

Business Administration and Business Economics

The Effects of Exchange Rate Market in the Economy of Kosova

Argjira Kadrijaj Dushi¹, Safet Merovci²

Abstract: From a conducted centralized economy, Kosovo's economy became a free market after 1999. This made the economy of Kosovo to face a lot of challenges. One of them and still a topic not studied among Kosovo economists is the Kosovo currency. Kosovo is not yet a member of EU but since 2002 is using euro currency. What are the advantages and disadvantages of using euro currency for the economy of Kosovo? This was not questionable in 2002, because Kosovo was still in the first steps of creating a financial system. But, today the importance of exchange rates in economy is crucial as a result of the internationalization of businesses, the constant increase of world trade with the national one and the rapid change of money transfer technology. In this research, through quantitative and qualitative methods is analyzed the development of exchange rate market in Kosovo and the effects of exchange rates movements in Kosovo economy, its GDP and inflation and in consumer price index. The research will point out the importance of exchange rates as an interest variable for some of Kosovo businesses and its effects in the transition economy of Kosovo which has not been exposed to exchange rates risk on macroeconomic variables.

Keywords: foreign exchange rate; exchange market; commercial bank; oil businesses; consumer price index

JEL Classification: F30; F31; F41

1. Introduction

We are living in an age of globalization, at which governments, companies and individuals make agreements among themselves. This makes everyone exposed to foreign currency exchange risk resulting from fluctuations of foreign currency exchange. Even if a company does not deal with the rest of the world, it is exposed to foreign currency exchange risk because changes in the exchange rate affect that company's participation in the local market. For example, evaluation (appreciation) of the national currency attracts foreign companies to enter in the local market and

¹ Master of Science, University of Prishtina, Kosova. Address: Mother Teresa Str., 10 000 Prishtina, Republic of Kosova, Tel.: +38138244183, Fax: +38138244187. Corresponding author: k.argjira@gmail.com.

² Associate Professor, PhD, University of Prishtina, Kosova. Address: Mother Teresa Str., 10 000 Prishtina, Republic of Kosova, Tel.: +38138244183, Fax: +38138244187. E-mail: safetmerovci@gmail.com.

it jeopardizes market participation of domestic companies (Pilbeam, 2006). This is an example of microeconomic effect of foreign currency exchange movement. From the macroeconomic perspective, the movement of foreign currency exchange affects production, employment, inflation, external balance, interest rates and fiscal policies.

One of the many challenges that Kosovo faced after the war was the choice of a monetary framework. Given the great rush to cash holdings of foreign exchange currencies and the disappearance of the Yugoslav dinar as a transaction tool, not surprisingly in September 1999 UNMIK approved the use of the Deutsche mark and other foreign currencies in Kosovo. Deutsche Mark was unilaterally adopted as a de facto legal currency in Kosovo, and there were no negotiations with Bundesbank in Deutschland or the European Central Bank at that time. There was considerable amount of cash in circulation. The population was familiar with this currency. Adoption of monetary structure, based on the use of the Deutsche mark was introduced as a natural choice. The usage of a stable currency was important in maintaining macroeconomic stability and it played a crucial role in rebuilding confidence in the financial sector. It also stipulated providing of significant support for the development of a strategy directed from abroad, which more than a choice was a need, taking in consideration the size of the domestic market.

In early 2002 the replacement of the euro legacy currency in the Eurozone countries, made it necessarily also the replacement of the Deutsche mark in Kosovo. In contrast to the “adoption” of the Deutsche mark as the main currency in Kosovo in 1999 and the legalization of its wide use, switching to euro currency was made in cooperation with the European Central Bank, as well as some national central banks of Eurozone. Special circumstances faced by the authorities in Kosovo, appeared in numerous challenges in preparations. The high degree of orientation of cash in the economy meant that there was no direct way to assess the volume of the Deutsche mark in circulation. Based on the decisions taken by the European Central Bank, the former Banking Payments Authority of Kosovo decided to disperse about 100 million euros before 1st January 2002.

