Global financial crisis and its impact in the countries in transition – with special emphasis in Kosovo

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Abstract

Financial crises are characterized as phenomena that have been recorded for a long time. These phenomena are considered as bad events because they are associated with a deep decline in economic activity, and many of them are considered to happen due to the lack of central banks, lack of a strong currency or the lack of a steady banking system (reduction of money supply and narrowing of loans).

The first financial crisis of the modern world related to the real existence of the market and its own capitalism as the system emerged in 1636 in the Netherlands, known as the tulip crisis, a flower symbolizing the Netherlands. Later, during the period of the first industrial revolution in England and France, dozens of crises emerged. While in the US, the first industrial crisis emerged in 1819, followed by many to the Great Depression crises of 1929-1933.

According to the researchers, all these crises have occurred for the same cause: financial speculation is neglected in order to benefit as much as possible. From such a fact, one can think that crises and monetary illusions are an inevitable fatality. They have been co-drivers of development and capitalism, so it does not seem strange that most of the books and studies determined to financial crises end with the question: What is the next crisis???

Keywords: global financial crisis; countries in transition; financial crisis in Western Balkan countries.

Introduction

The crisis of 2007-2008 is the worst crisis that occurred after the Great Depression of 1929 and the world is still facing the consequences of this crisis. According to Minsk (1992), this happens because people are characterized by short memories and they forget previous experiences and allow crises to occur again. Meanwhile, Merrouche and Nier (2010), in their study, estimated that financial imbalances, inefficient monetary policies and inadequate oversight were other important factors that have affected the deterioration of the financial situation. Other authors estimate that these changes in the financial field offered opportunities for large profits that provided financial innovations under unspecified conditions and rules as a result of a tendency by the households, businesses and bankers to experiment with new financial products and also as a result of legal and administrative interventions by governments and central banks that were initially not present, and later appeared incorrectly. Therefore, there are many causes of the crises of 2007-2008 also called the "subprime mortgage crisis", which is also referred to as the "subprime loans crisis".

Only during the first three quarters of 2010, 8 million jobs were closed, impoverishing the American people even more. Vehicle manufacturing companies, construction companies and many other companies operating in many parts of the world closed factories by spreading the crisis everywhere. The number of patients in mental health centers increased along with criminal activity. According to FAO data, the number of malnutrition people grew by 11% in 2009, making this number to exceed 1 billion for the first time, which was due to rising food prices at the international level (FAO, 2009). The grain prices on world markets in February 2008, compared to three years ago, increased by 181%, while food prices by 83% (Angela, 2012, p. 156). Here, though, as the price crisis deepens, poverty grows.
In general, social problems were big, adding the economic problems as well. US public debt reached over 60% of GDP. Many urban centers that were characterized by various entertaining activities turned into ghost towns, such as Detroit. In California, the green fields were filled with shelter tents.
The result of the global financial crisis was the largest and deepest decline of the world economic activity that the modern era has experienced (McKibbin and Stoeckel, 2009). In 2009, many world economies saw themselves in recession. According to OECD data, international trade fell down by 13% from 2008 to 2009. The crisis radically changed the US and the world and it was time to think of a new economic model. The shock even touched on the taboos on the model of free market economy and capitalism itself. By this time it was thought that the markets functioned themselves that government interventions were not needed, but this crisis proved that regulation itself was not possible and that government interventions were more than necessary.

The impact of the Global Financial Crisis in Transition Countries

Just as other countries of the world, the transition countries are negatively affected by the recent global recession, which is also known as the worst crisis the world has seen since the Great Depression, 1929-33. The consequences were severe not only in the countries where this crisis originated but also across the ocean, both in European countries and in the Balkans. This crisis was like a powerful wave of the sea that would crumble everything in front of it. There was hope that the Balkan countries would not be affected by this crisis as these countries had macroeconomic stability over the last years, with the average growth rate of the entire region of 7-8 per cent per year due to three factors:

- Successful transition to market economy, economic liberalization, privatization and financial stabilization;
- Unexploited human capital;
- International integration and global flourishing.

