

ALBANIA AND ITS ACCESSION IN THE
WORLD BANK

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**TEN YEARS OF MEMBERSHIP OF ALBANIA IN THE WORLD BANK:
RESULTS ACHIEVED, LESSONS LEARNED**¹
by Franco Passacantando²

1. INTRODUCTION

It is a great honor for me to participate in this Conference among so many Albanian friends and representatives of the international community. Let me thank the organizers of this Conference, and particularly Prime Minister Meta and Governor Cani for providing this opportunity, on the tenth anniversary of the membership in the Fund and the Bank, to discuss what has been achieved in ten years of collaboration between the Bank and Albania and the challenges lying ahead. This conference takes place at a time when the public opinion, policy makers and the academic world are closely watching how the World Bank operates, and its impact on development. Needless to say, the opinion that receives the greatest attention is that of the critics. They often claim that the

¹ Paper presented at the Conference "Albania between Domestic Reforms and European Integration" organized by Council of Ministers and the Bank of Albania (Tirana, Albania December 6-7, 2001).

² The author wishes to thank Kristaq Luniku, for his invaluable input in the preparation of this paper, and Luisa Masutti for useful comments.

value generated by the Bank is not worth the money that donors and shareholders put into it, or that the policies advocated by the Bank harm the poor, and increase social injustice.

I think the case of Albania gives a good example of how wrong this view can be. This is a country that joined the Bretton Woods institutions after more than four decades of isolation and a particularly authoritarian communist regime. A country which had very little previous experience with the instruments and rules of a market economy. A country that has undergone a rapid transformation, which has given rise to acute social tensions. A country that is located in one of the most difficult regions of the world. Yet, as I will show, Albania has been able to greatly leverage World Bank assistance and to benefit from it. This does not mean that everything has worked well. Mistakes have been made and, in many areas, progress has been uneven.

But overall, the membership of Albania in the World Bank has positively contributed to the development of this country.

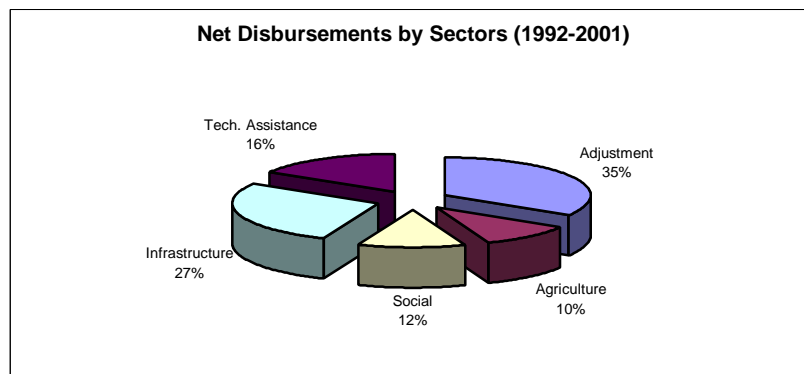
2. A SNAPSHOT OF THE BANK PROGRAM

The history of the Bank involvement with Albania is presented in Annex I, where it is first analyzed the period from 1991³ to 1996, when the initial reforms to create a market economy were made, and when the macroeconomic stabilization following the crisis of 1992 was achieved. Then it is shown how the Bank supported Albania in overcoming the crisis of 1996, due to the collapse of the pyramid schemes, and that of 1999, when Albania had to face an unprecedented flow of refugees from Kosovo. The Annex finally shows how the Bank, taking stock of the lessons learned in the first years of involvement in Albania, reoriented its strategy, by accompanying initiatives to further promote private sector growth with a program to strengthen the governance, accountability, and efficiency of public institutions, together with greater attention to social issues.

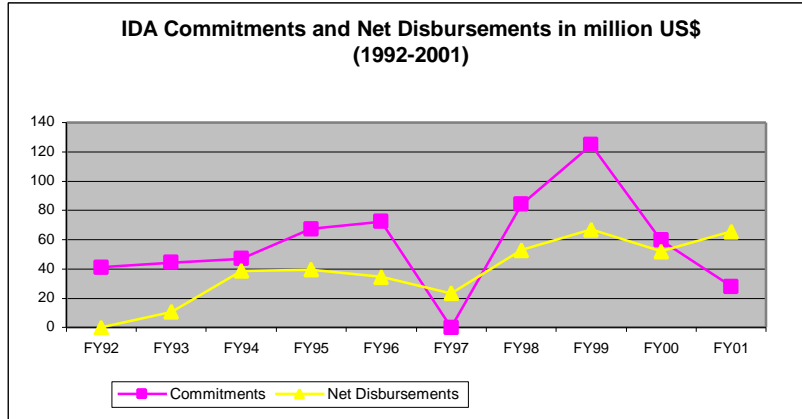
In ten years the World Bank Group, through IDA, has approved 42 loans and completed 22 projects. IDA has disbursed in total 392.4 million dollars, which means an average of 114 dollars per every Albanian. The World Bank plays a significant role within the donor

³ Albania became a member of the Fund and the World Bank Group in October 1991, joining the constituency which comprises Italy, Portugal, Greece, Malta, and San Marino.

community as the overall funds committed represent about 18 per cent of the total official assistance made to Albania by the donor community since 1991. The largest share of disbursements has been in adjustment lending, but this is mainly due to operations made in 1998 and 1999 (see table II.3 in Annex II). In other years the main sectors were Infrastructure, and Agriculture. Technical Assistance lending has also played an important role, both at the beginning of decade and in the fiscal year 2000, when the Bank concentrated its efforts on institution building.



