecting a notable increase in 2020). In the past nine years, Kosovo averaged an FDI net inflow level of 4.55% of its GDP.

Some of the issues that have enhanced this decrease include the limited international integration of Kosovo, political instability, corruption, a large informal economy, tenuous rule of law, etc. Focusing on the elaborated incentives and utilizing the recommendations provided in this study, foreign investors, especially the diaspora, can increase FDI in Kosovo and diversify their portfolio, whereas the Government of Kosovo could create an attracting environment for FDIs. An increase in FDIs in Kosovo could contribute to the flattening of the unemployment rate, increase production and exports, decrease the number of unskilled workers within the labor force, and would highly benefit the welfare of Kosovar citizens.
The United Nations Conference on Trade and Development (UNCTAD) defines FDI as “an investment involving a long-term relationship and reflecting a lasting interest and control by a resident entity in one economy (foreign direct investor or parent enterprise) in an enterprise resident in an economy other than that of the foreign direct investor.”

According to the Corporate Finance Institute, there are two typical types of FDI:

- **Horizontal**: a business expands its domestic operations to a foreign country.
- **Vertical**: a firm conducts different activities abroad but these activities are still related to the main business.
The other two forms of FDI include:

- **Conglomerate**: a business acquires an unrelated business in a foreign country
- **Platform**: a business expands into a foreign country but the output from the foreign operations is exported to a third country.

![Diagram of FDI flows](image)

On the other hand, USAID classifies FDIs in terms of the investors' motive as:

1. **Natural Resource-seeking FDI**: Investors seek petroleum and mineral resources, and often forestry, agricultural and other natural assets;
2. **Market-seeking FDI**: Investors seek new customers and clients by locating production in foreign markets rather than by exporting;
3. **Efficiency seeking FDI**: Investors seek cost-productivity improvements lowering the cost of production within global production networks;
4. **Strategic Asset-seeking FDI**: Investors look for very specific tangible or intangible assets that complement the multinational's asset base. [1]

Financially, FDIs have three components:

1. **Equity capital**
2. **Reinvested earnings**
3. **Intracompany debt** [2]

Furthermore, FDIs contribute to economic growth by enhancing human capital accumulation, technological innovation, foreign trade, and incentivizing domestic investment. The impact of FDIs on Kosovo’s overall economic performance will be elaborated in the following pages of this Case Study.

[1] USAID, Foreign Direct Investment, pg.55, [Link](#)
[2] Ibid, pg.8
Article 1: Purpose

“The purpose of this law is to protect, promote and encourage foreign investment in the Republic of Kosovo, to provide foreign investors with a set of fundamental rights and guarantees that will ensure foreign investors that their investments will be protected and treated with fairness in strict accordance with the accepted international standards and practices.”

The Law on Foreign Investment entered into force in 2014 and repealed Law No. 02/L-33, Law No.02/L-05, and Law No.03/L-03. It aims to incentivize Foreign Direct Investment (FDI) by providing articles that ensure equitable, non-discriminatory treatment to foreign investors, whose investment “shall not be subject to any form of expropriation or nationalization.”

For reference, the Law considers the following as FDI - any asset owned or otherwise lawfully held by a Foreign Person in the Republic of Kosovo for the purpose of conducting lawful commercial activities, including but not limited to:

1.4.1. movable and immovable property, including rights in and to such property such as a mortgage, lien, pledge, lease or servitude;
1.4.2. intangible and intellectual property, including rights in such property, as well as goodwill, technical processes and knowledge;
1.4.3. cash, securities, commercial paper, guarantees, shares of stock or other types of ownership interests in a the Republic of Kosovo or foreign business organization; bonds, debentures, other debt instruments;
1.4.4. claims or rights to money, goods, services, and performance under contract;
1.4.5. concessions or licenses conferred by law, administrative act, or contract; and
1.4.6. returns yielded by an investment in the Republic of Kosovo or an investment elsewhere.
In the event that current Kosovo’s laws come into conflict with a provision of an international agreement on FDI, Article 19 accords that such international agreement shall prevail.

