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Here I am again, writing the acknowledgements again. The sensation is feel now again is overwhelming because this moment marks the end of a journey and for sure the beginning of an exciting new adventure. In these pages, I take the opportunity to thank the people who were close to me in this journey and I sincerely hope not to forget anyone. First, I want to thank Professor Antonio Palestrini for the precious teaching and the dedicated hours to my thesis.

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Abstract

L'Obiettivo di questa o tesi è quello di analizzare il ruolo delle organizzazioni internazionali nello sviluppo economico dell'Albania, dopo la caduta del regime comunista.

Inizialmente farò riferimento ai primi anni dopo la caduta del regime comunista.

Successivamente andrò a spiegare il ruolo delle organizzazioni internazionali nello sviluppo del nostro paese, ho scelto di analizzare la missione di solo tre di organizzazioni internazionali, ovvero Unione Europea, Banca Mondiale e FMI.

Per quanto riguarda la metodologia utilizzata per scrivere questa tesi è stata fatta ricercando e facendo riferimento a vari libri contemporanei, materiali web ottenuti da indirizzi ufficiali, articoli, riviste e rapporti di organizzazioni sulle prestazioni di sviluppo dell'Albania.

Il processo di sviluppo in Albania è stato accompagnato dall'apertura dell'economia e della democratizzazione delle istituzioni.

Le organizzazioni internazionali sono diventate una parte importante del processo di sviluppo e democratizzazione del Paese e la loro presenza è avvertita in ogni aspetto della vita politica e sociale.

Lo sviluppo e il progresso del Paese sono stati raggiunti attraverso investimenti stranieri in tutti gli aspetti dall'educazione, politica, sociale, sistema sanitario e della società civile, ecc.

Nel primo capitolo andrò ad elencare tutti i dati rilevanti dell'Albania dalla dichiarazione dell'indipendenza fino all'installazione del regime comunista, descriverò lo sviluppo economico e gli eventi politici. Successivamente il capitolo continua con la descrizione dello sviluppo del paese nei primi anni della transizione, è poi gli schemi piramidali o meglio conosciuto come schema di Ponzi.

I principali fattori che hanno contribuito alla crescita del fenomeno della schema piramidale è stata l'inadeguatezza del sistema finanziario formale. Le tre banche statali che dominavano il mercato dei depositi (che detenevano oltre il 90 per cento dei depositi) non avevano intermediari affidabili, tuttavia, il sistema dei pagamenti era gravemente inadeguato.

Nel secondo capitolo descrivo il ruolo delle organizzazioni internazionali nello sviluppo economico dell'Albania.

Il periodo 1992-1996 è stato un periodo caratterizzato dalla instaurazione dei rapporti con l'UE.

In seguito all'istaurazione dei rapporti con l'UE, le istituzioni politico-economiche, gli organi decisionali democratici, le politiche delle banche centrali, l'organizzazione della privatizzazione delle industrie e la regolamentazione delle imprese private - hanno avuto tutti un impatto positivo in questa prima fase del periodo di transizione.

Una delle principali riforme che sono state attuate è la liberalizzazione e la privatizzazione dello sviluppo del settore privato. Il processo di liberalizzazione,

d'altra parte, si è rivelato una procedura complicata e delicata rispetto agli aspetti economici e sociali. La crescita economica in Albania per il periodo 1992-1996 rappresenta doppi standard.

Le condizioni del settore informale è il ruolo che hanno avuto le istituzioni internazionali come l'Unione Europea e la Banca Europea per la Ricostruzione e lo Sviluppo (BERS), il Fondo Monetario Internazionale (FMI), la Banca Mondiale, nello sviluppo economico dell'Albania. L'analisi si basa sulle prove esistenti e esamina tutti i fatti relativi alle caratteristiche dell'economia in via di sviluppo in Albania e il rapporto con le istituzioni economiche internazionali e le loro raccomandazioni.

Nel terzo e ultimo capitolo, mi sono concentrata sull'attuale sviluppo economico dell'Albania, dopo le diverse riforme intraprese in seguito alle raccomandazioni fatte dalle organizzazioni internazionali.

In primis, la crisi finanziaria del 2008 ha avuto un impatto importante sull'economia globale che è diventato normale riferirsi ad essa quasi come un'era diversa "prima e dopo la crisi". Il fatto è che molti aspetti dell'attività economica sono cambiati radicalmente dopo il 2008, dal punto di vista dell'infrastruttura finanziaria globale o del comportamento degli attori economici, sia istituzionali che individuali.

Gli effetti della crisi del 2008 sono stati trasmessi a diverse economie attraverso canali diversi. Per fortuna in Albania la crisi non ha avuto un impatto devastante

nel 2008, ma il degrado della performance dell'attività economica è emerso anno dopo anno per arrivare al culmine nel 2012 e 2013. L'anno 2012 è stato l'anno in cui l'Albania ha toccato il culmine della povertà, poi nel 2013 con le politiche economiche del nuovo governo per limitare in parte i danni causati dalla crisi ha aumentato il debito pubblico, portandolo ai massimi livelli.

Il paese è in una nuova realtà oggi; l'economia albanese è tornata a crescere e l'anno 2013 sembra una realtà lontana. L'economia albanese cresce al 4%. La domanda è: è abbastanza? Questo è un dibattito che non finirà mai. Il 4% non è sufficiente, il 7% probabilmente non è sufficiente, il 10% probabilmente non è sufficiente per convergere con i livelli dell'UE abbastanza presto, ma confrontandolo con lo 0,8% del 2013 che abbiamo rischiato il collasso totale, ovviamente il 4 è positivo. Il prossimo anno la crescita dell'Albania è stimata al 4,3%, che si ritiene sia la più alta della regione.

Introduction

This paper aims at examining the role that international organizations have played in the development of Albania after the overthrow of the communist regime. Initially there is a retrospect of Albania's development since the declaration of independence until nowadays. Afterwards, there is a descriptive theoretical part of the international organizations, and their role in the global economic development. The paper then focuses on Albania, dealing with the relationship Albania had with international organizations in the post-communist period. Following this theoretical part continues the concrete benefits and the role played by various international organizations in the development of our country, where due to the large number of organizations that have contributed to Albania I have chosen to analyse the mission of only three of them: European Union, World Bank and IMF.

Regarding the methodology used to write this paper, I can emphasize that the conception of this study was done by researching and referring to various contemporary books, web materials obtained from official addresses, articles, journals and reports of organizations on Albania's development performance. The development process in Albania was accompanied by the opening up of the economy and democratization of institutions and society with the assistance expressed through loans and funds of international organizations such as the World Bank, International Monetary Fund, Union European etc. International organizations have become an important part of the country's development and

democratization process and their presence is felt in every aspect of political and social life. The development of the paper reveals the thesis that international organizations have influenced the process of development and democratization of the country through their economic contribution and assistance in almost every field. The development and progress of the country has been achieved through foreign investment in all aspects of political, social, health education, civil society, etc.

The first chapter is a retrospect of Albania since declaration of independence until the installation of the communist regime, described the economic development and political events in Albania. Afterwards the chapter 1 continues with the description of the development of the country in the first years of the transition and the development of pyramids or differently known Ponzi scheme.

The main contributing factor to the growth of the pyramid scheme phenomenon was the inadequacy of the formal financial system. The three state banks that dominated the deposit-taking market (holding over 90 percent of deposits) were not reliable intermediaries of savings, and private banks were slow to emerge and not particularly interested in attracting domestic currency deposits, devoting their attention mostly to trade financing. The problem in the state banks was not low interest rates: to ensure that depositors were offered interest rates that are positive in real terms, the Bank of Albania set minimum interest rates on time deposits, and from mid-1993 onward, these were consistently above the prevailing rate of

inflation. However, the payments system was seriously inadequate. In September 1996, the average completion time for payment transactions between accounts at different branches of the same state-owned bank was 5–6 days, and the completion time when the transaction involved accounts at different state-owned banks could exceed 15 days. Because of these problems, and of a general distrust of the banks, the public tended to hold an unusually high proportion of their financial assets in cash (at end-1995 the currency/deposit ratio was 64 percent) and was on the lookout for alternative investment opportunities.

On the lending side, the banks' problems were even worse, leading to the emergence of an informal credit market. Banking supervision and regulation was rudimentary, and this, combined with a culture under which loans from state banks were often regarded by borrowers as not requiring repayment, led to a growing bad loan problem. By the end of 1994, of loans made since June 1992 when the state banks began operations, 27 percent were nonperforming. By the end of 1995, in two of the three state-owned banks, overdue loans accounted for almost half of total outstanding loans.

In response to the banks' poor credit evaluation and loan collection, the Bank of Albania imposed bank-by-bank credit ceilings. These were set at levels that were well below what the banks wanted and insufficient to meet the demands for credit to the private sector at prevailing interest rates. The limitations of the banking

system made these measures sensible, indeed necessary, but the result was that businesses increasingly turned for credit to the informal credit market.

In the second chapter I describe the role of international organizations in the economic development of Albania. 1992-1996 was a very distinctive period for the relationship between EU and the Western Balkan countries, especially for Albania. In the new way of market economies development, each country addressed their problems in distinct manners. The relevant politico-economic institutions, democratic decision-making bodies, central banking policies, the organization of privatization of industries, and the regulation of private firms – all had an impact in this first phase of transition period. When these institutions are inappropriate for the development of free market economies, one reaction in many countries is the spontaneous development of informal economies. One of the main strategies of stabilization and liberalization was privatization and the development of the private sector. The liberalization process, on the other hand, proved to be a complicated and delicate procedure with respect to both economic and social aspects. The economic growth in Albania for the period 1992-1996 represents double standards. This paper presents a study of the role of the informal sector in transition. This chapter seeks to present the economic growth of Albania during the first post- communist decade. It will analyse the conditions for the informal sector to emerge. On the other hand the paper examines the role of the economic institutions like European Union and European Bank for Reconstruction and Development

(EBRD), the International Monetary Fund (IMF), the World Bank, etc. The analysis are based on the existing evidence which examines all the facts for the characteristics of developing economy in Albania and the report with the international economic institutions and their recommendations.

In the third and last chapter, I focused on the actual economic development of Albania, after the different reforms undertaken and the following of the recommendations given by the international organizations.

The 2008 financial crisis has had such a major impact on the global economy that it has become normal to refer to it almost as a different era "before and after the crisis". The fact is that many aspects of economic activity have changed radically after 2008, be they from the point of view of global financial infrastructure or the behaviour of economic actors, both institutional and individual.

The effects of the 2008 crisis were transmitted to different economies through different channels. Albania thankfully did not engage in a "classic" recession after the 2008 crisis, but the degradation of economic activity performance emerged year after year culminating in 2012 and 2013. 2012 was the year when Albania was considered at the height of poverty and in 2013 when the domestic debt was in alarming levels.

The country is in a new reality today; the Albanian economy has left behind the difficult year of 2013. The Albanian economy grows to 4%. The question is: is it enough? This is a debate that will never end. 4% is not enough, 7% probably not

enough, 10% probably not enough to converge with the EU level soon enough, but when comparing it to 0.8% of 2013 or the risk of a total collapse , of course 4 is positive. Next year Albania is projected at 4.3%, which is thought to be the highest in the region.

Chapter I- Economic development and Crisis in retrospect

1.1 Since Declaration of Independence

Albania has gone through a difficult and tiring road, and this has been reflected in the performance of its economy. Albania declared independence in 1912, had fragile governing structures, fragile democracy and, consequently, fragile economy. The efforts of the new Albanian state have continued for years to strengthen its institutions, democracy and above all the economy. In 1913, the secret conference of Ambassadors in London, decided the official borders of Albania. More than half of Albanian territory was left out of the official borders. It should be noted that during that period, agriculture was the main sector of the economy and the remaining land outside the borders constituted the fertile agricultural regions and occupied the largest agricultural area of Albania. With the detachment of these territories, within the borders of Albania remain the poorest provinces, in most mountainous areas, while the plains were mostly marshy and unusable for agricultural purposes. The year 1913 can be considered a year of economic crisis for Albania. Historians judge that Albania's territorial mutilation had profound economic consequences for the Albanian state. The territorial division of the country led to the abolition of the creation of the internal market that had begun as an economic process since the previous century. This fragmentation caused independent Albania since the very beginning a deep economic crisis. Leaving beyond the boundaries of Albanian territories with rich farming economies had

profound consequences in the field of domestic and foreign trade. With the poor mountainous regions that remained within state borders, independent Albania with its agricultural crops normally met 59-60¹ percent of the population's needs. So the country was forced to import not only the previous industrial products, and considerable amounts of agricultural produce, without being able to cover it with its exports. As a result, the Albanian independent state was born with a passive trade balance, where the mass of imported goods increased and the goods exported by Albania were constantly reduced.

One problematic of this period is ownership over the land. With the declaration of independence, the country was also liberated financial obligations to the High Gate and so incomes of the national economy remained inland. This is considered to be a favorable circumstance for the development of the industry, however it is judged that the national economy did not sufficiently benefit from the declaration of independence. The first 8 years of independent Albania, 1912-1920, were years of lack of stability which hindered the economic development of the country.

However, with Ahmet Zogu ruling the country in 1924 and his closeness to the Italian Kingdom, the situation changed. Albania received considerable loans from the Italian Kingdom to modernize the country. And in fact, there were some positive results in terms of economic development, but it did not last for long.

The world economic crisis known as "The Great Depression" began in October 1929 with the collapse of Wall Street and soon spread all over the world. The effects

¹ Historia e Shqiperise – Akademia e Shkencave e Shqiperise, volume 3, 2002

that this crisis brought were high unemployment, poverty, low profits, deflation, reduced income in agriculture and sharp economic decline. But above all, this crisis brought about a loss of confidence for economic growth in the future. The crisis started in 1928 would last until 1933. The world economic crisis that emerged in 1929 affected Albania, but unlike other capitalist countries, Albania was not involved in the crisis as a result of the super-production of domestic capital. It is estimated that it deepened the difficulties that existed before, while the negative effects extended even after 1933².

The first effect Albania felt in this crisis was the decline of remittances. As a result, households living from these remittances entered deep poverty.

Other countries affected by the crisis, to ease themselves from the economic crisis, lowered commodity prices by conquering the markets of other countries, including Albania. The goods that came to Albania in this period easily competed with the products of Albanian artisans who remained in stores or in houses.

Official history points out that in this period an artificial super-production was created which resulted in lowering the prices of handicraft products that followed with their rapid depreciation. The effects of the crisis in this period would also affect the state bank, where the government was not able to continue the initial investments nor pay regularly the salaries of the public administration employees, where there were cases where the delay in the payment of salaries ranged from 4 to 7 months. These factors greatly reduced the country's purchasing power, which also

² Historia e Shqiperise – Akademia e Shkencave e Shqiperise, volume 3, 2002, pg. 58

led to an unprecedented price cut. In 1934, the prices of articles were nearly three times lower than in 1928.

Characteristic of the effects of the crisis in Albania was that it culminated in 1934 and not in 1932 as it did in other countries. This crisis created an unfavorable situation for the industry in the country. During this period, no new factories were opened, while existing ones slowed down their economic activity or suspended their activity. Thousands of artisans failed to pay taxes and sell their products, which led to a profound depletion of this category, forcing them to shut down shops and workshops.

As in other countries, the effects of the crisis produced profound unemployment. In this period, because of the crisis, a large number of impoverished peasants fled to cities, migrants began to return to their homeland, while emigration was no longer seen as a job opportunity, which led to a large increase in the number of unemployed. The collapse of small economies and the growth of the unemployed led to the growth of debts and the rapid development of the usury phenomenon. Huge debt demands brought the interest rate rise, where it reached up to 100³ percent. After 1934, Albania began to feel the first improvements in the economy. The industry in Albania started recovering from the fact that the cycle of the global economic crisis was fueling the rise in the price of goods.

³ Historia e Shqipërisë – Akademia e Shkencave e Shqipërisë, volume 3, 2002

Years of the world economic crisis marked a new stage for the country's history as the need for foreign investment and capital would increase the presence of Italian capital in Albania to the extent that it would serve as the official motivation for the occupation of the country.

After the Second World War, the country was plagued by war and many branches of the economy were underdeveloped. According to the population census conducted on September 30, 1945, the population in the country reached 1,122,044, of whom 21.3%⁴ lived in the city and 78.7%⁵ lived in the village. Over 80% of the population was illiterate.

State finances had touched the end. The economic conditions in which the country was located were the most difficult among Eastern European countries. It should be noted that the Axis war and invasion did not fundamentally change the economic conditions of Albania. Historically, the base of the Albanian economy was agriculture and stockbreeding, as about 80% of the pre-war population was engaged in agriculture and agriculture. The situation in these activities was backward and primitive. Except for oil and chromium production, Albania did not have any other industry. Italian invasion improved the traffic network, expanded the ports and built new roads connecting the mining areas with the ports, but these minimal investments were not enough for the development of the economy

When the Communists came to power, Albania began applying the centralized economy model, similarly to other countries of the east. In this period, the country

⁴ Historia e Shqiperise – Akademia e Shkencave e Shqiperise, volume 3, 2002

⁵ Same book

receives considerable support from the allied countries, initially from Yugoslavia, then from the Soviet Union and then from China. Until the 1970s, Albania recognized positive development trends, but after the collapse of China's relationship with the lack of aid from a powerful ally, it would also lead to the degradation of the economic system and would therefore be reflected in a crisis that would ultimately lead to changing the economic and political model. After the termination of relations with China, the economy would be based on domestic resources by bringing strong constraints to the economy.

Gradually, Albania started to receive less and less foreign aid, based on domestic resources, while on the other hand, the need for the principle of self-restraint and saving was publicly cultivated. Within 12 years, Albania was turning from a country 50%⁶ dependent of trade and aid to other countries, in a country that would rely on the principle of support in its own forces. Albania's goal was concretized in the 1976 Constitution, which stipulated the prohibition of foreign aid, credit. In the same constitution was also determined that the Albanian economy would be based on domestic resources.

In the period 1980-1990, the Albanian economy changed course. This period is considered as one of the most difficult moments faced by the country's economy.

During this period, Albania starts a new phase where, in the face of the difficulties or crisis that might come, the measures taken were austerity. In addition to what happened to budget planning and spending cuts, propaganda at the time paid special

⁶ Historia e Shqiperise – Akademia e Shkencave e Shqiperise, volume 3, 2002

attention to spreading messages about the need to save. In this period, Albania begins to diversify economic relations with other countries.

From the 1980s to the 1990s, the Albanian economy was not performing well and the coercive measures finally reached food rationing. In this period, the country fell into a deep economic and financial crisis. The 2 % growth rate at the beginning went to a minus at the end. Under the conditions of relying on its own forces, low labor productivity, technology depreciation, inability to invest in it and not receiving loans and aid from abroad, the country would face an economic model that cannot be compared to any other country. Isolation of the country would bring irrational economic policies, maintaining a low level of consumption in the population, and increasing austerity measures for the population.

Shops faced long-standings for basic products. In addition, state property was affected by negative phenomena such as damage, theft or fictitious reporting on the work and implementation of the plans. Some of the policies that the former regime leaders themselves described as being wrong were associating the cooperative yard and collecting livestock of members of agricultural cooperatives or transforming high-profile cooperatives into agricultural enterprises. Yarding and fencing of livestock turned the peasant from the producer to the customer, just as a worker in the city, which would result in the disappearance of farmers' interest in increasing the production.

All these signals meant only one thing for Albania, that the country was heading for bankruptcy and this led to the government's withdrawal from the previous extreme measures, but that did not give the expected effect of the economic revival of the country.

It should be noted that in the same period, other countries of the East were also facing economic difficulties, applying the centralized economic model. The hybrid economic model that was applied in Albania during this period came first in the realization of the plan and not the market need by not meeting the growing needs of the population. Eventually, the government of that time was not able to provide anything for its own people and the end of 80s saw dramatic changes in the political sphere in Albania. People started riots and the regime fell opening the country to democracy and to the West.

1.2 Regime changes. Ponzi scheme

Changing the system in the 1990s was accompanied by numerous economic difficulties, to the point that government leaders in the early years of democratic power faced deficiencies in the state's reserves where the primary risk was the rapid ending of food reserves. This risk brought the intervention of international humanitarian missions to overcome the emergency supply of the population with food.

The beginning of 90s were years of dramatic changes in Albania. Massively people were leaving the country to find a better future in Europe, even if the major leitmotif of every person who partook in the riots of 1990 was, “We want Albania like all of Europe”.

However, the changes of regimes opened Albania. International Organizations such as the European Community, World Bank and the IMF were the first to join Albania and to engage in helping her in her new path of democracy and market economy.

First years were difficult, since neither the Government of Albania nor the public administration familiar with the concept of market economy. However, the presence of World Bank, IMF and the European Community guided the country in making the necessary changes and taking the necessary steps to overcome the economical difficulty.

Albanian economy started giving positive in the early years of transition to the point it was considered impressive recovery.

	1991	1992	1993	1994	1995	1996	1997	1998
	(Percent change)							
Real GDP	-28.0	-7.2	9.8	9.4	8.9	9.1	-7.0	8.0
Retail prices (during period)	104.1	236.5	20.9	5.8	6.6	17.4	-42.1	8.7
	(In percent of GDP)							
Saving-investment balance								
Foreign saving*	19.7	57.1	28.7	-4.3	9.7	11.5	14.3	8.3
Domestic saving	-13.2	-51.9	-15.9	3.5	8.3	-4.0	-7	7.7
Public*	-27.4	-21.9	-14.1	-0.5	-6.5	-5.0	-10.0	-8.1
Private	13.9	-30.0	-1.3	-4.2	14.9	17.0	12.4	15.9
Investment	6.1	5.2	13.2	7.9	18.0	12.5	18.0	16.0
Public	6.1	4.0	9.5	8.5	8.5	4.5	4.0	2.2
Private	0.0	1.2	3.7	9.5	9.5	11.0	12.0	16.8
Fiscal sector								
Revenues	31.7	23.5	25.7	24.5	23.9	19.7	16.9	20.3
Expenditures	62.2	44.0	40.2	36.3	34.3	36.3	29.4	36.7
Overall deficit	43.5	20.3	14.4	2.4	10.3	11.7	12.6	16.4
Domestically financed deficit	43.5	20.0	9.1	7.3	6.8	10.6	10.8	6.4
Monetary indicators								
Broad money growth (in percent)	...	...	75.0	40.5	51.8	47.8	28.4	19.9
Growth in private sector credit (in percent)	...	...	...	61.4	15.9	30.5	19.0	15.8
Broad money/quest. GDP	...	...	2.68	2.83	2.22	1.97	1.92	1.94
Interest rate (%) monthly deposits)	...	...	14.0	7.0	10.0	18.5	26.0	16.5

Figure 1 Albania: Basic Indicator and Macroeconomic Framework, 1991 -1998

Source Chris Jarvis - Rise and Fall of Pyramid Schemes in Albania

Albania faced initial shocks: output fell by nearly half between 1989 and 1992, and inflation rose to triple digits. However, during 1993–95 GDP growth averaged close to 10 percent while inflation fell to single digits and external imbalances were reduced sharply¹.

Eventhough, there were huge steps forward in the economy with the reforms taken, there were still other problem emerging. Structural reform was stagnant, and the most critical reform to be taken was in the banking sector. The inadequacy of the formal banking system lead to the growth of pyramid scheme phenonmenon.

¹ Chris Jarvis – Rise and Fall of Pyramids Schemes in Albania

Over 90 %² of the deposits of Albanians was held by 3 state banks that dominated the market. The problem with the inadequacy of the state banks lied not much on the low interest rates but instead in the time required to complete a transaction with the bank that on average was 5-6 days and at time could even exceed 15 days. In addition, lending was another problem. Banking³ supervision and regulation was rudimentary, and this, combined with a culture under which loans from state banks were often regarded by borrowers as not requiring repayment, led to a growing bad loan problem. By the end of 1994, of loans made since June 1992 when the state banks began operations, 27 percent were nonperforming. By the end of 1995, in two of the three state-owned banks, overdue loans accounted for almost half of total outstanding loans.

