

ECONOMIC
BULLETIN J u n e
2 0 0 7

B a n k o f A l b a n i a

*If you use data from this publication, you are requested to cite the source.
Published by: Bank of Albania, Sheshi "Skënderbej", Nr. 1, Tirana, Albania
Tel.: 355-4-222230; 235568; 235569
Fax.: 355-4-223558
E-mail: public@bankofalbania.org*

www.bankofalbania.org

*Printed by: Bank of Albania Printing House
Printed in: 360 copies*

C O N T E N T S

| | |
|--|-----|
| <i>Review of monetary policy in the first semester of 2007</i> | 7 |
| <i>Interview by Mr. Ardian Fullani, Governor of the Bank of Albania to Voice of America during the Spring Meetings of the World Bank and the International Monetary Fund, Press office, April 19, 2007</i> | 51 |
| <i>Speech by Mr. Ardian Fullani, Governor of the Bank of Albania At the presentation of the 2006 Annual Report of the Bank of Albania before the Economy and Finance Commission of the Parliament of the Republic of Albania Tirana, 25 April 2007</i> | 53 |
| <i>Speech by Mr. Ardian Fullani, Governor of the Bank of Albania At the seminar "Catching-up in South East Europe: The Role of the Financial Sector", "Tirana International" Hotel, 3 May 2007</i> | 71 |
| <i>Speech by Mr. Ardian Fullani, Governor of the Bank of Albania At press release with the IMF Mission and the Ministry of Finance at the end of the IMF Mission in Tirana. Tirana, 8 May 2007</i> | 73 |
| <i>Speech by Mr. Ardian Fullani, Governor of the Bank of Albania At the award ceremony by the President of the Italian Republic, His Excellency Giorgio Napolitano with the Order of the Star of Italian Solidarity Tirana, 7 June 2007</i> | 75 |
| <i>Interview by Mr. Ardian Fullani, Governor of the Bank of Albania To "Klan" magazine. Tirana, 23 June 2007</i> | 77 |
| <i>Speech by Mr. Ardian Fullani, Governor of the Bank of Albania At the press conference on the decision of the Supervisory Council of the Bank of Albania on raising the key interest rate by 0.25 per cent. Tirana, 27 June 2007</i> | 82 |
| <i>New Law "On Banks" and its compliance with the supervisory regulatory framework. Obligations for regulatory changes in the implementation of the Directives of the European Union. June 2007</i> | 84 |
| <i>The new Law No. 9662, dated 18 December 2006 "On banks in the Republic of Albania"</i> | 103 |
| <i>Lending activity: The absence and the advantages of a crucial development factor</i> | 108 |
| <i>Bank of Albania news over April-June 2007</i> | 128 |
| <i>Legal events over April-June 2007</i> | 131 |
| <i>Bank of Albania management, 30 June 2007</i> | 135 |
| <i>List of all entities licensed by the Bank of Albania</i> | 136 |
| <i>Banks and branches of foreign banks</i> | 136 |
| <i>Non-bank institutions</i> | 139 |
| <i>Foreign exchange bureaus</i> | 140 |
| <i>Unions of savings and credit associations</i> | 146 |
| <i>Savings and credit associations</i> | 147 |
| <i>Representative offices of foreign banks</i> | 157 |

T A B L E S

Review of monetary policy in the first semester of 2007

| | | |
|---------|--|----|
| Table 1 | Some main economic indicators in annual terms (in percentage) | 10 |
| Table 2 | Some main indicators of regional countries | 12 |
| Table 3 | Indicators of rail, sea and road transportation | 17 |
| Table 4 | Annual growth rates of fiscal indicators during the first 5-month period (in percentage) | 18 |
| Table 5 | Labour market indicators (in thousands of people) | 20 |
| Table 6 | Annual inflation rates by main groups | 25 |
| Table 7 | Realization of the Bank of Albania quantitative objectives | 31 |
| Table 8 | Intermediation cost in ALL | 41 |
| Table 9 | Main macroeconomic indicators | 43 |

Statistical annex

| | | |
|----------|---|----|
| Table 1 | Annual inflation rate (in percentage) | 47 |
| Table 2 | Contribution of basket constituent groups to total inflation | 47 |
| Table 3 | Performance of monetary indicators (in billions of ALL) | 47 |
| Table 4 | Performance of NFA indicators by main groups, May 2007 (in millions of USD) | 48 |
| Table 5 | Performance of Net Credit to the Government by main groups | 48 |
| Table 6 | Performance of some main indicators | 48 |
| Table 7 | Outstanding credit indicators as a share to total | 48 |
| Table 8 | New credit indicators as a share to total | 48 |
| Table 9 | Distribution of credit by sectors of economy (in percentage to total) | 49 |
| Table 10 | End-month interest rates and their change compared with previous periods (in percentage points) | 49 |
| Table 11 | Interest rates and their change in the lek deposits and credit market (in percentage points) | 49 |
| Table 12 | Interest rates of deposits denominated in foreign currency (in percentage points) | 50 |
| Table 13 | Interest rates of credit denominated in foreign currency (in percentage points) | 50 |

Lending activity: The absence and the advantages of a crucial development factor

| | | |
|---------|---|-----|
| Table 1 | Loan structure according to allocation in economy (in % to total portfolio) | 110 |
| Table 2 | Some macroeconomic indicators | 111 |
| Table 3 | Number of licenses for banks (after 1997) | 113 |
| Table 4 | Banking system financial indicators | 113 |
| Table 5 | Credit structure by currency (in % of credit portfolio) | 114 |
| Table 6 | Credit distribution by economic sectors (in % of credit portfolio) | 114 |
| Table 7 | Deposits structure by currencies (in % of credit portfolio) | 115 |

C H A R T S

| | |
|---|---|
| Review of monetary policy in the first semester of 2007 | |
| Chart 1 | USD/EUR spot exchange rate and the nominal effective exchange rate of the euro and the dollar 12 |
| Chart 2 | Price performance of one crude oil barrel (in USD) 13 |
| Chart 3 | Sales growth and contribution by sectors (in percentage) 14 |
| Chart 4 | Contribution of industrial sub-sectors to the annual growth of industry 15 |
| Chart 5 | Energy sources and uses by constituent items in GWH 15 |
| Chart 6 | Annual growth of construction cost index, house price index and sales index (in %) 16 |
| Chart 7 | Contribution of sub-sectors to the annual growth of services (in %) 17 |
| Chart 8 | Annual change of total agricultural production by sectors (in %) 18 |
| Chart 9 | Annual change of imports and exports of unprocessed agricultural products (in %) 18 |
| Chart 10 | Main fiscal indicators for January-May (in billions of ALL) 19 |
| Chart 11 | Contribution of main items to the annual growth of income (left) and of expenses (right) for the 5-month period (2004-2007) (in %) 19 |
| Chart 12 | Cumulative financing of budget deficit, January 2002 - May 2007 (in billions of ALL) 20 |
| Chart 13 | Number of unemployed (left) and unemployment rate (right) 20 |
| Chart 14 | Current deficit and balance of payments as a share to GDP 22 |
| Chart 15 | Total imports and exports and imports by three purposes of use (in millions of EUR) 23 |
| Chart 16 | Annual inflation (in percentage) 24 |
| Chart 17 | Contribution of main items to annual inflation (in percentage) 24 |
| Chart 18 | Annual inflation of "Processed foodstuffs" and "Unprocessed foodstuffs" 25 |
| Chart 19 | Annual inflation rates of "Housing" and "Administered prices" 26 |
| Chart 20 | Annual inflation rates of "Durable consumer goods" and "Services" 26 |
| Chart 21 | Annual inflation rates of "Non-foodstuff consumer goods" 27 |
| Chart 22 | Annual rate and linear trends of core and total inflation (in percentage) 28 |
| Chart 23 | Annual rates and inflation linear trends of tradable and untradable goods (in percentage) 29 |
| Chart 24 | Performance of core inflation rate 31 |
| Chart 25 | Annual growth of monetary aggregates 32 |
| Chart 26 | M3 and credit to economy annual growth (in billions of ALL) 32 |
| Chart 27 | Annual growth of real M3 (left) and of net Government borrowing in real terms 33 |
| Chart 28 | Share of deposits in foreign currency and of currency outside banks to M3 33 |
| Chart 29 | Contribution of demand for money constituents to M3 annual growth 34 |
| Chart 30 | Performance of lending activity 36 |
| Chart 31 | Annual growth performance of credit by currency 36 |
| Chart 32 | Composition of businesses and households' portfolio by purpose of credit use 37 |
| Chart 33 | Net foreign assets of the banking system (in millions of USD) 38 |
| Chart 34 | Gross financing of budget deficit (in billions of ALL) 38 |
| Chart 35 | Short-term (left) and long-term (right) interest rates 39 |
| Chart 36 | Interest rates in the interbank market and BoA's standing facilities 40 |
| Chart 37 | Securities' yield in the primary market 40 |
| Chart 38 | Interest rates of up to 1 year maturity term in Albania and the Euro area 41 |
| Chart 39 | Annual changes of ALL in nominal effective terms (NEER) 41 |
| Chart 40 | Daily performance of ALL/EUR and ALL/USD 42 |
| Chart 41 | ALL exchange volatility in quarters 42 |

REVIEW OF MONETARY POLICY IN THE FIRST SEMESTER OF 2007

1 GOVERNOR'S SPEECH

The first semester of 2007 marked a positive performance of the Albanian economy in terms of being in line with the projected economic growth rate, of further consolidating the macroeconomic stability and carrying on with the structural reforms in economy. The economic development has been along the lines of the projected framework in the country's economic development programme, observing the main objectives of the three-year programme and achieving a further milestone towards the economic and financial integration with the regional and international markets. Alongside, some specific developments over this period have raised the need for continuous attention to potential risks and for designing and implementing preventive policies in due time, in order to guarantee the country's economic balances and its long-term development.

Judging on the available information, the Bank of Albania observes that the economic development has been in line with the projections of the beginning of the year which projected an economic growth of 6 per cent. The economic growth has been driven by both domestic demand for goods and services and external demand. It reflects the expansion of economic activity in services, transportation and industry, while construction has recorded a relative slowdown, among others as a result of the reduction in extending construction permits. Despite the expected seasonal slowdown, the sales index increased by 14 per cent over the first quarter of 2007. Economic growth has been reflected in other indicators as well, such as the increase of retail sales in economy, the increase of tax income, the growth of exports, the increase of the level of capacities utilization in economy and of employment. The expansion of economic activity has been also perceived by the Albanian businesses and consumer, who have generally provided positive opinions on the performance of economy over the first quarter and are quite optimistic about the economic activity performance over the second quarter.

The economic activity over this period has been mainly driven by the increase of domestic demand which was reflected in the increase of consumption and investment in economy. The growth of demand for goods and services has been fuelled by the growth of credit to economy and by the monetary conditions, which remain stimulating for the economic activity. Moreover, the consolidation of macroeconomic stability has had a positive influence on the economic activity through the extension of the business plans time horizon and the mitigation of Albanian household consumption cycle. These factors have affected the maintenance of high credit rates to the private sector. At end of May, this type of credit amounted to ALL 228 billion or to 24.6 per cent of the GDP projected

for 2007, confirming as such its role as the main consumer of the Albanian economy funds. In addition, the external demand for Albanian products has grown, causing the Albanian exports to increase by 26 per cent over the first quarter of 2007. The overall world environment which was characterized by satisfactory growth rates in our main partners – the Euro area and the regional countries – has favoured the expansion of the Albanian exports.

Fiscal sector activity during the first semester is characterized by the increase of income and expenses, as well as the creation of fiscal excess as a result of unrealized capital expenses' execution. The main fiscal indicators continued to have positive trends, but with slower annual growth rates compared with the previous year. Based on the data provided by the Ministry of Finance, as of end May were collected 95.6 per cent of projected income and were executed 83 per cent of planned expenses. Fiscal activity did not exert any pressures on domestic demand over the first semester; however, the change of fiscal performance in the second semester of the year as a result of the concentration of budget expenses and public borrowing may push the presence of inflationary pressures and the possible fluctuations in the money market over this period.

The growth of domestic demand was followed by the deepening of current deficit over the first semester of 2007 in the presence of the rapid growth of exports and imports. Current deficit recorded an annual growth of about 40 per cent over the first quarter, mainly as a result of the increase of imports by 22 per cent and of the trade deficit in goods by about 25 per cent. Imports for intermediate consumption grew more compared with other categories, while the increase of investment-oriented imports continued to remain stable. Worth to be mentioned in terms of the external sector development is the increasing coverage of current expenses with capital income, which provides evidence that our country is being oriented towards the financing of current deficit with long-term capital inflows and foreign investments.

Despite the growing demand over the first semester, the pressures on the overall level of prices have been low, as a result of the favourable supply-side developments. The annual growth in the overall consumer prices level over the first semester fluctuated at around 2.3 per cent, while annual inflation marked 2 per cent in June 2007. The highest increasing rates in prices were displayed in processed foodstuffs, in housing services and in goods and services with administered prices. Consumer goods inflation was considerably affected by temporary seasonal factors which act downward and from a relative balance between supply and demand. On the supply-side, the positive influence of domestic agricultural production on inflation was more dominant than the high oil prices effect, while wages did not increase significantly and the inflationary expectations remained anchored around the Bank of Albania target. On the demand-side, the current monetary conditions have resulted to have been adequate to contain inflation in this period.

The performance of money supply indicators has displayed the high demand for monetary assets during 2007. Money supply recorded an

average annual growth of about 17.5 per cent during 2007. The annual growth of M2 aggregate fluctuated around 12 per cent compared with the average growth rates of about 7-8 per cent during the second semester of the previous year. In annual and foreign currency structure terms of money supply, the performance of M2 aggregate to M3 growth reflects the creation of foreign currency monetary assets in the private sector of economy. The annual expansion rates of monetary base in economy have had a stable performance of about 10-12 per cent.

Notwithstanding this setting, the analysis of the current and expected economic developments suggests that the inflationary pressures may increase in the medium run. The growth of domestic demand in economy, the current expansion tendency of imports and the current deficit deepening, the rapid growth of monetary assets in economy and the presence of potential risks in the expected dynamics of inflationary pressures pushed the Bank of Albania to tighten its monetary policy in June through the increase of the core interest rate by 25 basis points. Starting from 28 June the core interest rate applied on the repurchase agreements is 5.75 per cent. By means of this growth, the Bank of Albania aims to stabilize the inflationary expectations through the minimization of potential risks on the monetary and macroeconomic balance. The transmission of this signal to the financial markets will bring about the re-balancing of the current upward tendency of domestic demand in favour of financing the stable growth of economy in the long run.

Through the management of liquidity, the Bank of Albania monetary operations have aimed to minimize the interest rates fluctuations in the financial markets, in line with its long-term policy. In compliance with this policy and depending on the fluctuations of the banking system liquidity, the Bank of Albania has used the one-week repo operations, both by injecting and withdrawing the liquidity to signal its policy, and one- and three-month repos for the structural management of liquidity in the system. The excess liquidity and the downward tendency of interest rates caused the Bank of Albania to withdraw the liquidity in the second quarter. Meanwhile, the same logic but applied under the conditions of the absence of liquidity in the second quarter caused the Bank of Albania to inject liquidity in this period. These interventions allowed the reduction of interest rates fluctuations and the observation of the quantitative objectives of the Bank of Albania. In the foreign currency market, the exchange rate resulted to be relatively stable with a slight depreciating tendency in the first quarter. Meanwhile, the lek appreciated to the American dollar in the second quarter and it was relatively stable to the euro. The Bank of Albania was present in the foreign currency market in order to stabilize the short-term fluctuations in this market.

In conclusion, I would like to re-emphasize that the macroeconomic developments over 2007 had a positive performance in terms of economic growth and macroeconomic stability, mainly owing to the dynamics of the private sector. Moreover, this period identified a number of structural deficiencies in economy, among which the solution of the energy situation

and the provision of energy supply are of primary importance. The quick and final solution of this issue will spur the achievement of the projected economic growth rates. The good rate at the end of the country's risk assessment process assigned by the well-known Moody agency will lead Albania to the international financial markets and make it access funds which will support the country's needs for development. However, this borrowing requires the formulation of strategic and consistent development plans in order to guarantee the efficient and prioritized use of funds. Moreover, it requires the maintenance of domestic macroeconomic balances, which guarantee the foreign investors and drop Albania's borrowing cost. In the context of economic policies, the assurance of macroeconomic stability will be our future challenge, under the conditions of inflationary pressures expansion and current deficit deepening. This challenge will require the commitment of both core economic policies, the monetary and fiscal policy, and their co-ordination not only during the formulation stage, but also through the implementation over the financial year. The Bank of Albania remains committed to take the proper policy and regulatory measures, which will assure the observation of its legal objective and the maintenance of financial stability.

2 WORLD ECONOMY

Global economic activity is still in a fast developing momentum as recorded during 2007's first months. The high and constant growth of some developing economies has been the main engine to fuel world economic activity. Meanwhile, economic activity in some developed countries is expected to slow down, reflecting to a large extent the under capacity growth of the American economy. Euro area economies show to be an exception to this prospect, due to the fact that its economies continue to record positive developments based on foreign and domestic demand.

The constant economic growth on a global level during these last four years has triggered improvements in capacity utilization from the businesses and it has improved the advancement in the labour market. The high level of production capacity utilization for a relatively long period has triggered a general lift in core inflation resulting in the tightening of monetary policy in a number of central banks. The constant economic activity growth has influenced consumption and oil prices as well. The world price index for raw materials¹ has recorded an increasing trend for the month of May reaching the highest level recorded during the last nine months. Especially important for the increase in these products' prices is the high level of Chinese economic growth and its strong demand for natural resources.

Table 1 Some main economic indicators in annual terms (in percentage)

| | GDP annual growth, Q1 | Unemployment rate, May | CPI, May |
|-----------|-----------------------|------------------------|----------|
| USA | +1.9 | 4.5 | 2.4 |
| Euro area | +3.0 | 7.0 | 1.9 |
| Germany | +3.6 | 6.6 | 2.0 |
| France | +2.0 | 8.7 | 1.2 |

| | | | |
|-------|------|------|-------|
| Italy | +2.3 | 6.2* | 1.9 |
| Japan | +2.2 | 3.8 | - 0.2 |

*For March.

Source: Eurostat; ECB, Report for June; Bureau of Economic Research, Department of Commerce, USA

EURO AREA ECONOMY

Euro area economy recorded a 3 per cent growth in annual terms during the first quarter of 2007 and short-term indicators suggest stable growth for the remaining of the year. Economic growth has been strongly supported by domestic and foreign demand. The macroeconomic environment has triggered the continuous improvement of the labour market and conclusively has influenced private consumption. High investment returns, favourable financing terms and the high level of capacity utilization have supported corporate investments. Positive future expectations are based on different indicators resulting from different actors in the European economy.²

Starting from December 2006, the European Central Bank has started to pursue a tighter monetary policy with the intention to anchor the medium-term inflation expectations with price stability. Fluctuations in oil prices, the increased VAT in Germany and pressures resulting from the high economic activity have increased the mid-term risks associated with inflationary expectations. In their monetary policy meeting in June, the Governing Council of the ECB decided to raise the key interest by 0.25 per cent to 4 per cent.

USA ECONOMY

US economy finds itself in a transition period. After a long period of high economic growth, the American economy has shown a relative slowdown since the second half of 2006. During the first quarter, it recorded a 2 per cent annual GDP growth from 3 per cent recorded the previous period. The economic slowdown is related to the lack of investments, demand in the real estate market, net exports and inventories. The slowdown in construction and housing market has not been significantly reflected in the performance of the sectors of economy. Employment has recorded a continuous growth, since the dropping in the number of job opportunities in construction has been offset by the available job opportunities in other sectors of economy.

Core inflation continues to be over the desired level and unemployment is lower than the steady level. Under these conditions, the Federal Reserve has decided to keep the key interest rate unchanged at 5.25 per cent since June 2006. For the period to come analysis show that the high efficiency and the slowdown of economic activity will balance the inflationary pressures in the economy.

ECONOMIES IN THE REGIONAL COUNTRIES

Regional economic development has recorded satisfactory levels for 2006 at an average of 5.1 per cent. Foreign direct investments have played a major role in this growth, being reflected in the positive influence on the privatization

process and business climate. However, economic growth is expected to slightly slow down during 2007 at 5 per cent. Domestic demand, mainly private consumption and investments, still remain the main sources for development in the region and furthermore foreign demand is expected to play an increasing role in the future. Expectations for 2008 suggest for an improvement in the average annual growth rate at 0.2 per cent.

The beginning of 2007 found some of the West Balkans³ countries in geopolitical turmoil being reflected directly in their economic development. Overall the resolution of Kosovo's final status has remained the major problem in the region. In the Former Yugoslav Republic of Macedonia the biggest Albanian ethnic party boycotted the parliament. Meanwhile the prolongation of the new government formation in Bosnia and Herzegovina and in Serbia, as well as the upcoming elections in Croatia, may influence these countries' economic performance.

Table 2 Some main indicators of regional countries

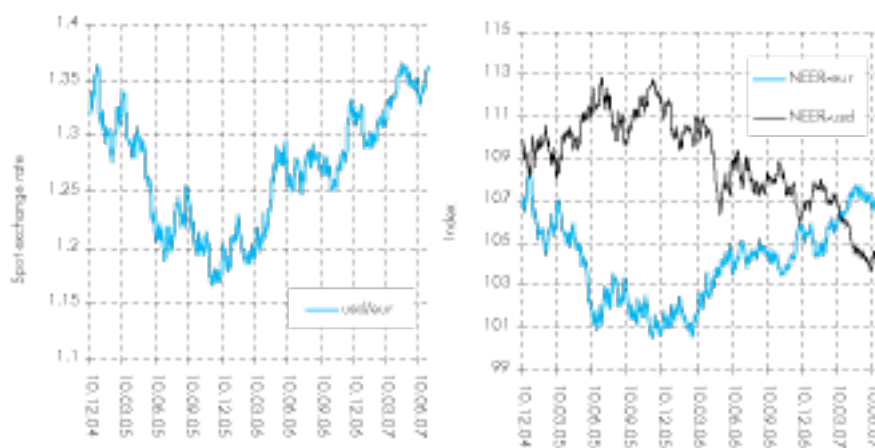
| Countries | GDP (in %) 2006 | CPI (in %) (in %) | Exchange rate: | | Interests (in % ⁴) | |
|-----------|--------------------|----------------------|----------------|-----------|--------------------------------|----------|
| | | | EUR | USD | Loans | Deposits |
| Kosovo | 3 | 0.3 (April) | -- | 1.35 | 13.72 | 3.4 |
| Greece | 4.4 | 2.6 (May) | -- | 1.35 | 4.06 | 3.74 |
| Italy | 1.9 | 1.5 (May) | -- | 1.35 | 4.95 | 2.42 |
| Macedonia | 4.0 | 1.0 (April) | 61.19 MKD | 45.59 MKD | 10.3 | 4.7 |
| Kroatia | 4.6 | 2.2 (May) | 7.31 Kn | 5.44 Kn | 7.44 | 4.13 |
| Serbia | 5.4 | 4.4 (May) | 80.73 CDS | 59.18 CDS | 13.01 | 4.60 |

Source: Central banks bulletins, IMF.

EXCHANGE RATE PERFORMANCE

The effective exchange rate of the EUR⁵ has continuously appreciated during the first months of 2007. To a great extent the appreciation of the European currency has come as result of fluctuations in the USD market. The appreciation of the EUR to the USD has been gradual and has started since the last quarter of 2006. On 25 April 2007, EUR appreciated to 1.36 USD reaching the highest exchange value in the history of these two currencies.

Chart 1 USD/EUR spot exchange rate and the nominal effective exchange rate of the euro and the dollar

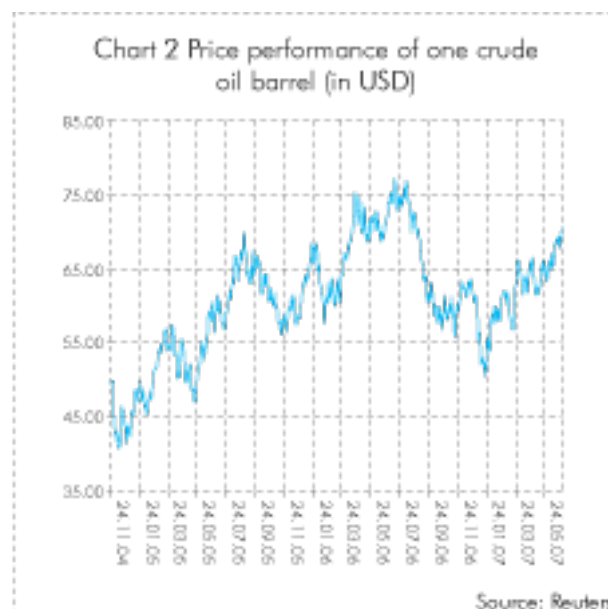


Source: ECB; Federal Reserve of USA

Positive developments in the Euro area economy and the moderate economic activity in the USA have positioned exchange markets expectations and the main tendency of the exchange rate between these two currencies.

OIL PRICE

Oil price has recorded a gradual increase since the beginning of 2007 and reached peak levels in June, when one barrel was sold for USD 71. The lack of coordination of the increasing demand, production and overcapacity of inventories placed in an unsafe geopolitical environment explains the performance of oil prices during these last months. Global demand for oil is expected to increase by 2 per cent for 2007, where developing countries are expected to double their demand compared with 2006. On the other side, there is still uncertainty in oil production from both OPEC and other countries. The International Energy Agency (IEA) observes that non-OPEC production will still be not sufficient and demand will be mainly satisfied by OPEC. In these conditions oil prices are expected to be high and to fluctuate, due to the uncertainty in demand and supply equilibriums and geopolitical risks.



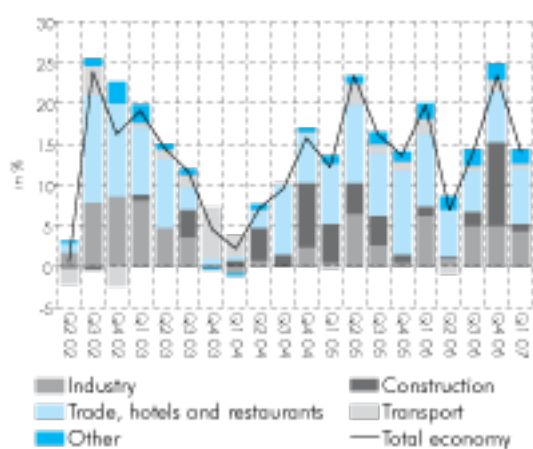
3 ALBANIAN ECONOMY IN THE FIRST SEMESTER

Albanian economy during the first semester of 2007 was characterized by a growing domestic demand which has been supported by the macroeconomic stability, economic growth, growth in salaries and wages and the favourable monetary conditions. This high demand is based on the credit expansion on both business and households, which is reflected in relatively low interest rates and the fast development of the banking system.

The increasing demand is reflected in a number of macroeconomic indicators such as, higher employment indicators, higher sales in different economic sectors and the deepening of trade deficit.

Based on the sales performance, production by sector is in comparative levels to those recorded during the first quarters of the last two years, where annual sales growth reached 14 per cent for the first quarter in 2007. Major contributions to sales' growth were provided by trade and services (hotels and restaurants), while industry has recorded higher sales levels compared with the last years. Demand for energy during the first semester in a limited production environment has been overcome with imported energy. Sales values recorded from the construction sector have remained relatively steady compared with the sales levels of last year. Annual growth in transportation and telecommunication remains modest. Analyses related to the agricultural sector suggest that annual growth will keep the same pace as that recorded during the last year.

Chart 3 Sales growth and contribution by sectors (in percentage)



Source: INSTAT and Bank of Albania estimations

During the first quarter of 2007, employment recorded an annual growth of 2000 people, while the unemployment rate continued to record a slight decrease from quarter to quarter ending at 13.6 per cent at the end of March. Current deficit recorded an annual growth of about 40 per cent during the first quarter mainly as a result of an increase in imports and the trade deficit in goods by about 25 per cent. Imports for intermediate consumption have recorded a higher increase compared to other imports' categories, while investment-oriented imports have remained steady. A main development related to the external sector is the decrease in the trend of covering current expenses with current income. During 2006 this ratio was recorded at around 85 per cent whereas during the first quarter of 2007 this ratio has been recorded at 80 per cent. The country is

moving towards financing current deficit through long-term capital and foreign investments. Another indicator that signals an increase in consumption is the retail market, which has recorded an increase of about 10 per cent during the first quarter and employment in these businesses has recorded an increase of 20 per cent.

During the first semester the fiscal sector was characterized by slow developments in the public expenses, mainly in capital expenses, not exerting pressure on demand growth. Fiscal results during the first five months of 2007 recorded a surplus of 2 per cent of GDP. This fiscal profile is expected to change during the second semester, which comes as a result of the concentration of expenses in the last months of the year and bringing about increases in the fiscal stimulus in economy.

Despite demand growth during the first semester it is observed that pressures on the overall price level have been low due to the favourable developments on the supply side. Annual growth of consumers' price level during the first semester has been observed at around 2.3 per cent, where the average growth rate was faster during the first quarter rather than during the second. Higher level of price rise has been observed in processed foodstuffs, accommodation services and in goods and services with administered prices. Monetary policy has been neutral during the first semester of 2007. However, the Bank of Albania has constantly underlined the growing risk in price stability due to the growing domestic demand and its influence on the fast growth of monetary assets in the economy. In these conditions, at the end of June the Bank increased the key interest rate by 0.25 per cent, reaching 5.75 per cent.

3.1 PRODUCTION BY SECTORS OF ECONOMY

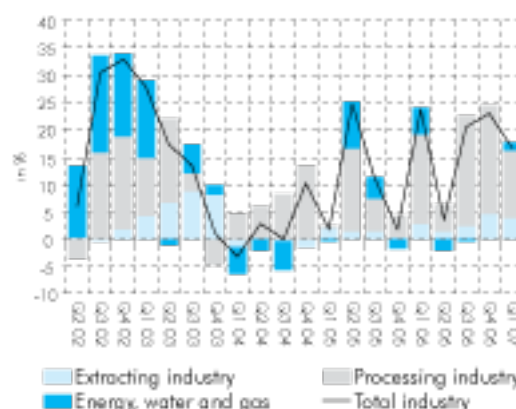
INDUSTRY AND ENERGY

Sales in the industry sector recorded an annual growth of 17 per cent during

the first quarter of 2007, which is close to last year's average. The annual contribution of this sector to total sales in economy was positive reaching around 4.4 per cent. In terms of quarterly changes, seasonal adjusted sales of industry have increased by 2 per cent during the first quarter of 2007 showing steady developments in the economic activity of this sector.

These developments were supported from both the extracting and processing sub-industries at respectively 4.1 per cent and 12.5 per cent. As a result of the gradual revival of the extracting industry's activity it has recorded a positive contribution to total sales in economy. The growth of exports has provided a considerable contribution to the sales of extracting industry. In annual terms the exporting volumes of the extracting industry have nearly doubled. The processing industry dominates the performance of sales in industry, providing about 64 per cent of sales and contributing by 17 per cent to the total sales in economy. The exporting activity of processing industry remains in the same levels as in the previous year. Around 30 per cent of sales in this industry were realized in the foreign market and this positive environment during the first quarter expressed in growing exports, employment and improvements in their financial situation as well as the growing business confidence in the industrial production sector.

Chart 4 Contribution of industrial sub-sectors to the annual growth of industry



(KESH) was obliged to increase power imports to five times the normal levels. Meanwhile power import levels have reached 1.4 billion kwh and it is expected that until the end of this year another 1 billion will be imported. The low production level and high import levels have negatively influenced the Albanian Electro-Energy Corporation's (KESH) financial balance.

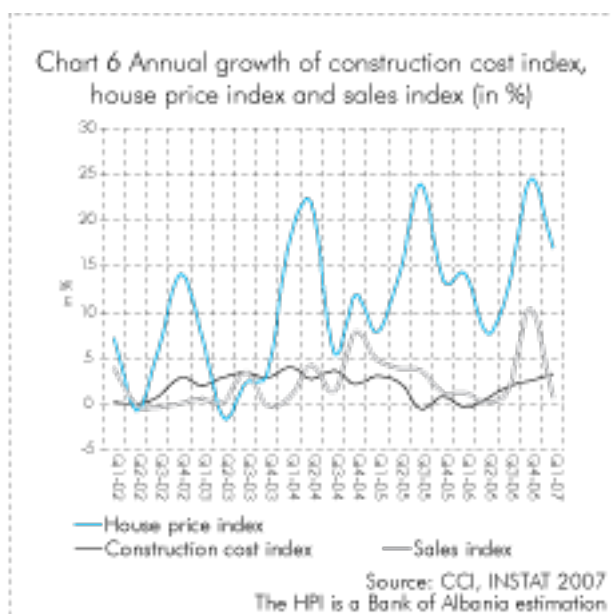
Household and non-household consumption has declined considerably during this period, being respectively 3.3 per cent and 1.9 per cent lower than the previous year. The administration measures taken by KESH influenced on the increase of collections, while the net losses recorded an annual decline by about 21 per cent. Despite the measures taken for the improvement of this situation, the Albanian Electro-Energy Corporation (KESH) informs that the limitations in power supply will still be present during the foreseeable future, stressing the importance of prioritizing direct intervention in power problems.

CONSTRUCTION

Official figures from sales volumes and the figures provided by the periodical surveys carried out by the Bank of Albania in cooperation with the construction firms show that construction activity in the country has experienced a sharp decline during the first quarter of this year, recording a 31 per cent decline in its contribution to total sales compared with the previous year. In terms of quarterly changes, the seasonally adjusted sales resulted about 40 per cent lower. It has been observed that the decline in granting construction permits

has strongly influenced the slowdown of this sector's activity, while demand on the other side is still high. This has been confirmed by the high positive figures in the balance for demand indicators resulting from construction companies' declarations during the business confidence survey.

The high demand level and the limited construction permits have resulted in high real estate prices. The annual growth rate of housing price index⁶ resulted at 17 per cent for the first quarter of 2007, otherwise expressed as some per cents higher than the last five years' average. On the other hand, annual growth rate of construction cost index was recorded at 3 per cent, a fact which shows that prices in construction are to a large extent led by the increase in the ratio of demand/supply rather than the increase in production costs.



SERVICES

Trade activity of hotels and restaurants (considered as the most important for the services sector), recorded continuous annual growth rates of sales volume for the fifth consecutive year. Nearly half of the total sales growth in the economy is provided by this sub-sector, where during the first quarter of 2007 the annual sales growth rate recorded 14.7 per cent. Trade activity follows this sub-sector, sharing 44 per cent of total sales in the economy.

Work volume in the retail market, as based on the Retail Market Index (INSTAT, 2007), shows positive annual growth at 11 per cent. In terms of the number of employed, this sector has contributed by 20 per cent. The above developments are indications that support the growth in consumption and domestic demand in the country for the relative periods.

The transportation sector during the first semester of 2007 recorded an annual growth of 49 per cent, pointing towards a positive reorientation of its downward trend of the last four quarters. Even though the share of this sub-sector to the total sales volume is small, its high annual growth contributed by about 1.6 per cent to the annual growth of sales in economy. Positive achievements were recorded in the seasonally adjusted sales at 14 per cent compared with the previous quarter. These developments are based on the data collected from sea and air transportation.

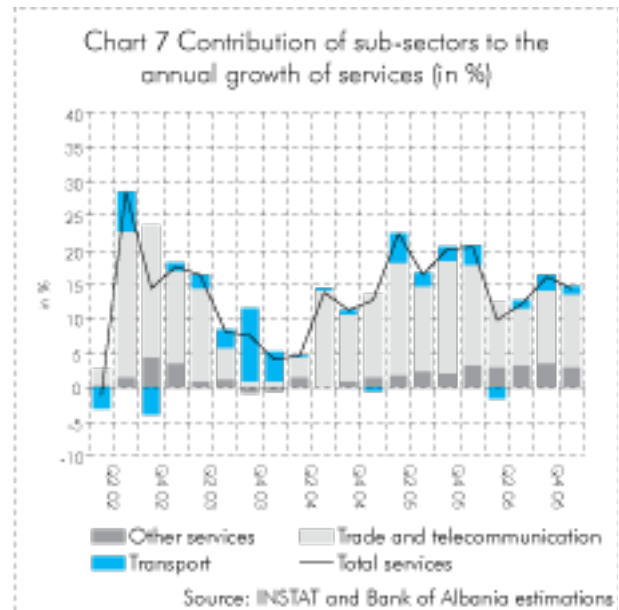
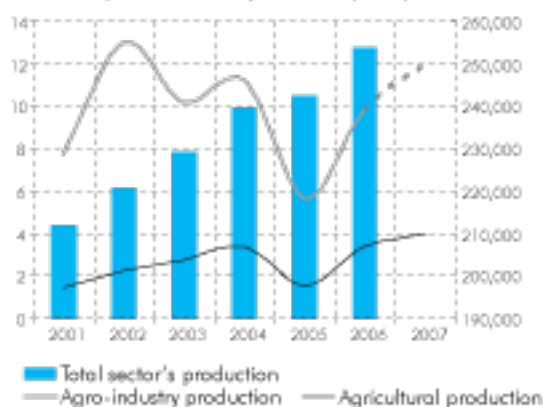


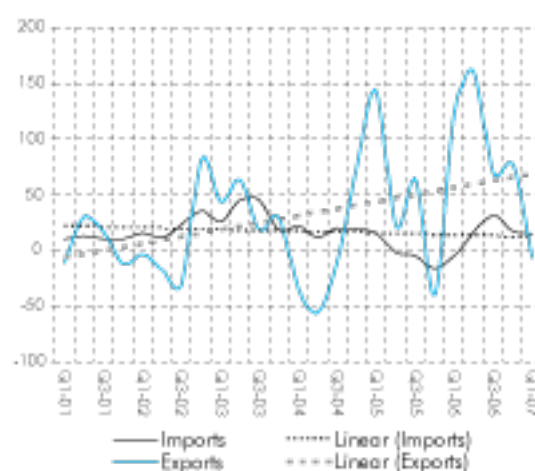
Chart 8 Annual change of total agricultural production by sectors (in %)*



Source: Ministry of Agriculture, Food and Consumer Protection, April 2007

* The data on agro-industry for 2007 refer to the projections of the Ministry of Agriculture, Food and Consumer Protection.

Chart 9 Annual change of imports and exports of unprocessed agricultural products (in %)



Source: Bank of Albania

of production structure in the agricultural sector. In annual terms, total agricultural production grew by 3.4 per cent in 2006, mainly due to high fruit production.

Production in the agro-industrial sector is expected to grow by 12 per cent in 2007. Its positive performance during the first months of 2007 has been expressed in the slowdown of imports of agro-industrial products. A similar picture is observed in unprocessed agricultural imports as well, where annual growth rate has recorded a decline.

3.2 FISCAL SECTOR

Fiscal sector activity during the first semester is characterized by an increase of income and expenses, as well as the creation of fiscal excess as a result of non-executed capital expenses. The main fiscal indicators continued to have positive trends, but with slower annual growth rate compared with the previous year.

Table 4 Annual growth rates of fiscal indicators during the first 5-month period (in percentage)

| | 5M 2004 | 5M 2005 | 5M 2006 | 5M 2007 | Average |
|--------------------------------|---------|---------|---------|---------|---------|
| Total income | 8.5 | 8.2 | 13.0 | 7.5 | 8.7 |
| Tax income | 11.1 | 8.0 | 15.0 | 9.0 | 9.3 |
| Income from local government | 18.2 | 7.4 | -8.8 | -4.7 | 2.9 |
| Income from independent budget | 9.9 | 12.2 | 12.5 | -0.4 | 10.7 |
| Non-tax income | -11.8 | -2.1 | 7.8 | -9.0 | 4.5 |
| Total expenses | 6.6 | 7.9 | -8.1 | 13.3 | 6.6 |
| Current expenses | 7.7 | 7.2 | -4.6 | 10.0 | 6.3 |
| Capital expenses | -1.1 | 14.0 | -34.4 | 49.8 | 9.7 |
| Deficit | -12.0 | 5.0 | -266.8 | -35.4 | -66.9 |
| Domestic | -10.6 | 25.2 | -390.0 | -35.7 | -22.0 |
| Foreign | -13.5 | -18.2 | -48.9 | -38.3 | 2.9 |

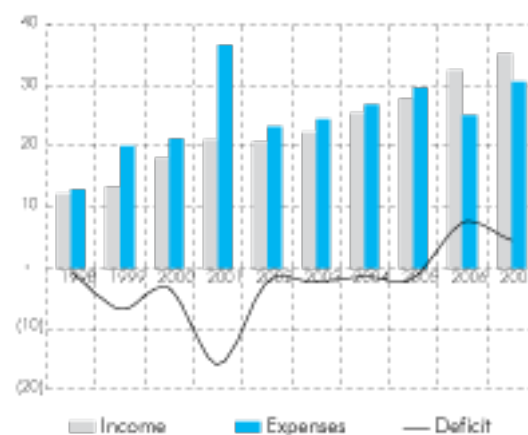
Source: Ministry of Finance

Based on the Ministry of Finance data, until the end of May was collected 95.6 per cent of projected income and were executed 83 per cent of planned expenses. Meanwhile, for the second consecutive year public finances ended the first five months of this year with a positive balance reaching a surplus of ALL 6.7 billion.

BUDGET INCOME

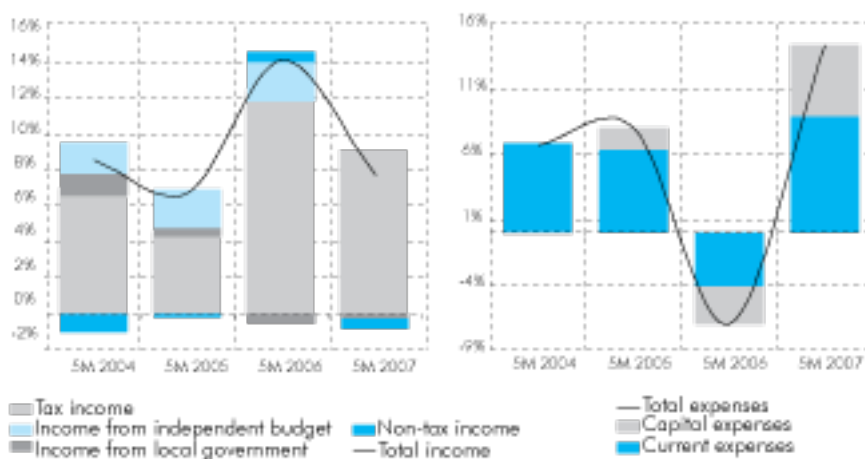
Budget income recorded an annual growth of 7.5 per cent during the first five months of 2007. The biggest contribution to this growth was provided by the collection of tax income, where the VAT, tax on personal income and excises had the best performance.

Chart 10 Main fiscal indicators for January-May (in billions of ALL)



Source: Ministry of Finance, June 2007

Chart 11 Contribution of main items to the annual growth of income (left) and of expenses (right) for the 5-month period (2004-2007) (in %)



Source: Ministry of Finance, June 2007

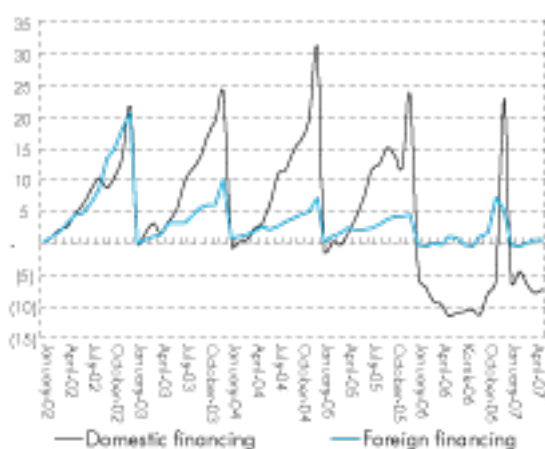
BUDGET EXPENSES

Budget expenses recorded an annual growth of about 13.3 per cent during the first five months of 2007. However, for this period only 83 per cent of expenses were executed according to the budget programme, otherwise expressed as 30 per cent of planned expenses for the entire year. Capital expenses' growth has been faster than current expenses' growth; however their realization remains far from the projected levels. On the other side, the positive balance of the first months and the low level of interest rates have resulted in a decrease in expenses for settling the debt interests by 0.4 per cent.

FISCAL RESULTS

The fiscal balance resulted in a surplus over the first five months of 2007, though in lower levels than the previous year. Its financing profile by sources

Chart 12 Cumulative financing of budget deficit, January 2002 - May 2007 (in billions of ALL)

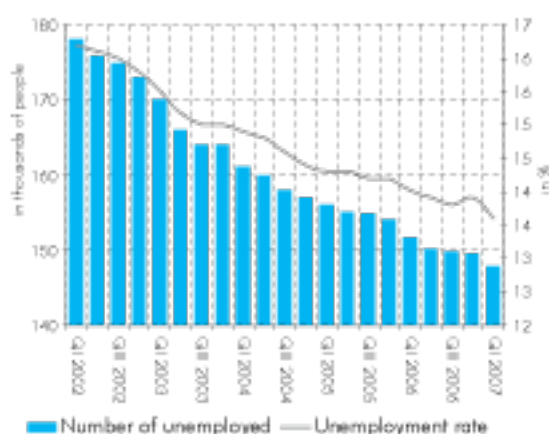


Source: Ministry of Finance, June 2007

is presented similar with the previous year's. In most of the previous year there was an accumulated surplus and in the last months the very rapid growth of expenses accelerated considerably the deepening of deficit which was mainly covered with domestic financing.

The up-to-now performance of the fiscal balance, almost alike with the previous year's, increases the possibility for the recurrence of public expenses and budget deficit concentration in the last months of the year. The Bank of Albania believes that the prevention of such a scenario would help the establishment of a more adequate climate in the financial market and the more efficient use of its sources.

Chart 13 Number of unemployed (left) and unemployment rate (right)



Source: INSTAT, Conjecture, Q1, 2007.

3.3 LABOUR AND WAGES MARKET

The increase of domestic production led to improvements in the labour market. As a result of the annual increase in the employment levels and the dropping of the number of unemployed recorded in the Employment Offices, the annual unemployment rate dropped slightly during the first quarter of 2007.

Despite the seasonal dropping in the first quarter, total employment has increased in annual terms. The data provided by INSTAT indicate that the number of unemployed recorded in the Employment Offices is 147.7 thousand people, dropping by about 5 thousand compared with the previous year. Although the number of long-term unemployed has

been decreasing, they still constitute more than half of unemployed (57 per cent). The ratio of long-term unemployed to total unemployed is nearly 9 per cent less than in 2006. Long-term unemployment remains more present in the group of people with less education.

Table 5 Labour market indicators (in thousands of people)

| | 2006 | | | 2007 | |
|--|-------|------|-------|-------|-------|
| | Q1 | Q2 | Q3 | Q4 | Q1 |
| Total labour force | 1,082 | 1081 | 1,084 | 1,084 | 1,080 |
| A. Total employed | 931 | 931 | 934 | 935 | 933 |
| i) in the public sector | 174 | 172 | 170 | 169 | 168 |
| ii) in private non-agricultural sector | 215 | 217 | 221 | 224 | 223 |
| iii) in private agricultural sector | 542 | 542 | 542 | 542 | 542 |
| B. Unemployment | | | | | |
| i) Total unemployed | 152 | 150 | 149 | 149 | 148 |
| ii) Unemployment rate | 14.0 | 13.9 | 13.8 | 13.9 | 13.6 |

Source: INSTAT, Conjecture, Quarter 1, 2007

The average wage in the public sector increased by about 17 per cent compared with the same period the previous year and by 1.4 per cent compared with the previous quarter.

Box 1 Opinions of businesses and consumers on salaries and wages and their re-evaluation.

