

BANK OF ALBANIA BULLETIN

2010 H2

www.bankofalbania.org

If you use data from this publication, you are requested to cite the source.

Published by: Bank of Albania

Sheshi "Avni Rustemi", Nr.24, Tirana

Tel.: + 355 4 2419301/2/3; + 355 4 2419409/10/11

Fax: + 355 4 2419408

E-mail: public@bankofalbania.org

www.bankofalbania.org

Printed in: 370 copies

Printed by Adel PRINT

C O N T E N T S

Foreword	5
Editorial	
- New Monetary Policy Operational Framework: Targeting Short-Term Interbank Interest Rates	7
- The Credit Register	15
Addresses and Presentations by Bank of Albania's Administrators in Activities in Albania and Abroad	21
Papers	
1. Confidence Indicators, their Information Content and Synchronization with EU Countries Ermelinda Kristo	83
2. Balance of Payments Developments Merita Boka and Eglent Kika	101
3. Financial Intermediation Analysis Erjona Suljoti and Olta Manjani	105
4. Information on Recent Monetary Developments and Selected Economic Indicators in the Main Advanced and Central and Eastern European Countries Medvin Shehu, Priam Ramaj and Valentina Semi	119
Bank of Albania Bulletin News, July – December 2010	135
Monetary Policy Decisions	140
Legal Events, 2010 H2	141
Bank of Albania Management, 31 December 2010	151
List of all Entities Licensed by the Bank of Albania, 31 December, 2010	152
Publications issued by the Bank of Albania over 2010	156

FOREWORD

Dear reader,

Since 1998, you have been receiving a quarterly Economic Bulletin of the Bank of Albania. Through its analysis and assessments, this Bulletin has helped you be informed on the latest developments in world and domestic economy, impact on inflation and the monetary policy applied by the Bank of Albania to keep it under control. Moreover, the Economic Bulletin has featured a variety of documents reflecting the work and research of our central bank experts over the years.

In the framework of its public information policy, the Bank of Albania continuously and heedfully reviews and improves its publications. As of 2010, another publication is added to our list: Bank of Albania Bulletin, a half-early publication. This Bulletin comes to you following the restructuring of our Economic Bulletin, with the Monetary Policy Statement now published as a separate quarterly report.

At the beginning of the Bank of Albania Bulletin, you will find an “Editorial” with information on the biggest project, activity or engagement during the reporting period. Topics may range from monetary policy to bank supervision, from payments systems to European integration, from public education to national currency issue, depending on the multitude of duties and functions of the central bank.

Other rubrics in this publication inform the public on the activities, projects and aspirations of the Bank of Albania to develop and consolidate into a transparent and professional institution as it strives to achieve its goals.

We invite you to welcome and appreciate this publication!

EDITORIAL

NEW MONETARY POLICY OPERATIONAL FRAMEWORK: TARGETING SHORT-TERM INTERBANK INTEREST RATES

The Bank of Albania (BoA) has changed its operational philosophy in the interbank market. On 30 June 2010, the Supervisory Council adopted a decision on the change of BoA's monetary policy operational framework. As a result of this change, the BoA's operational target will be steering the short-term interest rates in the interbank market close to BoA's key interest rate, and curbing their fluctuations.

BOA'S PRIMARY OBJECTIVE

Macroeconomic stability is key precondition for ensuring a stable and long-term economic growth. Monetary policy is one of the main policies contributing in this regard. BoA, as the monetary authority of the Republic of Albania, has the exclusive right to formulate, adopt and implement monetary policy, whose primary objective is to achieve and maintain price stability. Achieving and maintaining price stability implies achieving low, but positive, inflation rates and maintaining them for relatively long periods of time. BoA's target for inflation is $3 \pm 1\%$.

The control of inflation is based on the control of other indicators, which, on one hand, have a strong relation with the inflation target, and, on the other, are under a more direct control of the BoA. These are the intermediate and operational (quantitative) targets.

Operational targets play a key role in the formulation and implementation of monetary policy. They link monetary authority's interventions in the money market and the intermediate and final monetary policy target, thus serving as the starting point of the monetary policy transmission mechanism.

Since BoA's inception as a central bank operating in a market economy, monetary policy was designed under the monetary targeting framework, in a floating exchange rate regime where the final objective – price stability – was achieved through a quantitative intermediate money target, the M3 money supply. Net domestic assets¹ NDA (ceiling) and net international reserves² NIR (floor) have served as operational targets for achieving the intermediate target.

Within this framework broadly based on monetarist theory, the monetary

¹ *Net Domestic Assets – the sum of BoA's claims excluding its foreign currency claims on non-residents.*

² *Net International Reserves – the difference between claims on non-residents and BoA's liabilities to non-residents.*

policy pursued by the BoA has evolved in response to the stabilization of the economy, higher banking system efficiency at home and deeper financial intermediation, thus becoming more flexible and employing market-oriented instruments. In view of enhancing its efficiency, these developments also called for the re-design of the operational framework for monetary policy. Ongoing analyses and discussions within the BoA identified the targeting of short-term interbank interest rates as the most appropriate approach to replace quantitative monetary targets. In June 2010, the BoA's Supervisory Council decided to change the operational target. It is formally expressed as:

"The operational target of BoA's monetary policy will be steering the short-term interest rates in the interbank market close to BoA's key interest rate set by its Supervisory Council, and curbing their fluctuations".

WHY WAS THERE A NEED FOR CHANGE? QUANTITATIVE TARGETS: WHY WEREN'T THEY APPROPRIATE ANYMORE?

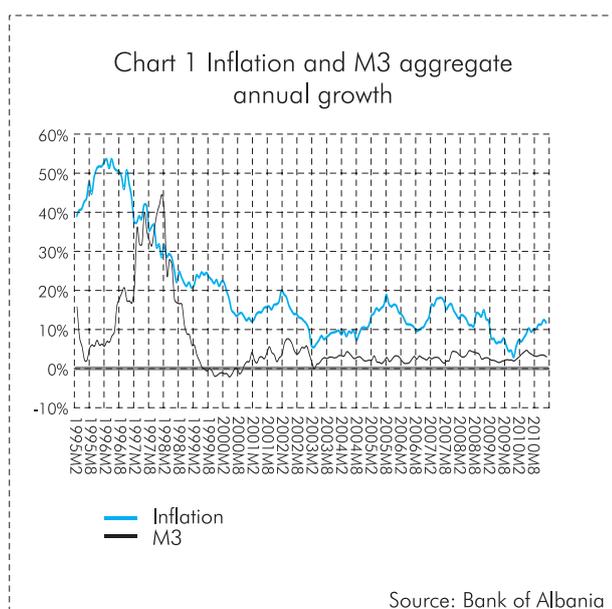
In parallel with the enhancement of analytical and forecasting capacities, the analysis of inflation at the BoA is now comprehensive. Inflation forecast, which is based on a wide range of economic indicators, has a primary role in the decision-making and formation of economic agents' expectations, thus preparing the ground for it to serve as an intermediate target for monetary policy in the future.

Although it is widely accepted that inflation in the long run is a monetary phenomenon, it is also argued that over the short and medium run, it may be also affected by a number of variables, which in turn has diminished the role

of monetary aggregates in monetary policy decision-making. In addition, the latter is almost entirely guided by the forecast of inflation over the medium run and the balance of risks to achieving the target. This monetary policy decision-making philosophy shifted money from its function as an exclusive intermediate target, thus making the NDA and NIR targets less useful in the implementation of monetary policy decisions. Besides being widely discussed within the BoA, these developments have also been formally communicated to economic agents through the Monetary Policy Document for 2009-2011 Period, adopted by BoA's Supervisory Council.

In order to meet the quantitative monetary targets, two primary conditions have to be met: a stable money demand and a strong relationship between money and the final target, inflation.

Although monetary policy-making based on quantitative monetary targets has for a long time had an incontestable performance, meeting both conditions



seems now insufficient to steer monetary policy decision-making based on this operational framework rightly³.

Empirical studies on the case of Albania show that demand for money is stable only over the long run⁴. While this finding has implications for monetary policy, it is however of little use for the operational aspect of monetary policy. The fact that the parameters of determining money demand do not provide sufficient accuracy in the short run, makes the forecast of optimal levels of M3 intermediate target and setting of operational targets in line with it, in order to meet the inflation target, hard.

Moreover, it results that money has no strong power to forecast inflation in addition to other variables, thus providing evidence for the weak relation between money and the monetary policy target. In addition, as shown in Chart 1, for quite some years, inflation volatility has been low, while money growth rates have fluctuated around a broad interval, thus making it hard to determine appropriate quantitative targets in view of achieving the final target.

The aforementioned concerns facing the Albanian monetary policy may be also well described in the light of other countries' experience with a similar monetary policy framework, according to which, particularly with the stabilization of inflation at low rates, monetary indicators lose their explanatory power, and eventually their forecasting power, for inflation⁵. Therefore, meeting a quantitative monetary target does not necessarily lead to meeting the inflation target. In addition, monitoring and controlling money becomes harder once the financial markets become more developed, while the signalling of monetary policy is more challenging for the central bank. On the other hand, the implementation of monetary policy through quantitative monetary targets generates excess volatility in interest rates, which in turn hamper the further development of markets.

Against this backdrop, keeping NDA and NIR as operational targets did not provide a flexible and adequate framework for transmitting monetary policy decisions to the economy efficiently anymore. In response to the need to improve BoA's operational framework and further enhance the efficiency of policy rate transmission, the quantitative targets were replaced by the short-term interest rates in the interbank market.

NEW OPERATIONAL FRAMEWORK – INTEREST RATE TARGETING

Central banks in developed countries and, in the recent years, central banks in developing countries have been targeting the short-term rates in the

³ This is broadly discussed in Fullani (2007), Kolasi and Themeli (2006), Ibrahim and Luçi (2005).

⁴ See Tanku (2006).

⁵ See Estrella and Mishkin (1996) for a more extensive analysis of the role of quantitative monetary targets in monetary policy.

interbank market for more than two decades. A similar operational approach does not necessarily relate to a pure inflation targeting regime. It is also considered optimal in the cases of a flexible monetary targeting regime, against a background of low inflation and an unstable money multiplier, or in the cases when the central bank makes decisions based on a number of indicators. Nowadays, there seems to be a broad consensus among academics and central bankers that the short-term interbank interest rate is an appropriate operational target for implementing the monetary policy.

Experience shows that this operational approach leads to lower interest rate volatility versus the use of quantitative monetary variables as operational targets⁶. By controlling the short-term interbank interest rate and allowing for the predictability of its changes through a clear monetary policy strategy, the medium and long-term interest rates – which are more important in the transmission of monetary policy – respond predictably to changes in short-term interest rates. In addition, the interest rate operational targeting is simpler to be comprehended by the economic agents and enables a clearer signalling of the monetary policy stance.

The BoA has paid increasing attention to the performance of interest rates in the interbank market, particularly in the last couple of years. Once macroeconomic stability firmed up and the financial market at home developed, and in view of the need for a more flexible monetary policy framework, placing the short-term interbank interest rates in the role of the operational target was a natural step.

WHAT INTERBANK RATE?

The choice of the appropriate operational target should be based on the fulfilment of these three general criteria: simplicity in measurement, controllability and predictability of influences on the final monetary policy target. In the case of the interest rate targeting, the first criterion is not appropriate to choose among the different interbank interest rates, since all interest rates that may be used are simple to be measured. Thus, the discussion is principally focused on the controllability and efficiency of its transmission to the final target.

The selection of the maturity of the short-term interbank interest rate that serves as an operational target may include a trade-off between the fulfilment of the last two criteria referred to above. It is generally considered that short-term interest rates are more easily controllable by the central bank and at a higher level of accuracy than in the case of long-term interest rates⁷. However, these interest rates play a more modest role in the transmission of monetary

⁶ One of the representative examples is the analysis of Fed's monetary policy by Bindseil (2004).

⁷ See Van't dack (1999) for an extensive analysis of the characteristics of the interest rate serving as an operational target.

policy, and perhaps an interest rate of longer maturity would result more appropriate to transmit the central bank's policy to the entire spectrum of the yield curve. On the other hand, concentrating on long maturities has costs in terms of the possibility to control the interest rate. Moreover, targeting interest rates of longer maturity versus interest rates of short-term maturity may give rise to higher volatility and provide room for speculative actions in the market.

The solution of this trade-off, at least in practice, is shown by the choices of other central banks, which, in general, focus primarily on short-term interbank interest rates. The characteristics of the Albanian interbank market provide another argument in favour of the use of short-term interest rates as BoA's operational target. Albanian banks are more active in the short-term borrowing market – perhaps due to the limited experience in forecasting the liquidity –, thus making it the deepest interbank market segment. It was therefore considered that BoA's steering of interest rates would be more efficient by targeting short-term interest rates.

HOW TO APPLY IN PRACTICE?

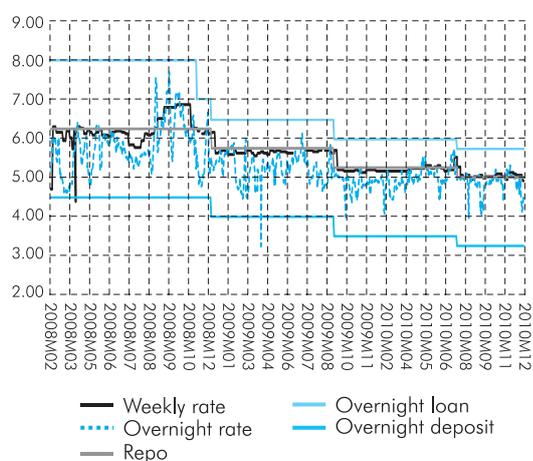
The change of the operational target is directly related to the way the BoA orients its money market operations, that is the liquidity-related operations in the banking system.

Simply put, at a given moment, some banks have excess of liquidity and some others suffer liquidity shortages, while the central bank fills the liquidity shortages or withdraws the excess of aggregate liquidity in the banking system. Based on the operational change, the BoA supplies the banking system with the required amount of liquidity at an interest rate that is close to the key interest rate set by BoA's Supervisory Council. The same logic is used in the case when the banking system has excess of liquidity. Until 30 June 2010, the central bank had no official commitment to provide the entire required amount of liquidity to the banking system, while banks had no formal guarantee that they would get the entire liquidity they needed. Subsequently, they were more conservative with one another or with the management of their liquidity. However, once the changes took place, the liquidity situation seems to have balanced (there is neither liquidity shortage nor excess of liquidity), liquidity at the aggregate level is close to zero and trading is oriented close to the key interest rate.

INTERBANK MARKET RESPONSE TO THE NEW OPERATIONAL FRAMEWORK

Overnight and one-week maturity interbank market segments are the most active. Transactions of 1-month or longer maturity are also present in this market but at lower frequency. Therefore, these interbank market segments are still of little significance for the transmission of monetary policy.

Chart 2 Short-term interbank interest rates, in %

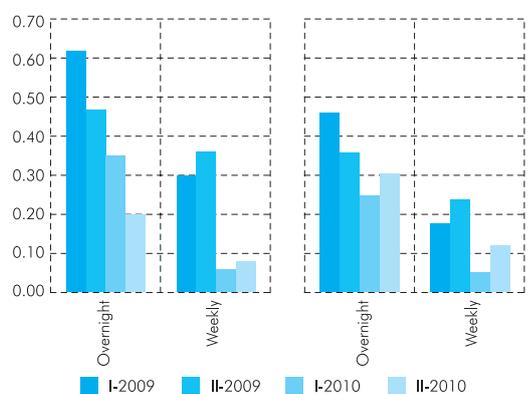


Source: Bank of Albania

Chart 2 shows the performance of interest rates of overnight and one-week maturity, the key interest rate and the interest rates on overnight loan and deposit starting from early 2008. As shown in the Chart, these interest rates, particularly that of overnight maturity, have been getting closer to the key interest rate and showing lower volatility.

Although it is yet too soon to analyze the effect of the new operational target, a comparison between the pre- and post-change period provides us an overview of the market response after the change took place. The spread between the interest rates and the key interest rate (see Chart 3, left-hand) is a simple way to measure the performance of monetary operations under the new framework. This indicator has been measured for four semesters covering the respective period of 2009-2010. As shown in the Chart, the spread between overnight and one-week interest rates and the key interest rate has been declining markedly. Although the operational target was officially changed in June 2010, it was preceded by an early preparatory work by the BoA. This also explains the beginning of the narrowing of these interest rates deviation from the key interest rate prior to the formal change of the operational target.

Chart 3 Deviation from the key interest rate (left-hand) and standard deviation (right-hand) of short-term interbank interest rates



Source: Bank of Albania

In order to measure the volatility of interbank interest rates, we have used their standard deviation, measured for the same period and frequency as the average absolute deviation (see Chart 3, right-hand). Although this indicator shows slightly higher values in the second half of 2010 versus the first half of the same year, in average annual terms, it is lower in 2010 than in 2009. In addition, it should be taken into account that a higher level of volatility is acceptable in periods following significant changes, until the market stabilizes fully in response to these changes.

INSTEAD OF CONCLUSIONS

Setting NDA and NIR as operational targets for monetary policy has been closely related to the early use of money as an intermediate target. The shift of money from this role and the evolution of other monetary policy framework elements naturally brought forth the need for a more flexible and efficient operational approach. In response to this need and in view of enhancing the monetary policy efficiency and transparency, the BoA decided to apply as its

operational target the steering of short-term interbank interest rates close to the key interest rate, and curbing their fluctuations.

Interbank interest rates targeting is an operational approach that finds vast theoretical support and which has proved successful in a number of advanced and developing economies. This operational framework allows for a better control of the short-term interest rate curve horizon, thus contributing to a more transparent monetary policy and clearer signalling of its stance. It also contributes to a more relaxed interbank market, lower risk premium and better management of short and medium-term liquidity in the banking system. A comparison between the performance of short-term interbank interest rates during the pre- and post-change period shows that they got closer to the key interest rate and were less volatile. It is worth noting however that these rates have been under BoA's special focus before their official change into the central bank's operational target took place.

It is also worth noting that this change does not affect BoA's monetary policy strategy, but only its operational framework⁸. In addition, this change does not imply money will be disregarded by the monetary policy decision-making. Monetary indicators will continue to serve as indicators that contain useful information for inflation, particularly in the long run, without necessarily being designated the target status. In addition, NIR will be under BoA's special focus in the conduct of monetary policy, but they will be more medium and long-term oriented.

⁸ For an extensive analysis of BoA's monetary policy strategy, see "Monetary Policy Document for the 2009-2011 Period", revised by BoA's Supervisory Council decision No. 43, dated 30 June 2010. The change of operational targets has been reflected in page 10 of this Document.

REFERENCES

1. Bindseil, Ulrich, 2004, "The operational target for monetary policy and the rise and fall of reserve position doctrine", ECB Working Paper 372.
2. Borio, C E V, 2001, "A hundred ways to skin a cat: comparing monetary policy operating procedures in the United States, Japan and the euro area", BIS Paper 9.
3. Estrella, Arturo and Frederic S. Mishkin, 1996, "Is there a role in for monetary aggregates in the conduct of monetary policy?", NBER Working Paper 584.
4. Fullani, Ardian, 2007, "Evolution and adoption of the Bank of Albania's monetary policy: A forward-looking vision and a call to be pre-emptive", in "Monetary Policy Strategies for Small Economies", pages 219-284.
5. Ibrahim, Fatos and Erjon Luçi, 2005, "A review of Albanian monetary targeting regime with insights into the future", in "Central banking in the time of integration" – proceedings of the Bank of Albania's Conference.
6. Kolasi, Gramoz and Erald Themeli, 2006, "The IT case in Albania. A tentative road-map for implementing IT in Albania", in "Round Table on Inflation Targeting 2", Bank of Albania, pages 15-37.
7. Tanku, Altin, (2006), "A është kërkesa për para e qëndrueshme në Shqipëri?" BoA's unreleased study material, 2006.
8. Van't dack, Jozef, 1999, "Implementing monetary policy in emerging market economies: an overview of issues", BIS Policy Paper 5: "Monetary policy operating procedures in emerging market economies", pages 3-72.

EDITORIAL

THE CREDIT REGISTRY

BACKGROUND - WORLD PRACTICE ON THE CREDIT REGISTRY

With a growing demand for loan products by households and businesses in the world, the first problems started to appear, from delays in payments of instalments to total failure to pay off the loan. The number of default clients started to grow progressively and complete and accurate information about their situation in the banking or financial system lacked.

Therefore, credit registries, now efficiently functioning in most countries of the world, were established to tackle lack of crediting information, centralise this information and generate it in a summarised format.

Interested parties, through a centralised electronic database of the Credit Registry, may generate summarised information about the borrower's and related persons' loan exposure, credit guarantor, relevant collateral, performance of borrowers in the system, etc.

There are two types of Credit Registries:

- Public Credit Registries, and
- Private Credit Registries.

Public Credit Registries are administered by public state institutions or supervisory authorities of not-for-profit entities. This is the case in France, Belgium and Latvia, whose Credit Registries are administered by the relevant supervisory authority.

Private Credit Registries, with different characteristics from public Credit Registries, are established by associations. Such credit registries are used in England, the Netherlands, Greece, etc.

World practice has shown that private and public Credit Registries complement and do not substitute each other. Their main difference is that participation in public Credit Registries is mandatory and stipulated in regulatory or legal acts, whereas participation in private Credit Registries is generally voluntary.

In the European Union (EU)¹, three countries operate exclusively with public Credit Registries, 13 countries operate only with private Credit Registries, and 10 countries have both public and private Credit Registries.

¹ Year 2009.

In the U.S., the private reporting industry identifies three major providers of credit information: Trans Union, Equifax, and Experian.

The first Credit Registry in the world was established in the U.S. in 1830 as a result of information asymmetry in the markets. The 170-year history of the Credit Registry in the U.S. has contributed to the development and adoption of this system in accordance with economic or technological developments of the time. Meanwhile, the generation of borrower's report for clients was a much later development in the U.S., i.e. the 20th century. Furthermore, the EU legislator continues to pay particular attention to the personal data protection component in reporting as compared to the U.S. in this regard.

Most industrialised countries, such as the U.S., Canada, and EU countries, seek to have broader systems of information exchange than the developing countries. In industrialised countries, this is due to a number of reasons, such as high crediting volume and intensity, stronger legal and regulatory infrastructure on information exchange, consumer and personal data protection, more sophisticated communication technology, higher mobility of borrowers, etc.