As the following chart shows, the support to Albania has been continuous, except during the crisis of 1997, when no new loan was approved, and has reached a maximum in 1999, during the Kosovo crisis, when funds committed topped 125 million dollars in a year. Over the almost ten years of IDA's involvement in Albania, per capita commitments have increased rapidly from 12 dollars in 1992, to about 23 dollars in 2000.



3. ASSESSING THE RESULTS ACHIEVED

We can now turn to the question of what has been achieved by the Bank with its programs in Albania. What results can be shown to the donors to prove that the 400 million dollars they have given to Albania, through IDA, in ten years were well spent? And what results can be shown to the Albanians to prove that the programs of the Bank are worth the present and future burdens they face in terms of conditions to comply with and debt to service? Unfortunately, no easy answer can be provided to these questions. Some tangible results are visible in roads improvements, irrigation channels, schools, and hospitals. But today the Bank believes that what matters most for development, besides infrastructure and physical capita, are the rules, laws, and institutions of a country, as well as the quality of human and social capital.

Measuring and tracking results in these areas is exceptionally complex. It is also very difficult to separate the specific Bank contributions from those of other donors or agencies or from what the Albanian government has done on its own, independently from the international community. However it is possible to identify some areas in which the Bank has been most successful, those where problems were encountered and the main challenges still lying ahead. I will focus on three areas: promotion of private sector activity, institutions and governance, human and social development.⁴

⁴ An independent assessment of the Bank's program is available in World Bank, Operations Evaluation Department, *Albania, Country Assistance Evaluation*, Washington, D.C. November 16, 2000.

3.1 PROMOTION OF PRIVATE SECTOR ACTIVITY

One of the main achievements of the past decade lies in the promotion of a vibrant private sector in Agriculture and in the area of small business enterprises. Although Albania acted largely on its own initiative to disengage the state from productive activities, the Bank has greatly contributed to this process, especially in the second half of last decade. By 1997, 92 per cent of all small and medium enterprises in the agro-processing and agricultural marketing business was fully privatized. About 450,000 farms with an average size of 1.1 hectares were created. Thanks also to improvements in irrigation systems, the gross value of Agricultural Output at constant prices increased by 57 per cent from 1991 to 1995. One of the most successful projects, which also contributed to these developments in agriculture, has been the rural credit program. By 1996, 7,500 medium and small firms were sold. Important privatizations have also been conducted in the mining and telecommunication sector, and within the banking sector.

Needless to say, in many areas progress has been uneven and important steps have yet to be made. Important improvements in port and road infrastructures have taken place, but to favor private investment the overall *transport* system should be much more extensively developed. In the *energy and water sector*, fundamental reforms are still needed, and immediate improvements in the management of the utility companies are necessary. IDA has made an effort to create a viable and self sustainable *financial sector* but access to long term financing is still limited. The privatization of the Savings Bank, and new legislation on banking activity, which is being prepared with the assistance of the World Bank, will be important steps for the creation of a modern financial system. Of great importance will also be the creation of new financial intermediaries as leasing companies.

Improvements in all these areas are necessary to continue the good work done in the first stage of economic liberalization. Problems today are in a way more complex than those faced at the early stage of the liberalization process, but they need to be addressed aggressively if Albania wants to attract foreign direct investment and diversify its economy that is still too much dependent on the agriculture and construction sectors.

3.2 Institution building and Governance

This has been one of the priorities in the strategy pursued by the World Bank with the Albanian authorities in the second half of the nineties. One of the main achievements has been that made by the Bank of Albania, with the contribution of the World Bank and the International Monetary Fund. The concept of a central bank that would regulate money and supervise financial institutions was totally new when the Bank of Albania started its operations in a small office ten years ago. Today the Bank is a well-structured and respected institution, thanks to the courage and hard work of its professional staff under the leadership of Governors Vrioni, Luniku, and Cani. The monetary policy procedures and instruments have continuously improved. While there is still substantial room for improvements in areas such as Bank supervision or the payment system, much has been achieved, bringing about surprising results in terms of monetary and exchange rate stability, which have been crucial in leading the country to the path of recovery after the numerous crises it faced.

These achievements on the monetary front have been coupled by equally important achievements in budgetary policies, thanks mainly to the improvements in revenue collection and the strengthening of tax and custom administration. On the public expenditure side, the development of a Medium-Term Expenditure Framework has greatly helped identifying a mechanism to select expenditure priorities. Minister Malaj and Minister Angjeli and their staff have achieved these results in exceptionally difficult circumstances. Major challenges still remain. Budget revenues need to be further raised. The tax base, further broadened. Public debt, though still manageable, has to be closely and continuously monitored.

An area in which the Bank has recently paid increased attention is that of Legal and Judicial Reform as well as the Public Administration Reform. Two projects approved by the Board of the Bank in March 2000 will assist Albania in these two areas of crucial importance for the investment climate and the quality of public services in general. In the past, failure to develop a comprehensive civil service reform program led to a rapid exodus of good quality staff from public administration exacerbating the mistrust towards public institutions. A rapid implementation of the new bankruptcy law and creditor rights could provide an important contribution to the creation of a favorable investment climate.