In absence of a more recent official indicator of salaries and wages and of their policies in the private sector and in order to have a clearer view of future supply-side inflationary pressures, the Bank of Albania held a survey in the first quarter of 2007 and interviewed 670⁹ big companies and 1200¹⁰ consumers.

Around 45 per cent of the companies which were part of this survey answered that they review the salaries and wages in an average periodicity of 2 years, while the rest does not observe any time rule in their review. This is also confirmed by the answers of consumers employed in the private sector, most of who say that the review of salaries and wages is not regular. Around 48 per cent of employed consumers say that there are not any negotiating parties and moreover, they do not participate in this process. The time profile of salaries and wages review changes from one sector to another. Salaries and wages in construction are more volatile than in industry and services. Construction companies review the salaries and wages more often – about 60 per cent of businesses in this sector say that there is an annual review in salaries and wages. Average review frequency of salaries and wages in this sector is below the average of 1.7 years of total economy.

During 2006, 40 per cent of businesses and 31 per cent of consumers answered that there had not been a rise in salaries and wages. According to the answers of businesses and consumers who say that there has been a rise in salaries and wages, it results that the average rise is 8.5 per cent.

As far as businesses are concerned, construction has applied the highest average rise in salaries and wages, rising by 9 per cent. Companies review salaries and wages based on certain factors, among which the most important ones are: the company's financial result, the use of a rise in salaries and wages as motivation instruments, competition in the salaries and wages market within the sector and the seniority at work. Meanwhile, the rise in salaries and wages results to be less affected by factors, such as past and expected inflation in economy and the rise of salaries in the public sector. It results that the rise of salaries and wages in the public sector is higher than the one declared by businesses in this survey. The above results indicate that in determining the salaries and the wages, the companies consider the meeting of some micro conditions (within the sector), rather than the information in macro level (past and expected inflation). The Bank of Albania appreciates the positive signal for low inflationary expectations in the future, especially considering that this signal comes from businesses which are the main actors of economic activity in the country.

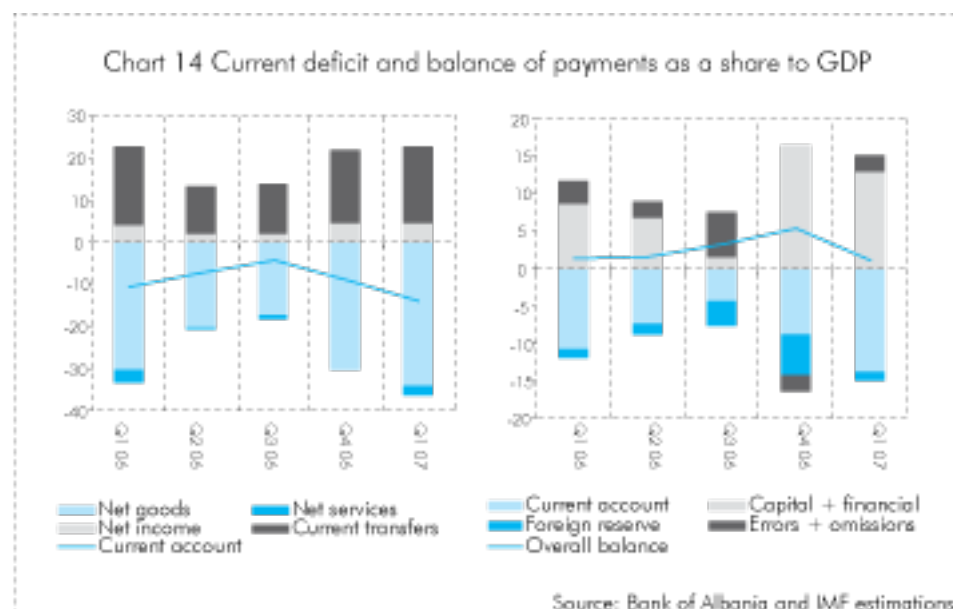
As of end 2007, about 85 per cent of interviewed companies are expected to review/rise the salaries and wages by 8.7 per cent on average. Production and construction companies are expected to apply the highest rise, by about 9 per cent. The reaction of the private sector to possible rises in salaries and wages in the public sector is expected to be balanced. About half of businesses would not be influenced (would not respond), while the rest would respond by rising the salaries and wages modestly, in response to their rise in the public sector.

Moreover, the consumers expect a rise in their salaries and wages by the end of 2007. They claim to have a rise of about 18 per cent or 10 per cent more than the one declared by businesses. This is a well-known phenomenon in the process of reviewing salaries and wages among parties, where the employers (businesses) set lower limits than the employees and their trade unions in order to come to a negotiable point at the end of the process. In determining the expected level of salaries and wages review, consumers consider as important factors not only at micro level, such as education and professional performance, but also macro factors, such as the performance of prices in the future, the exchange rate, in particular of the lek to the euro.

Based on these facts, the Bank of Albania considers prudently both the signals deriving from businesses and consumers. The Bank of Albania emphasizes that the preservation of balances in the salaries and wages market boosts economic growth and helps anchoring the public's inflation expectations to the central bank's objective.

3.4 EXTERNAL SECTOR OF ECONOMY

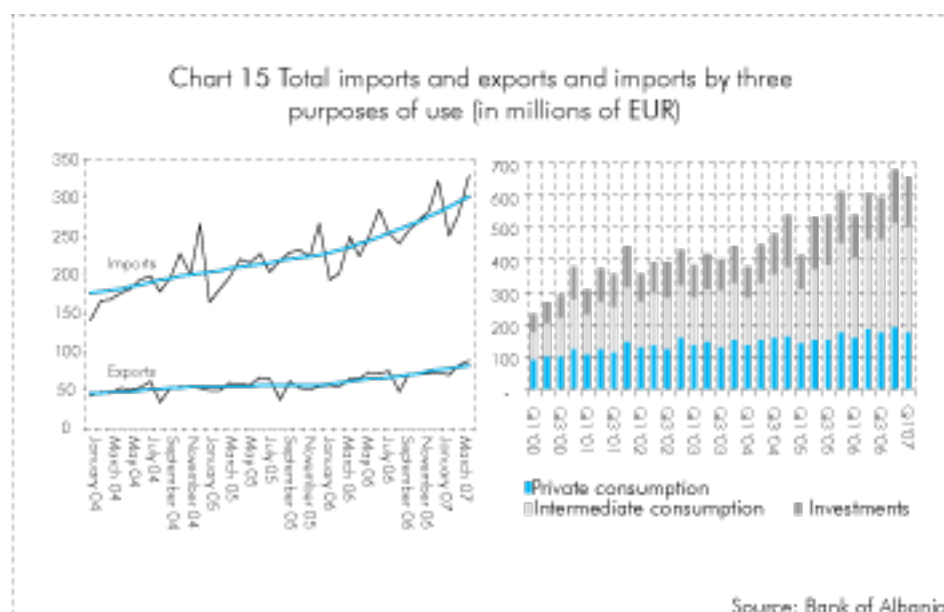
Current deficit deepened by about 40 per cent during the first quarter of 2007 compared with the first quarter of 2006. As a result of the current deficit deepening, its share to the GDP is assessed to have reached 14 per cent. The current deficit deepening for this quarter is mainly attributed to the increase of trade deficit in goods, which is estimated to share about 34 per cent of the GDP.



The volume of current transactions amounted to about EUR 1.8 billion in the first quarter, while current deficit reached EUR 180 million. About 70 per cent of overall current expenses (EUR 950 million) was used for the purchase of import goods, while the rest was used for the purchase of services by

residents. From the export of goods and services was generated 24 and 36 per cent of current income. The balance of current transfers, mainly private ones, continued to record positive figures. Net transfers financed about 50 per cent of trade deficit in goods and services.

Trade deficit in goods was about 8 per cent lower over the first quarter compared with the last quarter of the previous year, but about 20 per cent higher than the deficit of the same period the previous year. Imports and exports of goods amounted to about EUR 630 and 180 million and the coverage rate of imports by exports results to be about 30 per cent.



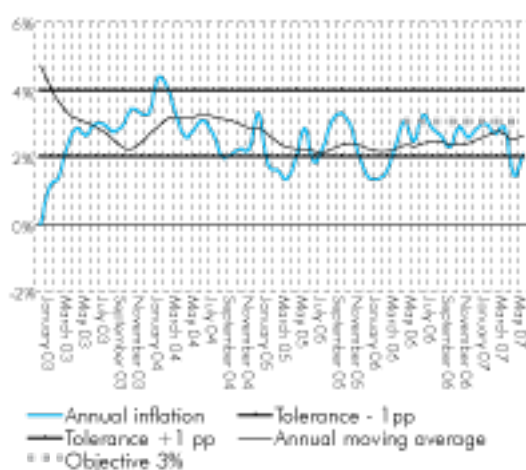
The import of goods recorded an annual growth of about 22 per cent, while exports were about 26 per cent higher than the first quarter the previous year. In terms of imports by use, it is concluded that the share of imports for private consumption has dropped slightly compared with the first quarter the previous year, while imports for intermediate consumption recorded the highest growth rate and the largest share to total imports (about 50 per cent). More than half of total exports are shared by the export of textiles and footwear, while the first quarter was characterized by a high increase in the export of minerals. The increase of export of chrome to China has provided a considerable contribution in this context.

Trade in services ended in a negative balance of EUR 30 million in the first quarter, while the balance of income ended positive with about EUR 60 million. Services account continues to be dominated by travel services, while other services have managed to end the deficit in travel. Income from travel services amounted to about EUR 170-180 million. The dropping in income from tourism is mainly attributed to the decrease in the number of non-resident travellers and to the reduced average duration of stay. Current transfers, which are mainly represented by workers' remittances, financed

about 50 per cent of trade deficit in goods. Net transfers totalled about EUR 240 million, while their share to the GDP has remained almost unchanged compared with the same period the previous year.

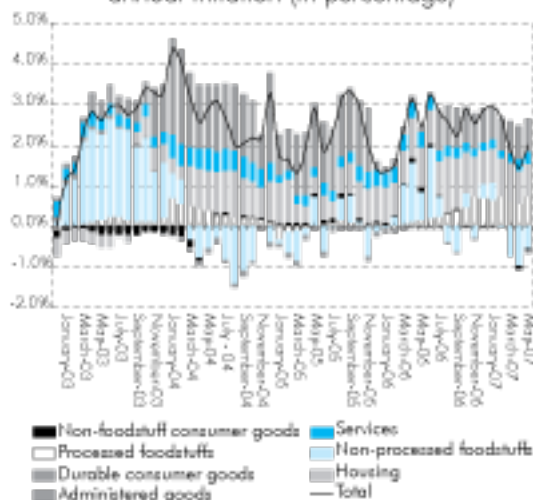
Capital and financial account net flow was about EUR 170 million over the first quarter, out of which EUR 30 million were in the form of capital transfers inflows and EUR 140 million were in the form of residents' financial liabilities. The increase of residents' financial liabilities to non-residents came as a result of the increase of foreign investments and of borrowing from abroad. For the first quarter, foreign direct investments were mostly concentrated in processing and manufacturing industry and in communication. External debt increased by about EUR 36 million over the first quarter. About 90 per cent of this debt is shared by state borrowing. As of end the first quarter, Albania's foreign reserves amounted to about EUR 1.376 billion. This amount of reserves is assessed to be sufficient for covering about 4.4 months of imports of goods and services.

Chart 16 Annual inflation (in percentage)



Source: INSTAT and Bank of Albania

Chart 17 Contribution of main items to annual inflation (in percentage)



Source: INSTAT and Bank of Albania estimations

4 DEVELOPMENTS IN CONSUMER PRICES

Annual inflation rate was relatively low in the second quarter of 2007. In June 2007, it marked 2 per cent, while the second quarter resulted in an average annual rate of 1.8 per cent. Over this quarter, annual inflation displayed a downward trend, dropping by nearly 1 percentage point on average compared with the previous quarter. Inflation was considerably affected by temporary seasonal factors and by a relative balance between supply and demand. The current monetary conditions and the fiscal balance of the first five months have been adequate to keep inflation contained. Notwithstanding this setting, the expectations on the performance of some important monetary and fiscal indicators for the rest of the year suggest that the inflationary pressures may increase.

4.1 INFLATION BY CATEGORIES

Annual inflation rate averaged 2.3 per cent for the first semester of 2007. The average rate marked in the first quarter was considerably higher than in the second quarter. The performance of inflation rates of special categories created according to economic function was relatively uniform throughout the period, except for 'unprocessed foodstuffs'. The other categories recorded positive annual inflation rates.

'Processed foodstuffs' recorded high annual inflation rates. In June, it marked the highest inflation rate of the year of 3.3 per cent. This increase is attributed to the price rise in 'bread and corn'. This development reflected the price rise of bread in some cities in Albania. This item's average inflation marked 3 per cent in the first six months, which is quite a few times higher than the inflation rate of 0.2 per cent marked in the same period the previous year.

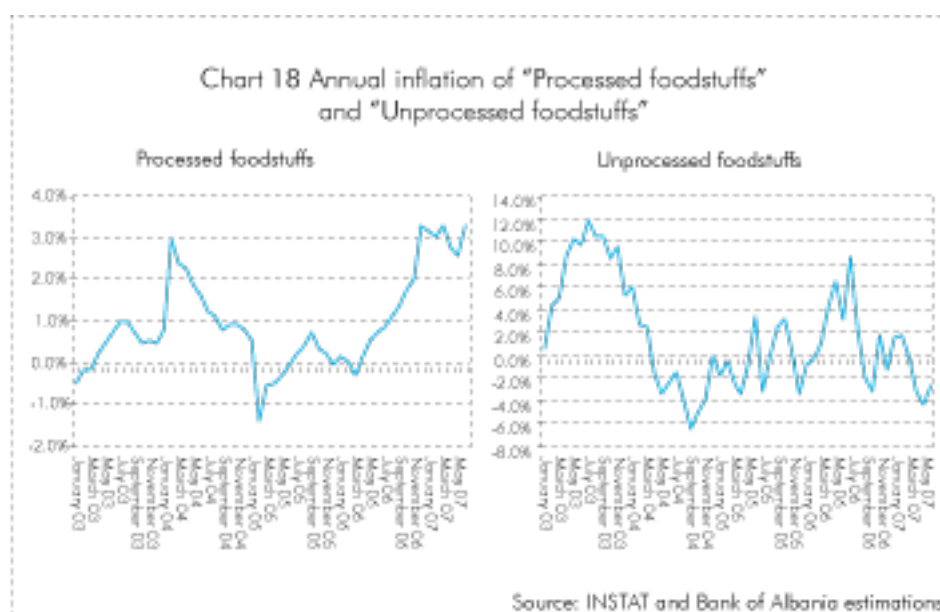
The rise in excise duty on some sub-items in September 2006 and the consumer price rise in partner countries also influenced on this category's positive inflation rate.

| | Alcoholic beverages and tobacco Annual inflation (%) | | | Foodstuffs and non-alcoholic beverages Annual inflation (%) | | |
|---------------|---|-------|--------|--|-------|--------|
| | Albania | Italy | Greece | Albania | Italy | Greece |
| June '06 | 1.6 | 5.2 | 4.9 | 1.9 | 1.3 | 3.5 |
| September '06 | 11.4 | 5.1 | 6.7 | -1.1 | 2.5 | 4.7 |
| December '06 | 12.1 | 5.0 | 10.7 | 0.2 | 2.7 | 4.3 |
| March '07 | 12.2 | 5.7 | 10.8 | -0.5 | 2.4 | 2.7 |
| April '07 | 12.9 | 4.4 | 10.8 | -1.2 | 2.7 | 1.7 |
| May '07 | 13.6 | 4.4 | 8.8 | -2.0 | 2.7 | 2.0 |
| June '07 | 14.3 | | 6.7 | -0.7 | | 2.2 |

Table 6 Annual inflation rates by main groups

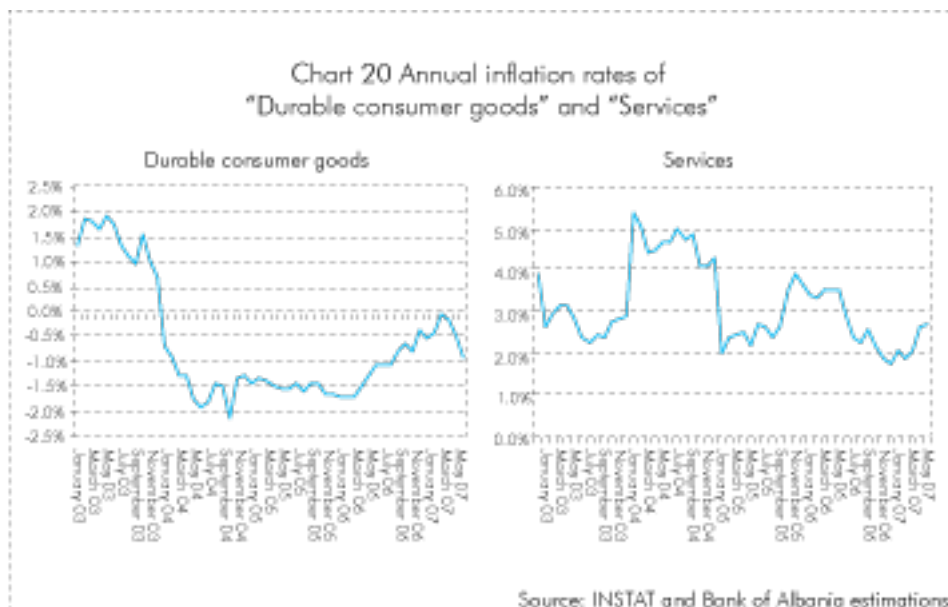
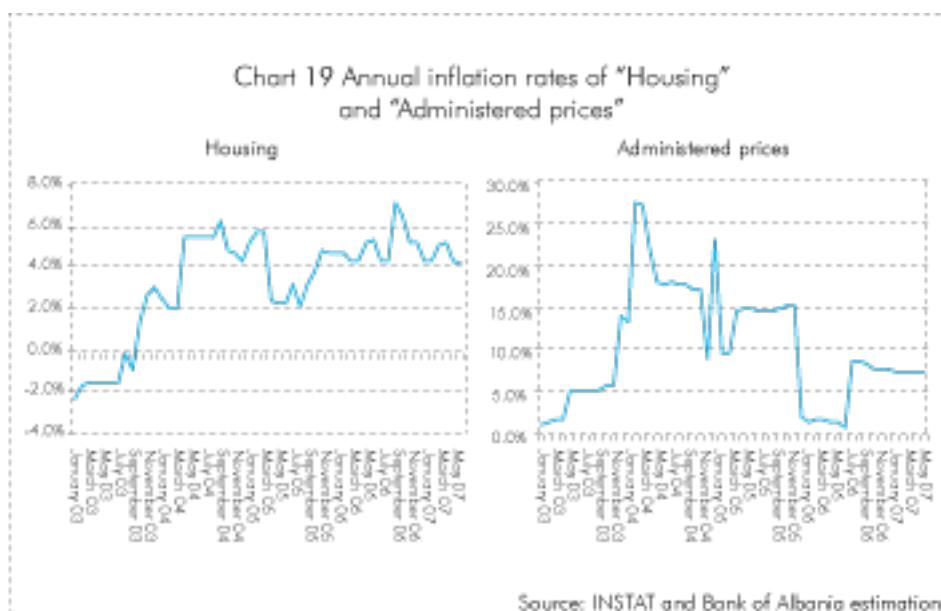
Source: ISTAT; <http://www.istat.it>; National Statistical Service of Greece; <http://www.statistics.gr>; INSTAT, CPI, June 2007

Annual inflation of 'unprocessed foodstuffs' marked -2.6 per cent in June, while in June the previous year it marked 3.2 per cent. This item's average annual rate for the first semester was -1.1 per cent from 2.4 per cent the previous year. The dropping of this item's prices mainly attributes to the considerable decrease in the prices of 'fruit' and 'vegetables including potatoes' which continued over June as well. In contrast to the previous year, the growth of supply for these productions as a result of the entry of domestic agricultural products in the domestic market brought about the drop in prices. Moreover, the decrease of these goods' prices occurred earlier this year compared with the previous year.



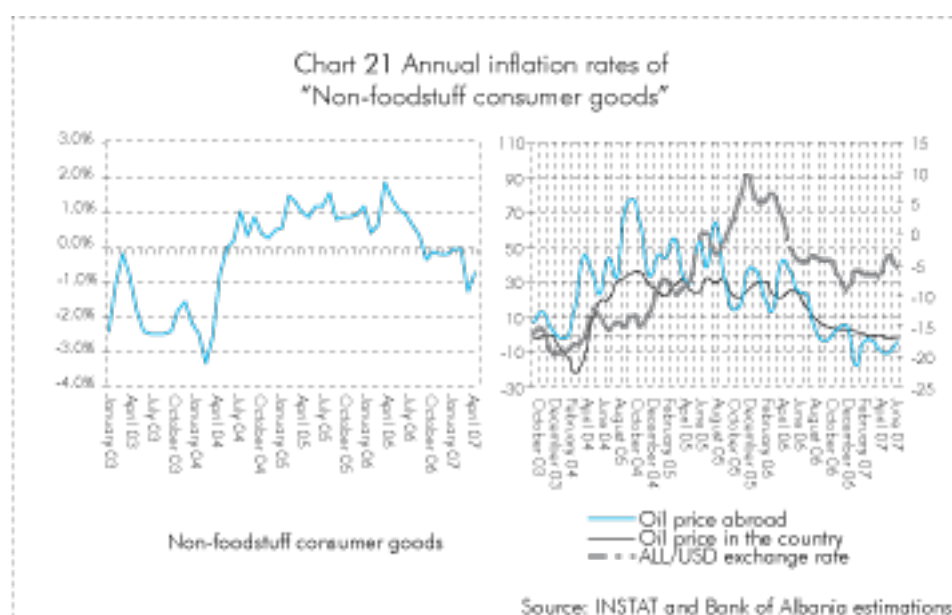
Annual inflation of 'housing' continued to record positive rates, though it dropped slightly in the first months of the year. In June, this item's annual rate marked 4.1 per cent, while the average inflation for the six-month period resulted in about 4.5 per cent. Compared with the first six-month period the previous year, it is observed that the price rise rates of housing services are lower. In general, this item has been characterized by seasonal price fluctuations being under the influence of domestic demand.

Annual inflation rate in administered prices of goods and services fluctuated at around 7 per cent over the first semester of 2007. Energy price has had a direct influence on inflation through the increase in the cost of energy consumed by households. The influence of the inflation in administered prices of goods and services on the total inflation rate is significant. This item has been contributing by about 0.8-1.0 percentage points each month starting from August 2006. Almost all services in this group have gone through slight fluctuations in the prices over the first semester of the year.



Annual inflation of 'durable consumer goods' and 'services' (-0.9 and 2.7 per cent) resulted to be quite close to the average annual rate of -0.7 and 2.4 per cent. The inflation performance of durable consumer goods is in line with the trend in other countries. As a result of the rapid technological development there is an ever-increasing quality improvement and dropping in prices. The price rise in services on the other hand provides evidence for the increasing demand and improved quality.

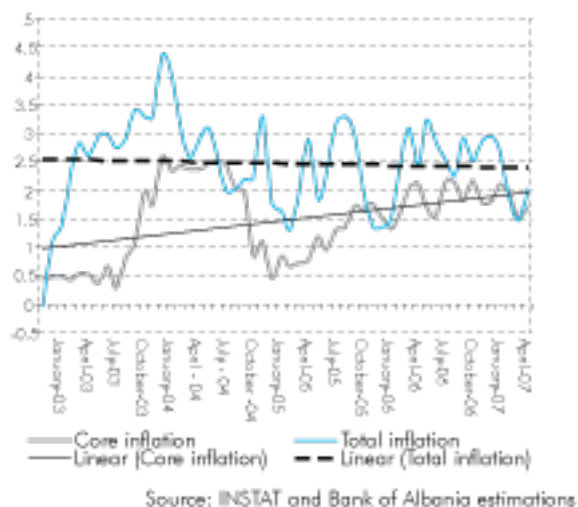
Annual inflation of 'non-foodstuff consumer goods' recorded the negative figure of -0.8 per cent in June 2007. The average rate for the first semester of 2007 was -0.4 per cent, while the previous year it marked 1.1 per cent on average. This decrease was manifested in both main items: 'clothes and footwear' and 'services to personal transport vehicles'. The phenomenon of the negative inflation in 'clothes and footwear' is quite a long one, starting from February 2000. The inflation of 'services to personal transport vehicles' is affected considerably by the oil price performance in the domestic market, which on the other hand is both influenced by the oil price performance in the international markets and by the exchange rate developments. The recent oil price rise, following the dropping for some months since last October, was offset by the appreciation of the lek to the US dollar.



4.2 INFLATION AND MACROECONOMIC ENVIRONMENT

The first semester of 2007 was characterized by the growth of domestic demand in the presence of the absent fiscal incentive, accommodating monetary conditions and of the by and large positive supply-side developments. The high domestic demand was reflected in the increase of sales and in the deepening of trade deficit. In the monetary area, the rapid growth of monetary assets and liquidity was followed by pressures on the decline of interest rates, while the exchange rate has shown a relative stability. The first quarter provided evidence for the growth of economic activity and the improved situation in the labour

Chart 22 Annual rate and linear trends of core and total inflation (in percentage)



market, despite the energy crisis early this year. The sales index increased by 14 per cent compared with the previous year and the unemployment rate continued to drop. On the supply-side, the positive influence of domestic agricultural production on inflation was more dominant than the high oil prices effect, while wages did not increase significantly and the inflationary expectations remained anchored around the Bank of Albania target.

The upward trend of the annual core inflation rate constitutes another signal for the monetary policy, providing evidence for the increasing inflationary pressures in economy. Annual core inflation rate marked 1.7 per cent in the second quarter of 2007, which is almost equal to total inflation rate. In April and May were recorded slightly higher core inflation

rates compared to total inflation rate. In June annual core inflation marked 1.7 per cent, which is higher than the previous year. The price rise effect of bread¹¹ and some processed foodstuffs¹² affected this rate for June.

The analysis of total inflation performance indicates that the latter is often subject to high fluctuations in the short-term. Therefore, the Bank of Albania assesses core inflation, or inflation "cleared" from temporary influences, as important and supplementary information because it informs the monetary policy and the public on the permanent inflation rates.

Box 2 More on core inflation and on its measurement

Core inflation is an important information for the analysis and monetary policy decision-making process in central banks. Literature defines core inflation as the long-term and durable part of total inflation. From the central bank point of view, core inflation is a component of total inflation, which is mainly caused by monetary factors. Based on these theoretical considerations, core inflation would result after the short-term or transitory fluctuations, which are usually caused by factors out of the monetary policy sphere, were excluded. The practice of measuring core inflation provides a wide spectrum of methods. The selection of a method, on the basis of which it is derived an adequate core inflation series, is quite debatable in both the academic and central banking circles (Silver, 2006). Theoretical and practical debates point out the advantages and disadvantages in applying different methods. Notwithstanding the difficulties and dilemma in selecting the method for the measurement of core inflation, the method to be selected should: first, exclude to a great extent the transitory volatilities from total inflation; second, have a high level of transparency, in order to be familiar and understandable to the public. The vast experience of different central banks and of the European Central Bank in particular, and the experience of the Bank of Albania indicates that the method of permanent exclusion of some items from the consumer basket is an alternative for the measurement of core inflation. From the comparison of different methods' results of core inflation measurement in the case of Albania, it has been concluded

that the measurement of core inflation by using the method of permanent exclusion satisfactorily meets the statistical, transparency and public understandability criteria. Moreover, the total inflation may be forecasted more adequately. Notwithstanding the advantages of this method, some well-known researchers (Wynne, 2001; Cechetti, 2006) believe that the permanent exclusion of some items does not always imply that the remaining is only temporary or transitory inflation. Therefore, the results of core inflation should be carefully considered as additional information in deriving conclusions on inflation trends in the long run.

Based on the principles and experience in applying the method of permanent exclusion, from the Albanian consumer basket have been excluded: (a) highly seasonal goods and services, which cause high and temporary fluctuations in prices (usually some unprocessed foodstuffs); (b) goods with administered prices (energy and water); (c) goods, the prices of which are often subject to fiscal policy (excise goods); (d) goods, the prices of which are closely related to external conjunctures (oil). After the exclusion is made, the share of the sub-basket, upon which core inflation is measured, is about 78 per cent.

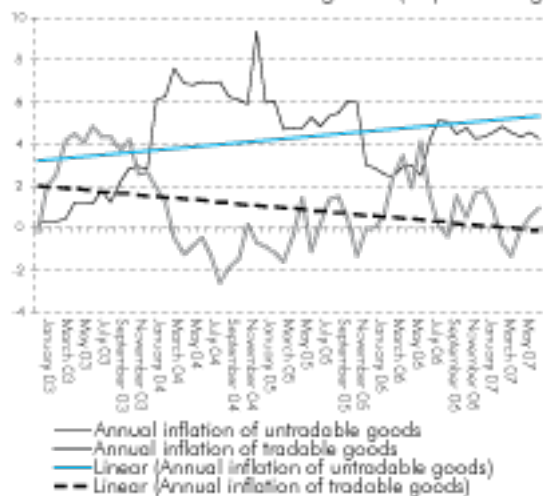
The presence of demand-side inflationary pressures is expressed in the prices of non-tradable goods and services¹³. Over the last four years this item's average annual inflation marked 4.2 per cent; however there is an upward trend from one quarter to another for 2007.

The highest inflation rate of non-tradable goods for the first semester was recorded in April (4.8 per cent). The high inflation rates of these types of goods have been partly neutralized by the low inflation of tradable goods which has been displaying a downward trend in the last months.

Monetary policy has continued to react through the increase of the core interest rate, remaining however accommodating to the economic growth. Under the conditions where the demand of economy for monetary assets has been growing, trade deficit has been deepening and the interest rates have been fluctuating around low levels, the Bank of Albania decided to increase the core interest rate at the end of June 2007. This increase aimed to keep the demand for monetary assets and the effects of its growth on the inflation perspective on check. On the other hand, the increase of the core inflation rate aims to balance the credit growth rates by better managing the level of liquidity in the market. It also seeks to harmonize the private sector's demand for money with that of the public sector's in the future, under the conditions where the latter is expected to grow. Consequently the increase of the core interest rate will establish a balanced macroeconomic environment and it will provide stable economic growth rates.

The public sector's fiscal position did not affect the increase of inflationary pressures over the first semester of 2007. Fiscal policy has been prudent in

Chart 23 Annual rates and inflation linear trends of tradable and untradable goods (in percentage)



Source: INSTAT and Bank of Albania estimations

implementing the fiscal programme in terms of income collection, while the execution of expenses resulted less than projected. Budget spending in the first semester of 2007 increased compared with the same period the previous year, while their execution level for this period was as much as 30 per cent of the amount projected for 2007.

The supply of goods, in particular of agricultural goods, and the economy's production capacities have managed the moderate growth of domestic demand by not generating inflationary pressures.

Exchange rate developments play a key role in the performance of inflation. Domestic market continues to be import-oriented. For the first semester imports resulted to be four times higher than exports. Imported inflation was positively influenced by price stability in partner countries and negatively affected by the continuous depreciation of the lek to the euro. The foreign prices rise effect on the total level of domestic consumer prices is assessed to have been neutral. As far as domestic production is concerned, the increase in the supply of foodstuffs, mainly over the second quarter managed to meet the largest part of demand for this type of goods. Considering that this is a seasonal phenomenon, the depreciating environment of the lek to the European currency would bring about serious problems to the inflation rate in case the domestic demand of the economy remains high in the medium run. Despite the positive performance over the first half of the year, oil price has begun to fluctuate again in high levels. In case of a potential energy crisis, this situation increases the risk of a rise in the production cost in economy.

5 MONETARY DEVELOPMENTS AND FINANCIAL MARKETS

5.1 MONETARY POLICY OF THE BANK OF ALBANIA

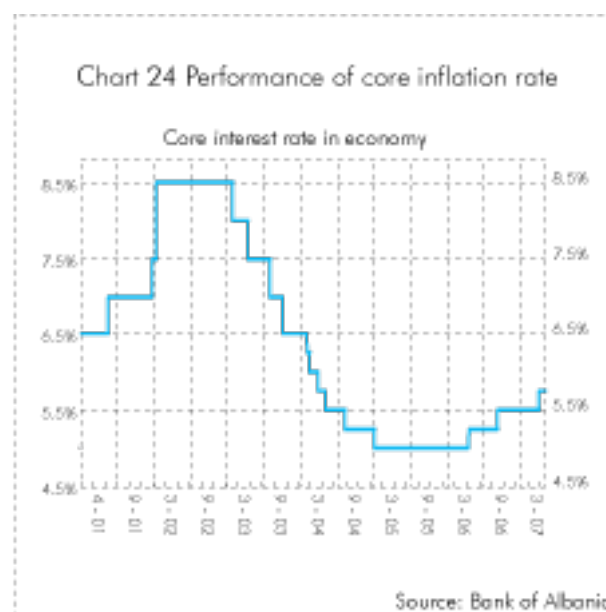
The analysis of monetary conditions evidences high expansion rates of money supply in economy, while the inflation rates forecasts confirm its upward trend from the current average rate. Annual money supply growth rate has averaged 17-18 per cent in the last six months compared to the average growth rates of 10-11 per cent in the second semester of 2006. The high growth rates of money supply have been supported by the high demand for credit from the private sector of the economy while the public sector's fiscal position contributed to the weakening of monetary expansion rates. At the same time, the presence of inflationary pressures was reflected in the price rise of non-tradable goods in the last quarters.

The effect of the increasing domestic demand for monetary assets has been partly amortized in the form of both trade and current deficit deepening. Over the first quarter of 2007, current account deficit deepened by about 39 per cent. The preliminary data on the trade balance for April and May confirm the deficit upward trend. Against the backdrop of the growth of domestic demand in economy, the current expansion trend of the economy external position over 2007 and the presence of potential risks in the expected dynamics of

inflationary pressures, on 27 June the Supervisory Council of the Bank of Albania decided to increase the core interest rate by 0.25 per cent. The core interest rate applied on the (reverse) repurchase agreements is 5.75 per cent.

By means of this growth, the Bank of Albania aims to stabilize the inflationary expectations through the minimization of potential risks on both the monetary and macroeconomic balance. The transmission of this signal to the financial markets will induce the re-balancing of the current upward trend of domestic demand in favour of financing the stable growth of economy in the long run.

In line with its long-term policy, the Bank of Albania has been operating in the financial markets in order to maintain the balance. The monetary operations for the first quarter operated through the short-term repurchase agreements and long-term reverse repurchase agreements, aiming to stabilize the liquidity situation in the market. The stable liquidity situation in the banking market was followed by the gradual increase of interest rates in the second quarter, being in line with the targeted monetary policy. The Bank of Albania was present in May by injecting liquidity and in June by withdrawing the liquidity. These operations aimed to minimize the interest rates fluctuations. In the foreign currency market, the exchange rate was relatively stable with a slight depreciating tendency in the first quarter. The Bank of Albania was present in the foreign currency market in order to stabilize the short-term fluctuations in this market.



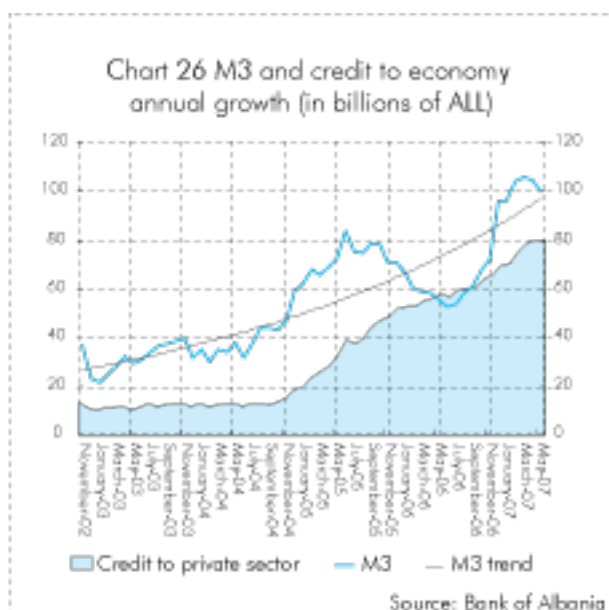
5.2 MONETARY AGGREGATES DEVELOPMENTS

The performance of money supply indicators has evidenced the high demand for monetary assets during 2007. Money supply recorded an average annual growth of about 17.5 per cent during 2007. However, the expansion of money supply in economy, expressed by the narrowest monetary aggregates, results in lower rates. The annual growth of M2 aggregate fluctuated around 12 per cent compared with the average growth rates of about 7-8 per cent during the second semester of the previous year. In annual and foreign currency structure terms of money supply, the performance of M2 aggregate to M3 growth reflects the creation of foreign currency monetary assets in the private sector of economy. The annual expansion rates of monetary base in economy (reserve assets) have had a stable performance of about 10-12 per cent.



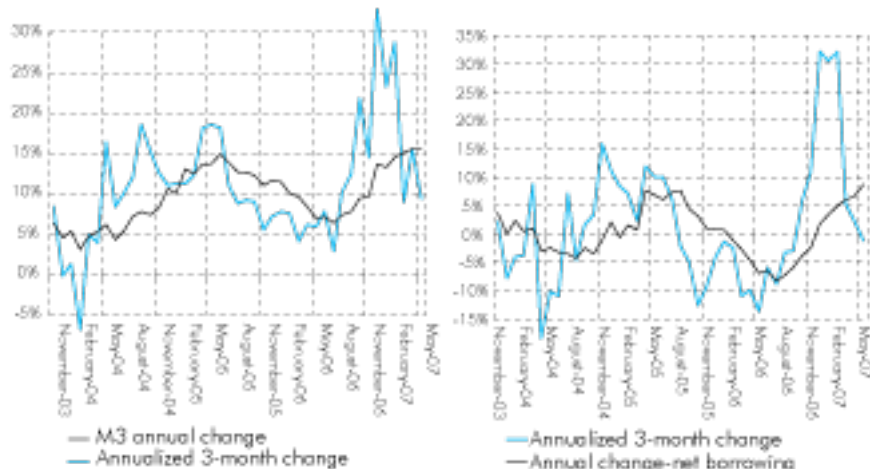
Both time and foreign currency structure of the economy demand for monetary assets have been balanced in the monetary aggregates structure. The long-term trend of M3 growth has been influenced by the creation of monetary assets in the form of credit to the private sector, while the fluctuations over the months have reflected the effect of domestic borrowing for the financing of deficit in generating money flows. The balanced performance of the fiscal position during 2007 contributed to the stabilization of money supply performance.

The creation of money flows was mainly in foreign currency. About half of annual money supply flow took the form of foreign currency deposits held with the banking system. As of end May 2007, the share of foreign currency deposits to M3 increased to about 31 per cent compared to 29 per cent as of end 2006. In annual terms, the performance of foreign currency deposits has followed the upward trend of the creation of foreign currency assets in economy, mainly because of foreign currency credit. Foreign currency workers' remittances also make a contribution to the annual growth of foreign currency deposits on seasonal basis.



The second main component of money creation in economy, domestic borrowing, has been a determining factor of the short-term behaviour of M2 aggregate and of the liquid component of money supply which is currency outside banks. The creation of ALL deposits held with the banking system was mainly supported by the generation of currency from ALL credit to the private sector. Meanwhile the share of currency outside banks to M3 dropped to

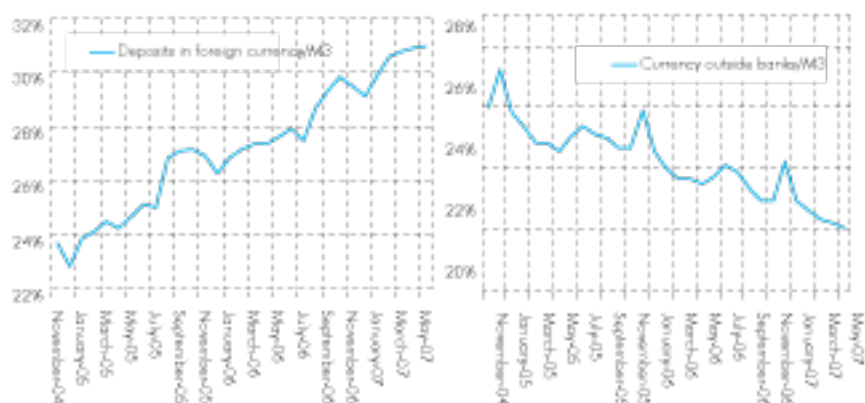
Chart 27 Annual growth of real M3 (left) and of net Government borrowing in real terms



Source: Bank of Albania

22.0 per cent in May compared to 24.2 per cent in December. The dropping of this ratio is partly seasonal. In May 2006, this ratio was 23.5 per cent or 1.5 per cent less than the current ratio. ALL deposits have grown annually by about 12.5 per cent, while their share to M3 accounts for about 47 per cent. In general, the structure of money supply is being oriented to less liquid assets. This orientation influences positively on the reduction of potential M3 growth effects on the creation of inflationary pressures.

Chart 28 Share of deposits in foreign currency and of currency outside banks to M3

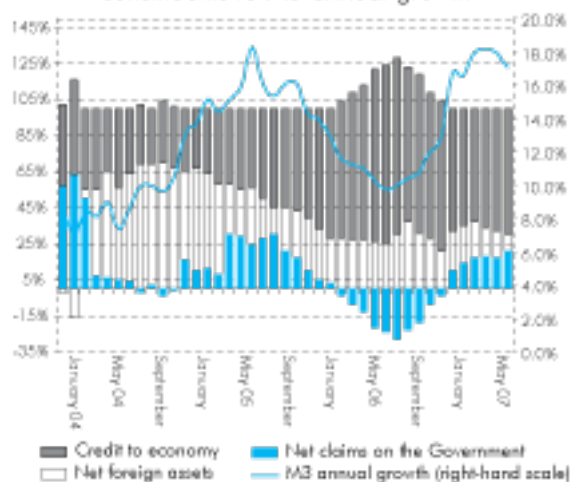


Source: Bank of Albania

5.3 PERFORMANCE OF DEMAND FOR MONEY AND CREDIT TO ECONOMY

Demand for money has grown under stable rates in April and May 2007. Being pushed by the higher demand of the private sector, its main

Chart 29 Contribution of demand for money constituents to M3 annual growth



component, domestic credit, continued to grow. The growth of credit to economy has provided the main contribution to the annual growth of demand for money by 71 per cent. This performance has offset the downward contribution provided by its foreign currency component. On the other hand, the public sector has had a moderate demand for money and the Government's fiscal position continues to be characterized by budget surplus. The focus of the banking system to crediting the private sector is affecting the constant dropping of the share banks' claims on the Government have on domestic credit to 54 per cent from 65 per cent it accounted for the previous year.

Credit to economy constituted the main impulse to the growth of demand for money in the second quarter. As of end May, this type of credit amounted to ALL 228 billion or 24.6 per cent of the GDP projected for 2007. In the last two months, the credit growth of ALL 14 billion has been more sluggish than the end of the first quarter, being close to the projection in the monetary programme of the Bank of Albania. In annual terms, credit growth rate reduced to 55.6 per cent from 58.7 per cent it peaked in March. Meanwhile, new credit extended during the second quarter maintained high levels (ALL 20 billion a month). The satisfactory performance of new credit was followed by high levels of settlements, which led to a more modest growth of outstanding credit. The first months of 2007 indicate a reduction in the average duration of new credit signalling a more sluggish growth of outstanding credit as a result of the high settlement levels for the following periods.

Box 3 Performance of credit in Central and South East Europe

Central and South East European countries have for many years been experiencing a boom in the credit to the private sector from commercial banks. The annual credit growth rates are high, being followed by a considerable increase in the ratio of credit to private sector to the country's GDP. However, this ratio is to a large extent below the average of many European countries with developed banking systems, where the ratio of credit to the GDP exceeds 100 per cent.

Credit boom in regional countries was pushed by the overall macroeconomic stability, the reforms in sectors of economy, the establishment of market economy institutions and the application of legal reforms (in particular, the legal obligation for the execution of contracts). The sound economic growth pushed further the expansion of lending activity, influencing on the expectation for the increase of individual income and earnings. This growth has encouraged the timely substitution of savings/consumption, pushing credit further.

Table 1 Performance of main indicators of lending activity in regional countries*.

| Countries | Credit per cent GDP | Annual growth | Foreign currency credit/ GDP | Credit to households/ GDP | Real estates credit /GDP | Credit interest rates | Non- performing loans/total |
|--------------------------|---------------------------|------------------|---------------------------------------|---------------------------------|-----------------------------------|-----------------------------|-----------------------------------|
| Bulgaria | 49.1 | 30.7 | 22.8 | 17.7 | 7.6 | 8.4 | 2.2 |
| Romania | 26.3 | 59.3 | 12.5 | 11.8 | 2.3 | 13.9 | 8.5 |
| FYROM | 31.6 | 33 | 8.3 | 10.4 | 1.4 | 10.7 | 7.6 |
| Albania** | 23.4 | 58.9 | 16.9 | 7.9 | 4.6 | 14.1 | 3.3 |
| Serbia | 28.7 | 13.9 | 13.5 | 10.2 | 21.3 | 15.9 | 24 |
| Croatia | 74.4 | 22.4 | 60 | 39.5 | na | 9.1 | 2 |
| Poland | 33.3 | 31 | na | 18.4 | 5 | 7.8 | 6.6 |
| Czech Republic | 37 | 21.4 | 16.5 | 17 | 12 | 7.2 | 3.6 |
| Average in the region | 38.92 | 33.83 | 22.33 | 16.25 | 7.44 | 12.02 | 9.12 |

*Data for March 2007 (unless otherwise mentioned).

** Data for May 2007.

Source: "Southeastern Europe and Mediterranean Emerging Market Economies Bulletin", vol 8, Economic Bulletin NBG, and economic bulletins of central banks.

As shown in the table, lending activity in Albania displays high growth rates, boosting the country's economic development further. The annual growth rates of the last two years are the highest in Central and South East Europe. However, Albania has the lowest ratio of credit/GDP in the region. The low ratio of credit/GDP implies that there is room for further financial deepening and credit growth.

Lending developments in Central and South East Europe may be mainly interpreted as a manifestation of further financial intermediation deepening. But, in the same time, the rapid credit expansion implies increase of risk in many countries. Financial stability situation in these countries is positive; however, the rapid credit growth calls for special attention in terms of supervision, for the credit quality to be satisfactory. In macroeconomic terms, the credit boom has led to the growth of demand. As a result, in some countries with high and continuous credit growth, the deficit on current account has gone further the stable levels in a long period of time. The great risk of credit growth has been subject to measures taken by the decision-makers to keep it as close as possible to acceptable levels for the overall macroeconomic stability of the country.

Reference:

P. Backé, B. Égert & T. Zumer, 2006: "Fast credit expansion in Central and Eastern Europe: catching-up, sustainable financial deepening or bubble?"

P. Backé, & T. Zumer, 2005: "Focus on transition" OENB, Volume 2.

The structure of credit by currency is dominated by foreign currency denominated credit. This type of credit maintained the same growth rates during the second quarter as in the first months of the year, growing by 53 per cent in annual terms. Credit to businesses provided the main contribution to its growth, though credit to households denominated in foreign currency displays higher rates. Compared with the first quarter of 2007 there has been a slight improvement in the ALL denominated credit portfolio, which reached to 28.6 per cent in May. Annual growth rates of ALL denominated credit continue the downward trend to 63.1 per cent in May compared to 71.1 per cent in the first quarter. The growth of credit to households during the second quarter has favoured the performance of credit denominated in domestic currency.