ADVANTAGES OF CREDIT REGISTRIES IN FINANCIAL MARKETS

Many scholars state that, globally, many banks are transitioning from a "collateral-based" to a "more information-based" crediting system. Hence, recently more emphasis is put on verifying and enriching the information in public or private Credit Registries in order to have a more comprehensive and well-supported judgement.

The Credit Registry provides the interested parties with aggregate information on credit exposure for a borrower, exposure of a party related to the borrower, information on relevant collaterals, information on a borrower's performance in the system, etc. This information is translated into economic terms as "moral collateral"; therefore, everyone is interested to have positive collateral.

Subsequently, the Credit Registry offers advantages for all stakeholders; to mention a few, it:

- reduces information asymmetry between lenders and borrowers;
- provides lenders with the possibility to assess the risk for each borrower more carefully and improve portfolio quality;
- minimises the problem of "selecting the bad borrower" and may reduce crediting costs for a good borrower;
- enhances access of various legal or natural persons to borrowing and, as a result, increases the crediting level of the institution/bank;
- contributes to reducing operational costs and, consequently, increasing profitability through including information from the registry into the credit score for each borrower.

ALBANIAN PRACTICE AND NOVELTIES IN 2010 H2

Pursuant to Law No. 8269, dated 23.12.1997 "On the Bank of Albania" and Law No. 9662, dated 18.12.2006 "On banks in the Republic of Albania", the Credit Registry at the Bank of Albania started to function on 3 January 2008. The establishment of this Registry was first envisaged in the law "On banks in the Republic of Albania" of 2006. The old law of 1998 did not stipulate this function.

In Albania, the Credit Registry is administered by the Bank of Albania, an institution of the state/public administration, and functions as a public service. Thus, it is not a service offered by an association/community of banks or any other specialised company, as is the case in some countries.

Until November 2010, only the banks and branches of foreign banks were contributors or data reporters to the Credit Registry.

One of the objectives of the Bank of Albania was to involve other credit institutions in order to have complete information about banking and financial system borrowers in the Republic of Albania. The use of this information for a more cautious credit process would minimise the risk arising from the lack of information. As the Credit Registry serves the Bank of Albania in its supervisory role, the inclusion of other reporting institutions adds to its efficiency in supervision. The process underwent a number of important stages with the inclusion of not only new reporting institutions but also the Supervision and IT departments of the Bank of Albania.

Given its importance, significant time was committed to data verification. Data accuracy and integrity in compliance with the envisaged criteria of the Credit Registry were prerequisites for the continuation of the project.

Moreover, the secondary legislation governing the functioning of the Credit Registry was reviewed in parallel. More specifically, on 13 October 2010, the Supervisory Council of the Bank of Albania approved the Regulation No. 67 "On information content and functioning of the Credit Registry at the Bank of Albania", as well as Instruction No. 68 "On procedures to issue borrower's report and review of Credit Registry data".

Among the main issues addressed in the revised acts, we may point out the content expansion of the term "data reporter", which, in addition to banks and non-bank financial institutions licensed by the Bank of Albania, shall include other financial institutions according to an agreement between the Bank of Albania and these institutions and/or their supervisory authorities. This is the case of unions of savings and credit associations, as representatives of their member savings and credit associations. Moreover, we may list the content expansion of the term "credit" and "data reporter", alignment of the terminology with the new law "On protection of personal data", and regulation of some issues stemming from the three-year functioning.

The new regulation underlines that documents or information generated by the Credit Registry for data reporters do not aim to analyse or assess a borrower's credit risk, but merely to provide the reporter or the requestor with a summary of the borrower's exposures and performance in the system. This system reflects what entities report in it and reporters use this information, as the case may be, for a client performance assessment during the credit process.

Upon completion of the testing phases and entry into force of the secondary legislation, on 19 November 2010, five new institutions started their live reporting to the Credit Registry at the Bank of Albania, namely:

- Fondi Besa sh.a.;
- Opportunity Albania sh.a.;
- Vision Fund Albania sh.p.k.;
- Union of savings and credit associations; and
- Jehona - Union of savings and credit associations.

Subsequently, the total number of active reporters to the Credit Registry in Albania is 22².

The new reporters enriched the database of the Credit Registry with additional and valuable information thus taking the number of reported credits to 577,451, of which 318,719 are active. In other terms, it means by about 11% and 18%, respectively.

INFORMATION REPORTED TO THE CREDIT REGISTRY AND BORROWER'S REPORT

Data reporters submit information about their borrowers' credits, overdrafts, credit cards, letters of credit, etc., to the Credit Registry at the Bank of Albania. In addition, they report detailed information about the guarantor or other persons related to the borrower as well as information on the pledged collateral.

This is a detailed report with identification details such as first name, family name, father's name, date of birth, Tax ID Number, etc., as well as data on borrower's exposure to the banking and financial system such as approved amount, outstanding amount, past-due amount, credit disbursement date, currency, classification of the borrower by risk category, etc. In addition, the report by the institution includes information on the borrower's status, i.e. natural or legal person, industry sector and the purpose of the credit.

The reporters enter daily new and paid-off loans and update monthly classification by credit risk categories. The Credit Registry has positive and negative information about the borrower. Retention period for these data at the Credit Registry is five years.

² Including the Bank of Albania for credits to its personnel.

The credit approval process requires high cautiousness in assessing an applicant's creditworthiness. Through the information received from the Credit Registry, the reporter checks, in real time, the client's exposure and his history and classification or performance in the banking and/or financial system.

The time component is equally important. The credit institution is now able to save time in the decision-making process. For example, the time an institution needs to obtain an attestation is relatively "expensive" in the credit market.

With the new opportunity to read the history of a borrower's status (the latest 24 months) with a certain reporter, another reporter, where this borrower may have applied for a new credit, may have detailed information on the applying borrower's performance; whether he has delayed payments, these delays are still pending, situation has improved or the credit has been paid off, etc.

Moreover, the reporting institution is able to assess a borrower's displayed honesty when declaring credits received by other institutions. The institution crosschecks information received from the Credit Registry with the declaration of the potential client and, if it does not match, the applicant's honesty is taken into account when making the decision.

We should underline that only the Bank of Albania has the right to provide interested parties with a borrower's report for a 500 Lekë fee and upon compliance with the documentation requirements specified in the relevant regulation and instruction. Any natural or legal person, a person related to them, an heir, or a proxy may request the generation of a borrower's report and may receive it in person in accordance with the timeliness established in the regulation. This report, in addition to the above-mentioned information, which is also accessible by the reporter, features the name of the bank/non-bank institution the client has a certain exposure to. In the borrower's report received from the Bank of Albania, the borrower reads a summary of his obligations in the banking and financial system. Furthermore, any client, whether a legal or a natural person, is entitled to request, free of charge, the revision of his borrower's report in the case of potential claims on its accuracy. Then the credit registry office verifies the claims and, at the end of the process, delivers the revised or non-revised report, accordingly.

The Bank of Albania may use the information generated by the Credit Registry for statistics and detailed analysis used mainly for supervision and optimised credit risk management by entities it supervises.

The Bank of Albania Supervision and IT departments were part of a detailed analysis for the revision of the query fee. Decision No. 69 of the Bank of Albania, dated 13.10.2010, sets out the current applicable fees of 100 and 50 Lekë per query, respectively by bank and non-bank reporters. Former fee was 110 Lekë per query.

BANK OF ALBANIA BRANCHES, PART OF THE GENERATION OF BORROWER'S REPORT

The branches of the Bank of Albania assist persons who reside out of Tirana and request a borrower's report. Currently, legal or natural persons address the Bank of Albania branches to request a borrower's report. The generation of the information from the Credit Registry, as stated above, reduces a bank's time to make a decision on a credit. This is also an advantage for the applying borrower because his request is processed much faster and it saves not only time, but also credit costs. He does not have to obtain paid certifications from different banks to attest his obligations or their lack thereof to the bank where he applies. The applying borrower saves additional travel costs and time for obtaining a borrower's report at the Bank of Albania's Head Offices in Tirana.

ADDRESSES AND
PRESENTATIONS BY
BANK OF ALBANIA'S
ADMINISTRATORS IN
ACTIVITIES IN ALBANIA
AND ABROAD

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

At the Joint Press Conference with the IMF
Mission and the Ministry of Finance
July 14, 2010

Dear print and visual media representatives,

The visit of the International Monetary Fund Mission was characterised by fruitful and intensive discussions. They focused on the recent economic developments at home, their perspective in the near and distant future and the role of structural and macroeconomic policies to encouraging and ensuring the sustainable development of the country.

At the end of these discussions, we conclude that we share a common opinion on the role and importance of prudent policies, which should have at their heart the maintenance of the underlying economic balances, as an essential precondition for the stable and long-term growth.

Likely positive is the fact that the principal decision-making institutions remain committed to take concrete and timely steps to ensure this development.

The Bank of Albania has already adopted this position with transparency, as guidance to its decision-making process in the area of monetary policy and banking supervision. Its explanation has made up the essence of our communication with the other players of the economy and the public at large.

Let me now touch on the issues discussed during these days and summarise the opinion of the Bank of Albania in this regard.

The economic developments of the recent months offer encouraging signals, but they also show some weakness of the Albanian economy and the trade-offs that policy-makers should acknowledge to accomplish their targets.

The Albanian economy performed in line with our projections in the first half of 2010, being characterised by a positive, but slow, growth of the economic activity.

This growth is considerably grounded on the quick increase in exports as a reflection of the recovery of the world economy, the more competitive position of the exchange rate, and the efforts of businesses and industries operating in this sector to find new markets and use their competitive advantages.

On the other hand, domestic demand slowed down, mainly reflecting the still high uncertainty and the difficulties in financing the economic activity. As regards to the underlying balances of the economy, this period has been

followed by controlled and downward inflationary pressures, as well as correcting trends in the external position of the country.

The economy's financial soundness has improved, confidence in the banking system has recovered and the risk premium has been declining. These general trends are expected to persist in the period ahead.

Economic developments during the first half of the year have called for the need to review the fiscal policies and projections for the rest of the year. The realization pace of public revenues and the need to preserve the fiscal sustainability and public confidence called for measures that guarantee the control of budget deficit and public debt.

Making continuous calls for measures, the Bank of Albania considers the envisaged fiscal measures in the revised budget as the right step in this regard.

The realistic management of the fiscal situation and the adoption of a prudence-type philosophy in the 2010 budget implementation are necessary to guarantee long-term fiscal sustainability and strengthen macroeconomic balances.

Among others, a lower pressure of the public sector on the domestic money markets enables more adequate conditions for the private sector lending through the reduction in the risk premium and the control of long-term interest rates.

The Bank of Albania remains willing to further support these developments with other monetary policy steps that will aim at the transmission of a prudent monetary stimulus to the economy. In parallel, we will make due efforts for the banking system to transmit this incentive timely and successfully, thus augmenting the lending to the private sector.

Finally, allow me to emphasise that the current situation and the future developments are expected to remain positive, but they however call for due attention in order to avoid the possible risks that may hit the economic stability and threaten the long-term growth potential.

Albania's external position will particularly remain the focus of our attention. In the short-term, it measures and conditions the economic incentives that may be successfully absorbed by the Albanian economy. In the long-term, we reiterate our call that the encouragement of foreign direct investments or other forms of long-term capital inflows is the right path for the long-term development of the country. Along with domestic structural reforms, public authorities should pay an increasing attention to this objective in order to release the development potential of the Albanian economy.

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

At the Press Conference on the Monetary Policy Decision-Making of the Supervisory Council of the Bank of Albania
July 28, 2010

At its meeting of 28 July 2010, the Supervisory Council of the Bank of Albania analyzed and approved the Monetary Policy Report of the second quarter of 2010. After scrutinizing the latest economic and financial developments at home, the future outlook and the expected risk balance, at the end of discussions, the Supervisory Council of the Bank of Albania decided to cut the key interest rate by 0.25 pp. Following this decision, the interest rate on the repurchase agreements of one-week maturity is 5%.

Economic and monetary developments of the first two quarters of 2010 were by and large in line with Bank of Albania's forecasts. Economic activity posted positive growth though at decelerated rates.

The inflationary pressures have been downward and the external balances of the Albanian economy have recovered. The financial markets were provided a breathing space and featured lower risk premium, improved liquidity figures, downward interest rates, and relative exchange rate tranquillity. The period ahead is expected to feature similar characteristics.

The performance of the Albanian economy may be considered as positive, particularly when put in the context of the developments in global economy and the regional countries, and considering the challenges faced over this period. The latter represented a tough test for the sustainability of the Albanian economy, both at a macro and micro level, and in terms of the institutional and political capacities of economic management.

However, when viewed elaborately, economic and monetary developments in the first half of the present year provide numerous shadings for their interpretation. The Albanian economy still suffers the low domestic demand and activity financing-related concerns. Economic growth and economic development are not balanced yet for all the sectors of the economy. They have mainly relied on foreign demand rather than domestic demand and they attest to a more dynamic performance of industry and services and slower performance of agriculture and construction.

In addition, economic growth has been coupled with slower labour market and employment figures, hence increasing the non-utilized human and capital capacities of the Albanian economy. On the other hand, economic performance has confirmed the importance that the preservation of macroeconomic balances has to our country's stable and long-term development, as well as the need for the contribution of all economic players to guaranteeing them.

These messages, which constitute the main topics of this quarterly report, will be further elaborated below.

The global context that outlined Albania's economic development over this period has recovered, however the financial markets and investor sentiment remain highly volatile.

Global economy continued to recover in the second quarter of 2010, being largely driven by the rapid economic growth in developing economies and the fiscal and monetary stimulus in advanced economies. The euro area is showing signs of stable growth but our main trading partners, Italy and Greece, are performing less positively. Despite the higher demand, the worldwide negative output gap has yielded low inflationary pressures, which are expected to remain so in the medium run as well.

However, this positive setting is still incomplete as long as unemployment remains high in the majority of countries. Public debt figures are weighed down further by the fiscal burden contracted as a result of the high-cost government measures undertaken over the last two years to fuel the economy, while the fiscal room has narrowed down substantially.

Concerns over fiscal sustainability, particularly in some euro area countries, have been also reflected in the performance of financial markets, which featured higher risk premium and elevated profit margins.

Against this global background, official statistics show that the Albanian economy has experienced a rebound in growth. Following the decline of GDP in the last quarter of 2009 and the weak economic activity in the early months of 2010, the available data on the real and monetary sector suggest that the Albanian economy posted positive growth rates in the first half of the present year.

According to INSTAT's preliminary data, GDP grew 2% y-o-y in the first quarter of 2010.

The growth in foreign demand was reflected positively in the performance of industry, which grew 27.5% for this period.

On the other hand, the slower domestic demand was manifested in moderate growth rates of services and progressive contraction in the construction sector.

The more positive performance of GDP in the first quarter of 2010 finds more support in the qualitative data. Economic Sentiment Indicator particularly increased 4.6 points versus the previous quarter, though remaining well below its long-term average.

Along with other indirect indicators, like credit growth trend and the higher pace of budget revenue, business and consumer expectations for the second

quarter of the present year suggest that economic growth posted similar rates to the first quarter.

In absence of timely data on the performance of demand components, our analyses based on quantitative and qualitative indirect indicators suggest that domestic demand has been affected by the decelerated consumption and decline in investments, as well as the lower fiscal sector's contribution.

On the other hand, the higher foreign demand and the improved terms of trade have been reflected in considerably higher exports and their elevated contribution to aggregate demand.

Consumer spending was contained in the first half of 2010. The decline in consumer loans and remittances, the lower increase of wages, the lower growth in the imports of consumer goods, the low consumer confidence, and the higher household savings trend attest to lower growth rates of private consumption over the course of this period. The latter was affected by the slower growth rate of disposable income, the restrained financial resources, a more conservative consumer behaviour against a background of elevated uncertainties over the future, and the slower employment figures.

Private investments were downward in the first half of 2010; however their negative contribution was lower than in the second half the previous year. This performance owes to a large extent to the low capacity utilization in economy. In addition, banks' tight lending terms have discouraged the demand for loans.

However, the latest developments, like the growth of business demand for investment loans and the increase of imports of intermediate and capital goods provide positive signals for the possible recovery of this demand component.

The public sector continued to contribute positively to the growth of aggregate demand in the first half of 2010. The government ran an expansionary fiscal policy, but rather more moderately relative to the previous year. Budget deficit, albeit narrowed 36% y-o-y, was pronouncedly higher than the projection. Budget expenditure is 4% lower than in the first half of 2009. The annual growth rates of current expenditure slowed down to 7.1%, whilst public investments declined 33.5%. Against a background of slow economic performance, fiscal revenue grew at low historical rates, 3.3%.

The Bank of Albania considers the downward revision of budget deficit and public expenditure as a positive and required step.

Guaranteeing fiscal sustainability, lowering the risk premium associated with it, shoring up public confidence, and providing room for greater private sector access to financial markets, are some of the key elements that enabled the further easing of the Bank of Albania's monetary policy, hence preventing a plausible sterilization of our actions related to the interest rate.

However, in order to maintain appropriate parameters of deficit and public debt figures, fiscal consolidation should progress beyond the actions undertaken in the short run. Fiscal sustainability needs to be addressed in the future through the adoption of a clear fiscal rule that should serve as a guide to and determinant of fiscal policy behaviour in the medium run and beyond.

The growth of foreign demand and the more favourable exchange rate fuelled our exports, which grew 62% in the first five months of 2010. In parallel, the weak domestic demand has led to a low annual increase of imports, hence causing the balance of trade deficit to narrow 16.2%.

Consequently, net exports provided a more positive contribution to aggregate demand. They also led to the continuous correction of the current account deficit, hence stabilizing the national currency further. The downward correction of the current account deficit by 2.7 pp of GDP provides an encouraging signal for the sustainability of Albania's external position. However, net financial inflows into the capital and financial account reduced 62.9% y-o-y in the first quarter of 2010. In addition, remittances, which make up a major source of trade deficit financing, are down 6.7% y-o-y.

Both these concerns re-accentuate the fact that the external position of the Albanian economy remains a structural weakness that calls for further correction.

Foreign direct investments, which grew 25.8% in the first quarter of 2010, represent the safest source of current account deficit financing. They need to be further boosted with attractive policies for foreign investors and structural reforms in the Albanian economy.

Annual inflation marked 3.2% in June. The slowdown in annual inflation, which commenced in March this year, was triggered by the low demand-side pressures, the lower agricultural products' prices and a more stable exchange rate.

Against a background of non-utilized capacities in the labour and capital markets, the low core inflation rates attest to the low inflationary pressures balance. The contracted demand will determine the downward inflation pressures in the period ahead, whilst the performance of monetary indicators shows weak inflationary pressures of a monetary nature.

As expected, supply-side shocks on consumer prices were transitory and did not affect economic agents' expectations of inflation, which remain well-anchored around the Bank of Albania's target. Price stability has been achieved as a result of an adequate monetary policy decision-making, though amid substantial uncertainty over the future prospects and absence of timely statistical data. Over the stated period of time, our monetary policy was stimulating, maintaining low interest rates and injecting the required liquidity and at well-suited maturity terms, in order to boost activity in the financial markets and lending to the economy.

In response to this policy, the interest rates in the interbank market were stable, reflecting largely the stable liquidity position in the system, while long-term interest rates maintained a downward trend as a result of lower risk premium. In the primary market, Government security yields of all maturity terms continued to decline in the second quarter. In addition, this period featured further growth of banking system deposits and their time-related shift to time deposits. Once household savings placed in the system increased, the interest rates on deposits showed a downward tendency.

On the other hand, private sector lending continues to post low growth rates despite the improved liquidity figures and the lower activity financing costs. The annual growth of private sector lending averaged 9% in the second quarter of 2010.

The credit market continues to feature volatile interest rates and tight lending conditions. However, the latest months' developments show positive signals, particularly in terms of the rather higher credit growth rates, its greater orientation towards supporting investments and the recovery of foreign currency lending to economic units that enjoy natural hedge against exchange rate risk.

The Bank of Albania has been promoting this performance and will continue to do so, and encourages the banking system and borrowers to work harder in finding effective forms, instruments and practices that fuel credit.

Today's decision-making of the Bank of Albania reflects a comprehensive analysis of the economic and financial developments that have been characterizing the Albanian economy in the recent months, the developments in the region and broader, the balance of risks, and future forecast and expectations.

The Bank of Albania believes that the banking system will transmit this decision to the economy timely and at the right intensity. The growth in deposits, the banking system's liquidity position and the downward Government demand provide real room for greater orientation of funds to private sector lending.

The Bank of Albania will also pay due attention to foreign currency intermediation by the banking system. The performance of foreign currency-denominated deposits and a wide array of other developments provide a safe ground for their channelling into the economy at a lower cost. This will be followed up closely in the remaining of 2010 and beyond.

The Bank of Albania considers that the monetary conditions and the demand-supply ratios in the major markets are well-suited to maintain price stability in the medium run. Our monetary policy will continue to be prudent in view of meeting the inflation target and maintaining macroeconomic stability.

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

At the Press Conference on the Monetary Policy Decision-Making of the Supervisory Council of the Bank of Albania
August 31, 2010

At its meeting of 31 August 2010, the Supervisory Council of the Bank of Albania analyzed and approved the monthly Monetary Policy Report. After considering all the information available for the latest economic and financial developments at home and their future outlook, at the end of discussions, the Supervisory Council of the Bank of Albania decided to leave the key interest rate unchanged at 5.00%.

The available data about the global economy confirms the progressive recovery in the economic activity. The stimulating monetary and fiscal policies have affected the increase of demand for goods and services and the expansion of trade activity. Survey results and future forecast suggest further improvement of economic indicators, signalling that the global economy will continue to strengthen. The inflationary pressures at a global level remain contained and central banks' interest rates continue to hit record lows. The financial markets featured high volatility in interest rates, financial products' prices and trading volumes.

On the one hand, this volatility has reflected the positive signals deriving from the real economy and the encouraging stress-test results of large banks; and on the other hand, the uncertainty arising from the increasing levels of public debt. At a political level, the debate characterising the private and public economic authorities is the definition of the due size and duration of macroeconomic stimulus. The response to the economy's support dilemma, without prejudice to the risk premium and its long-term balances, will considerably condition the performance of the global economy and Albania's short and medium-term growth perspectives.