These problems lead to the flourishing of the informal market of money lending. Such activity was generally seen as a not harmful activity but that instead made an important contribution to growth. For a long time it was difficult to understand whether it was informal lending market or pyramid scheme as both informal credit market and the companies that invested on their own behalf drew resources from the domestic savings and from flows of remittances.

In early 1996 started a real mania to deposit money in pyramid schemes as more of them were emerging. The newest pyramid schemes entered the market and offered

² IMF Country Report 1997

³ Chirs Javir – Rise and Fall of the Pyramid Scheme in Albania

high interest rates, up to 8 %. This was a real competition between pyramid schemes, who was going to offer the highest rate. People started selling everything they owned to deposit their money in these companies. The situation became alarming for the IMF and the World Bank, which constantly asked the government to take action against these companies and their activity.

By the end of 1996 and early 1997, pyramid companies started declaring bankruptcy. This event triggered riots among Albanians and collapse of the state. The country entered the state of complete chaos and borderline civil war. All progress achieved up that moment was destroyed in the matter of 4 months.

The aftermath of March 1997, was continuous recovery programs and generous funds to help Albania recover.

Chapter II - The role of International Organizations in Economic Development

International organizations are important actors in the critical episodes of international politics, with power in mediation, dispute resolution, peacekeeping, applying sanctions and others. They also help in managing various key areas of international concern, from global health policy to the monetary policies around the world⁴.

An international organizations may be defined as an institutionalized arrangement among members of an international system to solve tasks which have evolved from systemic conditions. The organization therefore reflects the attributes, aspirations and preoccupations of its members.⁵

Over the last decades, international organizations have elongated and amended their mandates and objectives, achieving global coverage through the number of members. This way, they were also subject to criticism for speeding up the globalization, non-fulfilment of their missions or superficial supervision and liberalization of international trade by providing the framework for the negotiations and formalizing trade agreements⁶

⁴ (Abbott and Snidal, 1998)

⁵ International organizations and systems – wolfram f. Hanrieder 1966

⁶ Zohal, H., What Determines Trust in International Organizations? An Empirical Analysis for the IMF, the World Bank and the WTO, MPRA Paper No. 34550, 2011

However, states still rely on International Organizations, as a mechanism for cooperation. A few issues are raised by their structure and tasks, and furthermore by global relations hypotheses including these intricate cases. The autonomy of these organizations relies upon states, since they can constrain or broaden their self-governance, meddling in their movement, rebuild or break them down. There are times when they come into conflict with the state when they make new structures for controlling trans-border connections.

One of the main reasons for States to set up, or participate in, an international organization is to delegate authority on matters which require expertise, knowledge, information, time and resources they themselves do not readily have at their disposal⁷.

⁷ Jan Wouters, Philip De Man - INTERNATIONAL ORGANIZATIONS AS LAW-MAKERS (March 2009)

2.1 The European Union

The late 80s and early 90s was a time of change all over the world, in Europe and certainly in Albania too. End of the Cold War, Reunification of Germany, political changes in European Eastern countries. Political change was inevitable for Albania too (as explained in chapter I)

In 1991, Albania was poor, had a weak democracy and people were fleeing the country to find better life conditions elsewhere. This was the year when a diplomatic relationship between the European Economic Community and Albania was established. In May 1992, Albania signed the Trade and Co-operation Agreement with the European Economic Community. From this moment, Albania was eligible for the PHARE program. Poland and Hungary: Assistance for restructuring their Economies, as the name itself implies, this program was original set up in December 1989 to provide economic support to the emerging Polish and Hungarian democracies. In September 1990 it was expanded to include Bulgaria, the Czech and Slovak Republics, the German Democratic Republic, Romania and Yugoslavia.

Prior to IPA (Instrument for Pre-Accession), PHARE⁸ was the main means of pre-accession assistance to EU candidate countries. The main purpose of this program

⁸ European Union website

was to support the candidate countries in the process of adopting and implementing the acquis and preparing these countries for the administration of Structural Funds. With this in mind, this program focused on two priorities:

- Institution building;
- Investment financing.

Support for civil society is not a novelty for European Commission policy in general or the enlargement policy in particular. The first experience with this support dates back to enlargement policies for the former communist countries in Central and Eastern Europe, which were addressed with the instrument PHARE. This program developed the idea of the PHARE Partnership Program (PPP)⁹. The idea behind this program was the development of civil society in the former communist countries, as an important part of consolidating democracy. Within this framework, the empowerment of citizens in the political life of the country, in the decision-making process and in general in the conditions in which they lived, is considered an important step towards a consolidated democratic political culture. In this respect, the development of Non-Governmental Organizations is considered an essential indicator with an important contribution to the creation of a democratic political culture. Integration of civil society was also considered a way for countries to effectively meet the Copenhagen criteria for EU membership.

⁹ Enika Abazi - Perspektivat dhe Sfidat e Integritit të Shqipërisë në Bashkimin Europian (2013)

At the time, Albania needed exclusive international assistance as it remained the poorest country in Europe and for almost fifty years had experienced only the power of one party system, and one of the toughest regimes in all communist Europe. The communist regime had totally isolated the country and terminated the western-educated intellectuals or dissidents¹⁰.

The PPP has also served to help build partnerships between the European Union and the Balkan countries and establish co-operation networks between Non-Governmental Organizations, seen as an important mechanism for transferring European Union knowledge and experience to help the reform and integration process. The philosophy behind this financial and technical assistance is to build legitimacy and moral support for political reform and decision-making, as well as to encourage Western learning processes on a variety of issues.

Through the PHARE programs from 1991 to 2000, the EU provided about 694 mln of euros to Albania¹¹. These EU funds were managed by the Commissions' Directorate General (DG) for External Relations. The following table provides yearly figures for the course of PHARE funding from the EU to Albania.

¹⁰ Freedom House, "Albania: Freedom in the World 2001,"

¹¹ Hoffmann, Judith, "Integrating Albania: The role of the European Union in the democratization process,"
Bogdani, Mirela & Loughlin, John, Albania and the European Union: The tumultuous journey toward EU integration,

TYPE OF PHARE ASSISTANCE	1991	1992	1993	1994	1995	1996	1997	1998	1999	TOTAL 1991-99	2000*	TOTAL 91-2000*
PHARE NATIONAL PROGRAMMES												
Agriculture		15.0	10.0	3.0		1.7	6.0	6.3	5.2	49.2		
Infrastructure (1)		4.4		1.0	18.4	17.0	7.0	8.0	5.5	63.3		
Private Sector Development (2)		3.3	7.6	1.0	2.0					14.9		
Health			6.0	7.0						13.0		
Water and Environment			3.3			1.5	6.7	2.5	11.6	26.6		
Education (incl. TEMPUS)		1.2	2.5	2.4	4.2	2.5	2.3	0.7	1.6	17.6		
Local Community Development					8.5		5.0	3.0	7.1	23.1		
Public Administration Reform (3)		1.8	1.2	0.8	1.0	1.4	6.3	8.9	11.4	43.7		
Approximation of Legislation				0.3						0.3		
Aid Coordination (4)				0.5		1.7		1.1	2.0	5.3		
Financial Sector and Audit							0.3		0.1	0.4		
TOTAL Phare National Programmes		25.0	30.3	22.3	35.3	31.0	24.0	26.5	45.0	200.0	26.0	290.0
PHARE CROSS-BORDER PROGR.				20.0	19.3	24.0	29.0	12.0	14.0	104.0	40.0	144.0
OSCE ELECTION SUPPORT							1.8			1.8		1.8
BALANCE OF PAYMENTS SUPPORT		36.0	35.3		36.3					107.6		107.6
SPECIAL BUDGETARY ASSISTANCE							14.9			14.9		14.9
ASSISTANCE IN FAVOUR OF KOSOVO REFUGEES									62.0	62.0		62.0
PHARE HUMANITARIAN AID	10.0	40.0	10.3	7.0						77.3		77.3
OVERALL PHARE ASSISTANCE	10.0	110.0	75.3	49.0	85.0	61.0	70.4	42.5	121.5	619.4	75.0	694.4

Figure 2.1 Overall PHARE Assistance in Albania, 1991 - 2000 (milliom Euros)

Source: REPORT FROM THE COMMISSION On the feasibility of negotiating a Stabilisation and Association Agreement with Albania, 1999

Starting in 1991, the EU facilitated Albania through other institutions such as Humanitarian Aid, Food Security, OSCE and European Investment Bank to support S&A Process. The main areas supported by these EU aid programs are:

A) Institutional reform, which includes strengthening democratic and citizenship practices, restructuring the judicial system, creating an active civil service,

collecting key revenues for the state, training police officers and promoting the educational system.

B) Development of infrastructure, which includes constructing ports and roads, improving water supply and dispersion, building a much better working environment for the public services and protecting the environment.

C) Food relief and food safety, in assisting the democratic government cope with the transition, from 1991 to 1992, the EU provide Albania with food aid in an amount of 120 million euros. Food security programs were created to support Albanian structural regulations based on food safety.

D) Micro-economic support provided to Albania in three various procedures, loans through the European Investment Bank, budgetary assistance and fund to the balance of payments¹².

In 2000, the EU created a new financial program called “Community Assistance Reconstruction Development and Stabilization” (CARDS) for the Western Balkan countries, including Albania, in order to enable the aspiring countries of the region to participate in the Stabilization and Association Process¹³. CARDS intended to bring a more effective approach to the EU assistance by financing the mechanisms and purposes of the SAP, by providing greater financial resources assigned to the aspiring Balkan countries

¹² European Commission Archives, “Albania- A Future with Europe,”

¹³ Europa, “The CARDS Programme (2000-2006),”

and by shifting the main areas of funding. It focused on the development of the institutions and reforms that are fundamentally required on the SAP. The EU requires effective implementation of the SAA as a prerequisite for any further evaluation of an aspiring Balkan state's prospect of accession. A major part of the CARDS programme focused on support for the judicial system and the police – construction and renovation of courts, police and justice assistance missions (PAMECA and EURALIUS, respectively), border management etc. Particular attention was dedicated also to the effective functioning of the customs service which was a necessity not only as regards the fight against trafficking and organized crime, but also in view of Albania's improved prospects to conclude the SAA and focus increased resources for the implementation of the Interim Agreement. Concerns over the functioning of the market economy and support to business and investment environment represented an additional intervention area of the CARDS programme (support in taxation, European standards such as standardisation, certification and inspection, metrology, veterinary and phytosanitary inspection etc.). Additional support was provided also to consolidate democracy and the development of civil society, rural development, community awareness and involvement of local communities in decision-making, higher education, vocational education and training, as well as a number of other problematic areas.

Through the CARDS assistance, which was effective until 2006, the EU invested a total of 4.65 billion euros in the development of the Western Balkan

countries; concentrating mainly on the subjects that respected the principals of democracy, rule of law, human and minority rights, fundamental freedoms and the application of democratic, economic and institutional reforms¹⁴.

As each country shows more progress toward the accession process, EU assistance focuses more on supporting the institution building and reforms needed to implement the membership requirements of the Stabilization and Association Agreement. There are precondition requirement specified in Article 5 of the CARDS program that a county must meet in order to be eligible for EU assistance. In 2001, Albania became eligible for the EU's CARDS financial assistance¹⁵, where for the period 2001-2006 the country received 282 million euros.¹⁶ The EU's assistance to Albania under the SAP was conditional on further development in meeting the Copenhagen political criteria and showing progress in respecting key areas specified under the European Partnership with Albania. Failure to meet these conditions could make the EU restrict its financial support in Albania. The 2001 Albania Country Strategy Paper (CSP) shows a strategic framework of the EU's fund provided to Albania through the CARDS assistance program. There are five major areas where the EU allocated its assistance¹⁷:

¹⁴ Europa, "The CARDS Programme (2000-2006),

¹⁵ European Commission, 2001, "Albania Country Strategy Paper, 2002-2006,"

¹⁶ European Commission, 2005, "Albania 2005 Progress Report,"

¹⁷ European Commission – European Community CARDS Programme Albania Country Strategy Paper 2002 - 2006

Justice and Home Affairs - CARDS assistance has been amongst the most significant in the overall external assistance provided. Assistance to institutional and capacity building includes actions aimed to strengthen the performance and independence of key judicial institutions such the High Council of Justice (CJ), School of Magistrate and General Prosecution Office; strengthen the capacities of executive bodies responsible for implementation of the judicial reform such as Ministry of Justice (MoJ); enforcement system and establishment of new system of juvenile justice. In addition, assistance has been focusing on supporting enhancement of the judicial system in commercial matters that contribute to overall improvement of the investment climate. Other interventions include support for establishment of court for serious crimes and strengthening the penitentiary system. A large amount of support has been provided to improvement of infrastructures in judiciary with investments in the court buildings and pre-detention centres.

Administrative Capacity Building - CARDS allocated assistance within Administrative Capacity Building for horizontal public administration reform projects, and vertical reform projects. The horizontal group concerns projects involving the overall administrative capacity building and reforms at central and local level administrations such as public administration reform, civil service reform, European Integration and decentralisation. The vertical acquis group includes projects addressing the implementation of the acquis in areas such as statistics, procurement, state aid, internal and external financial control.

Economic and Social Development - Rebounding from the financial collapse of 1997, Albania has sustained high rates of economic growth. Economic activity recovered and real Gross Domestic Product (GDP) growth rates accelerated to an average annual rate of 7 % over the period from 1999-2005, allowing Albania's per capita GDP to approach the average for middle income country levels.

Since its transition, Albania's growth has been driven primarily by improvements in the allocation of resources from low-productivity sectors, firms and activities (e.g. subsistence agriculture) to high-productivity ones (e.g. export manufacturing). Future challenges include support to a fair business environment to promote SME development, exports and Foreign Direct Investment (FDI), and to build consumer protection systems. CARDS assistance to economic development has been concentrated in three main components; (i) support to strengthening quality infrastructure systems, focusing on standards, certification, accreditation, market surveillance, food safety; (ii) trade regulation and investment promotion; and (iii) community development, focusing mainly on small-scale rural infrastructure investments. Allocations of CARDS 2005 and 2006 have decreased to almost half of the contributions of 2001-2003. This is due to a decrease in allocations for "local community development programmes", which received around 60 % of funds supporting economic development.

Environment and Natural Resources - The CARDS projects within the environmental sector have been either in the form of major technical assistance projects mainly targeting MEFWA, or in the form of clean-up of environmental hot spots. The vision has been to act as a catalyst for additional funding from International Financial Institutions (IFIs) such as the European Investment Bank (EIB), the European Bank for Reconstruction and Development (EBRD), the World Bank (WB), or other bilateral funding. CARDS has, in total, supported ²³ projects within the environmental sector during 2002-2006: Nine of these projects were major projects while the others were preparatory projects¹⁴. Emphasis in the evaluation of this sector is placed on the major technical assistance projects where the Ministry of Environment, Forests and Water Administration (MEFWA) has been the main beneficiary. Additional comments and recommendations are made concerning the hot spot projects. Altogether seven environmental projects have formed the basis for the assessment.

Civil Society Development - Support to CSOs has a very limited role in CARDS and was mostly directed towards supporting service delivery or establishing a national CS register. The projects assessed in this chapter were funded through CARDS grant scheme for CSOs, which provided support to 19 projects within a total budget of € 750,000 under CARDS 2001 and 2005, and which has recently approved 15 projects under CARDS 2006. Whereas CARDS 2001 focussed on civil society only, CARDS 2005 had three categories, CSO, Media and Gender, where

five projects within each category have been selected for support. The grants were within the range of € 30,000 to € 100,000 and were distributed through an application process undertaken by the European Commission Delegation (ECD) itself, albeit supported by experts from Albanian think tanks.

Macro Sector	Sub-sector/ Cluster	Projects evaluated			Total CARDS M€
		Interviews/ Desk	Survey	CARDS M€	
Justice and Home Affairs	Justice	8	2	18.62	121.00
	Asylum and Border management	6	1	18.20	
Administrative Ca- pacity Building	Public Administration Reform (PAR) (hor- izontal and vertical)	7	5	15.75	47.10
Economic and So- cial Development	Economic Development/Internal Market	6	7	27.00	88.50
	Education (Vocational Education and Train- ing)	5	2	10.40	
Environment and Natural Resources	Environment	5	2	14.18	36.00
Civil Society Devel- opment	Civil Society Development	3	3	6.90	8.50
Other		-	-	-	3.2
In total		40	22	111.05	282.10^a

Figure 2.2 Allocation of CARDS funds according to macro-sectors

Source ICOWI Ad Hoc Evaluation of the CARDS Programmes in Albania,

The performance of CARDS assistance has overall performed better in acquis related areas than in public administration reform. The overall performance of the CARDS assistance has been acceptable and has met strategic objectives of the key CARDS strategic documents, but project design has been weak in some sectors, in

particular in public administration reform due to, among others, a lack of sector strategies and in-depth needs assessments. CARDS has experienced delays in implementation and limited capacity for planning of assistance programmes as well as capacity for implementation. Results and outputs have been observed in many of the sectors/clusters evaluated. There have been important effects of CARDS in terms of development and strengthening of institutional and legal framework, and development of strategies in sectors such as border management, economic development and justice. The key concern with regard to CARDS assistance delivered is, however, the medium to longer-term impact and potential sustainability as the capacity of the Albanian administration varies in sectors. Human resource development and turnover in staff pose significant problems for creating an effective administration. The overall rating is moderately satisfactory. The new financial perspective for the period between 2007 and 2013 of the European Union outlined a new assistance programme for candidate and potential candidate countries – the Instrument for Pre-accession Assistance (IPA) – which entered into force in January 2007.

The IPA consists of five components: (I) Transition Assistance and Institution Building, (II) Cross-Border Cooperation, (III) Regional Development, (IV) Human Resources Development, and (V) Rural Development. Only candidate countries can benefit from all five components of the IPA programme while potential candidate countries (such as Albania) benefited from the first two components only.

The overall objective of EU financial assistance to Albania is to support its efforts to carry out reforms in line with EU law, with the aim of fully preparing the country to assume the obligations of EU membership. .

The Multi-annual Indicative Planning Document (MIPD) for the period 2011-13 set out the main EU assistance objectives for the country. The MIPD was based on the needs identified in the European Partnership with Albania and those identified in the Commission Opinion 2010 on Albania's application for EU membership. The MIPD also took into account Albania's strategies, in particular the National Strategy for Development and Integration (NSDI) 2007-2013, as well as the National Plan for the Implementation of the SAA 2010-2014.

The IPA 2013¹⁸ National Program for Albania was based on the main objectives of the Multi-annual Indicative Planning Document (MIPD) 2011-2013, which were:

- Strengthening the rule of law, guaranteeing the independence, efficiency and accountability of judicial institutions and enhancing the fight against organized crime.
- Supporting public administration reform, with the aim of enhancing its professionalism and de-politicization, strengthening the merit-based transparent approach to appointments and promotion, and strengthening the fight against corruption at all levels.

¹⁸ Plani i detajuar për menaxhimin e decentralizuar të fondeve të BE-së”

- Strengthen and protect human rights, especially for women, children and the Roma minority, and implement effective anti-discrimination policies.
- Supporting issues related to the acquis, in particular administrative capacity, adoption and enforcement of legislation, as well as investments in the field of transport, the social field and the environment and agriculture.

In 2014, Albania was officially nominated a Candidate Country to adhere the European Union. From this day, Albania was eligible for the IPA II funds, meaning that she could benefit from all 5 IPA components: (I) Transition Assistance and Institution Building, (II) Cross-Border Cooperation, (III) Regional Development, (IV) Human Resources Development, and (V) Rural Development.

2.2 World Bank

The World Bank is involved in the creation and implementation of reforms through advisory policies, lending and technical assistance. From the very beginning, her actions, together with those of the International Monetary Fund, they aimed at succeeding at three basic objectives:

liberalize the economy, price system, exchange rate and trading regimes, as well and promote private sector initiative, fair competition and market discipline.

achieve stabilization of macroeconomics through fiscal and monetary policies, which aimed at ensuring a sustainable balance budgetary and external sector.

create institutions and markets, through structural reforms in the areas of tax administration, privatization, breaking the monopolies, legal reforms to property and property, banking and social security network adjustments for it protect the poor.

In the early years, both by the government and the World Bank, the main focus was on the first two objectives.

By the time Albania joined the WB in 1991, the country was in a deep crisis. Assistance was needed throughout all sectors. In this context, humanitarian assistance was an urgent priority - food aid, medical support was key - along with macroeconomic stabilization.

Foreign assistance was massive. In five years, from 1992 until 1996, Albania received about 1,525 billion¹⁹ US dollars in total aid or about 475 US dollars per capita, most of which was an official gift (about 68 %)

Due to the outdated infrastructure of Albania, loans IDA data focused on the most pressing infrastructure rehabilitation needs. Transportation and the energy sector were identified as key priorities. Most of the World Bank's commitments, about 21 percent, concentrated in the transport sector. Project for transport and projects for national roads and rural roads aim to improve national road conditions and rural and impose policy market oriented reforms on these sectors. Given the institutional weaknesses in both production and distribution sectors, energy has been and continues to be one of the key priorities of program of the World Bank. In 1993, credit for imports critically funded the immediate adjustments of the HPP over the Drin River. In addition, projects on loss reduction energy and transmission and energy sharing have intended to reduce very large technical losses and non-technical energy, as well as inefficient use of electricity. The second largest sector, accounting for 19 percent of total commitments, was the agricultural sector to which the World Bank intervened with six loans, including loans for renewal of the agricultural sector, rehabilitation project of irrigation system and project for development of agricultural processes. The most successful project was the one on

¹⁹ Banka e Shqiperise – Shqiperia dhe Anetaresimi i saj ne Banken Boterore , 2001

rural development and the pilot program for poverty alleviation in rural areas, which introduced new mechanisms for small loans for farmers. A special support to the strategy has been given to agrarian reforms, which also aimed to develop the market of land farming. All state cooperatives were dissolved and about 450,000 farms were created with an average size of 1.1 hectare.

Macroeconomic indicators deteriorated considerably in the second half of 1996. The fiscal deficit reached 10.5²⁰ percent of GDP. Inflation accelerated and the local currency depreciated. In this already unfavourable macroeconomic climate erupted the crisis of pyramid firms. The situation of the immediate growth of pyramid schemes was not unique to Albania, yet nowhere else resulted in a catastrophic decline of civil order, as in Albania. The schemes, in part, emerged because of one backlog in the banking system, as no legitimate bank would be able to offer interests comparable to those provided by the companies operating the schemes. The general lack of the public's familiarity with financial matters, too, contributed to the development of the schemes. Initially, the real danger of the phenomenon was even underestimated by the Monetary Fund International and World Bank, which initially treated these companies as part of the informal market. As the schemes gained much popularity, concern began to be expressed especially from the Bank of Albania. In the middle of in 1996, the Governor of the Bank of Albania opposed

²⁰ Banka e Shqiperise – Shqiperia dhe Anetaresimi I saj ne Banken Boterore , 2001

forcedly in relation to the danger that lurked by the schemes and incited the government and the force of law to close them. From October 1996, under the strong pressure of the Bank of Albania and the Monetary Fund Internationally, the Albanian Government agreed to denounce publicly the risk of schemes, but then it was too late. At the beginning of 1997, all schemes were blocked, leading to the spread of civil disorder.