Despite these positive factors, avoidance from the global financial crisis of 2007 was impossible. After a period of several years of growth, the performance of the economies of the South East European countries was adversely affected by the effects of the crisis generated in the developed countries. Once these countries had many benefits from agreements with developed countries, but in 2007 and 2008 the crisis was transmitted because of this cooperation (Sanfey, 2010).

The year 2007 marked the beginning of the global financial crisis, both in America and Europe, but 2008 marked the peak of this crisis when Europe was officially declared recessionary. In summer 2008, Europe was in a difficult situation where real estate prices went out of control and stock markets hit the highest slump while making funding very difficult. Europe, unexpectedly, found itself with a few or few international finances leading to the necessity to apply for financial support from the IMF.

In 2009, most EJL countries recorded a decline in GDP resulting in an average decline of 7.54% for the entire region, while only Kosovo and Albania were exempt marking positive GDP growth rates, (3.8% and 2.5% respectively, CBK, 2010b), but this growth was lower than in previous years.

The fundamental problem was the excessive entry of short-term bank loans attracted by the low exchange rate which led to the creation of large private foreign debts. Public finances, on the contrary, were in excellent condition with the exception of Hungary and Romania that had large budget deficits, but Hungary also had public debts. Domestic vulnerabilities were aggravated by the worst financial panic of all time. The capital fled to states - 'paradises' perceived as safe places, i.e. in gold, dollar, euro, yen and Swiss francs. The financial panic was a market failure that had to be recovered by the state, and internationally by the IMF which was expected to provide countervailing financial flows.

The desire for EU membership pushed SEE countries into deep structural and macroeconomic reforms which increased the level of economic stability, manifested by high growth rates, high levels of FDI (FDI) and the double-digit growth rate of bank loans. But the financial and economic crisis significantly jeopardized the achievements and economic sustainability of the Balkan countries. The effects of the crisis were mainly manifested with lower exports, low credit rating by banking sector, IHD drops and remittances, which were also the channels through which the financial crisis was transmitted to the Balkans.

Central banks of the region made a special contribution to the success shown in good management of crisis. No bank, of any particular importance, has bankrupted in the entire region. Two actions of central banks were distinguished on the occasion of crisis. Firstly, central banks focused on reducing mandatory reserves in order to increase liquidity and lending, and secondly, central banks in some cases (eg Serbia and Romania) intervened in foreign exchange markets to protect the domestic currency.

It is understood that central banks, and generally the management of crises in SEE countries, were largely supported by international financial institutions such as the IMF, the World Bank, the European Bank for Reconstruction and Development and the European Union. The IMF's reaction was quick and good. IMF requirements for crisis management related to:

- Budget closer to balance;
- A real exchange rate policy and
- Bank restructuring with recapitalization.

On the other hand, for the fulfillment of these conditions, the IMF offered much larger loans than previously. With the emergence of the crisis, excellent ad hoc cooperation

was developed between the IMF and the European Commission (EC). The IMF has assisted with staffing, rules and procedures to deal with the financial crisis. The EC co-funded the IMF programs for Hungary and Latvia, and several European countries, including Scandinavia, and contributed with substantial funding to the Latvian program. Three other international institutions also played a substantial role, namely the World Bank, the European Bank for Reconstruction and Development, and the European Investment Bank. Their main focus was bank recapitalization (IMF, 2009).
One of the worst concerns was that Western European banks which had bought most of Eastern European banks were planning to withdraw from the region. In Ukraine, 17 European subsidiary banks in the country had pledged to recapitalize their Ukrainian subsidiaries by $ 2 billion in 2009. Many people worried that the crisis would cause social upheaval and regime change. People seemed to understand the seriousness of the crisis and the powerful demands. Four countries in crisis changed governments during this period of crisis. In general, new governments were more supportive of the free market than previous governments. In Latvia, the most liberal party joined the center-right coalition government and took the lead to explain to the public why it is required to cut wages and expenses. In Hungary, a Socialist Prime Minister was replaced by another. Eastern Europe's policy largely responded to the crisis in an appropriate way.

