

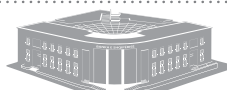
## 2. INTERNATIONAL DEVELOPMENTS

**(6) Global economic developments were and stable over 2017 H2.** The pickup in growth was broad based and synchronised across regions. Economic growth was driven by the favourable financing conditions and the continuation of stimulating policies; while oil price recovery contributed to boosting the economies of oil-exporting countries. Conditions in financial markets were favourable, notwithstanding the divergences among the monetary policies of main central banks. The European Central Bank continued to implement an accommodative policy supporting the regional economic growth, while Federal Reserve, Bank of England and other major central banks in developing countries have taken steps towards monetary tightening. Overall, global inflationary pressures, were subdued, but showed an upward trend occasionally, supported also by the recovery in oil prices.

**(7) Economic activity in advanced economies continued to expand firmly, while emerging regions showed considerable recovery signs.** Among advanced regions, the United States economy continued to grow positively over the period, driven by the good financing conditions and the strengthening of both domestic demand and investments. The inflationary pressures have remained low. Conditions in the labour market improved and the unemployment rate fell at 4.1%. In the United Kingdom, the economic activity recorded a modest growth in 2017 H2, after slowing down in 2017 H1. In emerging regions, China and India continue to lead the economic growth; meanwhile, the recovery of oil and primary commodity prices has boosted the economies of oil-exporting countries.

**(8) Economic growth in the euro area continued to be firm and balanced across regional countries.** All EU member countries recorded a positive annual economic growth over 2017 Q3, and this trend is expected to continue in 2017 Q4 as well. The activity is mainly supported by the increase in consumption and investments, as well as the growth of exports given a better situation of the global economic growth. Labour market conditions continued to improve, underpinning the increase in households' income and consumption. Unemployment fell at 8.7% at end 2017. Inflationary pressures, notwithstanding the upward trend at the end of 2017, remained subdued, with inflation rates below 2%. Given that, the European Central Bank continued to maintain the accommodative monetary policy, to support the economic activity of the region.

**(9) In euro area banking sector, lending has been gradually recovering.** Loans to enterprises and households grew firmly in most countries. This positive



trend noted since the beginning of 2014, resulted from the considerable fall of interest rates due to the ECB's accommodative policies and the recovery of credit demand. The pressure of increasing competitiveness and the decrease of the risk perception also boosted these developments. The European banks continued the efforts to clear and consolidate their balance sheets over the period. Nevertheless, the non-performing loans ratio remains high in certain countries, hence decelerating lending.

**(10) Global economy is expected to continue to grow positively and firmly in the medium term<sup>7</sup>, fluctuating around the long-term average.** The economic expansion in advanced regions and further recovery in emerging regions, supported by better financing conditions, the continuation of stimulating policies and oil price recovery shall underpin global growth. Inflationary pressures are expected to increase driven by the pickup of demand and the narrowing of unutilised capacities. *Risks to the global growth outlook*, overall, appear balanced in the short term. Nevertheless, the considerable growth in assets value in financial markets, given the rather low rates and premia, has driven to the increase of risk of values correction in the future. Also, low interest rates have urged the channelling of funds towards higher-risk investments, searching higher profits, by dampening the imbalances in the financial markets. Last, geopolitical tensions and protectionist policies in certain regions pose risk to global economy performance.

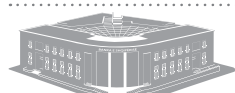
**(11) The forecast shows that the euro area economy will grow firmly in the next years.** Monetary policy pass-through in the real economy has facilitated the consolidation of balance sheets in economy. This is expected to provide space for further increase of consumption and expenses, by supporting the economic growth of the region. The labour market improvement and the low financing rates will provide also a positive support to the growth of the domestic demand and investments, while the global economy recovery will boost the external demand for European exports. *Risks to economic outlook in euro area*, overall, are assessed as balanced. Currently, they are considered to be more related with external factors, such as developments in real exchange markets, clarity on trade relations with the United Kingdom after "Brexit", or the potentially strained trade relations with the United States.