Chart 30 Performance of lending activity

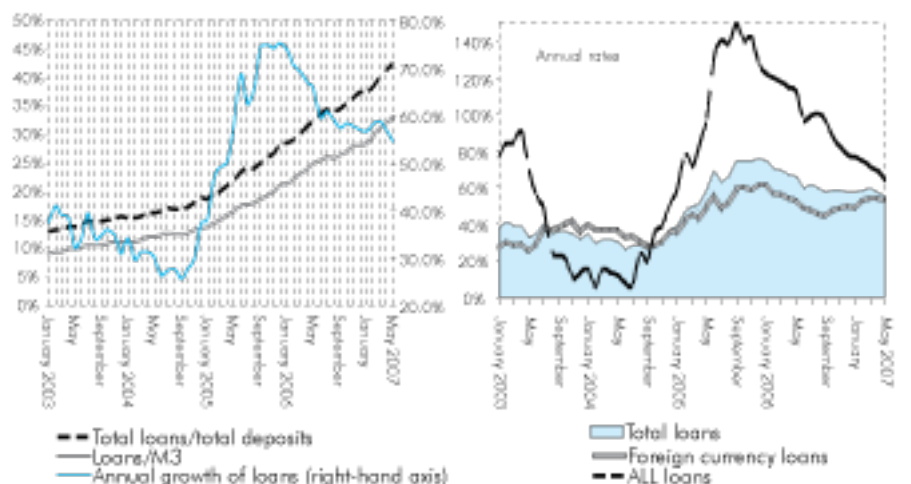
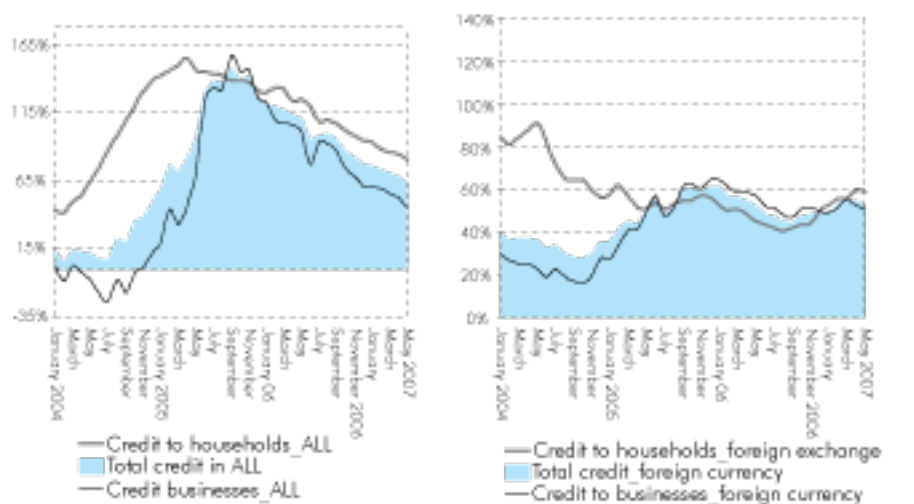


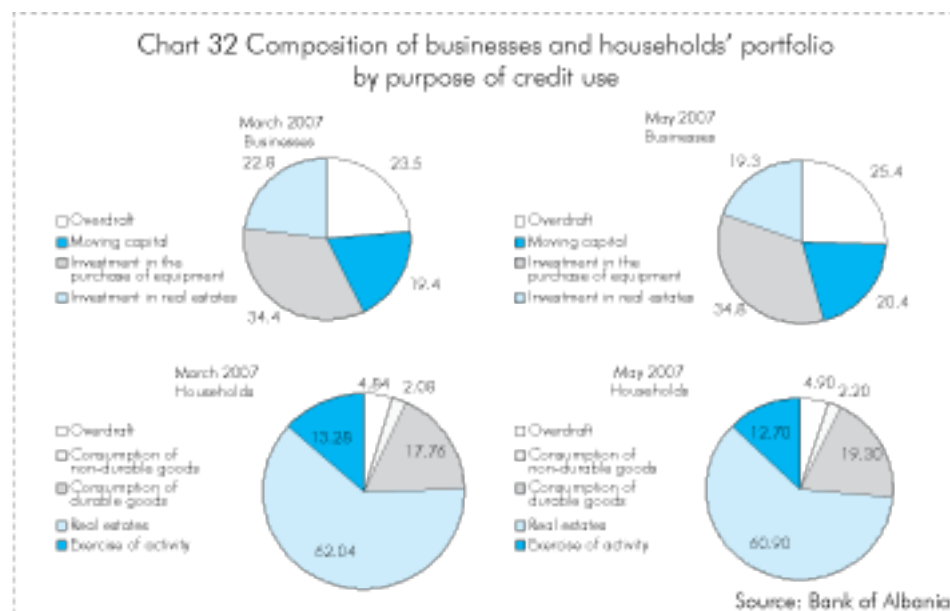
Chart 31 Annual growth performance of credit by currency



Private companies' demand for credit is the main impulse of credit growth. As of end of May, credit to businesses reached to 16 per cent of the GDP. In annual terms, it was 48 per cent higher than the previous year. The growth rates of credit portfolio to businesses have been dropping, mainly as a result of the high credit settlement levels during this period. Credit to public sector also increased during the second quarter. This euro denominated credit became active following the use of the credit line by the state-owned company KESH in one of the banking systems. The largest increase of this credit was observed in April (ALL 1.8 billion).

In terms of purpose of use, credit to business extended by the banking system was mainly used for the purchase of equipment. However, compared with the previous quarter there is an increase in the credit for moving capital and overdraft which accounted for 45.8 per cent of credit portfolio to

businesses. In terms of sectors of economy, the second quarter displayed a moderate growth in credit to agriculture, construction and collective services. Although the trade sector has a more reduced credit portfolio it remains the most credited sector of economy sharing 20 per cent of credit portfolio.

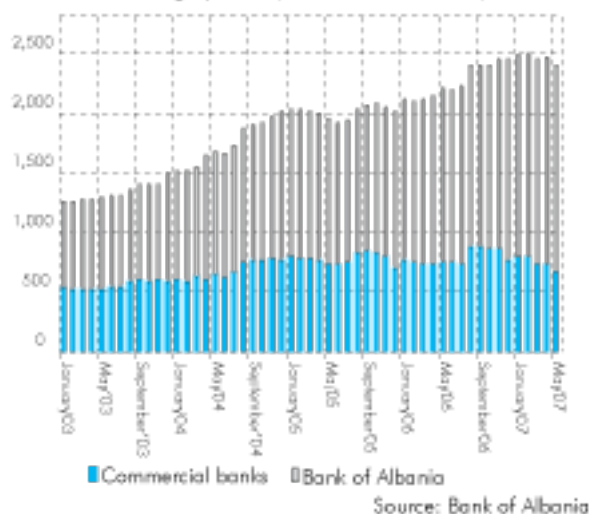


Compared with the previous quarter, there was an increase in credit to households in the second quarter of 2007. As of end May, it accounted for 34.5 per cent of total portfolio and its growth rate reached to 68.3 per cent. Credit portfolio to households provided evidence for an increase over the second quarter in the share of consumer loan for durable goods, which offset the reduction in the share of credit portfolio for real estates extended to households. However, real estates credit shares most of the weight in the households' portfolio by 61 per cent. Meanwhile, consumer loan grew over the second quarter, reaching the level of December 2006 and accounting for 9.1 per cent of the portfolio. The performance of consumer loan seems to be closely related to the holiday and vacations season.

The banking system net foreign assets amounted to about USD 2.4 billion as of end of May. The performance of commercial banks' net foreign assets has determined the performance of the foreign currency component of demand for money, which decreased compared with the previous quarter. The reduction of foreign assets is the net result of the higher financing of economy by banks, in the form of foreign currency credit and the growth of foreign currency deposits held with these commercial banks. Compared with the end 2006, commercial banks' foreign assets dropped by USD 95.5 million.

The developments in the net foreign reserve of the Bank of Albania have made a positive contribution to the banking system net foreign assets. The net foreign reserve of the Bank of Albania amounted to USD 1.72 billion in May, increasing by USD 34.7 million compared with the end of 2006. The changes in the EUR/USD exchange rate affected considerably the performance of these

Chart 33 Net foreign assets of the banking system (in millions of USD)

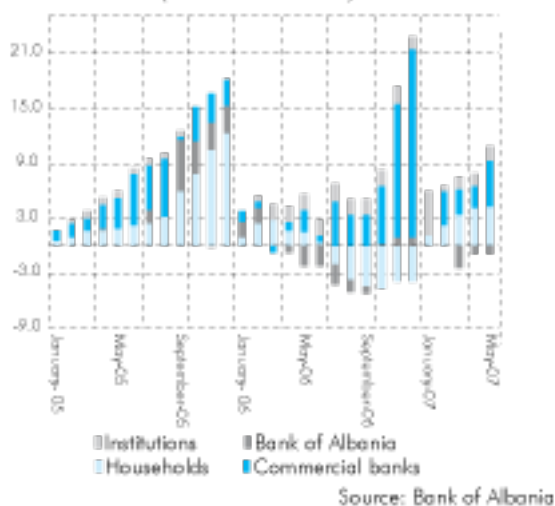


assets over this period. Excluding the appreciation effect of the euro to the American dollar, the net foreign reserve of the Bank of Albania results to have dropped by USD 4.9 million.

Fiscal balance for May continued to be characterized by a budget surplus¹⁶, which increased by ALL 1.9 billion compared with the end of the previous quarter. Fiscal surplus led to a moderate demand of the Government for monetary assets. The fiscal surplus and the issue of Government securities provided to the Government ALL 14.2 billion of surplus at the end of the first five months of 2007. Domestic financing totalled ALL 2.9 billion in May or only ALL 0.1 billion more than the end of the first quarter. The issue of ALL 5.8 billion of 2 and 5-year bonds helped to create Government

inflows. While the issue of Treasury bills of smaller amount than their matured amount and the ALL 6 billion investment in reverse repurchase agreements in the banking system helped the outflow of Government funds. The excess Government liquidity situation is also reflected in the Government's account balance held with the Bank of Albania which as of end of May resulted in a surplus of ALL 5.4 billion or ALL 2 billion more than as of end of March.

Chart 34 Gross financing of budget deficit (in billions of ALL)



The Government's gross financing during the first five months of 2007 was accomplished through the increase of households and institutions' securities' portfolio by about ALL 5.7 billion. Meanwhile, commercial banks continued to shift the portfolio to securities of longer maturity terms, that is Government bonds. Commercial banks increased their investment in Government bonds by ALL 19.2 billion; while on the other hand, they reduced the Treasury bills' portfolio by ALL 14.1 billion. In the light of these developments, as of end May the Treasury bills' portfolio accounted for 73.2 per cent of Government's securities portfolio from 85.7 per cent it accounted for the same period the previous year.

5.4 FINANCIAL MARKETS, INTEREST RATES AND THE EXCHANGE RATE

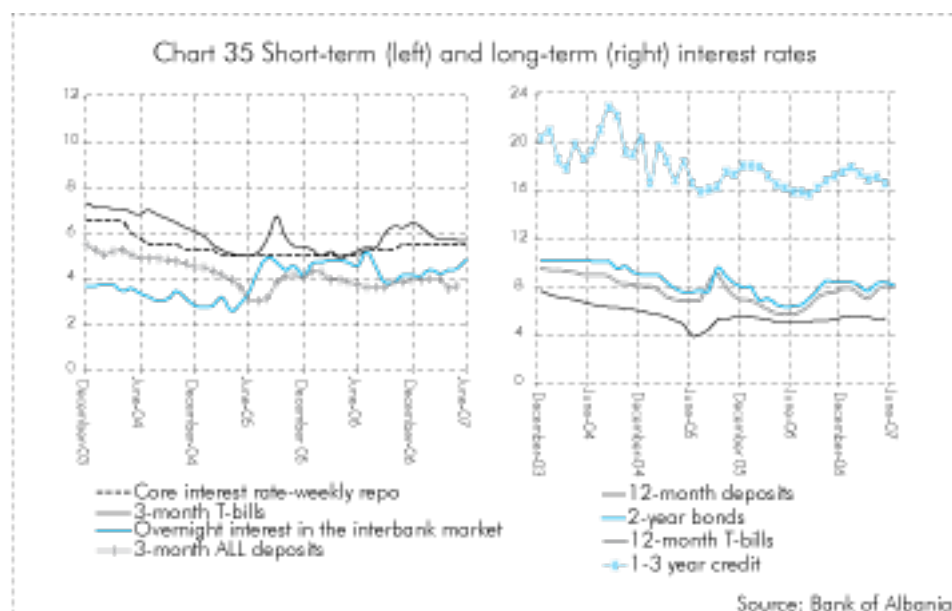
Trade activity in the markets has been more reduced and the interest rates have had an upward trend in the second quarter of 2007. The monetary policy stance remained unchanged for the period, maintaining the same core interest rate of 5.50 per cent since November 2006 when it was raised by 25 basis points. There was a signal for a raise in the core interest rate in the second quarter (which occurred at the end of June), which created

expectations partly reflected in the raise of interest rates in the money market at the end of the same quarter. The interest rates raise in this market over the second quarter was pushed by the decrease of the liquidity level in the banking system (to ALL 3.1 billion on average from ALL 4.9 billion in the first quarter).

LIQUIDITY PERFORMANCE AND ITS MANAGEMENT

The Bank of Albania intervened in the market through its main instrument, by withdrawing or injecting liquidity of one-week maturity term fixed at 5.50 per cent. As a result, the markets have generally operated with stable interest rates, in particular in the short-term maturity. The interest rate fluctuations were affected by the changes in the liquidity situation in the system. In light of these developments, in the second quarter, in addition to its main instrument, the Bank of Albania used the reverse repurchase agreements of three-month maturity, by injecting liquidity in the market. The average weighted yield of reverse repurchase agreements was 6.20 per cent in the second quarter. On the contrary, during the first quarter of 2007, the Bank of Albania intervened in the market by withdrawing the excess liquidity through the repurchase agreements of three-month maturity. Their average weighted yield was 6.00 per cent.

The interests which resulted from the use of the Bank of Albania's instruments oriented the interest rates in the market. Except for credit interests, interests of short maturity term fluctuated within a narrow range. Interests of long maturity term increased when the demand for liquidity grew in the second quarter of 2007.

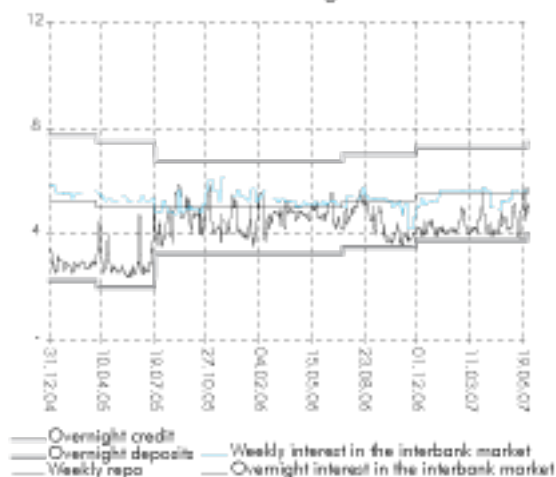


INTEREST RATES PERFORMANCE

The determining corridor of interbank market interests in the money market remained unchanged at minimal levels of 3.75 per cent (overnight deposits interest) and maximum levels of 7.25 per cent (overnight credit interest).

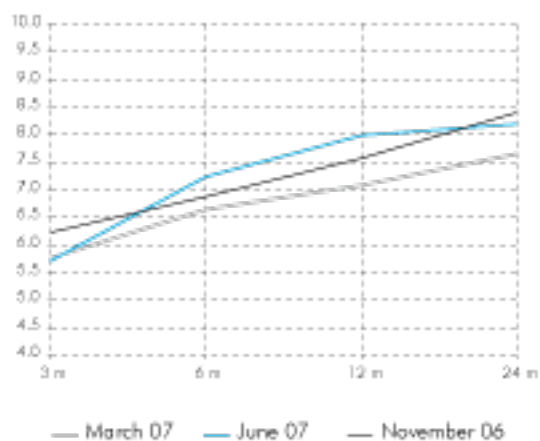
Within this corridor, overnight borrowing interests in the interbank market fluctuated between the lower limit and the core interest rate, while increasing in the second quarter. The average daily change between the core rate and the overnight interest dropped to 0.98 per cent from 1.24 per cent in the first quarter. Weekly borrowing interests fluctuated around the core interest rate, averaging 5.66 per cent. The average daily level of borrowing in the interbank market dropped to ALL 1.6 billion from ALL 1.8 billion in the first quarter and it mainly consists in overnight transactions.

Chart 36 Interest rates in the interbank market and BoA's standing facilities



Source: Bank of Albania

Chart 37 Securities' yield in the primary market



Source: Bank of Albania

The Treasury bills' yield in the primary market¹⁷ increased by almost 1 per cent in the second quarter. As of end June, the 12-month yield reached 7.99 per cent from 7.07 per cent as of end of March. In March, the yields decreased by about 0.50 per cent from the percentage of last November (the last time when the core interest rate changed) affected by the high excess of liquidity (as a result of the seasonal effect and the reduction of the Government demand for monetary assets). The opposite occurred in the second quarter. The ratio of Government demand for financing with Treasury bills and the system's supply for investing in them dropped to 1:1.2 from 1:1.9 in the first quarter.

The expectations for an increase in the core interest rate (which was raised by 25 basis points on 28 June) partly affected the increase of the yield. As of end June, the 12-month yield was 0.40 per cent higher than as of November 2006.

The long-term interest rates in the bonds market fluctuated depending on the ratio of Government's needs for financing and the liquidity conditions. Two-year bonds fell to a minimum of 7.65 per cent in March, along the same line with the Treasury bills yield and increased the following period (by 0.50 per cent on average). Three-year bonds, which are issued on quarterly basis, resulted 8.05 per cent in April, when some banks' bids were refused.

The general trend in the ALL deposits¹⁸ market was the increase of interest rates for all maturity terms throughout the first five months. Calculated as a simple average, the interest rate of 12-month deposits reached 5.69 per cent in May or 0.14 per cent higher than in March and 0.28 per cent higher than in December 2006¹⁹. In the ALL credit market²⁰, the weighted average of loans' interest rates reached to 12.7 per cent in May which is 0.23 per cent less than as of end of the first quarter²¹. The interest rates of loans of 6 months to three years maturity term decreased during this

period, leading to the increase of demand for short-term and medium-term loans.

Intermediation cost, which is measured as the difference between ALL credit interests and ALL deposits interests, is presented in table 8.

| | December '06 | March '07 | May '07 |
|-------------------------|--------------|-----------|---------|
| 6-month credit-deposits | 7.54% | 7.73 | 10.32 |
| 1-year credit deposits | 5.70% | 6.18 | 4.73 |

Source: Bank of Albania

Table 8 Intermediation cost in ALL

Intermediation cost for 6-month maturity terms increased compared with the end of 2006 and the end of March 2007, as a result of the larger increase of ALL credit interest rates than ALL deposits interests rates. Meanwhile, the intermediation cost for one-year maturity term decreased as a result of the decrease in ALL credit interest rates.

EUR deposits interest rates fluctuated over the months; however, they have followed the upward tendency of interest rates in the Euro area. In May the weighted average rate of EUR deposits increased to 3.10 per cent or 0.13 per cent more than the first quarter and 0.30 per cent more than in December.

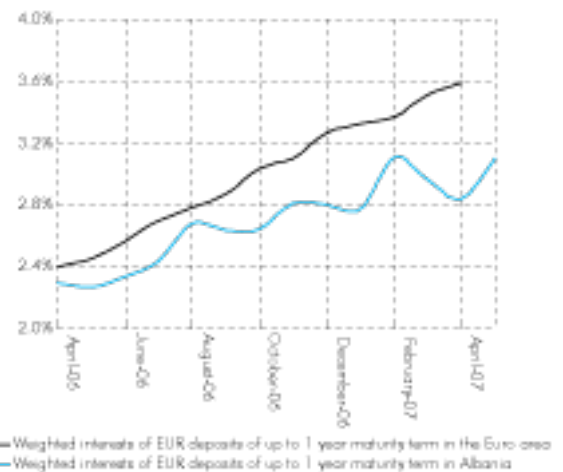
USD deposits interest rates²² dropped for all maturity terms, except for deposits of 1-month and 36-month maturity term. The expectations for the decrease of the core interest rate by the Federal Reserve affected the performance of USD deposits interest rates. The greatest decrease occurred in demand deposits interest rates, which dropped by 0.44 per cent during the second two months of 2007.

The interest rates of foreign currency loans increased in April and May, both for the EUR and the USD. In terms of weighted average, the interest rates of EUR and USD loans reached 8.53 per cent and 11.81 per cent in May. As of end the first quarter, they were 8.13 per cent and 8.86 per cent, respectively²³.

THE EXCHANGE RATE

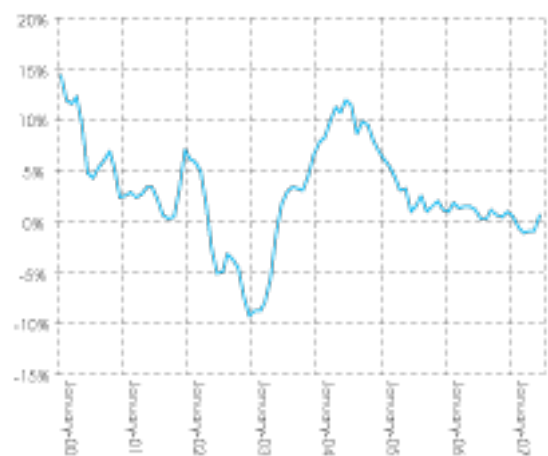
Lek performance in the second quarter of 2007 was different compared with the previous quarter. The depreciating tendency of the lek shifted, being reflected in the swift decrease of the EUR to the ALL in our foreign exchange market. This decrease was originally affected by the low demand for foreign currency in the foreign exchange market (mostly

Chart 38 Interest rates of up to 1 year maturity term in Albania and the Euro area



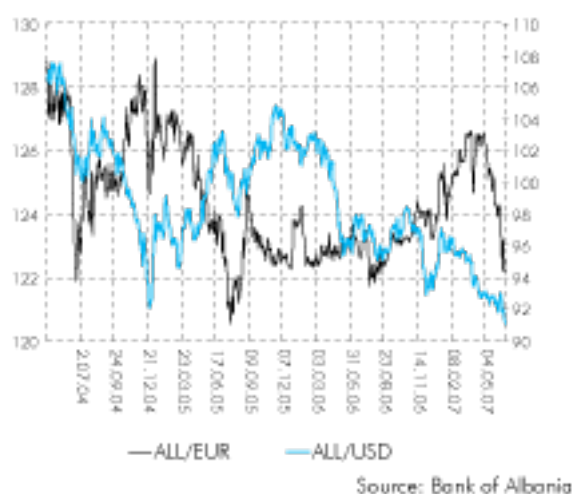
Source: Bank of Albania and ECB

Chart 39 Annual changes of ALL in nominal effective terms (NEER²⁴)



Source: Bank of Albania

Chart 40 Daily performance of
ALL/EUR and ALL/USD



in May). Later, an increase in the supply of foreign currency in June deepened this decrease further, going against the appreciating pressures of the euro in the international market. Compared with the end of March, the lek appreciated by 3.7 and 4.7 per cent to the euro and the dollar.

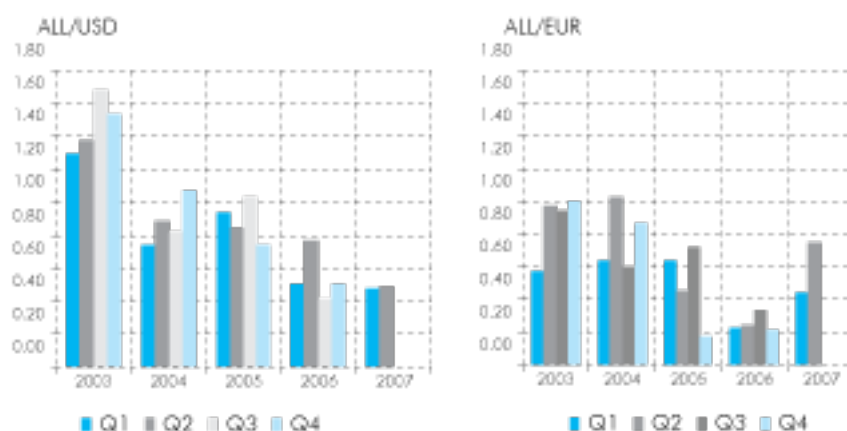
The annual dynamics of the lek performance is presented stable, with moderate fluctuations, which has been a characteristic of the last two years. In June, the lek appreciated in annual nominal effective terms by 0.7 per cent. The stable performance of the lek during the first semester of 2007 was also affected by the macroeconomic environment. The growth of demand in economy, along with the increase in the deficit on current account brought about depreciating pressures on the lek. The

narrowing of the spread between lek - foreign currency interest rates exerted pressure on the same direction.

On the other hand, the low inflation rates have supported the performance of the lek. The rise of the interest rate by the Bank of Albania is expected to increase the spread of interest rates, providing support for the position of the lek.

The seasonal supply in the foreign exchange market has also been exerting appreciating pressures on the lek. The exchange rate performance in the future will depend on the macroeconomic conditions and on the abovementioned factors' influence on the supply and demand for foreign currency.

Chart 41 ALL exchange volatility²⁵ in quarters



6 PERFORMANCE OF ECONOMY OVER 2007

The macroeconomic developments during 2007 provided evidence for a dynamic economic activity in the private sector. The growth of credit to the private sector projected for 2007 is expected to increase the annual money supply rate and aggravate the current account. While in the public sector, the annual framework of fiscal developments does not project any changes in the projections at the beginning of the year. However, the concentration of the public sector's domestic borrowing in the second half of the year will tighten the liquidity conditions in economy for 2007, by exerting pressures on the performance of interest rates. After an analytical assessment of the macroeconomic factors, this June the Bank of Albania tightened its monetary policy by raising the core interest rate to 5.75 per cent. This increase aims to maintain the inflationary expectations in order to achieve the inflation target. In line with these developments, the current projections for the economic growth and the inflation rate for 2007 remain unchanged.

| | 2002 | 2003 | 2004 | 2005 | 2006* | 2007° | 2008° |
|---|---------------------|--------|--------|--------|--------|--------|--------|
| Real economy indicators | (in percentage) | | | | | | |
| GDP growth | 2.9 | 5.7 | 5.9 | 5.5 | 5.0 | 6.0 | 6.0 |
| Annual CPI (average) | 5.2 | 2.4 | 2.9 | 2.5 | 2.4 | 3.0 | 3.0 |
| Nominal GDP (in billions of ALL) | 624.7 | 682.7 | 766.1 | 836.6 | 896.3 | 980.0 | 1,075 |
| Fiscal indicators | (as a share to GDP) | | | | | | |
| Fiscal deficit (with grants) | -6.6 | -4.5 | -5.1 | -3.6 | -3.2 | -3.9 | -3.9 |
| Domestic financing | -3.3 | -2.9 | -2.3 | -2.7 | -2.3 | -2.0 | -2.3 |
| Income | 24.7 | 24.5 | 24.1 | 24.4 | 25.2 | 25.9 | 26.4 |
| Expenses | 31.4 | 29.0 | 29.2 | 28.0 | 28.5 | 29.8 | 30.3 |
| External sector | | | | | | | |
| Trade deficit (in millions of EUR) | -1,214 | -1,248 | -1,307 | -1,617 | -1,752 | -1,985 | -2,031 |
| Current account deficit (%/GDP) ²⁶ | -7.2 | -5.3 | -3.9 | -6.5 | -5.8 | -7.4 | -6.5 |
| Monetary indicators | (as a share to GDP) | | | | | | |
| Money supply (%/GDP) | 65.3 | 65.0 | 65.7 | 68.4 | 74.4 | 79.0 | 83.3 |
| Credit to private sector | 6.4 | 7.7 | 9.4 | 14.9 | 21.8 | 28.7 | 35.0 |
| 12-month T-bills yield | 12.0 | 9.5 | 8.1 | 6.9 | 7.8 | -- | -- |

* Preliminary data.

° Projections.

Source: Bank of Albania, Ministry of Finance, INSTAT

Table 9 Main macroeconomic indicators

MONETARY SECTOR AND MACROECONOMIC BALANCE

The growth of demand for money in economy during the first half of 2007 exceeded the initial projections. Lending rates have been higher as a result of the growth of demand by the private sector and the moderate domination of public sector borrowing. The Bank of Albania has revised the projection for the annual growth of credit to ALL 85 billion from the projections of ALL 63 billion at the beginning of the year. Following this review, as of end 2007 the share of credit stock extended to economy to the GDP is projected at about 29 per cent. Although the public sector's domestic borrowing remains unchanged, the money flows from domestic borrowing in the banking sector are expected to be higher²⁷. This projection is conditioned by the execution

of public expenses within the year. The higher demand for monetary assets, mainly from the private sector, led to the review of the projection for the annual growth of money supply to about 16.3 per cent from the projection of 11.9 per cent at the beginning of the year.

The expected performance of monetary indicators requires a prudent monetary policy which aims to maintain the level of interest rates in harmony with a balanced ratio between savings in economy and national income. The high credit rates have affected the savings-consumption balance and the external macroeconomic position. Hence, the savings rate in economy is projected to account for 18.3 per cent to the GDP in 2007 from the projection of 19.9 per cent at the beginning of the year. Under an unchanged level of investments which were projected to account for about 26 per cent of the GDP, the foreign financing rate increased to about 7.4 per cent of the GDP from the earlier projection of about 6.2 per cent²⁸. This rate implies an aggravation in the current deficit account. During this year, it is expected to be reflected in the increase of trade deficit.

The current lending rates in economy affect the upward tendency of consumption rate in economy. These factors – the high lending rates and the increase of consumption – tend to create inflationary pressures in economy in the medium-run. Moreover, they affect the dropping of savings rate opposed to national income, leading to the aggravation of current account and providing the grounds for misbalances in the foreign exchange market in the future. The accumulation of these factors and their further actualization would infringe the economic growth stability in the future. The Bank of Albania considers the pursue of a monetary policy oriented towards the increase of the current savings rate as a positive factor in the macroeconomic stability in the medium-term.

ENDNOTES

¹ Global PMI Input Price Index is calculated from JLMorgan and NTC Economics in cooperation with ISM and IFPSM.

² DG ECFIN regularly monitors the development of different industries in the economy in EU member countries and candidate countries. These surveys cover industry, services, retail, construction and consumption and through these key indicators business and consumer confidence indices. Another important indicator is the index of industry developments, PMI, where surveys are conducted in production, new orders, raw materials' prices and employment.

³ Bosnia and Herzegovina, Croatia, Montenegro, Macedonia, Serbia and Albania.

⁴ The interests for Bosnia and Herzegovina and Croatia are long-term average weighted; for Serbia total weighted average and for Macedonia weighted interests for credit and deposits in denars. For Greece and Italy is given the rate of deposits to households with up to 1 year maturity term, and the interest rate for new real estates credit. For Kosovo is given the interest of deposits to households with up to 1 year maturity term, and the interest rate of consumer credit.

⁵ Measured against 24 main trade partners in the Euro area.

⁶ Estimated and measured by the Bank of Albania.

⁷ The respective index in the CPI is used as deflator.

⁸ This consideration should not be taken for granted, considering the limited and fragmentized information on agriculture. It is only based on preliminary assessments of experts in this area.

⁹ Respondents in this survey were 615 businesses of production, construction and services.

¹⁰ For this survey were considered only that part of respondents who declared to be employed in the private and public sector. The respondents were about 700 consumers.

¹¹ In the sub-basket of core Consumer Price Index, the normalized share of "bread and grains" is about 10 per cent.

¹² Milk, cheese and eggs.

¹³ The price performance of tradable goods is determined by the level of prices in trade partner countries and their effect is transmitted or amplified through the exchange rate.

¹⁴ The quantitative objectives of the Bank of Albania are part of the new PRGF/EFF 2006-2008 arrangement, signed between the Albanian Government, the IMF and the Bank of Albania in January 2006, and lately reviewed in May 2007.

¹⁵ The objectives in the third and fourth quarter are determined as the amount of monetary flows and the base of December 2006. For the first quarter, the calculation base is December 2005. The change of the base results in a higher level of quantitative objectives for September and December 2007.

¹⁶ See the part on fiscal sector for the budget surplus and its components.

¹⁷ See: Statistical annex, Financial Markets, Table "Interest rates as of end month and their change with previous periods".

¹⁸ The latest data refer to May 2007.

¹⁹ Weighted interest decreased in May and April, as a result of the change in structure by shares of new deposits.

²⁰ The latest data refer to May 2007.

²¹ See: Statistical annex, Financial Markets, Table "Interest rates and their change in the ALL deposits and credit market".

²² See: Statistical annex, Financial Markets, Table "Interest rates of deposits in foreign currency".

²³ See: Statistical annex, Financial Markets, Table "Interest rates of credit in foreign currency".

²⁴ NEER – nominal effective exchange rate measured against two currencies according to an approximate share they have in trade with abroad, EUR (80 per cent) and USD (20 per cent). An increase of the NEER implies an appreciation of the lek.

²⁵ Measured as the quarterly average of exchange rate volatility. Exchange rate volatility is measured by the standard deviation indicator.

²⁶ The data on the current account deficit have been revaluated since 2002.

²⁷ This increase results from the execution of projected expenses for January 2006.

²⁸ The projection of investments has slightly declined by 25.7 per cent compared with the projection of 26 per cent to the GDP at the beginning of this year. Foreign financing rate is the deficit on current account.

STATISTICAL ANNEX

INFLATION

Table 1 Annual inflation rate (in percentage)

| | 2001 | 2002 | 2003 | 2004 | 2005 | 2006 | 2007 |
|-----------|------|------|------|------|------|------|------|
| January | 2.2 | 6.5 | 0.0 | 3.3 | 3.3 | 1.4 | 2.9 |
| February | 1.5 | 7.6 | 1.1 | 4.4 | 1.8 | 1.3 | 2.9 |
| March | 2.9 | 7.5 | 1.3 | 4.0 | 1.6 | 1.5 | 2.7 |
| April | 3.0 | 6.5 | 2.3 | 3.2 | 1.3 | 2.4 | 1.9 |
| May | 2.5 | 4.6 | 2.8 | 2.6 | 2.0 | 3.1 | 1.4 |
| June | 4.0 | 3.7 | 2.6 | 2.9 | 2.9 | 2.4 | 2.0 |
| July | 5.6 | 4.2 | 3.0 | 3.1 | 1.8 | 3.2 | |
| August | 4.1 | 5.5 | 3.0 | 2.7 | 2.3 | 2.9 | |
| September | 3.5 | 5.3 | 2.8 | 2.0 | 3.1 | 2.6 | |
| October | 1.8 | 5.8 | 2.9 | 2.0 | 3.3 | 2.3 | |
| November | 2.8 | 3.7 | 3.4 | 2.2 | 3.0 | 2.9 | |
| December | 3.5 | 1.7 | 3.3 | 2.2 | 2.0 | 2.5 | |
| Average | 3.1 | 5.2 | 2.2 | 3.0 | 2.4 | 2.4 | 2.5 |

Source: INSTAT

Table 2 Contribution of basket constituent groups to total inflation

| | June - 06 | July - 06 | Aug. - 06 | Sep. - 06 | Oct. - 06 | Nov. - 06 | Dec. - 06 | Jan. - 07 | Feb. - 07 | March - 07 | April - 07 | May - 07 | June - 07 |
|--|--------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|---------------|---------------|-------------|--------------|
| Foodstuffs and non-alcoholic beverages | 0.80 | 1.86 | 0.51 | -0.45 | -0.59 | 0.45 | 0.09 | 0.66 | 0.70 | 0.32 | -0.51 | -0.81 | -0.27 |
| Rent, water, fuels and energy | 1.04 | 0.88 | 1.78 | 2.32 | 2.19 | 1.91 | 1.87 | 1.70 | 1.70 | 1.84 | 1.85 | 1.71 | 1.27 |
| Transportation | 0.24 | 0.19 | 0.13 | 0.10 | 0.09 | 0.08 | 0.05 | 0.02 | 0.01 | 0.04 | 0.04 | -0.02 | -0.55 |
| Hotels, café and restaurants | 0.22 | 0.16 | 0.18 | 0.18 | 0.15 | 0.15 | 0.14 | 0.14 | 0.17 | 0.14 | 0.15 | 0.23 | 0.25 |
| Other | 0.15 | 0.15 | 0.24 | 0.40 | 0.40 | 0.32 | 0.40 | 0.34 | 0.35 | 0.35 | 0.35 | 0.30 | 0.30 |
| Total | 2.45 | 3.24 | 2.84 | 2.55 | 2.24 | 2.91 | 2.55 | 2.86 | 2.93 | 2.69 | 1.88 | 1.41 | 2.00 |

Source: INSTAT, Bank of Albania

MONETARY INDICATORS

Table 3 Performance of monetary indicators (in billions of ALL)

| | May - 07 | Monthly change | | Annual change | |
|------------------------|----------|----------------|------------|---------------|------------|
| | | Absolute | Percentage | Absolute | Percentage |
| Currency outside banks | 151.7 | -1.2 | -0.8 | 13.4 | 9.7 |
| Total deposits | 536.9 | 1.2 | 0.2 | 87.0 | 19.3 |
| - in lek | 323.6 | 0.8 | 0.2 | 35.9 | 12.5 |
| - in foreign currency | 213.3 | 0.4 | 0.2 | 51.1 | 31.5 |
| Demand deposits | 141.1 | 0.7 | 0.5 | 6.9 | 5.1 |
| - in lek | 73.5 | -0.6 | -0.7 | -9.1 | -11.0 |
| - in foreign currency | 67.5 | 1.2 | 1.8 | 15.9 | 30.8 |
| Time deposits | 395.8 | 0.5 | 0.1 | 80.1 | 25.4 |
| - in lek | 250.1 | 1.3 | 0.5 | 44.9 | 21.9 |
| - in foreign currency | 145.8 | -0.8 | -0.5 | 35.2 | 31.8 |
| M1 | 225.2 | -1.7 | -0.8 | 4.4 | 2.0 |
| M2 | 475.3 | -0.4 | -0.1 | 49.3 | 11.6 |
| M3 | 688.6 | 0.0 | 0.0 | 100.4 | 17.1 |
| Monetary base | 209.5 | -2.0 | -0.9 | 18.8 | 9.9 |

Source: Bank of Albania

Table 4 Performance of NFA indicators by main groups, May 2007 (in millions of USD)

| | May - 07 | Monthly change | Annual change |
|---------------------|----------|----------------|---------------|
| Net foreign assets | 2,390.0 | - 70.8 | 192.4 |
| Foreign assets | | | |
| Bank of Albania | 1,826.7 | - 19.0 | 257.1 |
| ODC | 1,147.1 | - 33.3 | 218.2 |
| Foreign liabilities | | | |
| Bank of Albania | 103.2 | - 0.9 | - 4.2 |
| ODC | 480.6 | 19.4 | 287.1 |

Source: Bank of Albania

Table 5 Performance of Net Credit to the Government by main groups

| | May - 07 | Monthly change | Annual change |
|--|-----------|----------------|---------------|
| Net claims on the Government | 291,753.4 | - 22.25 | 23,733.6 |
| Bank of Albania | 48,407.9 | 3,627.5 | - 2,545.2 |
| ODC | 243,345.5 | -3,649.7 | 26,278.8 |
| Deposits held with the Bank of Albania | 6,190.6 | - 3,313.4 | - 638.6 |
| Budget deficit | | | |
| | 5,261.0 | 557.7 | - 3,729.8 |

Source: Bank of Albania

Table 6 Performance of some main indicators

| | 2004 | June - 05 | December - 05 | June - 06 | December - 06 | March - 07 | April - 07 | May - 07 |
|---|-------|-----------|---------------|-----------|---------------|------------|------------|----------|
| Money supply (in billions of ALL) | 507.2 | 541.8 | 578.04 | 594.5 | 674.3 | 686 | 688.6 | 688.6 |
| Domestic credit (in percentage to M3) | 68.9 | 69.9 | 70.03 | 71.0 | 71.8 | 73.9 | 74.6 | 75.5 |
| Credit to the Government (in percentage to M3) | 55.1 | 52.2 | 48.94 | 45.3 | 43.4 | 42.8 | 42.4 | 42.2 |
| Credit to economy (in percentage to M3) | 13.8 | 17.7 | 21.10 | 25.71 | 28.4 | 31.1 | 32.2 | 33.1 |
| Credit to economy (in percentage to total assets) | 16.9 | 20.8 | 25.11 | 28.7 | 31.3 | 33.6 | 34.5 | 35 |
| Credit to economy (in percentage to GDP) | 9.0 | 11.2 | 14.57 | 17.6 | 21.3 | 23.4 | 24.1 | 24.6 |
| Credit/deposits ratio (in percentage) | 19.0 | 23.6 | 28.47 | 33.7 | 37.4 | 40.1 | 41.4 | 42.4 |

Source: Bank of Albania

Table 7 Outstanding credit indicators as a share to total

| | 2003 | 2004 | 2005 | Q1-06 | Q2-06 | Q3-06 | Q4-06 | March-07 | April-07 | May-07 |
|---|------|------|-------|-------|-------|-------|-------|----------|----------|--------|
| Outstanding credit (in billions of ALL) | 50.7 | 69.3 | 121.6 | 134.6 | 152.8 | 165.3 | 191.2 | 213.6 | 221.7 | 227.9 |
| Credit to households | 24.5 | 30.6 | 32.3 | 31.9 | 32.3 | 33.3 | 33.4 | 33.8 | 34.2 | 34.6 |
| Credit to private sector | 75.5 | 69.4 | 67.7 | 68.1 | 67.6 | 66.7 | 66.5 | 66.2 | 64.7 | 64.4 |
| Short-term credit | 46.0 | 34.0 | 32.3 | 32.5 | 31.1 | 30.0 | 29.6 | 30.5 | 30.7 | 31.1 |
| Medium-term credit | 33.3 | 36.0 | 29.7 | 30.0 | 31.2 | 32.6 | 31.6 | 30.6 | 30.2 | 29.7 |
| Long-term credit | 20.7 | 30.0 | 37.9 | 37.5 | 37.7 | 37.4 | 38.8 | 38.9 | 39.1 | 39.3 |
| Lek | 19.6 | 19.5 | 26.6 | 26.0 | 28.2 | 29.8 | 28.9 | 28.0 | 28.1 | 28.6 |
| Foreign currency | 80.4 | 80.5 | 73.4 | 74.0 | 71.8 | 70.2 | 71.1 | 72.0 | 71.9 | 71.4 |

Source: Bank of Albania

Table 8 New credit indicators as a share to total

| | Total | 2005 | | | | 2006 | | | | March | April | May |
|---------------------------------|-------|------|------|------|------|------|------|------|------|-------|-------|------|
| | 2004 | Q1 | Q2 | Q3 | Q4 | Q1 | Q2 | Q3 | Q4 | -07 | -07 | -07 |
| New credit (in billions of ALL) | 99.7 | 22.1 | 32.8 | 32.1 | 32.9 | 29.4 | 35.7 | 35.8 | 53.9 | 18.9 | 20.2 | 20.2 |
| Short-term credit | 62.54 | 53.2 | 47 | 47.4 | 48.7 | 44.2 | 42 | 45.8 | 46.7 | 52.1 | 55.1 | 48.3 |
| Medium-term credit | 22.53 | 22.4 | 31 | 30.3 | 25.6 | 30.1 | 33 | 31.2 | 27.4 | 23.9 | 20.5 | 19.7 |
| Long-term credit | 14.93 | 24.4 | 22 | 22.2 | 25.7 | 25.7 | 26 | 23.0 | 25.9 | 24.0 | 24.4 | 32.0 |
| Credit in lek | 32.59 | 30.1 | 32.8 | 30.2 | 31.4 | 27.7 | 35 | 39.6 | 26.2 | 35.5 | 32.1 | 37.8 |
| Credit in foreign currency | 67.41 | 70 | 67.2 | 69.8 | 68.6 | 72.3 | 65 | 61.4 | 73.8 | 64.5 | 67.9 | 62.2 |

Source: Bank of Albania

Table 9 Distribution of credit by sectors of economy (in percentage to total)

| | Q1- '05 | Q2- '05 | Q3- '05 | Q4- '05 | Q1- '06 | Q2- '06 | Q3- '06 | Q4- '06 | March- 07 | April- 07 | May- 07 |
|--|------------|------------|------------|------------|------------|------------|------------|------------|--------------|--------------|------------|
| Agriculture, hunting and silviculture | 1.3 | 1.5 | 2.4 | 2.7 | 2.2 | 0.9 | 0.7 | 0.7 | 0.6 | 0.7 | 0.8 |
| Fishing | 0.01 | 0.1 | 0.1 | 0.1 | 0.1 | 0.1 | 0.11 | 0.1 | 0.4 | 0.1 | 0.1 |
| Extracting industry | 2.35 | 0.6 | 0.5 | 0.5 | 1.4 | 2.3 | 1.0 | 1.0 | 1.4 | 1.5 | 1.5 |
| Processing industry | 15.8 | 15.6 | 13.9 | 13.8 | 14.2 | 15.3 | 15.5 | 14.3 | 13.4 | 13.2 | 13.0 |
| Production and distribution of energy, gas and water | 6.27 | 2.9 | 2.9 | 2.6 | 2.4 | 1.1 | 1.2 | 1.5 | 1.7 | 2.5 | 2.4 |
| Construction | 10.6 | 11.2 | 12.8 | 13 | 13.0 | 12.2 | 12.6 | 12.6 | 12.5 | 12.6 | 12.8 |
| Trade, repair of vehicles and household appliances | 20.5 | 19.1 | 20 | 18.9 | 19.0 | 22.5 | 23.1 | 22.4 | 22.0 | 21.5 | 20.9 |
| Hotels and restaurants | 2.5 | 4.7 | 4.4 | 4.3 | 4.8 | 4.1 | 3.9 | 3.5 | 3.4 | 3.5 | 3.5 |
| Transportation and telecommunication | 2.5 | 1.7 | 1.7 | 1.5 | 1.3 | 1.6 | 1.6 | 2.0 | 2.0 | 1.9 | 1.9 |
| Financial activities | 0.2 | 1.1 | 0.7 | 0.8 | 0.7 | 1.3 | 0.7 | 2.1 | 1.9 | 1.9 | 1.9 |
| Health and social activities | 0.1 | 0.4 | 0.6 | 0.7 | 0.6 | 0.6 | 0.3 | 0.0 | 0.3 | 0.3 | 0.4 |
| Collective, social and personal services | 8.3 | 7.4 | 5.9 | 5.8 | 4.6 | 1.7 | 2.0 | 0.6 | 2.5 | 2.1 | 2.5 |
| Other* | 29.6 | 33.7 | 34.1 | 35.4 | 35.7 | 36.2 | 35.1 | 39.2 | 37.8 | 38.2 | 38.3 |
| Total | 100 | 100 | 100 | 100 | 100 | 100 | 100 | 100 | 100 | 100 | 100 |

Source: Bank of Albania

*"Other" includes credit extended to some sectors sharing a small weight in the country's economic activity and credit to households. Upon the introduction of new credit forms it was required to review the credit distribution by sectors, where the new classification was introduced.

FINANCIAL MARKETS

Table 10 End-month interest rates and their change compared with previous periods (in percentage points)

| | June '07 | Change June '07-March '07 | Change March '07-December '06 |
|-------------------------------|----------|------------------------------|----------------------------------|
| Core interest rate | 5.50%* | +0.00 | 0.00 |
| Interbank market | | | |
| Overnight interest | 5.12 | 0.61 | -0.01 |
| Weekly interest | 5.67 | -0.01 | 0.44 |
| Primary market | | | |
| 3-month Treasury bills yield | 5.83 | -0.01 | -0.75 |
| 6-month Treasury bills yield | 7.23 | 0.59 | -0.47 |
| 12-month Treasury bills yield | 7.99 | 0.86 | -0.64 |
| Bonds market | | | |
| 2-year bonds yield | 8.20 | 0.55 | -0.75 |
| 3-year bonds yield | 8.05 | -0.85 | 0.10 |
| 5-year bonds yield | 9.83 | -0.31 | 0.46 |

Source: Bank of Albania and commercial banks

* The Bank of Albania raised its key interest rate by 25 basis points, from 5.5 to 5.75 per cent on 27 June 2007.