2. Euro Benefits in Kosovo

Euroisation supported the development of the financial sector, which should have been established immediately after the war. In the beginning, there was no bank in Kosovo and virtually all transactions made in cash. In fact, for almost two years, in Kosovo there was no financial sector and the single financial entity, Micro Enterprise Bank (MEB), was specializing in microcredit. However, two years witnessed a rapid development of financial intermediation in Kosovo, especially

the banking sector. Between March and November 2001, six banks were established, which brought much needed competition in the banking sector.

In 2002 and 2003, seven commercial banks in Kosovo expanded significantly. Given the small size of the economy and population of Kosovo and negative experiences with banks in the past, Kosovo's financial system is characterized by a strong participation of foreign entities. In late December 2004, Kosovo's financial system consisted of seven banks, which operated through 247 offices, 14 microfinance institutions, 3 other non-bank institutions, 7 insurance companies and one company saving company.

Reduction of cash from circulation was one of the main objectives of the former BPK. Change from DEM to EUR provided a unique opportunity to achieve this objective and at the same time helped to strengthen the banking system. Former BPK planned to let down free the exchange amounts up to 1,000 DM, and imposed a fee of 2 percent fee for amounts between 1,000 and 10,000 marks, it was also the maximum amount allowed exchange cash. Amounts that exceed 10,000 DEM should be placed as bank deposits in euros. At the same time, every effort was made to facilitate the role of enterprise sales at Deutsche mark removal from circulation through a natural process.

Setting maximum limits on the amounts of exchange, as well as clearly defining the deadline period of dual currency circulation, greatly encouraged holders of cash to deposit their money in banks, rather to risk not to be exchanged in time. This strategy was accompanied by incentives from banks, which have already improved and multiplied their services to attract new clients to open their accounts. Although this scenario seems simple, its implementation posed some problems. The most important, of course, was the continuing lack of confidence in the banking system. This was hurt most by a still limited access of banking services. At this time, commercial banks in Kosovo had available only 24 offices, while the former BPK operated through a network of 23 offices, of which more than a half were small local agencies, which were opened only with limited hours. Disposal of the euro was successfully completed on 28 February 2002. Thus, from this moment, Kosovo's economy is "euroized" completely and effectively. Euroisation often defined as the adoption of the euro as legal currency and official currency by the authorities of a country outside the euro zone. This definition also implies that the authorities decided to reject their instruments of monetary policy and to abandon their national currency. Given the widespread use of informal Deutsche mark and its role UNMIK rejected this option as a "fait accompli" (a completed fact) At the time when Kosovo chose euroisation, the country put a sound monetary foundation that was needed for economic reconstruction, social and political development in the years to come.

The adoption of the euro as a national currency brought also monetary stability in Kosovo. The risk of devaluation of the national currency disappeared. CBK, which acts as a fiscal agent of the Government of the Republic of Kosovo, does not take any exchange risk, and manages the official reserves. These reserves are mainly invested in euro zone countries, in the central banks and financial institutions with good rating. Kosovo's economy faces no significant exchange risks. In the same way, euroisation has prevented Kosovo in having dual exchange rate of the currency, legal and informal. The introduction of the euro significantly simplified and reduced transaction costs both within and outside of Kosovo, especially when considering the importance of trade within the economy. Neighboring countries, mainly former Yugoslav republics, remain the main trade partners of Kosovo. However euro currency, the same as Deutsche Mark before 2002 is widely used in the region.

2.1. The Effects of Euroisation

Euroisation in Kosovo had also some long-term policy objectives. Euroisation in Kosovo was expected to foster economic stability, solve the problem of reliability, and mainly to increase fiscal discipline by eliminating the possibility of reproducing the money to cover fiscal deficits. After a longer period of time this will lead to increased foreign direct investment. Generally, euroisation was expected to foster economic integration, which has adopted the euro with the economies euro emission countries, in this case with the whole euro area. The adoptive country would already have a stronger economy or political ties with the country issuers. Euroisation in Kosovo did not follow this pattern, since it was a direct result of political and economic disintegration of the former Yugoslavia, and the intervention of the United Nations. But looking at the future, it should actually accelerate the full integration of Kosovo in the Euro zone.