The impact of the Global Financial Crisis on Western Balkan countries, with focus on Kosovo

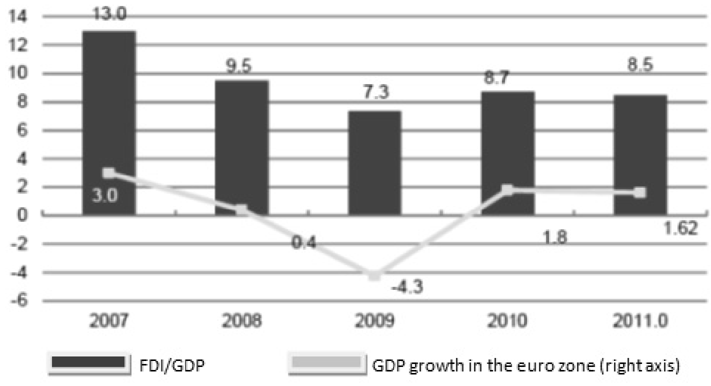
Western Balkan countries are characterized as countries that are still in the development phase. They are not with a too high level of openness towards international financial markets which has affected the banking system of these countries to be more stable and not affected by the toxic financials instruments (Pere and Hashorva, 2012). But again, these countries do not have strong mechanisms for crisis protection. So, like other countries in the world and the Western Balkan countries, they have been negatively affected by the recent global recession. Although several years have passed since the beginning of the global financial crisis, these countries are still not recovering.
The crisis has hit the countries of Western Europe, as it has also hit the countries of the Western Balkans, Albania, Bosnia and Herzegovina, Kosovo, Macedonia, Montenegro and Serbia. The crisis came to this part of Europe 9-12 months after it had passed through Western and Central Europe causing an immediate decline in GDP. Different authors value the crisis as a powerful sea wave that encompasses all the places in the world and now the West Balkans line was ranked. The pain was not just because the crisis arrived there but, because it came when these states saw a little light at the end of the tunnel. They had just recovered and the crisis made them turn back into darkness.
A report from the World Bank, "South East Europe Regular Economic Report, no. 3 "of December 18, 2012, seeing that the effects were severe for a region that had not yet emerged from the economic problems that it had had earlier, stresses the need of these six countries to use the most opportunities to improve the investment climate and reduce public debt and at the same time to eliminate public sector payment

delays, which would help improve financial discipline in the overall economy of each country (World Bank, 2012b). According to this institution, Western Balkan countries need to take immediate measures to improve the economic situation as they are characterized as one of the regions with unsustainable economies and with a high level of unemployment.
Although these countries have just emerged or are at the end of the transition process and have not achieved yet full economic and political sustainability, they have succeeded to have a positive economic development trend from the 2000s onwards. The global crisis affected the upward trends of these countries and brought them back to the initial step. The negative effect of the crisis on the economic development of these countries can be seen from various macroeconomic indicators such as GDP, unemployment, budget deficit, trade deficit, current account deficit, inflation, etc.

Transmission Channels of Crisis in Kosovo

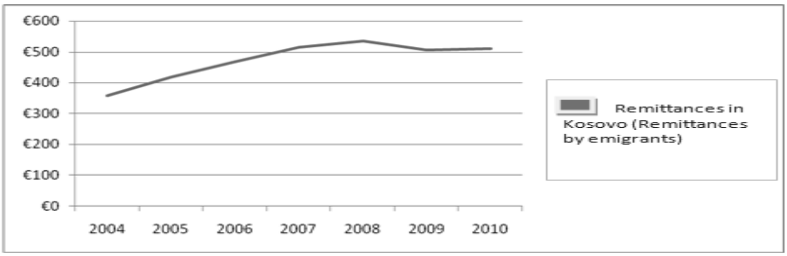
Like the Western Balkan countries, Kosovo has been affected by the global financial crisis, which began in 2007 but deepened in 2008. This financial catastrophe covered the US, the Eurozone, Asia reached the Western Balkans and hit the doors of Kosovo. However, fortunately, the limited financial ties that Kosovo has with the world helped our country as much as possible to be protected from the crisis or feel less crisis. Despite the crisis, Kosovo has managed to maintain positive GDP growth, which was 6.3% in 2007, 6.9% in 2008 and 2.9% in 2010. However, these figures show that although Kosovo has managed to maintain its growth Of GDP, these increases have fallen down due to the crisis.
In Kosovo, we can say that the crisis has not spread from the channels mentioned so far, because Kosovo is not a country characterized by exports, it has not been exposed to the international financial markets, there is no flexible currency exchange regime and there is no high level of FDI.