Table 11 Interest rates and their change in the lek deposits and credit market (in percentage points)

| | May '07 | Change May '07- March '07 | Change March '07 – December '06 |
|--------------------------------------|---------|------------------------------|------------------------------------|
| Core interest rate | 5.50 | 0.00 | 0.00 |
| Interest of ALL-denominated deposits | | | |
| 1-month | 3.96% | 0.57% | 0.04% |
| 3-month | 3.68% | -0.34% | 0.08% |
| 6-month | 4.55% | -0.09% | 0.00% |

| | | | |
|------------------------------------|--------|--------|--------|
| 12-month | 5.39% | -0.09% | 0.02% |
| 24-month | 5.64% | -0.35% | 0.11% |
| 36-month | 7.00% | 0.82% | -0.24% |
| Interest of ALL-denominated credit | | | |
| Up to 6-month credit | 14.87% | 2.50% | 0.19% |
| 6 month to 1-year credit | 10.12% | -1.54% | 0.50% |
| 1-3 years credit | 16.69% | -0.29% | -0.72% |
| Over 3-year credit | 13.18% | 0.67% | 0.30% |

Source: Bank of Albania and commercial banks

Table 12 Interest rates of deposits denominated in foreign currency (in percentage points)

| | May '07 | Change May '07 – March '07 | Change March '07 – December '06 |
|--------------------------------------|---------|-------------------------------|------------------------------------|
| Fed – Core interest rate | 5.25% | 0.00 | 0.00 |
| Interest of USD-denominated deposits | | | |
| 1-month | 3.32% | 0.13% | 0.16% |
| 3-month | 3.61% | -0.02% | 0.19% |
| 6-month | 3.77% | -0.15% | 0.05% |
| 12-month | 4.74% | -0.01% | 0.46% |
| 24-month | 4.68% | -0.11% | -0.07% |
| ECB – Core interest rate | 3.75%* | 0.00 | +0.25 |
| Interest of EUR-denominated deposits | | | |
| 1-month | 3.02% | 0.32% | 0.16% |
| 3-month | 3.33% | 0.17% | 0.25% |
| 6-month | 3.37% | -0.06% | 0.14% |
| 12-month | 3.92% | 0.13% | 0.34% |
| 24-month | 4.11% | -0.13% | 0.08% |

Source: Bank of Albania and commercial banks

* In June 2007 it was raised by 25 basis points to 4.00 per cent.

Table 13 Interest rates of credit denominated in foreign currency (in percentage points)

| | May '07 | Change May '07 – March '07 | Change March '07 – December '06 |
|------------------------------------|---------|-------------------------------|------------------------------------|
| Interest of USD-denominated credit | | | |
| Up to 6-month credit | 12.25% | 2.99% | -0.50% |
| 6-month to 1-year credit | 9.84% | 0.75% | -0.02% |
| 1-3 years credit | 12.06% | 5.97% | -3.91% |
| Over 3-year credit | 11.00% | 1.79% | 0.15% |
| Average weighted interest | 11.81% | 2.95% | -0.56% |
| Interest of EUR-denominated credit | | | |
| Up to 6-month credit | 7.96% | -0.01% | 0.34% |
| 6-month to 1-year credit | 8.33% | 0.61% | -0.73% |
| 1-3 years credit | 9.51% | 1.41% | -0.35% |
| Over 3-year credit | 8.50% | 0.05% | 0.11% |
| Average weighted interest | 8.53% | 0.40% | -0.05% |

Source: Bank of Albania and commercial banks

INTERVIEW BY MR. ARDIAN FULLANI, GOVERNOR OF THE BANK OF ALBANIA

to Voice of America during the Spring Meetings of the World Bank and the International Monetary Fund
Press office, April 19, 2007

Question: Mr. Governor, you have come to Washington for the Spring Meetings of the International Monetary Fund. What have you discussed during the meetings with Fund's officials?

Spring meetings are an extremely important occasion for member countries to meet with highest representatives of the IMF, but simultaneously to talk with other colleagues and representatives of important international institutions about the development policies, a country's development perspectives, and about the policies a country should follow on the basis of political-economic programs.

A characteristic of this meeting was that the Deputy Managing Director of the International Monetary Fund, Mr. Murilo Portugal confirmed to come to Tirana in May. It is the first time that such a high personality of the IMF is coming to Albania and undoubtedly, this indicates a maturity of Albania and a greater commitment of the IMF to support the reforms in Albania.

Dealing a little bit with the macroeconomic stability of the country: For some years it is said that Albania has a stable macroeconomic situation and a growth fluctuating within the limits of 5-6 percent, while it is known that the Albanian economy is largely based on services system, instead of being based on industrial output. Under these conditions, how will this economic growth be maintained in the future?

The economic growth of a country is important. Economic issues are always open for discussion in such meetings with the IMF and beyond it. The main elements are the ones related to structural reforms. Therefore, it is very important to carry out reforms at planned paces, in order to maintain these high development rates.

Which are some of these elements?

Energy is one of the key problems to which we should pay a special importance. Solutions to the energy problem should be long-term and steady ones, guaranteeing not only the supplying of the economy with energy, but also at low costs.

It is largely spoken about the Albanian economy informality. How much has it really damaged the economy?

I am not of the opinion that informality in Albania or elsewhere can be eliminated by means of slogans or campaigns. Our strategy has been as

follows: reduction of informality comes naturally, by establishing a broad structure of services. The financial and banking system development itself, credit sector development, payments and banking sector development, have made Albania presently enjoy a qualitative financial service, providing a large variety of products, naturally leading to reduced informality. Credit growth in the country by 50 to 60 percent a year, increased banking activity through banks' windows, increased volume of transactions carried out through banks compared to those in cash, development of international payments and of many new banking products for absorbing officially the emigrants' remittances, are factors that have obviously influenced on curtailing informality in Albania.

Do you see any risks in such a rapid growth of credit to Albania, under the conditions when no necessary rules exist for controlling this phenomenon?

We should take into account that two years ago, the credit to the Albanian economy was 7 percent of GDP, whereas currently it has reached 21 percent of GDP. Actually, this is a process of constant growth, but based on our analysis, this is not an uncontrolled growth. There is noticed increased financing, not only for consumer goods but also for investments. Also, the variety of products supplied by banks has increased, with regards to loans for house purchases and consumer loans, which have undergone a natural development.

SPEECH BY MR. ARDIAN FULLANI, GOVERNOR OF THE BANK OF ALBANIA

At the presentation of the 2006 Annual Report of the Bank of Albania
before the Economy and Finance Commission of the
Parliament of the Republic of Albania
Tirana, 25 April 2007

Honourable Mr. Chairman,

*Honourable ladies and gentlemen, members of the Economy and Finance
Commission,*

It is a special privilege for me to present to you, pursuant to law requirements,
the 2006 Annual Report of the Bank of Albania.

This report provides a summary of the Bank of Albania activity in implementing
the legal and constitutional obligations. First of all let me focus on the
national economy performance, and then on more specific parts related to
the institutional responsibilities and direct contributions of the Bank of Albania
to subduing inflation, maintaining financial stability, enhancing the financial
infrastructure and on our role to European and regional integration.

1. ECONOMIC DEVELOPMENTS OVER 2006

The country's economic development over 2006 has generally complied
with its medium-term development plan. The overall Albanian economy has
undergone comparably satisfactory growth rates, due to the private sector's
dynamism, macroeconomic stability and the fruits of the so-far structural
reforms. The banking system has provided a powerful incentive to economic
activity sustainability and to growth of credit to the economy by about ALL 70
billion or above USD 700 million.

Based on available economic indicators, the growth rate is estimated at
about 5 percent. This growth has been associated with price stability, reflected
in an annual average inflation rate of 2.4 percent. The monetary conditions,
characterised by historically low interest rates and exchange rate stability
have favoured the rise of investments and consumption in the economy. In
particular, they have also been reflected in rapid credit growth, by further
sustaining the economy growth. The fiscal developments have taken place
within the programmed limits, contributing to further consolidation of public
finances and budget deficit control.

However, the realization of capital expenditures requires a larger focus on
the programmed level, as concerns the pace these expenditures have been
carried out.

The economic growth has been reflected also in the labour market. The
number of employed persons in the country has boosted, though it has not yet

fully reflected the developments in other sectors of the economy. The country's economic activity extension has been associated with increased foreign trade exchanges. The balance of payments has been closed in positive terms, thus supporting the exchange rate stability.

The quantitative and qualitative indicators of economic performance show a satisfactory growth, based mainly on the activities of services and industrial production. The sales carried out by economic enterprises during the first nine-month period accounted for about 11 percent higher than in 2005. The fact that the first quarter recorded a high annual growth of sales shows that services and production enterprises overcame the problems entailed by power supply constraints at end of 2005. The industry sector, particularly the process industry has recorded positive developments. The country's trade activity continues to ensure the majority of sales, and to record significant annual growth rates.

It is estimated that construction sector has performed almost at the same level with that of the previous year. Direct and indirect indexes of this sector impose the necessity for a broader attention, particularly to a better allocation of private or public financial resources. Construction developments over the recent years, and particularly the extreme concentration of constructions on certain territories, prove the lack of efficient urban development policies, without guaranteeing long-term sustainability of the branch. Furthermore, construction continues to be dominated by housing buildings, lagging behind other strategic items, such as investments in road infrastructure, in industrial constructions, in land improvement and in agricultural infrastructure, as well as other investments directly related to the standard of living of small urban and rural communities.

Agricultural production during 2006 partly recovered the growth rate decline noticed in 2005. The sector growth projection stands at 2.5 per cent for 2006, higher than the growth of 2005, but lower than the average growth rate noticed over five latest years. Investments in agricultural sector and financing by the banking system will increase in accordance with the potential of this branch, providing that hurdles arising from various structural problems are eliminated.

Agricultural land is not used at maximum, because of external and internal migration and the problems with ownership titles. The relatively underdeveloped rural infrastructure makes more difficult the emerging of products in the market. The parcelling out of agricultural land impedes the effective organisation of production, decreases the profitability and raises the agricultural mechanics utilization cost.

The Bank of Albania deems that energy remains our main challenge in the short-run and in the medium-run.

We have been faced with underlined power supply constraints for about a decade. The current crisis coincidence in time with a global environment that is

rather sensitive to this problem has relatively increased the energy import costs, which could be unsustainable in the long run. It has resulted out of Bank of Albania surveys that the negative consequences arising from this situation are numerous and directly related to the economic activity of the productive sector, in both levels, corporate and small and medium sized enterprises. The frequent recurrence of such situation poses the risk that periods of significant power constraints are no longer regarded as accidental shocks, but they are more and more classified as permanent factors that should be factorised in the production cost, and hence should be taken into account in pricing policies and their expectations.

To this end, the Bank of Albania estimates that, starting from 2007, all the respective decision-making stakeholders should apply a new concrete management policy, different from the 15-year practice. An integral part of it should be not only the management of current energy resources, but also concrete steps in the distribution network, as short-term measures to pass to long-term operations, which would imply the establishment of alternative energy sources. The solution of the energy situation at the soonest time possible will provide positive impacts on the Albanian business, the soundness of public finances, the country's sustainable economic development and the macroeconomic stability.

Concluding this part, I would like to point out some other issues, which I think should be encompassed in the priority list of the country's medium-term economic and financial development. The Albanian economy is leaving the status of a transition economy and is approaching to that of a developing economy. This qualitative step requires further deepening of structural reforms, enhancement of effectiveness of development policies and enlargement of the country's absorbing capacities in terms of fostering the Albanian economy competitiveness at regional context and beyond it.

I would highlight the constant trade deficit deepening, as an issue of the present and the future. Even though the current cross-border position of the country is not problematic, being materialised in such indicators as external debt, foreign reserve level or overall balance of payments position, I would point out that the rise of exports is not sufficient, particularly in the context of high reliability of the Albanian economy on remittances. The relatively high current deficit, around 7.6 percent of GDP, is another argument in this regard. The latter one, also in the presence of a fiscal deficit, increases our economy's exposure and makes necessary the provision of foreign currency inflows of a more steady nature. This would be translated into a need for more qualitative foreign direct investments, which in turn, would contribute to a steady growth of exports.

To this end, taking advantage of the global environment, which is constantly searching for new markets, I would suggest a more qualitative national marketing strategy. This strategy should highlight professionally and contemporarily, all the recent incentives and the multiple opportunities Albania provides. Also, I think it is just the time to integrate even the joint regional projects into our long-term development plans. Road infrastructure, energy, communication, tourism and other areas are still underdeveloped in regional level. Therefore, I assess that regional projects of strategic nature

raise the interest of domestic and foreign investors. If taken separately the economies of the region are relatively small, but altogether they form an attractive market, with more investment opportunities.

In recent years, it is noticed that the penetration of foreign investments in our region is relatively small and mainly, it reflects the privatization process of important public properties. The same thing has occurred to the Albanian economy. More concretely, during 2000 – 2006, the overall foreign direct investments, according to the balance of payments statistics, are estimated to about usd 1.45 billion, about 3.5 percent of GDP realised over the same period.

If we would identify the reasons why FDI inflows are so modest, we might mention the complex problems characterising our region, while different reasons that reduce the absorbing capability of our economy exist even in the national plan.

The Bank of Albania deems that the country's current stage of development creates great possibilities in this regard. The experience of the newly acceded countries has indicated that the signing of the Stabilisation and Association Agreement and the following negotiations have been associated by high FDI inflows. However, we can not assume that this phenomenon will be automatically present even in Albania. Therefore, the Bank of Albania deems that further deepening of structural reforms is necessary and that this process should be followed by improvements in the business climate and by enhancement of the degree of law enforcement.

The last but not the least, I would like to point out that the degree of economic activity coverage with statistics is still low. The monetary policy that we are following is an as much dynamic as visionary process. Besides the existence of efficient markets, it also needs to be supplied with new and methodologically accurate statistics.

Besides our constant efforts and good understanding with INSTAT, we find it necessary to appeal for a greater attention of the whole society and of respective institutions in particular, to increasing statistical information and further consolidating the existing one. It is just the time that all the monitoring, licensing and decision-making institutions, including also the numerous non-governmental organisations, must feel a great responsibility in this regard. It is just the moment that they develop indirect measuring and estimating approaches for many demographic, economic, social and financial indicators.

Let me now present another important issue in my speech, which has to do with one of the main legal responsibilities of the Bank of Albania, i.e., consumer price stability.

2. INFLATION AND MONETARY POLICY

Consumer goods price inflation over 2006 was generally within the Bank of Albania's targeted range of 2 to 3 percent. Year-end recorded a 2.5 percent

annual inflation rate. It was almost similar to the 2005 annual inflation rate of 2.4 percent. Inflationary pressures, though moderate, have been increasing over 2006. The average annual inflation rate amounted to 2.7 percent during the second six-month period of the year, from 2.0 percent it was in the first half of the year.

In general, the annual average inflation steadiness during the recent years, speaks for the inflation rate stability, in spite of the fluctuations in time and size of the factors that have conditioned the consumer price performance. Developments on the demand and supply side of the economy have been balanced, without creating premises for inflationary pressures.

The fiscal policy has observed the programmed indicators on annual basis, stabilizing the impact of the public sector component on the aggregate demand. Also, the monetary policy has controlled liquidity conditions and interest rate developments, and has attended the exchange rate performance, monitoring through them the economic activity financial stimuli. On the other hand, the low inflation rates in the recent years have been reflected in anchoring the inflationary pressures of the economy close to the Bank of Albania's target. The latter might have contributed to constraining the second-round effects that may be caused in the Albanian economy by some supply shocks, such as high oil prices and managed price rises, with which the Albanian economy was faced.

- MONETARY CONDITIONS AND MONETARY POLICY DECISIONS

Monetary policy decisions on the key interest rate in the economy have been taken on the basis of constantly analysing the current and expected developments of the demand and supply factors springing from internal and external environment. Under the conditions when an enlivening of inflationary pressures was evidenced and in the presence of a number of factors expected to further favour this situation, the Bank of Albania decided on changing its monetary policy stance, at the beginning of the third quarter of 2006. This change occurred after a neutral period that had lasted about one year and a half. The monetary policy change was materialised in raising the key interest rate twice during the second half of 2006. In July and November 2006 the one-week repo rate was lifted respectively by 0.25 percentage point. The maturity in monetary policy decision-making was reflected in the time lag between both tightening movements in the interest rates.

In July-November 2006, many assessments have been made on the degree of banking market response and sensitivity to monetary policy stance on interest rates. The interest rate rise by 0.5 percentage point is estimated to have normalised the annual monetary supply growth rates, fully responding to the public and private sector demand for monetary assets. Monetary policy operations have assisted in stabilizing inflationary pressures of economic agents in the medium run.

- FISCAL POLICY

The Bank of Albania has estimated that during 2006, the fiscal policy provided a satisfactory support to inflation developments. Fiscal indicators

were realised in accordance with the budgetary program, preventing premises for inflationary pressure rise in the economy. During the fourth quarter of 2006, a high concentration of budgetary spending was noticed. The budget deficit realization as of year-end, estimated at about 3.2 percent of GDP or 0.7 percentage point less than that of the previous year, has influenced on the contraction of inflationary pressures and control of monetary expansion.

- DEMAND FACTORS

During 2006 domestic demand has significantly sustained the positive economic growth rates. Good performance of the domestic demand has been indicated by a number of economic activity indicators. Hence, the sales index for the first nine-month period of the year recorded an annual growth of 12.4 percent. In particular, the rise of imports of machinery and equipment and the real estate credit growth are indicators of investment expansion in the country. The domestic demand has been increasing also due to rapid growth of lending activity, which recorded a 57 percent increase in annual terms. Notwithstanding the positive effects of investment expansion, the domestic demand growth exercises pressure on the overall price rise.

In absence of any obvious inflationary pressures on the demand side, it is estimated that the Albanian economy is making use of free capacities without raising the costs and final prices of goods and services. Also, it should be highlighted that part of this domestic demand has been met by rise of imports and trade deficit, thus mitigating the pressure on consumer prices.

- SUPPLY FACTORS

Import prices. The Albanian economy is a relatively open economy and therefore, import prices constitute an important element of the country's inflation. Generally speaking, the economic conditions of trade partner countries of Albania have been favourable during this year, easing the control on supply side pressures and enabling the observance of inflation target.

Oil prices: Consumer prices during 2006 were influenced by a stressful situation in the interbank oil price market. The impact of this factor, as concerns the intensity of operation in inflation rate, was not uniform, being higher during the first nine months of the year and recording a decline during the last quarter.

Exchange rate: During 2006 exchange rate developments have dampened inflationary pressures of the supply side. The national currency has been appreciated against the American dollar and has maintained unchanged its position vis-à-vis the euro. The lek's appreciating tendencies, though weakened in the recent months, have led to the decline of import price in domestic currency. In this way, the exchange rate has contributed to containment of the high international oil price effect and to maintaining a low inflation rate.

Agricultural production: Agricultural production is one of the main domestic factors, which condition the consumer price developments. The quantity of domestic agricultural production influences instantly on foodstuff price level. During 2006, the seasonal effect of agricultural production rise appeared

later than in the preceding years, leading to foodstuff price decreases only in September and October.

Production prices: During 2006 the production prices continued the downward trend noticed since April 2005. However, the concentration of production price index on the productive sector of industry makes difficult its comparison to consumer price index. Also, the domestic production share is not yet a determinant component of goods supply in the domestic market, thus not affecting the consumer prices.

Wages and unemployment: The good performance of the economic activity during 2006 was also reflected in labour market indicator, and particularly in unemployment rate. New employment possibilities were created, making unemployment rate continue its downward trend observed since more than two years ago. Improvements have also been made in terms of incomes. So, government sector wages, the minimum wage and pensions have increased in accordance with the budget plan. The so-far inflation performance shows that Albanian economy does not suffer from any significant discrepancy between wage rise and productivity.

Inflationary expectations: The business and public expectations in short- to medium-term have fluctuated around the inflation rates recorded. According to Bank of Albania periodic estimates, the public expectations have converged, mostly around 1-3 percent. In the meantime, the business expectations on price performance have reflected a high volatility. The monetary policy and the consolidation of macroeconomic stability have played an important role in anchoring the expectations of public at large to Bank of Albania's inflation targeted rate.

3. MONEY SUPPLY

During the major part of 2006, monetary indicators have reflected the stabilised demand for monetary assets. The average M3 growth rate resulted to 12 percent. The demand for money of the public sector grew by 3.3 percent during 2006. This relatively low borrowing has balanced the high lending rates of the private sector, positively impacting on the maintaining of monetary stability. In compliance with the trend noticed over the latest years, monetary developments have been characterised by shifting to longer-term monetary assets.

Currency outside banks has followed the general trend of the demand for money. The currency outside banks to M3 stood at 24.2 percent at year-end or 1.7 percentage points less than in the previous year. In nominal terms, the currency outside banks grew by ALL 13.6 billion or 9.1 percent.

The macroeconomic environment during 2006 has been favourable for a steady growth of banking system lek deposits. The positive real interest rates have been associated with further rise of lek deposits. They rose by 38 billion during 2006, satisfying the needs of the economy for ALL 35.9 billion and the needs of the government for credit in ALL.

In 2006 foreign currency deposits rose by about 29.4 percent. The higher growth rate of foreign currency deposits versus the money supply growth rate led the ratio of foreign currency deposits to M3 to about 29 percent. The share of foreign currency deposits to total deposits rose to 38.5 percent, against 35.5 percent in 2005.

4. DEMAND FOR MONEY

The increase in the demand for money reached its peak in December, by an annual rise of 16.7 percent. The main contribution to the increased demand for money throughout the year was rendered by credit to the economy. This contribution recorded its maximum in June, being mitigated during the coming months due to growth of public borrowing. Foreign currency position has maintained a relatively steady weight in establishing monetary assets during the year.

- CREDIT TO THE ECONOMY

The banking system developments and the increased role of banks as financial intermediaries, have led to significant expansion of lending activity during the recent years. The loans portfolio amounted to ALL 191.2 billion or 21.3 percent of GDP at end of 2006. The loans portfolio for the economy constituted 31.3 percent of total banking system assets and about 37.4 percent of the banking system deposits.

During 2006, credit to the economy increased by ALL 69.3 billion in absolute terms, compared to ALL 52 billion in 2005. During two latest years, commercial banks have better met the increasing demand for ALL loans, which at end of 2006 constituted 29 percent of the loans portfolio, thus evidencing a moderate extension of its share.

Corporate credit constitutes the main share of banks' portfolio, amounting to 66.5 percent of the total at end 2006. In annual terms, corporate credit increased by 52 percent. The credit distribution structure by use has tended to be more uniform in comparison with the previous year. Most of corporate loans (34.5 percent) have been used for purchasing machinery and equipment, while 23.2 percent of corporate loans portfolio has been used for financing investments in activity area expansion.

In 2006 the household credit was 7 percent of GDP, or 33.5 percent of the total loans portfolio. More than half of loans to households (59.3 percent) have been extended for financing real estate purchases, while the financing of consumer goods purchases has also increased. The ratio of consumer loans to total household portfolio is 27.3 percent, from 20 percent in the previous year. In particular, consumer loans increased obviously during the summer holidays and during the end-year celebrations.

Concerning lending to specific sectors, it should be underlined that trade remains the sector mostly credited by the banking system, by 22.4 percent of the loans portfolio. The growth rate of credit to construction has been inhibited

during 2006. This sector presented temporary improvement signs during the summer, then turned back to the downward trend. In the meantime, the low volume of credit to agriculture speaks for constant structural problems that inhibit lending to this sector.

Given the geographical coverage with loans, it is observed that 68 percent of the portfolio is concentrated in Tirana. Durrës and Vlora come afterwards, by respectively 8 and 4 percent of the loans portfolio. This reveals the high economic importance of Tirana, and the need for improving the economic infrastructure in the rest of the country.

- NET FOREIGN ASSETS

The foreign currency position of the banking system improved during 2006. Net foreign assets of the banking system amounted to US\$ 2.4 billion at year-end, recording an annual growth of about US\$ 440 million.

- GOVERNMENT DEMAND FOR MONEY

The government account has had an unusual performance during 2006. During the major part of the year, the government demand for money was negative, concentrating the planned domestic borrowing on two last months of the year. The overall deficit financing for 2006 resulted to about ALL 22.6 billion.

5. FINANCIAL MARKET AND INTEREST RATES

Year 2006 was characterised by an increased activity in money and capital market, while the interest rate performance was generally oriented by the Bank of Albania's monetary policy. Under the conditions of excess liquidity, the interest rates had a downward trend during the first half of the year. The interest rates went upward after the tightening signal of monetary conditions in the second half of the year.

The interbank market was more active during 2006, thus ensuring a more efficient way of banks' excess liquidity management. The average daily volume of transactions amounted to ALL 1.6 billion or ALL 0.2 billion more than the previous year average. The interbank market was characterised by narrowing the interest rate spread according to maturities and their positioning close to key interest rate. The average overnight-weekly interest rate spread dropped to 0.7 percentage point in 2006, from 1.6 percentage points in 2005.

In the first half of 2006, there was a constant decline in treasury bills yields and government bonds, due to low government demand for funds. In the second half of 2006, following the Bank of Albania's tightening signals and the increased demand for liquidity in the system, there was a gradual rise of these yields. The yields increased respectively by 0.83, 0.45 and 0.98 percentage point in comparison with the previous year.

The government bonds issues has increased compared to the previous year, making the banks' portfolio, as the sole participants in this market, increase to

ALL 37.0 billion. The share of bonds to total government securities increased 22 percent in 2006 from 12 percent in the previous year. Their maturity structure varies from 2 to 5 years. Five-year bonds were issued for the first time in November of this year, for the amount of ALL 6.3 billion. The demand for them resulted higher than the issued amount.

Lek deposit interest rates went down during the first half of 2006, and up after the tightening monetary policy signals. The interest rates were raised faster for long-term maturities, reflecting the adjustment of their term to long-term government debt rise.

Lek credit interest rates went down for all maturities during 2006. The weighted average interest in December 2006 fell to 12.92 percent, from 13.50 percent it was in the previous year. Though the intermediation cost declined in comparison to the previous year, the spread level is still high. It is influenced by imperfect competition in this market and by higher risk nature of loans extended in ALL.

The interest rates of deposits denominated in lek and euro continued to go up, as a result of monetary policy tightening by the Fed and the European Central Bank during 2006. Simultaneously, the interest rates of loans extended in these currencies went up. The interests of six-month to one-year loans in Euro and six-month loans in usd underwent the highest rise. At end of 2006, the weighted average interests of loans in usd amounted to 9.42 percent and interests of loans in Euro amounted to 8.17 percent, from 8.47 percent and 7.95 percent they were respectively at end of the previous year.

6. EXCHANGE RATE

During 2006, the Albanian lek has maintained its appreciating trend against the principal foreign currencies, though at a low intensity. In effective nominal annual terms, the lek has been appreciated on average by 1.1 percent during 2006. During the previous year, this appreciation was 2.8 percent. The lek-foreign currency interest rate spread, though downward during three latest years, continued to be at positive levels.

Economic developments during 2006 have sustained a stable domestic currency. The lek's appreciating pressures have been concentrated mainly on July - August and December. Besides the seasonal entry of foreign currency, which is the main factor of the lek's appreciation over this period, the key interest rate increase has also been reflected in the market. The high foreign currency supply over this period has been absorbed partly by the Bank of Albania's interventions, in respect of the target on the rise of net international reserve and in compliance with the country's overall macroeconomic program.

7. MONETARY POLICY INSTRUMENTS

Fixed-price one-week repurchase agreement is the main instrument employed during 2006. According to the liquidity situation, the Bank of Albania has switched from repurchase agreements to reverse agreements,

while the maturity term has changed from weekly to quarterly. This spectre of movements has been imposed by seasonal factors, by the budget behaviour and by the need to reveal certain monetary policy signals.

To meet longer-term needs of the market for liquidity during the four last months of 2006, four Treasury bill outright purchase transactions were carried out, at a total nominal value of ALL 3.2 billion.

During 2006 commercial banks employed the overnight deposit facility for investing their free liquidities with the Bank of Albania, on average at ALL 1.6 billion a day or ALL 0.82 billion more than in 2005.

Overnight credit has been employed only in seven cases, despite the lack of liquidity over the third quarter of the year. For the fourth consecutive year, the final lending facility of the Bank of Albania, i.e., the Lombard loan was not employed at all.

The required reserve instrument was used constantly even during 2006, for withdrawing the banking system liquidity. The monthly pace of ALL required reserve rise during 2006 was on average higher than in 2005, 0.92 percent versus 0.76 percent, reflecting the rise in the respective categories included in the required reserve account.

8. FOREIGN RESERVE MANAGEMENT

During 2006 the gross foreign reserve, estimated and reported in USD, has been increased by usd 368.06 million, recording the value of usd 1,793.12 million as at end of December.

Out of this growth, about usd 205 million is accumulated from Bank of Albania's interventions in foreign currency. They were intended at meeting the quantitative target for these assets and mitigating the volatility over the peak periods of foreign currency supply. While the exchange rate effect has been positive, at usd 106 million, the rest of the growth has been contributed by receipts from foreign disbursements.

9. BANKING SYSTEM PERFORMANCE

The banking system continued its stable development during 2006. The net banking system result for 2006 stood at a profit of ALL 7.45 billion, about 12.9 percent more than in 2005. Revenues from the principal activity (net income from interest) resulted to 31.2 percent more than in the previous year, reflecting the banking system orientation to activities of higher return and a rise in the overall volume of assets.

At end of 2006, the net income from interests was 92.6 percent of the gross banking system incomes, compared to 84 percent at end of 2005. This indicator has recorded constant growth, particularly over three last years, reflecting the overall net income sustainability for the banking system.

During 2006, the banking system assets grew by ALL 127.7 billion, or about ALL 57.6 billion more than the growth of assets noted in 2005. The main contribution to the growth of banking system assets was given by large banks, though their share in the market is downward. The estimates show that the lending activity concentration level is lower than that of assets and deposits concentration.

The significant growth of lending has been associated with increased share of non-performing loans portfolio, by about ALL 3.1 billion compared to end of 2005. The loans portfolio quality indicator, expressed as a ratio of non-performing loans to total loans portfolio in gross terms, is estimated at 3.1 percent as at year-end, against 2.3 percent as at year-end 2005.

The banking system capability of covering loss loans with capital has been downward, but still at good levels. The “non-performing loans to outstanding loans (net)” indicator, which estimates the net size of exposure to credit risk, continues to be at low levels, by 1.4 percent as at year-end 2006.

Compared to year-end 2005, the capital adequacy ratio of the system decreased by 0.5 percentage point down to 18.1 percent at end 2006. The capital adequacy ratio for 2006 continued to maintain the downward trend reflected in the preceding years. Large banks have recorded a rise of capital adequacy indicator, mainly due to increased regulatory capital at end of the year, by about 62.3 percent.

At end of 2006, the ratio of liquid assets to total assets of the banking system recorded 57.6 percent, compared to 62.6 percent it was at end of December 2005.

During 2006 the banking system underwent important qualitative and quantitative developments. At end of 2006 the Albanian banking sector consisted of 17 banks, of which three are of fully Albanian private equity. At the beginning of 2006 the Union Bank commenced its activity. On May 2006, there was approved the selling of the Italian-Albanian Bank's 80 % stake, which belonged to the Ministry of Finances of the Republic of Albania and to Capitalia S.A., Italy, to the new stockholder SanPaolo IMI S.p.A., Italy. At the same period, there was also approved the 60 percent (plus 2 shares) ownership transfer of the National Commercial Bank's stake from Kent Bank/Bayindir Bank, to the new Turkish institutional stockholder, Çalik-Seker Konsorsiyum Yatirim Anonim.

On August 2006 the ownership transfer of 11.25 percent of the ProCredit Bank's stake, from EBRD to ProCredit Holding AG (existing shareholder) was approved. On October 2006, the 71.97 percent transfer of the stake of Emporiki Bank S.A. of Greece to Credit Agricole S.A., France shareholder was approved. This transfer influenced also the indirect participation of Credit Agricole S.A. to the Emporiki Bank of Albania's equity, to the same extent.

During 2006, the banks' network was extended also by 62 new branches and agencies, in the whole territory of Albania and abroad, having the highest

share in Tirana, with the establishment of 30 new branches and agencies. Also, the opening of two branches outside the territory of Albania was approved and the opening of two other new branches is under the process of approval.

10. NEW ACTIVITIES OF THE BANK OF ALBANIA

- PAYMENT SYSTEM

From the regulatory and operational point of view, the payment system in Albania has already created the physiognomy of a modern system. The number of transactions processed during 2006 has increased by 13 percent, compared to 2005. In the meantime the value of transactions has increased by 21 percent during 2006, amounting to ALL 2,664.43 billion. Compared to 2005, the daily average number of payments (in both systems) has increased from 312, to 352 or 40 more transactions per day. In 2006, a new bank was added to the payment system, leading the number of participants to 17 banks.

On March 2006 the e-payment settlement by VISA cards started. Currently, this scheme counts 6 member banks. The number of cards in circulation has increased by 9 times during 2006, compared to 2004. The addition in cards number counts 127,552 cards compared to 2005, i.e., about 56 percent. Parallel to increased number of cards, the number of ATMs and POSs has also increased, respectively by 130 and 404.

- INTERNATIONAL INTEGRATION AND COOPERATION

The Bank of Albania's obligations stemming from the SAA relate to the meeting of the economic criteria of Copenhagen, guaranteeing the right of establishment and freedom of services for banks and other communautaire financial services, liberalizing capital movement and current payments between Albania and the EU, and approximating Albanian legislation to that of the *acquis communautaire* in these areas.

One of the most important developments during 2006 regarding the approximation of national legislation to that of the *acquis* was the drafting of the Law "On Banks in the Republic of Albania". This Law has adopted the largest part of the provisions of the 2000/12/EC Directive, with regards to initiation and continuation of credit institutions activity.

On 8 November, 2006, the European Commission published the Albania 2006 Progress Report. The European Commission evaluated in the report the policy followed by the Bank of Albania in terms of cooperating with international financial institutions and maintaining inflation under control, contributing to keeping a steady macroeconomic environment in the country.

At the same time, the Commission also evaluated the reliable monetary policy followed, highlighting particularly the measures taken by the Bank of Albania in terms of gradually changing its monetary policy strategy towards explicit inflation targeting regime, aiming at enhancing transparency and credibility of its monetary policies.

The report highlighted also the positive developments in the banking sector of the country and assessed the progress achieved regarding the establishment of the loans register, free movement of banking and financial services, freedom of establishment of foreign banks and further liberalization of capital movement.

On 27 January, 2006, the Executive Board of the IMF adopted the three-annual agreement with Albania, at SDR 17.045 million. The main targets of the new program have to do with the maintaining of macroeconomic stability, as a prerequisite for economic growth, and the improvement of financial institutions.

Under Reserves Advisory and Management Program (RAMP), during 2006 the World Bank's group provided consulting and technical assistance to the Bank of Albania for foreign reserve management.

During 2006 the Bank of Albania established constant contacts with the EBRD, mainly in terms of providing information and statistics for the development of the Albanian economy in general and financial sector in particular. The Transition Report 2006 assessed positively the maintaining of inflation within the Bank of Albania's target and the consolidation of the banking system over 2006.

The Bank for International Settlements (BIS) is another institution with which the Bank of Albania kept close contacts during 2006. The BIS has been particularly active in providing technical assistance to the Bank of Albania, through workshops and training courses organised by the Institute of Financial Stability, which promotes the international financial stability through information sharing and cooperation in financial system supervision area.

During 2006 the Bank of Albania enhanced the mutual relations with the central banks of the region and beyond it. Personally, I have paid official visits to many central banks of the region and Europe, discussing about latest developments in the Albanian economy and further extension of mutual cooperation and technical assistance that these banks can provide to the Bank of Albania. In June the Governor of the Bank of Greece, Mr. Nicholas C. Garganas paid a two-day official visit to Albania. It took place in the light of mutual relations between both institutions, laying special emphasis on sharing of information and experience in banking supervision area.

Enhancing relations with central banks of the region reached the peak in the round table of October 2006 held in Tirana, where the governors of the central banks of Rumania, Serbia, Montenegro, Bosnia and Herzegovina and Kosovo discussed about financial stability of the region.

In the framework of the Bank of Albania's objective to benefit from the experience of the central banks of the CEE, recently acceded in the European System of Central Banks (ESCB), during 2006 the cooperation relations with the Central Bank of Poland, National Bank of the Czech Republic and the National Bank of Bulgaria have been intensified.

- CURRENCY ISSUING

The increase of currency in circulation over 2006, by ALL 14, 7 billion is a response to the balanced macroeconomic development of the country. The commercial bank's receivables by the Bank of Albania during 2006 stood at ALL 105 billion, remaining almost at the same level with that of 2005. Concerning cash payments, from Bank of Albania's cash-boxes to commercial banks, the supply was carried out according to their requests, and intending, at the same time, to maintain the currency in circulation structure within the projected limits for year-end 2006.

The velocity of money circulation over 2006, for the shortened cycle of circulation, totalled almost at the same level as in 2005. However, the velocity of circulation underwent changes for certain denominations of banknotes and coins. Hence, a significant increase of velocity of circulation was proved in the 5.000 lekë, 1.000 lekë and 500 lekë denominations, respectively by 13.3 percent, 38.9 percent and 8.3 percent.

- CHANGES IN BANKING LEGISLATION

During 2006, further to the signing of the Stabilization and Association Agreement on 12 June, 2006, the banking legislation was amended and improved substantially once the Law "On the Banks in the Republic of Albania", No. 9662 of 18.12.2006 was passed by the Assembly of the Republic of Albania, which shall become effective on 1 June, 2007.

The Law "On the Banks in the Republic of Albania" enables the European Union member states banks and all foreign banks to provide banking services to Albania, through their branches or subsidiaries, without making any distinction in the licensing terms for their branches and subsidiaries and for Albanian banks. Furthermore, in line with the SAA provisions, the adopted law requires their treatment as Albanian banks in every aspect, once they are granted the licence to carry out banking business and financial activity.

The new law provides for clearer rules on management of risk the banks may be faced with while carrying out their activity, in order to guarantee and strengthen the protection of depositors and investors and to maintain banking system stability. Given the current conditions of rapid credit growth in the banking system, the new law treats fully the other types of risks as well, other than that of credit risk, with which banks may be faced, and the permitted exposures of the latter ones when faced with such risks.

The law requires for the first time, inter alia, the establishment and maintaining by the Bank of Albania of the loans register. Under the conditions of a rapid credit growth, the purpose of establishing such a register is to assist banks in making well-informed decisions when extending loans to their clients, as well as to strengthen the Bank of Albania's supervision on the Albanian banking system.

During 2006 the Bank of Albania started examining the prerequisites and implementation conditions over a mid-term period (year 2009), of a new monetary policy regime. In this context, analyses are carried out about the

possibilities of improving the legal infrastructure for the creation of such conditions in compliance with international standards in this area. Also, the possibility of improving the organic law of the Bank of Albania has been considered, coinciding with the prediction of its alteration as a mid-term priority of the National Plan for the Implementation of the SAA.

It is forecasted that these alterations will stipulate clearly the competences and procedures for the decision-making process of the Bank of Albania and the transparency of this process, which constitutes also a substantial precondition for the compilation and implementation of an effective monetary policy.

In the framework of the legal reforms undertaken by the Ministry of Justice for the amendment and improvement of the Civil Procedure Code, the Bank of Albania has been fully committed to cooperating with the banking sector for the completion and accuracy of mandatory execution procedure of executive titles.

The Bank of Albania proposals have aimed at improving the legal base on the application of procedures for the execution of acts that constitute executive titles. The main purpose is to cut the time for the execution of those acts, aiming to increase security in the lending activity, thus reducing the credit risk the banks are faced with.

At end of 2006, the Bank of Albania closely cooperated with the Ministry of Finance in compiling the draft-law "On Preventing Money Laundering and Terrorism Financing". In accordance with the respective European Union directives and other international recommendations, the Bank of Albania, being the supervisory authority of the banking system, regards with priority the legal framework improvement for preventing the use of banking system for laundering money and wealth that derive from criminal activities.

During this year, with the assistance of the World Bank, the drafting and completion of the regulatory framework for foreign reserve management was carried out successfully, reviewing the Bank of Albania's policy on the management of such reserve, the management criteria and terms, as well as the decentralization of decision-making competences during this process.

- INTERNAL AUDIT

In 2006, 44 audits and 3 verification procedures were carried out. The inspectors presented 269 findings and 197 recommendations out of these audits, which were carried out at the Bank of Albania and at its five district branches, the Printing House included.

11. BANK OF ALBANIA BALANCE SHEET

During 2006, the Bank of Albania assets further increased, totalling ALL 255.5 billion, about 14 percent higher than at end 2005.

The constituent groups, both foreign currency and domestic assets, have reflected growth, while the first group occupies about 68 per cent of total

assets, the same level as that of the previous year. On the liability side, foreign currency liabilities fell slightly (from 8 to 7 percent of the total) in comparison with the previous year, whereas domestic liabilities increased by 16 percent. Currency in circulation is the indicator that bears the main weight in this growth (about 45 percent of the growth), followed by the "due to the government" item (about 29 percent of the growth) and "due to banks" item (about 26 percent of the growth).

In general, the accounting balance sheet of the Bank of Albania and the income and expenditure statement reflect some basic developments that have occurred in the economy, where the Bank of Albania plays an important role.

The revenues realised during 2006 outstripped the level of the previous year only by about 5 percent. The main impact on this growth was given by income on foreign currency interests (about 20 percent more than in 2005). This reflects the performance of interest rates in foreign exchange markets. This effect absorbs the reduction of "income from ALL interests" item (about 7 percent less than in 2005), which reflects an average interest rate below that of 2005, irrespective of the upward trend at year-end.

On the other hand, interest expenses outstrip the previous year level by about 25 percent, reflecting the positive phenomena of the increased level of deposits and liquidity position in the banking system. Foreign currency interest expenses have been outstripped by 64 percent compared to the previous year, whereas ALL interest expenses have increased by 14 percent. Other (operational and amortization) expenditures are almost at the same level with that of the previous year.

Finally, the almost full compensation between increase of incomes and expenditures makes the net profit of the Bank of Albania for 2006 be in the same level with that of the previous year, at about ALL 5.16 billion (or 99.6 percent of the profit for 2005).

Honourable deputies,

Concluding my speech, I would like to underscore that during 2006 the Bank of Albania included in its agenda all the recommendations given by the Albanian Parliament in its resolution adopted on 25 May, 2006. I would also like to assure you that even in 2007, the same philosophy will characterise our work. Understanding correctly the role and mission of our institution, on behalf of the Supervisory Council of the Bank of Albania, I declare that the Bank of Albania will continue to be an accountable institution, deeply committed to fulfil its obligations vested by the Law and the Constitution.

We have many priorities for 2007, but let me highlight the most important ones:

- Maintaining consumer price stability remains the main legal target of the Bank of Albania. We are confident that the decisions taken in 2006

were appropriate and have served to orient inflationary expectations to the targeted range. Based on our forward-looking philosophy, we will prudentially evaluate all the risk factors, so that we operate on due time and intensity.

- Macroeconomic stability is of primary importance, but definitely the financial stability is also of as much crucial importance. Given the importance and the current level of economic and financial development of the country, this priority assumes extraordinary importance. Furthermore, the rapid credit growth is an argument for more prudence, particularly with regard to its quality. Being fully aware of our role as a decision-making and regulatory institution, we have decided to raise our vigilance in this regard, establishing the Financial Stability Department as a first step.
- Once more, the Bank of Albania emphasises its objective for further consolidation of the banking system. This process, which was present during 2006, should further continue in the current year. Our intention is that the banking system becomes a unity of sound institutions: that are supported by powerful shareholders, experienced in banking industry; that apply best standards of accountability in management; that carry out a balanced activity with well-managed risks; that are able to be faced with and develop under the open market competition provided by an open and integrated market into the international financial market; that support the economic development of the country and that transparently provide efficient and qualitative banking products and services to the public.

I would like to thank the Albanian Parliament once more for the good understanding and constant support it has given to the Bank of Albania.

Thank you for your attention.

SPEECH BY MR. ARDIAN FULLANI, GOVERNOR OF THE BANK OF ALBANIA

At the seminar "Catching-up in South East Europe: The Role of the Financial
Sector",
"Tirana International" Hotel, 3 May 2007

Dear participants!

Today's workshop on "Catching-up in South East Europe: The Role of the Financial Sector" is of special importance, because it is aimed at providing a panorama of the financial sector development trends in the countries of the region. Actually this seminar follows the VI Annual Conference of the Bank of Albania, held in October of the past year, which focussed on financial stability issues from the viewpoint of regional financial sector.

It's our pleasure to have today the presence of Mr. Max Watson, an Economic Adviser to the Director General on Economic and Financial issues at the European Commission. He will hold a presentation about economic developments and financial systems of our region. Taking advantage of the opportunity of Mr. Watson's presence in this workshop, I would like to inform you that the Bank of Albania has established a constant communication with the European Commission, concerning the country's economic and financial developments through its participation in some periodic meetings taking place annually between the Republic of Albania and the European Union.

The organisational, legal, operational approximation with the European System of Central Banks, stated also in the Bank of Albania's Mid-term Development Strategy, remains one of its main strategic targets. In view of this, the Bank of Albania has paid special attention to establishing specific structures and creating human resources capable of being faced with various approximation phases and eventual membership to the European System of Central Banks. Also, approximation of laws and by-laws with the Acquis legislation remains of special importance. The Law "On the Banking System in the Republic of Albania", passed by the Parliament in December, provides a good example in this regard.

Simultaneously, the Bank of Albania has actively contributed to the maintaining of the country's macroeconomic stability, by keeping low and steady inflation rates and by supervising the banking system prudentially. It is aware of its role as a promoter of the country's economic development, a process that will naturally facilitate our integration into the European Union.

Over the previous year our economy was characterised mainly by rapid credit growth. The loans portfolio reached lek 191.2 billion, or 21.3 percent of GDP at end of 2006. In absolute terms, credit to the economy grew by lek 69.3 billion, compared to the growth by lek 52 billion over the previous year. In 2006 the annual credit growth was 56.7 percent, providing good support

for economic needs. The relatively high pace of banking system lending to the economy also continued over the first quarter of the current year, drawing our attention, as the regulatory authority of the banking activity, to the need to monitor any risks this expansion may pose.

More concretely, this growth has led to decrease of capital adequacy rate and liquidity; however, banks have continued to be well-capitalised, liquid and profitable. Quarterly stress-tests carried out by us have indicated that the country's banking system is flexible against any probable shocks relating to exchange rate, interest rates or credit quality.

The Bank of Albania has continued to prudentially monitor the rapid credit growth, enhancing its banking supervision. In this framework, the establishment of the Credit Registry, expected to be carried out within December 2007 is of special importance. Currently, we are working for completing the legal framework that will enable the Registry establishment and functioning. At the same time, the decision has already been made on selecting the company that will provide technical solutions to the Registry.

We are confident that all these measures will contribute to the maintaining of credit quality and the financial stability of our country.

Wishing you a fruitful workshop, I give the floor to Mr. Watson.

Thank you!

SPEECH BY MR. ARDIAN FULLANI, GOVERNOR OF THE BANK OF ALBANIA

At press release with the IMF Mission and the Ministry of Finance
at the end of the IMF Mission in Tirana
Tirana, 8 May 2007

Concluding the intensive negotiations of two past weeks with the IMF Mission and the Ministry of Finance, which were finalised with an overall good understanding on the main issues discussed and further to the concluding statement of the IMF Mission and the messages given by the Ministry of Finance, allow me to express some opinions on behalf of the Bank of Albania.