Although there were positive effects on the economy, the Euro currency also brought costs. If we exclude the cost of changing the initial euro held in cash, then the loss of income from the “right of the older” and the cost of the opportunity of holding cash reserves in the Central Bank leads to significant cost for Kosovo. However, costs can be considered affordable, compared with the advantages of euroisation. After the unilateral adoption of the euro, CBK maintains available cash reserves in order to supply the economy, which can be used in exceptional circumstances. If euroisation did not solve all the financial problems in Kosovo and has brought restrictions on running an independent monetary policy, its advantages are undoubtedly positive mainly because the use of the euro has contributed to the stability of the overall financial sector.

3. The Exchange Market in Kosovo

Kosovo is still an economy in transition and laws and regulations have been created and managed by foreign mechanisms, consequently the currency was inherited from Europe because the country had an emergency situation. However, there are several factors that have contributed to the creation and development of the foreign exchange market in Kosovo. Many Kosovar citizens have migrated to foreign countries because of difficult economic conditions and their income are transferred to their family members, remittances, which are still the most important driver of the economy of Kosovo. So the foreign exchange market existed much earlier than the war since we needed remittances into usable currency in Kosovo. Even today, except the fact that remittances are highest revenues in Kosovo, they have shown the necessity of establishing the foreign exchange market and the competition in this market. Today in Kosovo, there are exchange bureaus, special financial institutions licensed by the Central Bank of Kosovo, who do the service of conversion of foreign currencies into euros and vice versa. These exchange bureaus operate throughout Kosovo, but the greatest concentration of exchange is in the region of Pristina, Prizren, Gjilan and Ferizaj.

But, exchange bureaus as one of the participants of the foreign exchange market, they need to convert foreign currencies collected and thus these create monetary reserves, monitors the foreign currency movements and benefit from foreign currency exchange movements. Other participants in the foreign exchange market are commercial banks in Kosovo. Commercial banks in Kosovo have the possibility of opening accounts in foreign currencies, depositing foreign currencies and withdrawing them, and also exchanging foreign currencies such as USD, CHF and GBP in Euro and vice versa. Exchange bureaus also have separate accounts in commercial banks and through these they exchange foreign currencies. Thus, through the collection, exchange, deposits and withdrawals of foreign currencies, each commercial bank in Kosovo creates open position in foreign currencies. The purpose of commercial banks in Kosovo is holding this open position (known internationally as Open Currency Position-OCP) as close as possible to zero, meaning that the bank's assets and liabilities should be equal. Foreign currency assets of a commercial bank are: cash in hand, the balance of current accounts of commercial banks, placements with correspondent banks, foreign currency bonds, loans or overdrafts in foreign currencies. The main liabilities in foreign currency of the balance sheet of a commercial bank are customer deposits in foreign currencies.

Kosovo Central Bank has so far licensed 31 exchange bureaus. To earn a license these exchange bureaus must have minimum capital of EUR 50,000.00 and an object in which they conduct their activity. However, according to several exchanges with which I approached the research, some of which are: "Euro"

exchange bureau In Prizren city, “Prizreni” in Prizren city, “CUFA” in Prishtina city, exchange bureau “Veli” in Prishtina, “Gazi” exchange bureau in Peja city, said they had no control or monitoring by the supervisory institution of these special financial institutions. Consequently, commercial banks in Kosovo when they purchase foreign currencies from their customers; they have to sell them through their account in correspondent banks and vice versa. In this way, in one hand the bank increases the assets side, cash in foreign currency, while on the other hand they reduce the balance of foreign currency in their correspondent bank account. But besides the exchange bureaus, the most important part of the market are businesses that cooperate with other countries and do business in foreign currencies. Among the businesses that mostly do their business in dollar currency are oil businesses. Oil imported from neighboring countries and Kosovo businesses licensed to import petroleum oil make this business cycle in dollar currency. This is due to the fact that exchange rate movements in financial market are very sensitive and the price of oil is affected by the movement of exchange rates. Below is the graph that shows the oil price movements depending on the exchange rate of the dollar against euro.