Due to the recovery of demand, raw material prices continued to manifest an upward trend during the recent months. Wheat prices in particular hit a record high in the world markets in August, following the fluctuation of supply and demand ratios and the restriction of exports from one of the main producing countries. Their pass-through on Albania's headline inflation is expected to be weak, but it will remain subject to monitoring during the months ahead.

The Albanian economy continued to be characterised by the gradual improvement of economic indicators, confirming an increasing activity – but relatively slow. Official statistics reveal positive growth rates in the first quarter of the year, whereas confidence survey results and other indirect data suggest the persistence of these rates in the second quarter as well.

The economic activity at home has been supported by the growth of foreign demand and Albanian exports, whereas domestic demand has recorded slower growth. This performance has been reflected in a sharper increase of industry and services sector, whereas construction and agriculture have provided a low contribution to economic growth. In addition, the Albanian economy suffers non-utilized capacities and low inflationary pressures arising from the domestic demand. The monetary stimulus resulted adequate to accommodate a growing economic activity but without creating excess liquidity. In the presence of anchored inflationary expectations, this economic environment helped absorb the shocks on inflation derived from supply-side factors. Consequently and in line with our expectations, inflation has been waning during 2010. CPI annual inflation pointed to 3.4% in July. This inflation rate owes mainly to the upsurge of administered and basic prices in the international markets, and the depreciation of the domestic currency. These supply-side factors are expected to have a transitional impact on inflation, thus not being translated into stable inflationary pressures.

This dynamic has conditioned and will continue to condition the performance of inflation in the period ahead. In absence of unexpected supply-side shocks, the projections of the Bank of Albania set the annual inflation rate close to the central bank's 3% target in the medium run.

Private consumption has provided a positive contribution to the economic activity during the second quarter.

This performance is confirmed by the higher growth rate of tax income, which in turn provides an insight into the level consumption in economy, the growth of consumer goods' import, and the improved consumer confidence indicators. The generally sound financial balances of Albanian households allow for a quick response to the improvement of the current climate and the macroeconomic perspective, rise in disposable income, and the decline of uncertainty. On the other hand, the possibility of households to finance their consumption through banking loan results problematic as long as their access into consumer and mortgage loans is decreasing.

Private investments are gradually recovering their upward paces, but at markedly lower levels than in the previous periods. The more positive business confidence climate, the increasing support with banking loans, the higher capacity utilisation in economy, and the increase of capital and intermediate goods' import suggest that the level of private investments has increased during the recent months. Confidence indicators show positive expectations for the third quarter of the year, hence supporting our assessments for the fuelling of aggregate demand from the private sector.

Public sector curbed the fiscal expansion starting from the beginning of the second quarter. At the end of July, budget deficit amounted to ALL 23.1 billion, about 42% lower relative to the previous year. Budget revenues grew by 3.7% y-o-y, whilst expenditures contracted by 5.1%.

Capital expenditures in particular continue to record negative growth rates, being in line with the Ministry of Finance plan on curbing budget expenditures and reducing public investments for 2010.

The Bank of Albania considers that the observance of the deficit and public debt level in the revised budget plan will help preserve the economic balances. The prudential management of public borrowing will generate downward pressures on both the risk premium and the long-term interest rates, thus providing more room to boosting the private sector lending. It will also increase the flexibility of fiscal policy in the medium and long run.

Net exports continued to increase their contribution to aggregate demand during the second quarter of the year. This performance was triggered by the annual growth of exports by 86% against the growth of imports by only 6% during this period. These developments materialised in the further narrowing of the trade deficit by about 14% y-o-y. The reduction of trade deficit was accompanied by lower pressures in the foreign exchange market and a more stable exchange rate.

The Bank of Albania considers that the current export growth rates, albeit encouraging, will be difficult to be preserved. Therefore, the long-term stability of Albania's external position will require a more careful approach to the trade deficit and the encouragement of stable capital inflows.

The slow improvement of domestic demand is reflected in a more stable growth of money supply. This indicator recorded an annual growth of 10.1% in June and continues to be mainly supported by the high contribution of the banking system's net foreign assets. In the meantime, private sector lending continues to record relatively slow growth rates, reflecting both the performance of demand and the still tight lending terms.

Excluding the exchange rate effect, the annual credit growth in June pointed to 6.4%, from 4.9% in the end of the last quarter. It was mainly triggered by the growth of credit to businesses, where the loans extended for investment purposes has the highest share.

The annual deposit growth of 15.8% in June improved the liquidity indicators of the banking system's balance sheet. The augmentation of liquidity in the system, the controlled public sector borrowing in the domestic financial markets, the lower risk premium and the anchored inflationary expectations have conditioned the decrease of interest rates in the financial markets. The decrease in both deposit and Government securities' interest rates, due to the key interest rate cut in July, is expected to create more adequate conditions to boost the economic activity.

The Bank of Albania has implemented a prudential monetary policy. In view of observing the inflation target, the Bank of Albania cut the key interest rate by 0.25 pp in July.

This easing of monetary conditions aims to provide further stimulus to the economic activity, controlling at the same time the inflationary pressures and the external balances of the economy. It was transmitted into the financial market in its short-term segment, thus leading to the decrease in banks' borrowing cost, and lowering of interest rates in the interbank market and the primary market of Government securities. In the forthcoming months, the monetary policy movement should also generate lower private sector borrowing cost. In terms of the operational aspect, we are present in the market by providing all the necessary liquidity in order to ensure a normal banking system functioning.

In its discussions, the Supervisory Council of the Bank of Albania concluded that in absence of unexpected shocks, CPI inflation will be in line with the Bank of Albania's target in the medium-term period. At the end of discussions, the Supervisory Council decided to keep the key interest rate unchanged at 5.00%.

With regard to the future, the Bank of Albania remains firmly committed to act by factorising the actual and expected performance of economic indicators, in order to maintain price stability and further consolidate the macroeconomic balances at home.

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

At the Roundtable “Economic & Political Challenges of Regional Cooperation”
September 8, 2010

Dear guests,

Dear participants,

I feel honoured to open today this roundtable. Before anything else, I want to welcome our colleagues from Oxford University, who have undertaken an important mission for Albania and the region: contributing to the growth of research capacity, of sapience, and to building a sustained long-term response to the growth challenges we come through on our common ways, similar but unique, towards the European Union.

It is a great pleasure for me and the Bank of Albania to have the opportunity to begin a series of studies about the domestic and regional economic policy, which will assist the scientific debate about the economic growth model, also backed by a regional point of view at social, economic and political level.

You may ask yourself why the Bank of Albania is so much interested in the economic growth and the economic policies overall, as the main target of the central bank is price stability. In the following minutes I will try to deal with some of the main points of the Bank of Albania’s agenda in recent years.

In this respect, they are the efficiency of monetary policy, the importance of internal and external economic anchors, the building up of research capacities for the purpose of implementing our policies, as well as public communication and education. The right addressing of these issues is indispensable for the monetary policy and its crucial role for the economic prosperity.

The successful central banks, whose main target is inflation, are increasingly giving more importance to the economic activity and other indicators of real economy. This trend is not only based on the fact that inflation is directly impacted by the fluctuation of economic activity and unemployment in the short run, but also on the theory of monetary economics, according to which the central bank should pay attention to the potential economic growth over the long run as well.

In addition, the argument about economic growth is the key target of economic policies. Therefore, the decisions of the central bank in the field of monetary policy, supervision and financial stability, should interact and be harmonised with this central target, thus guaranteeing the macroeconomic and financial stability of the country.

The Central Bank, in this respect, tries that its policies neither increase the short-term volatility of the economic activity, nor impede the potential economic growth over the long run.

The monetary policy of the Bank of Albania is similar to the policy implemented by the European Central Bank. It is based on two pillars: the first is the monetary analysis, and second the economic analysis. The second pillar has a considerable importance for the performance of inflation, particularly in the long run.

Inflation, in general, is a monetary phenomenon and as such, it depends considerably on the money supply and the pace the latter increases relative to the Gross Domestic Product. The right tie which exists between these variables requires the growth of money supply in the long term not to be faster than the growth of economic activity, thus the central bank and its monetary policy not to lead to inflation.

Having the maintenance of price stability and financial stability as main priorities, the Bank of Albania is determined to make all endeavours to encourage and play an active role in the convergence process of the country with the European standards.

One of the steps to be made immediately in this direction is the design of a new economic growth model, which should avoid the weaknesses of the current model built on the increase and expansion of lending and high consumption rates. In May of this year, the Bank of Albania held a scientific round table, which concentrated on the identification of the economic sectors that may provide a stable economic growth in the future. The meeting concluded that the next model of economic growth imposes the design of a national strategy for the economic development at home. The next model should be based on the upsurge of output factors in all sectors of the economy.

Given the small-sized and open economy, the increase and stability of exports is of outmost importance. Therefore, the research work, the reforms and the strategic decisions should be adopted in line with this target. In this respect, the role of the banking system acquires particular importance. It should carefully identify the primary and profitable sectors and should provide their ongoing financing. Banking credit has been and remains one of the main instruments, which will allow the sustainable performance of the economic and financial activity at home.

For this strategy to be successful, it must include as one of its substantial constituents the philosophy and development priorities of the South-eastern Balkan. This need does not only arise from the requirements of competitiveness and the achievement of the economy of scale, but also from our common target for European integration.

During the recent years, I have continuously highlighted that the key to a successful integration in the European Union is the regional cooperation.

There are many reasons backing the conclusion that our models of growth must be seen as complementary and not as competitive to each-other. It is indispensable that the entire process of structural reforms takes place quickly and in a coordinated way, and precede the membership to the European Union.

Only in this way the whole region will converge naturally, avoiding episodes of misbalances within the bosom of the European family upon the membership.

This will be a real contribution to the long-term sustainability of the European developments.

The whole region is going through a political, economic and social consolidation process. The policy-makers, the decision-makers, the examiners and almost everybody declare that their priority is the adherence to the European Union.

The question to ask is if:

- we have either to converge towards the European economic zone with small and fragmented economic structures competing with each other for European markets and opportunities,
- or embrace a model:
 - that gains from the economies of scale,
 - that encourages and makes use of the advantages of the current competitive positions;
 - that grows the economic prosperity of the whole region and of each individual economy?

Personally I think that the second alternative is the contemporary approach that our region should embrace with no hesitation. The success of this process will above all depend on all our attempts and devotion to see what our competitive advantages are and to build up the right economic, financial, legal and physical infrastructure to use and increase these advantages and to become competitive in the global economy.

Therefore, it is significantly important that the study of the growth model takes place not only from a regional point of view, but to be a deeply future-oriented approach.

The region in itself provides a lot of important advantages:

- the labour markets are situated amidst the Asiatic countries and the EU member countries;
- the opportunities for high return investments in real estate and infrastructure are huge and attractive for the developed markets;
- the region has a population of over 20 million sharing pleasant demographic characteristics;

- the region's tourism potential is extraordinary as a result of the combination between different climates and the geographical features and various ethnical and cultural traditions.

Preliminary results of empirical research at the Bank of Albania show that the economic opportunities to be made use of from the regional countries are huge.

Our analyses of external trade, based on gravity models, reveal that Albania's external trade with EU partners is at optimum levels, while trade with the region is under its potential.

- What hampers our regional trade to achieve the potential?
- What do we need to undertake coordinated structural reforms at a regional level?
- Are we encountering any weaknesses in coordinating the policies, information sharing, the establishment of institutions, the current legal infrastructure, or lobbying in European structures?
- How possible is the synchronisation of efforts for more effective and efficient convergence and the integration process?
- What are the main economic and political areas where there can be more room for the achievement of common regional policies?
- How has the last global financial and economic crisis impacted the Albanian economy, the regional economy, and primarily, the convergence process?
- Can we make it on our own?

These are all very important issues on which I think we should stop and study in depth. They are subject to research work, whose findings would shed light on the orientation of economic and structural reforms.

In this respect, the Bank of Albania has joined the forces with the University of Oxford to carry out scientific research dedicated to finding the answers to the above questions and other similar.

Answers to these fundamental issues are useful not only to Albania and its regional partners, but also to the EU and its political and economic structures.

I am confident that the European Commission can make use of the outcomes of this scientific research to build up new anchors in the form of economic and political incentives in order to enhance the efficiency of all regional sources.

These studies will help us better understand: How and what should we do to turn EU, its Pre-adhering Economic Programs and Fiscal and Economic Programs into stronger and more imposing external anchors for the national and regional policies.

However, it is important to realise that international restrictions cannot support the long-term and sustainable prosperity in absence of internal anchors.

Obligations that may be imposed from Brussels or other international organisations are indispensable as long as the internal anchors are fragile. Therefore, it is necessary that the society itself and the international institutions support the establishment and strengthening of internal anchors.

What would be an efficient internal anchor?

I think that the best internal anchor is a technician who thinks independently, who is proud of what he does, and who is conscious of the results and the consequences of the proper actions.

In other words, this implies setting up professional capacities as one of the cornerstones of long-term successful policies. Education and scientific research in this direction have an important and inalienable role.

All the issues mentioned so far, like:

- the new strategic model of economic growth;
- the effective, efficient and consistent monetary policies with the economic growth;
- the need for coordinated structural reforms in the region;
- the challenges of European integration;
- the common political economy of the region in the future;
- the importance of internal anchors and the study and use of external ones; and
- the need for establishing capacities,

are included in the research work's agenda of the Bank of Albania.

It is a great pleasure that we now have the possibility to cooperate with a remarkable partner as Oxford University, a distinguished institution for the high-level research in political and economic sciences.

I hope and I believe that many issues I discussed above will have an answer, partial or a complete one. The one thing I strongly wish is the involvement of as many domestic and regional researchers.

I would like to guarantee all the interested persons that we are open in this direction. On the other hand, I am confident that the collaboration we made official today, shall provide a sensitive contribution in terms of the education and establishment of professional capacities at a national level.

Let me close my speech returning once more to the argument of professional technicians. I still think that:

- We need to educate our technicians;
- Furthermore, we should make them financially and politically independent;
- And afterwards, we should educate them again.

On the other hand, the building of capacities is not a matter of “individuals”; it is rather a matter of institutions; in fact, it is a process independent from human resources.

This because, for them to be long-living, capacities should be based on “processes” and not on people. The good anchors are not only used by institutions which relate policies with them. They are instruments in the hand of the public, as strong arguments to encourage governmental agencies towards the formulation and implementation of long-term sustainable policies.

I believe that the European values may play a decisive role in this direction, by strengthening and supporting the establishment of respectable institutions, where the criticism occurs independently from the political processes and targets. This is the reason we have chosen to cooperate with the Oxford University.

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

At the Press Conference on the Monetary Policy Decision-Making of the Supervisory Council of the Bank of Albania, September 29, 2010

At its meeting of 29 September 2010, the Supervisory Council of the Bank of Albania analysed and approved the Monthly Monetary Policy Report. After scrutinizing the latest economic and financial developments at home and further to discussions on their expected outlook in the months ahead, the Supervisory Council of the Bank of Albania decided to keep the key interest rate unchanged at 5.00%.

In what follows, I will provide an overview of our main monthly analysis' conclusions and the issues discussed in the Supervisory Council meeting that motivated today's decision-making.

The Albanian economy has, over the last months, been operating amidst a global environment characterized by the slow recovery of economic activity and higher volatility in the financial markets. The main factors impacting these developments are the weaker effects of fiscal and monetary stimulus and the higher prudence of markets with regard to the developments in private and public debt indicators of various economies.

Despite the expectations for the slight rise in prices in the next few months, the inflationary pressures, at a global level, remain contained and the key interest rates continue to be at low historical levels.

In particular, the low lending, the concerns in both the real estate and labour markets, accompanied by the frail position of some countries' public debt, have left little room for pursuing countercyclical policies, and have elevated the uncertainty about the performance of economic activity at a global level.

The rise in raw material prices over the last months, and the low capital inflows to the economies of Central and Eastern Europe countries, suggest that the favourable effects of the global economic recovery in small-sized economies might be weaker than expected at the beginning of the year.

Overall, the current data on domestic and monetary economic developments have confirmed our interpretations that the Albanian economy continues to feature gradual improvement of the activity, but it however remains below its potential.

The main concern facing the Albanian economy is the low domestic demand. Despite the rapid growth rates of the Albanian exports, total demand

in economy has proved insufficient to fully utilize the domestic production capacities.

This situation has, among others, been reflected in:

- Low inflationary pressures generated by the domestic economy;
- A weaker performance of the labour market and employment figures; and
- A moderate demand of the economy for bank credit.

The growth in economic activity has been lately driven by the recovery of the private sector. Despite the public sector's positive impact due to the fiscal stimulus, it has lowered its contribution to the economic activity.

Concerning the demand, the rapid increase in exports and the positive tendency of private investments have provided the largest impact on economic growth. Private consumption, albeit low, has recently shown signs of improvement. This is evidenced by:

- The more stable performance of consumer loan,
- The upward tendency of core inflation, and
- The increase in the import of consumer goods.

Industry and services have been the most dynamic sectors of the Albanian economy, driven by the external demand and the gradual increase in private investments, whereas construction and agriculture have progressed more slowly. In addition to the weak demand for commodities and services, the increase of consumption and investments still faces tight financial conditions.

Although banks' balance sheets remain fully sound and the liquidity indicators have improved, private sector credit continues to feature higher banking system prudence and slow credit demand.

The annual growth of private sector credit pointed to 10.2%, slightly higher than the average growth rate in the second quarter of 2010. Credit to GDP is estimated at 38%, up by 2 pp relative to the same period of the previous year. This figure shows encouraging signs of the banking system's resumption of lending to the economy.

The weak domestic demand and the presence of unutilised capacities in the economy have impacted the absorption of shocks on inflation, generated by supply-side factors or the administrative rise in consumer goods prices. Annual inflation rate in August was within the Bank of Albania's target, pointing to 3.5% from 3.4% in July.

The slight increasing tendency during the last couple of months owes mainly to the administered price rise of water supply and the reduced supply of agricultural production. Both factors are not expected to generate second round effects, thus they will affect inflation only transitionally.

On the other hand, the impact of the exchange rate has been declining, and in light of the more stable demand and supply ratios for foreign currency, it is expected to affect inflation moderately. Overall, the Bank of Albania concludes that the inflationary pressures are contained and the economic agents' expectations for inflation remain anchored around its target of 3%. At this juncture, in the absence of other shocks generated by the administered prices or the external environment, the projections for inflation continue to show its downward trend in the medium run.

Fiscal indicators attest to the lower fiscal policy stimulation over the last months, and generally observing the figures projected in the revised budget. In annual terms, budget revenue grew by 5.7%, whereas expenditure contracted by 5.5% in the first eight months of the year. In addition, budget deficit shrank by nearly 50% relative to the same corresponding period in 2009.

To a large extent, this deficit has been financed by domestic sources, through the issue of T-bills and bonds in the domestic financial market. The lower Government borrowing has improved the system's liquidity indicators, being reflected in lower interest rates and greater room for private sector lending.

The decline in public expenditure and the slower widening of the budget deficit have provided a positive contribution to keeping the external balances of the Albanian economy in check. The Bank of Albania considers that the observation of both public borrowing and debt rate until the end of 2010 will help preserve the economic balances at home in the period ahead. The performance of the external sector of the economy in the second quarter shows encouraging signals in terms of the high current account deficit adjustment. Relative to the same corresponding period in 2009, the current account deficit to GDP has reduced by 4 pp to 9.2%.

The shrinkage in the trade deficit, attributable to the rapid increase in exports and the contained import levels, was the main drive in this reduction. Foreign currency inflows in the capital and financial account were almost sufficient to cover the current account deficit.

However, their volatility suggests that Albania's external position is still frail. Its recovery will call for further measures in order to reduce the current account deficit and increase the stable sources of foreign currency inflows. In particular, the Bank of Albania reiterates that the preservation of the current export growth rates remains one of the important strategic objectives in the short and long run.

Objective and subjective factors may turn the positive contribution of exports to the growth of aggregate demand and the recovery of external economy balances temporary.

Accordingly, the stable growth of exports in goods and services call for the persistence of structural reforms, from both the public and private authorities,

always aiming at enhancing the efficiency, fostering the competitive advantages of the Albanian economy, and enhancing the presence of our products in the international markets.

The financial markets at home responded duly to the decision of the Bank of Albania to cut the key interest rate by 0.25 pp at the end of July. The interbank and primary markets of Government securities have almost fully reflected this movement. In average terms, the daily rate has dropped by 0.32 pp, while the one-week rate has dropped by 0.26 pp. The primary market of Government securities manifests a similar declining tendency. The 3-, 6- and 12-month yield declined by 0.23, 0.13 and 0.21 pp, respectively.

In parallel, the interest rates on Lek deposits have declined, and banks' liquidity figures have improved. These developments have been also driven by the operational policy pursued by the Bank of Albania, which has supplied the banking system with ample liquidity in order to ensure its smooth functioning.

On the other hand, the pass-through of monetary conditions easing to interest rates on loans was weak due to the long monetary policy transmission chain and the presence of risk premium in the credit market.

In light of the foregoing information, the Supervisory Council assesses that the inflationary pressures are well-contained in the medium run, and the risk factors are by and large balanced.

The Albanian economy will continue to be affected by the rise in administered prices, while the presence of free capacities in economy during the period ahead will exert downward pressures on inflation.

In the absence of abrupt shocks, CPI inflation will be in line with the Bank of Albania's target in the medium run. The impact of further rises in raw material prices, or other possible rises in administered prices, on inflation, or the push of domestic demand beyond the projection, are risks that will be subject to intensive and ongoing assessment from the Bank of Albania.

At the end of discussions, the Supervisory Council decided to keep the key interest rate unchanged at 5.00%. The monetary conditions are considered appropriate for observing the inflation target in the medium run.

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

At the Regional Meeting in Gjirokastra
September 30, 2010

Dear guests,

It is a distinct privilege for me to return to the city of Gjirokastra. Through this communication today with representatives of the business community of your district, I would like to go back to some of the considerations that relate to the growth model.

First I would like to point that my discussion won't deliberate on philosophical considerations of political economy. That is, this discussion does not intend to address theoretical theses of the kind: a market economy or a planned economy? This choice has already been made and there is no hesitation or doubt that market economy is the right alternative approach. Similarly, this discussion does not intend to deliberate on the role of the state in economy, its size, the tax system or Government spending structure.

The debate about the role of the state is naturally a highly important topic, particularly when viewed from the business cycle theory viewpoint, when we explore the philosophy, role and the extent of government intervention to correct short-term fluctuations in economy, or the reallocation of income generated by the economy.