Whereas a foreign investor “shall act in compliance with all laws and standards applicable in the Republic of Kosovo,” the latter has obligations to the former. These obligations include providing stability for the investment regime, compensation to investors when appropriate, guaranteed transfers and adequate currency conversion. Point 1 of Article 21 establishes that the “Ministry shall establish and maintain a registry of foreign investors and investments” and Articles 22, 23 provide information on programs and investment supporting agencies in Kosovo.

In addition to the Law on Foreign Investment, it is important to note significant articles from other related and enforced laws. Point 4 of Article 4 of the Law on Strategic Investments (No. 05 L-079) notes that the Government of the Republic of Kosovo may invite investors to partake in the privatization process in accordance with the relevant provisions of the Law on Public Procurement. Foreign investors may find relevant information at the Privatization Agency of Kosovo (PAK), an independent public body responsible for the privatization of Socially Owned Enterprises (SOEs).

In the “2020 Investment Climate Statements: Kosovo,” the U.S. Department of State highlights the following as laws of particular relevance for foreign investors:

1. **Law on Foreign Investment** (No. 04/ L-220)
2. **Law on Business Organizations** (No. 06/L-016)
3. **Law on Strategic Investments** (No. 05/L-079)
4. **The Law on Late Payments in Commercial Transactions** (No. 05/L-110)
5. **The Law on Bankruptcy** (No. 05/L-083)
6. **The Law on Prevention of Money Laundering and Combating Terrorist Financing** (No. 05/L-096)
7. **The Law on the Establishment of the Kosovo Credit Guarantee Fund** (No. 05/L -057)

Additions include:

1. **The Law on Amending and Supplementing the Law No. 03/L-229 Protection of Competition** (No. 04/L-226)
2. **The Law on Anti-dumping and Countervailing Measures** (No. 04/L-240)
Central European Free Trade Agreement (CEFTA) with other signatory parties including Albania, Bosnia and Herzegovina, Macedonia, Moldova, Montenegro and Serbia. CEFTA seeks to facilitate trade by eliminating tariffs to regional trade.

Free-Trade Agreements (FTA) with Albania, North Macedonia, Croatia, Bosnia-Herzegovina, and Turkey. For more information on the FTAs, see the Kosovo Customs page.

Stabilisation and Association Agreement (SAA) with the European Union. The signatories and ratifiers of the SAA include Kosovo, Albania, Montenegro, Serbia, North Macedonia, and Bosnia and Herzegovina. The European Commission states that the agreements “establish a free trade area between the EU and the country concerned, identify common political and economic objectives and encourage regional cooperation.”

UK-Kosovo partnership, trade and cooperation agreement. According to the UK government site, the agreement includes provisions on trade in goods and services, intellectual property, and government procurement. For more information, see link.

Double Taxation Agreements (DTAs) with a number of international partner countries. Find the full list at AmCham Policy Spotlight: Tax on Dividend, pg. 4

Generalized System of Preferences (GSP) Program with the U.S., Japan, and Norway.

Another source that foreign investors may turn to for information regarding Kosovo’s laws, procedures, and other substantive assessments is ICLG, a leading global platform for legal reference, analysis and news.

Bilateral Investment Agreements and Taxation Treaties

Kosovo has signed the following agreements regarding trade and taxation, which may be useful for foreign investors:

1. Central European Free Trade Agreement (CEFTA) with other signatory parties including Albania, Bosnia and Herzegovina, Macedonia, Moldova, Montenegro and Serbia. CEFTA seeks to facilitate trade by eliminating tariffs to regional trade.

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Central Bank data presented below graphically by AmCham shows that whilst the value of FDIs in Kosovo (in millions) has remained high, there has been a notable decrease since 2007.

Data: CBK; Chart made by AmCham

Paradoxically, there is a much higher amount of FDI in 2007 than in the following years, despite the common assumption that the declaration of independence in 2008 should have reversed this trend. Political instability may partially explain the notable decrease in FDI in 2014, yet this does not represent the full picture for the full analyzed period.