The level of pyramid schemes, compared to the size of the economy Albanian was unforeseen. It is estimated that over 65 percent of the Albanian population had put savings in these misleading companies. The economic cost of bankruptcy proved to be very high in terms of loss of assets, destruction of infrastructure and private property, lack of trust in institutions and severe macroeconomic imbalances. In In 1997, GDP fell by about 7 percent, inflation accelerated to over 40²¹ percent and the fiscal deficit reached 14 percent of GDP. External balances deteriorated, foreigners' assistance was entirely divided and there was a sharp refusal to capital inflow from outside. In such circumstances, the re-establishment of economic stability, in particular fiscal recovery was a key. Another advantage was the implementation of banking laws and prudential regulation. Once conditions in Albania stabilized, accompanied by the intervention of an international law

²¹ Banka e Shqiperise – Shqiperia dhe Anetaresimi I saj ne Banken Boterore , 2001

enforcement force, the World Bank adopted in July 1997 a Coverage Program to help to turn the country into a development road.

By the 2000s, the macroeconomic situation in Albania was more stable, therefore the country could begin to put more emphasis on addressing issues related to poverty and economic growth in a structured way. Also in 2000, the Albanian government prepared the Growth and Poverty Reduction Strategy, which was assisted also by the World Bank. This strategy was not only a multi-sectoral approach to the reduction of poverty and to economic growth but was also a presentation of the long-term vision of the EU integration of Albania. This strategy was based on two main pillars: improved governance and strong economic growth. Such strategy helped sustaining high rates of economic growth and pursuing structural reforms.

The Country Assistance Strategy (CAS) by the World Bank for the period 2003-2005 made available made approximately US \$ 130 million. The implementation of this program achieved major progress overall and especially in the privatization, trade liberalization and the building of a sound financial sector. By the mid-2000, things had gained momentum .Growth continued at a steady pace as the institutional basis was consolidated and Albania was showing sound macroeconomic performance. The 2006-2009 CAS raised the bar and became more demanding with future achievements. This new CAS program focused on two pillars: continued economic growth through support to private sector development and improving the

delivery of public services, particularly in the social sectors. By the end of 2008, Albania benefited more than US \$ 170 million under the CAS with the realization of different projects in land management and business regulations, improvements in transport, community and agricultural infrastructure and municipal water supply service.

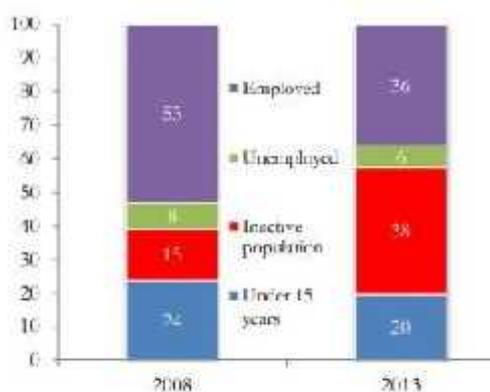
From 2010, the World Bank set up a new assistance framework, which is the Country Partnership Strategy for Albania (CPS) and has as priorities better governance through institutional development, transparency and efficiency, private sector development for growth and poverty reduction and human development.

Post 2008, unemployment and economic inactivity were also associated with lower Socio-economic status. Not only did inactivity rates double post-2008, but also poverty rates were also significantly higher among the inactive. From 15 percent in 2008, inactivity rates reached 38²² percent in 2013. Inactivity among women increased significantly during the crisis period. The decline was largest among young women (15-34 years age), with around 7 percent decline in labor force participation rate between 2007-2010. Individuals living in households in which the heads were active (either employed or self-employed) or retired were less likely to be poor than individuals living in households in which the heads were unemployed or inactive. Among households in the bottom 40, for instance, 20 percent of

²² World Bank Group - Country Partnership Framework For Albania For The Period Fy15 – Fy19

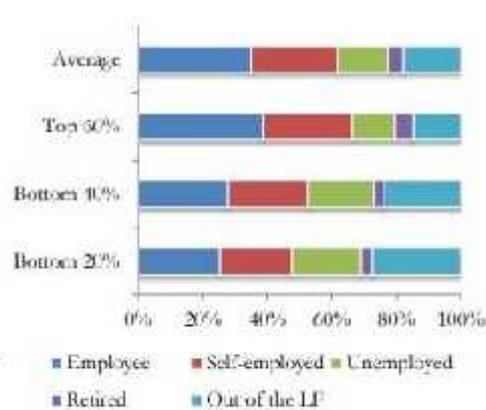
working-age members were in unemployment, and 24 percent were out of the labor force, compared with 13 percent and 15 percent, respectively, in the top 60 percent of the income distribution (the top 60). In 2012, the incidence of poverty was 11 percent among households headed by employed persons, 13 percent among households headed by retired persons, 22 percent among households headed by unemployed persons, and 24 percent among households headed by inactive persons. The profile of the less well-off thus shows a higher share of household heads in unemployment and inactivity between the bottom 20 and bottom 40.

Figure 1: Population Structure by labor status, (percent), 2008 and 2013



Source: INSTAT

Figure 2: Labor force status, household heads, 2012



Source: World Bank analysis based on LSMS 2012 data

Figure2.3

Source World Bank Group - Country Partnership Framework For Albania For The Period Fy15 – Fy19

The June 2013 elections opened a new opportunity for engagement in Albania on its medium-term macro-economic and structural reforms. The new coalition government with a strong parliamentary majority assumed office in September 2013. This reform-minded Government moved energetically to tackle a long overdue reform agenda, beginning with fiscal consolidation and public financial management, including eliminating arrears over time, as well as addressing structural challenges in pensions and energy sectors. The new government at that time, engaged in the preparation of the National Strategy for the Development and the Integration for 2015-2020, and WB contributed to the preparation of this Strategy. At the same time, the WB prepared its Country Partnership Framework to support Albania with her aspiration to integrate in the EU and to achieve equitable growth but simultaneously advancing progress toward the twin goals of reducing poverty and increasing shared prosperity. The CPF²³ is built around 5 fundamental priorities:

Restoring fiscal sustainability and maintaining financial stability – this is an area of WBG comparative advantage and long-standing engagement, where WBG brings established macro-fiscal analysis and a well-defined division of labor with the IMF. With championship from the highest level of Government to tackle longstanding

²³ The World Bank Group – Country Partnership Framework for Albania FY2015 – FY2019

imbalances, the WBG has an unprecedented opportunity to support reform in this area.

Establishing a high quality business environment – the WBG engagement in Albania reflects a global comparative advantage in this area (most visible through the Doing Business Report) as well successful WBG engagement in neighboring Balkan countries. WBG engagement exploits complementarity of the IBRD and IFC, building on an ongoing Trade and Competitiveness advisory engagement. It brings WBG expertise in assisting the Government to pursue legal and regulatory reforms aimed at improving the business environment and investment climate. The IFC engagement will also provide technical assistance in legal and regulatory reform in investment policy aiming to increase FDIs and investment in agribusiness given the sector's contribution to GDP and impact on employment. The Ministry of Economic Development has been given a leadership role in this crosscutting area, and is an effective champion and focal point for deepening reform in this area.

Providing clean, efficient, equitable and financially sustainable energy – the WBG will maintain a high level of engagement while applying lessons learned from its past engagement in the energy sector in Albania. WBG will engage in large operations expected to support a transformative turnaround in energy sector performance, The Government has already begun waging a high-profile campaign to improve power sector performance. IFC will support indirect finance through the banking sector for smaller renewable energy projects and through advisory work to

government, financial institutions and companies working in renewable energy. The full combined force of IBRD, IFC and MIGA was brought to bear on the reform and investment needs of the sector. WBG engagement also leverages resources from other partners such as the EBRD and EU.

Formalizing and enhancing inclusiveness and sustainability of land markets – the WBG is generally recognized as the lead partner for land administration reforms in the Western Balkans, including Albania, where the WBG’s earlier engagement has produced improved regulatory regimes and measurable results on land registration and management. The WBG also has a successful record of accomplishment in supporting environmental clean-up and land management in Albania, with important linkages to sustainable coastal tourism.

Enhancing governance, transparency and accountability of government – the WBG has a comparative advantage among international partners in supporting social services and public services’ governance reforms related to public service delivery, and has a strong body of analytic work including Public Finance Reviews to underpin such efforts. Government has made the strongest commitment at its highest levels to transform the relationship between citizens and Government, and has adopted a “science of delivery” approach. The WBG has the ability to support this science of delivery approach as it applies to deep reforms in public service delivery.

The above-mentioned priorities are grouped in three focus areas as depicted in the figure below.

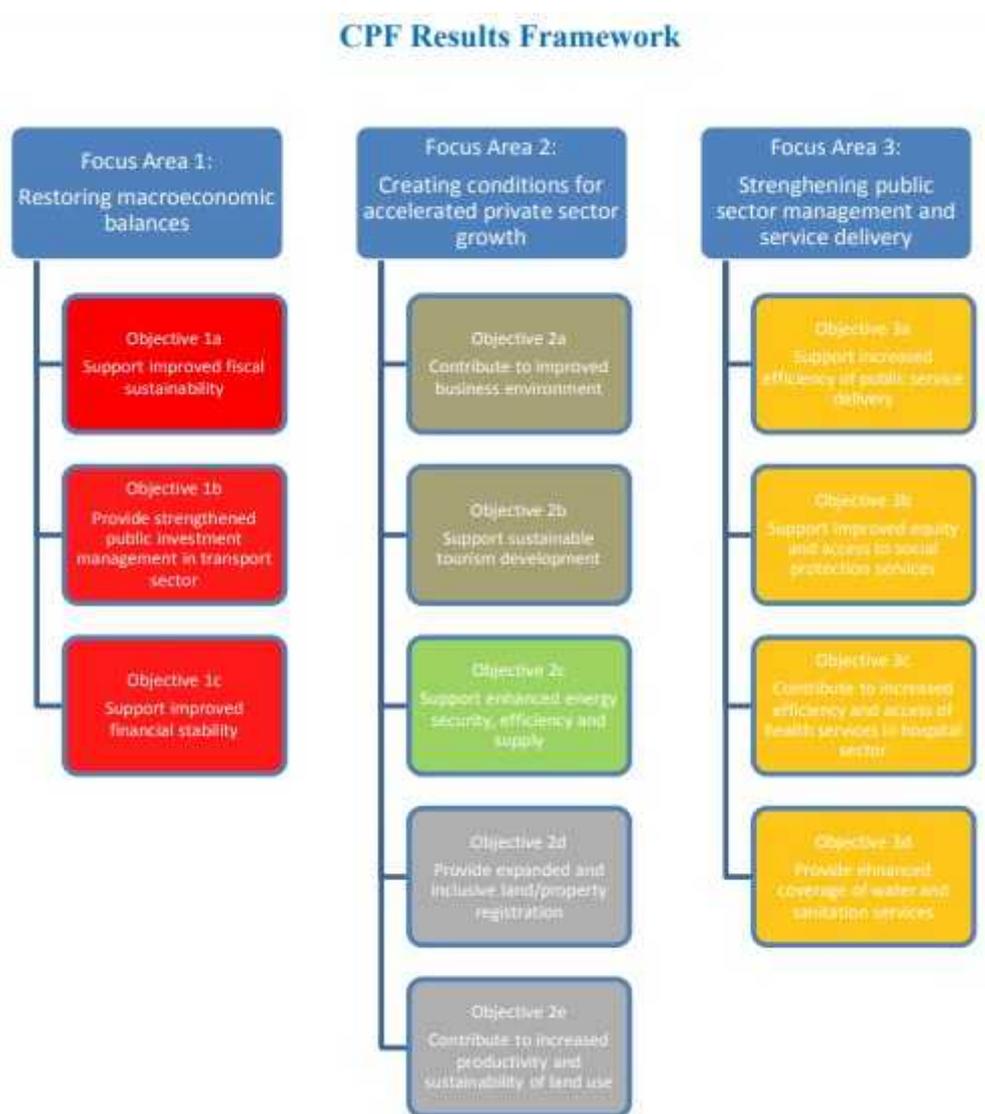


Figure 2.4 Country Partnership Framework Focus Areas and Objectives

Source The World Bank Group – Country Partnership Framework for Albania
FY2015 – FY2019

IBRD indicative financing up to US\$1.2 billion is proposed in support of the FY15-FY19 CPF program with significant front loading in the initial period keeping pace with Government reform and subject to exceptional progress on the reform program, country demand and IBRD's financial capacity. Under this assumption, up to forty percent of the indicative lending is expected to take the form of budget support subject to continued satisfactory performance on the agreed macro-fiscal framework.

FY	PROJECT	IBRD (US\$ million)
FY15	Albania Health System Improvement	40
	Road Safety and Maintenance	80
	Policy Based Guarantee (PBG)	220
	Power Sector Recovery Project	150
	Sub-total FY15	490
FY16	Citizen Centric Service Delivery	32
	Integrated Land Management	45
	Coastal Regeneration & Sustainable Tourism	53
	Financial Sector Development Policy Loan	100
	Sub-total FY16	230
FY17	Sub-National Finance and Governance	
	Competitiveness and Jobs DPL	
	SAMP Additional Financing	
Sub-total FY17	180	
FY18	Energy Sector Development	
	Skills & Employment	
	Development Policy Loan	
Sub-total FY18	200	
FY19	Transport Reform	
	Development Policy Loan	
Sub-total FY19	120	
TOTAL		1,220¹²

Figure 2.5 CPF Indicative IBDR Lendind Program FY15-19

Source The World Bank Group – Country Partnership Framework for Albania
FY2015 – FY2019

2.3 International Monetary Fund

The fall of the Berlin Wall in 1989, and the dissolution of the Soviet Union had transformed the International Monetary Fund into a universal institution. Places of sapodals from isolationist and totalitarian systems would soon become part of this international institution; the flood of membership was as intense as they were the problems that emerged. The transition from a system of centralized economy to that of Free trade and entrepreneurship were not easy to afford in Europe East and Southeast, including Albania.

On October 15, 1991, Albania became a member of the Monetary Fund International.²⁴ Alongside important political developments such as overthrowing the system communist and the development of pluralistic and democratic free elections that would bring one a government with new Western aspirations and ideals, the country would face changes important in terms of economic development. With his supervisory methods, advisory and financing, the IMF would help this new member stay in feet, but could not prevent the obstacles that would appear before nor the consequences and long-term negative impact for the common people and the economy of the country.

Membership in the International Monetary Fund would not be converted into a loan account with this institution. This meant that Albania was already able to refine its

²⁴ International Monetary Fund,, Toward a Global Monetary System, ANNUAL REPORT of the Executive Board for the Financial Year Ended April 30, 1992 Washington, D.C.

crisis and development strategies, aid programs, investment programs, foreign investment absorption programs and advanced technology. This meant that Albania could start implementing reforms in the economic, social and institutional fields, and could launch the opening and liberalization processes with the sole purpose of securing democracy building and economic development aiming at the long term. integration into Euro-Atlantic structures. Such an agreement would bring many benefits to Albania, benefits that would be realized over the years by the support of various WB and IMF projects.

The Albanian government, with the assistance of the International Monetary Fund, prepared a two-tiered banking system that would be operated by central bank and commercial banking laws. Under the banking system bills, the National Bank of Albania, the reorganized version of the State Bank of Albania, would issue and manage the national currency as well as oversee lending policies. The Central Bank would also manage the foreign currency reserve, act as a fiscal agent for the government and license other banks that could operate in Albania.

The agreement with the IMF states that the three specific points that Albania should focus on, that will be the core of any economic reform were: 1 changing the production structure and price structure in the economy, 2 changing the relations

that Albania there is in the outside world, 3 the creation of a financial network, which will allow the implementation of this reform without inflation.²⁵

The changes that occurred in the Albanian economy in 1991-1996 are based on the process of changing the form of ownership, through the rebirth and expansion of private property, through the process of privatization. The main characteristic of the transition would be the privatization of many sectors of the economy. This process would last almost throughout the 1990s and beyond, where they were privatized and important sectors of the economy. So until 1996 the state focused on:

1. Privatization of the land, which was done based on law no. 7501 - On Land - according to which the farmland was distributed to the peasants based on the number of family members and availability in any agricultural cooperative. In spite of the problems and objections, the law was implemented to some extent in order.
2. The privatization of wholesale and retail units, a process that gave property to only sellers, even at a very low price, bringing privileges only to one social group and even denying the rights that landowners could have over which were these objects.
3. Privatization of state apartments by those who resided in these apartments.
4. Privatization of small and medium-sized enterprises

²⁵ Albanian Archive – Year 1992, Folder 202

The Albanian economy during this period is described as a large informal sector where governance and knowledge in this sector was lacking, tax collection difficulties, poor public services, low incomes and low spending, all of which turn it into a vicious cycle with many consequences.²⁶ Certainly all of these reasons e made Albania a lonely and open country to the unknown and negative things in democracy.

Macroeconomic intervention attempts in terms of fiscal and budgetary control, tight monetary policy tried to prevent the immediate and rapid growth of spending. A taxation system was installed to create and provide a necessary source of revenue for the budget. The price liberalization process also extended to foreign trade, creating opportunities for Albania's integration into the world economy. The traditional state monopoly on foreign trade was abolished. There was no quantitative restriction on imports anymore, since licenses and all export taxes were abolished in 1994.

As a country unencumbered by the concept of free trade, at a time when the transition process had just begun, underdeveloped and fresh from isolation and collectivist society, Albania needed a policy orientation, technical assistance, consultations and financial support from foreign bodies. Membership as a new country in the International Monetary Fund, as well as the policy of opening up to

²⁶ Jan-Peter Olters, *Albanian Informal Economy: An Impediment to Economic Development* 2001

neighboring countries and beyond, would facilitate and somewhat simplify the way up to the emergence of new problems that would result in the 1997 crisis.

The events of the 1997 financial and political crisis in Albania forced the International Monetary Fund to terminate its mission in Albania for a while.

However, in a press release in November 1997²⁷, the IMF states that: in the aftermath of the riots, the IMF approved the Post-Conflict Emergency Assistance (EPCA) loan to Albania for emergency support in the amount of \$ 12 million, which would help Albania to come out of the financial crisis of 1997. This would be a very necessary help for Albania which was devastated by the economy. The IMF would try to help the country emerge from the crisis and recover the macroeconomic dimension, and would enable the 1997-98 economic program to be realized. The focus of the program was on the need for an immediate decline in inflation and boosting economic growth. The main objectives were to limit the fall in real GDP (8% in 1997) and increase it to 12% in 1998, maintain the annual inflation rate at 51-54% in 1997 and reduce it to 15 -20% for 1998 as well as maintaining international reserves over the equivalent of 3.5 months of imports for 1998.²⁸

The report of the IMF for the macroeconomic objectives²⁹ for 1998 were:

²⁷ IMF Approves Emergency Post Conflict Assistance for Albania, IMF Press Release No 97/51, Washington: 1997

²⁸ IMF Approves Emergency Post Conflict Assistance for Albania

²⁹ IMF Approves Emergency Post Conflict Assistance for Albania

(1) to limit the real GDP decline from 8 percent in 1997 to reach real growth of about 12 percent in 1998;

(2) achieve the maintenance of the annual rate of inflation from the range of 51 to 54 percent in 1997, to exceed 15 to 20 percent in 1998; and (3) maintain gross international reserves above the equivalent of 3.5 months of imports during 1998.

To achieve these objectives, fiscal policy will aim to limit the internally financed budget deficit to about 13 percent of GDP in 1997, and decrease to 10 percent of GDP in 1998. This will be done by seeing the resettlement and then improving tax collection; increase in tax rates, including a significant increase in the VAT rate; and exercising restraint on spending, including rationalizing the civil service.

These objectives were to be achieved through:

Structural reforms³⁰: Under the program the authorities are planning a wide range of structural reforms, including:

(i) progress in the privatization or liquidation of two of the three state-owned commercial banks;

(ii) the closure of the companies running the pyramid schemes;

(iii) civil service reform;

(iv) a resumption of enterprise privatization; and

(v) establishing a functioning agricultural land market.

³⁰ IMF Approves Emergency Post Conflict Assistance for Albania

Addressing Social Needs: The crisis has resulted in the impoverishment of the Albanian population. In the medium term, poverty alleviation will be based on achieving a high and sustainable growth driven by private sector development.

However, in the short term, targeted temporary support towards poorer families will be required. The government will therefore accelerate social assistance payments, and introduce public / community service schemes for social assistance recipients so they can work. Also, in the coming months, the government will address as a priority the shortages in pharmaceuticals, surgical goods and materials and equipment for public health services.

The second decade of the Albanian economic transition was characterized by the implementation of the Poverty Reduction Strategy, an idea proposed by the International Monetary Fund and the World Bank in 1999. This was also the attempt of international institutions in the context of poverty reduction strategies, designed to assist and economically, socially and politically orientate countries in need, members of these organizations. This strategy has been praised as a key tool for the International Monetary Fund and the World Bank, as well as other international donors, in delivering numerous technical assistance, consulting and lending packages. For the first time, the concept of participation and ownership was introduced, which means that the International Monetary Fund and the World Bank would not design a strategy for each country, but they put forward the initial idea of such an orientation, but would be leading governments in collaboration with local

government, civil society, and foreign donors and international partners who would make this possible. This would also serve as a guiding principle, because it is the local authorities, the ones who know the issues most deeply about their countries, and a strategy conceived by external authorities would not be able to help in depth. The International Monetary Fund and the World Bank would provide suggestions for drawing up and shaping the strategy framework in principle.

Albania's Poverty Reduction Strategy adopted in 2001 in the context of a broader IMF policy aimed at poverty reduction, through the assistance and economic, social and political orientation of countries in need that were members of the International Monetary Fund and the World Bank. Numerous efforts to implement this strategy during 2002, to expand it into a number of areas and sectors to increase participation, have gradually transformed it into a National Strategy for Socio- Economic Development. As negotiations on the Stabilization and Association Agreement began, the content of this strategy changed to one of key documentation for moving the country towards European integration.

In the analysis of the International Monetary Fund it is estimated that from 2002 to 2008 a number of objectives have been achieved. It has been estimated that although energy problems have been persistent, there has been economic growth as a result of easing policies in the key economic infrastructure sector, as a result of increased private and public investment, and a marked decrease and reduction of poverty, particularly between the years 2002-2005. But in parallel with this, the IMF report

points out that there is still a need for improvement in the public administration and governance sector. Moreover, spending on health and education has increased tremendously.

Concerning the strategy for 2007-2013, the analysis of the International Monetary Fund identifies as the strongest points the highest level of government accountability for the implementation of the strategy's objectives, greater involvement of civil society in policy implementation. public, better diagnosis for reduction of poverty, more ambitious plans for monitoring the overall effectiveness of public spending for Albania, removing barriers to private sector development, decentralization, and judicial reform. Parliament's involvement in the consultation process is also welcomed.

The three-year agreement with the International Monetary Fund was not renewed in 2009 because in the view of the Albanian government the economy was sufficiently stabilized to function without the need for continued monitoring by the International Monetary Fund. However, the 2009 world economic crisis may require further support from the International Monetary Fund for Albania. Despite the interest of the International Monetary Fund, the Albanian Government led by Mr. Sali Berisha was determined not to re-establish a financial relationship with this institution, considering the economic situation stable and no longer in transition, able to afford investment and walk on its feet. own. Although recent IMF

reports indicate a desire for co-operation and optimism for an efficient relationship, the Albanian authorities no longer wanted the IMF any longer and were looking forward to ending mandates to terminate them.