In my addresses related to this topic I have always discussed the role of the state in economy from the long-term economic growth theory viewpoint. In practice, these models are known as: the Asian growth model, which bases on the rapid growth of exports, or the Irish growth model, which stimulates the rapid growth of technology.

In this case, the entire state superstructure is designed in a way that supports the transformation of the economy (legal, economic, production, academic and pedagogical, and foreign policy structure) in accordance with the strategic development plan.

To better illustrate the foregoing concept, let each one of us ask himself these questions:

- What is my vision of the country's economic and financial development level in 30 years?
- What will be the distinctive features of our economy during this period?
- What model will we stick to in this long process of successive changes and adjustments?
- How will the legal basis be adopted?

- Who will the change in the structure of the economy favour?
- Will scientific thought have a special role in academic life?

This is the debate we want to stir up. Acknowledging the expected developments and structural reforms in economy is a necessity for us and our policies in order for them to sustain the trends of economic development, and ultimately, ensure the country's macroeconomic and financial stability. It is hard for a single institution to formulate this strategy in a single word. Moreover, it is wrong. As I said earlier, this debate is a property of the society, which should have a proactive role in both the formulation and implementation of the strategy. I consider that, in addition to the general discussion, these are the topics our discussion on the new growth model should focus on.

Albania's economic activity in the last 20 years corresponded to a relatively long period of cooperation agreements with the IMF and the World Bank, beginning from the funding to ease the balance of payments deficit, which was followed by the stabilization and poverty reduction programmes and concluded with the more liberal agreements on commercial terms in the recent years. The low per capita income and the large imbalances we inherited set the stage for large amounts of foreign inflows to enter Albania in the form of grants or soft loans. This was also followed by the incessant increase of foreign inflows via remittances and the privatization process. Consequently, gradually with the stabilization of basic parameters, the conditions were set for a rapid increase of trade activity with the rest of the world, particularly as far as imports are concerned. The consolidation of the banking system, which has increased lending to economy markedly in the recent years, was also a major impetus. Domestic consumption has been ever-increasing. The lack of sufficient domestic production capacities has been deepening the current account continuously over the years. This was more or less the model Albania's economic development was based on in the last 20 years. It spread throughout all former communist countries in Europe and it was known as the catching-up process.

The last crisis disrupted this mechanism of financing consumption through debt. It is a fact that this crisis put an end to financial abundance and the investor's risk-seeking behaviour. In other words, savers in advanced and emerging economies do not wish to make their funds available to consumers for the latter to increase production by purchasing houses, machinery or other consumer goods, or by going on holiday abroad.

Today, the transition of these countries from transition to developing economies demands further deepening of structural reforms and the implementation of new economic growth models.

We all need to understand that credit-fuelled consumption-led economic growth has had negative consequences for the economy. Current debt level accumulated under this model is relatively high. It is evident in the high trade and current account deficits that we have accumulated in the last 20 years. Albania's deficit compared to other nations shows a record high level of about

14% of GDP. In other words, we consume each year about 14% of the future GDP. Many empirical studies argue that in order to maintain the external economic balance, Albania must run a no higher than 5% current account deficit as a percentage of GDP. Endeavours to bring the current account deficit down to long-term and stable figures would subsequently improve the domestic production potential, and ultimately, the economic growth structure or model at home.

According to economic identity, a country's current account equals savings minus investments. That is, in order to bring the current account deficit down, Albania must increase national saving (or lower consumption) or reduce national investment. Maintaining high investment rates is essential as they are the basis for economic growth. Therefore, we must opt for a new growth model that keeps the level of savings in an optimal balance.

This brings us to another important argument. Financial market infrastructure and the instruments it provides still need to promote saving and finance investment. The current instruments in the form of deposits and investment in Government bonds are short-term, up to 5-year maturity. Hence, they do not encourage households to balance between present and future consumption. Unlike our economy, the structure of savings in advanced economies clearly encourages long-term investment, mainly in the form of pension funds. These types of instruments provide proper incentives to increase long-term saving. This is why I have many times been vocal about the need for a pension reform.

Economic growth theories elaborate extensively on similar topics that relate to the role of capital and other factors of production. Thus we can say the same when it comes to the unique role that land, as the major and most limited factor of production, plays. What are the obstacles that do not allow this major factor of production to produce similarly as in advanced economies or at least the regional economies? I won't elaborate on this topic, nor will I reiterate myself, considering that the use of land will also depend on the specific objectives we will set for our economy in the next 30 years.

I would like to elaborate further on the new economic growth theory. It establishes that the ability of an economy to grow is largely determined by its ability to be competitive and produce or adapt quickly and efficiently to the new production technologies.

These theories view the competitiveness of the economy in its ability to generate scientific innovation, to enhance productivity through a cheap labour force. Hence, competitiveness is not an attribute of the monetary values a country holds, but of the labour force capacity to increase labour productivity faster than labour cost. These theories corroborate the high importance of human capital and technology to economic growth.

Refraining from determining the nature and direction that education should take in order to have a competitive labour force in the 21st century (this should be part of the foregoing debate), I would like to draw your attention

and stir discussion about two key aspects: the nature of present-day education and the market instruments for intellectual property.

First, from the perspective of demand, our education-related strategies are generally based on the individual's adaptive expectations rather than on rational expectations. That is, the selection of the high school or university is past-oriented rather than future-oriented. Let us only remember that in the last 10 years, the labour market has generated jobs in the banking system, construction, or has yielded high income in the legal field. We have many lawyers, economists, construction engineers and architects. According to the latest INSTAT's figures, students' first choice branches of their university studies in 2008 were Economics (17%), Law (6.4%), Pharmacy, Construction Engineering and Political Sciences, which make up nearly 42% of graduate students. These branches have been the students' first choice, thus leading to the labour market's super saturation with similar experts. Concerning Economics-related branches, like Engineering in the branches of Mechanical Industry, Metallurgy, Mining Engineering, Industrial Chemistry, Mathematics and Physics, the number of graduate students has reduced substantially compared to 10 years ago, making up only 5% of graduate students in 2008.

One of the problems with the current economic growth model is that this group of graduates will face an economic structure that won't be able to involve these experts in the future. Despite the successful reforms in education (reflected in the number of students in the elementary and high school levels), attendance at the university level is still low, merely 28%. This figure still lags behind the countries we have to converge to, an average of over 50% (Italy 67%, Greece 95%, Czech Republic 50%). I do believe that the division of branches at university level should better suit the needs and aspirations of Albania's economic and social development in the future.

A similar situation may be also seen in high school education. In the early 1990s, about 50% of high school students attended vocational schools, while in 2009, only 16% of the students developed expertise in a particular profession. This gap between the market needs and the creation of human capital, by generally gaining expertise as technicians, does not represent an optimal choice for the long-term development. It is impossible to adopt a rational approach in demand for education unless there is a discussion about the priorities and branches that need to be prioritized in the development of Albania.

The labour market data provide essential supply for a sound decision-making of monetary policy and economic policies in general.

It should play a key role in formulating the curricula in our educational system, not only in terms of the attendance ratios (capacities), current programmes and textbooks, but also in terms of the academic staff and the base material for developing academic know-how.

How do these programmes and their attendance match with the long or

short-term objectives of the Albanian business development? What is the role of the Albanian business in funding these programmes?

These are highly essential issues to be discussed in the context of the economic growth model. It is generally hard to identify in the Albanian market whether there are financial and social instruments that allow this cooperation between education and the business. We can conclude that the development of human capacities in our case is occasional and past-oriented, and it does not necessarily contribute to the future and its model. Relevant forums and institutions should be an important part of discussions about the growth model.

Intellectual property and its support mechanisms are another key element in the design of the new economic model that our academic, business and state systems should focus on. Intellectual property, acknowledged to be a key component of technological development, plays a dual role in a country's economic development. It does not only provide a strong support to economic growth, but by promoting technology, it becomes the subject of economic development itself.

Lastly, I want to comment on the global aspect of the growth model. Establishing competitive standards and products in today's world economy is part of the global game. If you look at the development plans of the surrounding regional economies, you see that they mostly resemble competition among countries rather than regional cooperation which, given the similar features of our economies, would allow for setting up a joint market. The country's new economic model should also redefine Albania's role in the region.

The Albanian economy needs restructuring in order to find its spot in global economy. This also involves its re-dimensioning in the region in order to pursue collinear economic development policies across the Balkan countries. All these issues raise a question: What are the obstacles for the Albanian economy in setting up institutions that debate over these important issues? What should we do to make them debatable? How can we encourage the establishment of these institutions and their reliability?

These are the major issues I wanted to steer the future of debate over economic growth to. The Bank of Albania surely has the reputation and the intellectual capacity to contribute to stirring up, and also discussing, this debate. In this context, we have been cooperating with the University of Oxford in London and we are open to share the fruit of this cooperation with all the stakeholders. I invite you to be part of this debate and its driving force.

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

At the Press Conference on the Monetary Policy Decision-Making of the Supervisory Council of the Bank of Albania
October 26, 2010

At today's meeting of 26 October 2010, the Supervisory Council of the Bank of Albania analyzed and approved the Monetary Policy Report for the third quarter of 2010. After scrutinizing the latest economic and financial dynamics at home and the future outlook, the Supervisory Council of the Bank of Albania decided to keep the key interest rate unchanged at 5.00%.

In what follows, I will elaborate upon the analysis and the main conclusions today's decision-making of monetary policy was based on.

The performance of the Albanian economy during the third quarter of 2010 reinforced the main developments of the first half of the present year, featuring gradual recovery of aggregate demand, lower risk premium and consolidation of macroeconomic stability.

Broadly in line with our projections:

- economic growth has accelerated (resurged) and its base seems to have broadened;
- CPI inflation and expectations have been anchored close to the Bank of Albania's target for inflation;
- the external position of the Albanian economy has recovered and the exchange rate is more stable;
- liquidity in the system has increased and the interest rates have generally been downward.

These highlights reflect, inter alia, the macroeconomic policies pursued over the course of this period. Monetary and fiscal policies have, in a concerted manner, aimed at fuelling aggregate demand and economic growth, ensuring at the same time the preservation of macroeconomic balances.

July's state budget revision put emphasis on the measures required to be taken in view of maintaining medium and long-term fiscal sustainability, hence implying lower budget deficit and lesser impact of fiscal stimulus on aggregate demand in the short run.

This revision paved the way for pursuing an easier monetary policy. The key interest rate lowered by 0.25 pp, hence yielding the most stimulating monetary conditions during the last decade.

Nevertheless, complex challenges remain for the Albanian economy and the economic agents. Economic growth rate, albeit positive, seems insufficient

to yield improvements in the labour market and to lower unemployment. In addition, the sustainability of economic growth remains frail in the short run.

Its reliance on foreign demand and export growth may be insufficient against a background of a non-consolidated global economic outlook.

The waning of fiscal stimulus also requires greater contribution of the private sector to economic growth, hence bringing consumer and business behaviour to the forefront and accentuating the role of bank credit to their financing. Setting proper equilibrium between short-term stimulus and long-term stability requires courage and diligence from the policy-makers.

Ongoing structural reforms remain a priority in the long run. The latter should aim at broadening the potential growth rate of Albania and underpinning its macroeconomic sustainability.

In what follows I will elaborate on these issues, beginning first with a brief overview of the recent developments in global economy.

The recovery of global economic activity persisted in the second quarter of 2010, while indirect or preliminary data show more moderate growth rates in the third quarter. Economic outlook remains highly uncertain due to the fiscal stimulus withdrawal and the private sector's (unsatisfactory) soundness.

Growth in advanced economies and in our main trading partners was moderate due to the correction of private sector's balance sheets, weak lending and labour market, and low consumer confidence.

The low capacity utilization rate has yielded weak inflationary pressures at a global level. The financial markets continue to show high levels of volatility in response to the concerns over the economic outlook and the long-term sustainability of fiscal indicators.

In political terms, maintaining macroeconomic co-ordination at a global level and keeping open channels of the movement of goods, capital and technology, are considered priority measures to avoid a second recession.

This would certainly provide substantial contribution to the Albanian economy, which remains a net borrower in the global market and that has benefited largely from the growth of demand and global trade in the form of higher exports in 2010.

In light of these developments, and being largely affected by them, the Albanian economy has grown progressively over the year.

According to INSTAT, GDP grew by 3.3% y-o-y in the second quarter of 2010, considerably higher than 2.0% in the first quarter the same year. This growth was mainly driven by foreign demand, while domestic demand performed at more stable rates.

This performance was reflected in improved figures in industry, particularly in its export-related sub-branches. Construction and services did not perform alike:

- The gradual recovery of domestic demand boosted the activity in services further.
- By contrast, the construction sector continues to suffer from the weak demand in the real estate market, the limited financial resources and structural concerns related to its regulation. Subsequently, activity in the construction sector posted a high annual contraction rate in the second quarter, 28.9%.

Indirect economic and financial indicators suggest that economic growth performed similarly in the third quarter as well.

The weaker impact of the fiscal stimulus and the deeper trade deficit seem to have been offset by a better performance in tourism over this period.

The more positive economic outlook in the second quarter of 2010 was also reflected in the labour market. Although unemployment rate remained almost unchanged at 13.8%, the higher activity in industry and services increased employment by 1.8%. Nonetheless, the dynamics of these indicators is less promising than the pre-last quarter of 2008 period.

The analysis of economic activity by aggregate demand components allows for a more thorough assessment of the current and expected developments. (In the absence of direct data, it continues to be based on indirect quantitative and qualitative indicators.)

Available indicators suggest that the economy grew in the second quarter in response to the higher foreign demand. The performance of domestic demand attests to a more positive private consumption, higher private investment and a more positive contribution of the public sector, albeit more moderately than in the previous year. Except for a more pronounced waning of fiscal stimulus effect, these developments are considered to have persisted in the third quarter as well.

Although private consumption indicators are often contradictory, the overall setting shows a better performance compared to the first quarter of 2010. The rise in average wage and employment, the increase in the import of consumer goods and the substantial improvement of the consumer confidence index reinforce and signal the resurgence of consumption in the second and third quarter of 2010.

On the other hand, the further decline of remittances and the contraction of consumer loans, the drop in the retail trade index and the higher consumers' propensity to save suggest that the growth rates of consumption remain below the expectations.

Private investment recorded positive growth rates as evidenced by the increase of capacity utilization, higher import of capital goods and better performance of investment loans.

The further increase of investment in economy is reciprocally related to banking system lending; but ultimately, it will depend on the performance of domestic and foreign demand for Albanian goods and services.

The gradual increase of the capacity utilization rate in economy, as reported by business surveys, shows that there is more room at the current juncture for increasing private investment.

Fiscal policy has been more prudent in 2010 owing to the narrower room for fiscal expansion and the public debt approaching the threshold of 60% of GDP.

Despite the public sector's positive contribution to sustaining economic activity, the fiscal indicators point to its lesser impact on economic growth.

The Government's prudent approach in the first eight months of 2010, in view of meeting the planned deficit figure for 2010, actualized in the annual reduction of public expenditure and budget deficit. The latter amounts to ALL 23.2 billion, which is within the projected figure in the budget and about 51% lower than in 2009.

The 2010 state budget revision in July, which established the reduction of expenditure and budget deficit by 10% and 23%, respectively, is an expression of the fiscal authority's firm commitment to safeguarding economic stability and ensuring fiscal sustainability in the long run.

The high growth rates of exports and the contained performance of imports yielded a positive contribution of foreign demand to economic growth in the second quarter of 2010. Foreign trade data on July and August attest to moderate annual growth rates of exports and positive annual growth rates of imports, hence leading to higher trade deficit in this period.

The growth of exports in 2010 was fuelled by the recovery of global economy and the favourable conjuncture of prices in the global markets, the depreciation of the exchange rate, the Albanian entrepreneurship efforts to expand the market and by some other factors of transitory nature.

Therefore, promoting exports in a stable and long-term fashion requires undertaking structural reforms, which will in turn enhance the competitiveness of the Albanian economy. This would ultimately serve to the transition to a more stable economic growth model and, at the same time, to curbing the reliance on foreign financial sources.

Our analysis of monetary indicators concludes that the growth of money in economy is concurrent with the economic agents' demand for monetary assets, hence creating no room for inflationary pressures in the future.

Aggregate M3's average growth was 11.2% in July and August, being in line with the nominal economic growth and the enhanced confidence in the banking system.

Its growth during this period was mainly determined by the increase of the banking system's net foreign assets. Private sector credit grew by 9.8% y-o-y, close to the previous quarter's rate. Although the better liquidity figures and the improved banks' balance sheets led to higher banking supply and provided greater room for lending, the latter has progressed at moderate rates.

Our analyses of lending in economy show that demand remains contracted and the number of worthy projects to lend is still low. The foregoing remains a constant concern for the Bank of Albania.

To this purpose, alongside the banking system, we are considering the required measures that may lead to the growth of lending in line with the cyclical and structural needs of the economy.

Economic and monetary developments elaborated above yielded an environment of contained inflationary pressures. Average annual inflation marked 3.4% in the third quarter. Against a background of below-potential economic growth, and given the absence of monetary-related inflationary pressures, inflation was largely affected by the rise in administered prices. The contribution of the latter's rise to headline inflation is 1 pp.

In the absence of second-round effects, the effect of the rise in administered prices is expected to be transitory, while the inflationary pressures arising from domestic demand remain well contained.

On the other hand, the depreciation of the national currency has been declining, hence offsetting the rise of primary commodity prices in the world markets and the increase of inflation in Albania's main trading partners.

The absence of inflationary pressures in the medium run and the contained fiscal policy provided room for pursuing a stimulating monetary policy that sustains economic activity. In July, the Supervisory Council of the Bank of Albania cut the key interest rate by 0.25 pp bringing it to the historical low of 5.00%.

In addition, the Bank of Albania continued to supply the banking system with the required liquidity in order to ensure the smooth operation of the money markets and to enhance financial intermediation in economy.

The favourable liquidity situation facilitated the rapid transmission of the

key interest rate cut to the interbank and the primary market, hence allowing for the reflection of this cut in other interest rates in the economy as well.

The Bank of Albania considers that the inflationary pressures remain well contained all through the time frame of the monetary policy effect: the effect of supply-side factors is expected to be offset by the downward pressures arising from the performance of demand in economy.

The projections for inflation and inflationary expectations remain well-anchored around the Bank of Albania's target. Therefore, the central bank considers that monetary conditions in economy are adequate to warrant the safeguard of price stability in the medium run and to boost economic development further.

The Bank of Albania will, in response to actual and expected economic and monetary developments, continue to pursue a prudent monetary policy, thus providing the required monetary conditions for achieving the inflation target and safeguarding macroeconomic stability.

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

At the Joint Press Conference of the IMF Mission with
the Ministry of Finance and the Bank of Albania
November 3, 2010

Dear Mr. Minister,

Dear Mr. Bell,

Dear media representatives,

It is a pleasure for me to appear before you today following a week of intensive and fruitful discussions to present the Bank of Albania's position. Allow me first to underline that the meetings held broadly confirmed the conclusions provided in our last monetary policy report and the Bank of Albania's outlook regarding its future performance.

In what follows I will provide a brief overview of our opinions, dwelling upon the key topics of discussion: current and expected economic developments, risks and related concerns, and the appropriate macroeconomic policy response.

The Albanian economy had a positive performance in the first nine months of 2010, expressed in positive growth rates and improved key parameters of macroeconomic stability. In turn, the recovery has been reflected in contained and downward inflation rates, improved current account deficit, lower budget deficit and relative sustainability of public debt figures. These developments contributed to fully restoring confidence in the banking system, lowering the interest rates and the risk premium, enhancing the exchange rate sustainability and improving the liquidity and financial sector's balance sheet indicators. The analysis of economic growth factors suggests that foreign demand for Albanian products and services provided the major contribution, while domestic demand remains dampened and continues to suffer the heightened uncertainty about the future outlook and the tighter lending conditions. Monetary and fiscal policies have been prudent aiming at creating appropriate conditions for a stable economic development. In practical terms, this has materialized in greater orientation of fiscal policy towards the preservation of long-term public debt sustainability. In the meantime, monetary policy has been more stimulating.

As I noted in the presentation of conclusions on the quarterly monetary policy report, this performance is expected to persist in the period ahead as well. Macroeconomic stability and the improved banking system's balance sheets have created the proper preconditions for inducing consumption and investment in economy further.

However, it has to be acknowledged that several important challenges lie ahead for the country's development. In the short run, the correction of fiscal behaviour requires greater private sector's contribution to economic growth. This implies a more realistic consumer and business behaviour in their consumption and investment-related decisions, and greater financial support from the banking system. This need becomes even more critical in light of the expected performance of foreign demand. The positive tendency of Albanian exports is expected to persist in 2011, but their contribution to economic growth will be more moderate. This performance will call for the generation of domestic forms of aggregate demand, along the same lines as described above. In the long run, the persistence of structural reforms remains a priority for stimulating the economic growth rates.

The Bank of Albania has constantly called for the restructuring of the Albanian economy and the need for a new economic growth model. It should be an export-oriented growth model and it should create a more favourable environment for promoting foreign direct investment at home. Increasing economic growth potential is, among others, a necessity against a background of steady employment growth and lower unemployment figures.

The Bank of Albania has been consistent and transparent about the targeted macroeconomic policy approach. We have requested and welcomed the re-orientation of fiscal policy towards bringing the budget deficit down and keeping the public debt level in check. The successful borrowing via the issuance of Eurobond is a positive signal for the Albanian economy and it will help finance public sector's activity with foreign currency in the short run. On the other hand, the quotation of the Albanian sovereign debt in the international markets will require greater commitment in order to maintain appropriate parameters of fiscal sustainability. Pursuing these principles in 2011 budget and in the medium-term public finance framework would be the first right step in this regard.

Keeping inflation under control will continue to guide our monetary policy judgment and decision-making on interest rates and the liquidity conditions in economy. Without prejudice to the primary objective of price stability, we have been and remain firmly committed to providing the possible monetary stimulus to bolster economic growth. Lastly, we are scrutinizing the options of supporting this goal with prudent regulatory measures to be adopted in full concordance with financial stability at home.