The integral analysis of economic indicators suggests the recovery of economic growth rate close to its potential level. This behaviour has been dictated by the private sector development and has been favoured by the appropriate macroeconomic conditions and macro-finance stability. In this context, rapid credit growth is highlighted as the main source of supporting the economy with funds and as a driver of consumption and investment growth in the country. As an encouraging sign for the future, these developments have not transmitted excessive stresses to inflation or to other economic and financial stability indicators. In particular, we may highlight the positive role played by the monetary policy through raising, in due time and amount, the interest rates, through proper liquidity management and through monetary market development and expansion.

Naturally, these negotiations, being related and affecting directly the economic policies of a country, were oriented to the future. They were (and still are) primarily aimed at undertaking in due time the proper political responses, for further maintaining and strengthening the long-term perspectives of the country's development.

The vision of the Bank of Albania for the future is characterised by positive expectations, though the latest developments have increased the tones of prudence, highlighting the degree of our willingness to take necessary measures for guaranteeing the economic stability and growth in the long run.

The main development factors remain in place even for the future. Private sector's growth, particularly in services sector, and the macroeconomic stability will be fulfilled by further structural and infrastructural reforms, and should be associated by constant efforts for improving the business climate. In the medium run, these incentives should raise the Albanian economy profile, reducing the degree of dependence on imports, absorbing fixed long-term capitals and orienting them to prior sectors of the economy. It is the pleasure of the Bank of Albania to see that the rhetoric frequently used with relation to this program, as a maturity program for the economy and for the Albanian institutions, has been followed by concrete actions in most of

involved institutions. The Bank of Albania has taken a number of steps to strengthen the analysing and decision-making capacities in monetary policy, adopting a modern physiognomy in this area, as an institutional guarantee for maintaining inflation within its targeted rate. Together with the incentives taken for the development of the financial market and for the strengthening of its supervisory function, these steps are made concrete in tactile measures for the financial market and the economy.

Extending our tones of prudence mentioned earlier, allow me to refer to some of the main risks identified and to deal briefly with the measures projected by the Bank of Albania.

Concerning the above economic view, we have largely expressed, in the periodic contacts of the Bank of Albania with the public, our concerns about the potential risks that may break the monetary and price stability. Sparing the details, I would mention: the grave financial situation of Electric Energy Corporation of Albania, with its implications for the budget indicators and for the production costs; high level of the domestic demand, which impacts directly on price rise and on trade deficit enlargement; high credit growth paces; constant tightening of monetary policy of the Euro area and its impact on Albanian financial markets; These are essential reasons for re-considering the appropriateness of current monetary conditions in the country, aiming at maintaining inflation within the Bank of Albania targeted band.

Also, the Bank of Albania is paying special attention to the impacts of the above factors, particularly of rapid credit growth, to financial stability of the system. In this context, it is considering the possibility of applying a packet of regulatory measures, based also on the experience of the countries of the region.

Finally, I would like to emphasise that special priority is given to the need for further consolidation of the banking system. During 2006, striking achievements have been made in this regard; however, the qualitative inflows of the previous year should be followed by further processes of mergers and acquisitions, so that the number and quality of participants in the system approaches to contemporary parameters.

SPEECH BY MR. ARDIAN FULLANI, GOVERNOR OF THE BANK OF ALBANIA

At the award ceremony by the President of the Italian Republic, His Excellency
Giorgio Napolitano with the Order of the Star of Italian Solidarity
Tirana, 7 June 2007

*Your Excellency Mr. Ambassador Iannucci,
Honourable Mr. Ministers,
Honourable Mr. Deputies,
Your Excellencies Ambassadors,
Dear colleagues, friends and guests,*

I am overwhelmingly honoured for this appraisal.

It is natural for any human being to be appraised for the work done. Such moments have been present throughout my career. Nonetheless, I had never thought that another nation would have honoured me with its trust.

There have been very few moments in my life to have felt such a delight and motivation.

However, I will endeavour to speak in plain words in order to express my deepest gratitude and honour to the President of the Republic of Italy, His Excellency, Mr. Napolitano.

Being one of the selected, who for the last 6 decades have been honoured with the Star of Italian Solidarity (Ordine della Stella della Solidarietà Italiana) by the outstanding presidents of Italy, the cradle of European civilization, makes me feel proud and overwhelmingly obliged in my commitment. In spite of the natural emotions of such a great moment, I wish to express my heartfelt thanks to the Minister of Foreign Affairs, Mr. D'Alema, and to the bright diplomat and the great friend of all Albanian people, Mr. Iannucci.

In this exceptional day, I would also like to thank everyone who with their co-operation, support and presence throughout my career, have added my belief in success. Certainly, I wish to thank my family for the pouring of love and patience and for being present in both, good times and hard times.

I believe this is a remarkable moment for all my friends, colleagues, and relatives, present or not today in this hall. I am delighted to share with you this great event in my life.

Mr. Ambassador Iannucci,

It is with gratitude that I accept this decoration and I would like to assure you that my work and efforts towards enhancing the co-operation and solidarity with the friend country, Italy, will grow further.

It would not be excessive to say that enhancing friendship and human understanding among nations is in itself, a noble mission. An ancient expression says "Friendship does for people what the sun does for flowers. Pour it on and watch them blossom".

In ancient philosophy, accepting the honour from an eminent nation, ennobles you.

It is with immense gratitude and deep respect that I accept this decoration from the President of the Republic of Italy and the Italian people.

Amicitiae nostrae memoriam spero sempiternam fore - I hope that the memory of our friendship will be everlasting. (Cicero)

INTERVIEW BY MR. ARDIAN FULLANI, GOVERNOR OF THE BANK OF ALBANIA

To "Klan" magazine
Tirana, 23 June 2007

SOUNDNESS PASSES THROUGH .. BANK

- Mr. Fullani, initially we would like to have your comment on the efforts of the Government to channel financial business transactions through banks. Is this effort somewhat strained, given that the other party (the business) expresses itself that high transaction commissions of commercial banks increase business costs and the banks themselves are not ready to carry out the transactions?

The channelling of financial transactions through the banking system, as a process already tested and under development, is a much expected action, which outside the propaganda contours will really contribute to weakening of the infrastructure that nourishes the informality. In recent years, the banking system has passed through an irresistible process of development and consolidation. Actually it may be stated without hesitation that the banking system in Albania is completely capable of encountering with dignity this requirement of the time.

Dealing briefly with two or three important moments, I would start with the operation of two modern payment systems: Albanian Interbank Payment System (AIPS) where gross and real time settlements are made, and the Automated Electronic Clearing House (AECH) (small-value payments of clearing systems). Further on, I would highlight the significant growth of e-payments, the entry into the system of two well-known international banks, the increased number of branches, as well as increase of ATMs and POS terminals for card payments in the whole territory. Encountering successfully the channelling of public sector salaries through bank accounts, followed also by those of the private sector and by a number of other banking services, I think are indicators of the proactive, ever increasing role of the banking system.

To clearly understand what progress we have made so far in this direction, it's worth mentioning some statistics. The number of payments processed in AIPS system has increased by 11 percent, while the value has increased by 21 percent compared to 2005. In the meantime, both systems, the AIPS and the AECH have a much higher capacity than the current number of payments processed in them. At end of 2006, compared to end of 2004, the number of POS terminals was 7 times higher, while the number of electronic cards in use has increased more than 10 times and the transactions carried out through them was above 12 millions, with a value of about ALL 188 billion. During 2006, 62 branches and agencies of commercial banks were established, leading the number to 294 at year-end.

In this sense, I think that the current infrastructure of the national system of payments we provide is completely capable of facing the Albanian market demand for speed, number, quality, size and security of payments carried out through these systems. Furthermore, the Bank of Albania, in its role as the regulator of this system, is working for further standardization of payment instruments, which will lead to increased quality of services offered by banks to their clients.

On the other hand, the increased inflow of transactions in the banking system will further encourage competition within the banking system. Banks would be encouraged, in exchange of low commissions, to attract as many clients as possible, who in turn, would bring about more financial resources to banks. The banking activity, as any other business, aims at profit maximisation. Therefore, it is natural to charge commissions for services offered by the system, while their amount is an individual policy that changes from one bank into the other, in accordance with the size and other specifications. I am convinced that the increased volume of work will bring about reduced banking commissions. I do not have any doubt in this regard. What I would assure you, as the governor of the Bank of Albania, is the meeting of an early requirement of the banking system to be very transparent about its products, services, commissions and prices they generally apply.

- *As the process of channelling the financial transactions of business through banks had to be carried out since time ago, is it better to pass the costs of the moment and to channel the economy through the banking system?*

I would refer to "costs of the moment" as "benefits of the future". Imagine the other side of the medal. How much informed will the banking system be in relation to the potential the various businesses have, and how much safe will it feel in crediting them without any hesitation? From this viewpoint, it is concluded that the operation is necessary and furthermore, in the final analysis, businesses, and particularly individuals will be the beneficiaries. In a broader aspect, the information on economic-financial potential of the country would increase; the banking system effectiveness would increase; the variety of banking products and services would increase; the geographic coverage by banking services would increase; and in consequence the mobilization and re-allocation of funds would be more appropriate; the competition would increase and costs would decrease. All these achievements would contribute to creating a more complete economic infrastructure of the country, which would raise the formality of the economy and would accelerate the economic growth rates of the country.

- *Credit extension has increased fourfold during four last years, but this has not influenced on interest cut: Is this normal?*

It is true that during last years we have had a rapid credit growth. During 2005 credit increased by ALL 57.6 billion or about 82 percent in annual terms, whereas during 2006, it increased by 70.2 billion or about 55%. Upward trends are as strong even in the first half of 2007. According to latest estimates, credit

balance at end of 2007 will be around 21 percent of GDP. Without doubt, this view reveals that Albania, likewise most similar countries, has entered into the group of countries with high growth paces of credit to the economy. The first cause listed by experts is the so-called "catching - up process", which in other words means high growth caused by a rather low starting base.

Naturally, there are also other factors, such as: macroeconomic stability, the maintaining of inflation under control, low interest rates in Albania, Europe and the USA, exchange rate stability, increased banks' ambitions to lend and the public confidence in receiving credit. The banking system development in the recent years, its successful privatisation and the process of consolidation characterising it in 2006 are other factors that have influenced on rapid credit growth. Also we may mention the introduction of new credit products, such as consumer loans, house loans, and the efforts to make them more popular through aggressive marketing forms.

Rise of credit to the economy at so high levels carries over the potential of cutting the interest rates through which it is offered. Referring to Bank of Albania statistics, if an ALL loan of 6 - 12 month maturity at the beginning of 2002 was given on average by above 18 percent rate, in April 2007 it was given by only 10.16 percent. However, we should be prudent and always bear in mind the fact that about 75 percent of credit is in foreign currency and therefore, in forming the price of this kind of credit, banks refer to international financial market rates, such as euribor for the euro and libor for the American dollar. What is evidenced recently, thanks to increasing competition, is that ALL credit rates as an average expression of new credits have remained almost constant during the latest years, though euribor has increased almost throughout the whole period.

- *Is the default risk the one that keeps high interest rates or do we have a situation of profit by banks from an economy in transition, as randomly happens?*

It is not the high default risk the one that obliges banks to apply high rates. In price formation policies, banks, inter alia, factorise also the country risk, which for many objective reasons is higher than that of the developed countries. Also, besides this risk, there exists also the economy informality, problems about ownership, mortgage of properties and collateral execution. All these factors make banks work hard to ensure information about the borrowers. This leads to increased costs and to the risk of misleading financial analysis of the borrower, which would influence negatively on credit portfolio quality in the future.

- *Time ago you have issued the warning of "bad loans" risk; what is the current situation like in this regard?*

A governor should always be concerned about such an important problem, related to loans portfolio quality. The current situation of credit quality remains satisfactory. The ratio of "non-performing loans to (gross) outstanding loans,

which measures the net size of exposure to credit risk is estimated to 1.5 percent.

Constantly the Bank of Albania's attention has been to strengthening of banking supervision measures. Some amendments have been made to the Regulation on credit management, consisting in improvement of the lending process of banks, improvement of risk management and some measures have been taken for enhancing transparency with the public. Also, this regulation has provided some requirements on additional capital of banks, in case they have a high lending pace.

However, we have to do with a process, which never ends and which will always be at the top-list of Bank of Albania priorities. We will continue to monitor prudentially credit growth and its quality. We will further improve prudential regulations, making them in consistency with best standards used by European central banks. Only in this way a good credit quality will be ensured, for preventing any probable negative consequences on the financial stability of the country.

- *Until a year or so ago, treasury bills could be purchased only at central bank's windows, while the selling of treasury bills may be also carried out at some commercial banks. Has the liberalization process influenced on yield cut?*

The possibility of participation of individuals in primary treasury bill market through the banking system dates back to 1996, while the Bank of Albania was included in this process only during the second half of 2001. The Bank of Albania, in its role as a central bank, having the main target to achieve and maintain price stability, since the moment of opening its windows has regarded this presence as temporary. In essence, the establishment of these windows was another possibility for the people to have greater access in purchasing treasury bills. The participation of individuals in the primary market is of non-competitive nature, meaning that they do not influence on price formation. They just accept the resulting auction price. Therefore, we may state that their impact on yield rate fluctuations is almost insignificant. Since my taking office, I have insisted that the selling of treasury bills is an operation that naturally belongs to commercial banks. To this end, we have discussed more than once with the banking system and with the Ministry of Finance for designing a strategy for the Bank of Albania's gradual leaving from this "business" not natural to it, believing that the market forces and its principles are the ones that should manage this process. Therefore the banking system was required to be aggressive in this regard, providing to the clients the service of selling T-bills in primary and secondary markets.

Parallel to that, the Bank of Albania, concerning this service at its windows, made two important steps, charging a service commission that covers connected costs and deciding not to accept cash inflows of individuals who intend to invest in T-bills. Since then, participation in treasury bill auctions through Bank of Albania windows may be made possible only in case the intended amount for investment comes in the form of banking transfers.

- *Can you mention the positive sides of this liberalization?*

These measures may rightly create the idea of a liberalization process, which I think will really lead to further deepening and expansion of the financial market in Albania. Presently, we are working for presenting a new practice in the primary market of government securities, that of the main mediators, or as already known in other terms, "primary dealers". We believe that this relatively long period in transition has served as a school also for the public at large. What is more important in the whole process is the fact that individuals are getting more and more acquainted with market instruments. The better and with more conscience we know them, the easier is the path to real financial market development. In such an economy, individuals make the choice.

- *Recently you have received evaluations, since the institution you govern has succeeded in maintaining macroeconomic parameters and price level. Can you mention some of the measures you have taken during this period?*

It is true that the Bank of Albania 's role in maintaining macroeconomic stability , particularly in controlling inflationary pressures, has been recently highlighted by a number of institutions within the country and abroad. However, I would highlight the public evaluation for the institution I govern as the greatest success we have achieved. This evaluation is expressed clearly in anchoring inflationary pressures in the country and in increasing the degree of using their products. Naturally I regard it a direct reflection of high technical and professional investment the Bank of Albania has made in setting up an equilibrated framework of macroeconomic policies, in increasing financial markets, in developing the monetary market infrastructure and in consolidating the banking institutions. On the political plane, the Bank of Albania has kept unchanged its focus on monetary policy, to guarantee price stability in the economy. It has monitored prudentially the liquidity conditions and interest rates in the economy, as well as other factors of potential negative impact on inflation, raising twice the key interest rate in the economy. Also, the Bank of Albania has been a productive partner in coordinating the economic policies of the country and in the performance of the agreement with the IMF.

On the financial market development plane, the Bank of Albania has undertaken a number of incentives for completing the banking infrastructure and the legal framework. Reflecting largely on macroeconomic stability and on improvement of banking infrastructure, lending to the economy has undergone very rapid paces during three latest years. On the other hand, the strengthening of banking supervision measures and the prudential regulations serve as a guarantee that the banking system expansion and rapid credit growth to the economy will not create problems for the financial health of banks and for their long-term sustainability. The Bank of Albania is raising the degree of professionalism, which is a guarantee for strengthening the independence, transparency and accountability. Therefore, the decision-making process has been further perfected, thus increasing the credibility of the Bank of Albania to the public.

SPEECH BY MR. ARDIAN FULLANI, GOVERNOR OF THE BANK OF ALBANIA

At the press conference on the decision of the Supervisory Council of the Bank
of Albania on raising the key interest rate by 0.25 per cent
Tirana, 27 June 2007

Good morning!

In this communication with media, with you, with the financial market, with businesses, consumers and all other economic agents, I would like to inform you about today's decision of the Supervisory Council of the Bank of Albania on raising the key interest rate by 0.25 per cent.

In today's meeting, large discussions took place on the latest developments in consumer prices and on economic and monetary indicators. This meeting was a further elaboration of previous analyses of the Bank of Albania, confirming our conclusions about the performance of economic activity and inflationary pressures.

In a summarised way, there was drawn the conclusion that the overall macroeconomic objectives are within the limits envisaged in the country's economic development program. The Bank of Albania has assessed that the economic activity is stable. The overall environment over the first half of the year has turned out non-inflationary, with an annual rate fluctuating on average around 2-2.5 percent. Monetary developments have reflected an increasing activity as concerns the credit to the economy, while the fiscal activity has not performed according to the plan. As in the previous year, during the first 6 months of 2007 surplus is characterising the fiscal budget, reflecting mainly the low degree of capital expenditure realization. On the other hand, trade deficit has recorded an obvious enlargement during the first quarter of the year, generating premises for creating imbalances in the external sector of the economy.

Financial market has been characterised by a higher activity in all its segments. After the stabilization of banking system liquidity at the beginning of the second quarter of the year, the market interest rates have evidenced an upward trend, materializing, to a satisfactory extent, the earliest decisions of Bank of Albania monetary policy.

The exchange rate, which was characterised by a depreciating trend in the first half of the year, has recorded a more stabilised performance in the second quarter, responding to seasonal factors, international market developments and performance of monetary conditions in the country. In the meantime, through the increasing integration of Albanian financial markets, the policies followed by the European Central Bank and the Federal Reserve have been also reflected in the domestic foreign exchange market. These developments convey larger implications for other indicators of the financial system, for the economic activity and for monetary policy.

Expected developments in the economy, forecasts of the Bank of Albania's staff on inflationary developments in 12 coming months and potential risks, whose materialisation would have a reverse impact on inflation deviation from the 3 percent target of the Bank of Albania, were primary issues of discussions.

The Supervisory Council analysed prudentially the following risks:

- Growth of domestic demand, due to high lending pace and monetary conditions that have a stimulating character. The expected growth of budget expenditures and domestic borrowing in the second half of the year is an additional factor in this regard. The growth of the economy demand for goods and services is manifested in stronger inflationary pressures and in imbalances in the external sector of the economy, through expansion of trade deficit and pressures on the exchange rate. Both these forms of disequilibrium are damaging to the perspective of a stable economic growth in the long run.
- Rapid money supply growth, which is a premise for the emergence and constancy of inflationary pressures.
- Monetary policy tightening at global level and its implications for the monetary conditions in Albania.
- Expected growth of administered prices and high raw material prices at world level.
- The need for maintaining inflationary pressures anchored to the Bank of Albania target, as a precondition for a successful and effective monetary policy.

After dealing analytically with each risk element, the Supervisory Council of the Bank of Albania drew the conclusion that the materialisation of some factors has been consumed, while a real possibility of occurrence exists for some others. Against this background, the Supervisory Council of the Bank of Albania decided to raise the key interest rate by 0.25 percentage point, leading it to 5.75 percent. The Supervisory Council of the Bank of Albania deems that the latest decision is a movement in fulfilling the legal mandate of the Bank of Albania, which is the maintaining of price stability. This decision carries over a modern decision-making physiognomy: that of minimising the materialisation of risks in the future.

The interest rate rise is aimed at re-dimensioning the monetary conditions in the economy, bringing them in line with the target of maintaining price stability in the coming months. It will contribute to controlling domestic demand of the economy, revaluating monetary incentives for consumption and savings. It will also help contain the high growth of monetary assets in the economy. This signal expresses the Bank of Albania's willingness to keep inflationary pressures under control. Finally, the Bank of Albania highlights that, in its opinion, the monetary conditions still remain on the accommodating side of the economic growth.

Thank you for your attention.

NEW LAW "ON BANKS IN THE REPUBLIC OF ALBANIA" AND ITS COMPLIANCE WITH THE SUPERVISORY REGULATORY FRAMEWORK. OBLIGATIONS FOR REGULATORY CHANGES IN THE IMPLEMENTATION OF THE DIRECTIVES OF THE EUROPEAN UNION. JUNE 2007*

ABSTRACT

This paper deals with the compliance of the Law No. 9662, dated 18.12.2006 "On Banks in the Republic of Albania" with the existing supervisory regulatory framework, and the obligations for regulatory changes arising from the implementation of provisions of the Directive 2000/12/EU consolidated with the Directive 2006/48/EU.

The paper makes a comparison between the new Law No. 9662, dated 18.12.2006 "On Banks in the Republic of Albania" and the Law No. 8365, dated 02.07.1998 "On Banks in the Republic of Albania", which has served as a basis in drafting the existing supervisory regulatory framework. In this aspect, detailed analyses are made about all articles of the above laws and also they are compared to respective regulations that reflect these provisions. From such analysis, we draw the conclusion that some of the existing regulations need to be revised, so as to reflect the novelties arising from the implementation of the new legal framework. Another element of this analysis is the reflection of provisions of the Directive 2000/12/EU consolidated with the Directive 2006/48/EU, including the obligations deriving from the Stabilization and Association Agreement in the field of financial activities.

I. Compliance of the Law No. 9662 dated 18.12.2006 "On Banks in the Republic of Albania" with the supervisory regulatory framework. Needs for making regulatory changes, in implementation of the Directives of the European Union

The Law "On Banks in the Republic of Albania" No. 9662, dated 18.12.2006 is an improved version of the Law No. 8365, dated 02.07.1998 "On Banks in the Republic of Albania" and deals differently with a number of elements. The Law is designed taking into consideration the EU directives, the Basel Committee core principles on Banking Supervision. It is also drafted in compliance with the obligations deriving from the Stabilization and Association Agreement. As a consequence, the need for improvement and adjustment of the existing supervisory regulatory framework with the requirements of this law arises.

Given the above, the compliance of the Law "On Banks in the Republic of Albania" No. 9662, dated 18.12.2006¹ with the supervisory regulatory framework will be analysed according to respective chapters of the Law.

I.1 Chapter I: "General provisions"

This chapter is composed of general provisions, defining: the purpose of the Law, its scope, the structure and extension of the banking system in the Republic of Albania, definition of terms used in the Law, the rights and revocations in exercising banking activity, obligations for providing information on banking and financial system situation, the legal form of the bank and measures against using the banking system for purposes of money laundering or terrorism financing.

In Article 1 (which describes the purpose of the Law) and Article 2, point 2 of the Law (which describes the persons, entities of the Law), the term "bank" means either a bank with head-office in the Republic of Albania or a branch of the foreign bank, licensed by the Bank of Albania, without making any distinction as concerns the establishment, licensing or activity they carry out in the territory of the Republic of Albania (Article 5 of the Law). Such a treatment is in full compliance with freedom of establishment or freedom of provision of banking and financial services (Article 11 of the Law), cited also in the Directive 2000/12/EU, Article 23/5 and in Directive 2006/48/EU, Articles 38/1 and 38/3. More concretely, the Directive defines that: member states should not apply to branches of credit institutions, with head-office outside the territory of the EU, at the moment of starting or while carrying on its activity², provisions that result in a more favouring treatment than the treatment against branches of credit institutions with head-office inside the territory of the EU..

Despite the same treatment to banks and branches of foreign banks regarding the establishment and exercising of their activity in the Republic of Albania, an important element is the need for carrying out a differentiated supervision between banks and branches of foreign banks, in compliance with Article 27 of the Directives 2000/12/EU and 2000/12/EU consolidated with Article 41/1 of the Directive 2006/48/EU. This Article states that: Host member states shall retain responsibility in cooperation with the competent authorities of the home Member State for the supervision of the liquidity of the branches of credit institutions:

Whereas Article 28 of Directive 2000/12/EU and Article 42 of the Directive 2006/48/EU state that: this cooperation between supervisory authorities of the home and host country on supervision and monitoring of the activity of credit institutions should include, besides liquidity, also the management, ownership structure, solvency, large exposure limits and internal audit mechanisms..

Article 4 of the Law (on definition of terms used in the respective Law) provides improvements in the definition of some terms of the old law, and definition of some new terms. Briefly, this article provides the definition of the following terms: "bank", "banking activity", "licence", "monetary deposits", "persons or group of connected persons", "control", "branch of a foreign bank", "executive director", "nonbanking financial entity" as well as terms related to bank's equity; risk, "voluntary liquidity". Consolidated supervision is also defined.

From the viewpoint of consolidated supervision, new terms are also defined, such as: "initial minimum capital", "initial paid-in capital", "banking group", "financial holding company", "superordinate bank in a banking or financial group". Among other new terms, we may mention also the definitions given for "credit registry" and "deposit insurance agency". In this respect, the need for updating the existing supervisory regulatory framework arises, with the purpose to approximate the national legislation to that of the EU in the field of banking and financial services. (*Directive 2000/12/EU, Article 1 consolidated with Directive 2006/48/EU, Article 4, provides detailed definition of terms used in the abovementioned directives*).

1.II Chapter II "Licensing banks and branches of foreign banks"

This chapter of the law presents the characteristics, phases and requirements related to necessary documentation for receiving a licence to carry out banking and financial activity in the Republic of Albania; initial approval of the licence, refusal to grant the licence, commissions applied for receiving a licence; cases of licence revocation; publication of decisions for licence approval or revocation, initial minimum capital requirements, additional activities that may be carried out by banks or branches of foreign banks, as well as changes in the capital structure.

The Law vests the Bank of Albania with the executive right to license banks and branches of foreign banks, for carrying out financial and banking activity in the Republic of Albania (Article 14 of the Law), in full compliance with the *Directive 2000/12/EU, Article 4 consolidated with Directive 2006/48/EU, Article 6 and 28/1*. According to the Directive, it is stated that: The right to commence banking and financial activity is acquired only after a bank or a branch of a foreign bank has acquired a license.

Article 15, point 1 of the law specifies licence characteristics, as an administrative act issued by the Bank of Albania. The licence is perpetual, non-transferable, and what is new compared to the old law, it is not tradable.

Article 15, point 2 of the Law, unlike the old Law, extends the area of activities permitted for banks and branches of foreign banks with financial activities, defined together with banking ones, in the annex that is an integral part of the licence. This part of the Law complies with the *Directive 2000/12/EU, Article 21/1 consolidated with the Directive 2006/48/EU, Article 28/1* which states that: *credit institutions should notify in advance competent authorities of the activities on the list in the Annex of the banking licence acquired*.

Article 17 of the Law brings about a re-designing of the old law, as concerns the requirements related to documentation for receiving a licence to carry out financial and banking activity in the Republic of Albania, making a distinction between banks and branches of foreign banks. These requirements were previously specified only in the regulations of the Bank of Albania, but are presently defined in the new Law, thus highlighting their importance.

Also, more requirements are provided in relation to legal documentation for acquiring a licence, directly reflected in the Law, as for example concerning direct or indirect participation in bank's equity to not less than 5 percent; capital structure; information about any agreement or any other regulatory form by virtue of which control or influence on the decision-making process may be exercised in any other way; accounts and annual report of the legal person, consolidated accounts and annual report, and certified auditor's opinion (Article 17/1) as well as in relation to foreign bank's ownership structure; the name of the supervisory authority and its consent to the opening of the branch of the foreign bank, as well as information on Deposit Insurance Agency (Article 17/2).

Another new element is also the prevention of limitation of appointing by parent bank at least two resident administrators for managing the branch of the foreign bank. These changes should be presented in the Regulation "On granting a licence to carry out banking activity in the Republic of Albania"³.

Regarding the compliance with *point 1* of this Article with the EU Directive, we may underline that some of provisions of the latter are reflected quite well. More concretely, information on: the subscribed share capital and documentation evidencing the lawful source of contributions in the capital; capital structure; qualification; reputation and experience of at least two administrators; the business plan for the first three years of the activity; name, and address of every person that proposes to own qualified holding, all comply with the requirements of the provisions of the Directive 2000/12/EU and the Directive 2006/48/EU⁴.

We may draw the same conclusion also about the compliance of points 2, 3 and 5 of Article 17. So, information on statute of the foreign bank, accurate address of the legal seat, description of activity, amount of capital, management structure of the bank and its administrators; endowed sum of the initial minimum capital; permission for exercising banking activity granted by the competent authorities of the country where the legal seat is located; as well as list of activities for which the foreign bank is licensed; ownership structure of the foreign bank; conditions to be met by a branch of a foreign bank that proposes to own a qualifying holding in a bank; the BoA's right to request additional information, all reflect rigorously the information required under the Articles of the provisions of the Directive 2000/12/EU and Directive 2006/48/EU⁵.

Article 18, point 1 of the Law (on capital requirements), complies with the requirements of Article 5/1 of the Directive 2000/12/EU and Article 9/1 of the Directive 2006/48/EU, for depositing the initial minimum capital to acquire a licence to carry out banking and financial business. The provisions of the EU directives stipulate that the initial minimum capital shall be no less than EUR 5 million, whereas the BoA regulatory acts stipulate that this capital shall be no less than ALL 1 billion (approximately EUR 8 million). This higher level is due to the fact that the regulatory acts of the Bank of Albania take into account country risk whilst setting forth this amount.

Article 19, point 1 of the Law stipulates that the Bank of Albania shall have the right to grant or not to grant an initial approval for a licence (within three months of the receipt of application for a licence submitted by a bank or a branch of a foreign bank). This right given to the supervisory authority is also reflected in Articles 10 and 13, respectively of the Directives 2000/12/EU and 2006/48/EU, but with a distinction, that the above directives specify that: the maximum term of granting or not granting an authorisation is within 6 months of receipt of application.

Further to the old Law (that specifies the condition of existence of at least three shareholders for the acquiring of a licence by a bank or branch of a foreign bank), point 2/d of Article 19 specifies that the Bank of Albania shall give its initial approval for a licence only after it has been satisfied that no shareholder owns more than 1/3 of the capital or shares with voting rights of the bank. This re-designing should be reflected also in the Regulation "On granting a licence to carry out banking activity in the Republic of Albania".

Article 19, point 2/d (operational and control structures, including procedures and policies of banks or branches of a foreign bank) and point 3 (cases when the Bank of Albania shall refuse initial approval of a license for a bank or a branch of a foreign bank), are new elements compared to old Law requirements. In this way, the need to include them in the Regulation "On granting a licence to carry out banking activity in the Republic of Albania" (Article 6) arises.

Article 20, of the Law provides that one of necessary conditions for acquiring a licence by banks or branches of foreign banks is the submission of application and complete documentation to Deposit Insurance Agency, for receiving the deposit insurance certificate. Also, Article 22 of the Law stipulates that a bank or a foreign bank may not carry out banking activity without acquiring the deposit insurance certificate. Given the above, the need to include the conditions in the Regulation "On granting a licence to carry out banking activity in the Republic of Albania" (Article 7) arises.

Articles 21 and 29 on the announcement and publication of the decision for granting a license or for revoking it, are based respectively on Articles 11 and 14/2 of the Directive 2000/12/EU and Articles 14 and 17/2 of the Directive 2006/48/EU, which stipulate that: The name of each credit institution to which authorisation has been granted shall be entered in a list. The Commission shall publish that list in the Official Journal of the European Union. Also, in case of revoking a licence, the competent authorities shall provide the reasons of such revocation and shall publish this decision.

Article 24 presents cases when a bank or a branch of a foreign bank should apply for prior approval of the BoA on issues related to its activity. Unlike the old Law, additional cases are provided for prior approval, being presently specified in the Law (not only in the BoA regulations), for example: open a branch, subsidiary or representative office inside and/or outside the territory of the Republic of Albania or transfer ownership of a qualifying holding or the

control of the bank to third parties. Furthermore, additional requirements are provided, such as: change of the statute, distribution of its capital and increase of the percentage of a shareholder with qualifying holding exceeding 20, 33 or 50% of the bank's capital or its voting rights or to such degree that the bank becomes its subsidiary. The last requirement is in full compliance with Article 16/1 of the Directive 2000/12/EU and Article 19/1 of the Directive 2006/48/EU.

These directives prescribe also two specific cases which may be considered as important also for the Albanian reality. The natural or legal persons (Article 16, Directive 2000/12/EU and Article 20, Directive 2006/48/EU) are required first to inform the competent authorities if he proposes to reduce his qualifying holding in a credit institution, owned directly or indirectly, so that the proportion of the voting rights or of the capital held by him would fall below 20, 33 or 50 percent. Secondly, the requirement for information in favour of competent authorities arises not only for natural and legal persons who propose to acquire qualifying holding in credit institutions, but also for credit institutions proposed to be acquired (Article 21, Directive 2006/48/EU).

Points 1/c and 1/e of the Article 24 provide additional information. Letter c has been enriched with the fact that the Bank of Albania determines through its by-laws the criteria for entering into agreements⁶ with third parties, for exercising the functions and duties for the administration and management of the bank. *Letter f* specifies that prior approval of the Bank of Albania is required in cases of repurchasing bank shares or those of its connected persons, directly or through another person, by granting credit or issuing guarantees.

Article 24 point 3, which stipulates that the Bank of Albania grants or refuses to grant the prior approval within 3 months from the adequate submission of the request, in accordance with the documentation as defined though by-laws, is in compliance with Article 16 of the Directive 2000/12/EU and Article 19/1 of the Directive 2006/48/EU.

Article 25 specifies the cases when a person, who requests to change his qualifying holding in a bank, should address himself to the BoA to receive the prior approval. Point 6 of Article 25 stating: If a person holds a qualifying holding in the bank without the prior approval of the Bank of Albania, the action resulting in such occurrence shall be deemed null and void, complies with the requirements of Article 16/5 of the Directive 2000/12/EU and Article 21/2 of the Directive 2006/48/EU.

An important element is the distinction with the old Law, specifying that in case a person possesses a qualified holding in a bank, without prior written approval by the Bank of Albania, the licence was revoked (Article 13); the new law specifies that no right to vote is known to such shareholder.

Article 26 is a summary of cases found in various provisions of the old Law, adding some additional cases when banks and foreign bank branches should

notify the Bank of Albania about the existence of facts or verification of risky situations for the continuity and stability of their activity. We may mention here cases when: maximum permitted exposure limits are reached, when the liquidity or solvency of a bank or branch of a foreign bank is threatened, the financial position of the bank has changed to the extent that the bank does not possess any longer the regulatory capital or does no longer reach the minimum capital adequacy, the regulatory capital of the bank falls beneath the minimum initial capital required for the commencement of banking activities, etc..

Point 2 of this Article, on the requirement of the bank or the branch of the foreign bank to notify the Bank of Albania of cases when there are changes in the organizational structure, changes of the legal seat and its address, dismissal of administrators, reflects the requirements of Article 20/6 of the Directive 2000/12/EU and Article 26/3 of the Directive 2006/48/EU.

The only change between the provisions of this Article and the aforementioned directives stands in the term specified for the notification. The bank or the branch of the foreign bank notifies the Bank of Albania within 30 days from the moment of verification of any of the above cases, whereas in the EU Directive the obligation arises at least 30 days prior to the adoption of the decision for the aforementioned changes, so that adequate time is given to competent authorities for their approval.

Article 27 brings about a novelty in comparison to the old Law, as concerns the obligation of the licensed bank or branch of foreign bank to pay annual commission to the Bank of Albania for the validity and use of the licence. The amount of this commission remains to be specified by the BoA by-laws, which leads to the need for reviewing the Regulation "On granting a licence to carry out banking activity in the Republic of Albania" (Article 14).

Article 28 provides additional cases, when verification constitutes a motive for revoking the licence of the bank or of the branch of foreign bank. We may mention here: breaches of this Law or by-laws issued by the Bank of Albania, which may lead to or cause a significant financial loss; breaches of national and international legal standards on accounting; exercising of activities that risk the liquidity and the solvency of the bank; the bank or the branch of the foreign bank is not able to provide sufficient own funds, and is no longer able to be relied on to fulfil its obligations towards its creditors and particularly no longer provides security for assets entrusted to it.

Point 4 of Article 28, unlike the old Law, adds the requirement for notifying also the Deposit Insurance Agency for such a decision. This should be reflected also in the Regulation "On granting a licence to carry out banking activity in the Republic of Albania (Article 10, point 3). Cases of licence revocation (point 1) and communication of revocation of licence (point 4), generally comply with Articles 14 and 17 respectively of the Directive 2000/12/EU and Directive 2006/48/EU. Also point 1, letter e, about non-commencement of activity by the bank or the branch of the foreign bank, complies (as concerns the penalty)

with Articles 14 and 17 of the Directive 2000/12/EU and Directive 2006/48/EU, but with the distinction that the term specified in the latter is 12 months from acquiring the licence and not 6 months, as specified in the Law.

I.III Chapter III "Organization, management and audit of the bank and branch of the foreign bank

Chapter III defines clear rules on organising, managing and auditing the activity of banks and branches of foreign banks, with the purpose to create a safe and sound banking system.

Article 31 of the Law speaks for the independence of the bank and the branch of a foreign bank and is improved and more complete than the respective article of the old Law (Article 16), since it stipulates that:

The bank and the branch of a foreign bank is administered and governed based on free market and fair competition principles. No subject or public person may interfere without authorization to influence the administration or the governing structures of the bank or branch of a foreign bank, except when complying with by-laws of the Bank of Albania, execution of orders from the judiciary organs or when it is so stipulated in the Law. This Article entitles the bank to operate in the market based on the principles of fair competition.

Article 32 stipulates the directing organs of the bank and branch of foreign bank. Unlike the provisions of the old law (Article 17), which states that banks are directed only by the Steering Council, the new Law specifies that the bank is directed by the Steering Council and the Directorate, making also a distinction between directing organs of the bank and of the branch of a foreign bank (point 4).

Article 33 on internal by-laws regulating the activity of the bank and the branch of a foreign bank, point 1/d (boundaries to the powers of the directors) is enlarged, including not only administrators and other employees of the bank, but also any other person that acts in the name and on behalf of the bank. Also, this Article brings about a novelty, allowing the internal by-laws of the branch of the foreign bank be issued in accordance with the regulatory acts of the parent bank (foreign bank) as long as the latter do not contradict with the Albanian legislation in force.

Drafting a Regulation on Corporate Governance, which would define accurately the processes through which credit institutions are directed and audited, and all relations, not only reporting but also auditing ones, which exist among groups of interest: shareholders, governing board, administrators and staff or other persons the institution is related with, is of special importance.

Article 35 on the composition of the Steering Council, brings about a new element in point 2 of this Article. So, the number of members, unlike the old Law (Article 19) which defined only their minimum number (5 members), requires not less than 5 and not more than 9 members. It also adds that the

initial members of the Steering Council shall be nominated in the Statute (point 3), unlike the old law which does not mention such a thing. New elements of the Law are also the criteria for electing or dismissing members of the Steering Council. We may mention point 4, which stipulates that: At least one third of the members of the Steering Council shall be composed of individuals that at the time of their election and throughout their mandate are not connected through private interests with the bank, shareholders that control the bank or its executive directors. In consequence, these elements should be presented in the Regulation "On administrators of banks and foreign bank branches".

Article 36 (meetings of the Steering Council) and some points of Article 37 (powers of the Steering Council) are new elements of this Law. So, the point 1 of Article 37 stipulates clearly the criteria and motives guiding members of Steering Council in exercising their powers. Point 2 stipulates the main responsibilities of the Steering Council, and Point 3 provides the right of the members of the Steering Council to request "appropriate, timely and adequate information", in discharging their responsibilities during the decision-making process. Therefore, these novelties should be presented in the Regulation "On administrators of banks and branches of foreign banks".

Article 38, point 1 on Audit Committee, contains more detailed provisions in comparison to the old Law as concerns the re-election, since such a thing was not provided in the old Law. Article 38, point 3 on duties of audit committee, provides new elements in relation to: considering internal audit reports and monitoring the way conclusions from such reports are dealt with; evaluating the financial situation of the bank based on the report of the statutory auditor; approving the financial reports and statements prepared by the bank and which the bank intends to publish. *These changes should be reflected in the Regulation "On internal audit in banks and branches of foreign banks" (point 6.4).* Article 38 provides also restrictions for members of the Audit Committee (point 5) and the requirement of the Audit Committee to report to the Steering Council (point 8). Point 6 entitles the Audit Committee to select external auditors, unlike Article 20/3 of the old Law, where this power belonged to the Steering Council.

Article 41 extends the disqualifying criteria for administrators of banks and branches of foreign banks. More concretely, there are mentioned cases in relation to: shareholder of more than 5 % of the voting rights or the shares in another bank or a person connected with him; an employee of the Bank of Albania, penalized by the Bank of Albania in the past 5 years for a serious breach of this Law or for carrying out activities for which there was no license in force by the Bank of Albania; etc.. Also, a person who acts or has acted, at any time for the past 5 years, as administrator of a bank, which has been subject to compulsory liquidation procedures pursuant to the provisions of this Law, is disqualified from the duty as administrator of the bank or branch of the foreign banks. The aforementioned period changes from the 12-month term defined in Article 21 of the old Law. All changes and novelties provided in Article 41 should also be reflected in the Regulation "On administrators of banks and branches of foreign banks" (Article 4).

Article 44 on prevention and resolution of conflicts of interests defines accurately in point 2, the sources of private interests of the administrator, adding their number in comparison to the old Law, with: interests deriving from: gifts, promises, favours, preferential treatments; negotiations for potential employment or any other form of relationship constituting a private interest for the director in the future, after leaving the position as administrator carried out by him whilst in the position of the administrator of the bank; engagement in private activities with the view to profit or any other activities which generate income. *Point 5* provides as new element, the responsibility of the Steering Council for the approval of the internal by-laws which determine the basic methods of prevention and efficient resolution of the conflict of interest, having also the right to set up and authorize *ad hoc* committees (composed of non-executive members of this Council), who would be responsible for dealing appropriately with the conflict of interests in the bank. *Article 46* which that speaks about internal audit unit, provides new elements as concerns powers of the Steering Council for setting out the rules for the functioning and implementation of the internal audit system (point 2); appointing the members of internal audit unit by the decision-making organs of the foreign bank (point 4); prohibiting the employees of the internal audit unit to have any other position in the bank or in the branch of the foreign bank (point 5). The latter ones should be reflected also in the Guideline "On internal audit of banks and branches of foreign banks" (point 6.3). *Article 47* on financial reports, specifies, in its point 1 and 2, that the bank or the branch of the foreign bank shall maintain accounts and prepare financial reports on individual or consolidated basis (unlike the old Law where such a thing was not mentioned, and in compliance with the provisions of the Directive 2000/12/EU, Article 22/1 and the Directive 2006/48/EU, Article 29/1).

Point 3 (The Bank of Albania requires that every bank or branch of foreign bank shall have management and accounting procedures as well as sufficient mechanisms of internal auditing, on individual or consolidated basis) and *point 4* (on the right of the Bank of Albania to define the form, type, methodology, contents and the time of reporting of banks and branches of foreign banks to the Bank of Albania) are new elements.

Article 48 on statutory auditors, provides for the first time in the Law, the fact that the branch of the foreign bank is audited by the statutory auditor that audits the foreign bank (parent bank) or a statutory auditor approved by the Bank of Albania (*point 3*). *Points 6* and *7* of this Article provide limits regarding the key audit partner in an auditing company, who carries out a statutory audit on behalf of the audit company. The above cases are specified in the Law and not in the by-laws, thus emphasising their importance. *Point 5* of this Article specifies that the statutory auditor or the key audit partner responsible for carrying out the statutory audit on behalf of the audit company, shall rotate from the statutory audit engagement within a maximum period of seven years from the date of appointment as statutory auditor, and is allowed to participate in the audit of the audited bank or branch of a foreign bank, after a period of at least two years. These new elements should also be reflected in the Regulation "On statutory auditors" Article 8, point 8.1.

Article 49 on audit from the statutory auditor, extends the powers on audit and statutory auditor, which should be added to the Regulation "On statutory auditors of banks", precisely about policies of writing-off balance sheet items; consolidated reports; accounting registration; accuracy and adequacy of reports submitted to the Bank of Albania; and adequacy of accounting procedures and regulatory compliance.

Article 50, point 1, adds the requirement of the statutory auditor to produce copies of the auditing reports to the Shareholders' Assembly. *Point 2* defines in a detailed way the cases when the statutory auditor shall immediately notify the Bank of Albania of facts or decisions of the bank or branch of foreign bank which put the activity at risk. These cases should be amended to the Regulation "On statutory auditors of banks". *Point 4* (The statutory auditor of the bank or branch of foreign bank shall also immediately notify the Bank of Albania of any such facts found in the course of discharging his duties in a subject who is a connected person with the bank) and *point 5* (The notification submitted to the Bank of Albania by the statutory auditor of the bank or branch of the foreign bank shall not constitute a breach of any contractual, legal or regulatory provisions of transparency and the statutory auditor shall be entirely discharged of any liability thereto), are new elements in the Law and fully comply with Articles 31, point 1/b; 31/2; 53/1 and 53/2 of the Directive 2000/12/EU and 2006/48/EU.

Article 53 of the Law (on transparency) specifies that the bank or branch of the foreign bank shall publish periodical reports on its financial situation and its risk position, at least once every three months. The bank shall prepare and publish its report on annual basis. This article envisages the need for re-designing the Guideline "On transparency of banking operations and services" or for drafting a new regulation on transparency and it is in consistency with the requirements of Articles 145/1 and 147/1 of the Directive 2006/48/EU (where the term specified is at least on yearly basis).

I.IV Chapter IV "Permitted activities for banks and branches of foreign banks"

This chapter provides permitted banking and financial activities that may be carried out by banks and branches of foreign banks, documentation required to be maintained by the latter ones as well as documentation related to credit transactions.

Article 54 makes a distinction between financial and banking activities that may be carried out by banks and branches of foreign banks as well as financial activity that may be carried out not only by the latter but also by non-bank financial entities (*Article 126*). Such a division is made in point 2 of this Article, which unlike Article 26 of the old Law, brings about a new designing relating to the exercising of these activities. Point 2 of Article 54 does not condition the exercising of these Activities with necessary supplying of a certain level of capital, but extends the power of the organisational units within the Bank of Albania⁷ to consider whether the subjects of this law should be permitted to

carry out certain financial activities since the licensing moment or even later on, upon request of the entity itself.

Unlike the old Law (Article 26), Article 54 of the new Law extends the range of financial activities that may be carried out by banks and branches of foreign banks. We may mention here: consumer loan, mortgage loan, factoring, financing of trade transactions, as well as other payment services, where besides credit and debit cards, payment cards are also included.

Financial activities listed in Article 54, point 2, comply fully with the activities listed in Annex I of the Directive 2000/12/EU and Annex I, point 2-14 of the Directive 2006/48/EU.

I.V Chapter V "Risk Management"

The main purpose of Chapter V is to define clearly the rules for risk management the bank or branch of the foreign bank is faced with or undertakes whilst carrying out its activity. This chapter is designed as a separate chapter and contains more detailed rules than the old Law.

Article 59 on regulatory capital, capital adequacy and guarantees is a re-designing of Article 30 of the old Law. Point 3 specifies that the ratio of regulatory capital adequacy is determined through by-laws of Bank of Albania and shall not be less than 8 %, thus reflecting this value even in the Law⁸. Also point 6 of this Article states that the regulatory capital adequacy ratio shall be calculated on individual or consolidated basis, thus being in consistency with Articles 40/2 and 40/3 of the Directive 2000/12/EU, where such a fact is also stated. Point 4 (specifying that in exceptional circumstances, the Bank of Albania shall, through by-laws, have the right to determine that a bank have a higher regulatory capital adequacy ratio, where it finds that such a bank carries out or is involved in higher risk activities) is in consistency with Articles 47/1 and 47/2 of the Directive 2000/12/EU, which stipulates that: Credit institutions shall be required permanently to maintain the ratio of capital adequacy at a level of at least 8 percent. Notwithstanding the above, the competent authorities may specify higher minimum ratios as they consider appropriate.