Figure 1: Foreign direct investments as a percentage of GDP (GDP)



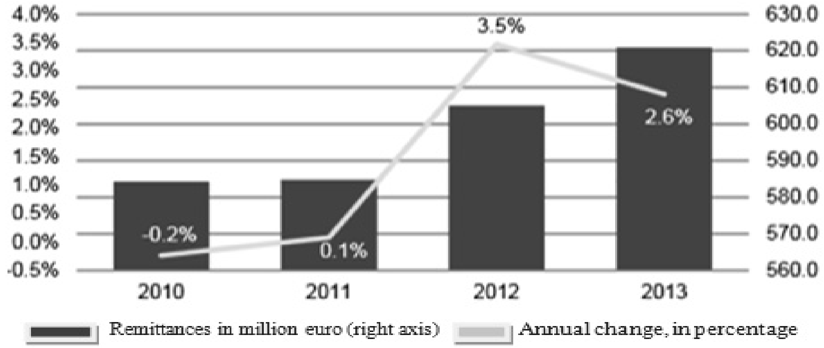
Source: CBK, 2012
Direct Foreign Investments as one of the most important sources of financing in

Kosovo in 2010 amounted to 311.2 million euro compared to 280.9 million euro in 2009, while in 2011 it was achieved net worth of 378.9 million euro. FDI inflow during 2011 was double-digit, reaching the rate of 14.4%. FDIs in Kosovo during 2012 were 232.0 million euro or 41.2% lower than in 2011. The figure above clearly shows a correlation between the GDP growth in the euro area and the share of FDI in GDP in our country where we can see that in 2009 there appeared an economic decline of 4.1% of GDP in countries of euro area, reflected in the decline of FDI participation in Kosovo's GDP to 7.3% from 9.5% in the previous year 2008.
The channel that could have touched Kosovo most is the income of our emigrants-remittances. It is evident that the countries of the region, and especially Kosovo, have a high number of immigrants living in EU and US states, countries that have been mostly affected by the crisis, and therefore, through the reduction of remittances towards Kosovo they affected the crisis transmission (Bartlett and Monastiriotis, 2010).
So one of the channels with which the financial crisis in Kosovo is reported is the remittances. They imply cash flow from immigrants to their families in order to help them financially. This phenomenon is very much present in transition countries, especially in Kosovo, as citizens depend on the income from their family members living abroad. The role of remittances, as a major source of external finance, is considered to be extremely useful for Kosovo. Regardless the income level received or the immigrant profile, remittances increase the recipients' income level which increases demand to consume goods and services, resulting into rising of the demand for consumer goods and services, and for local work force. In other words, the multiplier effect of remittances in Kosovo stimulates economic growth. However, this effect is much weaker in Kosovo because Kosovo mostly depends on imports. According to WB, imports account for 62% of the country's GDP (World Bank, 2012), although increased demand for imports may increase government revenue through higher levels of VAT or other taxes on imports. But if import were lower and export higher or in other words, if Kosovo's productivity were higher, the role and impact of remittances would be much more positive in economic growth and development.
Figure 2: Remittances (remittances) in millions given in € for 2004-2010 for Kosovo