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

At the Press Conference on the Monetary Policy Decision-Making of the Supervisory Council of the Bank of Albania
November 24, 2010

At today's meeting of 24 November 2010, the Supervisory Council of the Bank of Albania analyzed and approved the Monthly Monetary Policy Report. After scrutinizing the latest economic and financial developments at home and further to discussions on their expected performance in the months ahead, the Supervisory Council of the Bank of Albania decided to keep the key interest rate unchanged at 5.00%. In the Council's view, the current monetary conditions are appropriate for meeting the inflation target and keeping the economic activity stimulus going.

Let me provide a brief overview of economic developments and the key issues discussed at today's meeting.

The Albanian economy in the third quarter and onward has maintained the main development trends noted in the first half of the year. Based on the available data, which are preliminary and mostly indirect, the Bank of Albania concludes that economic activity at home continued to grow in annual terms. Macroeconomic stability has strengthened, while the inflationary pressures are held in check and the risk premium has been downward.

Economic growth has for the most part been underpinned by foreign demand and the activity generated by a satisfactory tourist season during the third quarter. In spite of its improvement, domestic demand remains subdued due to the sharp fiscal stimulus withdrawal in the second half of the year.

Our projections for economic growth show that it will maintain the current rates and the inflationary pressures will by and large be contained. Private sector's contribution to economic growth will be stronger and the economy will be underpinned by domestic demand to a greater extent than foreign demand. These developments will be buttressed by macroeconomic stability and the lower risk premium in the financial markets.

The low public sector pressures in the domestic financial market and the improved banking system liquidity figures are expected to push lending further, and ultimately, induce consumption and investment in economy. The exchange rate is expected to be more stable due to a more balanced foreign currency demand and supply.

On the other hand, the eventual actualization of the foregoing scenario bears some levels of uncertainty that will affect the macroeconomic management policies and their decision-making. The performance of the

Albanian economy with regard to the foregoing will also determine the Bank of Albania's stance in the future.

In what follows, I will elaborate upon the current and expected economic developments and the main conclusions of the Supervisory Council's decisions that motivated today's decision-making.

The global context surrounding economic developments at home shows heightened uncertainty. The world economy continued to show positive but downward growth rates in the third quarter of the year. This slowdown is expected to persist in the fourth quarter. To a large extent, this owes to the lower fiscal stimulus, sluggish labour market, further correction of economic agents' balance sheets and low consumer confidence. Worldwide inflationary pressures remain low, but food and primary commodity prices have picked up. Volatility in the financial markets has elevated due to uncertainties surrounding some countries' public debt performance.

These developments have yielded a less favourable environment for boosting the national economy. These risks are basically reflected in the projections for a lower contribution of foreign demand to economic growth at home and in the eventual impact of the upward tendency of primary commodity prices on inflation. In addition, foreign capital and financial sources may continue to be limited for a longer time than expected due to foreign investors' reluctance to take risk.

Going back to developments at home, worth noting is that statistical information on the performance of the Albanian economy during the third quarter and onward is preliminary and incomplete. However, indirect available data suggest that the positive growth rates of the Albanian economy have extended over this period as well. In addition, the data suggest a more dissimilar composition of growth in economic activity compared with the first half of the year. Hence, this growth has been driven more by the private sector's demand, while the public sector's contribution has been downward. Moreover, domestic demand has provided greater contribution to economic growth, while the impact of foreign demand on economic activity has been weaker.

The analysis of indirect data on consumption and private investment suggests positive but slower growth. The private sector's capacity to offset the room left by fiscal stimulus will remain the main driver of growth in the future. The Bank of Albania considers that the development perspective and current financial conditions allow for faster growth of demand. Above all, consumption suffers from the uncertainty about the future, while private investments need concrete and clear orienting policies.

The Bank of Albania considers that there is room for the Albanian business and consumer to adopt a more optimistic approach in terms of increasing consumption and investment at home in order to ensure that economic growth reaches its potential.

The fiscal sector continued to pursue a prudent policy in order to keep the budget deficit and public debt in check. As at September, the budget deficit totalled ALL 23.9 billion, down by 50% compared to the same period the previous year. In annual terms, public spending contracted by 3.3% during the first nine months of the year due to the significant reduction of capital spending.

On the other hand, revenue was about 7.1% higher than in the preceding year and their annual growth rate has been upward. The Bank of Albania has supported the measures taken over the course of 2010 and the results achieved in terms of fiscal consolidation.

However, against a background of public debt remaining close to the 60% of GDP threshold, we consider the persistence of fiscal awareness in the years ahead as highly essential. Therefore, the drafting of budget and projections of fiscal indicators for 2011 and onward should be based on cautious assumptions and forecast, and the addressing of potential risk factors should be made duly. In turn, this would ensure one of the main premises for achieving the fiscal deficit and public debt objectives, thus contributing to fiscal sustainability in the medium and long run.

The latest data on the external sector of the economy provide evidence for the curbing of trade deficit correction rates, attributable to the moderate growth of export and more accelerated increase in import.

Trade deficit contracted by merely 0.7% y-o-y in the third quarter of 2010, due to the increase of export and import by 45.3% and 9.5%, respectively. The curbed effect of transitory factors is expected to lead exports to a more normal escalating trajectory. Imports in the meantime will be more stable against a background of improved demand. Therefore, current account deficit correction and sustainability require greater attention in the future.

Economic developments have produced an environment of contained inflationary pressures. Below-potential economic growth has curbed inflation, thus eliminating the augmented inflationary pressures arising from imported inflation or the rise in administered prices. The monetary policy pursued by the Bank of Albania has contributed to providing appropriate monetary conditions for the development of economic activity in line with the price stability objective and for keeping the inflationary expectations contained.

Annual inflation marked 3.0% in October, down by 0.4 pp from September. The absence of demand-side inflationary pressures was expressed in low core inflation rates of 1.9%.

The improved exchange rate stability has slowed imported inflation down. The lower headline inflation rate in this month is to a large extent attributable to the termination of effects of the rise in some administered prices a year ago. Inflation will continue to be affected by the previous rises in administered

prices until the end of the first quarter of 2011 and it may be affected by other rises in the periods ahead.

The analysis of monetary indicators attests to the presence of contained monetary inflationary pressures in economy in the medium run. In September, money supply grew by 12.4% y-o-y, approaching its historical average.

In the meantime, the sluggish domestic demand was also reflected in the low private sector demand for bank lending. Private sector credit grew by 8.0% y-o-y in September, similar as in the first two months' average of the third quarter of 2010. The credit growth rates are however low.

The Bank of Albania considers that the banking system's balance sheets and financial position allow for a more active role in fuelling lending in the future. The Bank of Albania has provided the appropriate conditions for sustaining lending activity by:

- Furnishing the market with ample liquidity,
- Safeguarding macroeconomic stability,
- Ensuring the banking system's financial soundness, and
- Lowering the interest rates and transmitting them fully to the financial markets.

The financial markets featured low risk and liquidity premium, reflected in the continuous decrease of the yields in the primary market and interest rates in the ALL deposit and credit market. In the interbank market, short-term interest rates remained close to the key rate and showed low volatility. Foreign exchange in the Albanian forex market was also calm. The exchange rate was more stable as a result of the current account deficit correction and other macro financial equilibriums in economy.

Considering the foregoing information, the Supervisory Council assesses that the inflationary pressures are well-contained in the medium run. The inflationary expectations will remain anchored around the Bank of Albania's target for inflation.

In the absence of abrupt shocks, inflation is expected to mark rates within the central bank's target in the medium run. The risk factors surrounding this baseline scenario are also balanced.

At the end of discussions, the Supervisory Council concluded that the monetary conditions are appropriate for observing the inflation target in the medium run and decided to keep the key interest rate unchanged at 5.00%.

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

At the High-Level Policy Workshop on Macro-Prudential Policy
Frankfurt, December 14, 2010

Macro Financial Stability in EU Candidate Countries and Potential Candidate Countries: Lessons to be Learned

Dear colleagues,

It is a pleasure to discuss with you our experience with the crisis and share some thoughts on the relevant lessons for the future. My perspective on this issue will focus on the case of Albania; an emerging market economy, which imported the crisis through financial market channels and interconnectedness. The challenges posed to eastern European economies and decision makers were mostly the same in nature, while their policy response differed according to economic structures, institutional differences and degrees of freedom enjoyed by them.

Let me briefly preview the three main messages of my speech.

The first one is that there is no conflict between price stability and financial system stability in the long run - instead, they do mutually re-enforce each other and the resilience of the economy to external and internal shocks. From a central bank's point of view, a corollary to this is that any macro-prudential measure taken to enhance financial stability is an investment in medium and long term price stability. I believe this conclusion is amply borne from Albania's recent experience.

My second message is that global or even regional financial markets require global or at least regional supervision and crisis resolution mechanisms. Just as problems originating on a particular sector of the economy can escalate into general macroeconomic imbalances, so financial market imbalances in one financial institution or one country can disrupt other financial institutions or countries. Collaboration between home-host supervisors is therefore a must, but I would argue that probably more can be done in this regard.

My third message concerns the role of anchors in the design and implementation of macro-prudential policies. Monetary policy is made credible from the clear focus on a transparent measure of price stability (CPI inflation), which in turn increases the accountability of the central bank pursuing it and ultimately its operational flexibility. Financial stability is inherently a more difficult concept, even on a theoretical level, but I think more should be done to quantify the term and unify its understanding. This would allow for more transparent communication and increased public support for the central bank's action.

I will now expand on these issues.

1. PRICE STABILITY AND MACRO-PRUDENTIAL MEASURES

A panoramic glance at the experience of central and eastern European economies with the latest crisis would indicate a broad range of outcomes. While this might look normal at first view, it is worth remembering that CEE countries share quite a few commonalities in their economic and financial structures. Furthermore, they were hit by the same type of external shock, at exactly the same time. One has thus a fair approximation of a controlled experiment on the role of macroeconomic policies before and during the crisis.

At the risk of generalizing too much, I would say that CEE economies shared broadly the same development model and problems. We benefited from large capital inflows mainly in the form of FDI, remittances and cross-border loans. Western European banks penetrated our financial system, increasing financial intermediation and facilitating capital inflows. This process resulted in fast credit and economic growth based on a consumption-led model. While inflation has been generally under control, financial imbalances and vulnerabilities were increasing, in the form of rapid growth in real estate prices and balance sheet exposures in liquidity and foreign currencies.

Our economies were hit by the crisis since the first week of October 2008. The fear of contagion was enhanced further by a sharp decrease in the market value of the EU banking groups that operate in the region. It affected negatively the public trust in the system, resulting in widespread deposits withdrawals. Later, as the financial crisis progressed and transformed into a global economic recession, the effects extended to the real economy and exchange rate depreciation. Most of the countries in the region faced a rapid liquidity shortage caused by the deposits run, lower remittances and FDI outflows. The balance sheets across the region suffered from both liquidity problems and exchange rate depreciation. This was negatively reflected in consumption and investment, which further deteriorated the financial stability outlook with the possibility of a balance sheet deflation and economic contraction mutually supporting each other in a vicious spiral.

The ability of our economies to absorb these shocks was however different. The natural instinct of macroeconomic policies facing such a contraction scenario is to engage in countercyclical measures in the form of expansionary monetary and fiscal policies. However, the very presence of financial stability concerns in the equation significantly changed the equation. We can safely argue that countries which experienced the least macroeconomic and financial imbalances were the ones better placed to pursue countercyclical policies and in fact the ones which emerged the fastest from the effects of the crisis.

I believe Albania is such a country:

- We had no bank failures or public injections of capital;
- We did contain and reverse the confidence crisis in the financial system and its adverse effects. In fact, we did not experience financial disintermediation;
- We did continue to grow, albeit at a slower pace;
- We did manage to keep inflation expectations anchored.

Therefore, I will share with you our thoughts and measures throughout this period. To conclude this topic, I will briefly summarize my personal lessons from this crisis.

Before the crisis, the Bank of Albania was concerned for the possible financial threats that were being accumulated during the years of fast financial intermediation. To illustrate the point: most of the credit growth went to the non-tradable sector, with services and construction accounting for most of the expansion. At the same time, more than 70% of total credit was in foreign currency with Euro making the biggest share of the outstanding stock.

The tune of that period was the same in the entire region. The overall impression was that the financial innovations had reduced the risk and the abundant global liquidity had created a very optimistic picture. Despite some truth in this, the pace at which financial intermediation grew annually was frenetically high. In particular there were two main aspects of financial intermediation that were particularly troubling in my opinion. First, economic agents created financial excesses using mostly the financial system. While meeting their needs, the financial system aligns and matches agents' positions according to length of maturity and liquidity. This holds true under the assumption that all claims and obligation will be fulfilled in timely manner in the same order. Otherwise if they violate this assumption and end up overlapping each other, then the financial system might become unstable. Our concern was that too many gaps were opening too fast and the Albanian economy seemed to experience some sort of what later came to be named as risk-taking channel. Second, there appeared to be a general mispricing of risks from the banking sector. High concentration in particular sectors or clients indicated undue risk analysis or risk management from banks, while lending to unhedged borrowers in a flexible exchange rate regime seemed to be a potential moral hazard issue.

We addressed the first issue through increasing information sharing and facilitating the dialogue between the monetary policy and the financial stability and supervision of the Bank. Normally, the foresight of monetary policy is from the trough to the pick of the business cycle because it is mandated with smoothing the fluctuation in economy or prices. However, the duration of financial gaps and excesses might be very different and usually much longer. Therefore monetary policy by design has the potential to forget about financial stability; therefore we were potentially missing important information

regarding the effects that decision making on monetary policy could have on the sustainability of agents' budgets. That is why I believe was important to have guardians of financial stability in the monetary policy decision making process. With this reasoning we have brought the Director of Supervision and the Director of Financial Stability in the Monetary Policy Advisory Committee. In this respect, our monetary policy did not focus only on the discussion of macro effects but also on the discussion of the micro effects of decision making. This resulted in policy coordination within the central bank. I believe that this is the first line of defence that we had in our philosophy. This helped us strike the correct balance between all policies.

The second issue was addressed through tightening macro-prudential regulations and policies and strengthening the on-site supervision of banks. Through regulatory and supervisory interventions, we aimed to improve the commercial banks' governance and their transparency, to strengthen their risk assessment and risk mitigation strategies, to improve the capital adequacy and liquidity ratios, as well as to reduce the exposure to credit risk stemming from unhedged borrowers in foreign currency or predatory practices from commercial banks.

BOX 1 MEASURES TAKEN IN THE BANKING SUPERVISION AREA DURING THE PRE-CRISIS PERIOD

- *In June 2007, the new Law on Banks in the Republic of Albania entered into force. This Law stipulates rigorous principles and rules on the risk management, aiming at protecting the depositors, investors and fostering the banking system's stability.*
- *In January 2008, the Credit Registry started the operation representing a vital infrastructure-related development.*
- *In March 2008, the Bank of Albania adopted a package of regulatory amendments, which were generally oriented to adopting more conservatory policies in several main directions of day-to-day commercial banking running.*

In more concrete terms, this therapy can be described:

- *In compliance with the new Law on Banks in the Republic of Albania, new quantitative thresholds were set for the calculation, supervision and reporting of banks' large exposures to parent banks and related entities.*
- *In order to better diversify the risk arising from the concentration in banks' investments in the international financial markets, lower thresholds were set for banks' large exposures.*
- *Internal control is considered an integral part of banks' governance. Hence, special emphasis was put in designing the key principles for an independent, unbiased and accountable internal control. Internal control should cover each section of the bank in order to prevent the origination and development of undesired risks.*

- *Accountable governance is a key principle, especially on financial institutions, whose success is, among others, largely dependent on public confidence in them. Accordingly, the Bank of Albania considers the quality of human capacities - implying the hiring of skilful people in the decision-making process and risk management - as fundamental. The decision making process should always be based on such expert opinions and recommendations.*
- *The transparency related to the banking and financial products and services provided was also paid special attention. The new legal requirements standardize the manner and form of providing information to the clients on the banking products and services banks provide.*
- *Part of this new package was also the standardization of the required information that banks and branches of foreign banks should disclose, related to the banks' main activity, their organization and management, their financial performance and position, the risk management and the accounting policies.*

On the same line, our policy response during the crisis was cautious, prioritizing financial stability and the preservation of inflation expectations to outright economic stimulus. By the beginning of the first quarter of 2009, financial panic, liquidity problems especially in foreign currency, slowdown in EU economic area and the financial stress in the EU banking system affected both the real and the financial sectors of the Albanian economy. Credit slowed down considerably, exchange rate started to depreciate, and forecasts for economic growth and inflation were down. In the meantime, deposit withdrawals continued and liquidity concerns became more prominent.

The Bank of Albania provided ample liquidity in domestic currency in the interbank market while tightening its supervision on banks and increasing the collaboration with their home supervisors. A specific feature that needs to be mentioned is the timely increase of the deposit insurance scheme. This move marked a turning point in the confidence crisis of the public to the banking system and the liquidity problems of the system.

From a narrow perspective centred on its main objective of price stability, the focus of monetary policy would be an expansionary action. However, considerations of the external balances of our economy, its financial stability and the need to anchor expectations, constrained our decisions. I will elaborate briefly on these factors. Faced with contained upward pressures in inflation, the central bank focused its attention on determinant factors of financial stability. By refraining from pursuing an expansionary monetary policy, the central bank did not exacerbate the pressures on the exchange rate which would then put additional strain on unhedged borrowers and the banks' balance sheets. Furthermore, interest rate cuts had the potential to affect deposit withdrawals and cause liquidity problems and further depreciation. At the time these two were the main concerns to financial stability.

The Albanian economy did however receive some macroeconomic stimulus in the form of fiscal expansion. This countercyclical policy was made possible because of the previous work done to consolidate the fiscal position and to anchor macroeconomic policies and public expectations. Albania approached the crisis with sustainable fiscal position in terms of deficit and public debt, creating room for manoeuvre and fiscal expansion to support the economy before monetary policy could intervene. Therefore the first lesson from the crisis for authorities would be to follow countercyclical policies, which will permit for bolder action in time of crisis.

What are the lessons for the future? I think I already mentioned the first one. The second lesson, which relates to the price and financial stability, is equally important. Price and financial stability do not conflict each other in the long run. Central bankers should never forget that fiat money on which we base our way of life and prosperity, is a social contract, based on the society's trust that every bill will be honoured by the creator of that money, which in most of the cases is the central bank. This trust is one of the important pillars that guarantee not only the economic system but the entire society.

In my opinion, even in the short run, the central banks are well equipped to pursue these two goals with the instruments at their disposal: main policy rate on refinancing operation; macro-prudential policies on a systemic level; and, careful and diligent micro supervision of commercial banks. Having two goals and at least two instruments should allow for an optimal mix of policies, at least in theory. In practice, as is indicated from our experience, central banks should not shy to lean against the wind in order to discourage or at least contain financial imbalances. Furthermore, every time we face fundamental economic problems with potentially negative systemic implications, we revert to financial stability. I firmly believe that the first and most important job for a central bank is to ensure the integrity of money and the banking system.

2. JOINT SUPERVISION AND CRISIS RESPONSE MECHANISMS

Building bridges of continuous communication with local bank managers, home supervisors and headquarters of the parent institutions has proved to be critical in dealing with the problems before they get out of hand. While communication is an advice that is frequently used, we made a good use of that beyond mere courtesy. We acknowledged that financial development was following a certain pattern. Financial institutions like all other businesses adopt marketing strategies and stick to such strategies in all markets. What this means for us is that once new products are developed and tested in other markets, they will follow the same pattern of marketing in other markets as well.

In the years that preceded the crisis, financial institutions started the practice of lending in exotic currencies, offering very low interest rates and being without any economic relation with the borrower's activity. Being aware of these developments, from previous communication with other central banks

in the region, we were alerted to spot the first sign of such behaviour in our economy. Therefore at the first signs of such credits, we discussed with the management of our banks and stopped administratively lending in these currencies for all unhedged borrowers.

On a systemic level, I do believe the recent experience highlighted some issues that need to be looked more carefully in the future. I will highlight here only three of them.

- The policies that facilitated the capital inflows into economies of the region were not followed by actions which could have provided the needed liquidity when these flows reversed or stopped. Countries of the region did not benefit from the swap agreements or similar arrangements that would allow us access to short term liquidity. One can certainly say that in normal times that could be resolved at group level. However, this didn't necessarily prove to be the case in the recent experience. Because our financial systems are inter-connected, I think this issue deserves more attention in the future.
- A crucial step in alleviating the financial crisis in CEE countries was the Vienna initiative, which stabilized both the balance sheets of the big banking groups operating in the region and the trust of our public in them. I think such a facility needs to be permanent, at least in the case of global or European potential financial crisis. While it has certainly its drawbacks, not the least in the form of moral hazard issues, it would increase the resilience of the banking system and would encourage more cooperation between home and host supervisors.
- Financial regulation and regulatory arbitrage was a serious issue before and throughout the crisis. Before the crisis, banking groups would play regulatory regime and policies against each other and try to reach some kind of lowest common denominator throughout the region. Countless times we have heard the complaint "Why are you not allowing this, your neighbours do!", and I'm sure other people in this room have heard it too. During the crisis, we experienced several cases of countries trying to seek individual solutions to common problems. While fully respecting the idiosyncrasies and different timing priorities of each country, I think we would all benefit from a more collegial approach to regulation.
- On a national level, I believe the stress should be on the supervision of Systemically Important Financial Institutions, with the right care not to create wrong perceptions related with moral hazard. In our region, these institutions are typically banks. In my view, these banks should become subject of a more stringent regulatory framework, in terms of capital and liquidity requirements, business and risk profile, including contingency plans. The supervisory authority should always be prepared for the worse and make sure that crisis management procedures are complete and tested. In this process, valid recommendations

of international organizations will be closely followed for adequate implementation over time. It is important to have close coordination with other public authorities in the country, including the government.

3. ANCHORS OF MACRO-PRUDENTIAL POLICIES

The role of anchors in monetary policy is well known. I mentioned before that an important lesson from the crisis for authorities would be to rigorously pursue countercyclical policies. I would like to stop a bit here and focus on this issue. I believe that Albania was prepared for the crisis because IMF programs have played an important role as a credible foreign anchor for economic policies. The IMF programs and EU membership process have played a similar role in all CEE and SEE countries. However, as the countries have matured out of these programs or joined the EU, the political incentives to continue fiscal consolidation have been fading away. Current events show that the symptoms have spread to other older members of EU, where such policies become the reason behind instability.