Table 2.1 Selected macroeconomic indicators for the U.S. and euro area

	GDP change (annual %)				Annual inflation (annual %)		Unemployment (annual %)		Gross government debt (as a % of GDP)	
	2017 Q3	2017 Q4	2017f	2018f	Sept'17	Dec'17	Sept'17	Dec'17	2017 Q2	2017 Q3
U.S.	3.2	2.6	2.3	2.7	2.2	2.1	4.2	4.1	103.1	103.8
Euro area	2.8	2.7	2.4	2.2	1.5	1.4	8.9	8.7	89.0	88.1
- Germany	2.7	2.9	2.5	2.3	1.8	1.6	3.7	3.6	65.9	65.1
- France	2.3	2.4	1.8	1.9	1.1	1.2	9.6	9.2	99.3	98.4
- Italy	1.7	1.6	1.6	1.4	1.3	1.0	11.1	10.8	134.7	134.1
- Greece	1.4	1.9	-	-	1.0	1.1	20.8	-	176.1	177.4

Source: European Central Bank, Eurostat, International Monetary Fund (f- IMF estimates, January 2017), BEA -Bureau of Economic Analysis). "-": no available data.

<sup>7</sup> According to IMF Outlook (January 2018) global growth for 2018 and 2019 by 3.9%.



(12) In Western Balkans, economic activity expanded further in 2017 Q3, but at a different pace across countries. GDP growth accelerated in Albania, Serbia, and Montenegro and it remained unchanged or towards slowdown in Kosovo, Bosnia & Herzegovina and Macedonia. The regional economic activity expanded by 2.8% over the period (y-o-y), mainly supported by private consumption and investments. Notwithstanding the economic growth, labour market conditions continue to remain challenging to all regional countries, particularly for generating new jobs. Except Serbia, unemployment was downward in the other regional countries in 2017 H2. Fiscal consolidation seems to have slowed down in some of countries, resulting in an increase of fiscal deficits compared to the previous year. Low inflation continued to remain a common characteristic of the region, reflecting low commodity prices and the stability of the exchange rate. In the banking sector, bank credit continued to increase positively and to support the regional economic activity. The growth of loans to households exceeded loans to enterprises across all regional countries. The major part of regional countries continued to reduce the non-performing loans ratio, partly due to the improvement in the regulatory framework addressing them and the mandatory write off from banks' balance sheets.

Table 2.2 Selected macroeconomic and financial indicators for Western Balkans

	GDP (real, % annual)			Unemployment (in %)		Sovereign debt (% of GDP)		Credit growth (%annual)		Non-performing loans ratio (in %)	
	2017 Q2	2017 Q3	2017f	2017 Q2	2017 Q3	2017 Q2	2017 Q3	2017 Q2	2017 Q3	2017 Q2	2017 Q3
B&H	2.9	2.9	-	20.5	-	37.8	-	5.1	6.4	11.1	10.8
Macedonia	-1.3	0.2	1.7	22.6	22.1	37.9	37.8	2.1	4.8	6.7	6.5
Montenegro	5.2	4.7	3.9	15.3	15.1	57.7	56.9	9.3	7.7	8.8	7.4
Kosovo	4.4	4.4	-	-	30.4	-	-	10.3	9.9	3.6	3.6
Serbia	1.4	2.1	2.0	11.8	12.9	65.7	64.6	2.9	-2.1	15.6	12.2

Note: "-": no available data.

Source: European Commission, f- forecast November, 2017.