Figure 1. Oil Price movements vs. EUR/USD exchange rate

Source: www.bloomberg.com

An exchange bureau in the capital of Kosovo, “CUFA” in Prishtina which exchanges around 500,000 euros per day in foreign currencies USD or CHF, during our discussion for how activity in the foreign exchange market and the impact of the Kosovo businesses cited the clients interest for currency speculation is at lower levels, perhaps for lack of information and knowledge about this field. The only ones who actively deal with foreign exchange currencies, depending on rate

movements are speculators (informal exchange currency persons), which are not businesses at all. While based on exchange bureaus owner opinion, businesses that import goods from abroad, which are numerous, have a tendency to follow the market and to convert the amounts needed in the best moments, but nevertheless this is not a phenomenon that has a great impact. Mainly due to the lack of any proper planning and good management, business purchase USD to fulfill their needs when they need to realize transfers.

But, the important participants of the foreign exchange market are commercial banks in Kosovo. All banks, thus counting: ProCredit Bank, Raiffeisen Bank, TEB Bank, NLB and less participation from banks like Private Bank for Business and Banka Ekonomike perform foreign exchange transactions (USD, CHF and GBP) against euro and vice versa according to customers' requirements and the daily turnover of exchange foreign currencies may take up to EUR 2 Mio. From these transactions commercial banks in Kosovo create high profits, and those 100,000 euros per month. Commercial banks have access to the platform for the exchange of foreign currencies obtained from various international banks.

So bankers specialized for foreign exchange process and procedures, part of Treasury Departments of most of the commercial banks in Kosova follow the price of foreign currencies against the USD, CHF and GBP. Businesses and customers are those who are concerned about exchange rates and bank serves about advising them and also trying to complete their requests and needs on exchanging foreign currency funds. Banking officers working in the branches are the ones that meet the client and on their first request for exchanging money, inform Treasury Department of the bank and request the exchange rate from them. Depending what the request is, sale or purchase of foreign currency, Treasury specialists give the exchange rate to the client. Of course, the exchange rate offered to the client is weaker than the market rate and that depending on the bank's internal procedures. Once the customer decides to buy or sell currency, assets of the bank in that currency decrease/increase. So to cover the open currency position, which is the difference between total assets and total liabilities in foreign currency, commercial banks make the reverse operation, i.e. selling or buying a currency on the platform, meaning selling/buying the currency on their accounts in commercial banks. Platforms (such as the following example) when the bank decides to Buy or Sell then her account in foreign currency or in euro in any foreign bank is being credited/debited. So, the bank does the reconciliation of this position. Banks follow the movement of the different foreign exchange rates and quote the customers with a less favorable rate than the bank rate offered by correspondent banks. Or they even wait until the exchange rate is in favor of the bank. This difference is the pure profit of the bank. Below is shown the platform that some of commercial banks in Kosovo use:

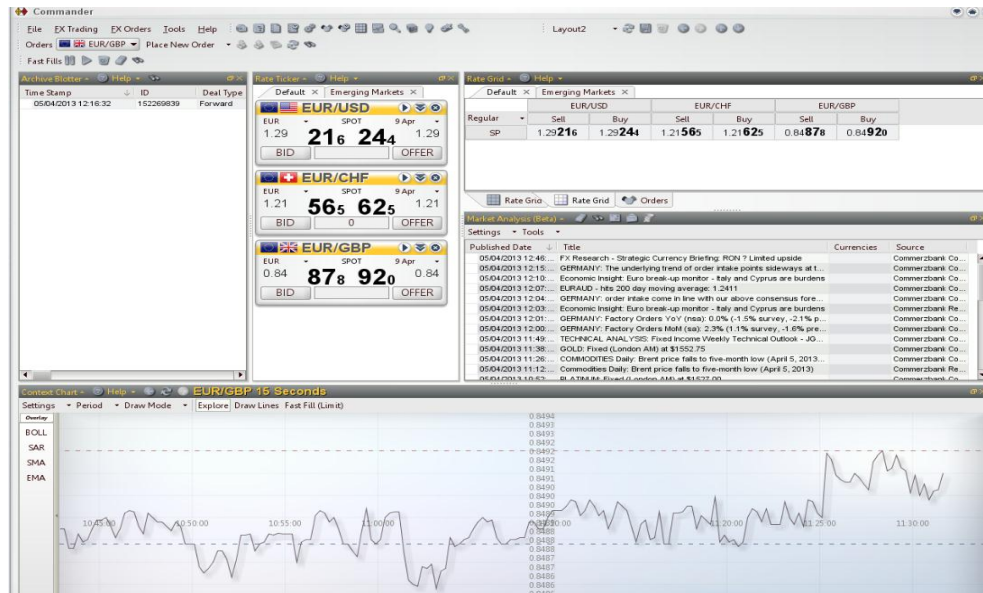


Figure 2. The interface of Commerz Bank for buying/selling of exchange

Source: www.commerzbank.com

Commercial banks of Kosovo are obliged to report on quarterly basis in Kosovo Central Bank the report on foreign currencies, which contains open positions in foreign currency. For these positions commercial banks realize revaluation gains or losses, as the remaining open position in a business day is valued with the exchange rate of that day while that position in the next business day the exchange rate has moved and this is the risk assessment of the bank considering that the exchange rate has moved, appreciated or depreciated within two days.

4. Oil Businesses in Kosovo

During my research in some of commercial banks in Kosovo and also based on the transactions realized with exchange bureaus, the largest share in exchange transactions in the Kosovo's exchange market have the oil business. This is because the oil is imported to Kosovo by some companies, which companies each year earn this right from the government and these companies set the price of oil in Kosovo. The price of oil depends on the financial markets and moves with the movement of the exchange rate EUR / USD.

Taking in consideration the fact that oil is one of the main products in measuring the CPI (consumer price index) in Kosovo, I have done a part of the research paper

on oil business in Kosovo. After meeting with some of the businesses, I can say that the price of oil in Kosovo is decided depending on the prices set from the larger companies that import oil in Kosovo and the office responsible for controlling and monitoring of this sector within the Ministry of Trade and Industry needs to do a better job in supervising this business in Kosovo. In a way this business can be called a monopolistic business in Kosovo. Kosovo citizen is one who does not follow the stock market; do not know if the reduction of oil prices in international markets reflects in his pocket. But, of course, from my experience, we observe that the increase of oil prices in international markets immediately reflect the price of oil in Kosovo. Why is it when we know that businesses have oil reserves and they are buying them with cheaper prices? Once these movements have no control prices and CPI moves depending on the movement of oil prices. The table below presents the consumer price index movements in Kosovo and the oil and gas group in the consumer basket, to be then compared with the movement of this index in the euro area in recent years.

Table 1. Consumer Price Index 2003 – 2011 Kosovo vs. Euro Area

Year	2003	2004	2005	2006	2007	2008	2009	2010	2011
Kosovo CPI	1.3	-1.1	-1.3	0.6	4.4	9.3	-2.4	3.5	7.3
EURO Area CPI	2.1	2.1	2.2	2.2	2.1	3.3	0.3	1.6	2.7