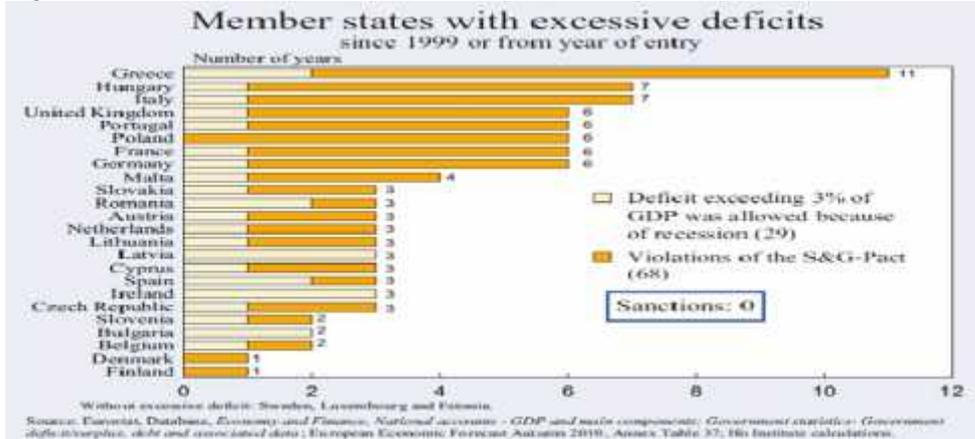
About 5 years after his departure, the Socialist government restored the International Monetary Fund to Albania. The parties announced the agreement was reached at a press conference, which gives the IMF a stronger role in overseeing the economy and public finances, against a \$ 300m loan.

Chapter III – Economic growth in the last decade

3.1 The effects of Financial crisis in Albania

The crisis we are experiencing in Europe in recent years is not direct result of what happened in the US and around the world for sub-prime loans, and derivatives, the toxic assets, the bankruptcy of Lehman Brothers, AIG, Fannie Mae and Freddie Mac. That crisis in Europe is structural and took part in the events that are open globally starting in the USA since 2008, but that was born especially from its insufficient dynamism. The EU has failed to respond adequately to its technological change, aging of its population, the largest shift of wealth to emerging countries that have occurred in recent decades. The weaker European countries have reacted to the deteriorating their competitiveness directly with the issue of greater public debt in support of domestic demand. In the case of Ireland that have favored a low- tax investment from abroad that in many cases have proved unprofitable has forced the state to settle the resulting deficit of banks. In Spain's case the push to domestic demand realized through a huge investment real estate and tourism, which has proved to be unsustainable in retrospect, which produced the banking crisis that required an intervention to save the banks. There is no doubt that the vast expansion of an off-budget spending and therefore out of control is at the origin of the Greek crisis.

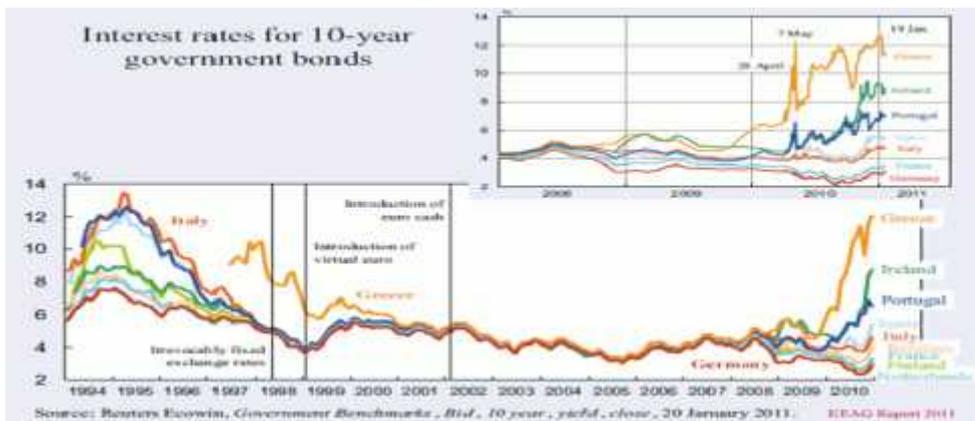
Figure 3.1 Member State with Excessive Deficits



Source. Eurostat, database, Economy and Finance, National Account= GDP.

It is accompanied with an impressive fall in national savings of + 20% to - 10% of GDP and use of the massive import of capital from abroad favored by their low cost because of entry into the Eurozone.

Figure 3.2. Interest Rates for 10 - year Government Bonds

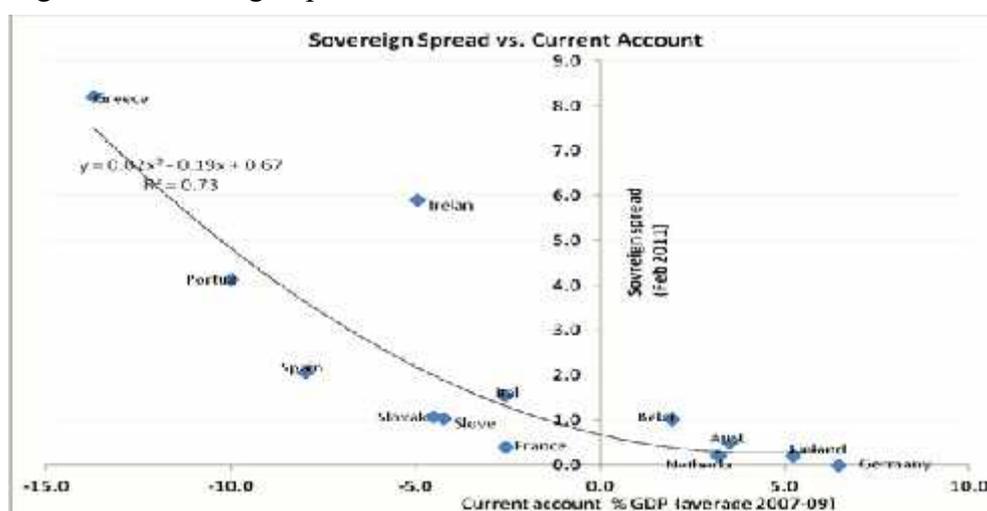


Source: Reuters Ecwin, Government Benchmarks, Bid, 10 year, close, 20 January 2011³¹.

³¹ See. <http://www.voxeu.org/article/crisis-mechanism-euro-european-stability-mechanism>

Therefore, it is clear at this point that this situation cannot be solved with only fiscal consolidation policies or privatization of beaches, ports or airports. We observe that these privatizations reduce public debt but also the public revenue and the balance is uncertain.³² The risk premium that a country pays on its debt is not only related to the amplitude of the debt relative to GDP but also its relation to the current account deficit of the same country.³³

Figure 3.3 Sovereign Spread vs Current Account



Source: Daniel Gros, 2011³⁴

The importance of foreign debt is shown by the case of Portugal which was had to pay a risk premium untenable and to ask for a bailout, despite indicators of deficit and debt compared were the line indicators with those of major European countries.

³² Cfr. <http://www.voxeu.org/article/why-privatisation-not-panacea-greece>

³³ See <http://www.voxeu.org/article/external-versus-domestic-debt-euro-crisis>

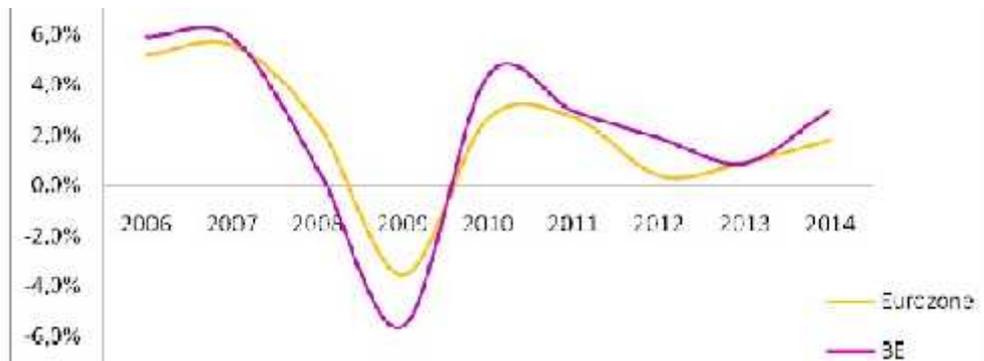
³⁴ See Daniel Gros, 2011.

A high foreign debt is in fact considered by the markets as a debt at risk given that the country does not cater to honor him by taxing its citizens.

The Irish case is still different because, even though the share foreign debt is relatively low, the amount of debt is very high. It is a case where the way should be the debt restructuring. This is a completely different picture, for Greece. Every time you pick up the issue of debt restructuring or "hair cut", there are harsh reactions from potential damaged parts, in this case the ECB and the Euro system that is exposed to the PIIGS through refinancing of European banks. The conclusion is that the regulation of the ESM will be decisive and probably needed an extension and adequate flexibility of its tasks. Just as important to the adoption of systematic monitoring of macroeconomic imbalances, in which the current account deficit and foreign debt are as important indicators of the balance of an economic system. The increase in cases requiring rescue operations in Europe and created dangerous possibility of contagion, it appears, in fact, after a long period of convergence of interest rates in 1998 following the fixing of exchange rates between the adopting the euro. Only since 2008 that begins to occur, this divergence between the rates on the public debt and the spread against benchmark German who gave the signal of the imbalances in place.

The crisis has caused a significant decline in the level of output (Figure below).

Figure 3.4 GDP Growth in EU and Eurozone



Source: Eurostat

In the period preceding the crisis, economic activity in the eurozone continued expands at a moderate pace.

All components of domestic demand, as well as exports, were economic net. During 2007 there was a slowdown in industrial production, an increase in the sector services and improvement in market conditions. Macroeconomic indicators short-term witnessed a labor slowdown in economic activity during the quarter third. Business investment and exports declined as a result of the strengthening of the euro and the decline in demand from US markets. The worsening liquidity situation u also in the European financial markets. These developments affected the economy of the eurozone, exacerbating the performance of some countries' housing markets, such as construction sector and consumer spending. The eurozone's economy recognized pace growth slowdown in 2008 was around 0.9%, compared to 2.7% in 2007. 2008 was characterized by a slowdown in domestic demand nd private

investment, contracting lending, rising unemployment and downward trend of business and consumer confidence indices.

In 2008, the eurozone economy contracted, thus entering a recession. This the economic slowdown is a consequence of the financial crisis and its transmission toeconomy. This has caused fluctuations in the housing market and the bankruptcy of some large financial institutions. Despite ancillary measures taken by the ECB, the pace the growth of domestic demand and private investment has slowed significantly.³⁵

Of course, this analysis should also consider potential growth. Evaluation of The impact of the crisis on potential growth is important because it is a determinant key to the development of living standards in the medium to long term.

If the level of potential output is underestimated, the risk of deflation and triggering of incentive policies will also be underestimated. The potential output is one important determinant of fiscal position. Lower potential output levels will generate (negative) lower output differences and consequently the structural component of the budget deficit will be greater.

Projections for potential economic growth before the crisis predicted a slowdown to the potential growth in the European Union of 2% per annum in the next decade for just over 1% from 2020 onwards, due to population aging. This the slowdown

³⁵ See http://www.econ.nyu.edu/user/gertlerm/JEP_NBER_WP.pdf

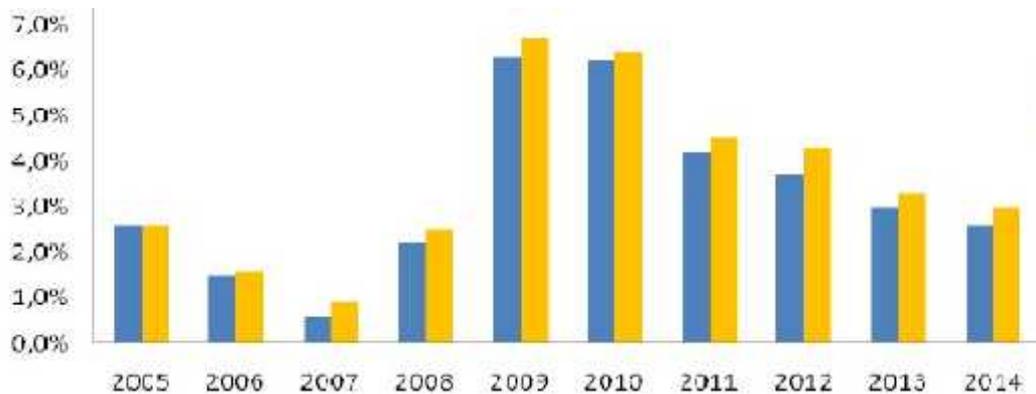
requires fiscal position adjustments, as also called the Pact of Stability and Growth. It is hard to imagine that this crisis will not have one long-term impact on the potential growth rate in the near future. During crises financial investment opportunities are limited, low demand and cost high borrowing. After coming out of the recession, reducing the level of GDP can not be easily offset if the economy converges to its potential level too slowly.

Moreover, if the crisis adversely affects the medium-term growth potential and in the long run, Europe will shift to a different path of growth with consequences important for its competitive position in the world and its living standards its population. Severe financial and economic crises testify to an impact strong and sustained negative in production and employment.

However, data on GDP performance are not the only ones that can demonstrate the effects of the crisis on the real economy. Performance in consumption and employment levels constitute a better indicator of the impact of the crisis on daily life citizens rather than changes in the level of GDP. Europe is facing a downturn catastrophic economic and social. Coercive measures taken during the fall Europe's economic growth has further contributed to rising poverty and unemployment.³⁶

Figure 3.5 The deficit in Eurozone and EU

³⁶ See <http://www.bioline.org.br/pdf?nd13075>



Source: Eurostat³⁷

The unemployment rate is another indicator of the consequences of the crisis on the economy real. EU anti-crisis measures were accompanied, especially in southern Europe, by tough austerity policies, significantly increasing the unemployment rate, reducing it the level of real wages and cuts in the social security system. Markets e EU work began to weaken significantly in the second half of the year 2008, further deteriorating during 2009. The unemployment rate in the EU has increased by more than 4 percentage points. The figure below shows the unemployment rate in the EU and the euro area in recent years shows that the increase in the unemployment rate unemployment is higher in the eurozone countries.

Even for this indicator there are consistent differences between different countries.

In Germany 's unemployment rate has slowed down compared to its very high high in Spain with about 8%. In fact, the existence of these differences relies on structural

³⁷ See <https://ec.europa.eu/eurostat>

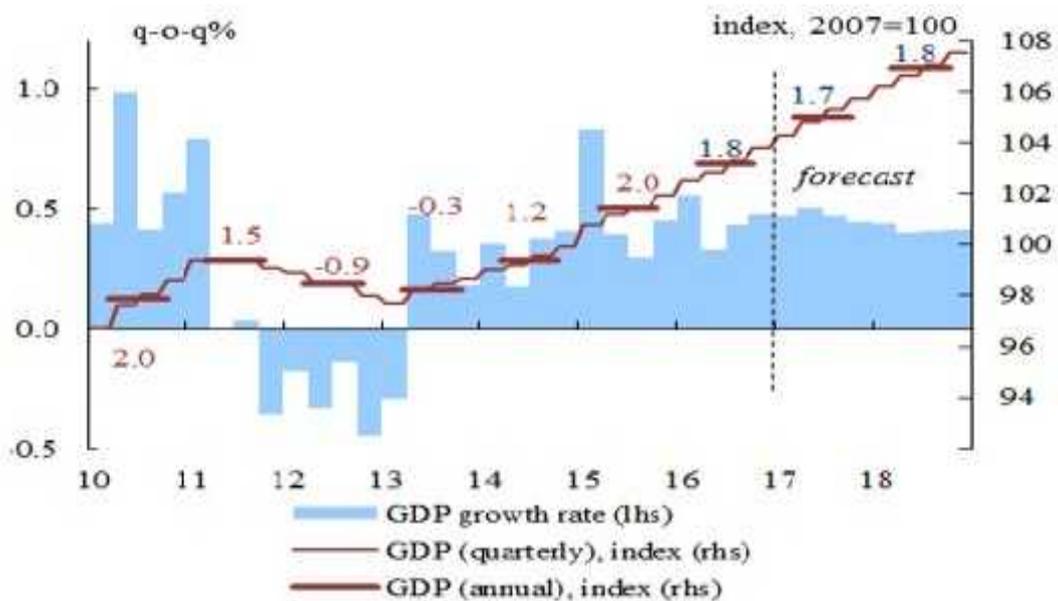
factors of the country's economy. German companies have invest heavily in their workforce skills and therefore hold on work their skilled workers even if some of them are temporarily absent needed. Meanwhile, in Spain most of the employment growth during the decade the latter consisted of low skilled workers in the construction industry and tourism. The deterioration in the performance of these sectors led to massive layoffs.

In the early stages of the crisis, most of the job losses were concentrated in only a handful of member states, mainly as a result of pre-existing vulnerabilities as well as a greater exposure to the consequences of direct shocks (eg financial sector and housing markets, exposure to international trade)³⁸. However, with the sharp contraction in domestic demand and external employment has declined in all member states since countries that have registered the most negative performance of employment rates are Spain and Greece. Socio-economic groups with contracts relatively flexible working and low and medium skills have felt the most much of the burden of the recession initially. A significant increase in unemployment is registered at the level of artisanal workers and those employed in the professions elementary, mainly in services. Women are less affected than men, thus given that the crisis hit when the number of men was relatively high (industry of cars, construction). The rise in unemployment was initially limited by a contraction of

³⁸ See <https://www.bis.org/publ/cgfs60.pdf>

power workers because of the discouragement of workers. These effects are mainly reflected in the number of non-national employees, who make up about 5% of the power of general worker in the EU. The risk that unemployment may not easily turn into pre-crisis levels pose a major challenge for EU countries. In this context it is estimated that if the right measures are not taken, the effects can be shocking. The along with the long-term effects on potential economic growth, this can be threatening the European model of social welfare, which is also struggling with aging population.

Figure 3.6 Real GDP Growth, Euro Area.



Source European Commission³⁹

³⁹See, https://ec.europa.eu/info/business-economy-euro/economic-performance-andforecasts/economic-forecasts/autumn-2015-economic-forecast_en

The crisis can certainly say that it has contributed to the slowdown of economic growth of Albania. Particularly the crisis in the neighboring countries Italy and Greece has been the most serious great. Albania 's exposure to trade, financial ties and remittances emigrants from these countries have increased the sensitivity of our economy to each unfavorable development in these countries.

According to experts, exports, remittances and foreign direct investment (FDI) have been the main transmission channels of the global financial crisis in the economy Albanian.

However, detailed analysis of factors and mechanisms for transmission of the crisis in our country goes beyond the main purpose of this study. Before presenting the empirical analysis, in this section we will give a description of the Albanian economy against the background of the economic financial crisis global.

The pre-crisis period was characterized by a favorable external environment, high economic performance driven by household spending, a high rate of growth in the construction sector, credit boom and substantial inflows from remittances. The impact of the global crisis on the deterioration of these factors has shrunk economic growth rate. The first signs of crisis were manifested in the quarter end of 2008, through the contraction of the level of consumption, blocking of investments and the emergence of some existing problems mainly related to financial system. The impact of the crisis on the domestic economy gradually increased until economic growth recorded its lowest rate in 2013. Developments Macroeconomics in the

country were significantly affected by the slowdown world economic growth, rising import prices and sluggish performance of domestic demand. During this period, the Albanian economy developed into one an international environment characterized by high uncertainty and market tensions financial⁴⁰. Of course, the uncertainty stemming from the shock of the global financial system was reflected in the withdrawal of some deposits from the system. These withdrawals caused liquidity problems in the system and were associated with rising rates of interest during this period. Moreover after 2010, arrears government consistent towards the private sector further deepened the existing shortage of liquidity.

On the other hand, this situation reduced the system's willingness to lend the economy, and consequently, the marked slowdown in lending rates.

In response, the Bank of Albania took action on injecting liquidity and maintaining public confidence in the banking system.

It also tightened oversight regulations during 2008, aiming at strengthening of financial system stability. These measures have proved to be effective and the system Albanian banking has successfully coped with the first blow of the economic crisis and world financial.⁴¹

⁴⁰See,https://ec.europa.eu/economy_finance/publications/occasional_paper/2013/pdf/ocp158_en.pdf

⁴¹ See Bank Of Albania Report 2008

In the years before the crisis and during the crisis inflation has been very close to the level set as a target, this and due to the decline in production level and low external inflationary pressures. Monetary policy faced a downturn global prices, a decline in production, and low labor demand The Bank of Albania has consistently lowered the key interest rate, reaching the historical minimum of 2% in January 2014⁴². However, the full transmission of the effect on the credit markets has diminished due to high euroization, premiums high risk, and poor credit demand. Local currency exchange rate (ALL) against the euro has been stable, changing slightly since 2011.

The current account deficit also increased significantly after 2008 significant imports and improvement in the trade balance for the energy sector, yes affect a current account improvement. Big external imbalances yes are gradually corrected, but external weaknesses remain. In the financial account, financing is done through debt and equity.

However, Albania has maintained macroeconomic stability, continuing with the payment of arrears and has taken steps to improve administration tax and revenue collection. However, economic growth remains low and the current account deficit remains large, reflecting weak competition.

⁴² See Ministry of Finance Report 2014

The budget deficit has been high since 2008 and the debt level is high the public has grown by further limiting the fiscal space for maneuver. Debt of growth has increased since 2009⁴³, but has remained at manageable levels. Albania should pursue fiscal policies aimed at reducing public debt, but at the same time it must undertake expenditure to stimulate economic growth.

The crisis that engulfed the global economy is reflected in our country in terms of downsizing of economic growth rates since the end of 2008. In the years immediately preceding the crisis, economic growth has recorded positive rates, supported by positive performance e services, industry, transport and telecommunications sectors. Increasing

The country's economic growth is largely driven by the rapid growth of demand interior. This demand has increased in all its components: consumption, investment and government spending. Another factor that has influenced growth Economic growth has also been driven by increased exports and foreign investment direct growth.⁴⁴ In the first three quarters of 2008, economic growth recorded rates of satisfactory. Meanwhile, during the last quarter of the year, affected by the crisis In the global financial and economic environment, economic activity showed signs of slowing.

⁴³ See INSTAT 2009 Report

⁴⁴ See Bank Of Albania Report 2007

Monetary indicators have also had significant fluctuations⁴⁵. Deepening the consequences of the crisis Worldwide financial and economic downturns were associated with lowered commodity prices and a lower level of imported inflation. Slowing down consumption Private equity, along with declining investment, have been major contributors to slowing aggregate demand growth rates. This trend continued for a long time while in 2010 macroeconomic stability and lower premiums of risks have contributed to the gradual improvement of aggregate demand. Recovery of continued in the world economy and its positive impact on export demand has supported the growth of the domestic economy during 2010. Economic activity had signs of recovery during the first half of 2010. Private investment increased only in the second half of the year. At the same time, the level of confidence of consumers increased by supporting private consumption. On the other hand, the contribution of public spending to aggregate demand and economic growth has gradually declined throughout 2010.

During 2011, the Albanian economy continued to grow at a moderate rate as well as over the last two years. This year's economic growth continued to be sustained by foreign demand, albeit to a lesser extent as a reflection of the deceleration of world economy. Internal demand has been contained and shaped mostly from the contribution of the fiscal sector during the first half of the year.

⁴⁵ See Bank Of Albania Report 2010

Even during 2012 due to the high level of uncertainty, tight conditions of financing and weak aggregate demand, economic growth remained relatively weak. It was not enough to exploit the country's production capacity, generating weak demand-side inflationary pressures. Uncertainty about the future, curbed consumer spending and investment.⁴⁶ Economic growth relies mainly on foreign demand, while domestic demand yields a low contribution. Economic activity expanded during the first three quarters of the year, largely supported by foreign demand. Also affected by the slowdown of outside economic activity, exports continued to grow, but at a lower rate.

On the other hand, domestic demand was sluggish, making a contribution minimum in aggregate demand growth.⁴⁷ 2013 was a challenging year for the Albanian economy and financial markets.