## 2.1 HIGHLIGHTS IN FINANCIAL AND PRIMARY COMMODITY MARKETS

(13) Over the period, developments in global financial markets, overall, were favourable and firm, notwithstanding the deepening of political divergences across regions. Monetary policy decisions in advanced and emerging regions have addressed the economic performance of the countries. Thus, the ECB continued its accommodative monetary policy stance given the inflation undershooting, while the Federal Reserve undertook new steps toward tightening the monetary policy stance at the end of the year<sup>8</sup>. The Bank of England also changed its monetary policy direction, by raising its policy rate - at 0.5% - for the first time in the last 10 years in view of pound depreciation and inflation increase. The large economies also showed divergences. Hence,

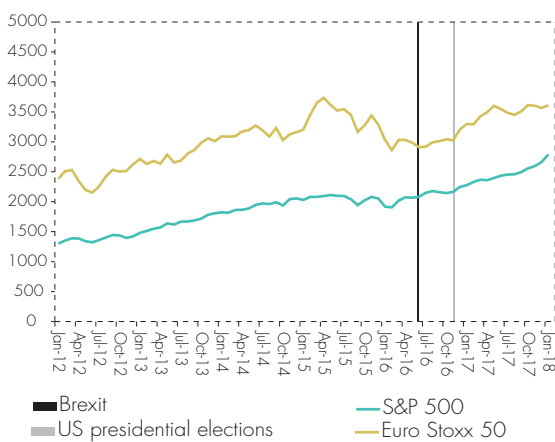
<sup>8</sup> In December 2017, the Federal Reserve raised the interval of the federal funds rate at 1.25% - 1.50%, and took steps to decrease its balance sheet.



China raised the interest rate to tighten the financing condition and limit lending, while the rest, like India, and some oil-exporting countries, central banks have further accommodated the monetary policy in view of the weak inflationary pressures. Notwithstanding these divergences, developments in financial markets have been optimistic and dominated by the confidence that the re-balancing of policies by the main central banks shall take place very gradually.

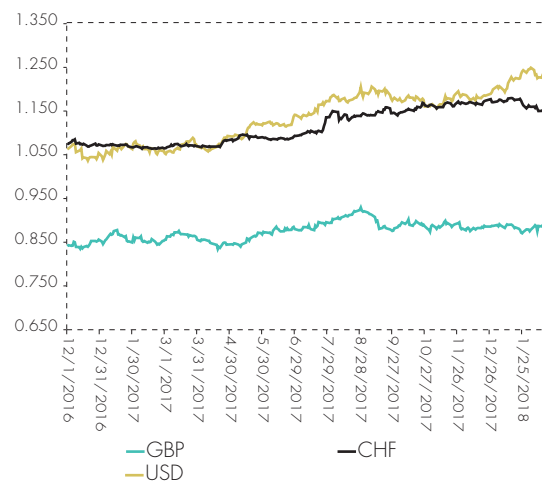
(14) The performance of values and rates in *advanced markets* has reflected the firm economic growth in these regions and the optimistic outlook for the future. Hence, the yield on sovereign securities in European markets, overall, have been unchanged, while in American and British markets they have trended up, throughout the period, driven by market expectations on the change of their monetary policy. In capital markets, developments were positive, characterised by increase of values, narrowing of spreads and fall of volatility. In *emerging markets*, the interest rates, overall, have been down, driving to a modest improvement in financing conditions and capital inflows. Equity prices in these markets have been down, supported by the expectations for a good economic outlook in oil and primary commodity-exporting countries.

Chart 2.1 Main indices in stock markets



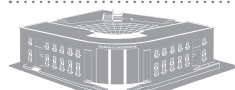
Source: European Central Bank.

Chart 2.2 Euro exchange rate against other currencies



Source: European Central Bank.

(15) Currency markets have broadly reflected the distinctions in the stages of economic cycle across countries and the expectations on the monetary policy stance. Hence, euro depreciated against the US dollar and the British pound and against the currencies of some of developing countries, over the period. On the other hand, the euro appreciated against the currencies of some advanced and developing countries, including the Swiss franc, Japanese yen, Chinese renminbi and a good part of European currencies outside the euro area.