Therefore, the role of anchors is very important for preserving and safeguarding financial stability. A sound, clear and enforceable fiscal rule would be an important step. Effective supervision based on simple and clear capital adequacy and liquidity rules would be another. The Basel III accord is a first step in the right direction. A unified approach and technical toolkit to stress-testing exercises would be also helpful. The joint stress-test exercise conducted by the ESCB is the right way forward. I would however encourage broadening its scope in candidate and potential candidate countries of CEE, in order to have a unified measurement system throughout Europe. Lastly, other measures of financial imbalances such as excessive asset price increases, under-pricing of risks, search for yields and increased risk taking need to be better incorporated in the standard models used by central banks.

CONCLUSION

In the light of this discussion, a central bank could not avoid the responsibility of engaging to protect financial stability, even though this is not defined as a particular mandate. Our experience as an emerging country indicates that price and financial stability are preconditions for each other. Our motto is that any investment that we make in financial stability today will return high benefits in price stability in the long run.

Concurrently, I think our collective experience throughout the crisis showed that more can be done in order to develop and institutionalize the proper mechanisms that would allow for better FX liquidity management in EE countries. A mechanism such as the Vienna initiative that would encourage the commitment of parent banks to their EE subsidiaries and would discourage their financial disintermediation in these countries can be made permanent with

added benefits to all the stakeholders. Furthermore, regulatory harmonization can be improved and regulatory arbitrage can be mitigated.

On macro-prudential policies I argued on the need to develop specific anchors that would make the goal of financial stability more credible, transparent and therefore achievable. Measuring financial stability, or instability, might be difficult but that should not discourage us from trying.

Thank you for your attention.

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

At the Reception Held by the Albanian Association of Banks
on the Occasion of the Closing of the Year 2010
December 16, 2010

Dear bank executive managers,
Dear guests,

It is always a pleasure to meet once the year-end approaches to make a summary of events that characterized the Albanian economy and the banking sector over the course of 2010.

The Albanian economy is forecast to grow in 2010 slightly higher than in 2009. Industry and services provided the largest contribution to the positive economic growth, yielding as well a relative improvement in the balance of payments' current account. Lek's exchange rate was more stable compared with the preceding year, whilst consumer prices fluctuated within the Bank of Albania's target of 3%.

Fiscal policy engaged in a process of fiscal consolidation during the present year, which we consider as critical in order to preserve the budget deficit and domestic debt levels and keep the level of interest payments in check.

Developments in the financial system attest to the full recovery of public confidence in the banking system. As at end of the third quarter of 2010, total banking sector assets accounted for 81.7% of GDP, up 12.2% y-o-y versus merely 0.9% in the same period in 2009.

Deposit growth and higher capital account provided the major positive contribution to the expansion of banking sector activity. Deposits have grown by 18% y-o-y, out of which more than 2/3 of this figure represents foreign currency-denominated deposit growth. Banking sector treasury and interbank operations declined versus the same period in 2009. Liabilities to non-residents have dropped by 32% y-o-y.

Concerning the composition of banking sector assets, we note that lending has grown by 8% on a yearly basis. The annual growth rate of lending has been constantly downward in the last couple of years. Banking sector and interbank operations have grown by about 25% on a yearly basis.

Banking sector investments in non-resident assets increased by 53% y-o-y. Net profit was positive and substantially higher than in the same period in 2009. Return on Assets and Equity stood at 0.6% and 6%, respectively. Capitalization and liquidity figures were at adequate levels. Capital adequacy ratio was estimated at 15.7%, while liquid assets accounted for 28.9% of total assets. As part of the regular stress-test analyses conducted by the Bank of

Albania, in the context of a more comprehensive risk evaluation, the banking sector results stable.

Let me now elaborate on some issues I find critically important for the future.

The banking sector weathered the hard liquidity situation at year-end 2008 and early 2009 successfully. Following that period, public deposits in banks have grown at stable rates and liquidity has improved markedly. However, lending has contracted pronouncedly, initially, as a result of the higher credit risk, and later, due to the fall of business and consumer demand for loans.

Therefore, the free funds were invested in non-resident assets against a background of lower return on investment in the global market. The deteriorated loan quality, the obligation to increase the reserve funds and the lower average rate of return were followed by the decline in the banking sector net profit.

For some banks, this situation needs careful monitoring by the governing structures and shareholders in order to identify those operations that would improve the expenditure and income structure of the activity and maintain its capitalization levels.

With regard to lending, the Bank of Albania has continuously called for greater banking sector commitment in this regard. This has not been a rhetorical-like request considering that we have taken all the necessary actions to meet the banking sector needs with ample liquidity and we have cut the key interest rate several times. These measures, coupled with lower Government borrowing, have provided room for lower interest rates on ALL lending.

Nonetheless, their decrease still seems insufficient to push credit demand higher. Loan quality remains a challenge both for ALL and foreign currency-denominated loans. Against this setting, it is essential that banks do not only create, in a prompt and rigorous fashion, reserve funds according to the regulatory requirements, but also complete and improve the procedures and human and financial capacities that enable following-up insolvent borrowers. The complete acknowledgement of loan quality-related concerns and the full commitment of governing structures and shareholders allow for its more rapid and ultimate handling.

Otherwise, the banking sector's capacity to intermediate more effectively would be impaired for a longer time. Banks need to be determined to follow collateral execution procedures for insolvent borrowers. On the other hand, court decisions and particularly the actions of bailiff officers should be prompt and effective. I take this opportunity to appeal to the authorities to prioritize these actions.

If legal procedures need to be complemented and improved further in order to enhance efficiency, the banking industry should make the necessary

proposals in a prompt fashion and the public authorities should commit to considering them.

Lastly, I want to elaborate on two other issues. The first relates to governance and accountability in banking operations and the second to the improvement of capacities for the identification, evaluation and management of risks.

These two issues have continuously been part of our regular communication as they rest on the cornerstone of a safe and successful banking activity, public confidence in which remains unwavering.

Concerning governance, last year I constantly highlighted the need for professionalism, commitment, responsibility, farsightedness and accountability to be reflected not only by you but be also embodied in your staff.

To make this happen, policies and rules for defining strategies for the development, concrete decision-making, control of particular activities and their reporting to the institution and the public need to be continuously completed and improved. Internal control systems are the ones to determine the institution's capacity to operate safely. They are indispensable to avoid any room that may be used for abusive actions that would impair the institution. I therefore request that you take the necessary measures in terms of financial, human and technological capacities in order to ensure the safety of each banking operation.

In pursuing its supervisory function, the Bank of Albania will have this matter under close focus and I assure you that any decision that may have hampered the safety of the activity will be handled with utmost stringency by the law. In a broader context, banking activity, in addition to operational risks, is faced with other financial-related risks.

We will therefore increase the regulatory requirements for banks to be engaged in an integrated process of risk evaluation and management proportionate to the level of development and sophistication. In a more practical approach, this implies that banks should have specific functional structures that monitor risks in the main activity areas, and seek to anticipate their possible evolution and impact on banks' activity. These structures must be in place in the largest banks and their products should be an integral part of the decision-making process.

Dear guests,

We are leaving behind a challenging year but other numerous challenges will follow for banking activity. They provide us the opportunity to put our vision into practice, in order to ensure a stable banking activity as a precondition for conducting an efficient intermediation activity with remarkable contribution to economic development at home.

Weathering the challenges requires courage and professionalism.

In addition, banking institutions should provide an environment where accountable and professional human capacities are in the service of the public and the institution. I am confident that you will prioritize the foregoing matters in 2011.

I wish you success in your work and many wishes for the New Year!

Thank you.

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

At the Presentation of the First Financial Stability Report
of the Central Bank of the Republic of Kosovo
December 21, 2010

Dear Mr. Gërguri,

Dear Members of the Governing Board of the Central Bank of the Republic of Kosovo,

Dear Mr. Yilmaz,

Dear guests,

It is always a great pleasure for me and my colleagues to come to the Central Bank of the Republic of Kosovo. I would like to express my positive consideration that this institution is now well-shaped and is growing stronger at a stable and rapid pace. This development is an outcome of the clear vision of the governing structures and the commitment of the central bank's staff in implementing the best standards relevant to the area. This time I am invited to testify another achievement of this institution, the first release of the Financial Stability Report.

I have the conviction that the public authorities, economic operators in Kosovo and the public will appreciate the contribution of the central bank with respect to the identification and management of risks facing the financial system's activity.

In my speech I will first provide a general assessment of the great deal of importance given to financial stability issues and the central bank's role in this regard. Then I will share our experience at the Bank of Albania with the institutional approach to financial stability assessment function.

The global crisis, which originally emerged as a financial system crisis, very soon transformed into a real economy crisis. Due to the high integration of financial markets as a result of the presence of financial institutions engaged in cross-border activities and the manifold inter-institutional exposures, a financial system crisis can spread rapidly across many countries. On the other hand, due to the exceptional role in financial intermediation, a financial system crisis may hit the real sectors of the economy, placing the economic mechanism in a negative spiral that tends to reinforce itself.

These developments will likely result threatening to the sustainability of the entire financial system and be followed by severe social consequences that are costly to public wealth.

This two-year experience triggered an accelerated identification process of the mechanisms and measures that aim at preventing and handling similar situations in the future. At a broader economic context, these measures aimed at reforming the international monetary framework and reduce imbalances in the global macroeconomic framework.

G-20 policy-makers, the Basel Committee, the Financial Stability Board and the international financial institutions have set out some measures, which in fact have only one aim: reduce systemic risk and create the conditions for its proper management.

At a global level, these measures envisage:

- a) Reforming the supervisory superstructure by establishing institutions that focus on assessing systemic risk;
- b) Setting higher quantitative and qualitative capital and liquidity requirements for systemically-important financial institutions, hence reduce their appetite for excessive risk-taking;
- c) Determining the mechanisms that reduce procyclicality in financial activity, mainly by creating reserve funds (in the form of capital or provisions) that may be used for countercyclical purposes;
- d) Strengthening the capacity of national authorities to address systemic financial crises.

For this purpose, legal changes need to be made in order to regulate the harmonization of inter-institutional relationships at home and abroad. I would summarize the following:

- Actions between supervisory authorities of different countries,
- Actions between public authorities at home, and
- The implementation of actions that enable a smooth exit from the market of those financial institutions that cannot be recovered.

Central banks play an important role in this process, which in some respects is unique and exclusive. In the monetary area, it should be guaranteed that the liquidity injection and collateral evaluation procedures are complete and adequate.

In the meantime, the sustainability of systemically-important infrastructure, more precisely the payment systems', must be monitored and guaranteed. Moreover, if the central bank is also responsible for the licensing and supervision of the banking sector, a modern supervisory framework must be in place in order to prevent and reduce systemic risk in accordance with the new international standards.

Public authorities should be prepared to act in situations of financial emergency, aiming at preserving public confidence in the financial system and ensure that there is a limited and efficient use of public resources. In the context of the role of a central bank that carries out an independent monetary

policy, the integration of financial stability considerations into the monetary policy decision-making is particularly important.

Countries of our region share similar features in terms of the financial system and the economic structure. Banks make up the bulk of activity and they are regulated and supervised by central banks. We almost share similar banks operating in our banking sector. Hence, the developments are similar and the dynamics of the emergence and performance of risk is often alike.

Though we do share similarities, we also have certain differences, mainly related to the monetary area and the capacity to implement an independent monetary policy.

Both similarities and differences are important in order to understand the role of our institutions in the assessment and availability of actions taken to safeguard financial stability. Despite the arsenal of these actions, central banks cannot carry out this mission alone. They are in possession of a full arsenal of measures and instruments, but their implementation, albeit timely and complete, cannot have full effect unless they are coordinated and supported by other agents' actions.

It is thus essential that all economically-important agents, public authorities, the public at large and the media are fully aware of this matter. Apart from legal definitions, this awareness requires receiving comprehensive, regular and timely information on the events that may jeopardize financial stability, and identifying the necessary protective actions. The regular release of reports dedicated to financial stability is the key instrument that meets this obligation.

Let me now share with you our experience at the Bank of Albania. According to our concept, the Bank of Albania has full legal responsibility for safeguarding financial stability.

The Bank of Albania is attributed the exclusive role of licensing and supervising the banking activity, the right to organize and monitor the operation of the payment systems, the lender-of-last-resort function to assist banks facing difficulties, the liquidity management function in the interbank market, and the determinant role in foreign exchange policy.

The Bank of Albania has the obligation to inform the public about the events that may jeopardize the financial stability. In early 2007, the Supervisory Council of the Bank of Albania considered a better coverage of developments in the financial system – that is, not only in the banking sector's alone – as highly important. In addition, it required strengthening the analysis of interaction between macroeconomic developments and the financial system's activity.

Our ultimate goal was to set up a more sustainable mechanism that would allow the conversion of these analyses into proposals for concrete actions, in order to reduce systemic risk not only through the Bank of Albania's actions

but also through measures taken by other public authorities that have a role in monitoring the developments in the financial market.

From the institutional viewpoint, in September that year, the Supervisory Council of the Bank of Albania, approved the establishment of the Financial Stability Department, by selecting the most outstanding human capacities in the area of monetary operations, banking supervision, research and statistics.

The conclusions derived from the analysis of this department would be regularly discussed at a higher central bank level, thus providing a useful filtering and enriching mechanism prior to the decision-making of the Supervisory Council of the Bank of Albania.

For this purpose, in November 2007, the Supervisory Council approved the establishment of the Advisory Committee on Financial Stability (ACFS), which gathers the high executives of the Bank of Albania and the heads of the main departments.

According to the regulation on the functioning of the ACFS, representatives of other public authorities are also invited to attend the meetings in cases when matters of particular interest are being discussed.

In addition to analyses for internal use purposes, the Financial Stability Department is responsible for releasing these two main products: a) Financial Stability Statement, which is also mandated by law; and b) Financial Stability Report. From the institutional viewpoint, this process has progressed. Very soon, the Financial Stability Department became operational and the Financial Stability Report, which was prepared and released from the first year this Department was established, has been released regularly and at an ever-increasing quality.

However, we had to face several challenges along this process, which I think exist no matter if the financial stability's assessment function operates as a single structure within the central bank or not. Among them I could mention:

- a) The necessity to obtain complete information from all the sectors of the economy and produce complete, reliable and timely statistics;
- b) The necessity to establish better communication among different departments within the central bank, as well as between the central bank and other institutions that may have a role in monitoring the financial market. This communication creates optimal conditions for the clear identification and full assessment of the most important issues that have affected and are expected to affect financial stability during the periods under consideration. Ultimately, a good level of communication allows inter-institutional cooperation to address the concerns that may jeopardize financial stability effectively;

- c) The need to quantify systemic risk. This objective is obviously not easy but our endeavours in this regard must be ongoing and begin from the easiest and concrete approaches;
- d) The need to have a balanced content of the Financial Stability Report. In this regard, we focused on the following considerations:
- First, this Report attempts to clearly identify the underlying risks to financial stability, not only those created as a result of the financial system's activity, but also those stemming from its interaction with the surrounding economic environment.
 - Second, the Financial Stability Report is an essential element of the monetary policy decision-making, thus providing a real understanding to macro prudence (Stability and monetary policy slogan).
 - Third, we intend this Report to be part of the triologue philosophy, which involves the Bank of Albania, the Government and the market, at an appropriate level of transparency before the media and the public at large.
 - Fourth, we intend not only to produce a Report that limits to the description of past events, but also enrich it gradually and to a certain extent with research analyses and incorporate elements of forecast.
 - Fifth, the Report should arrive at some conclusions on the issues it addresses, which enable the identification of relevant recommendations.
 - Sixth, the contents of the Report should include a main part, which must be consistent over time for the effect of consistency of analysis and its comparability, and another part which provides greater degree of freedom to elaborate on more specific issues that materialize the main analysis.
 - Lastly, we have paid special attention to the language used in producing this Report, aiming at using plain and clear language, free of equivoques and understandable to the professionals of this area and the public at large.

We are fully aware that this process requires constant improvement.

Dear guests,

In conclusion, let me offer the support of the Bank of Albania in cooperating with the Central Bank of the Republic of Kosovo on matters relating to financial stability. This cooperation may aim at identifying matters of importance for both institutions, which later may turn into joint projects.

More concretely, we can cooperate on the assessment of the suitability of stress-test methodologies or on the process of systemic risk quantification. In a more informal fashion, the parties may exchange information on the issues to be addressed in the next Financial Stability Report.

The parties may also discuss the way of transforming the findings in the Financial Stability Report into concrete actions of the central bank and other public authorities. I am fully convinced that regular and constant communication on these issues will expand into possible directions of cooperation.

Once again, I wish you success in your work!

Thank you for your attention.

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

At the Press Conference on the Monetary Policy Decision-Making of the Supervisory Council of the Bank of Albania
December 22, 2010

At today's meeting of 22 December 2010, the Supervisory Council of the Bank of Albania analyzed and approved the Monthly Monetary Policy Report for December. After scrutinizing the latest economic and financial developments at home and further to discussions on their future outlook, the Supervisory Council of the Bank of Albania decided to keep the key interest rate unchanged at 5.00%. In the Council's view, the current monetary conditions are appropriate for meeting the inflation target in the medium run.

Let me provide a brief overview of economic developments and the key issues discussed at today's meeting that motivated the foregoing decision.

Our analyses, which are based on the latest available economic and financial data, corroborate the persistence of positive economic growth rates in the second half of 2010. The assessment of economic growth by aggregate demand components shows its greater reliance on foreign demand for Albanian goods and services, whilst the growth of domestic demand remains moderate.

The latter's performance has been highly determined by the withdrawal of fiscal stimulus, which was particularly pronounced in the second half of the year. On the other hand, the increase in consumption and private sector investment remains poor, mainly due to the more conservatory behaviour of households and businesses in their expenditure and investment-related decisions. Economic growth rates, albeit positive, are below potential, thus yielding downward inflation rates during 2010.

The analysis of monetary indicators corroborates the presence of subdued inflationary pressures in economy in the medium run. At this juncture, annual CPI inflation maintained downward rates during the second half of 2010. In November, it marked 2.8%, slightly below the Bank of Albania's target.

In more elaborate terms, the latest data on world economy attest to a more moderate economic growth and trade exchange rates in the second half of the year. In the large industrialized economies, the persistence of economic growth was hampered by the progressive correction of economic agents' balance sheets, the poor labour market performance and the low consumer confidence.

In the meantime, economic recovery in emerging countries was more stable than in industrial economies, albeit more moderate than in the first half the

present year. Against a background of negative output gap at a global level, inflationary pressures remain by and large subdued.

Going back to developments in the national economy, indirect data suggest the sluggish increase in consumption and private investment in the third quarter of 2010. Despite the higher income – as evidenced by the performance of real wage, number of employed and remittances – consumer demand remains subdued.

The performance of consumer spending is mainly affected by the uncertain outlook as indicated by consumer survey results. In the meantime, the correction of Albanian households' financial balance sheets is required less than in other countries.

Although indirect indicators like the stable growth of investment loans and the increase of FDI in the third quarter of 2010 show positive growth rates during this period, private investment in economy remains subdued. However, in the presence of free capacities in economy and still tight lending terms, particularly for SMEs, private investment growth has been slow.

Future-oriented, I find it appropriate to reiterate the message delivered numerously by the Bank of Albania that the development outlook for the Albanian economy remains positive. We consider that there is room for the Albanian businesses and consumers to review their cautious behaviour adopted on their investment and consumption-related decisions.

Following the countercyclical approach pursued in 2009, fiscal policy in 2010 oriented towards fiscal consolidation and keeping the budget deficit and public debt in check. The data available until October show that budget revenue increased moderately, whilst budget spending was lower y-o-y.

This prudent fiscal approach yielded a deficit of ALL 23.3 billion, down by 53% y-o-y. The persistence of this fiscal approach, oriented towards keeping the long-term sustainability of public debt in check, will provide enough room for lowering the risk premium, keeping macroeconomic balances under control and developing the private sector in the future.

Data on trade exchanges with other countries show a positive contribution of foreign demand to economic growth, albeit more moderately versus the first half of 2010. The annual increase of exports by 63.4% in October was in line with the increase in the third quarter, but lower than in the first half of 2010.

This slowdown owes mainly to the expected reduction in electrical energy exports; however, the increase of exports continues to have a wide basis. On the other hand, the increase of imports in the third quarter and onward reflected in the lower correction of net export deficit. This deficit narrowed by 10.7% y-o-y during this period versus the average of 18.5% in the first two quarters.

This dynamics suggests that the external position remains a structural weakness of the Albanian economy, which requires due addressing by macroeconomic policies and structural reforms.

The persistent negative output gap, complemented with a stable exchange rate, termination of the effect of the rise in some administered prices and the anchored inflation expectations, materialized in the further decrease of the annual inflation rate in November.

Annual inflation marked 2.8%, falling below the Bank of Albania's target for the first time over the course of 2010. Annual core inflation marked 2.0%, thus corroborating the presence of weak demand-side pressures.

Monetary developments were broadly in line with the performance of real economy indicators. Broad money, M3, grew by 11.7% in October, quite close to its historical average. Our assessments show that money supply growth is in line with the real demand of economic agents for money.

The moderate private sector demand for money reflected in bank lending activity as well. Private sector credit grew at low historical rates, up 8.0% y-o-y in November. Loans for business investment purposes recovered during 2010, being also sustained by the increase in foreign currency lending. Mortgage and consumer loans show a poor performance. Our analyses show that there is still room for the lending terms applied by the banking system, mainly "non-price" lending terms, to ease further.

However, the main concern behind the non-satisfactory performance of lending is the low business and household demand. The Bank of Albania considers that once credit demand recovers, the banking system will meet all the required preconditions for carrying out its financial intermediation function. The banking system remains liquid, both in Lek and in foreign currency, and well-capitalized.

The financial markets were calm and featured low risk premium. Short-term interest rates in the interbank market stood very close to the key rate. Government security yields in the primary market dropped further as a reflection of the ample banking system liquidity and the low Government demand for funds. The interest rate on Lek loans remains at low historical levels, while that on Lek deposits dropped further.

The Lek continued to narrow its depreciation against the foreign currencies. The trading of the latter in the domestic market was relaxed and featured low volatility.

Our projections suggest that economic activity in 2011 will perform broadly in line with its performance during the current year. Economic growth will be positive, but the Albanian economy will continue to suffer the presence of non-utilized capacities, thus generating an environment of subdued inflation pressures. Inflation expectations will be anchored around the Bank of Albania's

target for inflation. CPI inflation is forecast to continue to mark rates close to our 3% target in 2011.