Aggregate demand proved weak: fiscal stimulus and foreign demand offset only partially the poor performance of consumption and private investment. Request of the private sector continued to be adversely affected by low agent confidence economies, from declining incomes, as well as from relative conditions tight financing. Also, the external economic environment, characterized from significant

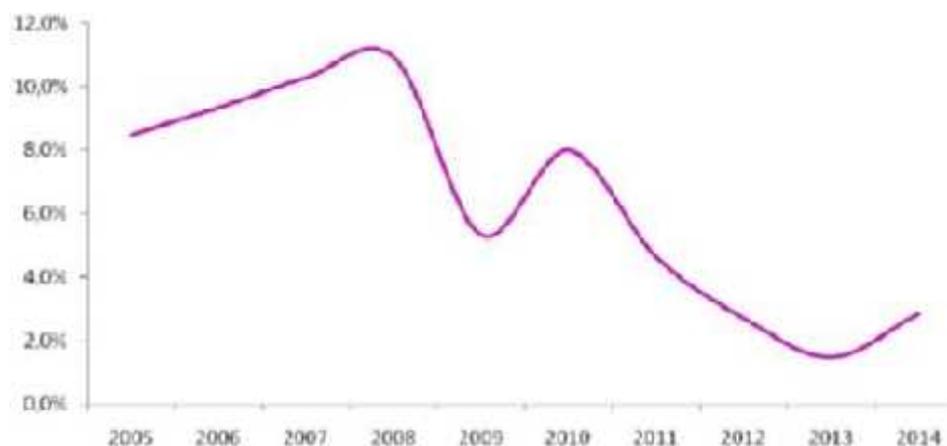
⁴⁶See, https://www.bankofalbania.org/Press/Speeches_Interviews_and_Articles/Interviews_and_articles/Interview_with_Gent_Sejko_Governor_of_the_Bank_of_Albania_Monitor_magazine_2523.html

⁴⁷ See Bank of Albania Report 2012.

economic difficulties in trading partners and the reduction of financing of developing countries, has not favored economic activity in the country.

The general election held during the year increased the uncertainty among agents economic and financial markets, adversely affecting their decisions investment consumption. The weak aggregate demand was reflected in a low growth Albanian economy. This performance was accompanied by a slow growth in employment wages and further generated low inflationary pressures. It created difficulties in financial situation of Albanian businesses and affected the deterioration of loans with problems in the banking system balance sheets. Moreover, the economic slowdown affected and public finances, which were characterized by the rapid growth of the budget deficit and public debt.

Figure 3.7 Nominal Growth of GDP 2005-2014



Source Instat⁴⁸

⁴⁸ See INSTAT

Economic trends show a gradual improvement in economic growth since third quarter of 2013.

Due to the increased domestic demand supported by fair fiscal policies and structural reforms, economic growth marked an acceleration in 2014. The business cycle has increased slowly, by reforms undertaken by the government, such as the payment of dues most of which is expected to be paid within 2015. A gradual recovery of directed economic growth is projected in the coming years by domestic demand. Gross Domestic Product (GDP) is projected to have been growing in the years ahead, largely driven by the increase in foreign investment direct. As a result of the payment of government arrears to business and lending expansion, it is also expected that private domestic investment will undergo significant growth. Private consumption is expected to have a positive impact by improving confidence and by lowering saving levels that had increased significantly in the immediate post-crisis years. Real investment growth is projected to be even more powerful, fueled by foreign direct investment inflows, improved liquidity, by paying off government arrears, and better financial conditions. Sustainable improvement is projected in all branches of the economy, with the largest contribution being made by the extractive industry and that of services. Also the slow recovery projected for the eurozone, is expected to gradually yield its positive effects. Albania needs a period prolonged strong growth to support the recovery process. This highlights the need to

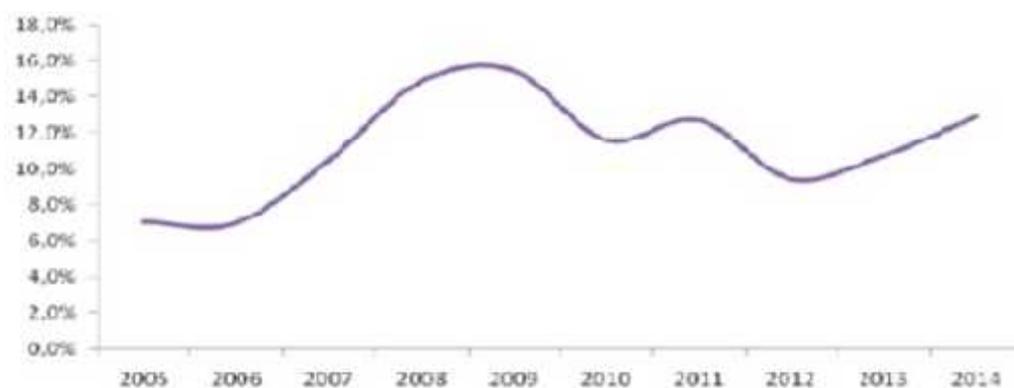
implement structural reforms aimed at enhancing economic potential in the long run. Expectations and forecasts point to an increasing trend, but still below pre-crisis levels and below its potential. But it can happen that these predictions do not materialize. The effects of slow European growth for a long period can extend their impact by damaging growth and external and financial sector stability. It depends on fiscal consolidation and effective progress in structural reforms to increase investor confidence.

Macroeconomic policies need to be cautious to ensure the long - term sustainability of the balance of payments, as one of the key aspects of macroeconomic stability of the country and one of the main drivers of growth long-term economy. Albania's current account deficit is a phenomenon of naturally, in the context of the level of development of the country⁴⁹. Especially positive is the fact that most of the country's imports are represented by imports of machinery and equipment, and the import of intermediate goods in terms of consumption. However, increasing the current account deficit is a development that should take place monitor continuously. Domestic demand is reflected in the deficit increase trade and current account deficit during 2008. As a result of the strengthening of the effects of the economic crisis on the economies of neighboring countries, the rapid growth of

⁴⁹ See <http://documents.worldbank.org/curated/en/330791468742523513/pdf/292570AL.pdf>

imports and the slowdown of remittances contributed to the increase in the account deficit current.⁵⁰

Figure 3.8 Current Account Deficits



Source Bank Of Albania⁵¹

It should be noted that some of the factors that have influenced the expansion of the account current, such as high prices of basic import goods and temporary expansion i budget deficit as a result of increased public investment for the road project Durres-Kukes, are of a temporary nature. In the absence of these factors, the deficit of the current account would have a lower value.

The current account deficit during this period recorded high values. the level Albania 's trade deficit has traditionally been considerable due to low level of production and exports. The weakness of domestic demand has contributed to its contraction during 2012 and 2013. In the period 2009-2013, at more than two thirds

⁵⁰ See Albania Central Bank, Report of 2008

⁵¹See,https://www.bankofalbania.org/Botime/Botime_Periodike/Raporti_Vjetor/Raporti_Vjetor_2008.html

of the current account deficit is financed by net inflows foreign direct investment although coverage was somewhat lower in 2014.

Direct investment inflows are expected to remain substantial. Although exports have continued to rise, and the high level of imports has again impacted its deterioration in 2014. The high deficit reflects the difference between needs for investment and relatively low savings. In the long run, this difference can be reduced as revenue and output increase. Fiscal discipline it should also contribute to raising the level of domestic savings.

Economic growth is largely financed by domestic sources financing, coupled with a rapid increase in credit to the economy. It credit has largely supported the growth of investment in the economy, manifested in the the dominant share of business loans in portfolio and portfolio add-on loan. Despite the slowdown shown during 2008, consumer credit also has recorded a significant increase, attesting to the increase in private consumption in economy.

The uncertainty that followed the shock of the global financial system was reflected in the withdrawal of a portion of deposits from the system. These withdrawals brought liquidity problems to the system and were associated with rising interest rates during this period.

On the other hand, this situation naturally reduced the readiness of the system to lend to the economy and consequently to the apparent slowdown of lending pace. This development, coupled with the reduction of remittances during this period

period, contributed to the slowdown of economic activity. In response, the Bank of Albania has taken steps to inject liquidity and maintain public confidence in banking system. It also strengthened oversight regulations during 2008, by aimed at strengthening the stability of the financial system. These measures have proved effective and the Albanian banking system has successfully withstood the first shock of the crisis economic and financial world.

The financial sector continues to face significant risks, especially those of exterior, but it remains stable and has recently shown improving trends. The economic crisis and the Greek debt pose a risk to Albania. BoA lowered the key interest rate in January 2015 to one level 2% record. Consequently, during 2015, interest rates continued to decline⁵².

The exchange rate of the euro has remained the same. Although monetary conditions and finances have improved, lending and demand for cash have remained lower. Widespread euroization, weak demand and risk aversion of banks, impede the transmission of monetary policy.

The authorities have taken some legal and administrative measures supported by World Bank and International Monetary Fund (IMF)⁵³ to address the problem of “bad credit”. Repayment of arrears until now has not significantly affected the reduction of loans with problems, but a decline is expected in the future. Progress

⁵² See <https://www.bis.org/review/r181114d.htm>

⁵³ See IMF and World Bank Reports

in clearing these loans with problems has been limited. Meanwhile, during 2015, banks are expected to cancel old loans considered non-recoverable, in accordance with the rules of Bank of Albania. Economic recovery, full payment of liabilities of bankruptcy and bankruptcy law reform would help ease restructuring of private sector financial positions and increase demand for loan. Despite the high level of non-performing loans, banks remain able good⁵⁴. The banking sector has remained profitable also due to the decrease in the need for creating provisions for credit losses.

Banking activity continues to be mainly financed by deposits. However though Non - performing loans remain high and are well provisioned, loans with problems still make up about 50% of the bank's capital. Moreover, regardless of a downward trend, the high euroization of the economy remains a concern, as it exposes banks to credit risk. Foreign currency credit still accounts for about a third of total loans, making their repayment more susceptible to an impairment possible of the lek. Also, since government securities make up 25% of of bank assets, an increase in sovereign risk would affect the solvency of banks⁵⁵.

Albania's good economic performance before 2008 was accompanied by changes positive employment and reduction in poverty rates. Poverty rate, measured by national standards, it dropped from 25% in 2002 to 12% in 2008, and rural poverty

⁵⁴ See <https://www.tiranabank.al/english/media/1533911261AnnualReport2017.pdf>

⁵⁵ See Ministry Of Finance Report 2015

has fallen at an even more impressive rate from 40 to 15% during the same period. Labor markets and public and private transfers have been the main channels for improving the standard of living. However, the effects of the crisis global growth and slow growth appear to have changed performance. Recent studies for measuring living standards show that the poverty rate has increased after the year 2008.

Available data on the unemployment rate show that it has increased by 12.5% in 2008 to 18% in 2014. The unemployment rate is higher youth and women. The increase in poverty was partially offset by pension income and social transfers. Further measures are planned to improve⁵⁶.

Public sector fiscal performance is crucial to the country's path to recovery EU membership. Coordinated support from international organizations has been particularly focused on improving public financial management. In the period preceding the onset of the global economic crisis, fiscal policy e the following has contributed positively to the overall performance of the economy. Politics The fiscal follow-up in this period can be generally considered tight. The budget deficit marked lower levels than planned. Year 2007 particularly coincides with the realization of some important reforms in the economy. Some of the most important reforms are related to improving the administration of tax and public spending,

⁵⁶ See https://financa.gov.al/wp-content/uploads/2018/09/NESS-ENG-8-1-15_final-version.pdf

further reducing customs tariffs on a set of products in accordance with the obligations arising from the trade agreement free trade with the European Union, streamlining and strengthening sector oversight financial as well as the creation of the National Registration Center.⁵⁷ As a result of the strategies and the Ministry of Finance policies to reduce fiscal risk and while maintaining macroeconomic stability in the country, the deficit has maintained one stable level and respecting the set limit value. Unlike the two the previous years, the deficit was mainly financed by privatization proceeds and u There was a significant decrease in the share of deficit financing through the issuance of securities. Fiscal policies in terms of revenue have been targeted main stimulating business and increasing the level of tax revenue.

From a budget spending perspective, fiscal policy has aimed at raising salaries at different sectors of the economy with priority on education and health, as well as reduction of social security contributions.

In 2008-2009 fiscal policy had an expansionary character. This character is reflected in the expansion of public investment and budget deficit. the level Government debt increased during 2008, but remained within the ceiling of 60%. However, improved public debt management in terms of extending the maturity and diversification of funding sources is positive development, which has helped

⁵⁷ See Bank of Albania Report of 2008

refinance debt and control its impact its cost in budget indicators. Government debt continued to rise after 2008, reaching 71% of GDP 2014. Overall, the largest contribution to this growth was due to debt i external. Debt growth was triggered by liberal fiscal policy, the needs for it supporting the energy sector and external shocks from the global crisis. Also the debt level in 2013 increased further, due to the recognition of liabilities of acklog to the private sector of 5.2%⁵⁸.

The budget deficit for 2008 is estimated to have reached 5.7% of GDP, being eepened by about 2.2 percentage points in annual terms. The main contributor to further expanding the fiscal deficit are investment spending.⁵⁹ Improvement of "capital expenditure" management, through a redistribution of funds towards larger projects, has represented one of the priorities of fiscal policy during the year 2008. This fiscal year has been characterized by a relatively high level capital expenditures compared to previous years, a considerable part of it which is represented by the costs for construction of Rrëshen road segment - Kalimash. Fiscal policy for this time period, generally characterized by an expansionary nature, has served as a fiscal stimulus to the economy. expenses

The budget is mainly concentrated in the second and fourth quarters of the year.

⁵⁸ See Ministry of Finance and INSTAT report of 2014

⁵⁹ See Bank of Albania Report of 2008

As in the previous two years, expenditures have been largely concentrated in the months of end of the year, exerting upward pressures on market interest rates overnment securities.

Even during 2009, fiscal policy was characterized by an expansionary nature of which, in addition to monetary stimulus, has helped the economy in generating rates positive of growth. The deficit widened at high rates, especially after the first quarter, estimated at the end of 2009 at around 7% of GDP⁶⁰. The main sources of financing the deficit were privatization proceeds and union credit. Extension the deficit also affected the growth of the public debt stock. growing of public debt and budget deficit during 2009 as a result of fiscal stimulus at In the context of revitalizing the economy, it has necessitated a change of direction fiscal policy in 2010. Under these conditions, in 2010 fiscal policy was oriented towards fiscal consolidation, a process which accelerated especially after the first half of 2010, with the adoption of the revised budget, which defined a lower level of expenditure than that adopted at the beginning of the year.

Fiscal consolidation during 2010 consisted mainly of controlling and reducing budgetary expenditures although measures to increase it were not lacking income. Due to slow economic growth the incomes were realized below planned level. Operational objectives of fiscal policy for 2011 at quantitative terms were expressed

⁶⁰ See INSTAT Of Albania Report of 2008

as respecting the public debt threshold below 60% of GDP, as even maintaining low levels for the budget deficit. These two fiscal anchors at function of the sustainability of public finances have conditioned fiscal space during 2011, which has made it necessary to pursue a fiscal policy careful about this budget year. The overall fiscal policy for 2011 can be easily described as stimulating. Low economic growth and weak domestic demand required the pursuit of one stimulating fiscal policy in 2013. The fiscal policy pursued was certainly closely related to the conduct of the elections. Increase budget deficit is estimated to have given a fiscal impulse. Much of it is created by discretionary fiscal policy, while automatic stabilizers have contributed to a lesser extent the fiscal impulse formation in 2013. Meanwhile, in 2014 fiscal policy has returned to its consolidating nature. Level the high level of public debt left no room for pursuing a stimulating fiscal policy.

The fiscal consolidation process has been driven by increased tax revenues, while the fiscal impulse generated by current primary spending has been offset by downward rates of capital expenditure. The fiscal consolidation program that began in the year 2014 and is included in the medium-term fiscal framework aimed at debt reduction government to GDP beginning in 2015. Fiscal reforms, including even those related to tax revenue and public finance management will be key reforms. The 2014 fiscal package included the imposition of a tax progressive personal income, profit tax modifications and reform excise. Further measures are needed to improve administration tax although such measures are likely to yield benefits only

in the period medium. Improving tax collection is one of the main objectives of current year. The tax administration is undergoing extensive reform, including implementation of a new electronic system aimed at reducing the chances of errors and corruption. The expected increase in the level of tax revenue is projected create the opportunity for increased spending, investment, and growth interest payments. The annual budget law for 2015 introduced fiscal measures for revenues and expenditures, aimed at reducing the fiscal deficit. Another key objective is landing of debt-to-GDP levels, ensuring a stable level for a country in development, not to affect long-term sustainability. Fiscal policies will focus on the efficiency of public spending, the priority of spending high impact policies, opening new perspectives for investment private sector, promoting efficiency gains, economic growth and employment. Albania's public debt is projected to drop below 60% by 2019, as a result of lower levels of deficit and GDP growth⁶¹. However, poor conditions cyclical set a maximum limit for the level of improvement of the site without causing negative economic and social consequences. Forecast verification is subject to several factors such as changes in the position of fiscal policy, the exchange rate, as unexpected liabilities from the sector energy. The Government of Albania is implementing a number of targeted reforms increasing the efficiency in carrying

⁶¹ See https://ec.europa.eu/neighbourhood-enlargement/sites/near/files/albania_erp_2019-2021.pdf

out expenses. Also essential reform must undertaken towards the social security system and the energy sector.

The pension system is currently in deficit and with the outlook for aging dramatic population growth over the coming decades, it will not be able to cope with the rising demand for pensions. Strengthening the fiscal framework and increasing its responsibility and accountability for the effective and efficient use of resources public finances are a top priority for the government. Lack of political measures would pose a serious risk to stability Macroeconomic. Increasing sovereign risk perception in the domestic paper market value may affect his willingness to finance government debt, by resulting in rising interest rates. Without appropriate policies and reforms Structurally indispensable, public debt would reach high impact levels negatively on economic growth.

The global financial crisis has affected all countries in the region and beyond. Restoring the stability and sustainability of public finances remains a major concern for governments in the region. Moreover, the crisis revealed the existence of high fiscal risk and weaknesses in the process of managing public finances. Also, the lack of Transparency in government actions in many countries has contributed to the deterioration situation. The general public has called for greater accountability in the use of public resources. As a result, there is recently a growing focus on improving the quality of public finance management worldwide. Many countries are taking important steps towards strengthening financial management

public and governance (Olden 2012)⁶². In this new approach of governments to management financiers will need new models and more sophisticated tools. In an environment where resources are limited it is very important to ensure effective distribution of resources. Thus, budgets need to be effectively linked to policy objectives. However, much remains to be done.

Why is public finance management important? The main objectives of Public finance management is the maintenance of fiscal discipline, the achievement of efficiency in the allocation process, ensuring operational efficiency, transparency and accountability. The quality of public service provided by the government is highly dependent on the level of efficiency of public finance management. Public resources should be used in the most efficient way possible, to minimize losses. Except this, Effective management of public finances is important for decision making. This of recent and effective resource allocations must rely on accurate information financial (Khagram, S. et al. 2013)⁶³. Increasing the efficiency of financial management the public can positively contribute to building a trusting relationship between government and the general public that is critical to the stability and development of the country.

⁶²See,https://researchrepository.griffith.edu.au/bitstream/handle/10072/45421/78119_1.pdf?sequence=1

⁶³See,https://books.google.al/books?hl=en&lr=&id=XGhv5Btkc6cC&oi=fnd&pg=PP1&dq=Khagram,+S.+et+al.+2013&ots=WPO6Gsmrx4&sig=S9JHn1JSLjEW92R0uS3aXfrQ0nI&redir_esc=y#v=onepage&q=Khagram%2C%20S.%20et%20al.%202013&f=false

This relationship can be further improved and strengthened through strong accountability and transparency in the use of public funds. Countries with strong, transparent and accountable public financial management systems, guided by the principles of efficient and effective use of public resources have tendency to provide better services to citizens and stability macroeconomic; two prerequisites for economic growth and poverty reduction. For her ensuring long-term and sustainable growth, a high level of responsibility e transparency and quality service to citizens, reforms must be undertaken important to address the weaknesses and inefficiencies of the system and processes public finance management.

In Albania, weaknesses in public finance management have led to an increase in debt government debt to GDP ratio above the 70% threshold and significant accumulation of debts mainly due to unpaid bills and unpaid refunds of VAT for business⁶⁴. The total stock of arrears is estimated at USD 700 million, equivalent to almost 5.3% of GDP⁶⁵. In on its way to EU membership, Albania needs to address the shortcomings public finance management system to develop a sound system.

Efficient administration and public services are considered key priorities for place. This section will highlight and discuss the major shortcomings of current management of public finances. Among the most important, will be taken at consider overly optimistic forecasts of public revenue; nonoperative planning mid-

⁶⁴ See https://eeas.europa.eu/sites/eeas/files/albania_2019_erp.pdf

⁶⁵ See IMF Country Report No 18/123

term budget; lack of transparency and participation of the public in the budget process; creating arrears of government; weak internal control systems and limited oversight by external audit institution.

To ensure prudent fiscal and financial planning, forecasts macroeconomics need to be significantly improved. Forecasts optimistic income have adversely affected multi-year commitments and have led to a significant accumulation of arrears and one increase in government debt. Moreover, a loss of efficiency has been recorded public expenditure. Capital investments were the most affected category of expenditures.

The effects would be costly even if the activities had been discontinued or completely blocked. Sometimes limited budgets from the beginning result in much more rather than unplanned cuts that limit and disrupt regular activities.

In addition, unplanned cuts can have a dramatic effect on the process of medium term budgeting. Ongoing budget reviews discourage budgetary institutions producing long-term and mid-term plans, worsening the quality of the process. (Potter and Diamond (1999))⁶⁶

In addition to optimistic revenue forecasts and revisions during the year as well deviations in expenditure composition have demonstrated a problem in the quality of the planning and budgeting process. Despite poor performance, targets

⁶⁶ See Guidelines for Public Expenditure Management

investment projects have been held to a very optimistic level. Mid-term budget and budget ceilings are not sufficiently related to the process annual budget. As a result, the cost efficiency turns out to be lower than it was planned. Significant weaknesses are also observed in internal financial control public.

The legal framework turns out to be adequate while there is a lack of enforcement risk management and other standards of control throughout public administration. For this reason, the proper development of control and audit of the interior will take time and effort. Recent evaluations by organs of independent or international organizations indicate that public administration and service the public has been affected by corruption and fraud. The latter can hurt seriously the outcome of public finance management reforms towards improving efficiency.

3.2 Macro-economic Indicators

3.2.1 GDP Growth

At the beginning of the decade of the 1990s, Albania began political transformation, economic, social, etc., towards a market economy, with the goal of integrating the country into international political, economic, military and cultural structures, with emphasis integration into the European Union. The basic principles the program would focus on transformation included liberalization and privatization of the economy, based on one sustainable macroeconomic ground. In the transition years, Albania has had many positive developments, but also many failures.

At present, the overall economic and financial crisis has been brought under control through drafting and implementation of six-month emergency programs.

Programs are designed to consolidate and maintain stability over the longer term medium-term three years whose core lay in carrying out deep reforms structural, legal, institutional and administrative, which would provide the conditions for consolidation of achievements in the macroeconomic field (relatively high economic growth, low inflation, establishment of fiscal and monetary discipline, etc.)⁶⁷. However, after a decade of political, economic and social transition, Albanian society entered in the new millennium with plenty of loads and facing a host of problems sharp. Albania failed in implementing most of it important of the

⁶⁷ See http://financa.gov.al/wp-content/uploads/2017/12/programi_ekonomik_e_fiskal_2007.pdf

mid-term development program, in carrying out deep reforms structural, institutional, legal and administrative. Weaknesses of the period of transitions can be summed up in poor governance, in the absence of transparency and accountability, in the existence of tax evasion of significantly, at high rates of corruption and smuggling. All of them phenomena prevented the consolidation of democracy and the state in Albania, consequently which was the crisis of 1997.