Another initially perplexing judgement is the increase of FDI in 2020, despite the shocking economic effects of the COVID-19 pandemic. The Central Bank of Kosovo notes that FDI in Kosovo increased by 34.2 percent in comparison to the previous year, reaching the value of 341.7 million euros.
The sector of financial activities, energy, as well as mining and quarrying, saw notable growth while the real estate sector decreased by 10.1 percent. The financial activities sector, particularly, increased its share of FDIs to 24.7 percent in 2020, from 5.5 percent in 2019. This may be mostly a result of undertaken measures that were recommended by the CBK during the pandemic crisis (the suspension of the dividend distribution by banks for 2019 and 2020).

Data: World Bank; Chart made by AmCham

Moreover, if the statistical anomaly of 2020 is disregarded, the following graph shows Kosovo's FDI net inflows as a percentage of the country's GDP since 2004. Congruous with the “FDIs in Kosovo” graph, this one too shows the significant increase of FDIs (as % of GDP) before the declaration of independence (2008) and the noteworthy decrease after 2007-8.
In comparison to other countries in the Balkan region, the following heat map and table show the comparative values of Kosovo’s FDI net inflows (as % of GDP) in 2019 and since 2012, respectively. As can be seen in the table assembled by AmCham, Montenegro had some of the highest values of FDI net inflows (as % of GDP) in the past nine years, along with Albania and Serbia (especially in the last few years). Kosovo, on the other hand, averages an FDI net inflow level of 4.55% of its GDP for the period indicated below.
**A SECTORAL REVIEW**

As it pertains to the sectoral position of international investments in 2009-20, the CBK graph below shows this in millions. The table [3] and following chart provide more information on FDIs by sector (%) during the years 2009-15 and 2020. The third chart visualizes the main countries that provide direct investments in Kosovo (up to April, 2021).

Financial activities cover most of the investment values above, as do the other sectors. Real estate, renting & business activities have the most FDI in percentage during the period 2009-15 and this top place is true for 2020 (in millions of euros) as well. As per the state that provides the most FDI in Kosovo (2020), it is Germany.

### FDI by sector

<table>
<thead>
<tr>
<th>Sector</th>
<th>2009</th>
<th>2010</th>
<th>2011</th>
<th>2012</th>
<th>2013</th>
<th>2014</th>
<th>2015</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Agriculture, hunting, forestry, fishing</td>
<td>13.1</td>
<td>0.9</td>
<td>0.6</td>
<td>0.3</td>
<td>0.4</td>
<td>0.2</td>
<td>0.9</td>
<td>24.8</td>
</tr>
<tr>
<td>Mining/quarrying &amp; Electricity/gas/water supply</td>
<td>15.7</td>
<td>17.7</td>
<td>-5</td>
<td>-22.8</td>
<td>34.6</td>
<td>17.6</td>
<td>-12.7</td>
<td>79.1</td>
</tr>
<tr>
<td>Manufacturing</td>
<td>57.6</td>
<td>101.1</td>
<td>46.9</td>
<td>27.4</td>
<td>11.5</td>
<td>-34</td>
<td>23.1</td>
<td>287.4</td>
</tr>
<tr>
<td>Construction</td>
<td>35.5</td>
<td>54.2</td>
<td>133.1</td>
<td>31.1</td>
<td>17.3</td>
<td>-19.9</td>
<td>46.3</td>
<td>311.2</td>
</tr>
<tr>
<td>Transport, storage &amp; communication</td>
<td>21.9</td>
<td>-15.9</td>
<td>29</td>
<td>32.4</td>
<td>51</td>
<td>-9.1</td>
<td>-6.2</td>
<td>154</td>
</tr>
<tr>
<td>Financial intermediation</td>
<td>75.3</td>
<td>39.4</td>
<td>33</td>
<td>22.4</td>
<td>4.4</td>
<td>41.9</td>
<td>64.3</td>
<td>390.3</td>
</tr>
<tr>
<td>Real estate, renting &amp; business activities</td>
<td>43.9</td>
<td>75.5</td>
<td>60.5</td>
<td>115.7</td>
<td>136.1</td>
<td>142.1</td>
<td>189.6</td>
<td>825.5</td>
</tr>
<tr>
<td>Other sectors</td>
<td>32.5</td>
<td>95.7</td>
<td>86.4</td>
<td>22.5</td>
<td>25</td>
<td>12.4</td>
<td>19</td>
<td>330.7</td>
</tr>
</tbody>
</table>