No reform in the Public Administration can be successful if it is not accompanied by a strong commitment to combat corruption, illegal trafficking, money laundering, and any form of financing for terrorism and organized crime. The Bank began its cooperation with Albania on anti-corruption issues in 1997. The year after, the results of surveys of household and public officials, which showed how widespread corrupt practices prevail in Albania, were presented at a workshop organized by the Bank with the Albanian Government. Since then, the Bank has assisted the Government with technical assistance to the Government's Anti-Corruption Steering Group. The Bank is also providing support for anti-corruption through the ongoing Public Administration Reform and Legal and Judicial Reform Projects. Anti-corruption work for Albania is also being channeled through the SPAI initiative (Stability Pact Anti-Corruption Initiative). The Bank is a member of the management committee of the SPAI.

3.3 HUMAN AND SOCIAL DEVELOPMENT

While Albania has achieved macroeconomic stabilization and introduced important structural reforms, poverty is still the highest in Europe and in the South East region. About 20 per cent of the population is poor, with 90 per cent of them living in the rural areas.

Poverty is strongly linked to poor education and difficulty of access to basic services. In both areas much has been done, but success has been at best uneven. The strategic focus on school rehabilitation was correct in the initial years of IDA Assistance, and quite good progress was made in repairing physical plants from 1993 to 1996. But the resources presently allocated to health and education are scarce, and institutional reforms are very much incomplete.

An area in which results have been excellent has been the involvement of local communities and civil society organizations in the project design and implementation. Some of the most successful projects were in fact those in which there was some form of community involvement. In rural and irrigation projects, beneficiary associations were created like the Village Credit Funds or the Water User Association. The credit originated by the rural project had a 100 per cent repayment record. This has resulted in an increase in the incomes of poor families from 15 to 70 per cent

and between 30 to 50 per cent for the better off families.⁵ As the OED evaluation of Albania appropriately points out, the greater ownership of World Bank projects by local population has greatly diminished the consequences of social crises. In 1990-01, irrigation networks, along with other rural infrastructure, were widely destroyed. In 1997, by contrast, members of the Water User Association guarded those facilities during the social upheaval that followed the collapse of the pyramid schemes, minimizing damages.

4. LESSONS LEARNED

In conclusion, ten years of membership of Albania in the World Bank have brought about important results in a number of areas. Though much remains to be done, what has so far been achieved does not seem to support the view that Official Development Assistance, as intermediated by the World Bank, produced no returns or that it may harmed the beneficiary countries. At the same time I think that the association of the Bank with Albania and the experience accumulated have taught many important lessons, which I would like to briefly summarize to conclude this paper.

The first lesson is that macroeconomic stability and pro-market reforms are necessary, perhaps indispensable conditions, but not sufficient ones. Low inflation and a strong currency have somewhat shielded the country from external shocks. For instance Albania was minimally affected by the Asian crisis and also rapidly recovered from the Kosovo crisis. But a fairly good overall macroeconomic performance and rapid growth did not prevent major social unrest, the most serious one being that experienced in 1997, and may have at times created a sense of complacency, which delayed action on the structural and social fronts.

The second lesson is that investments in social capital and attention to social and gender issues are of great importance. This is true both at the project level, as we have seen that the projects that have been prepared and implemented with the involvement of local communities have been most successful, and at a broader government policy level, as the lack of social cohesion has been an important factor in undermining the long-run sustainability of development programs.

⁵ OED report on Albania, page 40.

The third lesson is that institutions and a good public administration matter. The Albanian experience highlights the apparent paradox that to reduce the role of the state and its presence in productive activities it is necessary to strengthen the state, and its institutions. The uneven progress in public administration reform, as well as in legal and judiciary reform, resulted in the expansion of illegal or non transparent activities, in widespread corruption, and in a public mistrust towards the government and state institutions.

The fourth lesson is that a successful development program requires a balanced and integrated approach. In the early nineties the good results achieved in infrastructure rehabilitation and, most of all, in privatization, were not accompanied by significant progress in health and education and in institution building and governance. The result was rapid economic growth but high social vulnerability. In the second part of the decade, the attention shifted to institutional and social issues, but the deterioration of infrastructure, as in the energy sector, created a major bottleneck for further investments and growth.

The fifth lesson is that donor coordination is crucial for two reasons. First to allow different donors and institutions to contribute according to their expertise and comparative advantage. Second, because the costs for maintaining relationships with the international community and to adapt to individual procedures and needs may impose a very heavy burden on a country. In many occasions I have seen the Minister of Finance of Albania completely overwhelmed by the need to keep relationships with the international institutions and different donor agencies. The PRSP process, and the Comprehensive Development Framework have the potential to greatly improve donor coordination.

The sixth lesson is that the quality of the individual projects is important but it does not guarantee the overall success of a development program. Albania has been one of the most successful countries in terms of project performance but this has not prevented a major and largely unexpected overall program failure in 1996. This does not mean that individual investment projects should be abandoned, but that they should be integrated in broader programs in which specific investments are accompanied by wider reforms.