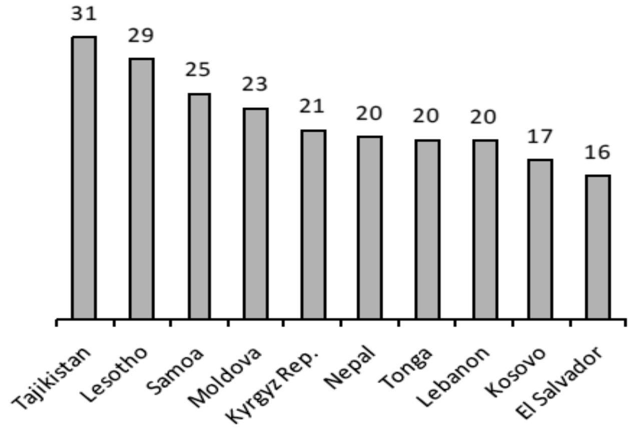


Source: CBK, 2011
Kosovo is influenced through this channel because according to the Ministry of Finance and Economy, Kosovars receive more money from abroad than they earn in Kosovo, and as a result they have depended on their relatives living abroad. Remittances also play an important role in the composition of GDP and in the well-

being of Kosovo residents. They account for 19.4% of GDP in 2009 and 18.5% in 2008 (World Bank, 2013).
Figure 3: Remittances received by immigrants in Kosovo



Source: CBK, 2014
During 2009, remittances totaled 505 million Euros. Remittances declined as a result of the crisis and rising unemployment in developed countries, and after the crisis of 2009 remittances continued to grow with a positive growth trend, but always decreasing. Remittances from abroad during the six months of 2011 amounted to about 580 million Euros. During 2012 there were about 600 million Euros. Also, during 2014, according to CBK's forecasts, there was an increase in remittances.
Kosovo is one of the countries with the largest remittances in the Balkans and belongs to the world's 10 largest countries that receive remittances (World Bank, 2007). More concretely, Kosovo is the 9th country in the world which receives most remittances as a% of GDP (2010).
Figure 4: Top 10 countries that received the most remittances as a% of GDP for 2010



Source: Mohapatra et al., 2011, p. 3
From 1918 to 1999, Kosovo was part of the former Yugoslavia, a period which, due to the difficult economic and political conditions prevailing, was characterized by mass emigration. The biggest wave of emigration was especially in the 1990s when

Serbia abolished the status of autonomy for Kosovo and as a result many people were made redundant (Mustafa, et al., 2007). Even during the Kosovo war in 1998-1999, many immigrants were heading towards European states, such as Germany and Switzerland, for a better life. Although these people left Kosovo, they have tried to help their family by sending them money back. Sending money from emigrants to their family members in Kosovo has a particular impact on the Kosovo economy, through the impact on the consumption of Kosovo families.

According to a questionnaire conducted in 2007 by the Riinvest Institute, about 315,000 Kosovars were living abroad. Although Kosovars live in many countries of the world, remittances are mainly sent from Germany and Switzerland. The table below shows the distribution of immigrants around the world.

Table 1: Distribution of emigrants by country as well as percentage of emigrants in sending countries

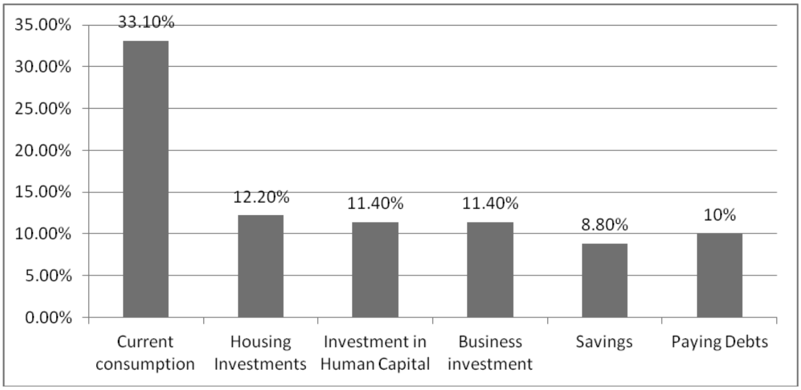
Country of dispatch	Total number of immigrants in dispatching countries	Percentage in total number of immigrants (%)
Germany	**124,110**	**39.4**
Switzerland	**73,080**	**23.2**
Italy	**22,050**	**7.0**
Austria	**21,105**	**6.7**
Scandinavia	18,270	5.8
Great Britain	15,120	4.8
USA	11,025	3.5
France	6,615	2.1
Canada	5,040	1.6
Neighboring countries	11,655	3.7
Other countries	6,930	2.2
	315,000.00	(Total number of immigrants according to the questionnaire from Riinvest. 2007)

Studies on the effect of remittances on macroeconomic performance are scarce in Kosovo but it is suggested that deliveries from abroad have a direct effect on poverty reduction and economic growth through increased investments and trade. They obviously have an impact on improving family welfare because these remittances are used to fund education, finance spending on health care, consumption, and many other services and products (Haxhikadrija, 2009).