**Data:** KIESA; Graph above by AmCham
FDI RELATIONSHIP WITH THE LEVEL OF EMPLOYMENT AND UNEMPLOYMENT IN KOSOVO

The graph above compares the level of employment in Kosovo (in %) and the value of FDIs in millions of euros for the period 2011-2020. As can be seen, there is not a direct, continuous relationship or trend between employment and FDI level, but this can be explained by the high level of investment in real estate, not a job-producing sector.

Yet, it cannot be denied that FDIs in different sectors produce new jobs for Kosovo’s labor force and the latter’s characteristics attract FDI. According to the Kosovo Agency of Statistics, 46.4% of youth is unemployed in Kosovo (Q1, 2020) and this represents a great opportunity for foreign investors to utilize the youth in their businesses [4]. Further, the pie charts below showcase the level of male/female/total unemployment (in %) by educational level. As demonstrated, there is still a highly educated (and uneducated) level of unemployed (job-seeking) labor force that can be of use to foreign investors.

[4] Note: This figure is not greatly enhanced by the pandemic. KAS states that “the impact of the COVID-19 pandemic on the first quarter data was very low.”
In fact, in a survey conducted by AmCham in 2010, more than 60% of the respondents (potential foreign investors) considered human resources to be “the strongest potential that Kosovo provides to foreign investors.” This remains the case, as recently highlighted by a Dutch investor in an interview with AmCham. He noted the remarkable difference of worker availability in Kosovo with the Netherlands’ lack thereof and the great abilities of Kosovo’s unskilled workers to “learn very fast.”

In addition to labor force characteristics, labor policies which favor low minimum wages compared to EU countries have also attracted many foreign investors. For a summary of Kosovo’s labor policies, see Section 11 of the U.S. Department of State’s “2020 Investment Climate Statements: Kosovo.”

Lastly, it is important to note the results of a 2019 survey conducted by the Institute for Free Market Economy (IFME), supported by Konrad-Adenauer-Stiftung (KAS). The survey of 38 Kosovar enterprises with foreign capital concluded that these businesses have “full confidence in their [Kosovar] employees,” which sends a positive message “to new foreign businesses that are interested in investing in Kosovo” [5].

An increase in FDIs in Kosovo as well as a flattening of the unemployment rate would highly benefit the welfare of its citizens.

FDI RELATIONSHIP WITH REMITTANCES

The value of remittances has always been higher than that of FDIs and, as shown in the graphs above, this value (in millions of euros) has had a steady and significant increase during 2012-2019. The diaspora can positively impact the level of FDIs in Kosovo by redirecting remittances into investment. However, a 2010 UNDP study, summarized by Group for Legal Studies, states that around “40% of remittances are used for household consumption, another portion for housing and human capital investment, whereas only a small amount is used for business investment.” This has mainly remained the case until now, except for a noteworthy investment by the diaspora into the real estate market.

Remittances do benefit the welfare of Kosovar citizens, but different studies draw mixed conclusions on their economic impact. A study using regression models and World Bank data for the Western Balkans, concluded that the economic “impact of FDI...was...highly significant,” whereas considering remittances as “not key determinants of growth” [6]. They suggested that respective authorities should “create an adequate environment for new, successful investments, and [make] good use of incoming remittance flows.” Notwithstanding the debated economic impact of remittances, this study suggests that the diaspora should consider redirecting remittances towards FDI or their current investment in real estate towards other beneficial and profitable sectors. On the other hand, Kosovo and its respective authorities should work towards attracting FDIs from the diaspora and establishing effective mechanisms for the utilization of diaspora capital. It is important to note that the diaspora faces a lower investment risk than other potential investors and remains the hope for an increase in FDI levels.