Despite the efforts made during the last two years, the Albanian economy is currently still suffering from structural deficiencies, unconsolidated governance and problems related to law enforcement and the strengthening of law and order⁶⁸.

The dream of easy gain soon turned into a nightmare for Albanian savers. In 1997, when the house of cards is collapsed, only the rubble of the country's resources remained. The collapse of the financial pyramids (financial companies that had collected savings public with very high promises of interest) have caused, in addition to the economic ruin of thousands of creditors who had invested practically the savings of a lifetime (about 1 billion dollars), a strong one economic and political crisis of the Albanian state (GDP fell to -7%), e about 2,500 victims in the violent clashes that followed.

However, after that annus horribilis for Albania, despite slowness and uncertainty, the production engine resumed almost immediately to turn. The framework of the

⁶⁸ See <https://www.ucl.ac.uk/ssees/research/funded-research-projects/inform>

country is now definitely in the process of stabilization. The year 2000 opened for Albania under the banner of the turning point in the social field cheap. The main indicators show positive trends and, according to the analyses of the International Monetary Fund, the national authorities have managed to maintain the macroeconomic situation of the Country, with the economy that, in 2001, showed inflation at 3.5%, a ratio between GDP and foreign debt of 28.2%, among the lowest in the Balkan area⁶⁹.

All of this opens up concrete prospects for Albania to go back up positions also in the rankings of Gross Domestic Product and income per capita, in which it is still lagging behind other countries Balkans.

Support from the International Monetary Fund and the other international supporters remain absolutely essential for Albania, so that, for the next few years, there are no signs for a decrease in external resources, which nevertheless remain conditioned from the search for ever greater political stability in the country and consequently from a political-social reform program, necessary for the normalization process.

Nevertheless, for international observers the rating of the country risk remains at a high level. An improvement has occurred SACE has in fact approved Albania's passage from the 7th to the 6th risk category (category 1 lower risk, 7 greater risk)⁷⁰.

⁶⁹ See https://ec.europa.eu/economy_finance/publications/pages/publication15155_en.pdf

⁷⁰ See <https://globaledge.msu.edu/countries/albania/risk>

The main problems are identified in the insufficient capacity administrative, in the scarce application of the laws, in the weakness of the judicial system, rampant corruption, crime and presence of a strong underground economy. Economically the country is the poorest in Europe and one of the poorest in the world (in 2001 second data from the Economist Intelligence Unit - EIU - 30% of the population was below the poverty line) with a production almost non-existent industrial and agriculture still at the pure level subsistence. About 20% of the workforce today is active abroad, in particularly in Greece and Italy. Unemployment, the levels of tenor minimum life, extremely low production growth rates, the strong dependence on international aid, the deep crisis in the sector energy and the need to consolidate recent reforms, are the elements relevant in today's Albania, which the new government will not be able to certainly underestimate if it really wants to bring the country to a stable e common development process.

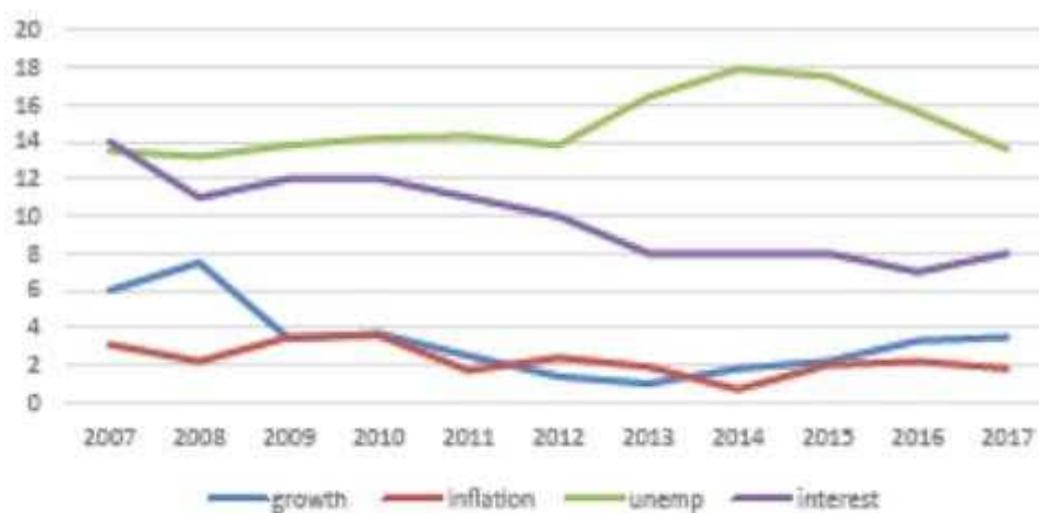
According to the analyses carried out by the International Monetary Fund, the Albanian authorities managed to keep the picture stable overall macroeconomic situation in the country, and the pace of economic growth it's constant⁷¹.

The 2004 figures show that the main economic indicators have had a positive trend. GDP reached 8.3 billion of dollars in 2004 and grew by 6% compared to 2003. This growth is supported by private investments, remittances from abroad and exports.

⁷¹ See <https://www.imf.org/en/Countries/ResRep/ALB>

Base inflation did not exceed the Bank's forecast of Albania, reaching 2.9% in December 2004, in line with the targets set and in any case at the lowest levels among the economically priced countries in the process of transition of south-eastern Europe. This is due to different effects factors, including the reduction of tariffs for fixed telephony and prices contents of agricultural product

Figure 3.9 Main Economic Indicators in Albania



Source: Gngr Turan

Albania has been credited with sustained economic growth during the period 2000-2008, it averaged about 6.1% and had good performance until the beginning of the financial crisis of 2008 (7.5%, in real terms). The impact of this crisis was largely reflected in the years then, when the economy grew by only 3.5% (2009). Activity economic growth slowed further in 2011, marking 2.9% on average, while in 2012 economic growth reached on average 1.6%.

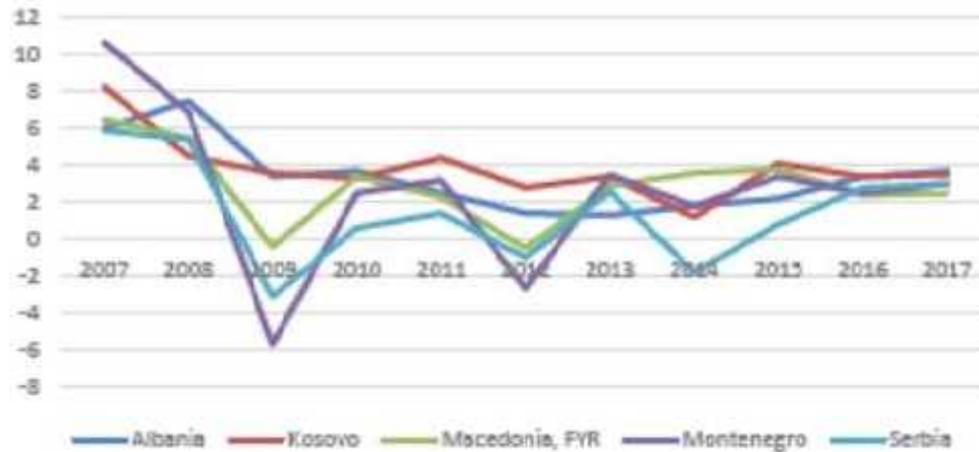
Thus, during the years 2000-2008 there is a flourishing o construction sector, contributing to 13.8% of value added in 2008, while the services sector contributed 51.1% during the period 2000-2008. On the other hand, the contribution of the sector to agriculture has slowed to an average of 20.3%, while the industry sector continues to make a modest contribution (8.1%). With the onset of the financial crisis, the construction sector has suffered more, and consequently its contribution to it has diminished real economic growth, while the services sector has continued to expand steadily.

Regarding the inflation rate we can say since 2000 has so far fluctuated in the 24% range, hence consistent with a target of 3% (+/- 1%) of the Bank of Albania⁷². After the crisis financially, the average inflation rate rose to about 3.5% at 2010 and 2011, up from 2.2% in 2009, mainly due to of high prices from abroad. However, low economic growth during 2012, mainly due to declining consumption and investment, lowered the average inflation rate to 2%⁷³.

⁷² See Bank of Albania paper of 2012

⁷³ See http://financa.gov.al/wp-content/uploads/2017/12/programi_ekonomik_e_fiskal_2007.pdf

Figure 3.10 Real GDP Growth rates in Western Balkans 2007-2017



Source: Eurostat

During the last ten years, the macroeconomic performance of the Albanian economy based on real GDP growth, seen in Table 3.1, was relatively successful in the region comparing to a group of competitor economies with similar characteristics in the region, in Western Balkans. Real GDP grow rate average was higher than Serbia, Montenegro and Macedonia, and slightly lower than Kosovo. In the last two years, Albania has been diverged positively from the others realized the highest level of increases in annual output in the region.

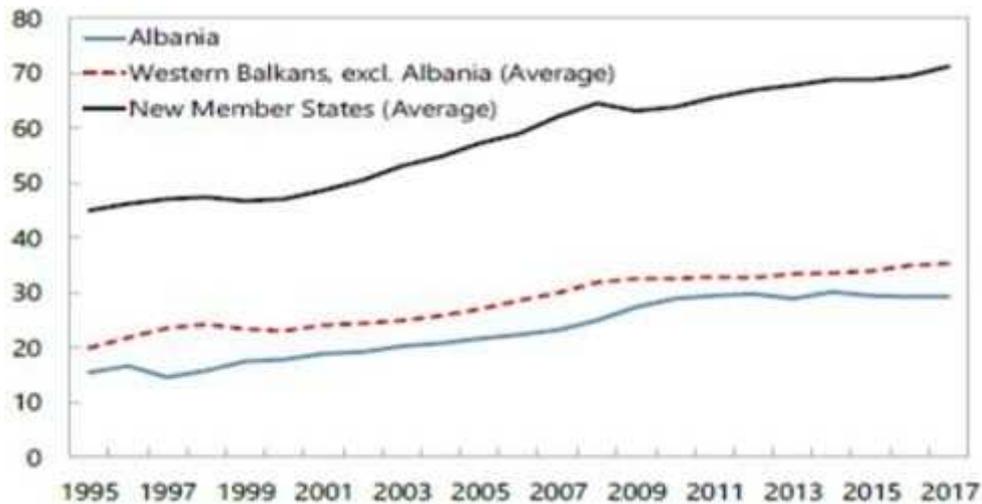
Table 3.1 Real GDP Growth rates in Western Balkans, 2007-2017

Years	Albania	Kosovo	Macedonia, FYR	Montenegro	Serbia
2007	6	8.3	6.5	10.7	5.9
2008	7.5	4.5	5.5	6.9	5.4
2009	3.4	3.6	-0.4	-5.7	-3.1
2010	3.7	3.3	3.4	2.5	0.6
2011	2.5	4.4	2.3	3.2	1.4
2012	1.4	2.8	-0.5	-2.7	-1
2013	1.3	3.4	2.9	3.5	2.6
2014	1.8	1.2	3.6	1.8	-1.8
2015	2.2	4.1	3.8	3.4	0.8
2016	3.4	3.4	2.4	2.5	2.8
2017	3.7	3.5	2.5	3	3
Average	3.35	3.86	2.91	2.65	1.51

Source: IMF and World Bank

Albania has enjoyed strong economic growth over the past two decades and has mitigated the immediate macroeconomic vulnerabilities that emerged after the Euro-area crisis. At the same time, per capita income remains at only a quarter of the EU average, and about half of new member states (NMS). Challenges in shifting from consumption-led growth to an investment and export-led expansion are compounded by outward migration, with about one third of Albanians living outside of the country. In addition, policy efforts— including under the program supported by a three-year Extended Arrangement that was successfully concluded in early 2017—to resolve imbalances in the fiscal and financial sectors still need to be brought to completion.

Figure 3.11 GDP per Capita, in PPP(Percent of EU per Capita)



Sources: WDI World Bank database; and IMF staff calculations.⁷⁴

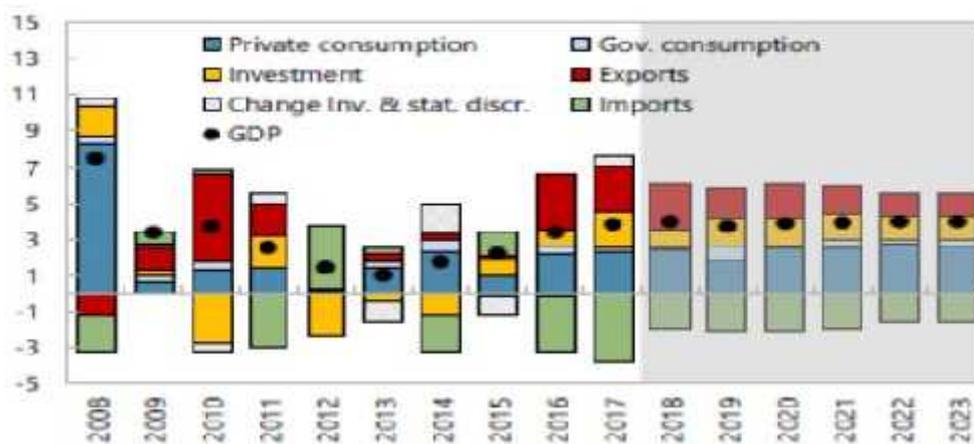
Real GDP growth has been on an upward trend for five consecutive years, reaching 4.3 percent over the first half of 2018. While growth was broad based, the largest driver was electricity generation, owing to favourable climate conditions, with an all-time high contribution of 1.8 percentage points⁷⁵.

For the year, growth is expected to settle at 4 percent, supporting a sustained decline in unemployment. Large idiosyncratic capital inflows (e.g., the conversion of commercial bank capital into Lek) spurred an appreciation of the exchange rate

⁷⁴ See WDI World Bank database; and IMF staff calculations.

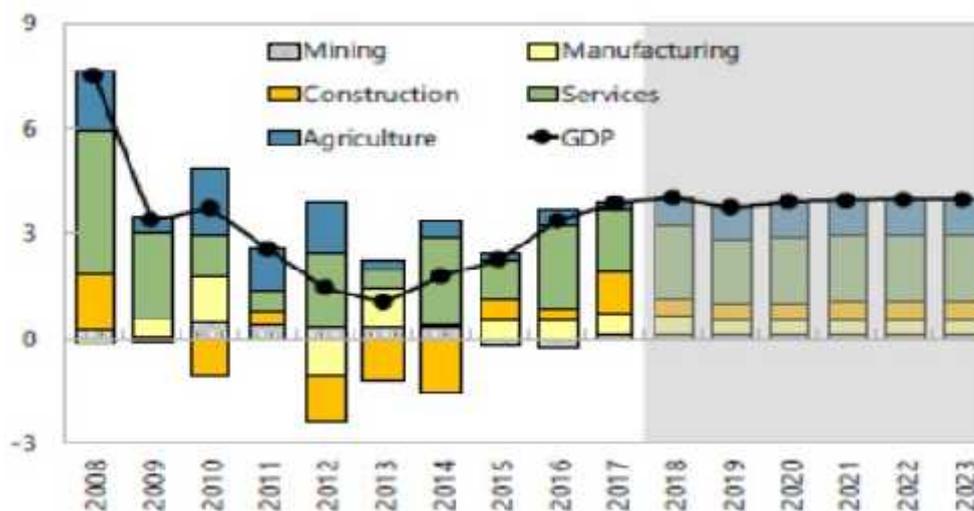
⁷⁵ See <https://www.worldbank.org/en/country/albania/overview>

Figure 3.12 Real GDP Growth: Expenditure Contributions (Percent)



Source IMF⁷⁶

Figure 3.13 Real GDP Growth (Percent)



Source INSTAT and IMF Calculation⁷⁷

⁷⁶ See IMF and Instat Database

⁷⁷ See https://ec.europa.eu/neighbourhood-enlargement/sites/near/files/swd_albania.pdf

The fiscal stance is expected to be broadly neutral in 2018, with the overall deficit edging up to 2.2 percent of GDP.² In the first nine months, the overall and primary balances improved as revenue underperformance was more than offset by lower current spending. The revenue underperformance was partly driven by the clearance of VAT refund arrears. The total stock of government arrears has oscillated through the year; and stood at 1.5 percent of GDP at end-September. The authorities issued a seven-year €500 million Eurobond at favourable rates in October 2018 and used €200 million to buyback a portion of the €450 million 2015 Eurobond falling due in 2020. The stock of public debt is expected to decline to 70.5 percent of GDP in 2018, mainly thanks to exchange-rate appreciation.

Despite an accommodative monetary policy stance, private credit remains weak.

In June 2018 the Bank of Albania (BOA) cut its policy rate by 25 bps to a historical low of 1 percent and initiated ad-hoc purchases in the foreign exchange market. The BOA's decision aimed to address disorderly market conditions and deflationary pressures following the sharp appreciation, against the background of a negative output gap. Despite low interest rates and ample liquidity in the system, private sector credit contracted by 5.4 percent at end-September 2018.⁴ Although this decline was mostly driven by credit in foreign currency, credit in local currency to corporates also fell, with only a minor increase in credit to households and SMEs. Credit is mostly driven by domestic banks, while EU-owned banks are

deleveraging. On the demand side, recent BOA surveys indicate that the appetite of firms and households for new loans remains weak.

During the last ten years, the macroeconomic performance of the Albanian economy based on real GDP growth, seen in Table 3.1, was relatively successful in the region comparing to a group of competitor economies with similar characteristics in the region, in Western Balkans. Real GDP growth rate average was higher than Serbia, Montenegro and Macedonia, and slightly lower than Kosovo.

In the last two years, Albania has been diverged positively from the others realized the highest level of increases in annual output in the region.

Figure 3.14 Real GDP Growth rates in Western Balkans



Source: World Bank⁷⁸

⁷⁸ See <https://www.worldbank.org/en/news/press-release/2019/04/02/western-balkans-sees-rising-risks-to-growth-outlook-amid-slowing-job-creation>

Consequently, after five consecutive years of economic slow-down, the average annual growth rate in Albania, rose to 3.5 per cent in 2017. Furthermore, that rate remains over the average for a group of comparator economies with similar characteristics in the region in Western Balkans. This upward trend is forecast to continue due to increases in consumption and investment both in private and public, and therefore resulting decreases in unemployment, particularly rising from expected spill over effects of Trans Adriatic Pipeline both in output and employment. Therefore, growth in Albania is expected to strengthen further in 2018, 2019 and 2020.

Albania's economic reform programme (ERP) projects economic growth to accelerate to 4.5% by 2021 based on strong private domestic demand. GDP growth in 2018 was robust at 4.2%. Private demand is expected to continue driving economic growth in 2019-2021, based on greater employment, rising wages and favourable lending conditions for households. Private investment activity is projected to pick up significantly in this period, driven by emerging capacity constraints and favourable financing conditions. Net exports are expected to make only a marginal contribution to the economic expansion. The growth outlook appears optimistic considering a worsening external environment, continued low levels of lending to businesses, and enduring weaknesses in the business environment.

The ERP expects Albania to cut public debt from 67% to below 60% of GDP by 2021 by reducing current expenditure and stabilising tax revenue. The 2018 budget deficit has turned out lower than planned with estimated 1.5% of GDP, mostly due to lower than expected capital spending⁷⁹. The ERP expects the budget deficit to fall to 1.2% of GDP in 2021 by reducing current expenditure but does not provide details of a fiscal consolidation strategy. The relatively low public expenditure does not allow for significant expenditure cuts which partly explains the moderate pace in debt reduction.

The relatively low tax revenue is planned to stabilise without major reforms outlined and will thus remain below potential. Public investment is set to increase to over 6% of GDP by 2021 but achieving this increase could be difficult due to weaknesses in the planning and management of capital expenditure⁸⁰.

3.2.2 Inflation

Inflation rate is one of the main indicators that provide information about the state of the economy. If inflation rises above the forecast value, the economy will have negative consequences, reducing savings, increasing uncertainty for businessmen to sign contracts, hampering economic growth and, if there are three-digit values,

⁷⁹ See <https://financa.gov.al/wp-content/uploads/2019/02/Economic-Reform-Programme-2019-2021.pdf>

⁸⁰ See <https://balkaneu.com/ec-criticizes-albania-for-growing-number-of-ppps/>

may also cause social and political upheaval. In most countries, the central bank is responsible for designing and implementing monetary policy. There are countries where monetary policy decisions are made by the central bank in cooperation with the government. For the monetary policy to function properly, the monetary regime that has been formally implemented should be well-defined. The three main types of monetary regime are: monetary targeting regime, exchange rate targeting and inflation targeting. In recent years, many central banks have adopted an inflation targeting regime that controls the rise in the general price level. In this context, the central bank publishes the target inflation rate and then tends to move the current inflation to that target, using instruments such as interest rate changes⁸¹. The mechanism of operation of the inflation targeting regime is relatively simple and understandable. Inflation targeting is straightforward, at least in theory if there are differences between the forecast and the target the central bank should take the necessary actions to regulate monetary conditions. Some countries have chosen inflation targets expressed at intervals, while others have identified only a target inflation rate or a maximum inflation target. All countries have set their inflation targets at low single digits. In this regime it is not necessary to achieve the set objective at all times, but the achievement of the objective in the medium term is emphasized. This allows policy to address other objectives such as economic

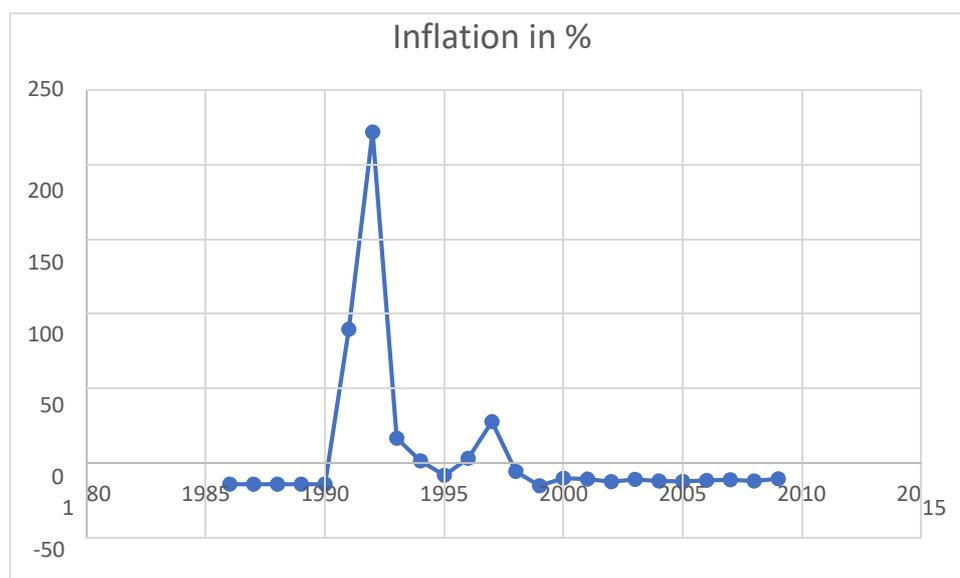
⁸¹ See <https://www.investopedia.com/articles/insights/122016/9-common-effects-inflation.asp>

growth or financial stability. Thus, inflation targeting provides more of a framework within which the central bank has the right to respond to the shocks of a strict rule or law. Under the inflation targeting regime, monetary authorities clearly define the target inflation as well as the relevant instruments to achieve this objective. Specifying the target inflation includes (i) determining the price index to determine the target, (ii) depending on the price level or inflation level, (iii) expressing this objective in numerical value, determining whether the target will be point or interval. For this regime to be successful, the central bank must have the ability to model the behaviour of key macroeconomic indicators and thereby accurately predict inflation fluctuations. Monetary policy analysis has the goal of recognizing the interactions of key macroeconomic variables and the outcome of their macroeconomic over the medium term. For this, it is helped by macroeconomic models that simplify the way decisions are made and their effects until the final objective is achieved. Given that Albania has since 2006 sought to meet the conditions for the implementation of inflation targeting and in January 2015 has passed to explicitly implement this regime, I can say that the main reasons that led me to study the inflation targeting regime are: 1) Achieving macroeconomic stability; 2) Stabilizing the overall price level; 3) Detailed analysis of the features of the inflation targeting regime; One of the widely dealt with aspects of macroeconomics consists in the relation between nominal and real variables, a fact that translates to the question: how should monetary policy be used to support

sustainable, prosperous growth and low inflation? Understanding the functioning of the monetary policy transmission mechanism underlies the answer to this major question.