The seventh lessons is that country ownership of the programs to be implemented with international institutions is crucial but also

that conditionality is in many occasions important, and that the two are not necessarily inconsistent. International Institutions urged the Government of Albania to close the pyramid schemes, but perhaps bolder and earlier initiatives could have been taken. Had this happened, the crisis of 1996 might have been somewhat mitigated, though it is unlikely that the Government at that time would have chosen a different course, even under much heavier international pressure. Also, the conditionality associated with the power project has contributed to important progress in utility collection rates. At the same time, the adjustment programs would not have led to the results of macroeconomic performance without a strong commitment and ownership of these programs by the Albanian Authorities.

And this leads me to my concluding comment. While I very much believe the World Bank has greatly contributed to the development of Albania, I have to say clearly that the great merit of the success achieved mainly lies with the Albanians, their sacrifices and their resolve to move forward even in the most adverse circumstances.

ANNEX I.

THE EVOLUTION OF THE WORLD BANK PROGRAM IN ALBANIA FROM 1991 TO 2001

The Bank has been involved in the design and implementation of reforms through policy advice, lending and technical assistance. Since the very beginning, its action, together with that of the Fund, aimed at achieving three broad policy objectives. The first was to liberalize the economy, the pricing system, the exchange rate and trade regimes, and to promote private sector initiative, fair competition, and market discipline. The second was to achieve macroeconomic stabilization through fiscal and monetary policies aimed at ensuring sustainable external and budgetary balances. The third objective was to create institutions and markets, through structural reforms in the areas of tax administration, privatizations, break-up of monopolies, legal reform on property and ownership,

banking regulation and social safety nets to protect the poor. In the first years the emphasis, both of the government and the World Bank was mainly on the first two objectives.

I.1 BUILDING THE FOUNDATIONS OF A MARKET ECONOMY

At the time of joining the institutions, in 1991, the country was in a deep crisis. Assistance was necessary in all sectors. The immediate priorities were emergency humanitarian assistance - food aid, medical supplies, and key agriculture inputs – together with macroeconomic stabilization. The Critical Imports Project of the Bank and the Stand-by arrangement of the Fund, approved in 1992, marked a crucial step in abandoning decades of central planning and supported the country's comprehensive restructuring program toward market-based system. At the outset, the Bank recognized the need to act together with many other donors and agencies. Many operations were designed and implemented in co-financing with other donors. To better coordinate activities, several aid and donor meetings were organized and a special program was designed to support their assistance strategies and lending programs. Foreign assistance was massive. In the five years between 1992 and 1996, Albania received about 1.525 billion dollars, or about 475 dollars per capita, in total aid, the vast bulk of which (68 per cent) were official grants. In the same period, IDA commitments to Albania amounted to 272.5 million dollars, or about 18 per cent of the total aid. Ida disbursements totaled 123.6 million dollars, 38 per cent of which allocated to technical assistance programs, and 25 per cent to infrastructure projects. Given the macroeconomic uncertainties and the weak implementation and public administration capacity, the IDA country assistance for FY 94-96 was very broad.

Main Outline of IDA's Assistance Strategy (1992-1996).

Sector	Objectives	Nature of IDA support (Projects and ESW)
Rehabilitation of infrastructure and basic public services	<ul style="list-style-type: none"> • Rehabilitation • Cost recovery 	<ul style="list-style-type: none"> • Power • Transport • Water supply
Support to private agriculture	See below	See below
Social sectors and policies	<ul style="list-style-type: none"> • Move social insurance toward actuarial basis • Better targeting of social assistance • Development of policy 	<ul style="list-style-type: none"> • Social Safety Net • School rehab. • Health rehab. • Labor Market • Urban Poverty

	for poverty alleviation	<ul style="list-style-type: none"> • Poverty Surveys
Privatization, restructuring and financial sector restructuring	<ul style="list-style-type: none"> ➤ Privatization of small- and medium-scale enterprises ➤ Development of Bank Infrastructure and reg. 	<ul style="list-style-type: none"> • Enterprise & Financial Sector Project
Development of new central, and local administration	<ul style="list-style-type: none"> • Improve capacity for reform preparation and implementation • Improve absorptive capacity 	<ul style="list-style-type: none"> • 1994-96 Public Invest. Program • Study on Civil Service Reform • Tax Administr. Public Administr. Action plan
Foreign debt	<ul style="list-style-type: none"> • Voluntary settlement of Albania's Debt 	<ul style="list-style-type: none"> • Use of IDA-Debt Reduction

Source: The World Bank – Albania CAS Evaluation, November 2000.

Because of the dilapidated state of Albanian *infrastructure*, IDA's lending focused on immediate needs of physical rehabilitation. Transportation and the Power Sector were identified as key priorities. The largest amount of Bank's commitments, about 21 per cent, were concentrated in the *transport sector*. The Transport project and the National Road and Rural Road projects aimed to improve the conditions of the national and rural roads, and put in place market-oriented policy reforms in the sector. Given the institutional weaknesses both in generation and distribution systems, the *power sector* has been and still remains one of the key priorities of Bank's programs. In 1993, the Critical Import Credit supported immediate repairs to the Drin River Hydropower stations. In addition, the Power Loss-Reduction and the Power Transmission and Distribution projects aimed at reducing the very large technical and non-technical electricity losses and the inefficient use of electricity. The second largest recipient, representing 19 per cent of total commitments, was the *agricultural sector*, in which the Bank intervened with six lending and adjustment operations, including Agricultural Sector Adjustment Credit, the Irrigation Rehabilitation project, and the Agroprocessing Development project. The most successful projects were the Rural Development project and the Rural Poverty Alleviation pilot program, which introduced new mechanisms to provide credit to small farmers. The Forestry project was designed to promote the restoration and conservation of natural forest ecosystems. Particular efforts in the strategy have been given to the land reform which aimed also at the development of agriculture land market. All state farms disappeared and about 450,000 farms with an average size of 1.1 hectares were created.