Point 7 (on requirements of the branch of a foreign bank to invest part of its initial endowed capital in at least one of the following assets: deposit in the Bank of Albania, securities issued by the Government of the Republic of Albania or the Bank of Albania and assets bearing low risk, point 8 (on the criteria of investment, in relation to the initial endowed capital) and point 9 (on guarantees for the settlement of liabilities of the branch of the foreign bank towards third parties in the Republic of Albania) are new elements amended to this Law. In consequence, the need for dealing with them more specifically in BoA by-laws arises.

Article 60, point 2 stipulates that the weighted coefficient for asset items on and off-balance sheet shall be determined according to the coefficients

specified by the Bank of Albania. But, unlike the old Law, it envisages the right of banks, with the approval of the Bank of Albania, to apply other methods and models for the evaluation of credit risk. Precisely, *point 3* of this Article (the bank may, with the approval of the Bank of Albania, apply other methods and models for the evaluation of credit, market and other risks) is in consistency with Article 84/1 of the Directive 2006/48/EU.

Article 64 on the maximum permitted exposure brings about a novelty in its *point 2*, because it reduces the maximum exposure to a person or persons connected to the bank from 30 percent to 25% of the regulatory capital (when the connected person or persons are a parent company, a subsidiary of the bank, one or more subsidiaries of the parent bank). Also, the law now specifies that the bank's exposure towards connected persons may not exceed 10 percent of its regulatory capital (*point 3*). These elements should also be reflected in the relevant regulation. *Point 1* (the bank's exposure towards a person or a connected person to it cannot exceed 20% of the regulatory capital), *point 2* (where such person or connected persons thereto are the parent company, a subsidiary of the bank, one or more subsidiaries of the parent bank, the exposure may not exceed 25% of the regulatory capital) and *point 4* (the bank may not undertake large exposures, which altogether exceed 700% of the regulatory capital) change from the provisions of the EU directives. More concretely, in *Article 49 of the Directive 2000/12/EU* and *111 of the Directive 2006/48/EU*, the percentages specified are respectively 25 percent, 20 percent and 800 percent.

Article 68 on Reserves for covering losses and *Article 70* on capital investments are also mentioned in the old Law, but are now presented in a more detailed way. *Point 1* specifies that: the bank may invest in the purchasing of shares of commercial companies which are not banks or financial institutions or may be a partner of a commercial company, for an amount not exceeding 10% of the capital of that company, but the investment at any time may not exceed 15% of the regulatory capital of the bank and *point 2* which states that: The maximum allowed investment of a bank in several commercial companies which are not banks or financial institutions or the maximum holdings as a partner in such commercial companies shall not exceed 60% of the regulatory capital of a banks comply with the limits specified in Articles 51/1, 51/2 of the Directive 2000/12/EU and Articles 120/1, 120/2 of the Directive 2006/48/EU.

I.VI Chapter VI "Supervision"

Chapter VI contains general provisions relating to the supervision process of banking and financial activity carried out by banks and branches of foreign banks.

Article 72 stipulates clearly and in a summarised way the ways through which supervision is carried out, unlike in the old Law where such ways are implied.

Article 73 on supervision of a bank, a branch of foreign bank and a branch of banks outside the territory of the Republic of Albania, unlike the old Law, in

point 5 entitles the authorised employees of the foreign supervisory authority, in charge of banking supervision in that country, following an agreement with the Bank of Albania, to be allowed to inspect a bank which is a branch or a subsidiary of the foreign bank, which has its head office in that country or has a qualifying holding in the foreign bank, the legal seat of which is situated in that country. This point complies with the requirements of Articles 43/1 and 139/2 of the Directive 2006/48/EU where the principle of reciprocal cooperation with the home country is stated, with the purpose to exercise supervision of credit institution. Also, *point 6* (on allowing the control and cooperation with the inspectors of the Bank of Albania and the statutory auditor, approved by the Bank of Albania) and *point 7* (the branch of the foreign bank, at least once a year informs the Bank of Albania on the names of the shareholders and their participation in the capital of the foreign bank) of this Article are in consistency with Articles 141/1 and 21/1 of the Directive 2006/48/EU.

Article 79 and Article 81 on implementation of rules for risk management and of requirements on capital adequacy ratio, unlike *Article 44* of the old Law, stipulate clearly and in a detailed way the measures taken by the Bank of Albania when finding that there are breaches of risk management rules, or that the ratio of capital adequacy of the bank is lower than the minimal ratio stipulated in *Article 59* of this Law. Now the Law provides also the requirement of the bank or branch of foreign bank to meet the legal obligations relating to deposit insurance (*Article 79, point 1/i and Article 80/i*). These elements, together with the above legal obligation, should be reflected also in the "Manual of corrective actions for banks and branches of foreign banks in the Republic of Albania".

I.VI.I Subchapter I "Consolidated supervision"

The Law No. 9662 of 18.12.2006 "On Banks in the Republic of Albania" treats for the first time, and as a separate subchapter, the consolidated supervision, pursuant to the principles of Basel Committee on Banking Supervision and the standards specified in the EU directives, for a safe and prudential supervision. This subchapter defines in a detailed way the most important constituent elements of supervision process on consolidated basis of banks and branches of foreign banks. The provisions of this subchapter define the concepts of banking and financial group, superordinate and subordinate companies. Also, necessary legal space is provided to the concluding of cooperation agreements with domestic or foreign competent supervisory authorities, to raise the quality of consolidated supervision.

Article 84 on risk management in a banking group specifies that: A banking group shall be organized in such a way that a superordinate bank in a banking group is able to monitor the risks to which the banking group is exposed and implement the measures for managing those risks. Such an element should be reflected in the Regulation "On consolidated supervision", in the framework of raising the quality of consolidated supervision (*Article 8*). Also *point 3/d*, specifies that: A banking group as a whole shall determine the consolidated

position of investments in the capital of non-financial institutions, arising the need for reflecting this element in the above Regulation, in its Article 7.

Article 85 on consolidation of financial statements of a banking group, point 2, states that the frequency of consolidation should be specified by BoA bylaws. Such a requirement should also be specified in the Regulation "On consolidated supervision" (Article 10). Also, *point 4* states that the Bank of Albania may order a bank in a banking group to carry out the consolidation of individual items or individual operations or groups of operations within the banking group, if such is necessary for the complete and objective presentation of the financial position and operating results of the banking group as a whole or an individual bank in the banking group. This raises the need for presenting these elements also in the abovementioned Regulation (Article 10).

Article 86 (consolidation in other cases) and *Article 88* (submission of data) are new elements that should be also reflected in the Regulation "On consolidated supervision".

I.VI.II Subchapter II "Sanctions"

The Bank of Albania, in its role of the supervisory authority of the banking system, has the right to take measures against banks, branches of foreign banks and nonblank financial institutions, in cases of breaches of the Law and/or of the bylaws issued by it. Sanctions, unlike preventive, supervisory measures for the implementation of risk management rules and measures for the implementation of requirements of capital adequacy ratio, aim to correct not only the deficiencies or weaknesses observed whilst exercising the activity, but also the to ensure the compliance of operations of the licensed subjects with the standards of a safe and sound banking and financial activity. Subject to aforementioned measures may be either bank management organs or the bank itself.

Article 89 on penalising measures, unlike the old Law (Article 44) lists in a detailed way all cases when the Bank of Albania decides for taking penalising measures, such as fines, written warning notices to the administrators of the bank or branch of a foreign bank, reaching to extreme measures, such as revocation of the licence of the bank or branch of the foreign bank or placing the bank into conservatorship or liquidation. Point 6 the Law stipulates a new condition as concerns the capital adequacy ratio. In Article 44/3 of the old law, the BoA required from the shareholders to mend the situation if the ratio dropped below half of the minimum required capital. In the new Law, the BoA takes penalising measures if this ratio is more than half of the minimum initial capital, but less than the minimum required capital, thus applying more prudential measures. Such a change should be reflected also in the manual on corrective actions, in the part of capital adequacy.

Article 91 on the requirement to protect professional secrecy, in its *point 1*, unlike the old Law, obliges also the inspectors and Bank of Albania employees

to keep the professional secrecy, in consistency with Article 30 of the Directive 2000/12/E and Articles 44/1 and 44/2 of the Directive 2006/48/EU on keeping this secret. But, unlike the above directives, the new Law extends this obligation also to administrators, employees or current and previous agents of the bank or branch of the foreign bank and not only to employees of supervisory authority or to auditors and experts of the bank or of the branch of the foreign bank.

Unlike Article 44, point 1 of the old Law which gives the right to seek redress from the court within 8 days from the notification of the decision, the Articles 93/1 and 93/2, stipulate the administrative recourse to the Governor of the Bank of Albania as a necessary condition to enable the subject to seek redress from the court. The right to seek redress from the court is also prescribed in Article 33 of the Directive 2000/12/E and Article 55 of the Directive 2006/48/EU.

I.VII. Chapter VII "Conservatorship and liquidation"

I.VII.I Subchapter: Conservatorship

This subchapter mentions cases of placing the bank into conservatorship, legal effects of conservatorship, qualifying and disqualifying conditions of conservator, powers, duties and reporting, as well as termination of conservatorship process.

The new Law, Article 89 point 4/d, unlike Article 44 point 2/f of the old Law, does not require the placing into conservatorship and control by the Bank of Albania, but mentions the placing of bank into conservatorship as a penalising measure applied by the Bank of Albania. Therefore, the revising of the Guideline "On conservatorship and liquidation of banks" in points 22-27 is needed.

Article 96, in points 3 and 4, unlike the old Law, envisages also the publication of the decision of the Bank of Albania for placing any of the banks under conservatorship in the Official Journal of the Republic of Albania, Official Bulletin of the Bank of Albania, as well as in one or more of the national newspapers. The Bank of Albania shall notify of its decision the bank, subject to this decision, as well as the Deposit Insurance Agency. The decision of the Bank of Albania for placing under conservatorship any of the banks shall be included also in the register it maintains for the public in its premises.

Article 99 provided qualifying criteria for the conservator, thus emphasising their importance in the Law as well, not only in its by-laws.

Article 100 on disqualifying criteria for the conservator, which is a novelty of the new Law, enlists in its point 1 the cases when a person can not be appointed as a conservator. All these disqualifying criteria should be also reflected in the relevant guideline.

The new law envisages in a separate article, precisely in *Article 102*, the periodical reports the conservator shall submit to the Bank of Albania, which in the old Law is envisaged indirectly (*Article 49*, point 7).

Article 104/1 on the evaluation of results of the conservatorship every 3 months, provides some re-designing of the old Law (*Article 50*) and of the Guideline “On conservatorship and liquidation of banks” (point 12), bringing about the obligation for the approximation of this guideline to the requirements of the new Law.

I.VII.II Subchapter II: Liquidation

This subchapter deals with stages through which a bank or branch of a foreign bank passes, in case it is placed into (voluntary or compulsory) liquidation, starting from the initial moment, reaching then to bank’s selling and reporting to the Bank of Albania.

Article 106 on types of liquidation, distinguishes, for the first time, between *voluntary liquidation and compulsory liquidation*, unlike the old Law, which in its interpretation seems as if it is addressing only to compulsory one.

Articles 107/3 and 107/4 underline the importance of the protection of interests of the clients of the bank or the branch of the foreign bank, being focused on two directions: first, through notification to the Deposits Insurance Agency for it to exercise its powers under the Law “On deposits insurance; secondly, through the obligation of the shareholders, who, in case the bank or branch of the foreign bank has been placed into liquidation, must meet all the creditors’ claims. *Given the above, these new elements should be reflected also in the Guideline “On conservatorship and liquidation of banks.*

Article 108 on circumstances for compulsory liquidation, specifies and extends the conditions related to the placement of the bank or branch of the foreign bank into compulsory liquidation.

Article 115 on Liquidator’s independence and protection of confidentiality, is a new specific Article, which gives the liquidator the right of exercising independently the activity, and his obligation to keep the professional secret.

Article 120 on claimed liabilities, point 3 is a new element that specifies clearly the Court as the competent organ where the claim by the claimant shall be submitted against the Bank of Albania’s decision for placing the bank or the branch of the foreign bank into liquidation, unlike the old Law that does not specify the responsible organ.

Article 121 on the order for debt repayment, in its point 1 enlists, *inter alia*, even the obligation for the settlement of claims of the Deposit Insurance Agency before other debts.

I.VIII. Chapter VIII: Final Provisions

This chapter of the Law, unlike the old Law, deals with a number of new elements, such as: protection of client and protection of secret of information of the client, nonblank financial subjects, legal protection in the exercise of duties and the executive character of administrative acts of the Bank of Albania.

Article 125 on protecting the secret of information of the client, further reinforces protection of interests of the latter, specifying for the first time the principle of protection of this information in a legal provision. This is done by including this obligation in the content of the agreement or contract concluded between the bank or branch of the foreign bank and the client. (point 2). This Article, being a new element of the Law, *may be reflected in the Guideline "On transparency of banking operations and services"*. The above article complies with Articles 30 and 44 respectively of the Directive 2000/12/EU and 2006/48/EU.

Article 127, unlike the old Law, provides for the first time the maintaining of a credit registry by the Bank of Albania. The purpose of maintaining such a registry is to assist banks to take decisions based on complete and accurate information when extending loans to their clients, and to strengthen the supervision of the Bank of Albania on the banking system in Albania.

Finally, *Article 132 point 1* extends the range of individuals subject to this legal protection in discharging the duty to employees⁹ of the BoA as well, besides the administrators and the members of the Supervisory Council.

Given the above, we may conclude that the provisions of the Law No. 9662, dated 18.12.2006 "On Banks in the Republic of Albania", are generally in consistency with the requirements of provisions defined in the Directive 2000/12/EU and Directive 2006/48/EU.

ENDNOTES

* Prepared by: Juna BOZDO and Irini KALLUCI, Research and Consistency Office, Supervision Department, Bank of Albania.

¹ Hereinafter the Law "On Banks in the Republic of Albania" No. 9662, dated 18.12.2006, will be referred to as "the Law".

² If a credit institution of a member state would like to establish a branch in another member state, it must obtain in advance the approval of the supervisory council of the home country. The latter one should notify within three months the supervisory authority of the host country for such a fact. After carrying out the supervision by the host authority on the institution under discussion, within two months the approval or refusal on branch establishment will be given (see Articles 4, 20/1, 20/4 of the 2000/12 Directive and Articles 6, 25, 26 of the 2006/48 Directive).

³ The naming of this regulation should be revised in order to include the term "financial activity" in it.

⁴ For more information, we may refer to Articles 6, 7, 20 of the Directive 2000/12/EU and Articles 11, 12, 21, 25 of the Directive 2006/48/EU.

⁵ For more information, we may refer to Articles 7, 21 of the Directive 2000/12/EU and Articles 12, 19, 25, 28, of the Directive 2006/48/EU.

⁶ This is a novelty of the Law and as such it should be reflected in a new regulation on the conditions of concluding an agreement.

⁷ Licensing Office of the Supervision Department of the Bank of Albania.

⁸ The value of the capital adequacy ratio stated in the new Law, refers only to banks. Concerning branches of foreign banks we will refer to the Regulation "On supervising the activity of branches of foreign banks in the Republic of Albania".

⁹ As for example, inspectors of the Bank of Albania.

THE NEW LAW NO. 9662, DATED 18 DECEMBER 2006 "ON BANKS IN THE REPUBLIC OF ALBANIA"

The new banking Law No.9662, dated 18 December 2006 "On banks in the Republic of Albania", is the fourth banking Law approved in the last 15 years. The purpose of this Law is to improve the banking and financial activity in Albania.

Apparently, often changes in the banking legislation are result of the fast development of the banking system in Albania and of the necessity to comply with the new market economy conditions and with the economic and institutional reforms undertaken during this period.

The first Law "On the banking system in Albania", 1992, along with the Law "On the Bank of Albania" founded the legal framework basis for the two level banking system.

The Law "On the banking system in the Republic of Albania", 1996, was focused in further amendments to better fit to the new environment and to reflect the development status in the country. Unfortunately, the crisis of 1997, the pyramidal schemes and their bankruptcy, among others made evident the inadequate and incomplete banking system legal framework. The Law did not define the responsible governmental authority that should intervene in case of an illegal activity, as it was the wide public credit. This resulted in grave social, political and economic impact. As result, after the crisis of 1997, amending the banking system legislation became an immediate demand.

The Law "On banks in the Republic of Albania", 1998, founded the basis of an adequate legal and regulatory framework, to enhance a safe and stable banking system which is in compliance with the international standards. During this period, the banking system experienced fast tremendous changes in extending the banking activities, privatizing the state-owned banks, increasing the number of private banks and their branches throughout the country, increasing the credits and the effective banking products.

Apparently Albania has taken secure steps in establishing a stable and competitive banking system. Investments of foreign European banks such as Raiffeisen Bank, San Paolo IMI, Societe Generale etc. has further improved the banking system and simultaneously has developed the competition in the market.

The abovementioned developments, the necessity to insure the banking and financial stability in Albania, the fulfilment of the obligations under the Stabilisation and Association Agreement framework and the necessity to bring our domestic legislation closer to the European one, required the amendments to the banking legislation.

In the legal context, as highlighted above, the most important aspect of the new Law is its compiling in accordance with the European Community Directives concerning the financial institution activity. The new Law refers to the European directives on credit institutions own funds; on payment rates; on capital adequacy of investment firms and credit institution; on monitoring and control of high exposures; on the prevention of money laundering and terrorism financing through the banking system.

The new Law "On Banks in the Republic of Albania", according to the definition in Article 1, is focused on setting the rules and conditions for establishing, licensing, organizing, managing, custody and liquidation of banks, branches of foreign banks, the banking activity and the supervision of this activity in the Republic of Albania.

In our opinion, unlike the previous Law, the new Law is more complete and accurate, thus affecting positively on increasing commercial banks' confidence in their daily activity. Thus, the Law clearly defines the role of the Bank of Albania in relation to commercial banks, it sanctions certain rules that were part of the Banking Regulations, hence covering all aspects of the banking activity, including those left, to a certain point, outside in the previous Law.

The Law clearly defines the Bank of Albania as the responsible authority to implement this Law. This role is achieved through the licensing of entities that exercise the financial and banking activity and through their supervision. According to Article 72 of the Law, the supervision is achieved through:

- The regulatory framework;
- The financial analysis, verification of periodical reported data of the banks and branches of foreign banks;
- Full-scope or partial examinations of the banking activity;
- Corrective measures;
- Cooperation agreements with foreign supervision authorities and foreign banks that have branches or subsidiaries in the Republic of Albania;

Unlike the previous Law, the new one defines the documentation a bank is required to submit to the Bank of Albania prior to starting its activity. This reveals the importance the Law confers to banking licensing and the transparency of this process. Until the new Law entered into force, this documentation was part of the banking regulations.

According to the new banking Law, the Bank of Albania sets limitations to the banking and financial activities of the banks, based on its own judgments not in the amount of the invested capital.

In addition, the new banking Law foresees the cases when the Bank of Albania revokes the licence of the bank or the branch of a foreign bank. The number of activities subject to prior approval of the Bank of Albania is also increased. New activities are:

- Changes of status;
- Changes of balance sheet structure through purchasing or selling assets and liabilities or through any other transactions, to the extent that jeopardizes the financial stability and its legal status;
- Increase in percentage or change of influencing participation of a shareholder above 20%, 33% or 50% of the banking capital or the voting rights etc..

Changes in the new Law concerning the banking licensing process are a guarantee for a safe and financially sound banking system. The new supervisory measures will help to increase bank confidence in performing its activities and prevent mismanagement, deterioration of the financial situation and other indicators.

Compared to the previous Law, the new legislation expands supervisory authority and boosts the active role of the Bank of Albania, enabling it not only to supervise the activity of entities licensed by the BoA, but also to intervene when banking or financial activity is being performed by entities that have not been licensed.

Article 5 of the Law defines that "Entities may not engage in banking activity in the Republic of Albania, unless they have the proper licence issued by the Bank of Albania". In the meantime, Article 90 defines that engaging in banking/financial activity without the proper license issued by the Bank of Albania constitutes a crime and it is subject to fine or up to three years of jail time. These measures insure the stability of the banking system and the prevention of the informal activities. As soon as the Law entered into force, the Bank of Albania in collaboration with the Ministry of Finance intervened to close down the informal foreign exchange market in Tirana and other districts, because this activity is in violation to the provisions of the Law No. 9662, dated 18 December 2006 and constitutes a criminal act of "Exercising unlicensed activity".

At the same time, the Bank of Albania is undertaking further measures to decrease costs of exercising the foreign exchange activity such as reducing the required minimum capital and the respective commissions.

The new banking Law is a step forward in our legislation and brings it closer to the European standards in the field of financial services, thus, introducing the basis of the banking institutions foundations. The definition of certain terms facilitates the understanding and the interpretation of the Law. There are clear and accurate definitions for terms such as "Related parties or group related parties", "Controlling persons", "Subsidiary", "Minimum initial capital" that were ruled under the Bank of Albania regulations. In addition, for the first time there are defined terms related to the consolidated supervision such as "Qualified participation", "Banking group" etc.

Here it would be worth mentioning that for the first time a special section of the Law has been dedicated to the prevention of money laundering and

terrorism financing by the banks. Special importance has been placed to preventing individuals from using the banking and financial system for purposes of money laundering and terrorism financing.

This provision obligates the entities of this Law to inform the authorities responsible for the fight against money laundering and terrorism financing in accordance with the specific laws designed for this purpose whenever there are reasonable doubts that certain funds or assets originate from criminal activities and can be used to finance terrorism.

The Law stipulates the principle of independence of the activity of the banks, stressing that banks are administered and managed based on the free market and fair competition. In this regard, no one can intervene in an unauthorized manner to influence the administration and the management of the bank except in cases when this is required by the Bank of Albania regulations, upon a court decision or when such interventions are foreseen by the Law.

The changes regarding the "Composition of the Steering Council" and "The Directorate" have a positive impact on how those bodies are conceived and organized. From our point of view, this revision in terms of the way banks are organized and managed narrows the gap between our standards and those of the European Union.

Clear rules are set for the administration of risks that banks undertake in their activities. From the point of view of the Risk Department of Raiffeisen Bank Int. Stk., Article 59 "The regulatory capital, capital adequacy and the guarantee" makes a distinction between the bank and the branch of a foreign bank. According to this provision, further details and clarifications will be given through rules and regulations of the Bank of Albania.

Referring to the draft regulation "On the Risk Administration of a Foreign Bank Branch" drafted by the Bank of Albania, there are set limitations regarding the risk that foreign bank branches may take. This is seen as an improvement as it is likely to encourage the fair competition in the market.

Also in Article 60 "Assets pondered by risk", there is a change in the methodology of the evaluation of assets pondered by risk. The purpose of this change is to better monitor the growth and quality of the credit portfolio in proportion with the regulatory capital.

The new Law also boosts the authority of the Internal Audit Unit, which has a direct impact on the strengthening of the internal control system of the bank. According to the Law, the internal control system aims at monitoring the implementation of internal practices and procedures, evaluating the efficiency of banking activity and monitoring the compliance with the laws and regulations.

Increasing the Internal Audit authority aims at reaching full compliance of bank's policies, procedures and banking operations with the legislation in

power which in the final analysis serves to the financial security and stability of the banks. This is seen as a positive tendency by the Internal Audit Department of the Raiffeisen Bank Jnt. Stk. because it serves as a basis for the department's activity in controlling and monitoring the efficiency of the implementation of bank procedures.

A new element in the new Law is the inclusion of certain general provisions regarding the protection of customers' interests, which in the meaning of this Law is "the person who uses the banking and financial services". This provision also stipulates the obligations that foreign banks or branches must fulfill with regard to their customers. This relates to the "banking transparency" in relation to the customers, i.e., each entity exercising banking or financial activity must keep its customers fully informed on the data and information so that the customers are able to correctly assess the terms of agreement they are entering with the bank as well as the obligations thereof.

Stipulating such banking obligations in a special provision of the Law is also in harmony with the civil right principles regarding the correctness and good faith between parties in a contract.

In conclusion, we consider the Law in its entirety, a guarantee for a secure and stable financial activity of the bank and for the protection of the financial stability in Albania. What is important at the present stage is that each of the licensed banks take the necessary steps to change and adapt their internal procedures in order to ensure full compliance of their activity with the requirements of the new Law and the regulatory acts of the Bank of Albania.

* Raiffeisen Bank. Legal and Compliance Department.

LENDING ACTIVITY: THE ABSENCE AND THE ADVANTAGES OF A CRUCIAL DEVELOPMENT FACTOR*

BANKING SYSTEM PERFORMANCE AND CREDIT PERFORMANCE

INTRODUCTION

The role of the financial system in the real sector of economy is a widely debated and studied issue in the economic literature. The different findings, often contradictory, have raised much debate among the economists. A big group of researchers, being among them Nobel prize winners, consider overvalued the significance given to the financial system as a factor of economic growth, while they think that it has a more supportive function since “entrepreneurship leads – finance follows” (Levine 2004). Meanwhile, during the recent years, an increasing number of researchers present empirical evidences that show a strong positive correlation between the financial system and the long-term economic growth, and that countries with performing banking system and markets grow fast. Furthermore, evidence at micro level proves that relaxed financing restraints is one of the channels through which financial system supports firm growth and economic development¹.

In order to perform its core functions, a financial system can be based on banking institutions and capital markets. Depending on its economic traits, a country could have more developed banks or capital markets. Developing countries in general, have less developed institutions and financial system is based on banking system (Demirgüç – Kunt and Huizinga 2000). Economic growth brings financial system participants development, and there is a general inclination in rich countries (with some exceptions like Germany and Japan) where capital markets grow with a faster pace (Demirgüç – Kunt and Levine 2001).

The financial system core functions in our country are nearly totally performed with banking intermediation. The last two years, the banking system activity has significantly increased while the ratio total assets-to-GDP has risen by more than 30 per cent. The highly stressed credit expansion has brought more dynamics in the banking activity and economy. Credit process not only provides resources distribution on lucrative projects affecting economic growth, but it contains risks that relate to the institution and could be transmitted to the economy. Under these conditions, the determination of opportunities and risks takes special meaning toward undertaking proper policies with the purpose of taking advantage of opportunities and eliminating or reducing risks.

The Albanian banking system has an almost 15 years period history of evolution. Despite growth oscillations in the first half of this period, the events

after 1997 have shown a major progress of the system followed by activity regulation through the 1998 banking law and respective framework. The first years of transition were portrayed by legal, institutional and structural reforms. The approval of 1998 law determined the end of “foundation construction” stage and led to the normality of the banking operations. New banks were established during the following stage and gradual deepening of financial intermediation took place through new products offered and credit base expansion. The latest has been evidenced as one of the convulsive activities that highly effects not only the banking system, but the entire economy. Such factors has drawn our attention for further examination.

Based on literature and other countries experience, we will try to make an analysis of credit activity developments by indicating the activity characteristics and the reasons behind such major increase of the recent years. We will also try to identify opportunities and risks, which associate the intense activities of expanded loan portfolios and increased banking services.

CAUSES OF CREDIT GROWTH AND LOAN PORTFOLIO CHARACTERISTICS

CAUSES OF CREDIT GROWTH

Cottarelli, Dell’Ariccia and Vladkova-Hollar (2003) in a study on rapid credit growth on East and South European countries have defined Albania as a “Sleeping Beauty” due to a low ratio of loans to private sector-to-GDP (less than 1% during 1998–2002) compared to other countries. Nevertheless, since then the situation has changed significantly. Loans have increased moderately until 2004, followed by a sharp increase in the next two years, 82 per cent in 2005 and 55 per cent in 2006. Actually, the ratio loans-to-GDP accounts for more than 20 per cent.

In theory, there are identified two main reasons behind credit growth: supply shift and demand shift. An important factor that induces the demand is productivity shift (Keeton 1999). The source of loan supply is the banking system or the other non-banks financial institutions, while on the demand side are lined up individuals and business companies.

On one hand, the loans increase due to supply shift is a result of promoting policies of financial institutions for their customers, through decreasing interest rates or adding flexibility to the selection process or requirements toward collateral or financial analysis. On the other hand, the loans increase could be a result of an increased demand from borrowers. Such increased demand can be based on productivity shift, due to better projects or technological improvements, or based on other factors related to their specific financial situation.

For many years, the commercial banks have been applying a conservative approach toward private business. The deposits collected from the public have

been mainly invested in treasury bills or similar securities with high security and low return. The loan to economy, for the private activity as well as for the individuals, has been restricted, with high interest rates and long and careful procedures. The following table shows that the loan to public sector has been quite small and decreasing. In the meantime, the loan to private sector, the high portion of the loan portfolio, has been at low levels due to the fact that fewer assets have been invested in such activity (table 1).

Table 1 Loan structure according to allocation in economy (in % to total portfolio)

| | 2001 | 2002 | 2003 | 2004 | 2005 | 2006 |
|---|-------|------|------|-------|-------|-------|
| Domestic loan structure | | | | | | |
| Domestic loan (% M3) | | | 71.5 | 68.9 | 70.0 | 71.8 |
| Loan to the government (% M3) | | | 60.2 | 55.1 | 48.9 | 43.4 |
| Loan to economy (% M3) | | | 11.3 | 13.8 | 21.1 | 28.4 |
| Loan portfolio structure for the banking system | | | | | | |
| Public sector | 1.95 | 0.1 | 0.3 | 0.17 | 0.05 | 0.09 |
| Private sector | 83.31 | 81.4 | 75.2 | 68.82 | 69.41 | 66.91 |
| Individuals and others | 14.75 | 18.5 | 24.5 | 31.01 | 30.54 | 33.00 |

Source: Bank of Albania

The privatization of the biggest bank of the system in 2004 obliged the banks to reconsider their business strategies. The activity, which mostly felt such policy changes, was lending. The best part of the banks started applying a more active approach toward financing the economy. In this framework, the strategies of the banks generally included the relaxation of strict procedures, interest rates decrease and increased number of services offered. Such behaviour aimed at increasing the loan portfolio, market share and reinforcing their market position.

The borrowers' demand has always been steady, high and with an increasing trend. Despite the conservative approach from the banking system, high costs and low range of products offered, the businesses and individuals have always referred to banks' desks to finance their consumption, investments or fulfill the short-term liquidity requirements.

Based on the lending demand and offer dynamics, we could say that the sharp increase of crediting in the last two years is a product of combination of an incremented offer in a high demand environment. The increased competition in a stable macroeconomic environment with a high loan demand, established the necessary settings for the banking system to become active in the process of financing the economy.

The following part outlines our estimation about the main factors that effected the crediting increase.

- Macroeconomic stability. Duenwald, Gueorguiev and Schaechter (2005) in a study on rapid credit growth on three Eastern Europe countries assert that a steady macroeconomic environment with a high GDP growth and low inflation brings to a rapid credit expansion. During the last decade, it is estimated that Albania has reached a stable macroeconomic situation; the gross domestic production has

steadily increased, during 1999 – 2005 the real GDP has increased 6.5 per cent on average and inflation has been kept within the target range, fluctuating at around 3 per cent. The economic increase has been associated with unemployment decrease and income per capita increased. Since Albania is an economy in transition and aims at adhering the European Union, the economy and income will keep on with the increase in order to converge toward the western standards. The security associated with such a process and the stable macroeconomic environment have eased the future developments predictions. The increased security has affected the individuals and companies decisions to finance their consumption and investments as well as banks decisions to relieve more funds to the public and to lower interest rates (table 1).

Table 2 Some macroeconomic indicators

| | 1999 | 2000 | 2001 | 2002 | 2003 | 2004 | 2005 | 2006 |
|----------------------------|------|--------|-------|--------|-------|-------|-------|-------|
| Real GDP growth (%) | 8.9 | 7.7 | 6.5 | 4.7 | 6 | 6 | 5.5 | 5.0 |
| GDP per capita (USD) | | 1086 | 1329 | 1,438 | 1,807 | 2,329 | 2,620 | 2,855 |
| Average inflation (v/v) | -1 | 4.2 | 3.5 | 1.7 | 3.3 | 2.2 | 20. | 2.5 |
| Unemployment rate | | 16.9 | 14.6 | 15.8 | 15.0 | 14.6 | 14.2 | 13.8 |
| Budget deficit (% of GDP) | 12.3 | 9.4 | 8.0 | 6.2 | 4.6 | 4.5 | 3.3 | 3.2 |
| Current account (% of GDP) | | - 7.0 | - 6.1 | - 10.0 | - 7.9 | - 4.8 | - 7.3 | - 7.6 |
| Loans / GDP (in %) | 8.4 | 5.31 | 4.7 | 5.9 | 6.8 | 8.5 | 15.3 | 22.0 |
| Lending increase (%) | 12.7 | -31.05 | 0.22 | 37.72 | 31.1 | 38.1 | 74.3 | 56.8 |
| Loan interest rate (%) | 25.5 | 25.5 | 25.5 | 25.5 | 25.5 | 25.5 | 25.5 | 25.5 |

Source: Bank of Albania

- Restoring public confidence in the banking system. The actual level of relationships between banks and the public is a result of several factors and events, positive and negative, occurred since the creation of banking system. There are some elements with negative impact that need to be mentioned. It has often been debated about the low banking culture of the public. Such culture has been mostly expressed in the lack of knowledge toward banking products and avoiding the repayment of loan obligations. The latest has been induced by the preferential selection of the borrowers from the former-government owned banks. While the characteristic of the private banks has been restricted funds offered with high costs, which has somewhat created the opinion for non-equal selection of the applicants. Moreover, during the transition years, the banking system has faced two critical moments, the 1997 crisis and the 2002 panic, which shook the public confidence. Such events have affected the trust relationship between banks and the public and have held back the public non considering the bank as a partner in its activity.
- Meanwhile, the positive elements have had a major impact. Prudent policies, from banks and supervising authority, have brought continuous increment and stability in the financial activity, especially in the last years. The development of the system has created the necessary

environment for the restoration of public confidence in banks. The increased competition and the introduction of reputable banks in the international markets, have affected the consolidation of mutual relations, which is expressed in deposits increase and wide usage of banking products. The product of such events has been the activation of interrelated factors trust – banking culture. The latest developments have shown that earlier behaviours such as non-repayment of loan obligation, have radically changed. Consciousness over the financial burdens has brought back the mutual trust and the further extension of business relations between the bank and the customer.

- Low crediting base, catching-up hypothesis (see table 2, loans / GDP). One of the reasons of crediting increase is related to the very low loan level to the economy. The low economic development combined with the crisis effects, prudent policies on risk management of foreign banks, ceiling over credits set by the Bank of Albania for certain banks as well as behaviour/public non-trust, have negatively affected the banking system development in general and lending activity in particular. The improvement or the removal of these hurdles, has naturally inflicted banking development and activity increase.
- Property effect. The literature has identified a mutual empirical correlation between loans and real estate prices. For several years, the real estate prices have continuously increased. Prices increase affects crediting increase via two channels: (i) collateral value increase. Real estate is one the main objects required as collateral, hence its price fluctuation determines the borrowing capacity; (ii) future positive expectations, since real estate constitutes an important part of individuals or companies properties. Changes of asset prices impact on consumption and investment planning of the consumers.
- Ownership structure changes and new licences. The entrance of new banks in the market has significantly increased competition. Recently licensed banks, aiming at gaining market share and approaching more and more customers, have offered to the public a higher range of products. But, the major effect was in the market given the ownership change of the biggest bank in the country, which used to be the last ranked in terms of lending. The resurgence of this bank deposits has given a strong burst to quantity and variety of products offered. The most typical product provided is lending and, as mentioned above, the market demanded it with eagerness. However, the struggle between the new banks fighting to increase and the existing banks, which tend to maintain their shares, has brought to lending increase. Foreign shareholders, as major owners of banking system shares, have brought in the Albanian market the experience of the consolidated European markets and induced competition, “awakening” the sleepy banks. Ownership change is a continuous process that proceeds with the latest entrance in the market of big banks, a French one and an Italian one.

Table 3 Number of licenses for banks (after 1997)

| | 1998 | 1999 | 2001 | 2002 | 2003 | 2004 | 2005 | 2006 |
|---------------------|------|------|------|------|------|------|------|------|
| New banks | 2 | 2 | - | 1 | 1 | 1 | - | 1 |
| Shareholders change | | | | 1 | | 1 | | 2 |

Source: Bank of Albania

- Banks balance-sheet structure. As shown in table 4, banks assets have not been used in lending, hence its increase is expected to be the banks' focus (considering that the biggest bank in the system, possessing more than 50 per cent of the assets until 2004, was prohibited from lending). Moreover, banks, for years, used to have high adequacy ratios², which demonstrates their high capacity to undertake risks. Although profitability ratios announce good position, the main income resource related to the placements in banks outside the country, treasury bills investments and commissions from banking services, mainly transfers.

Table 4 – Banking system financial indicators

| | 1999 | 2000 | 2001 | 2002 | 2003 | 2004 | 2005 | 2006 |
|-----------------------------------|------|------|------|------|------|------|------|------|
| Systems assets / GDP | | 50.2 | 53.5 | 51.6 | 50.2 | 51.9 | 59.3 | 69.4 |
| Capital adequacy ² (%) | 8.2 | 42 | 35.3 | 31.6 | 28.5 | 21.6 | 18.6 | 18.1 |
| ROA (return on assets, %) | 0.6 | 2.1 | 1.5 | 1.2 | 1.2 | 1.3 | 1.4 | 1.36 |
| ROE (return on equity, %) | 16.4 | 20.7 | 21.6 | 19.1 | 19.5 | 21.1 | 22.2 | 20.2 |
| Deposits / Liabilities (%) | | | 86.2 | 84.0 | 87.5 | 87.0 | 87.2 | 83.3 |
| Loan / assets (%) | 16.4 | 10.4 | 8.9 | 11.5 | 13.6 | 16.4 | 25.7 | 31.5 |

Source: Bank of Albania

CHARACTERISTICS OF CREDIT PORTFOLIO

- Credit structure according to currency. In the Albanian economy, the usage of foreign currencies, particularly U.S. dollar and EURO, as references in transactions is widely spread. Until 2001, US dollar was considered the most important currency and it has been used since in most of the commercial activities, as a mean of protection from currency depreciation and for facilitating the transactions with the foreign companies. USD lost its prevalence with the entrance of Euro in Euro Zone in 2001. Reflecting this trend, the currency structure of banks' deposits was mainly made of these currencies. On the other hand, banks themselves have found the use of these currencies more convenient in their crediting activity to avoid the risk of exchange rate and interest rate fluctuations. The stability of exchange rate was in line with banks' prudence in risk taking activities and the stability of interest rate was in line with the careful planning for future revenues. The banks had also low incentives in investing in LEK since the interest they were receiving from investing in treasury bills was satisfactory enough. For the above reasons, the foreign currencies were dominant in the loan structure according to currencies. Furthermore, the public has not preferred loans in LEK since the interest rate applied was higher. As shown from the table, such trend has changed recently. The stability of LEK, the high liquidity and the increased competition has increased lending in home currency.

Table 5 Credit structure
by currency (in % of credit
portfolio)

| | 2001 | 2002 | 2003 | 2004 | 2005 | 2006 |
|----------------------------|-------|-------|------|-------|-------|-------|
| Loan portfolio by currency | | | | | | |
| Loans in LEK | 18.3 | 20.9 | 17.9 | 19.5 | 24.5 | 28.1 |
| Loans in other currencies | 81.7 | 79.0 | 82.1 | 80.5 | 75.6 | 71.9 |
| Loan portfolio by maturity | | | | | | |
| Short-term loans | 55.11 | 47.72 | 40.3 | 26.74 | 26.16 | 25.57 |
| Mid-term loans | 19.01 | 23.38 | 29.6 | 35.27 | 30.60 | 30.78 |
| Long-term loans | 5.40 | 7.56 | 9.2 | 15.75 | 23.15 | 19.03 |
| Real estate loans | 14.90 | 17.09 | 15.6 | 15.14 | 13.00 | 19.39 |
| Leasing | 0.0 | 0.0 | 0.0 | 0.0 | 0.05 | 0.02 |
| Other | 5.57 | 4.24 | 5.3 | 7.10 | 7.04 | 5.21 |

Source: Bank of Albania

- Credit structure by maturity. At the beginning of lending activity, as the low economic development suggested, the loans were issued on short terms and mainly for working capital purposes. As the economy of the country was mainly based on commerce with other countries than financing in short terms in compliance with the commercial cycle was more preferable. Only few investments were financed in long term. Such tendency has strongly changed and long-term financing has gained more ground. This is due to the increased investments in the economy as well as to the increased demand for real estates from the individuals, the latest has had the major impact. Earlier, a loan with a maturity longer than 5 years could not be issued, while actually the maturity on mortgage loans can be as long as 20 years.
- Credit structure by economic activity. From table 6 can be noticed that loans for real estates have increased significantly, considering that loan growth was 82 per cent in 2005 (see comments for maturity in the upper paragraph). Nevertheless, credit to industry and services have decreased, despite the sectors internal processes. Loan to agricultural sector, despite the increasing trend, still remains low in percentage of the entire portfolio. The best applicable type of loan to this sector could be the micro one, but the banks have not been able to provide it due to high expenses and the appropriate infrastructure it requires. There are some non-bank financial institutions that provide such loans, but their capacity is still not comparable to the banks. Meanwhile, the data show that construction remains important in the economy and the recent events have shown an increase in housing prices.

Table 6 Credit distribution
by economic sectors (in % of
credit portfolio)

| Economy sector | 2001 | 2002 | 2003 | 2004 | 2005 | 2006 |
|----------------------|------|------|------|------|------|------|
| Transport & Services | 58.4 | 57.7 | 57.8 | 43.8 | 36.8 | |
| Industry | 24.5 | 20.3 | 21.1 | 20.2 | 16.9 | |
| Construction | 12.5 | 8.6 | 10.0 | 9.8 | 13.0 | |
| Real estates | 6.3 | 9.1 | 13.0 | 9.8 | 14.2 | |
| Agriculture | 1.0 | 0.8 | 1.0 | 1.5 | 2.7 | |
| Other | 0.8 | 7.7 | 5.1 | 19.3 | 22.1 | |

Source: Bank of Albania

- Credits supported by deposits. Banks balance-sheets show that loans-to-deposits ratio is low and the deposit-to-assets ratio is high (table 4). Such fact is mentioned to show that the entire lending activity has been supported by public's funds (deposits). As mentioned above, the structure of the deposits according to maturity and currency has influenced the structure of the loan portfolio. Banks have rarely used external financing to support their credits. In different banks, loans-to-assets and/or deposits-to-assets ratios are various. The smaller ones have higher ratios of loans-to-assets and lower ratios of deposit-to-assets, while the contrary situation is faced for bigger banks. This is a sign of competitiveness and the struggle the smaller banks are making to maintain their market share. Such developments might bring changes in the future, like mergers of banks or purchase of smaller banks by larger ones, as the case of American Bank and Italian-Albanian Bank shows.

| | 2001 | 2002 | 2003 | 2004 | 2005 | 2006 |
|--------------------------------|------|------|------|------|------|------|
| Deposits in Lek | 11.4 | 10.5 | 9.3 | 16.6 | 37.3 | 40.3 |
| Private sector | 7.1 | 6.6 | 4.5 | 6.0 | 8.7 | 11.3 |
| Individuals | 1.3 | 1.3 | 1.6 | 6.5 | 24.3 | 23.9 |
| Deposits in foreign currencies | 42.6 | 44.0 | 47.3 | 55.4 | 72.7 | 94.0 |
| Private sector | 8.9 | 9.0 | 10.0 | 10.6 | 12.8 | 20.9 |
| Individuals | 28.6 | 30.1 | 33.7 | 41.5 | 55.2 | 68.0 |

Source: Bank of Albania

Table 7 Deposits structure by currencies (in % of credit portfolio)

OPPORTUNITIES AND RISKS

OPPORTUNITIES

Banks play a crucial role in the economic activity of most developed and developing countries. Rapid developments in the capital markets and the continuous improvements in the technology of information have lessened the importance of these institutions in the developed countries, while in developing countries banks still occupy the primary position in the intermediation process and remain an important source of economic growth. In literature it is emphasized a strong interaction between finance and the real sector. On one hand, financial development stimulates productivity and economic growth and on the other hand, economic growth is associated with wider, deeper and more developed financial system. Levine (2004) argues that financial development occurs when the financial structure – its instruments, markets and institutions – ameliorates the effect of information, enforcement and transaction costs. Albania has a bank based financial system. The privatization of the largest bank in the system has driven on competition, stimulating a chain reaction in the banking system per se and in the economy. Banks are expanding geographically, are introducing new and more complex products and services. At the same time, through this active crediting policy the dormant capital, stored in the safety vaults of the banks, now is channeled. An active crediting policy eases financial constraints imposed on firms, stimulating

growth and generating several positive effects. In the following part we will try to analyze the consequences that credit expansion and financial development might have in the real and financial sector.

The main function of a financial system is to facilitate the allocation and development of the economic resources in time, space in an uncertain economic environment. This is a narrow definition of the financial function and is far from being complete. Under a functional perspective, a financial system in addition to the function of pooling funds provides (ii) a payment system for the exchange of goods and services; (iii) mechanisms that transfer funds in time, space and across industries; (iv) tools to administer uncertainty and risk; (v) price information for a better decision making process in various sectors; (vi) techniques to ease the asymmetric information and incentive problems between parties, Merton (1995).

Asymmetric information is a critical issue in the crediting activity undertaken from banks, as one party, in this case the bank, does not have all the information on a certain project regarding the expected return and the real risk. This situation creates problems in the financial sector in two directions: before the occurrence of the transaction, creating the adverse selection problem³, and after the transaction, leading to moral hazard situation.

Adverse selection in financial markets is evidenced when banks select to finance borrowers that are most likely to become “bad credit risks” – poor projects or high risk, since it is difficult for banks to determine the quality of some borrowers. At the same time, investors that are involved in high risk projects are willing to accept high interest rates as they are the primary benefactor if the project is successfully finalized.

The moral hazard issue in financial markets might be observed when the borrower, after the loan is extended, gets involved in activities that are undesirable from the perspective of the lender as they might increase the probability of default. This situation is the result of the asymmetry of information between the lender and the borrower. The lender lacks information regarding borrower’s activities, permitting the latter to engage in activities that constitute moral hazard. Anyhow, asymmetric information is not the only reason for the occurrence of this phenomenon. High enforcement costs make it very expensive for the lender to prevent moral hazard despite being fully informed regarding borrower’s activities. The main reasons behind this situation are linked with the incentives that some borrowers have to invest in high risk projects in which if the projects are successful the borrower is the main beneficiary, otherwise the loss falls upon the lender.

To avoid the conflict of interest, result of adverse selection and moral hazard, lenders may decide to reduce the supply of funds, affecting the credit to the economy and the investment process. However, banks employ other means to reduce the effects of asymmetric information, such as collateral or the production and sale of the information on the activities of individuals and firms involved in projects that require capital. Collateral, giving the right to the

lender to sell it in case of default, reduces bank's losses, lessening the effects of adverse selection and moral hazard. While with the production and sale of information, the problem is dealt in a rather different manner. Lenders buy information on the activities of the investors who seek funds for their projects to lessen the asymmetry of information. However, the presence of free riders, persons who profit, free ride off, from the information that others pay for, diminishes the advantages of this tool. Banks help in reducing asymmetric information as these institutions are involved in long term relation with their costumers, enabling them to become experts in the production and sale of information on individuals and firms. Banks avoid the free rider problem by making private loans and exerting monitoring and enforcement activities to collect information.