Source: www.ec.europa.eu/eurostat

So, as it is observed, the movements of the consumer price basket in Kosovo can not be compared to price movements in a basket of European consumers. And this makes us think about the control of the pricing of products in Kosovo and particularly in the oil sector. According to the laws, the officers of the Ministry of Trade and Industry are responsible for regulating and monitoring the oil sector in Kosovo. In performing their duties, these offices adhere to neutrality, objectivity, independence and professionalism. Offices duties are defined in the Law on Petroleum and Petroleum Products in Kosovo. Their duties are to review the license, applications for equipment in the oil companies and make decisions on: the license, renewal of license, refusal of the application for the license. During my research I also visited some of the largest importers of oil in Kosovo, as Hib Petrol LLC, Fitorja LLC, Al Petrol LLC and Petrol Company LLC. High prices of petroleum products and price diversity are making Kosovo country with the highest prices in the region. Diesel prices, at the time of my research have reached from 1:25 to 1:29 euro from being 1:19 euro, while the price of gasoline was 1:23 to 1:27, from 1:18 as it was. In Albania, the price of diesel it is 1:21 euros, while

gasoline is 1:28 euros, while in Serbia, the price of diesel it is 1:14 euros, while gasoline 1:17 euros. This shows a difference in price, especially with Serbia. While in Macedonia in the time of my research the prices of petroleum were to go down for 1 cent and the price of gasoline for 2 cents, and all of this due to the Regulatory Commission's decision after making the control.

According to Kosovo citizens, prices have exceeded any possible level with the latest increase of oil price in the market of Kosovo in comparison with the standard prices. Citizens fail to understand all this, because when oil prices in Kosovo increase, the region is not acting according to it or vice versa. The businesses in Kosovo control the prices independently from any rule or control. As per citizen's opinion, the oil prices in Kosova are affected only from the competitiveness of the decrease or increase prices and these owners of oil businesses can raise or lower their prices by their own account. If the opposite would have happened, meaning the price increase then within two days it would be reflected immediately in Kosovo market, even with a greater increase than that of the increase in EU countries. Traders from Kosova say that the oil Kosovar Albanian great reduction is inhibited by the dollar price increase. The truth is that in a specific week in Italy the price of oil is down for 30 percent, also in France and in Deutschland. Even in Macedonia and Montenegro the oil prices decreased by about 30 percent. All of Europe and its customers are benefiting from lower prices of oil. Only the market of Kosovo has deaf ears and blind eyes. No movement from government, from its structures of consumer protection, not even by the Competition Authority that is part of MTI (Ministry for Trade and Industry). This increase in oil prices in the domestic market has a direct impact on the increased cost of production for many products, so there is a possibility to have a knock on effect on the price increase in the near future. Among the sectors that may be hit is agriculture. Prices of oil, grains and other food products in international markets may fluctuate, bringing destabilizing pressures on prices in the country. This is because Kosovo imports a very large consumer products from EU countries, and some countries of the region. The phenomenon of rising prices is inevitable in terms of so great dependence on imports and the absence of protectionist policies for local production.

So, in Kosovo the businesses and the effects of oil prices have a high impact on citizens. This directly impacts family budget. Oil price fluctuates is influenced by the exchange rate of EUR / USD. Kosovo government should monitor this detail in order not to create a monopoly of the business and thus not to allow that for the benefits of some businesses to be damaged the economy of Kosovo.

5. The Future of Kosovo Currency

Kosovo has a relatively new economy. Euro currency is being used as its official currency and cannot affect the money supply of money in the country. The financial crises of recent years many times by many Europeans have questioned the future of the euro, the question of whether Kosovo is ready to face a possible crisis of the EU currency or not. Deutsche, the main state of EURO currency has faced numerous debates about EURO advantages and cost-benefits analysis of this currency for the Deutsche people. They pay high taxes while their country is investing in recent years in other Eurozone countries that are in crisis to help and this way is helping so the stability of the EURO currency. But will this be allowed further if other countries continue to have financial debt crisis? To analyze this in my research, I did a survey among representatives of the Central Bank of Kosovo, representatives of commercial banks, the Ministry of Finance and the World Bank in Kosovo.