Agriculture Sector Assistance Strategy (1992-1996).

Area/subsector	Constraint/conditions	Strategic objectives
1. Land reform	Small size of farm	Development of market for land Privatization Study for Agro-Enterprises
2. Irrigation system	Poor physical state; inadequate institutions for small scale irrigation	Expand irrigation network. Water infr. maintenance Establish incentives for efficient water use
3. Rural credit	BAD/RCB cannot provide credit to small farmers	Facilitate access to credit by small farmers
4. Rural infrastructure	Poor state through lack of maintenance and damage	Rehabilitate rural infrastructure Improve rural roads
5. Agricultural inputs	Dire shortage	Develop infrastructure and enabling environment to support private sector trade

In the area of *poverty alleviation and social safety nets* several measures were taken to develop the legal and administrative frameworks for pensions, unemployment insurance, and job placement systems. While the short-term agenda was focused on rural poverty and the most vulnerable groups, the long-term program was directed at establishing a sound pension system, developing a poverty monitoring mechanism, and a policy framework to alleviate poverty and reduce inequality. With regard to the *health* and *education* sectors, the first efforts were directed at rehabilitating hospitals, redefining health districts and defining criteria to deliver health care based on population and epidemiological parameters. The Social Safety Net and Labor Market Development projects helped creating the policy and institutional conditions for the development of a more flexible labor market. Recognizing the weaknesses in the area of *Public Sector Management* and *Institutional Development*, the IDA worked with the authorities and other donors to help downsizing the civil service, developing the absorptive and institutional capacity of the core public sector, and strengthening the local government through a process of so-called participatory decentralization.

The Enterprise and Financial Sector Adjustment Credit supported the *privatization* of the state-owned enterprises, including the liquidation and downsizing of the non-viable ones. While 7,500 medium and small firms were sold by 1996, the larger state-owned

enterprises proved more intractable and the process of attracting investors disappointing. The two lending operations in *housing and urban sector* initiated a market-based housing system by broadening the role of the private sector.

In order to restore normal relations with creditors, the Fund and the Bank helped Albania developing a *debt management strategy*. In March 1995, Albania reached a deal with the creditor banks, using an innovative approach that settled the debt of 371 million dollar principal and 111 million dollar past due interest for only about 96 million dollars or at about 20 cents per dollar. The World Bank backed up this settlement with a 25 million dollars grant from the IDA- Debt reduction Facility. As a result, external debt declined to 29 per cent of GDP in 1996 from 108 per cent in 1992. Throughout this period, the Albanian economy underwent major structural and macroeconomic transformations. The balance of payments improved considerably, and the Central Bank foreign exchange reserves reached comfortable levels of about 3.5 months of imports. Inflation was quickly reduced, falling from 200 per cent to about 6 per cent in 1995.

I.2 RESPONDING TO THE CRISES OF 1996 AND 1999

Macroeconomic indicators worsened considerably in the second part of 1996. Fiscal deficit rose to 10.5 per cent of GDP, compared to an average of 7.5 per cent in the prior three years, as the country was heading to general elections in the summer of that year. Inflation accelerated and the domestic currency depreciated. In this already unfavorable macroeconomic climate the crisis of pyramid schemes erupted. The experience of a rapid mushrooming of pyramid schemes is not unique for Albania, but in no country this has resulted in a catastrophic breakdown in civil order as in Albania. The schemes in part emerged as a result of the backwardness of the banking system, though no legitimate bank could have ever offered rates competitive to those offered by the companies operating the schemes. The lack of familiarity of the general public with financial matters also contributed to the growth of the schemes. Initially, the real danger of the phenomenon was underestimated even by the Fund and the Bank, which initially treated the companies as part of informal credit market.

As the schemes gained more popularity, concerns started being expressed, especially by the Bank of Albania. Its Governor forcefully argued about the risks implicit in the schemes, and urged the Government and law enforcement institutions to shut them

down. By October 1996, under strong pressure from the World Bank and the Fund, the Government agreed to publicly denounce the risks of the schemes, but by then it was far too late. In early 1997, all the schemes collapsed, leading to widespread civil disorder. The office of the World Bank in Tirana was evacuated, because of the rapid deterioration of security conditions.

The scale of the pyramid schemes relative to the size of the Albanian economy was unprecedented. It is estimated that over 65 per cent of the Albanian population placed savings in these fraudulent companies. The economic costs of the breakdown proved to be very high, in terms of wealth losses, destruction of infrastructure and private property, erosion of confidence in institutions, and severe macroeconomic unbalances. In 1997, the GDP fell about 7 per cent, inflation accelerated to over 40 per cent, and fiscal deficit reached 14 per cent of GDP. The external balances deteriorated, foreign aid was entirely disrupted, and there was a sharp decline in inflow of capital from abroad. Under such circumstances, reestablishing macroeconomic stability, particularly fiscal recovery, was a key strategic role. Another priority was the enforcement of banking laws and prudential regulations.