(16) Oil prices shifted up over 2017 H2, driven by a set of both supply and demand side-factors. Over the period August - mid December 2017, gross oil prices increased by around 20%, standing above 60 USD/barrel<sup>9</sup>. This increasing trend has continued in the first months of 2018 supported by some factors, including the optimistic market expectations on the performance of the global economy, the extension of OPEC countries agreement on the cut of oil production quota, the political tensions in the Middle East and the adverse weather conditions in the USA at the end of the year. Risks on the further increase in oil prices are mainly related with the great potential of its production by the United States. Commodity prices have been down in 2017 H2, mainly driven by the fall on food prices.

## 2.2 DEVELOPMENTS IN FOREIGN BANKING GROUPS OPERATING IN ALBANIA

(17) The following table shows some main indicators of the financial statements of the parent banking groups operating in Albania, in relative terms, compared to the same period in the previous year.

Table 2.3 Highlights of foreign banking groups operating in Albania

Change (%)	Raiffeisen Bank International <sup>I</sup>	Intesa San Paolo <sup>II</sup>	Alpha Bank <sup>III</sup>	Piraeus Bank <sup>IV</sup>	National Bank of Greece <sup>V</sup>	Societe Generale <sup>VI</sup>
Assets	3.8%	3.0%	-7.4%	-18.0%	-19.5%	-5.9%
Credit	1.7%	3.1%	-2.9%	-6.0%	-5.8%	-0.3%
Deposits	4.3%	-1.3%	6.0%	6.0%	1.9%	-2.5%
Loan-loss provisions	-68.1%	-49.1%	-11.9%	-10.0%	21%	7.6%
Net profit	...	...	...	...	...	-27.6%
Operating income	4.0%	1.2%	4.5%	5.0%	0.0%	-25.4%
Net interest income	2.2%	-2.5%	2.0%	-5.0%	-5.0%	-
Net commission income	7.7%	5.5%	1.7%	55.0%	43.0%	-
Operating expenses	-0.1%	0.4%	-2.5%	-4.0%	-8.0%	6.1%
Net operating profit	10.7%	2.0%	-	-	...	-
<b>Ratios</b>						
Non-performing loans	6.7%	5.5%	37.3%	36.2%	-	4.4%
Net interest margin	2.46%	-	3.1%	2.73%	3.07%	-
Capital adequacy ratio	17.9%	17.9%	17.9%	16.6%	16.8%	17.0%
Bank's assets in Albania against the total group	1.31%	0.14%	0.91%	0.81%	0.42%	0.05%

<sup>I</sup> Report for 2017 Q3: <http://investor.rbinternational.com>

<sup>II</sup> Financial result for 2017: <http://www.group.intesasanpaolo.com>

<sup>III</sup> Financial result for 2017 Q3: <http://www.alpha.gr>

<sup>IV</sup> Financial result for 2017 Q3: <http://www.piraeusbankgroup.com>

<sup>V</sup> Financial result for 2017 Q3: <https://www.nbg.gr>

<sup>VI</sup> Financial result for 2017: <http://www.societegenerale.com>

Note: Note (...) shows pronounced change of this indicators (higher than 100%), in either positive or negative terms.

(-) shows not available data for this indicators in the releases of the relevant bank.

Source: Official websites of banking groups.

<sup>9</sup> Economic Bulletin, ECB, December 2017.



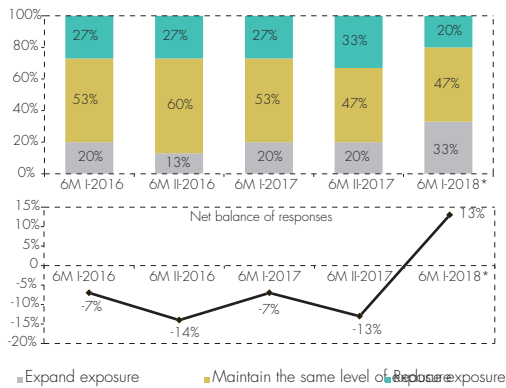
Indicators show a good capitalisation of all banking groups and an improvement of income level in some of them. The share of banks operating in Albania in total assets of the respective foreign banking groups remains low.