The information produced by banks can be used not only to reduce the effect of asymmetric information between parties, but it is also used to evaluate firms, managers or the economic environment. Banks collect, process and produce information and sell it to investors. This process helps investors reduce research and evaluation costs and at the same time improves economic resources allocation among higher value investments.

In the context of factors that stimulate the economic activity, it is emphasized the importance of foreign direct investment (FDI). FDI contribute in the modernization and development of the host country economy through technological transfer, managerial skills, know-how, productivity gains etc. Despite this fact, it is widely agreed that domestic market conditions and the degree of financial system development are determinants of the quantity and quality of FDI. Economies with better financial systems are more efficient in the resource allocation process, as they improve the absorption capacity of the economy and develop the operating environment of domestic and foreign firms. The practice of banks' activity in the country shows that in general foreign banks tend to target (build stronger relations) with customers from their countries of origin. In this perspective, the presence or the entrance of banks from various countries will not only be a support to the business from the respective country of origin but at the same time is expected to attract new investors and business in the production and services sector.

RISKS

Financial crises often are the negative and undesirable effects of the risky activities that banks are engaged in. Banks manage their operational activity trying to optimize between profitable and prudential activities. Lending activity is a core function performed by banks and very often is considered as the main purpose of the banking activity. That is why banks dedicate considerable resources – human and capital, for a continuous development and improvement of this process. Despite being a source of profits, lending activity is as well a source of risk. In the following section we try to elaborate the macroeconomic and microeconomic risk that might arise in the presence of rapid credit growth.

RISK DETERMINANTS

The empirical evidence of many countries has shown that the lending behavior of the financial institutions is procyclical and loan supply is closely related to the business cycles of the economy. In the expansion phase of the economic activity lending supply increases significantly, to fall during downturns. During this phase of economic activity, credit supply can fall dramatically as to create the situation known as “credit crunch”. Credit crunch usually is an extension of recession and in the presence of this situation it is difficult for companies to finance their projects because of high bankruptcies or defaults rates. Generally, changes in lending are more than proportional compared to the changes in economic activity, so loan supply tends to reinforce the business cycle. In the same line with lending supply behave loan performance problems. Reflecting the expansionary phase of the business activity loan performance indicators are in low values, to raise in high values during downturns. This suggests that the risk undertaken by the banks during expansion is materialized latter in time as it takes time for non-performing loans to appear.

There is a vast literature about the factors that explain fluctuations in bank lending policy and as the main factor is identified the (irrational) behavior of banks’ managers. The irrational behavior of bank’s managers will have an immediate effect on a misevaluation of credit risk and accumulation of problems. Management behavior is explained in the context of four main theories: disaster myopia (Guttentag and Herring, 1984, 1986), herd behavior (Rajan, 1994), agency problem and institutional memory hypothesis (Berger and Udell, 2003).

Disaster myopia arises when it is impossible to assign the probability of a future event. The occurrence of such event depends on changes in the economic regime, legal framework or several other hard to predict factors. Banks tend to underestimate the probability of low-frequency shocks over. For this reason, in the expansionary phase of the business cycle, banks will increase lending supply while in downturns, when the probability of low-frequency shocks increases, will decrease it drastically.

Herd behavior theory supports the idea that bank managers are concerned only for their performance and reputation in the short run. This behavior is noticed particularly in those managers that are not successful or those who constantly lose market shares. To avoid getting fired managers have incentives to follow their successful peers targeting as customers the same industries or groups. This behavior tends toward a similar evaluation of clients and accentuation of the lending and problem loans cycle. Short term performance and reputation of the managers prevail on bank’s long term and steady growth.

Principal agency theory inside an organization can be evidenced in two levels of hierarchy. The first level is between shareholders and high management. Shareholders put pressures on managers to achieve high profits and based on manager’s performance, measured through different bank performance

systems, the shareholders apply the reward scheme. However, the strategy followed here becomes important. If quantitative measurements of performance prevail over qualitative ones, then irrational behavior of managers might be expected. Their decisions will be directed toward quantitative growth and expansion leaving behind the financial worthiness of their decisions.

On the second level, the principal-agency may arise between the managers of different levels inside the institutions. Delegation of duties and responsibilities is followed by the establishment of measures of performance for managers of lower levels. Even in this case the accurate choice of measurements of performance becomes important for the bank to take the right decisions in compliance with the overall strategies. To some extent, the managers of a lower level might find it easier to find another job, which causes them less incentive toward the proper functioning of their entity.

Berger and Udell (2003) have elaborated a hypothesis named “the institutional memory”. According to this theory bad loan customer or relation are forgotten for two reasons. First, there exists a knowledge and professional gap as new employees are hired and the older ones retire. Second, loan officers, as time passes build confidence and forget past experiences and mistakes. It can be summarized that some employees / loan officers might have never experienced “problem periods”, while some forget past valuable experiences, this will result in an easing of credit standards, meaning higher risk.

In addition to management’s irrational behavior there is another institutional factor that can trigger risk – collateral. The collateralized level of the loan can, in many cases, shadow the qualitative evaluation of the customer. Jiménez and Saurina (2004) have dedicated a thorough analysis to this problem. The high level of collateral makes the loan officer lay back / shirk and devote less attention to the problems of the borrower. Such a problem is enforced by the type of borrower or the experience of the bank. As in the first stage of relation between the bank and the customer, officers are more attentive, while in a long term, consolidated bank – customer relation and when banks expand locally, the information asymmetry that might arise could in many cases be covered with the requisite for higher collateral.

With regards to risks there are other institutional factors that determine it. Godlewski (2004) has listed the following factors that lead to high risk taking:

- inadequate credit policy;
- inadequate risk administration structures;
- inadequate internal control procedures;
- inadequate systems of non performing loans identification;
- poor corporate governance and excessive concentration of decision authority.

These factors, combined or separately, are evidence of institutional weakness and can create incentives for possible failures and distress.

MICROECONOMIC RISKS

Microeconomic risks are mostly related to individual institutions or the whole banking sector. There are two approaches to analyze these types of risks. There are internal governmental decisions that lead to high and uncontrolled risks and there are uncertain situations which lead to tighter measures or reduced activity or even performance. As for the first case, we presented a brief overview in the previous part; here we will go through the second type, always having as reference credit growth.

The first and most direct source of risk is the one related to credit. Credit risk consists in the non-fulfillment of obligations from the borrowers' party. Delayed repayment of loan obligations causes the deterioration of the credit portfolio. Banks need to create more reserves to cover for losses, which in turn will impair their profits. The high level of nonperforming loans leads to contraction of credit activity due to both internal initiatives to reduce further risk taking and central governmental restrictive measures.

Bad loans creation significantly reduces profits, which as a result hinders the capital accumulation ability. Low capital levels put serious impairments to bank's further development; at least slows down the activity in the short run. As result of the risks undertaken, the bank has to meet the requirements of central bank for maintaining certain levels of risky loans in relation to the regulatory capital reflected in capital reduction. Lower capital availability will significantly deteriorate bank's financial position. In extreme situations, the high level of losses can deteriorate the financial position of the bank up to the bankruptcy point, with consequences in the banking system.

High insolvency rates affect the banks ability to fulfill its financial commitment toward third parties. This leads to the next risk source, liquidity. In the case of Albania, banks' investments have been mainly focused on low return and low risk securities such as treasury bills and short term placements in other banks. There have been few cases when investments have been directed to other countries' capital markets, but still the security has been the main criteria of choice. This prudential / conservative strategy has provided banks with enough liquidity, but on the other side banks have put low efforts on the management of funds. As the situation is under radical change, the past secure situation of banks is being put under hazard. Liquidity concerns are making banks reconsider their old policies and expand their diapason of interrelationship between financial institutions inside and outside the country. Maturity matching of assets and liabilities has been one requisite of central bank control, though in the situation of increased long-term loan creates what are called maturity GAP⁴. Despite the fact that actually in the banking system, loans are totally covered by deposit, the maturity gap is increasing. The average maturity for deposits is one year, while for loans the maturity period is substantially higher, up to 20 years for mortgages / housing. Liquidity management is taking an important role in bank's risk management process.

As it was mentioned in the first section, loan portfolio is compounded of several different currencies, with foreign currencies constituting the majority. The high quantity of foreign currency used in the country gives space to exchange rate risk effects. Such a structure of loan portfolio is a result either of funds (deposits) available or market demand. Under the context of risk management, banks manage their foreign currency funds through open position⁵. The level of the open position determines the level of exposure toward currency developments - appreciations/depreciations. Exchange rate volatility can damage balance sheet, assets – liability structure, in that currency, impairing its payment capacity, liquidity situation and profitability. Accumulated losses are covered by the bank's profits or capital creating a "domino effect", which is related to the sources of risks mentioned previously.

Actually, in the Albanian banking system there is a large scale of borrowers that generate their revenues in one currency and have to pay their contractual obligations in another currency. Very often, bank policies compel customers to borrow in a certain currency despite their revenue currencies. In this way borrowers are exposed to adverse movements of the exchange rate, increasing the probability to default.

In addition, the dominance of foreign currency in loan portfolio increases interest rate risk. Banks build their interest rate policies based on reference interest rates of respective currencies in use⁶. Usually banks issue loans based on basic interest rate adding a spread / margin. The matching strategy of different maturities of assets and liabilities of the same currency is needed to help them protect from adverse developments in the international environment.

All these risks lead to scarcity of funds for the banks. Therefore, to cope with this deficiency banks will seek funds in the financial market or customers. But a weak / poor payment capacity will have serious repercussion in the institution. From one side banks or other financial institutions will have less incentive to collaborate and on the other side public trust might be threatened. The second case is what is called episode of panic that leads to so called bank run. Such situations are harmful not only to one or few institutions; they might spread to all sectors with serious consequences for the whole economy.

MACROECONOMIC RISKS

Banking distress and economic downturns are highly correlated to one another. There is an extensive debate among economists on the direction of causality, which is the one that causes the other, but all seem to accept that there is a high degree of interaction. Even in this case, it is obvious that there are two ways of approach when analyzing the risks. As we will have a look upon the economic situation as a whole, a combination of cause-effect analysis on both sides will be included.

As the Albanian economy and banking sector are still in the early stage of economic development, they are both in a growth phase of business cycle.

In a recent study, IMF (2005) assesses that the financial system in Albania does not seem vulnerable to short-term shocks. However, the rapid credit expansion during the last year has caught the attention of this institution as well as other institutions in the country.

The Bank of Albania has proposed some restrictive measures to relate credit growth with bank's capital level. Such measures consist in the estimation that credit growth above a given threshold is considered risky; hence a higher weighting ratio is applied and the bank can issue loans as much as its capital adequacy allows.

Kaminsky, et. al (1998), in a literature review on banking crises, report that five out of seven studies find credit growth to be an important determinant of banking and/or currency crises. In the same study they find that three out of four credit booms are linked to banking crises and seven out of eight to currency crises. Kaminsky and Reinhart (1999) name the interrelation of these as twin crises. In fact, a currency exchange rate fluctuation will deteriorate the bank's financial situation due to the open position it creates (see footnote 6). In addition, the bank's borrower financial situation will worsen with currency crisis. It is a fact that many borrowers in Albania have a different denominated currency business cash flow from the loan currency. As they might receive their income in ALL and have to repay back the loan in another currency, say EUR, the depreciation of ALL toward EUR will weaken their liquidity position. Therefore, it will have a strong impact on the nonperforming loans. With the rapid credit growth, such impact is expected to be even higher.

In emerging markets credit booms are closely linked with economic downturns. While, during the development period credit booms are associated with higher domestic interest rates and deterioration of the current account deficit (IMF 2004a). In periods of high competition and credit growth, banks are in need of funds. One of the actions they might take is increase deposits from the public through the increase of interest rates. This is more typical for smaller banks that have less available funds. In events of crises, those are the most fragile ones and the main generators of panic or bank run.

Unexpected changes of interest rates might damage banks. Loans interest rates are settled based on a reference interest rate and have the option to adjust them generally for a period not shorter than one year. In the long run, banks can adjust their policies and interest rate, thus reduce exposure to unexpected interest rates changes. While, in the short run, covenants in the contracts prevent banks to adjust quickly which leaves them exposed. Interest rates management is an existing function in the bank, but still the level of maturity mismatching between assets and liabilities leaves them exposed to such risk.

Loan growth stimulates investment and consumption. Higher investment and consumption rates generally are associated with prices increase, so higher inflation. High inflation, on the other side, hinders economic activity, affecting the financial situation of businesses and households. A deteriorated financial

situation of the economic agents is reflected in arrears, unpaid loans or even bankruptcies. Credit growth leads to higher assets prices; as a matter of fact there is a strong interaction between the two. There is an increasing trend for mortgage loans in response to the high demand for houses / real estate. In most cases, such houses are used as the collateral for the loan. Usually banks evaluate the collateral and its value is always higher than the loan amount. Just recently, the Bank of Albania has warned about the possibility of the housing prices bubble and that a subsequent burst would have severe consequences in the banking system balance sheet and in the economic activity as well.

Increased domestic demand is also reflected in higher imports and a subsequent deterioration in trade balance and current account. The domestic economy is heavily dependant on imports thus this chain of events could bring serious danger to the economy in the form of higher prices and wages and real appreciation of the domestic currency. To sum up, deterioration in trade balance reflected in current account deficit, hazards the macroeconomic growth. Weak macroeconomic environment, on the other hand, has its repercussion in the financial positions of firms and individuals increasing the probability of borrowers' insolvency and this one to the creation of nonperforming loans.

CONCLUSIONS

In this material we tried to analyze the latest developments in the banking system, with a special attention to the credit activity. During the last 3-4 years the Albanian economy, like many other emerging economies in South-Eastern Europe, is experiencing a rapid credit growth. We believe that economic stability, the restoration of public trust in the banking system under the close supervision of the responsible regulatory authority have created the necessary conditions for a normal and stable activity in the banking sector and the economy. During this period banks were able to build financial and human capacities, which under the pressures of competition were materialized in a more developed banking system with credit activity on the lead. In addition to lending activity, the fierce competition has forced banks to improve existing products and services, to introduce new ones, expand geographically etc.

Developments in the banking system are expected to be transmitted in the real sector of the economy. By offering more products and services banks support their customers in the saving and investment decisions stimulating growth. At the same time, the banking system might improve the operational environment of domestic and foreign firms. But on the other side, rapid credit growth poses risks to the financial and economic stability. Credit cycles tend to follow business cycles, expanded high credit supply and low levels of nonperforming loans indicators, while in downturns low credit supply and elevated levels of nonperforming loans indicators. Thus, the risk undertaken during the growth phase will start to appear when the economic activity will start to moderate its pace. In addition, rapid credit growth might build inflation pressures, deteriorate trade balance and increase the exposure towards

international shocks through adverse movements in the exchange rate and interest rates.

Banks per se are fragile institutions, prone to risks, as result of adverse selections or of the risky environment they operate in. In these conditions, it is vital to have the timely and prudent intervention of monetary and supervisory authorities with the purpose of maintaining under control the negative effects and leading the progress toward a steady growth.

ENDNOTES

* Elona Bollano, Monetary Policy Department; Gerond Ziu, Supervision Department, Bank of Albania.

¹ For a detailed analysis of the studies over the correlation of finance and economic growth refer to Ross Levine, 2004, "Finance and growth: Theory and evidence", JEL Numbers: G0, O0

² This ratio is used for supervisory purposes. It is calculated as the ratio between the bank regulatory capital and the risk weighted assets. With the entry into force of the new banking law, it is required to be 8% at lowest, from 12% previously required.

³ Adverse selection, also known as "the lemon problem", was first noted by the American economist George Arthur Akerlof during the 70'. This situation arises from the inability of traders/buyers to differentiate between different qualities that certain products might have. The typical example cited to illustrate this situation is the second hand car industry. Refer to Majluf (1983) and Mishkin (1991), for a deeper analysis of the adverse selection problem in the financial system.

⁴ GAP is calculated as the difference between assets and liabilities of the same maturity. For its accuracy it is measured as a percentage of total assets or profitable assets. It is generally measured for 1, 3, 6 or 12 months in order to determine bank's solvency toward the individual depositors.

⁵ Open position in a currency is the difference between assets and liabilities denominated in the same currency. It is said to be long when assets overcome liabilities and short in the contrary situation. The regulatory framework of the Bank of Albania requires that this position must not be higher than 20% of the regulatory capital for each currency and not higher than 30% for all the open positions.

⁶ Actually there are three currencies in use in the Albanian banking system, USD, EUR and ALL (Albanian Lek). LIBOR / EURIBOR interest rates are taken as reference for USD and EUR loans and treasury bills discount rates for ALL loans.

LITERATURE

Berger, A., and G. UDELL (2003). "The institutional memory hypothesis and the procyclicality of bank lending behaviour", BIS Working Paper, n.º 125, January, Basel.

Bank of Albania Annual Reports, www.bankofalbania.org

Cottarelli C., Dell'Ariccia G., Vladkova-Hollar I., 2003, "Early Birds, Late Risers, and Sleeping Beauties: Bank Credit Growth to the Private Sector in Central and Eastern Europe and the Balkans", IMF Working Papers, WP/03/213

Demirguc, Asli & Huizinga, H, 2000, "Determinants of Commercial Bank Interest Margins and Profitability: Some International Evidence", World Bank Economic Review, Oxford University Press, vol. 13(2), pages 379-408, May.

Demirgüç-Kunt A., and R. Levine (2001), "Bank-Based and Market-Based Financial Systems: Cross-Country Comparisons", In: Financial Structure and Economic Growth: A Cross-Country Comparison of Banks, Markets, and Development, Eds: A. Demirguc-Kunt and R. Levine. Cambridge, MA: MIT Press: 81-140.

Duenwald C., Gueorguiev N., Schaechter A., 2005, "Too Much of a Good Thing? Credit Booms in Transition Economies: The Cases of Bulgaria, Romania, and Ukraine", IMF Working Papers, WP/05/128

Godlewski L. C., 2004, "Excess credit risk & bank's default risk, an application of default prediction's models to banks from Emerging Market Economies", Université Robert Schuman

Gourinchas, Pierre-Olivier, Rodrigo Valdes and Oscar Landerretsche, 1999, "Lending Booms: Some Stylized Facts," unpublished manuscript, Princeton University and Central Bank of Chile (August).

Guttentag, J., and R. Herring, 1984, "Credit rationing and financial disorder", The Journal of Finance, 39, pp. 1359-1382.

International Monetary Fund, 2004, "Are Credit Booms in Emerging Markets a Concern?", World Economic Outlook, April 2004, Chapter IV

International Monetary Fund, 2005, "Albania: Financial System Stability Assessment, including Reports on the Observance of Standards and Codes on the following topics: Banking Supervision and Payment Systems", IMF Country Report No. 05/274, August 2005

Jiménez G., and Saurina J., 2005, "Credit Cycles, Credit Risk and Prudential Regulation", Banco de España, Documento de Trabajo nº 0531

Kaminsky G., and C. M. Reinhart, 1998, "The twin crises: The causes of banking and balance of payments problems" International Finance Discussion Paper No.544 (Washington Board of Governors of the Federal System, March). /American Economic Review, 89(3), 473-500

Kaminsky G., and Reinhart C. M., 1999, "The Twin Crises: The Causes of Banking and Balance of Payments Problems," American Economic Review, Vol. 89, pp. 473–500.

Keeton W. R., 1999, "Does Faster Loan Growth Lead to Higher Loan Losses?", Federal Reserve Bank of Kansas City, Economic Review - Second Quarter 1999

Levine R., 2004, "Finance and Growth: Theory and Evidence", NBER Working Paper No. W10766

Merton, R. C. (1995), "A Functional Perspective of Financial Intermediation", Financial Management, 24: 23-41.

Mishkin F. S., 1996, "Understanding Financial Crises: A Developing Country Perspective", NBER Working Paper Series, Working Paper 5600.

Mishkin F. S., 1991, "Anatomy of a Financial Crises ", NBER Working Paper Series, Working Paper 3934.

Myers, S. C., and N. Majluf, 1984, "Corporate Financing and Investment Decisions when Firms Have Information that Investors Do Not Have", Journal of Financial Economics, 13: 187-221.

Rajan, R. (1994). "Why bank credit policies fluctuate: a theory and some evidence", Quarterly Journal of Economics, 109, pp. 399-441.

BANK OF ALBANIA NEWS OVER APRIL-JUNE 2007

On the seminar "EU approximation process in South East Europe: The role of the financial sector"

On 3 May 2007, the Bank of Albania organized the seminar "EU approximation process in South East Europe: The role of the financial sector". The seminar was held in the premises of "Tirana International Hotel" and it was attended by experts from the Bank of Albania, representatives of commercial banks, the Albanian Association of Banks and the Financial Supervisory Authority. Mr. Maxwell Watson who at present, holds the post of Economic Advisor to the Director-General of Economic and Financial Affairs of the European Commission (ECFIN) and is a senior member of St. Antony's College, Oxford was the main speaker. The participants discussed the role of the financial sector in the European integration process of the region, focusing on common concerns that characterize South East European economies, such as the fast credit growth in the private sector.

On the official visit of the Deputy Governor of the Bank of Sweden, Mr. Lars Nyberg, at the Bank of Albania

On 16 May 2007, the Deputy Governor of the Central Bank of Sweden, Mr. Lars Nyberg, invited by the Governor of the Bank of Albania, Mr. Ardian Fullani, attended a formal visit to our Bank. During his stay in Albania Mr. Nyberg was engaged in meetings with Governor Fullani, the First Deputy Governor, the members of the Supervisory Council and other officials of the Bank of Albania. The purpose of these meetings was to deepen institutional collaboration in the future. Mr. Nyberg also expressed the commitment of the Bank of Sweden to provide technical assistance. This collaboration will provide the Bank of Albania with expertise and technical assistance in specific fields, such as monetary analyses and estimations, financial stability, monetary policy implementation, supervision of financial markets, as well as public education and communication in general.

On the official visit of the Governor of the Bulgarian National Bank, Mr. Ivan Iskrov, at the Bank of Albania

On 18 May 2007, the Governor of the Bulgarian National Bank (BNB), Mr. Ivan Iskrov, invited by the Governor of the Bank of Albania, Mr. Ardian Fullani, attended an official visit in Albania. Governor Iskrov's visit marked a new step forward in strengthening multilateral relations and collaboration among the central banks of the region. During the meeting that was organized on this occasion, the two Governors discussed the latest economic developments and the challenges that both central banks have faced, in the pursuit of further consolidation of the macroeconomic and financial stability in their respective countries. On the occasion of the official visit of Governor Iskrov, the Bank of Albania held an open meeting in its premises. Deputies of the Economy and Finance Commission, representatives from the Ministry of Finance; the European Commission, diplomats accredited to Tirana, the commercial banks, and representatives from several research institutes, participated in

this open meeting. In light of the event, Mr. Iskrov delivered a speech on the subject "The Road to the European Union: The role of the Central Bank".

On 21 May, 2007, the Governor of the Bank of Albania, Mr. Ardian Fullani and the Deputy Managing Director of the International Monetary Fund (IMF), Mr. Murilo Portugal held a meeting at the premises of the Bank of Albania. During the meeting Governor Fullani valued the relations between the Bank of Albania and the International Monetary Fund as an ongoing support for the implementation of the necessary reforms and the consolidation of the Albanian banking system. On his side, Mr. Portugal expressed that Albania represents a country which has made a remarkable progress in terms of achieving and preserving the macroeconomic stability, where a special merit goes to the Bank of Albania, which has been very successful in implementing its monetary policies. In the IMF press release on the visit in Albania Mr. Portugal stated that: "Albania's inflation expectations are well anchored at low levels, thanks to the credibility, transparency and professionalism of the Bank of Albania. Looking ahead, strong independent institutions, such as the Bank of Albania, will become the key internal anchors for economic policy making. While the current very high rate of credit growth will entail additional challenges for the Bank of Albania, we are heartened to see that this growth is mainly directed at business investments."

On the meeting of the Governor of the Bank of Albania, Mr. Ardian Fullani, with the Deputy Managing Director of the International Monetary Fund, Mr. Murilo Portugal

The meeting ended with the conclusion that the future collaboration with the IMF will evolve to meet a new approach of the relation between the IMF and Albania, which will accompany the country throughout its journey from the position of candidacy to that of accession in the big European family.

The President of the Italian Republic, His Excellency Giorgio Napolitano, conferred the title "Commendatore dell'Ordine della Stella della solidarietà italiana/Commander of the Order of the Star of Italian Solidarity" on the Governor of the Bank of Albania, Mr. Ardian Fullani, with the citation: "For the distinguished contribution of Governor Fullani to the further enhancement of co-operation in the economic area between the Republic of Italy and the Republic of Albania. The award ceremony took place at the Bank of Albania premises, on 7 June 2007, wherein the Ambassador of the Republic of Italy in Tirana, His Excellency Mr. Attilio Massimo Iannucci, consigned the title to the Governor of the Bank of Albania, Mr. Ardian Fullani, in the presence of many national and international personalities.

The Governor of the Bank of Albania, Mr. Ardian Fullani was awarded with the Order of the Star of Italian Solidarity by the President of the Italian Republic, His Excellency Giorgio Napolitano

In his speech, Ambassador Iannucci commended the Governor of the Bank of Albania, Mr. Ardian Fullani for the efforts and merits in establishing concrete opportunities for the flow of both Italian and foreign capital into Albania, particularly in the financial sector. Mr. Iannucci said that Governor Fullani has also acted as the Albanian "economic ambassador", transmitting the achievements and challenges of Albania beyond the Adriatic Sea.

On the official visit of the Governor of the Bank of Albania, Mr. Ardian Fullani, at the Bank of England

In light of the intensification of relations with other central banks, the Governor of the Bank of Albania, Mr. Ardian Fullani, invited by the Director of the Center for Central Banking Studies, Mr. Mario Blejer, paid an official visit to the Bank of England. On this occasion Governor Fullani met with the Deputy Governor, Mrs. Rachel Lomax, the Director of the Center for Central Banking, Mr. Mario Blejer, and other high officials of the Bank of England. During these meetings they praised the bilateral institutional collaboration, which has been increasing during the last two years. The collaboration will continue to grow through the technical assistance provided, participation in regional seminars, and those organized by the Bank of England.

On the training seminar "The role of the Bank of Albania in the economy" organized by the Bank of Albania for the high school teachers in Tirana

On 25-29 June 2007, the Bank of Albania, with the support of the Regional Directory of Education in Tirana, organized a training seminar on the subject "The role of the Bank of Albania in the economy", at the premises of "President" hotel in Tirana. The seminar was intended for an audience of teachers of applied economics and sociology and aimed to discuss different issues of finance, economy and central banking, as well as to give a complete presentation of the role that the Central Bank plays in the economy, the dynamics of an open market economy, and the financial and banking system. Further on, this meeting between Central Bank specialists and high school teachers gave them the opportunity to think on and clarify questions or issues they encountered during their education process.

At the end of the activity, certificates were distributed to the teachers for their participation.

This training seminar represents a new activity for the Bank of Albania and it is the third phase of an educational project that was initiated during April of this year. The project focuses on the financial and economic field and it started by distributing educational brochures to the public and non-public high schools of Tirana.

Further on, the second phase was organized by the specialists of the Bank of Albania and consisted in informative discussions held with students during economics classes in some of the high schools of Tirana. During these discussion meetings, which were frequently held in the form of interactive discussions, were discussed issues such as the history, the functions, and the role of the Bank of Albania in the economy, as well as the banking system and the services it provides. Additionally, the discussions dealt with more tangible issues for the students, such as the personal budget, money, how to manage income, as well as how to spend and save money. In the last years, public education has been perceived by the Bank of Albania as a precondition not only for increasing the Bank's transparency and responsibility versus the public, but also for creating a suitable environment for the development of its activities. Consequently, the Bank of Albania frequently carries out initiatives in the field of financial and economic education, aiming to increase the reputation and credibility of the Central Bank as an institution and also to increase public knowledge on the open market economy.

LEGAL EVENTS OVER APRIL-JUNE 2007

MONETARY OPERATIONS

On 16 May 2007, the Supervisory Council of the Bank of Albania approved upon Decision No. 22 some amendments to the Regulation "On repurchase and reverse repurchase agreements" approved upon the amended Decision No. 93, dated 13 December 2006 of the Supervisory Council of the Bank of Albania. The purpose of these amendments was to improve and facilitate the use of repurchase and reverse repurchase agreements during the open market operations carried out while implementing the monetary policy of the Bank of Albania.

On 16 May 2007, the Supervisory Council of the Bank of Albania approved upon Decision No. 23 some amendments to the contract "On securities repurchase and reverse repurchase agreements", approved upon the amended Decision No. 13 dated 9 February 2005 of the Supervisory Council of the Bank of Albania. These amendments precede the amendment to the Regulation "On repurchase and reverse repurchase agreements" and it is required for the practical application of the instrument of repurchase and reverse repurchase agreements.

On 27 June 2007, the Supervisory Council of the Bank of Albania approved Decision No. 33 "On the raise of the interest rate of repurchase and reverse repurchase agreements". Upon this Decision, the interest rate of repurchase and reverse repurchase agreements (weekly repos and reverse repos) is raised by 25 basis points, reaching 5.75 per cent from 5.50 per cent.

ISSUE

On 6 June 2007, the Supervisory Council of the Bank of Albania approved Decision No. 29 "On the configuration of the banknote with nominal value 2000 lekë, having legal tender". This Decision approves the configurations of design and security elements of the banknote with nominal value 2000 lekë, having legal tender.

BANKING SUPERVISION

On 6 June 2007, the Supervisory Council of the Bank of Albania approved Decision No. 30 "On the approval of the transfer of ownership of 80 per cent of shares to the share capital of the American Bank of Albania Jnt. Stk.,

from the Albanian-American Enterprise Fund to Intesa Sanpaolo s.p.a., Italy". Upon the approval of this transfer Intesa Sanpaolo s.p.a. owns 80 per cent of the share capital of the American Bank of Albania while the Albanian-American Enterprise Fund owns 20 per cent.

On 6 June 2007, the Supervisory Council of the Bank of Albania approved Decision No. 31 "On the approval of the Regulation "On the licensing, organization, activity and supervision of foreign exchange bureaus"". The purpose of this Regulation is to set out the criteria and rules for the licensing, organization, activity and supervision of foreign exchange bureaus.

On 27 June 2007, the Supervisory Council of the Bank of Albania approved Decision No. 35 "On the granting of licence to the "First Investment Bank, Albania Jnt. Stk." to conduct banking activity". This Decision becomes effective upon its publication in the Official Gazette of the Republic of Albania.

ECONOMIC POLICY

On 10 April 2007, the Parliament of the Republic of Albania ratified upon Decision No. 9709 "The loan agreement between the Council of Ministers of the Republic of Albania and the European Bank for Reconstruction and Development (EBRD) for the financing of the rehabilitation and construction project of the road Fier (Levan) – Tepelenë". According to this Agreement, EBRD will finance an amount of EUR 35 million for the rehabilitation and construction of 70 km of the road Fier – Tepelenë.

On 11 April 2007, the Council of Ministers approved upon Decision No. 188 "The agreement between the Council of Ministers of the Republic of Albania and the Government of the Austrian Republic for the mutual assistance and cooperation in customs-related matters".

On 16 April 2007, the Parliament of the Republic of Albania approved upon Decision No. 9715 some amendments and insertions to the Law No. 9461, dated 21 December 2005 "On the nomenclature of goods and customs tariff".

On 19 April 2007, the Parliament of the Republic of Albania issued the resolution "On the assessment of the activity of Competition Authority for 2006". The Parliament observed that the activity of this institution has been in line with Article 164 of the Law No. 8417, dated 21 October 1998 "The Constitution of the Republic of Albania" and the Law No. 9121, dated 28 July 2003 "On the protection of competition", amended upon the Law No. 9499, dated 3 April 2006 and that the Competition Authority has played a key role in promoting and protecting free competition and consumers' interests.

On 19 April 2007, the Parliament of the Republic of Albania ratified upon Decision No. 9717, "The loan agreement between the Republic of Albania, represented by the Council of Ministers, and the Council of Europe

Development Bank". This agreement provides for the extension of a loan of EUR 14 million for the financing of the project "Quality and equality in education".

On 3 May 2007, the Parliament of the Republic of Albania issued the resolution "On the assessment of the activity of the Bank of Albania". The Parliament assessed the activity of this institution during 2006, in terms of maintaining the country's economic and financial stability and preserving the economic development rates in line with the projected rates. For the following year, the Parliament recommends to the Bank of Albania the formulation of medium-term monetary policies in order to meet the obligations deriving from the Stabilization and Association Agreement with the EU and the provision of monetary policy-related suggestions to the Government in order to formulate long-term strategies.

On 3 May 2007, the Parliament of the Republic of Albania approved Decision No. 9723 "On the National Registration Centre". This Law regulates the organization, functioning and activity of the National Registration Centre; the administration of commercial register and defines the entities to be registered and the registration procedures.

On 4 May 2007, the Council of Ministers approved the Decision No. 285, "On the establishment of the referring monthly wage, for the effect of calculating the social and health insurance contributions and the tax on personal income according to the nomenclature of economic activity for non-public sector employees who carry out qualified or non-qualified work and for their managing and technical-economical personnel".

On 7 May 2007, the Parliament of the Republic of Albania ratified upon Decision No. 9709 "The financial contract between the Republic of Albania and the European Investment Bank (EIB) for the financing of the rehabilitation and construction project of the road Fier (Levan) – Tepelenë". According to this agreement, the EIB will finance an amount of EUR 50 million for the rehabilitation and construction of 70 km of the road Fier – Tepelenë.

On 10 May 2007, the Parliament of the Republic of Albania issued the resolution "On the assessment of the activity of the Financial Supervisory Authority for 2006". The Parliament observed that in the first months of its activity, this institution has consolidated the regulatory and supervisory functions of non-bank financial activities and that it has played a key role in the licensing, supervision and regulation of the activity of entities in the banking financial sector.

On 10 May 2007, the Parliament of the Republic of Albania approved upon Decision No. 9731 some amendments and insertions to the amended Law No. 8894, dated 14 May 2002 "On the Loan Collection Agency". According to this Decision, the Loan Collection Agency is a public judicial person, under the Minister of Finance and the scope of this agency is to collect entirely state-owned loans and other assets transferred by commercial banks to this agency.

It also handles the investment portfolio in apartments from INSIG Jnt. Stk. and other assets transferred by special laws.

On 10 May 2007, the Parliament of the Republic of Albania ratified upon Decision No. 9730 "The financial agreement between the Council of Ministers of the Republic of Albania and the International Development Agency (IDA) for the land administration and management project". According to this agreement, the International Development Agency will provide a total amount of EUR 15.200.000 for enhancing the efficiency and effectiveness of land and urban administration.

On 14 May 2007, the Parliament of the Republic of Albania ratified upon Decision No. 9733 "The free trade agreement between the Republic of Albania and the Republic of Turkey". The scopes of this agreement are the enhancement and extension of economic cooperation between the two countries; the elimination of trade in goods restrictions and the provision of the right competition conditions in trade between countries.

On 17 May 2007, the Parliament of the Republic of Albania approved upon Decision No. 9737 some amendments and insertions to the amended Law No. 8560, dated 22 December 1999 "On tax procedures". According to this Law, the entities conducting economic commercial activity are obliged to register at the National Registration Centre, which at the same time implies the registration at the tax authorities.

On 31 May 2007, the Parliament of the Republic of Albania approved the resolution "On the assessment of the activity of Deposit Insurance Agency for 2006". The Parliament assessed positively the activity of this institution in the exchange of information with the Supervisory Authority (Bank of Albania) for the accuracy checking of the premium calculated by banking institutions and insured with this institution, as well as for the assessment of their financial situation. The Economy and Finance Commission recommend the deepening of studies in the deposits insurance schemes in the country's integration process.

On 7 June 2007, the Parliament of the Republic of Albania approved upon Decision No. 9751 some amendments and insertions to the amended Law No. 7638, dated 19 November 1992 "On commercial companies".

On 25 June 2007, the Parliament of the Republic of Albania amended upon Decision No. 9762 some amendments to the Law No. 8782, dated 3 May 2001 "On savings and credit associations". According to these amendments, the name of a savings and credit association in official and public letters and other documents of the association is preceded by the words "savings and credit association". Following these words, the name of the association and its registration number are written. These associations are registered in the authority responsible for the registration of the entities.

BANK OF ALBANIA MANAGEMENT 30 JUNE 2007

SUPERVISORY COUNCIL

| | |
|------------------|---------------|
| ARDIAN FULLANI | Chairman |
| FATOS IBRAHIMI | Vice Chairman |
| TEFTA ÇUÇI | Member |
| ELISABËTA GJONI | Member |
| LIMOS MALAJ | Member |
| KSENOFON KRISAFI | Member |
| ADRIAN CIVICI | Member |
| ARJAN KADAREJA | Member |
| HALIT XHAFA | Member |

GOVERNOR

ARDIAN FULLANI

GOVERNOR'S OFFICE

GENC MAMANI

DEPUTY GOVERNORS

| | |
|----------------|-----------------------|
| FATOS IBRAHIMI | First Deputy Governor |
|----------------|-----------------------|

GENERAL INSPECTOR

TEUTA BALETA

DEPARTMENTS AND OTHER UNITS

| | |
|---|-----------------------|
| HUMAN RESOURCES DEPARTMENT | Dashmir Halilaj |
| MONETARY POLICY DEPARTMENT | Gramoz Kolasi |
| RESEARCH DEPARTMENT | - |
| MONETARY OPERATIONS DEPARTMENT | Marian Gjermeni |
| SUPERVISION DEPARTMENT | Klodion Shehu |
| INFORMATION TECHNOLOGY DEPARTMENT | Xhilda Kanini Deliana |
| STATISTICS DEPARTMENT | Kliti Ceca |
| ISSUE DEPARTMENT | Valer Miho |
| ACCOUNTING AND PAYMENTS DEPARTMENT | Marseda Dumani |
| LEGAL DEPARTMENT | Toni Gogu |
| AUDIT DEPARTMENT | Teuta Baleta |
| FOREIGN RELATIONS, EUROPEAN INTEGRATION AND COMMUNICATION DEPARTMENT | Ina Kraja |
| ADMINISTRATION DEPARTMENT | Agron Skënderaga |
| SECURITY AND PROTECTION DEPARTMENT | - |
| PRINTING HOUSE | Alfons Theka |

BRANCHES

| | |
|-------------|-----------------|
| SHKODRA | Ermira Istrefi |
| ELBASANI | Valentina Dedja |
| GJIROKASTRA | Anila Thomaj |
| KORÇA | Liljana Zjarri |
| LUSHNJA | Shpresa Meço |

LIST OF ALL ENTITIES LICENSED BY THE BANK OF ALBANIA*

BANKS AND BRANCHES OF FOREIGN BANKS

1. ITALIAN - ALBANIAN BANK (JOINT-STOCK COMPANY)

Licence No. 1/1996, dated 17.07.1998

Approved by the Supervisory Council Decision of the Bank of Albania No. 89, dated 18.06.1998.

Certificate No. 1 "On Deposit Insurance".

Director: Luigi MASTRAPASQUA
Address: Rruga "Barrikadave", Nr. 70, Tirana, Albania
Tel.: 23 39 65, 23 56 97, 23 56 98, 22 62 62
Fax.: 23 30 34

2. RAIFFEISEN BANK (JOINT-STOCK COMPANY)

Licence No. 2/1998, dated 11.01.1999

Approved by the Supervisory Council Decision of the Bank of Albania No. 163, dated 11.12.1998.

Certificate No. 2 "On Deposit Insurance".

Director: Steven GRUNERUD
Address: Bulevardi "Bajram Curri", European Trade Center, Tirana, Albania
Tel.: 22 66 99, 22 45 40, 22 26 69, 22 54 16
Fax.: 27 55 99, 22 35 87, 22 36 95, 22 40 51

3. UNITED BANK OF ALBANIA (JOINT-STOCK COMPANY)

Licence No. 3/1998, dated 11.01.1999

Approved by the Supervisory Council Decision of the Bank of Albania No. 165, dated 11.12.1998.

Certificate No. 3 "On Deposit Insurance".

Director: Abdul Waheed ALAVI
Address: Bulevardi "Dëshmorët e Kombit", Nr. 8, Tirana, Albania
Tel.: 22 84 60, 22 38 73, 22 74 08
Fax: 22 84 60, 22 83 87

4. ITALIAN BANK OF DEVELOPMENT (BANCA ITALIANA DI SVILUPPO) (FORMER DARDANIA BANK)

Licence No. 5/1998, dated 11.01.1999

Approved by the Supervisory Council Decision of the Bank of Albania No. 164, dated 11.12.1998. Certificate No. 4 "On Deposit Insurance".

Director: Libero CATALANO
Address: Bulevardi "Dëshmorët e Kombit", Ndërtesa Kullat Binjake, Tirana
Tel.: 28 03 51 / 2 / 3 / 4 / 5.
Fax: 28 03 56.

5. NATIONAL COMMERCIAL BANK (JOINT-STOCK COMPANY)

Licence No. 6/1998, dated 11.01.1999

Approved by the Supervisory Council Decision of the Bank of Albania No. 162, dated 11.01.1999.

Certificate No. 5 "On Deposit Insurance".

Director: Seyhan PENCAPLIGIL
Address: Bulevardi "Zhan D'Ark", Tirana, Albania
Tel.: 25 09 55
Fax.: 25 09 56

* Up to June 30, 2007.

6. TIRANA BANK (JOINT-STOCK COMPANY)

Licence No. 07, dated 12.09.1996

Approved by the Supervisory Council Decision of the Bank of Albania No. 9, dated 12.09.1996.

Certificate No. 6 "On Deposit Insurance".

Director: Dimitrios FRANGETIS

Address: Bulevardi "Zogu I", Nr. 55/1, Tirana, Albania

Tel.: 23 34 41/42/ 43/44/45/46/47

Fax.: 23 34 17

7. NATIONAL BANK OF GREECE (JOINT-STOCK COMPANY) – TIRANA BRANCH

Licence No. 08, dated 25.11.1996

Approved by the Supervisory Council Decision of the Bank of Albania No. 4, dated 14.03.1996.

Certificate No. 7 "On Deposit Insurance".

Director: Spiro BRUMBULLI

Address: Rruga "Durrësit", Godina Comfort, Tirana, Albania

Tel.: 27 48 02; 27 48 22

Fax.: 23 36 13

8. INTERNATIONAL COMMERCIAL BANK (JOINT-STOCK COMPANY)

Licence No.09, dated 20.02.1997

Approved by the Supervisory Council Decision of the Bank of Albania No. 9, dated 30.04.1996.

Certificate No. 8 "On Deposit Insurance".

Director: Mahendra Sing RAWAT

Address: Qendra e Biznesit, Rruga "Murat Toptani", Tirana, Albania

Tel.: 25 43 72 / 25 62 54

Tel/Fax: 25 43 68

9. ALPHA BANK (JOINT-STOCK COMPANY) – ALBANIA

Licence No.10, dated 07.01.1998

Approved by the Supervisory Council Decision of the Bank of Albania No. 01/03/96, dated 27.12.1997.

Certificate No. 9 "On Deposit Insurance".

Director: Andreas GALATOULAS

Address: Bulevardi "Zogu I", Nr.47, Tirana, Albania

Tel.: 23 33 59, 24 04 76/77/78

Tel/Fax: 23 21 02

10. AMERICAN BANK OF ALBANIA (JOINT-STOCK COMPANY)

Licence No.11, dated 10.08.1998

Approved by the Supervisory Council Decision of the Bank of Albania No. 105, dated 10.08.1998.

Certificate No. 10 "On Deposit Insurance".

Director: Lorenzo RONCARI

Address: Rruga "Ismail Qemali", Nr. 27, P.O. Box 8319, Tirana, Albania

Tel.: 27 60 00 / 24 87 53 / 4 / 5 / 6

Tel/Fax: 24 87 62

11. PROCREDIT BANK (JOINT-STOCK COMPANY)

Licence No. 12, dated 15.03.1999

Approved by the Supervisory Council Decision of the Bank of Albania No. 22, dated 03.03.1999.

Certificate No. 11 "On Deposit Insurance".

Director: Frieder WOEHRMANN

Address: Rruga "Sami Frashëri", Tirana e Re, P.O. Box. 2395, Tirana, Albania

Tel.: 27 12 72 / 3 / 4 / 5

Tel/Fax: 27 12 76

12. FIRST INVESTMENT BANK (JOINT-STOCK COMPANY) - TIRANA BRANCH

Licence No. 13, dated 16.04.1999

Approved by the Supervisory Council Decision of the Bank of Albania No. 45, dated 13.04.1999.

Certificate No. 12 "On Deposit Insurance".

Director: Svetoslav MOLDOVANSKY
Address: Bulevardi "Zogu I", Nr. 64, Tirana, Albania
Tel.: 25 64 23, 25 64 24
Tel/Fax: 25 64 22

13. EMPORIKI BANK OF ALBANIA (JOINT-STOCK COMPANY)

Licence No. 14, dated 28.10.1999

Approved by the Supervisory Council Decision of the Bank of Albania No.105, dated 19.10.1999.

Certificate No. 13 "On Deposit Insurance".

Director: George CARACOSTAS
Address: Rruga "Kavajës", Tirana Tower, Tirana, Albania
Tel.: 25 87 55/ 56/ 57/ 58/ 59/ 60
Tel/Fax: 25 87 52

14. CREDIT BANK OF ALBANIA (JOINT-STOCK COMPANY)

Licence No. 15, dated 28.08.2002

Approved by the Supervisory Council Decision of the Bank of Albania No. 66, dated 28.08.2002.

Certificate No. 14 "On Deposit Insurance".

Director: Kamal Abdel MONEIM
Address: Rruga "Perlat Rexhepi", Al-Kharafi Group Administration Building, Kati 1&2" Tirana, Albania
Tel.: 27 21 68, 27 21 62
Tel/Fax: 27 21 62

15. CREDINS BANK (JOINT-STOCK COMPANY)

Licence No. 16, dated 31.03.2003

Approved by the Supervisory Council Decision of the Bank of Albania No. 22, dated 26.03.2003.

Certificate No.15 "On Deposit Insurance".

Director: Artan SANTO
Address: Rruga "Ismail Qemali", Nr. 21, Tirana, Albania
Tel.: 22 29 16, 23 40 96

16. POPULAR BANK (JOINT-STOCK COMPANY)

Licence No. 17, dated 16.02.2004

Approved by the Supervisory Council Decision of the Bank of Albania No. 06, dated 11.02.2004.

Certificate No.16 "On Deposit Insurance".

Director: Edvin LIBOHOVA
Address: Rruga "Donika Kastrioti", Pall. 11/1, Kati I, Tirana, Albania
Tel.: 27 27 88 / 89 / 90 / 91
Fax: 27 27 81

17. UNION BANK (JOINT-STOCK COMPANY)

Licence No. 18, dated 09.01.2006

Approved by the Supervisory Council Decision of the Bank of Albania No. 101, dated 28.12.2005.

Certificate No.17 "On Deposit Insurance".

Director: Gazmend KADRIU
Address: Bulevardi "Zogu I", Pallati 13-katësh, përballë Stacionit të Trenit, Tirana.
Tel: 25 06 53
Fax: 25 06 54

NON-BANK INSTITUTIONS

1. TIRANA FINANCIAL UNION S.R.L. (WESTERN UNION)

Licence No. 1, dated 08.12.1999, on conducting the following financial activities:

- offering payment services;
- mediating in the conduct of monetary transactions;
- acting as financial agent or advisor.

Director: Niko Leka, Edmond Leka

Address: Rruga "Reshit Çollaku", Pallati Shallvare, Sh 2, Nr. 18, Tirana, Albania

Tel.: 25 06 53

Fax: 25 06 54

2. ALBANIAN POST-OFFICE (JOINT STOCK COMPANY)

Licence No. 3, dated 18.04.2001, as a non-bank financial institution to conduct the following financial activities:

- offering payment services;
- acting as financial agent or advisor.