As soon as conditions in Albania stabilized following the intervention of an international force to restore order, the World Bank Board approved in July 1997 a *Recovery Program* to help the country return to a developmental path. The program emphasized the need to strengthen the country's administrative capacity, through a reform of public administration, the separation of executive and judiciary powers, improvements in oversight and transparency, and greater participation of civil society. High priority was also assigned to creating an independent civil service, free of political influence. Based on an early update of poverty assessment, steps were also taken by IDA to support vulnerable groups through restoration of health services and education.

In 1999 Albania was again struck by a major crisis, this time due to the large inflow of refugees from Kosovo, which strained domestic resources and increased the financing gap. The World Bank assisted Albania with a Public Expenditure Credit of 30 million dollars, which helped the country overcome the crisis. Also in this occasion, macroeconomic stability was soon reestablished and economic growth resumed. Inflation stabilized and reserves further increased. The budget deficit was reduced from 11.4 in 1999 to 9.1 in 2000 (Table II.1) . In both occasions, the World Bank was struck by the ability of the country to restore macroeconomic

stability. At the same time it was also clear that governance and social problems of the country had to be tackled aggressively to ensure sustainability of development programs.

I.3 REORIENTING THE BANK'S AGENDA AFTER 1996

The main lessons of these crises were incorporated in the Country Assistance Strategy approved in 1998 and the Progress Report in 2000. The main root cause of the crisis, which derailed Albania's development process, was considered to be an extremely weak state, lack of developed institutions, low commitment to community values, and high level of corruption. Efforts have therefore been focused on three strategic priorities; (i) governance and institutional building aimed at establishing accountable, transparent and efficient state institutions, (ii) private sector development, which is crucial for growth and poverty reduction, and (iii) human development and poverty alleviation. Improvements in *governance and institutional building* were directed at increasing the transparency and accountability of the state in Albania in order to improve the investment climate, alleviate poverty and build trust. The key projects in this area were the Public Administration Reform project and the Legal and the Judicial Reform project, both approved in March 2000. The first credit aims at strengthening public expenditure and human resource management in public sector institutions as well as the coordination capacities within the public sector. The Legal and Judicial Reform Project provides technical assistance, training, and goods for legal and justice system reform, to strengthen of the rule of law in Albania. The main components are: the improvement of education in legal areas, strengthening of the justice system through improvements in enforcement of judicial decisions and strengthening of judicial inspections, the creation of a mechanism for dealing with commercial disputes.

Governance and Institution Building.

I. Strengthen the Public Administration and Professionalize the Civil Service	<ul style="list-style-type: none"> a) Implementing regulation approved b) Functional reviews undertaken c) Pay reform implemented d) State Control Service established as independent national audit office
II. Strengthen Judiciary	<ul style="list-style-type: none"> 1. Repair of Court rooms 2. Training of judges 3. Reformulation of High Council of Justice (HCJ) 4. Legislation to provide criteria for appointment and dismissal of

	judges
III. Strengthen Local Institutions and Build Social Consensus	1. Local governments trained in infrastructure works and in methods of consulting population

Source: The World Bank – Albania CAS FY99-01.

The promotion of *Sustained Private Sector growth* required coordinated action on several fronts (see box below). In the area of *infrastructure*, the National Roads Project rehabilitated two main sections of the link between Tirana and Lezhe (in the North-South corridor) and the link between Tirana and FYR of Macedonia (in the East West Corridor). The Emergency Roads Repair Project has improved the condition of the *existing* road leading from Durrës to Kosovo, which was heavily damaged following the Kosovo conflict, while financing a feasibility study for a new road that the Albanian Government intends to build. Finally The Rural Roads project changed the way in which business is conducted in Albania in the road sector, creating a local contracting capacity in Albania, which did not exist before. Another important area of activity regards the Durrës Port, which is located at the western terminus of Corridor 8 and is a key transit point for almost all Albania's imports and exports as well as traffic to Macedonia and beyond. IDA has supported its transformation since the early 1990s. Accomplishments to date include the passage of commercially oriented port laws, establishment of an independent Port Authority, the ongoing privatization of port operations, staged improvement of cargo handling methods and port security, and the rehabilitation/replacement of key infrastructure and equipment.

Resumption of Sustained Private Sector Growth.

I. Macroeconomic Stability	<ol style="list-style-type: none"> 1. Improved management of public finances 2. Improved prioritization of spending Reform of pensions and unemployment system
II. Financial Intermediation	<p>Banking sector</p> <ol style="list-style-type: none"> 1. RCB closed; NCB privatized; Privatize SB 2. Amendments to Banking Law; new legislation on collateral; strengthening of banking supervision 3. Implementation of international accounting standards 4. Political Risk Guarantee <p>Microcredit</p> <ol style="list-style-type: none"> 1. Establishment of Autonomous microcredit foundation. <p>Legislative and supervisory framework for SCAs (Small Credit Associations)</p>
III. Infrastructure	<ol style="list-style-type: none"> 1. Reduction in outages and power distribution

Power	loss 2. Clearance of arrears to electricity companies
Transport	1. Creation of Inter-Ministerial Road Safety Committee 2. Reduction in railway staff and services 3. Durres port privatization action plan
IV. Sustain Agricultural Growth	1. Low and uniform tariff structure maintained 2. Accession to WTO 3. GDSR abolished 4. Agriculture Infrastructure 5. Agriculture & Rural Services 6. Natural Resource Management
VI. Promoting Sustainable Environmental Development	1. National Environmental Action Plan (NEAP) completed and implemented 2. Biodiversity Strategy and Action Plan (BSAP) completed 3. Joint environmental task force created. 4. Joint Lake Ohrid Management Board

Source: The World Bank – Albania CAS FY99-01.