**BOX 1. SELECTED RESULTS FROM THE CESEE BANK LENDING SURVEY H2-2017 (EIB) AND THE POSITIONING OF ALBANIA**

**A. International banking groups operating in the CESEE region**

In the last survey of 2017 H2, banking groups operating in CESEE seem to be tilted towards a selective expansion in the region, in terms of their market positioning, market potential, and profitability. **Exposures at group level to CESEE region have reduced over 2017 H2, compared with 2017 H1** (the net balance of responses fell from -7% to -13%), while the share of banks that have increased the exposure has remained the same. On the other hand, the forecast of groups for the next 6 months appears optimistic; around 33% of them expect to increase exposures to the region, against 20% that expect their further reduction (See Chart 2.3).

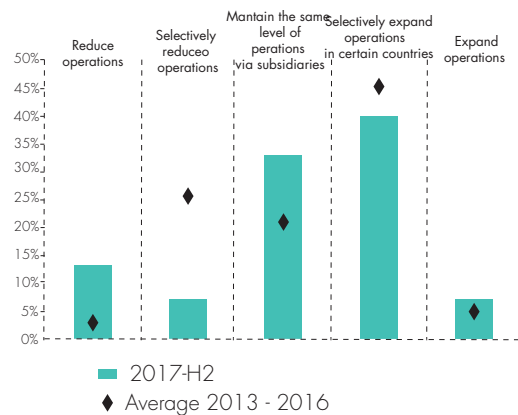
Chart 2.3 Groups' total exposure to CESEE (Share of responses in %)



Note: Net balance is calculated as the difference between the responses "Expand exposure" with the share of responses "Reduce exposure".

Source: European Investment Bank.

Chart 2.4 Group-level long-term strategies (beyond 12 months) in CESEE



Source: European Investment Bank.

Regarding the **long term strategies (beyond 12 months)**, (See Chart 2.4), banking groups appear to reassess their country-by-country strategies in CESEE region. Thus, as the results from the responses for 2017 H2 show, around 50% of groups declare to have a long-term expansion strategy (total of "selective expansion of activity in some countries" and "expansion of the activity" of the business in the region). On the other hand, around 20% of banking groups, where Greek banking groups are included, but not only, state that may reduce their activity in the region in the long term (total of "reduction of the activity" and "selective reduction of the activity").



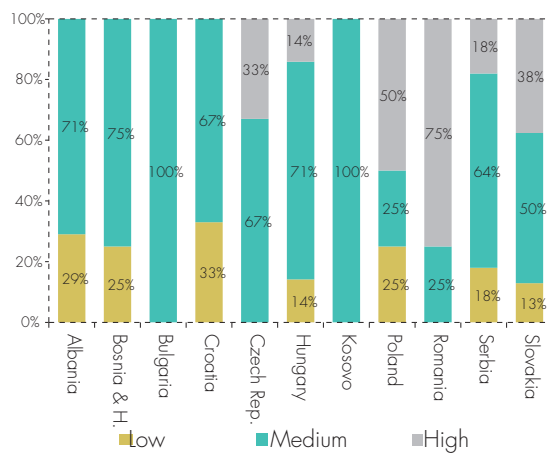
Overall, credit demand in the region is assessed as upward, while lending standards are eased over the surveyed period. Nevertheless, banks perceive that there is a notable gap in CESEE region between the high credit demand and the still contained supply. The major part of banking groups included in the survey assess that average profitability indicators of the region as a return on assets (ROA) and equity (ROE), are higher than the average of the group.

**B. Positioning of Albania in the CESEE region**

Most foreign banking groups (around 71%) that operate in Albania, for 2017 H2, see their market positioning as “fair”, while 14% see their market positioning as “optimal” (see Chart 2.5). On the other hand, 71% of the parent banking groups see Albania as a market with medium potential market positioning but comparatively with lower profitability than the group, also due to the cleaning-up of the balance sheets of banks that is still in progress (Chart 2.6).