Analysts of the economy of our country believe that EURO is a very strong currency to fail despite the economic crisis and debts crisis in some Eurozone member countries, but it will not affect the economy of Kosovo. Some countries are at risk of bankruptcy, which can lead to failure of the common currency, which is for a long time criticized as a thoughtless move by world renowned economists. Now that this risk threatens, Kosovo has no alternative plan for such a situation since uses the euro since February 2002. When the first contingent of about 100 million euros was brought to Kosovo for the first time in December 2001, the situation was felt immediately in the basket of Kosovars who had a little less cash in euros than in deutsche marks and they quickly became the same in values. While analysts commercial banks in Kosovo express their opinion based on the fact that Kosovo has a poor economy, hence not much related to the European one, and it makes the economy less fragile Kosovo by foreign exchange rates. Another element is the fact that Kosovo has small amount of foreign debt compared with other countries. Currently it is estimated that Kosovo's public debt amounts roughly 330 million euros.

Otherwise, in the absence of monetary policy instruments to manage monetary offer and to issue its currency, Kosovo should follow its fate by watching what happens in Deutschland – with which remains connected through the euro. This is because when Kosovo in 2002 adopted the Euro as its currency, we didn't have monetary policy and Deutschland became the guarantor of the euro amount in the country. A leading private bank in Kosovo admits that the debt crisis in some euro area countries has affected our country. According to him, the debts have led to a decline in deposits as well as the requirements for loans which are the largest in the interest of the region and beyond, they range from 11 to 14 percent depending on

the type of loan. Central Bank of Kosovo, CBK, which makes monitoring of banks and insurance companies and is responsible for maintaining the quality and quantity of the euro in the country, says there is no room for worry as “Euro currency remains one of the most strong in the world”.

According to statistics from the Central Bank of Kosovo, the economic crisis has caught the globe in 2008, has not affected the economy of Kosovo, thus relying on the fact that remittances to Kosovo had remained stable. Currently, they mainly come from the family countries- Deutschland and Switzerland. Since 2004 until the end of 2009 the Kosova diaspora, according to statistics of CBK, remittances sent to Kosovo were 2 billion and 798 million euros. Whereas in the first quarter of 2011 remittances amounted to 111.3 million euros, while in the same period last year this amount was 101.2 million euros. While officers from the Ministry of Finance in Kosovo support the fact that EUR will survive because until now it has shown its importance and power, but in case of any crisis, Kosovo will emit its currency. If we are ready or not to do so, was not possible to find any answers. So, Kosovo remains to invest and start thinking primarily for development and implementation of monetary policy, with the help of foreign financial institutions and thus be ready to better manage possible financial crises of its currency and be ready to control the money supply and why not in the future be able to have all institutions prepared to manage a new currency. This will be done through the Central Bank of Kosovo and the Ministry of Economy and Finance.

In this respect, for the future of Kosovo currency, namely the future of Kosovo financial markets, it is worth mentioning the Stock Exchange of financial markets. While most countries in the region are participating in stock exchange, then Kosovo, in order to develop the capital market and financial market, should be participant of the stock market in the future and also have a financial rating in order to be part of all financial markets worldwide. But, in this respect nothing is yet done. How to create the infrastructure of the stock market in Kosovo? This was a question with no answer at any of financial institutions in Kosovo. But, in this regard the Government of Kosovo, namely the Ministry of Economic Development should take examples of the region (Albania, Macedonia and Montenegro) and begin preparations for the establishment of the Kosovo stock.

6. Recommendations and Conclusions

Financial globalization is one of the trends that have reshaped the global economy unlike the economy designed by the Bretton Woods system in 1944 and has made the world know about economic factors that have a crucial influence in the future and the direction of the international monetary system. But, it would be difficult to

estimate the importance of the foreign currency exchange markets to the world economy. They affect production and employment through real exchange rates. They affect inflation through import costs and prices of commodities. They affect international capital flows through the risk and the return of assets. Foreign exchange rates reasonably are in focus of policymakers, the public and the media definitely. The fact that this indicator is not part of macroeconomic policy, part of the economic strategy development, citizens and the media was confirmed through the survey with Ministry of Finance, Central Bank of Kosovo, large businesses in Kosovo, exchange bureaus and commercial banks in Kosovo.