In the case of Albania, the inflation rate history can be divided into three sub-periods: Before 1991, where the inflation rate was 0, due to the centralized economy; 1991-1998, at very high rates and in some years with hyperinflation (hyperinflation is defined as an accumulated inflation over a 3-year period above 100%); After 1999, with inflation at low levels, under control.

Figure 3.15 Inflation in Albania



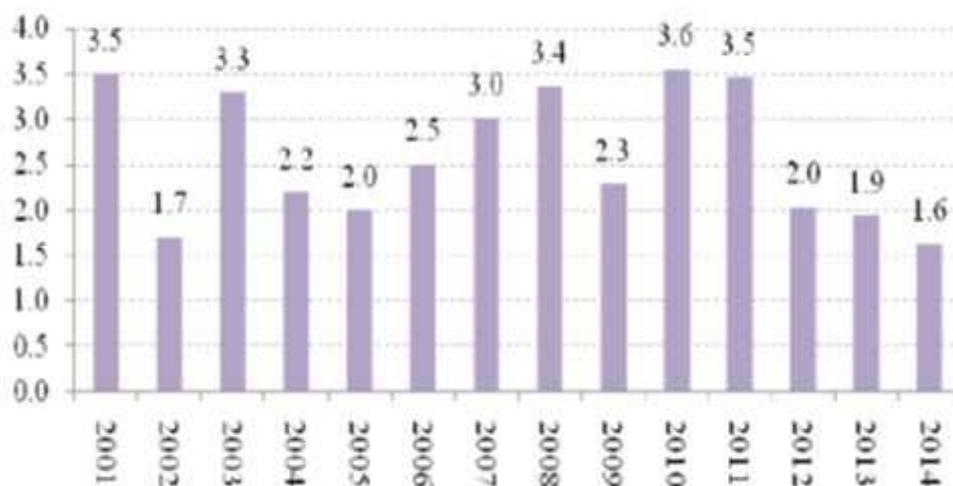
Source: Bank of Albania and Instat

The year with the highest inflation was 1992 with 236.6%. Also, the crisis year 1997 was characterized by a sharp increase in the price level, by 42.1%.

The Bank of Albania has set a target of an inflation rate of 3% objective 1% in order to ensure a sustainable economic growth without major fluctuations in the overall price level.

During the years 2000-2005, there is a downward trend in the annual inflation rate (excluding 2003), while starting from 2006 onwards the indicator has been steadily increasing (excluding 2008).

Figure 3.16 Annual Inflation rates in %



Source: INSTAT

Inflation data were also impressive, not far from the central bank's target of 3 percent for more than 13 years. After the CEZ problems, the level of payments was not very high, and the level of losses was low. In 2014, an operation was undertaken by the Albanian government that significantly reduced the level of outstanding bills, making OSHEE a positive balance after many years. The rise in electricity prices was expected to have a direct impact on the inflation rate. The strong economic growth made GDP per capita in 2007 almost USD 3250, ranking Albania among the middle-income countries. The upward trend of GDP / per capita has continued in the following years as well, but the upward trend has been positive, but not in an upward trend.

The Bank of Albania targets a positive inflation rate to consider the fast-technological evolution of products and their qualitative improvement. Also, by targeting a low value of inflation rate leads to maintaining positive real interest rates, consequently helping generate savings and financial flows in supporting investments in the economy.

The Bank of Albania has launched a target inflation rate of 3.0 % because of the need for higher relative price volatility and it also helps the convergence process with the developed economies to achieve the European Union. (Bank of Albania, 2014)⁸².

⁸² See Bank of Albania Report of 2014

The Bank of Albania revises yearly the inflation objectives and publishes them in the Bank of Albania annual Reports and the most important objective is still to maintain a target of 2 to 4% for mid-term period. One reason why the volatility of prices increases in Albania is because of the large weight food consumption and to get rid of the seasonal volatility is to target average inflation. The target of 2-4% is reasonable appropriate account price volatility despite the fluctuation weather during the period. (Bank of Albania, 2013)⁸³.

By comparing Albania to other transitions economies, inflation has been showing generally low rates and not far from inflation seen across EU countries⁸⁴. When the economy is not under major shocks, inflation seems to stabilize, and this is a dynamic and fragile equilibrium. A wide range of information is used in establishing the implementation of the monetary policy under inflation targeting, thus to the BoA is given an opportunity to include the higher complexity of the Albanian economy in the decision-making structure by allowing the central bank the necessary flexibility toward possible future macroeconomic shocks.

The benefits of inflation targeting in the long term are shown in the way of monetary policy is entertained by adopting Euro which is a long process if considered that it will take considerable period to the conclusion of this process.

⁸³ See Bank of Albania Report of 2013

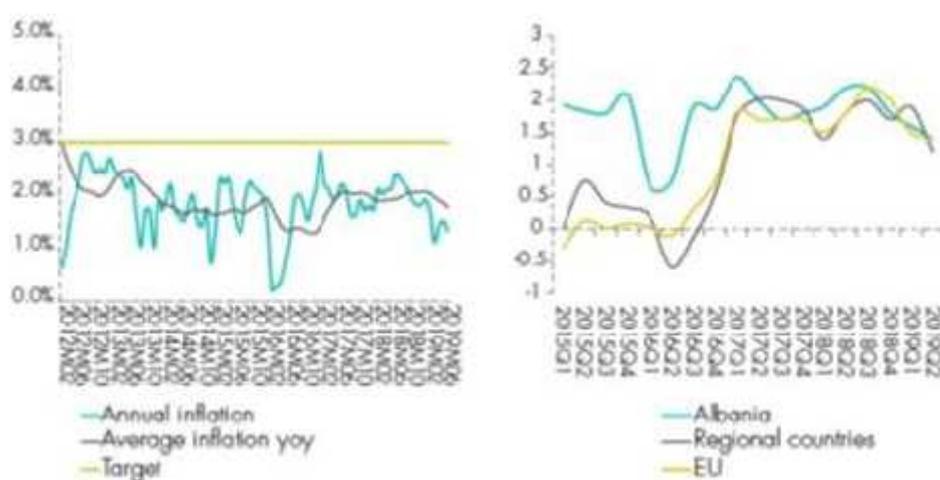
⁸⁴ See EUROSTAT 2014

Average inflation was 1.4% in 2019 Q2, standing lower than in 2019 Q1. Inflation slowed down in the second quarter reflecting a significant reduction in the contribution made by non-processed foods (-0.5 percentage point). On the other hand, an increase in processed food prices and a decline in the reductive impact made by fuel and housing (rent) prices, compared with the previous quarter, generated a positive contribution (+0.3 percentage point)⁸⁵ to the formation of headline inflation. Transmission of the impact driven by an appreciation of the domestic currency, coupled with a slowdown of inflation in EU and regional countries continued to curb inflation in Albania.

This development is seen in an increased convergence of inflation in Albania with inflation in regional and EU countries, since the end of 2017 and onwards.

⁸⁵ See Bank of Albania Report of 2019

Figure 3.17 Headline Inflation, target (Left), inflation in regional and Eu countries(right)



Source: Tradingseconomics.com⁸⁶

Albania's annual inflation rate rose to 1.5 percent in July 2019 from 1.3 percent in the prior month. Prices advanced faster for food and non-alcoholic beverages (2.8 percent vs 2.7 percent in June); furniture & household equipment (1.3 percent vs 0.7 percent); miscellaneous goods & services (0.1 percent vs a flat reading in June) while recreation & culture cost rebounded (1.1 percent vs -0.1 percent). In addition, transport cost declined at a softer pace (-0.1 percent vs -0.6 percent). On the other hand, inflation was steady for housing & utilities (at 0.8 percent); clothing & footwear (at 0.2 percent); communication (at 0.2 percent) and education (at 0.7 percent) while prices slowed for alcoholic beverages & tobacco (1.3 percent vs 1.4

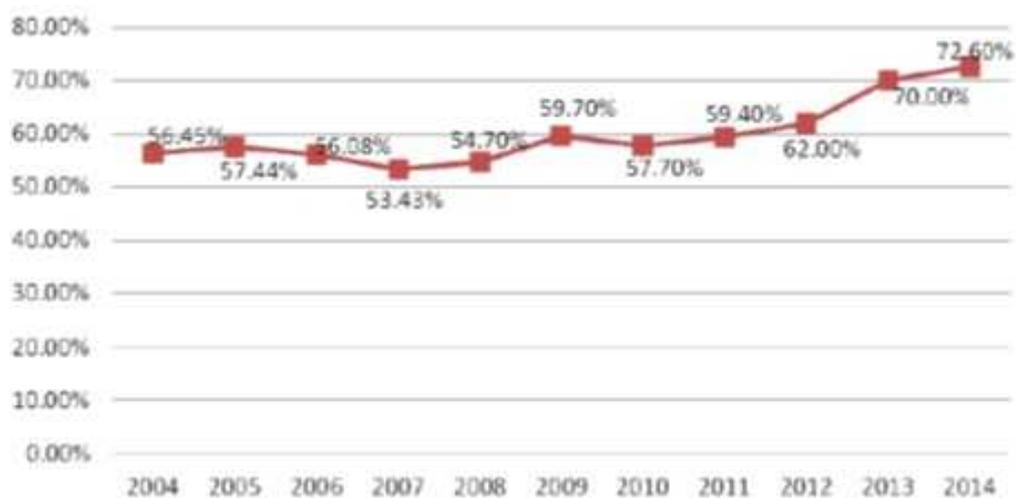
⁸⁶ See Tradingseconomics.com

percent) and for restaurants & hotels (1.1 percent vs 1.3 percent). On a monthly basis, consumer prices dropped 0.1 percent, following a 0.3 percent decrease in the prior month. Inflation Rate in Albania averaged 2.93 percent from 1995 until 2019, reaching an all-time high of 42.08 percent in December of 1997 and a record low of -2.11 percent in March of 2000.

3.2.3 Current Account Deficit

The fiscal situation has been constantly improving. The value of the budget deficit (including grants) has decreased from 10 per cent of GDP before 1999 to 3.2 per cent in 2006. Continuation of reform to reduce the level of the informal economy, which is estimated to be one of the highest in the country. region should continue to increase tax revenue in the future. Changing the tax system, moving from flat tax to progressive tax, is one of the important changes made after 2013 in order to increase budget revenues and a fairer taxation of individuals and businesses. Measures taken until 2008 have also reduced the debt-to-GDP ratio going to the lowest value of 53.4 percent in 2007, while after 2012 this ratio also exceeded the value of debt 60%. Currently, this ratio, considering the debts owed by businesses to the government, has reached a value close to 70 per cent which is well below the 60 per cent level set out in the Maastricht Treaty.

Figure 3.18 Public Debt / GDP ratio in %



Source: Ministry of Finance, Instat.

Figure 3.18 provides information on the public debt / GDP ratio, but does not include government liabilities to businesses. These values also show the upward trend of public debt in Albania after 2008.

High trade deficits in commodities are the main cause for current account deficits. The trade balance in Albania has reflected an increasing deficit, since the beginning of the transition. The reason it stands behind these deficits is the slow performance of exports, on average 7 percent of GDP and escalating import growth, estimated at about 30 percent of GDP. Between issues other structural, these figures point to a clear problem, related to the competitiveness of Albanian export and the growth of

powerful consumer. According to Bank of Albania statistics for trade, about 37% of imports (classification by United Nations economic), represents goods for consumption, while the rest consists of capital goods and intermediate.

Such a distribution gives signals about Albania's capability to boost investment and stimulate economic growth in the period long term. However, a closer look at the components import shows a much higher share of consumption against other uses of imports, thus creating additional concerns about current account sustainability.

Low savings rates forced Albania to rely in fluctuating foreign capitals, which make the country vulnerable from crises.

As Uvalic (2005) ⁸⁷concludes, low levels of its income, declining livelihoods, underdeveloped capital markets and financial, various pyramid schemes, lack of trust in official financial institutions, ongoing practices of savings under the mattress, as well as high levels of corruption and criminality....” they switched their savings. Starting from the year in 1994, the savings rate stabilized at about 5.6 percent the remainder of the 90s. Although low, this represents one robust recovery, versus -51.9 percent of GDP in the year.

Investments were also hurt at the beginning of the transition, but they recovered after structural economic reforms, including privatization and opening up of the external sector (see Kolasi and Tanku (1998))⁸⁸. These reforms pushed private

⁸⁷ See Uvalic (2005)

⁸⁸ See (see Kolasi and Tanku (1998)).

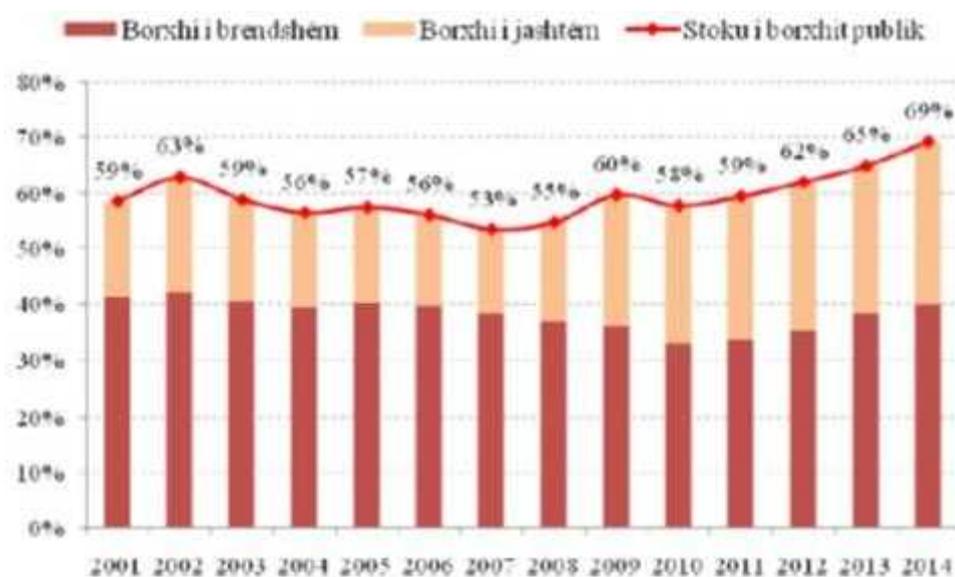
investment, which amounted to 11 percent of GDP in 1996 and provided conditions for further growth, reaching 20 percent of GDP in 2006. At the same time, public investment also suffered growth, but remained low at about 5 percent (fluctuating between 4.5 percent of GDP in 1996 to 5.2 percent in 2006).

While this increase in investment may mean growth of future savings and reduction of current deficits, increase of the rapid credit to economy observed over the last three years can lead to a faster decline in the savings rate, as uncertainty decreases, and liquidity constraints are relaxed.

Decomposing external imbalances in savings and investment shows that the increasing current account deficits represent an increase simultaneously at the average rate of investment and savings.

It follows from our discussion that there is no clearly defined trend in direction of the state of savings and investment, which together even with a shrinking fiscal deficit; they make it difficult to estimate current account deficit stability characteristics.

Figure 3.19 Total debt, internal and external

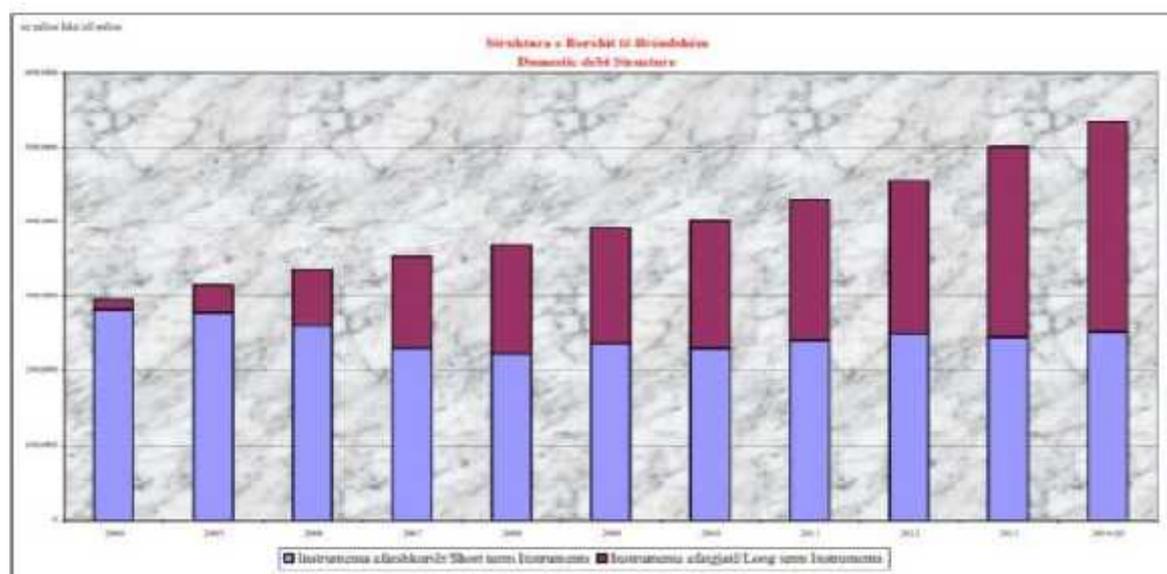


Source: Bank of Albania, Ministry of Finance

It is clear from the graph that debt, prior to the global financial crisis, was largely domestic, had a tight investment base, as shown in Figure 3.19. This led to the creation of carrying risks. Over time, however, the percentage of external debt to domestic debt has increased significantly. This trend is also shown in the chart above long term. The following chart shows the upward trend in the use of long-term instruments. The government has insisted on the issuance of debt instruments with longer maturity short-term / medium-term debt to total domestic debt is almost equal to the weight of long-term debt instruments. The positive experience with the first Albanian Eurobond has led the Albanian government to make the decision and prepare for its re-issuance.

From the graph that debt, up until the global financial crisis, was largely domestic, had a narrow investment base and as shown in graph 3.8 had a short run maturity. This created carry risks. Meanwhile over time it is the percentage of external debt to domestic debt increased significantly. This tendency is given even in the graph above.

Figure 3.20 Structure of internal debt



Source: Ministry of Finance

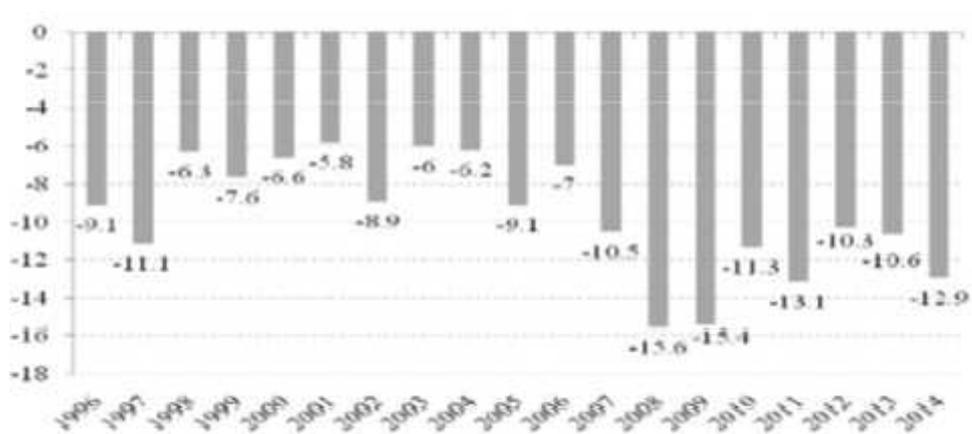
Meanwhile, the weight of short-term debt instruments has changed long-term instruments. The following graph shows the upward trend of use of long-term instruments. The government has insisted on issuing the instruments debt with a longer maturity. The data shown in graph 3.20 show that long 2013 and 2014 the

share of short / medium term debt instruments to total domestic debt is almost equal to the weight that long-term instruments have debt.

The positive experience with the first Albanian Eurobond has led the Albanian government to take over decision and prepare for its re-broadcast.

Albania throughout the transition period has been characterized by a large amount of current account debt that has fluctuated from -5.8 percent in 2001 to -15.6 percent in 2008. In 2014 this indicator was -12.9 percent.

Figure 3.21 Current Account Deficits/ GDP in %

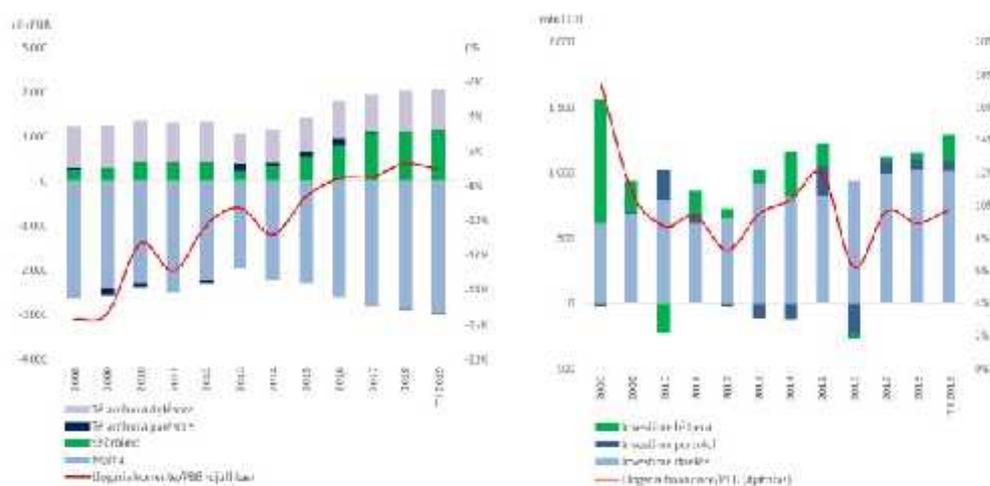


Source: Bank of Albania, INSTAT 2014

In the first quarter of 2019, the current account deficit amounted to EUR 243 million. In annual terms, the current deficit widened by about 41%. The deepening of the current deficit is largely driven by the widening of the deficit commodity trader — reflecting an increase in import spending and a decline in exports. At the

same time, the expansion of the negative balance of primary income and the fall in the surplus in secondary income has supported the deepening of the current deficit. The trade deficit (goods and services) expanded by about 13% to 406 million euro. Net inflow to the financial account (excluding reserve assets) stands at 289 million and fully covers the current deficit. Net inflows into the account finances are supported by the expansion of net liabilities in the form of investments direct investment, as well as the net positive flow of other investment liabilities. Reflecting the current account performance and developments in the capital and financial account, reserve assets fell by about EUR 71 million to EUR 3,353 million, enough to cover 6.8 months of imports of goods and services. In annual terms, financial transactions during the period resulted in the expansion of Albania's financial liability to the world by about 96%. The exposure rate of the Albanian economy is estimated at 226 million euros, rising with 72m euros down on the level a year ago.

Figure 3.22 Total Expenditure



Source: Bank of Albania ⁸⁹

During the period, the volume of current transactions amounted to EUR 2,610 million, up by about 7%. The current account deficit is estimated at 243 million euros, about 41% higher than a year earlier.

The deepening of the current deficit reflects the widening of the trade deficit of goods and the negative balance of primary income, as a result of the increasing repatriation of profits and dividends.