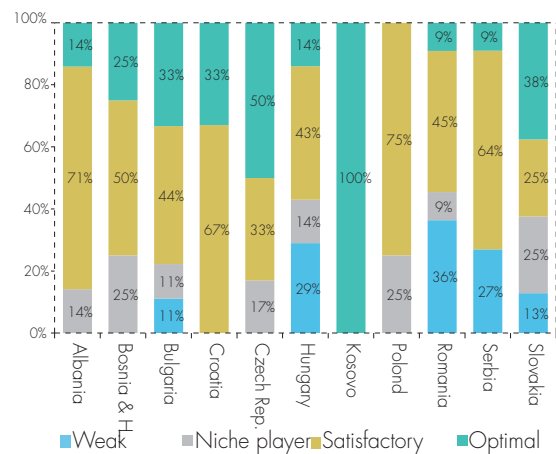
The majority of subsidiaries of banks operating in Albania are assessed to be less

Chart 2.5 Market potential in 2017-H2 (shares of responses, in %)



Source: European Investment Bank.

Chart 2.6 Market positioning in 2017 H2 (shares of responses, in %)



Source: European Investment Bank.

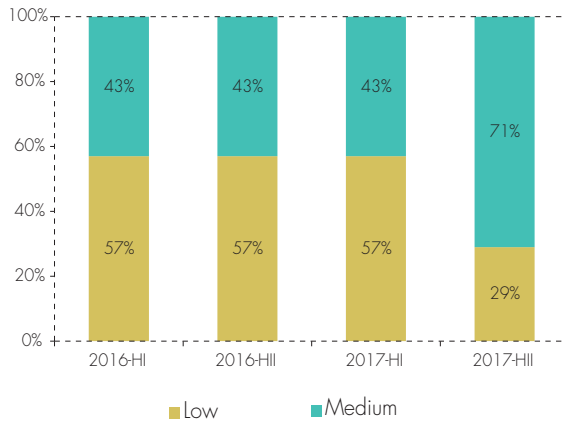
profitable than their parent banking groups in the last six months. The addressing of non-performing loans seems to have weighted negatively on banks profitability.

Currently, the satisfactory positioning of foreign banking groups, and their assessment for the market potential, suggest a relatively low willingness to expand in the Albanian market through either absorption or merger. On the other hand, the progress towards the cleaning-up of banks’ balance sheets is expected to drive to an improvement in profitability indicators and to be followed by the improvement of market potential.

Nevertheless, the comparison with the results of this survey in 2016 H2, where banking groups see Albania a limited potentially market and low profitability compared with the other part of CESEE region, it appears that banks’ point of view is somewhat more optimistic (Chart 2.7 and Chart 2.8).

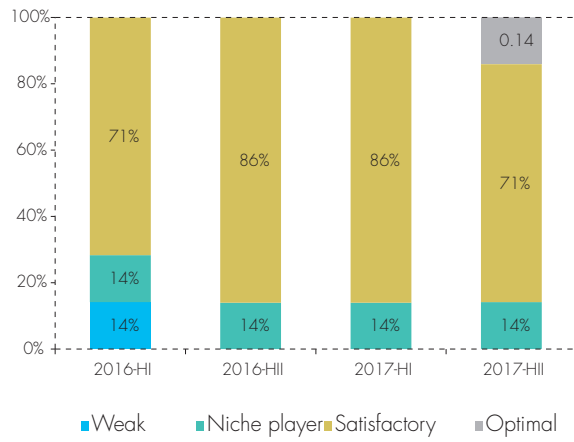


Chart 2.7 Albanian market potential in the last two years



Source: European Investment Bank

Chart 2.8 Banking groups positioning in the Albanian market



Source: European Investment Bank.