SECTORS WITH POTENTIAL FOR INVESTMENT

- **Energy Sector**

Kosovo is rich in natural resources and has been using its lignite (coal) reserve to produce energy. However, due to cost and environmental reasons, the World Bank and ContourGlobal, a British investor, withdrew support for the construction of a new lignite power plant in Kosovo, in 2018. By contrast, renewable energy now appears to be the lower cost alternative, as indicated in a review by the Institute for Energy Economics and Financial Analysis. Foreign investors may be attracted by these low costs, high demand for energy, and support for renewable energy from international development banks.

- **Agricultural Sector**

KIESA ranks Food Processing and Packaging as one of the main segments with potential for investment. It highlights that more than half of Kosovo's total surface area is agricultural land with fertility, nutrient-rich soils. Thus, foreign investors may take advantage by Kosovo's natural resources, strong agricultural tradition, and subsidies/grants that the Government provides for the agricultural sector.

- **Information Technology (IT) Sector**

This sector is developing fast and maintains great potential for FDI. According to the 2020 IT Barometer, the "most popular horizontal markets are Custom Development/ Outsourcing, followed by IT Consulting, Web design development, Mobile Solutions, E-commerce, Software Quality Assurance etc." Foreign investors may be attracted by the young, educated, and English-fluent work force.

- **Tourism**

Kosovo has potential to further develop eco-tourism, adventure, cultural, and medical tourism. The Skiing Center in Brezovica, in the Sharr Mountains, is within one-hour reach from the International Airports of Prishtina and Skopje. According to KIESA, there are about 22,000 hectares of unexplored land in the Sharr Mountains that are offered for privatization. Other places for investment include the Skiing Center in Rugovë, Kosovo's religious and historic sights, as well as its thermal springs.
INCENTIVES FOR INVESTMENT

This section provides a brief summary of facts about Kosovo that should incentivize foreigners to invest in the country.

Kosovo has a geostrategic position that foreign investors could use to their advantage. It is located in the heart of the Balkans and, as such, it provides easy access to the EU. The country is only about 262 km away from the port of Durres in Albania, 299 km from that of Tivat in Montenegro, and 329 km from the port of Thessaloniki, in Greece.

Further, Kosovo’s young population, working force, and low labor costs are a few of the main incentives for foreign investors. At the International Management Exhibition, Prime Minister, Albin Kurti, said the following:

“This [Kosovar] young labor force speaks the main languages that are spoken in the European Union...they bring together with their remittances the work ethics of German-speaking part of the EU.”

In an interview with AmCham, a Dutch investor said, “We see a lot of advantages [in Kosovo] and one of them is the availability of a highly educated workforce...that is quite exceptional!”

About the broad range of competitive sectors, the Prime Minister added:

“The range of sectors that Kosova is assumed to have competitive advantage in the region is broad, starting from IT sector, wood processing industry, metal processing industry, outsourcing of corporate support services, tourism and agriculture.”

Businesses can now be registered in 2 days and partake in a business environment with a ‘starting a business’ score of 95.9 (out of 100) [7].

In case of a legal dispute, international arbitration, available in Kosovo, is a great advantage for investors to settle commercial contentions in a quick, modern, and flexible manner. The Law on Investment stipulates the right of an investor to refer to arbitration (Article 10) for compensation for losses incurred as a consequence of any legal action/inaction directed against them. Article 16 provides the “Mechanisms for the Resolution of Investment Disputes” contingent on the established legal right of investors to require that an investment dispute be resolved in accordance with denoted procedures. In the absence of these procedures, a dispute may be resolved through arbitration governed by:

2.1. the ICSID Convention;
2.2. the ICSID Additional Facility Rules;
2.3. the UNCITRAL Rules; or
2.4. the ICC Rules

[8] The Institute for Free Market Economy (IFME), pg.31-2
Kosovo offers some of the lowest tax rates in the region. For comparison, see the table above [8].

Kosovo uses the euro as its currency and, as such, European investors do not have to worry about exchange rates or foreign currency instability.