Director: Arqile Goreja

Address: Rruga "Reshit Çollaku", Nr. 4, Tirana, Albania

Tel.: 22 23 15

3. CREDINS TIRANA (JOINT STOCK COMPANY)

Licence No. 04, dated 13.06.2001, as a non-bank financial institution to conduct the following financial activities:

- granting credit;
- offering payment services;;
- mediating in the conduct of monetary transactions (foreign currency included);
- offering guarantees;
- acting as financial agent or advisor (excluding herein the services set forth in point 3/a and 3/b of Article 26 of the Law "On Banking Law in the Republic of Albania".

Director: Elion Martini

Address: Rruga "Dëshmorët e 4 Shkurtit", Tirana, Albania

Tel.: 22 29 16, 23 40 96

4. MOUNTAINOUS AREA FINANCING FUND

Licence No. 5, dated 29. 03.2002, on conducting the following activity:

- granting credit.

Director: Bajram Korsita

Address: Rruga "Dervish Hima" Nr. 4, Tirana, Albania

Tel.: 25 90 80/1

Fax: 25 06 33

5. AK-INVEST (JOINT STOCK COMPANY)

Licence No.7, dated 31.12.2003, as a non-bank financial institution to conduct the following activities:

- offering payment services;
- mediating in the conduct of monetary transactions (foreign currency included);
- acting as financial agent or advisor.

Manager: Ilir Adili

Address: Rruga "Ded Gjon Luli", Nr. 2/3, Tirana, Albania

Tel.: 24 01 47

FOREIGN EXCHANGE BUREAUS

1. "JOARD" FOREIGN EXCHANGE BUREAU S.R.L., TIRANA
Licence: No. 1, dated 01.10.1999
Address: Rruga "Ded Gjon Luli", Nr.2, Tirana, Albania
Brokers: Josif Kote, Pajtim Kodra
2. "AMA" FOREIGN EXCHANGE BUREAU S.R.L., DURRËS
Licence: No. 2, dated 01.10.1999
Address: Rruga "Tregtare", Lagja 3, Durrës, Albania
Brokers: Mirlinda Ceka, Ilir Hoxha
3. "ARIS" FOREIGN EXCHANGE BUREAU S.R.L., TIRANA
Licence: No. 3, dated 01.10.1999
Address: Rruga "Luigj Gurakuqi", Tirana, Albania
Brokers: Ardian Goci, Ismet Noka
4. "UNIONI FINANCIAR" FOREIGN EXCHANGE BUREAU S.R.L., TIRANA
Licence: No. 4, dated 01.10.1999
Address: Rruga "Reshit Çollaku", Pallati Shallvare, Shk. 2/18, Tirana, Albania
Manager: Niko Leka
Brokers: Arjan Lezha (Manager), Albert Sara, Dhimitër Papadhopulli, Genta Angjeli (Agalliu), Piro Teti, Flora Simixhi, Petrika Mano (Manager), Lindita Shala, Mirela Bakalli, Anila Demiri, Emili Bakalli (Nako), Astrit Sferdelli, Mirela Kaiku, Erisa Emiri
5. "AGLI" FOREIGN EXCHANGE BUREAU S.R.L., TIRANA
Licence: No. 5, dated 01.10.1999
Address: Office No.1: Rruga "Islam Alla", Nr.1, Tirana, Albania
Office No.2: Rruga "Kavajës", Tirana, Albania
Brokers: Kujtim Nina (Manager), Agim Cani, Selim Luli
6. "EXCHANGE" FOREIGN EXCHANGE BUREAU S.R.L., TIRANA
Licence: No. 08, dated 24.11.1999
Address: Rruga "Durrësit", Nr. 170, Tirana, Albania
Brokers: Ivan Pavlovski, Ervis Myftari
7. "UNISIX" FOREIGN EXCHANGE BUREAU S.R.L., KORÇA
Licence: No. 09, dated 26.11.1999
Address: Bulevardi "Republika", Pallati 4, Korça, Albania
Brokers: Pandi Cunoti, Ernest Golka, Nikolin Bicka, Eli Bode
8. "ILIRIA 98" FOREIGN EXCHANGE BUREAU S.R.L., TIRANA
Licence: No. 12, dated 25.02.2000
Address: Sheshi "Skënderbej", Teatri i Kukullave, Tirana, Albania
Brokers: Edmond Ymeri, Ali Topalli, Ilir Janku
9. "SERXHIO" FOREIGN EXCHANGE BUREAU S.R.L., ELBASAN
Licence: No. 14, dated 07.04.2000
Address: Lagja "Luigj Gurakuqi", Rruga "11 Nëntori", Pallati 70, Nr.14, Elbasan, Albania
Brokers: Amarildo Canoku
10. "ALBTUR" FOREIGN EXCHANGE BUREAU S.R.L., TIRANA
Licence: No. 15, dated 07.04.2000
Address: Bulevardi "Zogu I", Pallati 32, Shk.1, Tirana, Albania
Brokers: Albert Rahmani, Artur Rahmani
11. "R & M" FOREIGN EXCHANGE BUREAU S.R.L., TIRANA
Licence: No. 16, dated 22.05.2000
Address: Rruga "Punëtorët e Rilindjes", Pallati 182, Tirana, Albania
Brokers: Edmond Stepa, Miranda Stepa

12. "T & E" FOREIGN EXCHANGE BUREAU S.R.L., DURRËS

Licence: No. 18, dated 11.06.2000
Address: Lagja 4, Rruga "9 Maji", Durrës, Albania
Broker: Shpëtim Hysa

13. "SHIJAK 2000" FOREIGN EXCHANGE BUREAU S.R.L., SHIJAK

Licence: No. 19, dated 24.11.2000
Address: Lagja "Popullore", Shijak, Albania
Brokers: Nazmi Ademi, Farije Ademi

14. "MANUSHI" FOREIGN EXCHANGE BUREAU S.R.L., TIRANA

Licence: No. 22, dated 18.04.2001
Address: Bulevardi "Zogu I", VEVE Business Center, Tirana, Albania
Brokers: Roland Manushi

15. "UNIONI SELVIA" FOREIGN EXCHANGE BUREAU S.R.L., TIRANA

Licence: No. 23, dated 21.05.2001
Address: Rruga "Sami Frashëri", Pallati 11, Shk.4, Ap.29, Tirana, Albania
Brokers: Denis Merepeza (manager)

16. "KALENJA" FOREIGN EXCHANGE BUREAU S.R.L., TIRANA

Licence: No. 24, dated 29.06.2001
Address: Rruga "Kavajës" (next to Turkish Embassy), Tirana, Albania
Brokers: Hair Shametaj, Rudina Shametaj

17. "TILBA" FOREIGN EXCHANGE BUREAU S.R.L., ELBASAN

Licence: No. 25, dated 30.09.2001
Address: Lagja "Kongresi i Elbasanit", Bulevardi "Qemal Stafa", Pallati 19, Elbasan, Albania
Brokers: Kristaq Bako, Vjollca Bako

18. "ANAGNOSTI" FOREIGN EXCHANGE BUREAU S.R.L., TIRANA

Licence: No. 26, dated 31.10.2001
Address: Office No. 1 - Bulevardi "Zogu I", Pallati 97, Shk.3, Ap.28, Tirana, Albania
Brokers: Jani Anagnosti, Odise Anagnosti, Edlira Anagnosti
Office No. 2 - Rruga "Kajo Karafili", Nr. 11, Tirana, Albania
Broker: Fredi Cami

19. "KO-GO" FOREIGN EXCHANGE BUREAU S.R.L., TIRANA

Licence: No. 27, dated 12.11.2001
Address: Rruga "Vaso Pasha", Pallati 16, Shk.2, Ap. 9, Tirana, Albania
Brokers: Mihal Konomi, Përparim Goxhaj

20. "ALB-FOREX" FOREIGN EXCHANGE BUREAU S.R.L., TIRANA

Licence: No. 28, dated 22.11.2001
Address: Office No. 1: Rruga "Abdyl Frashëri", Nr.3, Tirana, Albania
Brokers: Mirel Topçiu
Office No. 2: Bulevardi "Zogu I", ish-Pallati i Kulturës "Ali Kelmendi", Kati I, Tirana, Albania
Broker: Melsi Çami

21. "L&N" FOREIGN EXCHANGE BUREAU S.R.L., TIRANA

Licence: No. 29, dated 22.11.2001
Address: Office No.1: Rruga "Muhamet Gjollështa", Tirana, Albania
Broker: Leonora Mihalcka
Office No.2: Rruga "Dëshmorët e 4 Shkurtit", Pallati i Shallvareve, Shk.7, Kati përdhe, Tirana, Albania
Broker: Myzafer Velaj, Dashurije Rumbullaku

22. "EXCHANGE ALOG" FOREIGN EXCHANGE BUREAU S.R.L., TIRANA

Licence: No. 31, dated 22.11.2001
Address: Rruga "Mine Peza", Tirana, Albania

Brokers: Almida Sterio, Fatmir Tafaj, Eduard Andoni, Elida Hasamemi

23. "BASHKIMI 2001" FOREIGN EXCHANGE BUREAU S.R.L., TIRANA

Licence: No. 35, dated 12.12.2001

Address: Rruga "Kavajës", Tirana, Albania

Brokers: Bashkim Shametaj, Luan Shametaj, Ilir Mesini

24. "ARJON 2002" FOREIGN EXCHANGE BUREAU S.R.L., ELBASAN

Licence: No. 36, dated 14.12.2001

Address: Lagja "Kongresi i Elbasanit", Bulevardi "Qemal Stafa", Pallati 9-katësh, Elbasan, Albania

Brokers: Arben Kovaçi, Besnik Lulja, Alfred Kapxhi

25. "ALAKTH" FOREIGN EXCHANGE BUREAU S.R.L., TIRANA

Licence: No. 42, dated 18.01.2002

Address: Rruga "Dibrës", Nr.105/1, Tirana, Albania

Brokers: Kosta Papa, Arben Memko, Lorenc Konomi, Thoma Konomi, Aleko Plaku

26. "FORMAT" FOREIGN EXCHANGE BUREAU S.R.L., TIRANA

Licence: No. 43, dated 21.01.2002

Address: Rruga "Durrësit", Pallati 85, Shk. 1, Ap. 1, Tirana, Albania

Brokers: Diana Lemi, Egon Sinani

27. "TRI URAT" FOREIGN EXCHANGE BUREAU S.R.L., ELBASAN

Licence: No. 44, dated 05.02.2002

Address: Lagja "29 Nëntori", Elbasan, Albania

Brokers: Fahri Sanco, Ismail Bejta

28. "BESA 2001" FOREIGN EXCHANGE BUREAU S.R.L., TIRANA

Licence: No. 46, dated 15.02.2002

Address: Rruga "Myslym Shyri", Nr. 25, Tirana, Albania

Brokers: Belul Lleshi, Vladimir Avda, Mimoza Avda

29. "MARIO" FOREIGN EXCHANGE BUREAU S.R.L., SARANDA

Licence: No. 47, dated 14.03.2002

Address: Lagja 1, Saranda, Albania

Brokers: Vangjel Gramozi, Blerim Dhima

30. "DROGU" FOREIGN EXCHANGE BUREAU S.R.L., TIRANA

Licence: No. 49, dated 23.04.2002

Address: Rruga "Vaso Pasha", Kulla 1, Kati I, Tirana, Albania

Brokers: Shkëlqim Drogu, Kostandin Koteci

31. "HYSEN-C" FOREIGN EXCHANGE BUREAU S.R.L., LAÇ

Licence: No. 50, dated 23.04.2002

Address: Lagja Nr. 3, Laç, Albania

Broker: Cen Hyseni, Violeta Hyseni, Miranda Palaj, Albana Zhuzhi, Jonida Thanasi

32. "TAXI EKSPRES" FOREIGN EXCHANGE BUREAU S.R.L., TIRANA

Licence: No. 52, dated 20.05.2002

Address: Office No.1: Rruga "Sami Frashëri", nr. 11 (pranë shkollës "Edith Durham", Tirana, Albania

Office No.2: Bulevardi "Bajram Curri", Rruga "Lekë Dukagjini", No.5, Tirana, Albania

Brokers: Arben Sharra, Sokol Kaleci, Brikena Tole, Manjola Kume, Elona Zyra

33. "GLEAR" FOREIGN EXCHANGE BUREAU S.R.L., SHIJAK

Licence: No. 55, dated 23.07.2002

Address: Lagja "Kodër", Shijak, Durrës, Albania

Brokers: Argjend Calliku, Afërdita Calliku

34. "ALBA-POST" FOREIGN EXCHANGE BUREAU, TIRANA

Licence: No. 56, dated 28.08.2002

Address: Rruga "Reshit Çollaku", Nr. 4, Tirana, Albania

35. "ESLULI" FOREIGN EXCHANGE BUREAU S.R.L , TIRANA

Licence: No. 58, dated 17.10.2002.

Address: Rruga "Reshit Çollaku", Pallati "Shallvare", Shk. 4/1, Tirana, Albania

Brokers: Selim Luli, Kleomen Gjikhuri

36. "DENI&KRISTI-2002" FOREIGN EXCHANGE BUREAU S.R.L., TIRANA

Licence: No. 61, dated 02.06.2003

Address: Rruga "Myslym Shyri", Pallati 60, Ap. 3, Tirana, Albania

Broker: Maksim Çeku

37. "YLDON" FOREIGN EXCHANGE BUREAU S.R.L., TIRANA

Licence: No. 62, dated 03.06.2003

Address: Office No.1: Rruga "Qemal Stafa", Pallati 382/2/2, Tirana, Albania
Office No.2: Bulevardi "Bajram Curri", European Trade Center,
Tirana, Albania

Broker: Ylli Ndoqi (manager), Sabit Lika, Enkeleda Selamaj, Suela Marku,
Imelda Ahmeti

38. "I.S.N." FOREIGN EXCHANGE BUREAU S.R.L., TIRANA

Licence: No. 66, dated 06.05.2004

Address: Rruga "Kavajës", Pallati 3, Kati I, Tirana, Albania

Brokers: Nexhmi Uka, Salandi Brojaj

39. "ARIABA" FOREIGN EXCHANGE BUREAU S.R.L., TIRANA

Licence: No. 67, dated 07.06.2004

Address: Rruga "Abdyl Frashëri", Kati I, Shk. 5, Tirana, Albania

Brokers: Agim Xhemo (manager), Astrit Hado, Flamur Denaj

40. "ALBACREDITS" FOREIGN EXCHANGE BUREAU S.R.L., TIRANA

Licence: No. 68, dated 13.07.2004

Address: Rruga "Ded Gjon Luli", Nr. 5, Tirana, Albania

Brokers: Ermira Skënderi (manager), Engjëll Skënderi, Burhan Kodra

41. "ALB-KREDIT" FOREIGN EXCHANGE BUREAU S.R.L., TIRANA

Licence: No.69, dated 19.07.2004

Address: Office No.1: Rruga "Durrësit", Nr. 2, Tirana, Albania

Brokers: Arben Cani (manager), Vasil Marto, Rudina Muskaj, Valbona
Kadriu, Teuta Koltarka, Hajredin Toca, Doloreza Arapi.

Office No.2: Dega Peshkopi, Bulevardi "Nazmi Rushiti", Peshkopi,
Dibër

Brokers: Xhetan Krashi, Dritan Lala

42. "OMEGA" FOREIGN EXCHANGE BUREAU S.R.L., TIRANA

Licence: No. 72, dated 20.12.2004.

Address: Rruga "Abdyl Frashëri", Pallati 1, Shk.2, Ap.10, Tirana

Broker: Mihallaq Peko (manager), Ylli Meshau

43. "ELBA 2005" FOREIGN EXCHANGE BUREAU S.R.L., TIRANA

Licence: No.73, dated 28.04.2005

Address: Bulevardi "Bajram Curri", Pallatet Agimi, Nr.16, Tirana

Brokers: Kujtim Elbasani (manager)

44. "JONADA – 05" FOREIGN EXCHANGE BUREAU S.R.L., TIRANA

Licence: No. 74, dated 27.06.2005

Address: Rruga "Kavajës", Pallati 185, Shkalla 2, Ap. 9, Tirana, Albania

Brokers: Liliana Zyfi (manager), Pëllumb Zyfi

45. "BASHA – N.B." FOREIGN EXCHANGE BUREAU S.R.L., ELBASAN

Licence: No. 75, dated 08.07.2005

Address: Lagja "Shënkoll", Rruga "Thoma Kaleshi", Pallati 110, Shk.1, Kati I, Elbasan, Albania
Brokers: Nashifer Basha, Çlirim Basha

46. "I & K 2005" FOREIGN EXCHANGE BUREAU S.R.L., LEZHE

Licence: No.77, dated 09.09.2005
Address: Lagja "Besëlidhja", Pallati 73, Lezhë, Albania
Brokers: Ilir Malaj

47. "EUROTOURS" FOREIGN EXCHANGE BUREAU S.R.L., TIRANA

Licence: No.78, dated 17.10.2005
Address: Rruga "Reshit Çollaku", Nr. 2/18, Pallatet Shallvare, Tirana, Albania
Brokers: Albert Cara, Ilir Stafa, Dhimitër Papadhopuli

48. "A.B.I." FOREIGN EXCHANGE BUREAU S.R.L., TIRANA

Licence: No.79, dated 17.02.2006
Address: Bulevardi Zog I, Godina "Zëri i Popullit", Tirana, Albania
Brokers: Ilir Doçi, Suela Dedaj

49. "REGENCY INTERNATIONAL CASINO TIRANA" FOREIGN EXCHANGE BUREAU S.R.L., TIRANA

Licence: No.80, dated 06.03.2006
Address: Rruga "Dëshmorët e 4 Shkurtit", Parku Rinia, Tirana, Albania
Brokers: Florjan Lami, Suzana Aliu, Aides Goga, Murat Haruni, Gjergji Selala, Marsela Elmazaj, Vjollca Nurka, Leonard Gjonaç, Elvis Marku, Donald Mihal, Albana Sherifi, Armand Çadra, Ermelind Hystuna, Elis Nerguti, Nikolla Prifti, Aurela Shota, Razie Selimi, Valbona Halili, Kostandina Mejdi, Elona Martiro.

50. "ARBËR F" FOREIGN EXCHANGE BUREAU S.R.L., TIRANA

Licence: No.81, dated 07.03.2006
Address: Rruga "Kavajës", Pallati 3, Kati I (ish-Guden), Tirana, Albania
Brokers: Florina Jaho, Bukurosh Jaho

51. "EURO 2006" FOREIGN EXCHANGE BUREAU S.R.L., Durrës

Licence: No.82, dated 12.04.2006
Address: Lagjia nr.4, Rruga "Migjeni", pranë Poliklinikës Qendrore, Durrës, Albania
Brokers: Hysni Baganaçi, Medi Dyrmishi

52. "VOSKOP" FOREIGN EXCHANGE BUREAU S.R.L., KORÇA

Licence: No.83, dated 13.04.2006
Address: Lagjia nr.7, Blloku "8 Nëntori", Korça, Albania
Brokers: Anesti Leska, Rexhep Mankolli

53. "KRISTIAN 2002" FOREIGN EXCHANGE BUREAU S.R.L., LEZHA

Licence: No.84, dated 31.05.2006
Address: Lagjia "Besëlidhja", përballë Degës së Bankës "Raiffeisen", Lezha Albania
Brokers: Sander Marashi

54. "PRE-LAND" FOREIGN EXCHANGE BUREAU S.R.L., LEZHA

Licence: No.85, dated 31.05.2006
Address: Lagja "Skënderbej", ish-lokali "Gjahtari", Lezha, Albania
Brokers: Roland Kola

55. "SHQIPONJA VI" FOREIGN EXCHANGE BUREAU S.R.L., VLORA

Licence: No.86, dated 16.06.2006
Address: Pallati i Kulturës "Labëria", përballë portit detar, Vlora, Albania
Brokers: Vjollca Musaraj

56. "BONVOYAGE" FOREIGN EXCHANGE BUREAU S.R.L., Durrës

Licence: No.87, dated 20.06.2006
Address: Lagja 11, Bulevardi kryesor "Durrahu", Ap.243, Durrës, Albania
Brokers: Petrit Shtaro; Jusuf Milaqi

57. "ANICHRI" FOREIGN EXCHANGE BUREAU S.R.L., TIRANA

Licence: Nr. 88, datë 20.04.2007.
Address: Rr. "Vaso Pasha" Nr. 10, Përballë Bar "Rovena"(ish-blloku) Tirana.
Brokers: Ilir Gurashi, Lenije Murataj, Juliana Hajro.

58. "BROQI" FOREIGN EXCHANGE BUREAU S.R.L., TIRANA

Licence: Nr. 89, datë 20.04.2007.
Address: Rruga "Kavajës", përballë Kishës Katolike, Tirana
Brokers: Nikollë Broqi, Dhurata Murrizi.

59. "HENRY" FOREIGN EXCHANGE BUREAU S.R.L., ELBASAN

Licence: Nr. 90, datë 19.06.2007.
Address: Lagja "28 Nëntori", pranë Hotel "Skampa", Elbasan
Brokers: Albert Buzo, Sotirag Buzo.

60. "KOMPLEKSI TURISTIK RABOSHTA" FOREIGN EXCHANGE BUREAU S.R.L., SHKODËR

Licence: Nr. 91, datë 26.06.2007.
Address: Lagja "Vasil Shanto", përballë xhamisë, Shkodër
Brokers: Përparim Raboshta, Jetmira Raboshta.

61. "ÇELA 2005" FOREIGN EXCHANGE BUREAU S.R.L., LUSHNJE

Licence: Nr. 92, datë 26.06.2007.
Address: Lagja "Çlirim", Lushnje.
Brokers: Bledar Çela, Mondi Cejne.

62. "ARTUR 07" FOREIGN EXCHANGE BUREAU S.R.L., FIER

Licence: Nr. 93, datë 26.06.2007.
Address: Rr "Esat Dishnica" Nr.9, Fier.
Brokers: Artur Beqo.

63. "PACILI&GJIRITI" FOREIGN EXCHANGE BUREAU S.R.L., KORÇË

Licence: Nr. 94, datë 06.07.2007.
Address: Bulevardi "Edith Durham", pranë Hotel "Turizmit", Korçë
Brokers: Dylber Gjiriti, Jorgaq Pacili.

UNIONS OF SAVINGS AND CREDIT ASSOCIATIONS

1. "JEHONA" SAVINGS AND CREDIT ASSOCIATIONS UNION, TIRANA

Licence: No. 1, dated 27.06.2002

Address: Rruga "Kajo Karafili", Nr. 26/1, Tirana, Albania

Head of the Executive Board: Vojsava Rama

2. "ALBANIAN SAVINGS AND CREDIT UNION" SAVINGS AND CREDIT ASSOCIATIONS UNION, TIRANA

Licence: No. 2, dated 09.08.2002

Address: "Zayed Business Center" Rruga "Sulejman Delvina", Tiranë e Re,
Tirana, Albania

Head of the Executive Board: Zana Konini

SAVINGS AND CREDIT ASSOCIATIONS

1. "MËSUESI" SAVINGS AND CREDIT ASSOCIATION, TIRANË

Licence No. 1, dated 01.07.2002

Member of "JEHONA" SCA Union

2. "RIZGJIMI" SAVINGS AND CREDIT ASSOCIATION, TIRANË

Licence No. 2, dated 01.07.2002

Member of "JEHONA" SCA Union

3. "AFADA " SAVINGS AND CREDIT ASSOCIATION, TIRANË

Licence No. 3, dated 01.07.2002

Member of "JEHONA" SCA Union

4. "BLETËRRITËSIT " SAVINGS AND CREDIT ASSOCIATION, KORÇË

Licence No 5, dated 01.07.2002

Member of "JEHONA" SCA Union

5. "BREGAS " SAVINGS AND CREDIT ASSOCIATION, KORÇË

Licence No. 6, dated 01.07.2002

Member of "JEHONA" SCA Union

6. "FITORJA" SAVINGS AND CREDIT ASSOCIATION, PRRENJAS

Licence No. 12, dated 01.07.2002

Member of "JEHONA" SCA Union

7. "GRAMSHI" SAVINGS AND CREDIT ASSOCIATION, LUSHNJË

Licence No. 13, dated 01.07.2002

Member of "JEHONA" SCA Union

8. "HABA" SAVINGS AND CREDIT ASSOCIATION, TIRANË

Licence No. 14, dated 01.07.2002

Member of "JEHONA" SCA Union

9. "KANDAVIA" SAVINGS AND CREDIT ASSOCIATION, LIBRAZHD

Licence No. 15, dated 01.07.2002

Member of "Jehona" SCA Union

10. "KORÇARJA" SAVINGS AND CREDIT ASSOCIATION, KORÇË

Licence No. 17, dated 01.07.2002

Member of "Jehona" SCA Union

11. "KRUJA" SAVINGS AND CREDIT ASSOCIATION, KRUJË

Licence No. 18, dated 01.07.2002

Member of "Jehona" SCA Union

12. "METAJ" SAVINGS AND CREDIT ASSOCIATION, FIER

Licence No. 20, dated 01.07.2002.

Member of "Jehona" SCA Union

13. "ORIK" SAVINGS AND CREDIT ASSOCIATION, VLORE

Licence No. 21, dated 01.07.2002

Member of "Jehona" SCA Union

14. "PIRG" SAVINGS AND CREDIT ASSOCIATION, KORÇË

Licence No. 22, dated 01.07.2002

Member of "Jehona" SCA Union

15. "RINGJALLJA" SAVINGS AND CREDIT ASSOCIATION, VLORE

Licence No. 24, dated 01.07.2002

Member of "Jehona" SCA Union

16. "SHËNDETI" SAVINGS AND CREDIT ASSOCIATION, TIRANË

Licence No. 25, dated 01.07.2002

Member of "Jehona" SCA Union

17. "SHKËNDIJA" SAVINGS AND CREDIT ASSOCIATION, ELBASAN

Licence No. 26, dated 01.07.2002

Member of "Jehona" SCA Union

18. "STROPSKA" SAVINGS AND CREDIT ASSOCIATION, POGRADEC

Licence No. 29, dated 01.07.2002

Member of "Jehona" SCA Union

19. "SYNEI" SAVINGS AND CREDIT ASSOCIATION, KAVAJË

Licence No. 30, dated 01.07.2002

Member of "Jehona" SCA Union

20. "TEUTA" SAVINGS AND CREDIT ASSOCIATION, DURRËS

Licence No. 31, dated 01.07.2002

Member of "Jehona" SCA Union

21. "URA E KUÇIT" SAVINGS AND CREDIT ASSOCIATION, BERAT

Licence No. 32, dated 01.07.2002

Member of "Jehona" SCA Union

22. "VOLOREKA" SAVINGS AND CREDIT ASSOCIATION, POGRADEC

Licence No. 33, dated 01.07.2002

Member of "Jehona" SCA Union

23. "YLLI I KUQ" SAVINGS AND CREDIT ASSOCIATION, KORÇË

Licence No. 34, dated 01.07.2002

Member of "Jehona" SCA Union

24. "VELÇE" SAVINGS AND CREDIT ASSOCIATION, VLORE

Licence No. 36, dated 29.08.2002

Member of "Albanian Savings and Credit Union" SCA Union

25. "KALLM" SAVINGS AND CREDIT ASSOCIATION, FIER

Licence No. 37, dated 29.08.2002

Member of "Albanian Savings and Credit Union" SCA Union

26. "KURORA E ELBASANIT" SAVINGS AND CREDIT ASSOCIATION, ELBASAN
(CHANGED FROM "BANJE E SIPERME")

Licence No. 39, dated 29.08.2002

Member of "Albanian Savings and Credit Union" SCA Union

27. "MOLLAS" SAVINGS AND CREDIT ASSOCIATION, ELBASAN

Licence No. 40, dated 29.08.2002

Member of "Albanian Savings and Credit Union" SCA Union

28. "PASHTRESH" SAVINGS AND CREDIT ASSOCIATION, ELBASAN

Licence No. 41, dated 05.09.2002

Member of "Albanian Savings and Credit Union" SCA Union

29. "GJINAR" SAVINGS AND CREDIT ASSOCIATION, ELBASAN
Licence No. 42, dated 05.09.2002
Member of "Albanian Savings and Credit Union" SCA Union
30. "KUQAN" SAVINGS AND CREDIT ASSOCIATION, ELBASAN
Licence No. 45, dated 05.09.2002
Member of "Albanian Savings and Credit Union" SCA Union
31. "SHUSHICË" SAVINGS AND CREDIT ASSOCIATION, ELBASAN
Licence No. 46, dated 05.09.2002
Member of "Albanian Savings and Credit Union" SCA Union
32. "BESTROVË" SAVINGS AND CREDIT ASSOCIATION, ELBASAN
Licence No. 49, dated 05.09.2002
Member of "Albanian Savings and Credit Union" SCA Union
33. "SHALËS" SAVINGS AND CREDIT ASSOCIATION, ELBASAN
Licence No. 51, dated 05.09.2002
Member of "Albanian Savings and Credit Union" SCA Union
34. "OSHËTIMË" SAVINGS AND CREDIT ASSOCIATION, VLORE,
Licence No. 52 dated 23.09.2002
Member of "Albanian Savings and Credit Union" SCA Union
35. "BABICË E VOGËL" SAVINGS AND CREDIT ASSOCIATION, VLORE,
Licence No. 53 dated 23.09.2002
Member of "Albanian Savings and Credit Union" SCA Union
36. "NOVOSELË" SAVINGS AND CREDIT ASSOCIATION, VLORE,
Licence No. 54, dated 23.09.2002
Member of "Albanian Savings and Credit Union" SCA Union
37. "ROMANAT" SAVINGS AND CREDIT ASSOCIATION, DURRËS
Licence No. 55, dated 23.09.2002
Member of "Albanian Savings and Credit Union" SCA Union
38. "JUBE" SAVINGS AND CREDIT ASSOCIATION, DURRËS
Licence No. 56, dated 23.09.2002
Member of "Albanian Savings and Credit Union" SCA Union
39. "ARDENICË" SAVINGS AND CREDIT ASSOCIATION, LUSHNJE
Licence No. 58, dated 23.09.2002
Member of "Albanian Savings and Credit Union" SCA Union
40. "VAJKAN" SAVINGS AND CREDIT ASSOCIATION, FIER
Licence No. 54, dated 23.09.2002
Member of "Albanian Savings and Credit Union" SCA Union
41. "LLAKATUND" SAVINGS AND CREDIT ASSOCIATION, VLORE
Licence No. 60, dated 23.09.2002
Member of "Albanian Savings and Credit Union" SCA Union
42. "GRABIAN" SAVINGS AND CREDIT ASSOCIATION, VLORE
Licence No. 61, dated 23.09.2002
Member of "Albanian Savings and Credit Union" SCA Union

43. "MAZREK" SAVINGS AND CREDIT ASSOCIATION, TIRANË
Licence No. 62, dated 23.09.2002
Member of "Albanian Savings and Credit Union" SCA Union
44. "MUSTAFA KOÇAJ" SAVINGS AND CREDIT ASSOCIATION, TIRANË
Licence No. 63, dated 23.09.2002
Member of "Albanian Savings and Credit Union" SCA Union
45. "SHPAT ISUF MUÇAJ" SAVINGS AND CREDIT ASSOCIATION, TIRANË
Licence No. 64, dated 23.09.2002
Member of "Albanian Savings and Credit Union" SCA Union
46. "PINAR" SAVINGS AND CREDIT ASSOCIATION, TIRANË
Licence No. 65, dated 23.09.2002
Member of "Albanian Savings and Credit Union" SCA Union
47. "FUSHAS MUMAJËS" SAVINGS AND CREDIT ASSOCIATION, TIRANË
Licence No. 66, dated 23.09.2002
Member of "Albanian Savings and Credit Union" SCA Union
48. "QEHA" SAVINGS AND CREDIT ASSOCIATION, TIRANË
Licence No. 67, dated 23.09.2002
Member of "Albanian Savings and Credit Union" SCA Union
49. "DOBRESH" SAVINGS AND CREDIT ASSOCIATION, TIRANË
Licence No. 68, dated 23.09.2002
Member of "Albanian Savings and Credit Union" SCA Union
50. "SHILBATËR" SAVINGS AND CREDIT ASSOCIATION, TIRANË
Licence No. 69, dated 23.09.2002
Member of "Albanian Savings and Credit Union" SCA Union
51. "INIBA" SAVINGS AND CREDIT ASSOCIATION, TIRANË
Licence No. 71, dated 25.09.2002
Member of "Albanian Savings and Credit Union" SCA Union
52. "FUSHË-PREZË" SAVINGS AND CREDIT ASSOCIATION, TIRANË
Licence No. 72, dated 25.09.2002
Member of "Albanian Savings and Credit Union" SCA Union
53. "MËNIK" SAVINGS AND CREDIT ASSOCIATION, TIRANË
Licence No. 73, dated 25.09.2002
Member of "Albanian Savings and Credit Union" SCA Union
54. "MULLET" SAVINGS AND CREDIT ASSOCIATION, TIRANË
Licence No. 74, dated 25.09.2002
Member of "Albanian Savings and Credit Union" SCA Union
55. "ZALL-HERR" SAVINGS AND CREDIT ASSOCIATION, TIRANË
Licence No. 75, dated 25.09.2002
Member of "Albanian Savings and Credit Union" SCA Union
56. "BARËZEZ" SAVINGS AND CREDIT ASSOCIATION, TIRANË
Licence No. 76, dated 25.09.2002
Member of "Albanian Savings and Credit Union" SCA Union

57. "DAIAS" SAVINGS AND CREDIT ASSOCIATION, TIRANË
Licence No. 77, dated 25.09.2002
Member of "Albanian Savings and Credit Union" SCA Union
58. "PETRELË" SAVINGS AND CREDIT ASSOCIATION, TIRANË
Licence No. 78, dated 25.09.2002
Member of "Albanian Savings and Credit Union" SCA Union
59. "MANGULL" SAVINGS AND CREDIT ASSOCIATION, TIRANË
Licence No. 79, dated 25.09.2002
Member of "Albanian Savings and Credit Union" SCA Union
60. "PINET" SAVINGS AND CREDIT ASSOCIATION, TIRANË
Licence No. 80, dated 25.09.2002
Member of "Albanian Savings and Credit Union" SCA Union
61. "BERZHITË" SAVINGS AND CREDIT ASSOCIATION, TIRANË
Licence No. 81, dated 25.09.2002
Member of "Albanian Savings and Credit Union" SCA Union
62. "MARIKAJ" SAVINGS AND CREDIT ASSOCIATION, TIRANË
Licence No. 82, dated 25.09.2002
Member of "Albanian Savings and Credit Union" SCA Union
63. "ALLGJATË" SAVINGS AND CREDIT ASSOCIATION, TIRANË
Licence No. 83, dated 25.09.2002
Member of "Albanian Savings and Credit Union" SCA Union
64. "KAMÇISHT" SAVINGS AND CREDIT ASSOCIATION, LUSHNJE
Licence No. 84, dated 25.09.2002
Member of "Albanian Savings and Credit Union" SCA Union
65. "BUBULLIMË" SAVINGS AND CREDIT ASSOCIATION, LUSHNJE
Licence No. 85, dated 25.09.2002
Member of "Albanian Savings and Credit Union" SCA Union
66. "GORRE" SAVINGS AND CREDIT ASSOCIATION, LUSHNJE
Licence No. 87, dated 25.09.2002
Member of "Albanian Savings and Credit Union" SCA Union
67. "DRITHAS" SAVINGS AND CREDIT ASSOCIATION, VLORË,
Licence No. 88, dated 25.09.2002
Member of "Albanian Savings and Credit Union" SCA Union
68. "PALASË" SAVINGS AND CREDIT ASSOCIATION, VLORË
Licence No. 89, dated 07.10.2002
Member of "Albanian Savings and Credit Union" SCA Union
69. "MAMINAS" SAVINGS AND CREDIT ASSOCIATION, DURRËS
Licence No. 90, dated 07.10.2002
Member of "Albanian Savings and Credit Union" SCA Union
70. "RRAPËZ" SAVINGS AND CREDIT ASSOCIATION, LUSHNJE
Licence No. 91, dated 07.10.2002
Member of "Albanian Savings and Credit Union" SCA Union

71. "PANAJA" SAVINGS AND CREDIT ASSOCIATION, VLORE
Licence No. 92, dated 07.10.2002
Member of "Albanian Savings and Credit Union" SCA Union.
72. "HOLTA" SAVINGS AND CREDIT ASSOCIATION, GRAMSH
Licence No. 93, dated 07.10.2002
Member of "Albanian Savings and Credit Union" SCA Union
73. "GJERGJAN" SAVINGS AND CREDIT ASSOCIATION, ELBASAN
Licence No. 94, dated 07.10.2002
Member of "Albanian Savings and Credit Union" SCA Union
74. "GJONME" SAVINGS AND CREDIT ASSOCIATION, ELBASAN
Licence No. 95, dated 07.10.2002
Member of "Albanian Savings and Credit Union" SCA Union
75. "GRAMSH" SAVINGS AND CREDIT ASSOCIATION, GRAMSH
Licence No. 96, dated 07.10.2002
Member of "Albanian Savings and Credit Union" SCA Union
76. "SHPRESA" SAVINGS AND CREDIT ASSOCIATION, GRAMSH
Licence No. 97, dated 10.10.2002
Member of "Albanian Savings and Credit Union" SCA Union
77. "FIER 2002" SAVINGS AND CREDIT ASSOCIATION, FIER
Licence No. 98, dated 28.10.2002
Member of "Jehona" SCA Union.
78. "BUCIMAS" SAVINGS AND CREDIT ASSOCIATION, POGRADEEC
Licence No. 99, dated 28.10.2002
Member of "Jehona" SCA Union.
79. "LESHNICË" SAVINGS AND CREDIT ASSOCIATION, POGRADEEC
Licence No. 100, dated 28.10.2002
Member of "Jehona" SCA Union.
80. "TREGAN" SAVINGS AND CREDIT ASSOCIATION, ELBASAN
Licence No. 101, dated 27.11.2002
Member of "Albanian Savings and Credit Union" SCA Union
81. "BELESH" SAVINGS AND CREDIT ASSOCIATION, ELBASAN
Licence No. 102, dated 27.11.2002
Member of "Albanian Savings and Credit Union" SCA Union
82. "LUZI I MADH" SAVINGS AND CREDIT ASSOCIATION, KAVAJË
Licence No. 103, dated 27.11.2002
Member of "Albanian Savings and Credit Union" SCA Union
83. "BAGO" SAVINGS AND CREDIT ASSOCIATION, KAVAJË
Licence No. 104, dated 27.11.2002
Member of "Albanian Savings and Credit Union" SCA Union
84. "RADË" SAVINGS AND CREDIT ASSOCIATION, DURRËS
Licence No. 105, dated 05.12.2002
Member of "Albanian Savings and Credit Union" SCA Union

85. "HAMALLAJ" SAVINGS AND CREDIT ASSOCIATION, DURRËS
Licence No. 106, dated 05.12.2002
Member of "Albanian Savings and Credit Union" SCA Union
86. "TIRANA KREDIT" SAVINGS AND CREDIT ASSOCIATION, TIRANË
Licence No. 107, dated 05.12.2002
Member of "Jehona" SCA Union.
87. "RRUSHKULL" SAVINGS AND CREDIT ASSOCIATION, DURRËS
Licence No. 110, dated 24.12.2002
Member of "Albanian Savings and Credit Union" SCA Union
88. "FIER SEMAN" SAVINGS AND CREDIT ASSOCIATION, LUSHNJE
Licence No. 111, dated 24.12.2002
Member of "Albanian Savings and Credit Union" SCA Union
89. "FRAKULL E MADHE" SAVINGS AND CREDIT ASSOCIATION, FIER
Licence No. 112, dated 24.12.2002
Member of "Albanian Savings and Credit Union" SCA Union
90. "DAULLAS" SAVINGS AND CREDIT ASSOCIATION, FIER
Licence No. 113, dated 24.12.2002
Member of "Albanian Savings and Credit Union" SCA Union
91. "KALLM I VOGËL" SAVINGS AND CREDIT ASSOCIATION, FIER
Licence No. 114, dated 10.01.2003
Member of "Albanian Savings and Credit Union" SCA Union
92. "LEKAJ" SAVINGS AND CREDIT ASSOCIATION, KAVAJË
Licence No. 115, dated 10.01.2003
Member of "Albanian Savings and Credit Union" SCA Union
93. "ALLKAJ" SAVINGS AND CREDIT ASSOCIATION, LUSHNJE
Licence No. 116, dated 10.01.2003
Member of "Albanian Savings and Credit Union" SCA Union
94. "TOSHKËZ" SAVINGS AND CREDIT ASSOCIATION, LUSHNJE
Licence No. 117, dated 30.01.2003
Member of "Albanian Savings and Credit Union" SCA Union
95. "KAFARAJ" SAVINGS AND CREDIT ASSOCIATION, FIER
Licence No. 118, dated 19.02.2003
Member of "Albanian Savings and Credit Union" SCA Union
96. "LLESHAN" SAVINGS AND CREDIT ASSOCIATION, ELBASAN
Licence No. 119, dated 23.06.2003
Member of "Albanian Savings and Credit Union" SCA Union
97. "GOSË" SAVINGS AND CREDIT ASSOCIATION, KAVAJË
Licence No. 120, dated 23.06.2003
Member of "Albanian Savings and Credit Union" SCA Union
98. "HIMARË" SAVINGS AND CREDIT ASSOCIATION, VLORE
Licence No. 122, dated 23.06.2003
Member of "Albanian Savings and Credit Union" SCA Union

99. "KOTË" SAVINGS AND CREDIT ASSOCIATION, VLORE
Licence No. 123, dated 23.06.2003
Member of "Albanian Savings and Credit Union" SCA Union
100. "ARMEN" SAVINGS AND CREDIT ASSOCIATION, VLORE
Licence No. 124, dated 23.06.2003
Member of "Albanian Savings and Credit Union" SCA Union
101. "PERLAT" SAVINGS AND CREDIT ASSOCIATION, DURRËS
Licence No. 125, dated 15.07.2003
Member of "Albanian Savings and Credit Union" SCA Union
102. "REMAS" SAVINGS AND CREDIT ASSOCIATION, LUSHNJE
Licence No. 126, dated 16.07.2003
Member of "Albanian Savings and Credit Union" SCA Union
103. "MIZË" SAVINGS AND CREDIT ASSOCIATION, LUSHNJE
Licence No. 127, dated 04.08.2003
Member of "Albanian Savings and Credit Union" SCA Union
104. "DUKAT-RADHIMË" SAVINGS AND CREDIT ASSOCIATION, VLORE
Licence No. 128, dated 03.11.2003
Member of "Albanian Savings and Credit Union" SCA Union
105. "MJELLMA-HUDENISHT" SAVINGS AND CREDIT ASSOCIATION, POGRADEÇ
Licence No. 129, dated 03.11.2003
Member of "Jehona" SCA Union.
106. "GJEÇ KODËR" SAVINGS AND CREDIT ASSOCIATION, TIRANË
Licence No. 130, dated 26.11.2003
Member of "Albanian Savings and Credit Union" SCA Union
107. "MËRTISH" SAVINGS AND CREDIT ASSOCIATION, LUSHNJE
Licence No. 131, dated 26.11.2003
Member of "Albanian Savings and Credit Union" SCA Union
108. "MASHAN" SAVINGS AND CREDIT ASSOCIATION, GRAMSH
Licence No. 132, dated 26.11.2003
Member of "Albanian Savings and Credit Union" SCA Union
109. "PAPËR" SAVINGS AND CREDIT ASSOCIATION, ELBASAN
Licence No. 133, dated 26.11.2003
Member of "Albanian Savings and Credit Union" SCA Union
110. "KUKUR" SAVINGS AND CREDIT ASSOCIATION, GRAMSH
Licence No. 134, dated 07.01.2004
Member of "Albanian Savings and Credit Union" SCA Union
111. "BLETA" SAVINGS AND CREDIT ASSOCIATION, POGRADEÇ
Licence No. 135, dated 03.03.2004
Member of "Jehona" SCA Union.
112. "VAQARR" SAVINGS AND CREDIT ASSOCIATION, TIRANË
Licence No. 136, dated 01.04.2004
Member of "Albanian Savings and Credit Union" SCA Union

113. "GRACEN" SAVINGS AND CREDIT ASSOCIATION, ELBASAN
Licence No. 137, dated 23.06.2004
Member of "Albanian Savings and Credit Union" SCA Union
114. "SKENDERBEGAS" SAVINGS AND CREDIT ASSOCIATION, GRAMSH
Licence No. 138, dated 23.06.2004
Member of "Albanian Savings and Credit Union" SCA Union
115. "DARZEZË" SAVINGS AND CREDIT ASSOCIATION, FIER
Licence No. 139, dated 12.07.2004
Member of "Albanian Savings and Credit Union" SCA Union
116. "SPILLE" SAVINGS AND CREDIT ASSOCIATION, KAVAJË
Licence No. 140, dated 12.07.2004
Member of "Albanian Savings and Credit Union" SCA Union
117. "GOSTIMË" SAVINGS AND CREDIT ASSOCIATION, ELBASAN
Licence No. 141, dated 12.07.2004
Member of "Albanian Savings and Credit Union" SCA Union
118. "JADORA" SAVINGS AND CREDIT ASSOCIATION, SHKODËR
Licence No. 143, dated 17.11.2004
Member of "Jehona" SCA Union
119. "QARR - BISHAN" SAVINGS AND CREDIT ASSOCIATION, FIER
Licence No. 145, dated 28.04.2005
Member of "Albanian Savings and Credit Union" SCA Union
120. "KRUTJE" SAVINGS AND CREDIT ASSOCIATION, LUSHNJË
Licence No. 146, dated 29.07.2005
Member of "Albanian Savings and Credit Union" SCA Union
121. "TIRONA" SAVINGS AND CREDIT ASSOCIATION, TIRANË
Licence No. 147, dated 05.12.2005
Member of "Albanian Savings and Credit Union" SCA Union
122. "SHKAFANE" SAVINGS AND CREDIT ASSOCIATION, Durrës
Licence No. 148, dated 16.01.2006
Member of "Albanian Savings and Credit Union" SCA Union
123. "LIBRAZHD" SAVINGS AND CREDIT ASSOCIATION, LIBRAZHD
Licence No. 149, dated 10.11.2006
Member of "Albanian Savings and Credit Union" SCA Union
124. "HELMAS" SAVINGS AND CREDIT ASSOCIATION, KAVAJË
Licence No. 150, dated 22.11.2006
Member of "Albanian Savings and Credit Union" SCA Union
125. "LUKOVË" SAVINGS AND CREDIT ASSOCIATION, Vlorë
Licence No. 151, dated 14.12.2006
Member of "Albanian Savings and Credit Union" SCA Union
126. "CERME" SAVINGS AND CREDIT ASSOCIATION, LUSHNJË
Licence No. 152, dated 12.01.2007
Member of "Albanian Savings and Credit Union" SCA Union

127. "ELBASAN" SAVINGS AND CREDIT ASSOCIATION, ELBASAN
Licence No. 153, dated 18.04.2007
Member of "Albanian Savings and Credit Union" SCA Union

128. "DYRRRAH" SAVINGS AND CREDIT ASSOCIATION, DURRËS
Licence No. 154, dated 27.04.2007
Member of "Albanian Savings and Credit Union" SCA Union

129. "SEMAN" SAVINGS AND CREDIT ASSOCIATION, FIER
Licence No. 155, dated 21.05.2007
Member of "Albanian Savings and Credit Union" SCA Union

REPRESENTATIVE OFFICES OF FOREIGN BANKS

THE REPRESENTATIVE OFFICE OF BANCA POPOLARE PUGLIESE IN ALBANIA

Licence: No. 01, dated 02. 07.2003

Representative: Pasquale Guido Vergine

Address: Sheshi "Skënderbej", Pallati i Kulturës, Kati III, Tirana, Albania

Tel.: 25 67 82