After all facts and the reports done during my research, it would not be an exaggeration if we would emphasize that foreign exchange rates are one of the most important macroeconomic variable in open economies, especially in today's economic environment, financial deregulation and globalization of financial markets. The exchange rate market is one of the largest financial markets with average daily turnover of about 3 billion euros. Foreign exchange rates of a country affect the economy the aggregate demand through prices of import and export. When interest rates rise in a country, then that country's currency is strengthened as foreign investors may be interested in investing in the country. When the country has surplus in the current account, the country's currency is strengthened as in the case of the trade deficit on the current account of the country's, currency will weaken. Whereas, when gross domestic product of the country increases then this decreases the weakening of the currency. So GDP influences the movement of foreign currency exchange.

All these reflections of the foreign currency exchange in the economy of a country are not studied and taken into account by any institution in Kosovo. Officials of financial institutions of the state of Kosovo do not foresee any financial crisis in Kosovo and they are not making any adequate preparation or analysis in this regard. My first recommendation after this research would be that institutions of Kosovo, Central Bank and Ministry of Finance and Economic Development must make analysis about the financial environment in Kosovo for all economic variables and in this way the impact of foreign currency exchange in the economy will be no longer not estimated.

Regulatory office within the Ministry of Trade and Industry should be active in controlling the movement of prices of key products that affect the consumer price index in Kosovo, because based on research conducted on oil business, food oil and sugar, these businesses make only the raising prices based on the movement of these prices in financial markets, but they do not decrease the prices when it comes to price reductions of these products in global financial markets. The price index in Kosovo suffers increase depending on the price movement of oil from Kosovo

businesses, which have created a monopoly in Kosovo. This section requires state regulation and monitoring.

Commercial banks create benefits and are one of the key participants in the foreign exchange market in Kosovo, but this part, based on visits made during my research, was not monitored from respective institutions, but it remains the responsibility of the banks management. This could affect the performance of commercial banks in Kosovo. Also, the exchange bureaus make their activity without control and have their own high profits by speculating on exchange rate movements and thus, revenues collected mainly from remittances from Kosovars are exchanged and this money is part of part of the economy without a follow-up on global trends of these currencies and without control by the state.

Kosovo despite the current developments has a long road ahead to prepare for the management and monitoring of foreign currency exchange rate reflections on its economy, to work in preparation of a substitute currency of Euro in order not to be always left in the “mercy” of an alternative choice by the European Union. Kosovo’s work on preparing the infrastructure of stock market so that the country would gradually be in step with regional financial developments and would be able to protect first the customer, then businesses and to take preventive measures for economic variables which are affected from the movements of each other.

7. References

- Bailey, E. R. (2005). *The Economics of Financial Markets*. Cambridge: Cambridge University Press.
- Eiteman, D.; Stonehill, A. & Moffet, M. (2010). *Multinational Business Finance*. London: Pearson.
- Grath, A. (2008). *The Handbook of International Trade and Finance*. London: Kogan Page.
- Karadelogiou, P. & Terraza, V. (2009). *Exchange rate and macroeconomic dynamics*. Canada: Palgrave MacMillan.
- Levi, Maurice D. (2005). *International Finance*. London & New York: Routledge.
- Macdonald, R. (2010). *Exchange rates economics: Theories and evidence*. London & New York: Routledge.
- Pilbeam, K. (2006). *International Finance*. New York: Palgrave Macmillan.

Online sources

- www.bloomberg.com, date: 07.07.2013.
- www.commerzbank.com, date: 11.07.2013.
- www.bqk-kos.org, date: 09.05.2013.
- www.ec.europa.eu/eurostat, date: 09.05.2013.