To develop the *financial sector* the Bank Group has been involved in bank privatization, supervision, and financial infrastructure. The NCB has been privatized. The Financial Sector Institutional Building project, approved in June 2000, will assist the Authorities implementing the sector reform. Currently, the Bank and the IFC are assisting Albania in the privatization of the Savings Bank. Concrete steps have been taken in recapitalizing and preserving the value of the Bank, and further efforts are underway to establish contacts with interested strategic and well qualified investors. In addition, the Bank and the Fund have been providing extensive technical assistance in cooperation with Albanian authorities and with other international organizations in areas such as the government securities market, the creation of monetary and fiscal statistics, strengthening of prudential regulations and bank supervision. The Bank has also actively promoted *trade integration* of Albania in the surrounding region. In this respect the new political situation in Yugoslavia offers an opportunity for cooperation, economic and development integration. To facilitate the process, the Bank has launched a Trade and Transport Facilitation project in South East Europe, which is an important regional initiative aimed at strengthening and modernizing custom administration (see box below). This projects complements other activities, including highway corridors, ports' modernization, harmonization of regulatory and legal frameworks, cooperative work in combating trafficking, corruption and organized crime.

TRADE AND TRANSPORT FACILITATION IN SOUTHEAST EUROPE (TTFSE) PROGRAM.

Presently, the high costs of trade and transport in the countries of Southeast Europe create disincentives to foreign investment and high user costs. The most visible problem is the long lines at border crossing points, ranging from hours to days.

The program of Trade and Transport Facilitation in Southeast Europe (TTFSE) approaches these problems on a regional basis. The participating countries have signed a Memorandum of understanding establishing a Regional Steering Committee (RSC). Progress under the respective projects is to be monitored by performance indicators commonly agreed upon and to be compared at the periodic meetings of the RCS.

An important component of the program is the investment in border crossing points. Equally important is the simplification of procedures and service improvements. IBRD loans or IDA credits have been approved for six countries under the Program: Albania, Bosnia and Herzegovina, Bulgaria, Croatia, Macedonia, and Romania. Projects in Moldova and the FYR of Yugoslavia are under preparation.

Funding for the TTFSE is based on a partnership with other donors. The Bank mainly deals with the improvement of information services and of the border crossing facilities. Partnership with the EU is an essential element of the TTFSE. The United States and other donors support the components for trade facilitation and the reform of Customs operations. The UN ECE holds the secretariat to the RSC.

A small but innovative project to favor private investment has been the *Private Industry Recovery project* approved in 1998. The implementing agency AGA (Albanian Guarantee Agency) has issued about 22 guarantees, for a total amount of US\$ 7.7 million, with a positive impact on investment. Presently the project is being restructured to include financial and technical support for Albanian exporters, thus transforming AGA into Albania's export credit agency. In addition to political risk insurance, for which there is now less demand, thanks to improved overall climate, AGA will provide (i) import and export credit insurances, (ii) working capital guarantee/loans, (iii) exporter performance facilities, and (v) technical assistance to local enterprises for marketing, and export procedures.

Human Development and Poverty alleviation constitutes the third broad strategic direction of Bank's activity. In the *education sector*, efforts are focused on addressing the poor management and the inadequate governance and accountability in the system. Further measures are recommended to increase budgetary allocation for these sectors and the quality and effectiveness of education programs. Similarly, the Education Reform project aims at improving the managing and delivery of educational services. These projects have by an large achieved their objectives and have strongly contributed to the progress of the reform in the respective sectors. In the *health sector* progress has been unsatisfactory. Services continue to be inadequate and inaccessible to most of the rural poor. The Bank is involved in helping Albania reduce high rates of poverty and mortality for infants and children, improve health sector planning and management capacities, and increase the efficiency of budgetary allocation for the health sector. The SAC II will contribute in the public expenditure management in the health sector, while the Health Sector study will provide the institutional measures to strengthen the health sector planning and its management capacities.

Human Development and Poverty Alleviation.

I. Strengthening the Social Safety Net	<ul style="list-style-type: none"> • Increase social assistance benefits • Launch of LSMS (Living Standards Measurement Survey)
II. Improving the Quality of Education	<ul style="list-style-type: none"> - Reduce levels of authority between the Ministry and schools and downsize district education offices - Develop Learning assessment methods - Retrain teachers - Rehabilitate damaged schools - rationalize number of universities Increase share of fiscal resources for non-wage expenditures
III. Developing an Effective and Sustainable Health System	<ol style="list-style-type: none"> 1. Restore priority services 2. Strengthen Ministry of Health as policy making and regulatory body 3. Devolve routine planning and management to

	sub-national entities
	4. Preserve solvency of Health insurance
	5. Improve health services: coverage, utilization and outputs
	6. Improve capacity – management skills, modern clinical practice standards

Source: The World Bank – Albania CAS FY99-01.