Having a direct impact on education, health, investment, consumption, remittances also have a direct impact on economic growth. Since Kosovo has low exports and is heavily dependent on imports, economic growth has largely been supported by the flow of remittances and foreign direct investments (Bertelsmann and BTI, 2010). Remittances also affect the growth of bank deposits that subsequently affect the increase in the amount of loans banks can issue. The increase of loan supply may affect the reduction of interest rates, the improvement of the balance of payments and the growth of the economy because now people have the opportunity to increase the consumption of loans or investments in construction or private businesses and thus have an effect in economic growth.

In the Kosovo economy, remittances are of great importance, they account for 12.8% of GDP, while the foreign direct investments as well as the international assistance also affect economic growth of 7.53% and 9.4% of GDP. But to see more clearly how remittances affect economic growth, we will present distribution across remittance sectors in the way remittances are spent by Kosovo households. More specifically, 45% of remittances are used for consumption, 11% for investment in business and 12% for household investments. These data derive from a UNDP study on remittances in Kosovo. The following figure presents it in more detail.

Figure 5: Using the Remittances by Categories



Source: UNDP, 201

Remittances also affect the reduction of poverty. According to the World Bank, the poverty line is 20 percentage points lower for households in rural areas than in urban areas, because households in rural areas receive more remittances than households living in cities (World Bank, 2012a). About 70% of the immigrants send money to their family members in Kosovo (Mustafa et al., 2007). In general, remittances have a positive impact on business start-ups, job creation and as a result they affect poverty reduction.

Remittances are a very important source of foreign capital in Kosovo, but since remittances are mainly sent by countries that are heavily affected by the crisis, then the crisis also has been transmitted to Kosovo through remittances. Just as we saw in Table no. 14, a significant number of our immigrants live in Germany, Italy, USA, etc. And since these countries are heavily affected by the crisis, remittances have also decreased.

According to de Haas (2009), the micro and macro-economic impacts of remittances are diverse, depending on the context of the dispatching country, the selection of migrants and their use by recipient households. A common and extremely important feature in the context of human development is countercyclical nature: the ability to protect the families in the countries of origin / dispatch at the right time of economic downturn, political conflicts or natural disasters (de Haas, 2009). This, especially, makes sense in the case of larger remittance recipients such as Kosovo, where they account for 11% of the Gross Value Product (UNDP, 2010).

Conclusions

Global Financial Crises are being characterized as phenomena that are repeated occasionally, although the policy makers say that they should no longer be due to the great socio-economic consequences they bring. The crisis that shocked the world was that of 1929-1933, then that of 2007-2008. This last crisis is the biggest crisis that has occurred after the Great Depression of 1929 and the world is still facing the consequences of this crisis. The consequences have been huge in international trade, in manufacturing, in employment, and have affected the well-being of many people. Although Kosovo is one of the smallest states in the Western Balkans, this country has also been affected by the Global Financial Crisis. Transmission of the crisis has not occurred through financial channels, as it has happened in developed countries, nor from other channels such as foreign trade and foreign direct investment, but through remittances. This channel could have affected most Kosovo.

It is evident that the countries of the region, and especially Kosovo, which are mostly affected by the crisis, have a high number of emigrants living in the EU and US states, and therefore have affected that through the reduction of remittances towards Kosovo Even the crisis is transmitted. Remittances declined as a result of the crisis and rising unemployment in developed countries, and after the crisis of 2009 remittances continued to grow with a positive growth trend, but always decreasing.

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