The distribution of risks around this baseline scenario is relatively balanced.

On the upside:

- A better performance of the Albanian economy due to the rapid increase in trade exchanges with abroad or the higher fiscal stimulus,
- Further rise in administered prices; or
- Further rise in global primary commodity prices,

may elevate the inflationary pressures.

On the downside, the lack of private sector capacity to offset the downward contribution of foreign demand may widen the negative output gap and be followed by subdued inflationary pressures.

Based on these considerations, the Supervisory Council concluded that the monetary conditions are appropriate for meeting the inflation target in the medium run. The Council decided to keep the key interest rate unchanged at 5.00%.

CONFIDENCE INDICATORS, THEIR INFORMATION CONTENT AND SYNCHRONIZATION WITH EU COUNTRIES

ERMELINDA KRISTO *

ABSTRACT

Monitoring and analyzing the economic situation is a key process in monetary policy decision-making. A vast number of statistical indicators are considered during this process. This paper introduces the confidence indicators currently used at the Bank of Albania and the main uses of the information they contain. It also introduces two new uses: the study of the business cycle phases and the extent of synchronization between this cycle in Albania and other European Union countries.

** Monetary Policy Department, December 2010.*

The views expressed in this publication are the views of the authors and do not necessarily reflect the views of the Bank of Albania.

I. WHAT ARE CONFIDENCE INDICATORS (CIs)?

Data from business and consumer confidence surveys form part of the broad range of information available on the performance of economic activity and its short-term prospects. They provide in-depth information on various aspects of business economic activity and consumer behaviour. On a broader setting, survey data are used to measure less tangible concepts: economic “confidence”, “sentiment” or “tendency”. Although it is impossible to measure “confidence” quantitatively, it may be proxied through direct qualitative questions to business managers and households. These questions aim at measuring different aspects of businesses and households’ economic life. Theoretically, respondents have established an “opinion” or “confidence” prior to making decisions that have economic consequences (e.g. expansion of production activity, hiring of new employees, the acceptance of new order contracts, etc.). In addition, if consumers feel “more optimistic”, they will consume more thus increasing aggregate demand.

The information collected in confidence surveys is often described as qualitative, because respondents are asked to respond to questions on different aspects of the business life or consumer behaviour through an opinion, and assessing each aspect qualitatively rather than quantitatively. For example, in a business survey related to the performance of orders during the current quarter, the respondents might be asked to assign qualities such as “higher than normal”, “normal” or “below normal”. In a conventional quantitative industry survey, on the other hand, respondents may be asked to give quantitative information about their order books, such as the actual value of outstanding orders. It is generally much easier for respondents to give

qualitative rather than quantitative information (the former does not require respondents to consult their balance sheet statements or order contracts), hence the questionnaires can be filled in quickly. This is one of the main advantages of confidence surveys. Questionnaires for consumer surveys differ from those applicable to business surveys, however, they generally provide only qualitative information¹.

Business and consumer surveys date back in the history. Consumer confidence survey was introduced about 60 years ago by the University of Michigan and it is known as the Consumer Sentiment Index². Business confidence survey has a history dating from the 1920s and it was carried out by trade associations³. Central banks have been carrying out confidence surveys for some years as they need information on the current economic situation that is more up to date. An important development in confidence surveys in the recent years has been the harmonization of questionnaires with the survey methodology⁴. This allows the comparison of information from surveys among different countries. The information from surveys at the Bank of Albania is constructed based on the information obtained from 700 businesses and 1200 consumers. Çeliku and Shtylla⁵ (2007) and Lama and Istrefi⁶ (2007) provide in-depth information on the methodology of sampling, the construction of questionnaires and other characteristics of the data obtained from business and consumer confidence surveys.

The construction of questionnaires across many countries is very much alike. Surveys involve company managers and households. Their responses in general are characterized as “positive”, “no change” and “negative”. The “net balance” is calculated for each response, where the percentage of negative responses is subtracted from the percentage of positive responses. In cases when the response to a question consists in five categories, two positive, two negative and the one neutral, the response is weighed. The responses “highly positive” and “highly negative” are assigned double of the weight of “positive” and “negative” responses. The balances calculated as described above lose the information obtained from “no change” responses. Some countries include this option in calculating the balance. However, the added information in this case is inconsiderable compared to the balance estimated simply as the difference between positive and negative responses. The percentage of “no change” responses is often used to proxy companies’ and households’ uncertainty about different aspects. In the case of Albania,

¹ An exception to this rule is the question on capacity utilization, which requires companies to provide a numerical assessment, and the question on expected inflation after one year, which requires companies and consumers to choose between the quantitative intervals.

² Information on surveys, University of Michigan: <http://www.sca.isr.umich.edu/documents.php?c=i>

³ OECD (2003): “Business tendency surveys: A handbook”.

⁴ More concretely, CIRET (Centre for International Research on Economic Tendency Surveys), the European Union and OECD work together in designing and promoting the harmonized survey system and expanding it to transition and emerging countries.

⁵ Çeliku and Shtylla (2007): “Vrojtimi i besimit të biznesit: aspekte metodologjike dhe analizë ekonomike e rezultateve”.

⁶ Lama and Istrefi (2007): “Besimi konsumator dhe ekonomia shqiptare. Një urë e re informacioni”.

we note that there is higher uncertainty about those questions that require a degree of judgement on the future and lower uncertainty about those questions that require an assessment of the current situation. At a sector-level, the sector of industry shows the highest level of percentages of “no change” responses, while the sector of construction the lowest.

Balance values range from -100 to +100. A value above 0 shows a greater number of positive than negative responses in a given quarter. The larger in absolute value the bigger is the difference. For example, a balance of +10 pp shows that the number of positive responses is 10 pp higher than the number of negative responses. However, a given balance value in a given time does not imply much unless we compare it with its history over time. This is particularly important in cases of questions that receive repetitive pessimistic or optimistic responses. For example, consumer survey balances have historically marked negative values, while business expectations for the coming quarter are characterized by greater optimism than the current quarter assessment. Therefore, the balance results in a given quarter are not compared to 0 but to their historical average.

In order to better understand the performance of a given sector or the entire economy and to facilitate the analysis, the information obtained from the surveys is integrated into aggregated indicators called confidence indicators (CIs). CIs are time series that consist of several components. They aim at aggregating different economic agents' confidence, sentiment and expectations into a single indicator. By doing so, the analysis of a given sector is facilitated. CIs provide a more general overview for each sector or for the entire economy. The graphical presentation (see Chart 1) is a first step to understanding the information content of CIs. The four confidence indicators are incorporated in the same chart with the real GDP changes. Qualitative indicators obtained from surveys show a similar performance as the changes in the quantitative indicator of the economy, hence implying that they have the tendency to increase or decrease at the same time (for more information refer to part III).

CIs have some features that make them appropriate for economic analyses. Their main advantage is timely availability. CIs are available at the bank two weeks following the reference quarter, while official statistics are available after two or three months. Another advantage of CIs is that they do not require revision. Official data are generally revised periodically. Another characteristic of survey data, as will be shown below, is the high level of harmonization, which allows the comparison across different countries. In addition to these advantages, CIs have some other characteristics that make them more useful for economic analysis. CIs do not have trends, they are less volatile than quantitative information and they change more gradually. On the other hand, the greatest disadvantage of CIs is that they become invalid once official quantitative statistics are released. CIs are mainly used to signal the tendency or possible turning points of the economy faster; however, they cannot substitute the information obtained from quantitative official statistics.

II. HOW ARE CIs CURRENTLY USED AT THE BANK OF ALBANIA CONSTRUCTED?

The main purpose in the construction of CIs is to aggregate the collected information and provide the performance of different sectors of the economy in one single indicator. Currently, CIs at the Bank of Albania are constructed as the arithmetic average of seasonally adjusted balances of responses to those questions that result to be more closely related to the reference indicator. The latter is a quantitative series obtained from official statistics. Generally, the quarterly GDP is the ideal option as it summarizes the main developments in the economy into an aggregated and well-known indicator. The construction of CIs aims at providing as much as closer approximation to the reference series, or better preceding its changes. Based on the business and consumer confidence surveys have been constructed aggregated indicators for industry, construction, services and consumers⁷. Their construction goes through the following phases:

1. Selection of the reference series;
2. Selection of balances forming the CIs;
3. Seasonal adjustment, normalization; and
4. Aggregation in the form of CIs.

The first two phases, the selection of the reference series and the balances to be used for the CIs by sector, are applied only at the first moment of the construction of indicators. Once these two phases terminate, the selected balances are used for the construction of the aggregated indicators and they do not change from one period to another. However, the balances forming the CIs may be revised in different time periods. For example, Services Confidence Indicator was revised in December 2010 in order to reflect the changes in the real GDP series (see Table 1). In the third phase, which is repeated once new information obtained from the last survey is made available, the balances of each question are seasonally adjusted (excluding the Consumer Confidence Survey⁸). The fourth phase deals with the construction of CIs as the simple arithmetic average of seasonally adjusted balances. The balances used for the construction of the CIs by sector are later normalized and used for the construction of the Economic Sentiment Indicator (ESI). The ESI is calculated as the weighted average of seasonally adjusted and normalized balances by each of the four sectors. At the end, it is made sure that the ESI has an average value of 100 and a standard deviation of 10.

⁷ For more information on the methodology used for the construction of CIs, see *Methodological Explanatory Notes at the Bank of Albania's website*: http://www.bankofalbania.org/web/pub/metodologjia_vbb_vbk_anglisht_2426_1.pdf

⁸ The graphical presentation and the tests show that seasonal adjustment is not necessary for the consumer survey balance series.

Table 1 : CIs balances

Confidence Indicator	Constituent balances, assessment for the current quarter, unless otherwise stated	Constituent balances (reassessed in September 2010)
- Industrial Confidence Indicator (ICI)	-Production -Employment -Inventories (opposite sign)	-Production -Employment -Inventories (opposite sign)
- Construction Confidence Indicator (BCI)	-Demand -Production -Employment	-Demand -Production -Employment
- Services Confidence Indicator (SCI)	-Employment -Firm's economic activity -Firm's financial situation	-Performance of the economy -Firm's economic activity -Firm's financial situation
- Consumer Confidence Indicator (CCI)	-Financial situation_expectations -Economic situation_expectations -Major purchases -Spending and savings	-Financial situation_expectations -Economic situation_expectations -Major purchases -Spending and savings

III. WHAT ARE CIs USED FOR?

The data obtained from the confidence surveys are used at the Bank of Albania to monitor the economy at an earlier time than the release of official statistics and to make short-term forecasts of the GDP. Survey data are the first indicators to give a general overview of the real economy prior to the release of official statistics. CIs constructed from the surveys held with businesses and consumers have been used for several years by the Bank of Albania to monitor the short-term developments of the economy. They became available to researchers, businesses and other institutions starting from the beginning of 2009. New data are released at the Bank of Albania's website 45 calendar days following the reference quarter⁹. A summary analysis of the latest survey results is also released along with the update of the time series. The preliminary data obtained from surveys become valid for forecasts and internal use at the Bank 30 days following the reference quarter. Quarterly GDP data are released 90 days following the reference quarter.

In addition to their timeliness, survey data tend to be less volatile than the quantitative statistics. This derives from the nature of information underlying opinion survey data¹⁰. Opinions collected from surveys change gradually, while the quantitative statistics reflect factors like the climate conditions, holidays, etc. Another advantage of survey data lies in the high level of harmonization, which allows for comparative analysis across different countries¹¹.

Timeliness and the foregoing features make the data obtained from confidence surveys very useful for conjunctural analysis. However, their use would bring added value if the information brought by the CIs timely precedes the economic developments. To achieve this, comparative analyses of the

⁹ As from Q1 2011 survey, the new data will be made available at the Bank of Albania's website 15 days following the end of the reference quarter at:

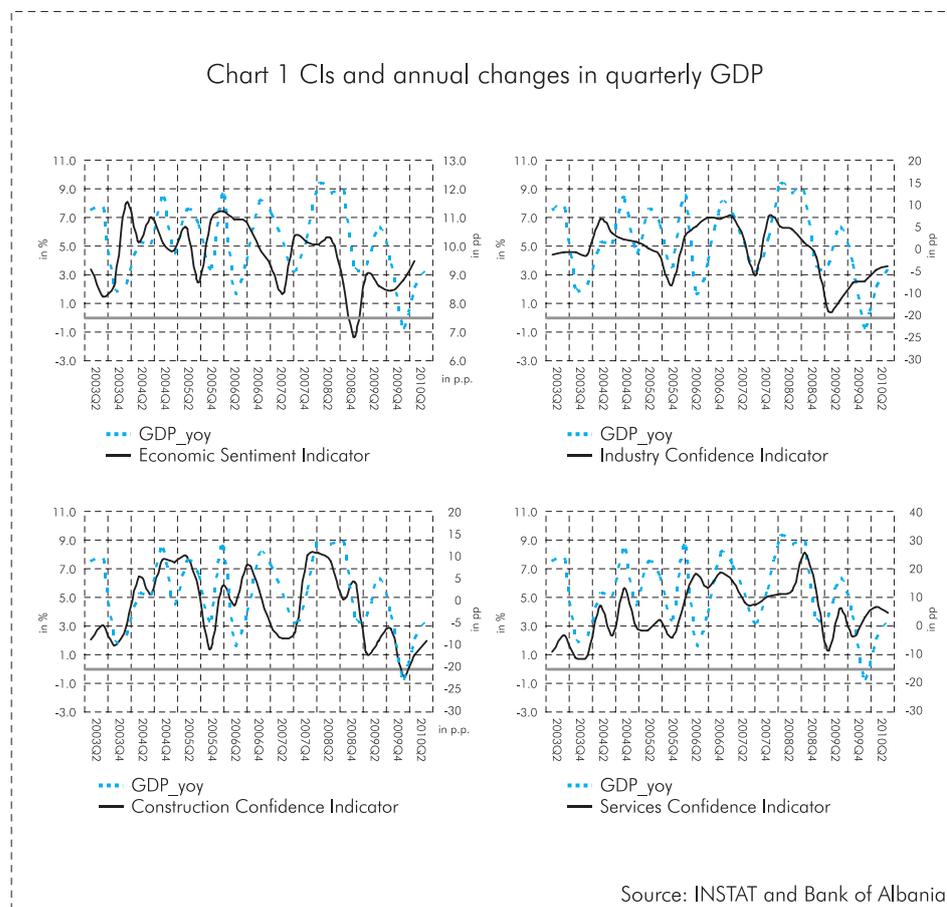
http://www.bankofalbania.org/web/Business_and_consumers_survey_5310_2.php

¹⁰ ECB (2004); "Opinion surveys on activity, prices and labor market developments in the euro area: features and uses", January 2004 Monthly Bulletin.

¹¹ European Commission (2006): "The joint harmonized EU programme of business and consumer surveys", Special Report No. 5.

survey data and quantitative statistics are frequently made. Chart 1 provides a rough idea about the information provided by the CIs regarding the economic developments. Graphically, the changes in the CIs are positively correlated with the real GDP changes. Table 2 provides the same information but more analytically through the results of the linear correlation analysis.

The correlation analysis and the graphical presentation show that the CIs are more closely related to the annual real GDP changes than to the quarterly changes. In fact, the Consumer Confidence Indicator is excluded from this consideration as it shows no correlation with the real GDP¹². The absolute value of the linear correlation coefficients between the CIs and the annual GDP changes is generally larger than the one between the CIs and the quarterly GDP changes. The conclusions of this analysis match with the conclusions derived from similar analyses carried out by European Union countries. Due to their higher volatility, quarterly GDP changes are reflected less by confidence indicators, which tend to change their trend more gradually. Therefore, the focus is placed on the annual changes (ECB 2001). According to Nilsson (2001) and OECD (1997), survey data seem to describe longer developments than as specified in the questionnaire. Hence, the annual real GDP changes are not only used as a reference series in the construction of the CIs, but also in the analysis of the business cycle. To analyse the latter, the long-term trend and the irregular movements are eliminated from the series.



¹² This phenomenon is observed in a number of countries.

Given that the quarterly changes are dominated by the short-term component, the annual changes become the optimal choice for this type of analysis.

	GDP_annual changes	GDP_quarterly changes
ESI	0.53	0.38
ICI	0.44	0.31
BCI	0.64	0.51
SCI	0.47	0.22
CCI	0.21	0.01

Table 2:
Correlation
between CIs and
GDP, annual and
quarterly changes

Source: Bank of Albania and author's own estimations

Table 3 shows the values of the linear correlation between the CIs and the real GDP at different lags. Looking at the results, it seems that the CIs are mostly simultaneous with the developments in the GDP. In the case of the BCI and ESI, it results that these indicators also have preceding features of 1 and 2-quarter lag, respectively. However, even when the CIs do not lead the developments in the real GDP, they are useful for conjunctural analyses as they are available about 2 months earlier than the first release of quarterly GDP.

Lag	t-2	t-1	t	t+1	t+2
ESI	-0.31	0.11	0.53	0.35	0.42
ICI	-0.29	0.13	0.44	0.34	0.20
BCI	-0.14	0.14	0.64	0.49	0.06
SCI	-0.16	0.20	0.47	-0.05	0.32

Table 3:
Correlation
between CIs and
GDP

Note: The correlation coefficients are shown in the form of $CI(t-lag)$ and GDP (annual changes). The values in bold show the maximum coefficients for each CI.

Source: Bank of Albania and author's own estimations

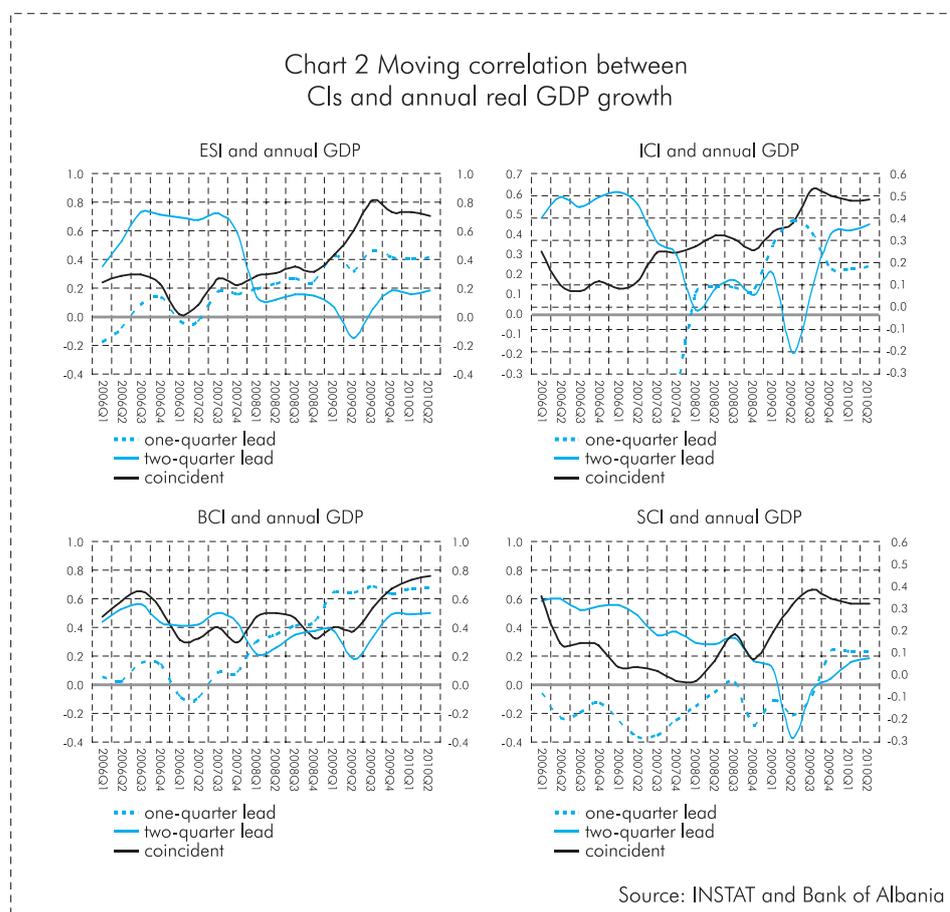
In order to see how the correlation between the CIs and the developments in the real GDP has changed over the time, we have applied the moving correlation coefficient technique. This analysis enables us to investigate the consistency of the correlation over the time. Chart 2 shows the correlation between the CIs and the annual GDP changes for a moving period of 12 quarters of 2003-2010. The correlation between the CIs and the real GDP changes was proved coincidentally, at 1 and 2-quarter lag. As shown in the Chart, the moving correlation coefficients for the coincident period generally prevail over the coefficients for the lag periods, hence supporting the conclusions derived from the correlation coefficient results in Table 3. They are also more consistent over the time. However, the relationship is generally more stable starting from the first quarter of 2009.

In addition to the linear correlation analysis (see the Appendix), Table 6 shows the Granger Causality Test results. This test determines whether the past values of the CIs help forecast the actual values of the reference series, in our case the annual real GDP changes. The test has been applied on both directions, that is, whether the CIs cause the GDP changes, and vice-versa, whether the GDP causes the CIs' behaviour. The results show that the CIs for industry, construction and services Granger-cause the changes in the reference series, and not the opposite. The test for the Consumer Confidence Indicator (CCI) does not reject the basic hypothesis that the CCI does not Granger-cause the quarterly GDP.

In addition to the conjunctural analysis, CIs and the disaggregated survey data have been used at the Bank of Albania to forecast the real GDP growth starting from 2009. The incorporation of survey data into the explanatory equations of the quarterly GDP has improved their explanatory and forecasting ability¹³.

Survey data are also used to obtain information that helps understand certain behaviours of economic agents over different time periods. Specific sections in the surveys provide information regarding different aspects of business and consumer behaviour. This information is also used to assess the impact of different events on economic development, such as the impact of the global financial crisis.

Lastly, this material (Sections 4 and 5) uses survey data to study the business cycles in Albania and its synchronization with the European Union countries.



IV. CIs AND THE STUDY OF BUSINESS CYCLES

Burns and Mitchell (1946) were the first to provide the definition of the business cycle. They define the business cycle as a type of fluctuation found

¹³ Çeliku et al. (2009): "Modelling the quarterly GDP. Role of Economic and Surveys Indicators", Working Paper.

in the economic activity of a nation. According to them, a cycle consists of an expansion phase, which occurs at about the same time in many economic activities, followed by similarly general recessions, contractions, and revivals, which merge into the expansion phase of the next cycle. The authors suggest that the business cycles last from one year and a half to 10 years. This definition, used in almost all the later studies on the business cycles, implies similar cyclical behaviours of many series, like production indices, price indices, employment, national account series, imports, confidence indicators, etc.