The new strategy followed by the Bank and the Fund in Albania very much relies on the *Growth and Poverty Reduction Strategy* being developed directly by the Albanian Government through extensive consultations with different components of the Albanian society. The strategy indicates a set of policy measures to improve living standards, and sets targets for social indicators, as well as mechanisms to measure and monitor poverty. The designed policies address governance and institutional capacity issues, health and education, the judicial and public administration reform, anti-corruption initiatives, social assistance, and rural poverty. Even though there are questions about Albania's capacity to ensure timely implementation of the strategy, the process can be of great importance in a country with very fragmented civil society, because it promotes participatory processes in the definition of the program and community-driven development projects.

I.4 AN OVERVIEW OF THE BANK PROGRAM

Since the start of the programs with Albania, the World Bank has approved 42 loans and has completed 22 projects. A quick picture of Bank's lending and main poverty indicators in Albania, compared to other countries is presented in Table. II.2 The data show a strong involvement of the Bank in lending activities in Albania, both as number of projects and disbursement levels. IDA commitments have reached 569.5 million dollars and disbursements 392.4 million dollars. This is quite a high rate of disbursement in comparison to other country programs. The implementation capacity, particularly procurement capacity has been low, but improvements have been made in most recent years through high supervision efforts and the allocation of large resources to the close monitoring of project implementation by the Bank. The current portfolio consists of twenty active projects for a total of 249.5 million. (Table II.3). Of these, 20 per cent supports agriculture, 44 infrastructure, 16 social sectors, and 20 technical assistance.

Most of the performance criteria and conditions of the programs have been met and the quality of Bank's loan portfolio has

improved since the 1997 crisis, when the share of projects rated unsatisfactory rose from 10 to 20 per cent and the share of those facing substantive risk from 30 to 65 per cent. Most of project objectives have been achieved. However, there is an issue of long run sustainability due to the instability of the region and the civil environment in the country. Currently one of the most important projects, the Power Transmission and Distribution project, is rated unsatisfactory in terms of development objectives, but satisfactory in terms of implementation progress⁶. A highly satisfactory Quality of Supervision rating has been given to major part of the portfolio and considerable measures are in place to ensure transparency, and accountability.

Table I.1 . Selected Indicators of Bank Portfolio Performance and Management.

Indicator	1997	1998	1999	2000
Portfol assessment				
Number of Projects Under Implementation	20	23	20	21
Average Implementation Period (in years)	2.77	3.03	2.73	3.02
Percent of Problem Projects by Number	25	21.74	10	14
Percent of Problem Projects by Amount	23.14	23.82	13.59	18.21
Percent of Projects at Risk by Number	30	21.74	10	14
Percent of Projects at Risk by Amount	29.69	23.82	13.59	18.84
Disbursement Ratio	16.4	20.71	21.41	8.71

⁶ Acknowledging the commitment of Government to implement the strategy in the power sector reviewed by donor community, on June 2001, IDA lifted the suspension of disbursements for the Power Transmission and Distribution Credit and 10.5 million dollars have been reallocated for financing the purchase of meters and for a comprehensive study regarding the future investment needs in this sector.

Portfolio Management				
CPPR during the year (yes/no)	Jo	PO	PO	PO
Supervision Resources (total US\$)	1,056.48	1,165.70	1,020.30	1,236.44
Average Supervision (US\$/project)	52.82	50.68	60.12	58.88

Source: The World Bank.

An interesting assessment of the structural reforms' progress in Albania, compared to other countries in South East Europe is given by the following table. As one can see, the development of banking system and the strengthening of legal and regulatory environment conducive to private investments in Albania (Enterprise reform index) remain relatively weak points and must be at the forefront of the agenda.

Table I.2. Progress Toward Reform in the Real Sector in the SEE Region.

	Private Share of GDP %	Enterprise Reform Index	Competition Policy Index	Privatization Reform Index	Banking Reform Index
Albania	75	2.0	2.0	3.0	2.0
Bosnia Herzegovina	35	1.7	1.0	2.0	2.3
Bulgaria	57	2.3	2.0	3.0	2.0
Croatia	60	2.7	2.0	3.7	2.3
FYROM	55	2.0	1.0	3.5	1.7
Romania	60	2.0	2.0	3.0	2.0
Average	59	2.2	1.9	3.1	2.1

EBRD Transition Report 1999. Indexes: 1 lowest , 4 highest.

As far as direct support to private sector is concerned, today the Bank Group has invested, through IFC, 47.5 million dollars in six operations, 31.5 million dollars of which are equity investments in projects such as Anglo-Albanian Petroleum, FEFAD, NCB, and Eurotech Cement. IFC strategy in Albania is focused on key strategic sectors, such as oil and gas, mining, banking, and telecommunications. IFC is also providing partial loan guarantees and technical assistance in reviewing the investment climate. They are also assisting in strengthening the insurance industry by improving the legal and regulatory framework. MIGA has also started to operate in Albania. However, its small exposure of only US\$8.6 million does not justify the great need for FDI and opportunities in the country. Political risk cover for commercial financing of productive industries has also been provided by an IDA *Private Industry Recovery Project*, approved by the Bank's Board on 1998. A more intense involvement of both the IFC and

MIGA in Albania is key for private sector development and for the overall economic sustainability of the World bank Group program.

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