The trade deficit deepened by about 13% in annual terms, as a result of both the increase in imports and the decline in exports. The increase in the import of goods is a result of the high flows of imports of minerals, fuels and energy and products

⁸⁹ See Bank of Albania Report of 2019

of the chemical industry. Meanwhile, the decline in commodity exports is dictated by the decline in electricity and base metal exports.

Meanwhile, the trade surplus in services expanded by 13%, mainly due to increased inflows to "processing services" and "other business services" as well as the contraction of payments made by the government in the form of technical assistance (services). Government).

The trade deficit in goods and services expanded by about 13% to EUR 406 million⁹⁰.

During the period, about 90% of current expenditures³ went to finance imports of goods and services, while foreign currency inflows⁴ were mainly provided by exports of services (at 57%) and of commodities and secondary income (together for about 36%).

3.2.4 Labour Market

The analysis of this report is based on various sources of information. The reason for using all official data sources is because of the differences that non-existent sources and at the same time due to the fact that the different time frequencies refer to them. It is important to note that two different sources of information are used in assessing labour market indicators in Albania; the first source refers to the data

⁹⁰ See INSTAT data of 2019

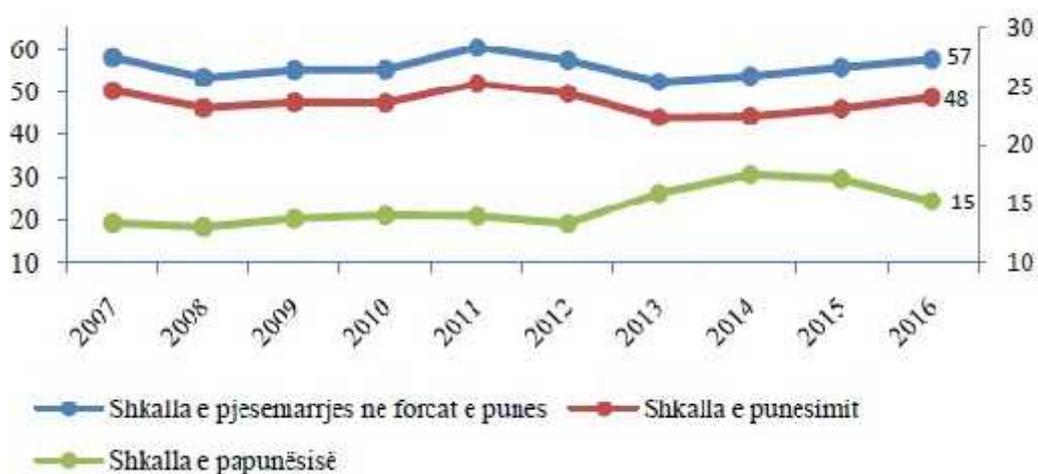
collected through the Labour Force Survey (LFS) which produced the first results in 2007 with annual frequency, and from 2012 also with quarterly frequency and the second source is the administrative data which are Available earlier since 2000. Earlier information is also available in World Bank (Development Indicators) data, which have been available since 1990 on an annual basis. Until 2000, these data are only available from estimates of the International Labour Organization (ILO), and after 2000, estimates from the Institute of Statistics of Albania (INSTAT) are included. The differences between the INSTAT and ILO estimates, which are included in the World Bank Development Indicators for the potential comparative period, are very small and the use of ILO-calculated data can be considered for the historical analysis of the Albanian labour market.

As transitional countries are often characterized by low utilization of job placement offices, compared to other forms, especially in the concept of recognition, there is often a significant difference between administrative and survey assessments. This phenomenon is well known in the country and therefore the use of AFP-representative data for the analysis of the domestic labour market.

Referring to the AFSA data, the labour force participation rate follows an almost constant trend throughout 2007–2016. In 2007, participation was about 58% of able-bodied individuals, reaching their peak level in 2011, at around 60%, then down to 57% in 2016. The unemployment rate has maintained an almost constant trend over the years 2007–2012, in the range of 13% –14% and then started to

increase, reaching a maximum in 2014 of 17.5% to start a downward trend again and in 2016 it reached 15%.

Figure 3.23 Employment And Unemployment Rates By Gender

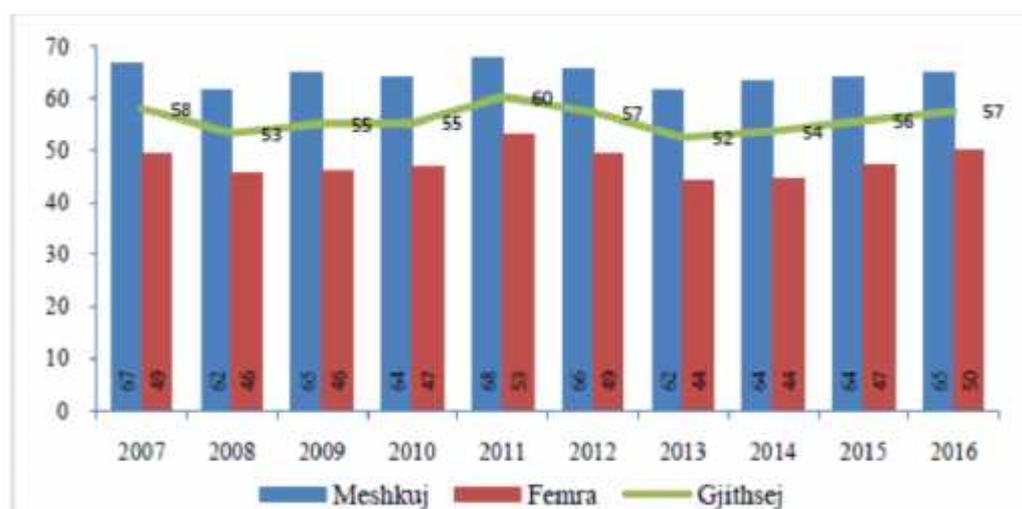


According to INSTAT's "Labour Market 2016" report, a large proportion of the Albanian population is economically inactive, with only 2016 accounting for 33.8% of the 15-64 age group, of which 37.2% are dominated by 10.7% of this age group for 2016 do not look for work because they think there is no available job for them. However, for this age group there seem to be other more important reasons not to be part of the labour market, where for 2016, 20% of them were inactive due to

fulfilling their family duties and responsibilities, while 27.7% of them for other reasons⁹¹.

The trend for labour force participation by gender has been in line with that of the population, but there has been a higher rate of male participation throughout the period. Thus, women appear to be more attracted to the labour market than men. In 2007, the rate of labour force participation for males was 67% while for females 49%, a large gap that persisted throughout the years and in 2016 the male labour force participation rate was 65%, while for females 50%.

Figure 3.24 Employment by gender



Source: Instat⁹²

⁹¹ See <http://www.instat.gov.al/al/publications/librat/2017/tregu-i-pun%C3%ABs,-2016.aspx>

⁹² See <http://www.instat.gov.al/>

Even the participation rate by age group tends to be the same as that of the total population over the years analysed, but it is noted that the participation rate for the age group 15-29 results throughout the period with a relatively large difference below the age group 30 -64 years old. So young people make up a small number of the workforce compared to adults.

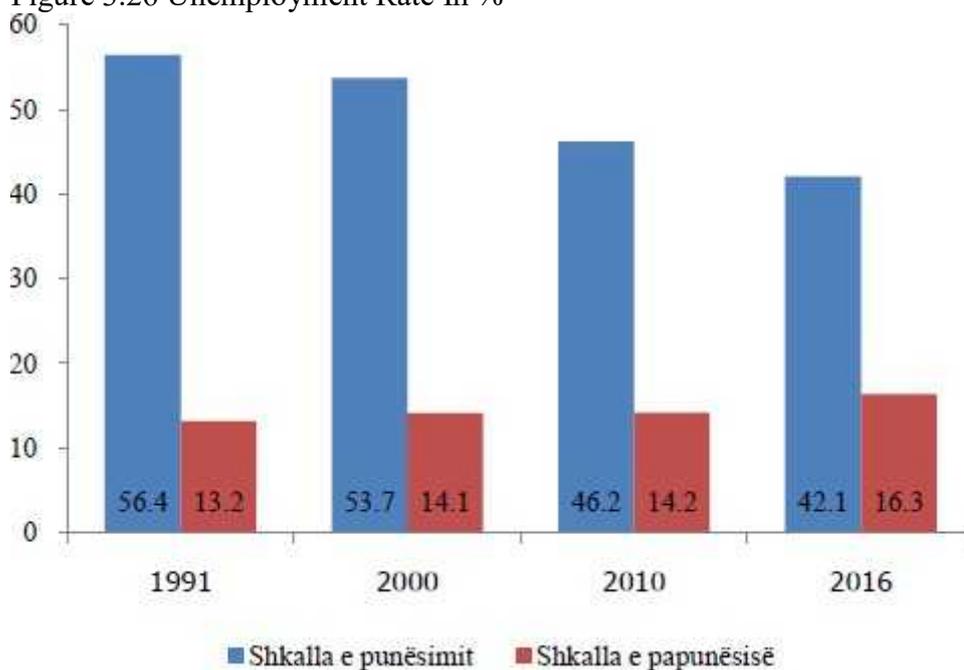
Thus, in 2017, the participation rate for the age group 15-29 was 50%, while the participation rate for the age group 30-64 was 76%, which is 26 percentage points higher. Over the years, the gap has changed little, but in 2016 the youth labour force participation rate has dropped to 46% while that of adults remains at 76%, further widening the gap.

Categorized by gender, the employment rate for women and men has followed the same trend as for total employees, but what is noted is that the employment rate for men results throughout the analysed period to be higher than for women, indicating that men are more active in the labour market. Regarding the division by age groups, it results that the highest number of employees is made up of persons aged 30-64. Moreover, with the decline of the rate of Overall employment in the period 2011-2013, the employment rate among the younger age group has dropped significantly more than that of adults. It can be said that young people find it more difficult to maintain a job than adults when total employment declines.

Based on the World Bank data for 2017, an analysis of employment and unemployment rates for 1991, 2000, 2010 and 2016 has been made. taken into

consideration. Compared to 2016 and 1991, the employment rate dropped from 56.4% to 42.1%, in other words, it dropped by over 25 percentage points.

Figure 3.26 Unemployment Rate In %



Source: Instat

The same cannot be said for the unemployment rate, which has experienced an upward trend over the years. From 2000 to 2010, this rate increased by only 0.7 percentage points. But in 2016, the unemployment rate reached 16.3%, the highest value for the years included in the analysis. The rise in the unemployment rate has been significant by comparing this indicator for 2016 with that of 1991, an increase of 23.5 percentage points. So, these data show that the rate of people actively seeking work but unable to find one has increased by 23.5 times during this quarter

century. The decline in the employment rate and the increase in the unemployment rate from 1991 to 2016 indicate that employment in the Albanian market has become a more problematic issue over the years, thus providing a strong signal for the need for market-oriented policies of labour, in order to increase the consistency between demand and supply of labour.

To have a fuller socio-economic picture, labour market analysis should also extend to the structures of jobseekers and unemployment benefit recipients. The chart below shows the performance of jobseekers in the years 2000-2016. The number of registered unemployed jobseekers has been steadily declining until 2008, while after this year this number has tended to remain the same, except for the last two years, where there has been an increase and then a decrease sensitive. On the other hand, it seems that the number of long-term unemployed job seekers has declined significantly over the years, especially after 2007, deepening the gap between registered and long-term job seekers. This can translate into a more efficient market, where labour supply and demand meet faster, reducing the time spent shifting from one job to another.

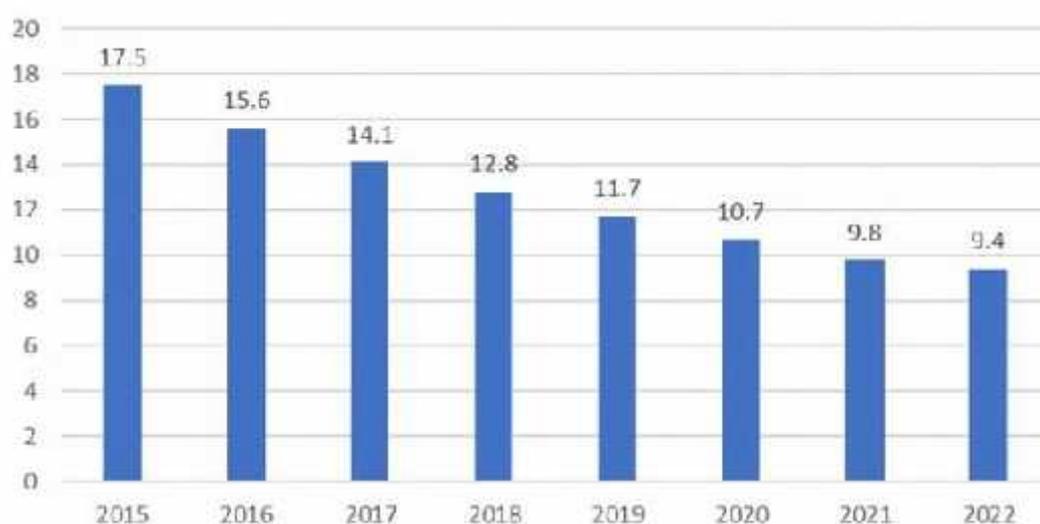
The unemployment rate is expected to decline by a percentage point this year, reaching 11.7% of total labour force in 2019, from 12.8% expected in 2018, according to the latest government forecasts.

The unemployment rate will continue to decline further to reach 9.4% in 2022.

According to the analysis of the Ministry of Finance and Economy, services are expected to contribute more to the growth of demand for labour compared to other sectors of the economy.

Despite the expected expansion of employment in the medium term, overall labour productivity is still expected to improve slightly over this period. Employment will also be on the right track with the unemployment rate falling. Employment is expected to grow at an average of about 2.4% per annum during 2020–2022.

Figure 3.27 Unemployment rate, actual and projections, 2019 -2022



Source: Instat and Ministry of Finance 2019⁹³

⁹³ See Ministry Of Finance 2019

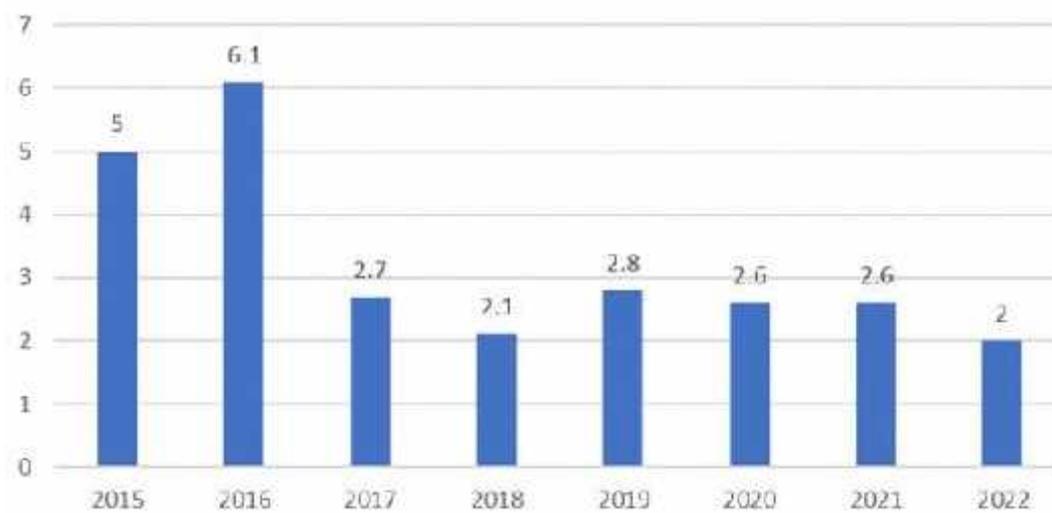
The higher labour force participation rate will be the main driver of the increase in the labour supply. While the increase in demand for labour is expected to reflect the same structure of the aggregate supply perspective of economic activity.

Referring to the quarterly labour force survey by INSTAT⁹⁴, employment by the third quarter of 2017 increased by 1.3% compared to the same quarter a year earlier, or by about 14.4 thousand newly employed for a year. Most of the employments belong to the public sector.

The unemployment rate (for the age group of 15-64 years) has continued its downward trend since Q1 2014 where it recorded its highest value of 18%, now down to 14% in Q3-2017, with a decrease by 1.2 percentage points from a year earlier (Q3-2016), or by a reduction in the number of unemployed persons by about 16.3 thousand in the one year period. Meanwhile, for the age group of 15 years and over, the unemployment rate during the third quarter of 2017 recorded a level of 13.6%. During 2018, the regions of Vlora, Tirana and Lezha had the highest unemployment rates compared to the national average. While in Dibra and Korça in 2018 were the regions with the lowest unemployment rates compared to the average.

⁹⁴ See INSTAT

Figure 3.28 Projections of annual employment growth, 2019 - 2020



Source: Instat Bank of Albania⁹⁵

⁹⁵ See Instat and Bank of Albania 2019

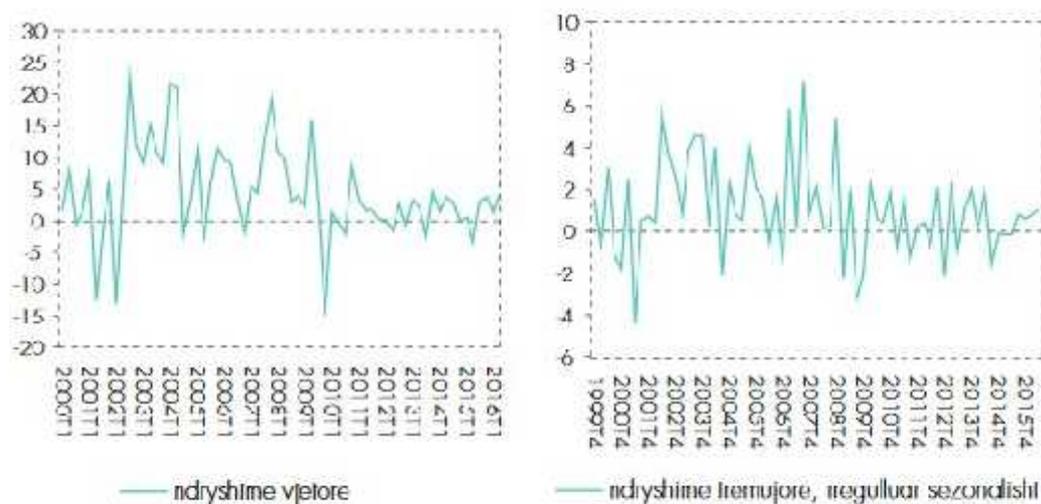
3.2.5 Consumption

For the creation of the database, series of real economy, fiscal sector, financial sector, foreign trade, as well as series of confidence surveys were reviewed. Their choice was guided by the economic linkage, the way national accounts are constructed, as well as the analysis of linkage strength by correlation coefficients. The quantitative indicators turned into annual changes, except for the interest rates, which were maintained at level 3. Qualitative indicators from the surveys and the uncertainty indicator were kept at a level because previous studies at the Bank of Albania have found that they are related to annual changes in economic growth. All series with a small correlation coefficient with annual changes of private consumption and private investment were put aside. Subsequently, after testing the linear linkage and the explanatory power in the models used, a good portion of the series were also removed, retaining those series which had the closest link.

Private consumption is available on a quarterly basis, starting in 2009. The real private consumption series for the period 2009-2016 is sourced from INSTAT⁹⁶. For the period 1999-2008, annual private consumption has been disaggregated into quarterly frequency series, using the dynamics of the retail trade index.

⁹⁶ See Instat 2016.

Figure 3.29 Private consumption



Source: Instat

Quantitative data with monthly frequency is: import of foodstuffs, from foreign trade data; value added tax income; and bank lending to individuals. Once transformed depending on whether they are stock or inflow, they are used in the first model, the bridging one. The quantitative data with quarterly frequency is only the salary fund index and is based on INSTAT⁹⁷'s publication "Short-term Statistics of Economic Enterprises"

Survey data are: the indicator of confidence in trade, services and consumers, and the indicator of uncertainty. Starting in 2016, confidence indicators are available on

⁹⁷ See Instat 2015

a monthly basis. Based on the lending survey, the balance of households' demand for loans is estimated, as estimated by bank experts. This series has a quarterly frequency. The uncertainty indicator is constructed based on the disaggregated consumer confidence survey data.

Some of the short-term indicators that were left out of the models and could be tested for a second time are: income from remittances, credit interest rates, exchange rate, inflation rate, import data car loans and household loan standards.

Conclusions

In conclusion, we can most certainly say that international organizations have had a very positive role in the economic development of Albania, and not only, since their assistance covered also the social development aspect of the country.

However, I would like to break down bit by bit my conclusions in the following pages.

If I refer to the first decade of the transition, 1990-2000, given the results of the first phase of the Albanian economic transformation, some conclusions can be reached. First, political instability was ultimately a powerful determinant of the path to economic transition. Secondly, it was understood that to run at a rapid pace without a specific strategy, especially in the case of Albania, would further aggravate the situation. Third, it was difficult to find the right direction and fit for the country's economy in terms of ideological clashes both inside and outside the political party campus. Finally, the inexperience and difficulties inherited from the past exacerbated the instability of the situation. However, the 90s, were years of consecutive crisis (regime change, 1997 pyramid schemes, 1998 attempt of coup d'état, 1999 refugees of Kosovo settling in Albania) which obviously had their negative effects on the progress achieved.

From the 2000 and on, the situation changed in Albania and so did the approach of the international organizations. There were real programmes and strategies to address issues in the development of the country and to guide future developments. They would raise the bar with the requirements and standards to be achieved by the Albanian Governments year by year.

Even though, there is no denying that Albania has come a long way since the 2000 (year when we can begin speaking of real developments in country, since the '90s were years of transition) there are still issues that need to be addressed for the economy to finally take off and be self-reliant.

The main reason why development has been holding back is the political instability. The unwillingness of politicians to cooperate with each other to continue with the implementation of reforms, such as the judiciary reform, have led the country to be perceived as unsafe, therefore unable to attract Foreign Direct Investments which would be very beneficiary for the economy.

Another issue is the inefficient public administration. Even though there have been constant investments and assistance from the International Organizations to develop and modernize the public administration, there is still a lot to be done. The public administration is still corrupted, inadequate which leads to inability to perform well, collect taxes and/or give feedback to improve the system.

Informal sector has been a problem in the development of the country since the early 1990 and it still is present nowadays. Stronger measures should be taken to

combat this phenomenon along side with tax evasion. Dealing properly with these issues would ensure the country to have healthy budget.

As explained in the second chapter, International Organizations gave their assistance in all aspects of development of the country, and acknowledged as high potential of development in Albania the sector of tourism. There have been done investments in this sector and more should be done. It would be beneficial if the government recognized this sector as a priority sector and planning future development programmes around this priority. There should be more investments to offer better infrastructure, to clean and maintain tourist areas. It is crucial to have a programme for the development of tourism, a strategy which should be break daown into yearly action plans to be able to achieve real and measurable results. This programme should be accompanied by an adequate fiscal policy to give the possibility not only big enterprises to thrive in this sector (the big tax payers), but most importantly small and medium enterprises. SMEs are not the biggest tax payers, but their contribution to employment, innovation, diversity and economic growth is crucial. Last but not least, the short history laid out in the first chapter, wasn't purposeless. The purpose was not only to explain how economy changed throughout the years, but also to show the political choices my country made. Poor political choices at the end of WWII, resulted in the gradual isolation until it was total isolation by the

end of '70s. Alone without any strategic partner, the economy degraded and population left poor.

The changes in political regime and the events that followed are the most important progress that my country has made so far, and for sure a path that should continue.

The vision to be member of the European Union, is a certainty that not only actual issues will be overcome but ultimately will become a prosperous and thriving economy.

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