Lastly, investors enjoy investment guarantees from:

- The Multilateral Investment Guarantee Agency (MIGA) (member of the World Bank Group) guarantees investments in Kosovo up to the amount of 20 million euros.
- The US Private Foreign Investment Corporation (OPIC) provides political risk insurance for foreign investors in Kosovo.
- Investments and credit guarantees from Austria - Austrian Kontrollbank (OeKN) and for Germany, Euler Hermes Kreditversicherung [9].

[9] The Institute for Free Market Economy (IFME), pg.30
CHALLENGES TO INVESTMENT

Some of Kosovo’s structural issues that the U.S. Department of State notes in its ‘2020 Investment Climate Statements’ are:

- limited regional and global economic integration;
- political instability;
- interference in the economy;
- corruption;
- an unreliable energy supply;
- a large informal sector;
- difficulty establishing property rights;
- tenuous rule of law, including a glaring lack of contract enforcement.

Kosovo is not part of the EU nor the World Trade Organization, but it tries to facilitate its EU accession agenda through CEFTA. However, neither Serbia nor Bosnia & Herzegovina recognize Kosovo’s independence and this has resulted in trade barriers. Kosovo’s limited international integration as well as internal political issues have disincentivized FDIs throughout the years.

Corruption remains another challenge. The study by IFME shows that 52% of the businesses surveyed (that enjoy foreign capital) consider corruption a major obstacle in Kosovo, and only 11% of them claim that it is not [10].

Pertaining to the tenuous rule of law, the same study showed that the level of trust in Kosovo’s courts is low with slightly more than 50% of the respondents showing some kind of trust in the courts [11]. As per the lack of contract enforcement, “33% of respondents stated that non-performance of contracts by Kosovo courts is a major obstacle, 25% answered that it is an obstacle, 38% of them stated that it is a small obstacle, while only 4% claimed that it is not an obstacle” [12].

In addition to these challenges, it is important to note the lack of freedom of movement due to the visa regime and the lack of information available for foreign investors. In fact, in a survey conducted by AmCham in 2010, one of the major reasons for reluctance to invest in Kosovo was the lack of information. This has led foreigners to create misconceptions about Kosovo regarding its business environment.

[10] IFME, pg.20
RECOMMENDATIONS

Some of the recommendations regarding FDIs, potential investors, and the Kosovar business environment that the American Chamber of Commerce suggests are as follow:

• The establishment of a primary point of information regarding investment. This could take the form of a task form within the office of the Prime Minister or other forms. Such an establishment would reduce bureaucracy and work towards marketing the image of Kosovo as a safe and profitable place for investment.

• The facilitated establishment of the Commercial Court. "AmCham estimates that such a decision of the Government of Kosovo will inevitably affect the increase of legal certainty in doing business, improving the investment climate, and consequently the image of Kosovo before foreign investors." Additionally, "the approval of the Draft Law by the Government, also contributes to the advancement of the public-private dialogue." This plan should partake in the bigger initiative of improving the rule of law in Kosovo, especially in establishing clear property rights.

• The investment threshold provided in the Law on Strategic Investments shall be reviewed and reconsidered for better coordination with government decision-making objectives and incentives through vital sectors of the economy. Further, strategic investors, without prejudice on the size of their businesses, shall be offered tax incentives contingent on their investment’s job-production level.

• The Government should promote new bilateral agreements that facilitate trade and attract foreign direct investment as well as new job opportunities.

• The establishment of the Special American Economic Zone would attract U.S. investors from the USA and other countries. These potential US investors shall be offered administrative and fiscal incentives within the economic zone in order to increase foreign direct investments.

• To eliminate the hesitancy of potential investors to invest in Kosovo due to its level of unskilled labor force, human resources should be developed through trainings and workshops. Doing so, potential foreign investors will not be ‘burdened' with the need of transferring technology knowledge in Kosovo.

• The Government should incentivize the diaspora to invest by means of strengthening diplomatic missions and creating organizations in countries where the diaspora predominantly resides.
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