The purpose of this section is to construct a composite indicator using data obtained from the business confidence surveys, which will go through the four business cycles. One of the survey data characteristics, in addition to earlier availability, is that they do not have a long-term trend. This makes them more favourable to analyze the business cycle¹⁴. The time series obtained from these series have been used in many OECD countries also because the information collected from them, expressed in the form of opinions, makes them more sensitive to cyclical developments¹⁵. Another reason for using the information obtained from confidence surveys to determine the business cycles and the turning points is the definition of “confidence” or “tendency” as a special source of shocks to the economy; the change in business or consumer confidence may lead to changes in their production or consumption-related decisions. This reason is particularly important in the context of the global economic crisis and the sharp decline in business and consumer confidence. Business and consumer confidence was considered as a crucial factor in the transmission of financial shocks to economic activity¹⁶.

The following describes the construction of the Economic Climate Tracer (ECT), derived from the business confidence surveys and based on the European Commission’s methodology¹⁷. This indicator is quite similar to Economic Sentiment Indicator (ESI) as it collects information from the confidence surveys of the four main groups, industry, construction, services and consumers. However, in contrast to the ESI, the ECT uses the information obtained from all the questions of the questionnaires, not only those whose balances have the highest correlation with the reference series. In this sense, the ECT is a broader indicator than the ESI. The main purpose of the ECT is to obtain a simple visual overview of the four business cycle phases. Figure 1 provides a schematic presentation of what the ECT would look like throughout the four business cycle phases. The standardized level of the indicator is placed on the vertical axis, and its quarterly changes on the horizontal axis. This positioning in the chart enables the counter-clockwise movement. The chart also allows us to see the performance of the indicator and its changes over the time. This indicator goes through the following four phases:

¹⁴ European Commission (2006): “The Joint Harmonized EU Programme of Business and Consumer Surveys”, Special Report No. 5.

¹⁵ OECD (1997): “Cyclical indicators and business tendency surveys”.

¹⁶ Weyerstrass, et al. (2009): “Business cycle and economic sentiment synchronization in the EU”.

¹⁷ Gayer, C. “Report: The economic climate tracer. A tool to visualize the cyclical stance of the economy using survey data”.

1. Expansion (upper-right), the indicator is above average and increasing;
2. Downswing (upper-left), the indicator is above average but decreasing;
3. Contraction (lower-left), the indicator is below average and decreasing;
4. Upswing (lower-right), the indicator is below average and increasing.

The indicator, which rotates counter-clockwise in all the four phases, provides a simple and clear identification method of the business cycle. The business cycle peaks emerge as positions in the upper centre, while troughs are positioned in the lower centre.

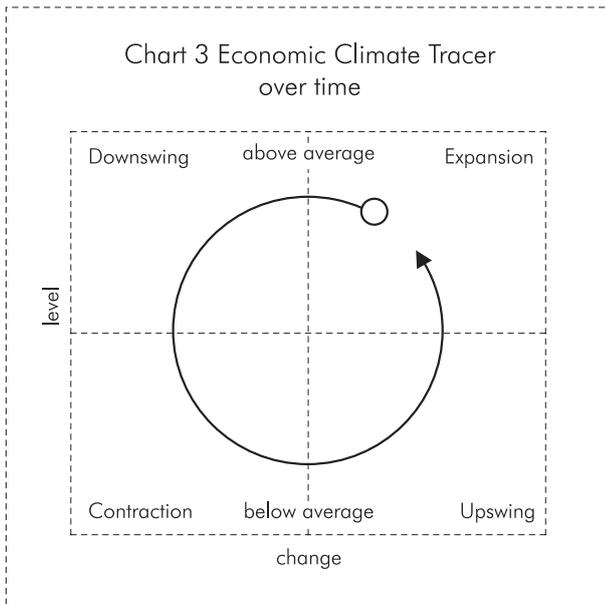
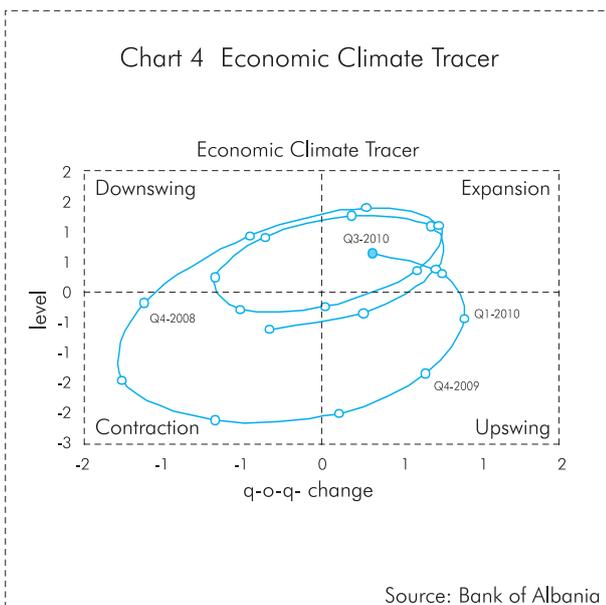


Chart 3 shows the real cyclical movement of the Economic Climate Tracer (ECT) for Albania, while Chart 6 in the Appendix shows the climate indicators for individual sectors of the economy. The climate indicators for each sector are based on the principal component analysis of the balance series of each sector, seasonally-adjusted. For the industry sector have been used 7 balances, for the construction sector 7 balances, for the services sector 5 balances and for consumers 10 balances¹⁸. The principal component is filtered and standardized in order to eliminate irregular movements and reach a common mean of 0 and standard deviation of 1. The ECT is a weighted average of the five principal component-based sector climate indicators. The chart shows clearly that following the boom in 2007 and 2008, all indicators are downward. The ECT peaked in

the second quarter of 2008 and after four quarters in recession crossed the turning point in the third quarter of 2009. This represents the trough of the business cycle. The changes in the ECT are positive during the last three quarters and it stands above the average. ECT by sector shows that confidence in industry and consumer confidence have been at the upswing phase for several quarters. The climate indicator for industry stands above its historical average in the third quarter of 2010 and very close to the previous quarter's level. The climate indicator for services crossed over its historical average in the third quarter of 2010. The performance of the climate indicator for the sector of construction shows more pessimistic levels; after approaching its average in the second quarter of 2010, its climate indicator changed to negative levels in the third quarter, thus entering the recession phase.



The changes in the ECT are positive during the last three quarters and it stands above the average. ECT by sector shows that confidence in industry and consumer confidence have been at the upswing phase for several quarters. The climate indicator for industry stands above its historical average in the third quarter of 2010 and very close to the previous quarter's level. The climate indicator for services crossed over its historical average in the third quarter of 2010. The performance of the climate indicator for the sector of construction shows more pessimistic levels; after approaching its average in the second quarter of 2010, its climate indicator changed to negative levels in the third quarter, thus entering the recession phase.

The ECT is used to provide a preliminary orientation of the level of confidence in economy.

¹⁸ The first principal component explains 85% of the variance for the sector of industry, 68% for the sector of construction, 55% for the sector of services and 57% for consumers.

Its added value consists in the fact that it provides faster information than the release of quantitative data. It has two advantages over the other aggregated indicator for the economy, Economic Sentiment Indicator (ESI); the first is that the ECT uses all the possible information obtained from the business and consumer confidence surveys, that is not only the information of some selected balances, as is the case with the ESI; the second is that the ECT conveys the information through a clear schematic view, where it can be easily identified the business cycle phase the economy is suggested to be in. However, the change of the methodology for the construction of the ECT versus the ESI causes the information derived from it to be sometimes different from the one derived from the ESI. In addition, the ECT may signal possible turning points in the economy but this information does not substitute the one obtained from quantitative statistics. The turning points are only confirmed by official data.

V. SYNCHRONIZATION WITH THE EUROPEAN UNION COUNTRIES

The analysis of the extent of the business cycle synchronization across different countries is one of the uses of the information obtained from CIs. In general, the studies on the business cycle synchronization use information provided by the GDP or industrial production. However, the economic sentiment synchronization is relevant for the decision-making as shocks to confidence are considered an independent source of macroeconomic volatilities in the EU countries¹⁹. The study conducted by the European Commission on the use of business and consumer confidence survey results for the European Union countries concludes that the Industrial Confidence Indicator of the member states is more closely related to the movements in Europe's production index than to their own countries' cycles²⁰. The study concludes that there is a common European component in the industrial confidence indicators of the member states.

Against this setting, it would be of interest to analyze whether these shocks or fluctuations in Albania's "sentiment" or "optimism" synchronize with other European countries. We first make a graphical presentation of the confidence indicators for each individual sector in Albania, Italy, Greece and the Euro area. At first view, confidence indicators in Albania (Chart 5 in the text and Chart 9 in the Appendix) show a considerable extent of synchronization with other countries. The similarity is more evident with Italy's confidence indicators. The rationale behind this synchronization may be the closer economic and trade relations with Italy. Closer economic and trade relations cause the changes in confidence to be more similar as a shock to or improvement of confidence in one economy would be transmitted to the other economy. The chart shows clearly the fall of confidence in all the sectors of the economy at the end of 2008 as a response to the global economic and financial crisis. Economic

¹⁹ Weyerstrass, K. et al. (2009), "Business cycle and economic sentiment synchronization in the EU".

²⁰ Weyerstrass, K. et al. (2009), page 46.

Sentiment Indicator reached the trough starting from the first quarter of 2009. After confirming the turning point in the second quarter of 2009, this indicator began to improve, except for Greece's ESI, which declined in the first two quarters of 2010. Industrial Confidence Indicator shows the most pronounced improvement in the last four quarters, triggered by the revival of demand as a result of the gradual recovery of global economic growth. Confidence in the other sectors shows less uniform developments.

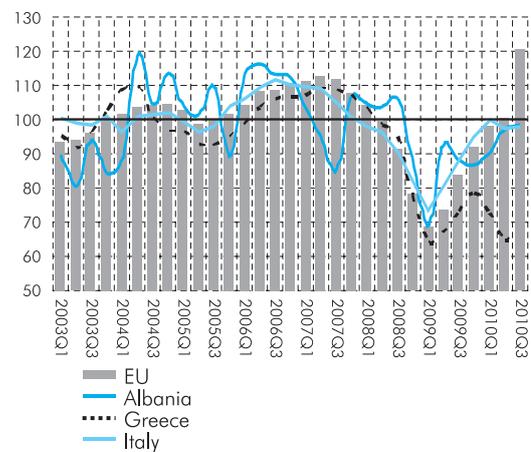
The graphical presentation and the analysis of linear correlation for the period under analysis (2002:Q2-2010:Q3) show that the developments in the ESI and CIs for industry, construction and services in Albania are positively correlated with the developments in the respective indicators of EU, Italy and Greece. By contrast, the developments in the Albanian consumer confidence indicator are poorly correlated with those of other countries. The rationale behind this fact is that consumer opinion and confidence are affected by specific events in each individual country. CIs in the sector of industry show the closest correlation coefficients, ranging between 0.77 (Greece) and 0.76 (Italy). The common performance of industrial confidence indicators relates to the common factors that affect this sector and the closer trade relations between these countries. The opinions of industry-related businesses are affected similarly by external shocks (e.g. rise in primary commodity prices, fall of demand due to the global crisis, etc.). The sector of services shows the least strong correlation among the sectors of the economy. The linear correlation coefficients range from 0.48 with Italy and 0.54 with Greece. Services-related businesses are affected more by specific factors characterizing the country they operate in rather than by common shocks to their sentiment. Construction confidence indicator in Albania shows some strong positive correlation with the CI in EU and Italy (the correlation coefficients is 0.58 and 0.52, respectively), but it shows no correlation with Greece's CI.

In conclusion, the industrial confidence indicator shows the strongest synchronization. Given their export-oriented nature, sales in industry depend largely on foreign demand. The Albanian construction sector also shows good levels of synchronization with the EU countries. The reasons behind this synchronization are the characteristics of the Albanian housing market and the high level of raw material imports. Money remitted from Albanian expatriates residing in EU countries represents a vital source of the purchasing power of residential buildings in Albania; a large number of Albanian expatriates are employed in the sector of construction. The lack of synchronization in the sector of services may be explained by the non-tradable nature of goods this sector produces. Tourism, which may establish a stronger correlation between the countries, is characterized by low demand elasticity in the case of Albania. Foreign demand to spend vacations in Albania is mostly determined by Albanian travellers who reside abroad and visit their relatives in Albania, regardless of their economic conditions. Similarly, the synchronization of consumer confidence indicators is low as their confidence is affected by specific factors characterizing individual countries.

It is difficult to compare the business cycles by the CIs in Chart 5 due to the short-term fluctuations of the series. This is more evident in Albania's CIs. In order to better compare the information provided by the CIs for the identification of the business cycles we apply the methodology used by Weyerstrass et al. (2009). The authors state that the business cycle cannot be observed without preliminary assumptions about its characteristics. The very short-term fluctuations in the series in the charts make it less easy to identify the business cycle. In general, the series consist of three components: very short-term fluctuations in the series, or the irregular component; very long-term fluctuations, or the trend; and the medium-term fluctuations, or the cycle component. Hence, in order to observe the cyclical component in a series, we have to eliminate the long and short-term component. In order to eliminate the irregular component in the CI series, we applied the Christiano-Fitzgerald (CF) filter. It enables the elimination of the trend and the irregular component, while preserving the business cycle component. By applying the CF filter on the series, we eliminate the fluctuations shorter than 6 quarters and longer than 32 quarters, and preserve the fluctuations occurring between the interval of 6-32 quarters.

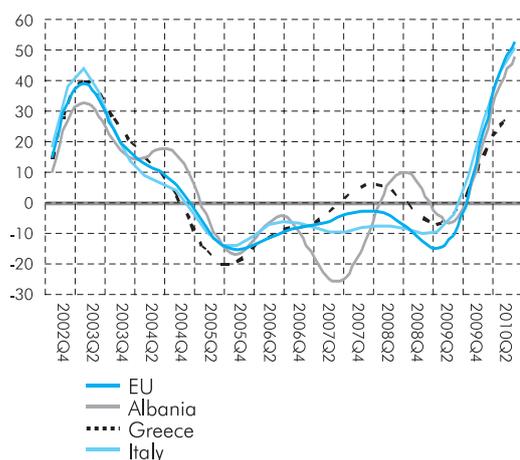
Chart 6 below and Chart 10 in the Appendix show the cyclical components of the Economic Sentiment Indicator and the CIs for each individual sector for the four countries under analysis. The charts show more clearly the considerable extent of synchronization of confidence in different sectors of the economy. Excluding the BCI between Albania and Greece, the cyclical component shows the best synchronization between Albania's and EU's CIs. In order to obtain more detailed information on the correlation between the CIs, we need to analyze the lags as well. The table showing the correlation coefficients (see Table 4) provides us with this information. The correlation coefficients are calculated for different time periods, but the table shows only those coefficients that resulted with the highest correlation. The results show that the CIs between Albania and EU countries generally reach the strongest correlation after 1 or 2 quarters. Otherwise said, the developments in the confidence of EU countries precede the developments in the Albanian business confidence with 1 or 2 quarters.

Chart 5 Economic Sentiment Indicator in Albania and EU countries



Source: Bank of Albania and European Commission

Chart 6 Cyclical component of Economic Sentiment Indicator



Source: Bank of Albania and European Commission

The synchronization of the business confidence cycles has become stronger in the last two years, a period that corresponds to the last economic crisis. Chart 8 shows the moving correlation coefficients for a 4-year period of the CF filter between the Albanian CIs and EU, Greece and Italy's CIs. The Economic Sentiment Indicator shows a low level of synchronization during 2007-2008, following a 2-year period of high synchronization. At present, the correlation of the Economic Sentiment Indicator between Albania and other countries has been increasing. The chart showing consumer and construction confidence indicators provides a similar setting. The Albanian construction confidence indicator shows no relevant correlation for the prior-2009 period. Industrial confidence indicator shows by large the most stable correlation over the time, while the services confidence indicator shows the weakest correlation.

Table 4 Correlation between CIs in Albania and other countries

	ESI	ESI_CF filter	ICI	ICI_CF filter	BCI	BCI_CF filter	SCI	SCI_filter	CCI	CCI_CF filter
EU	0.53 (-1)	0.88	0.75 (-1)	0.84 (-1)	0.58 (-2)	0.63 (-2)	0.49 (-2)	0.64 (-2)	0.27	0.77
Greece	0.45 (-1)	0.82	0.77 (-1)	0.84 (-1)	0.11	0.09	0.54 (-2)	0.59 (-1)	-0.1	0.68
Italy	0.40 (-1)	0.89	0.76 (-1)	0.88 (-1)	0.52 (-1)	0.71 (-1)	0.48 (-1)	0.52 (-1)	0.09	0.89

Source: Bank of Albania and author's own estimations

CONCLUSIONS

The analysis of confidence indicators plays a key role in the pool of information scrutinized during the monetary policy decision-making. They have provided very useful information at the Bank of Albania and have helped in the process of analysis and short-term forecast of quarterly real GDP. Given the advantages characterizing the confidence indicators: timely availability, lack of revision and stationarity, they may also be used to identify the business cycle phase the Albanian economy is in. This paper introduced the Economic Climate Tracer, whose graphical presentation provides a simple view of the business cycle for the economy and its main sectors. By comparing the information obtained from the confidence indicators of Albania and some EU countries, we concluded that there is considerable synchronization between Albania and EU countries.

REFERENCES

- Burns dhe Mitchell (1946): "Measuring Business Cycles", NBER.
- Çeliku and Shtylla (2007): "Vrojtimi i besimit të biznesit: aspekte metodologjike dhe analizë ekonomike e rezultateve".
- Çeliku et. al (2009): "Modelling the quarterly GDP. Role of Economic and Surveys Indicators", Working Paper.
- ECB (2001),: "The information content of composite indicators of the euro area business cycle", November Bulletin.
- ECB (2004); "Opinion surveys on activity, prices and labor market developments in the euro area: features and uses", January 2004 Monthly Bulletin.
- Gayer, C. "Report: The economic climate tracer. A tool to visualize the cyclical stance of the economy using survey data".
- University of Michigan, information on surveys: <http://www.sca.isr.umich.edu/documents.php?c=i>
- Lama and Istrefi (2007): "Besimi konsumator dhe ekonomia shqiptare. Një urë e re informacioni", Bank of Albania Paper.
- Nilsson (2001), "Business tendency surveys: methodology, analytical use and presentation of results".
- OECD (1997): "Cyclical indicators and business tendency surveys".
- OECD (2003): "Business tendency surveys: A handbook".
- European Commission (2006): "The Joint Harmonized EU Programme of Business and Consumer Surveys", Special Report No. 5.
- Santero and Westerlund (1996): "Confidence indicators and their relationship to changes in economic activity", OECD, WP Nr. 170.
- Weyerstrass, K. et. al. (2009), "Business cycle and economic sentiment synchronization in the EU".

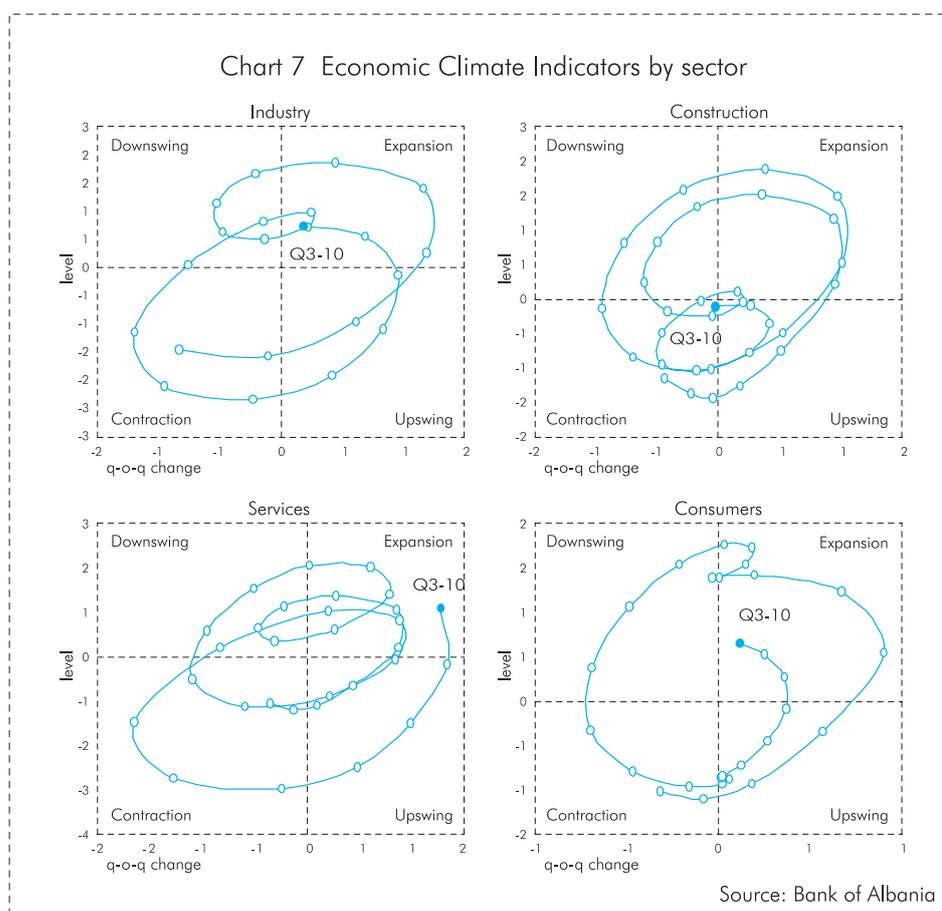
APPENDIX:

Table 5
Correlation
between CIs and
GDP, y-o-y and
q-o-q changes

		GDP_y-o-y	GDP_q-o-q
Industry	Production	0.37	0.28
	Inventories	-0.25	-0.03
	Employment	0.51	0.31
Construction	Demand	0.66	0.48
	Production	0.67	0.46
	Employment	0.65	0.5
Services	Performance of economy	0.34	0.22
	Economic activity	0.44	0.23
	Financial situation	0.47	0.19

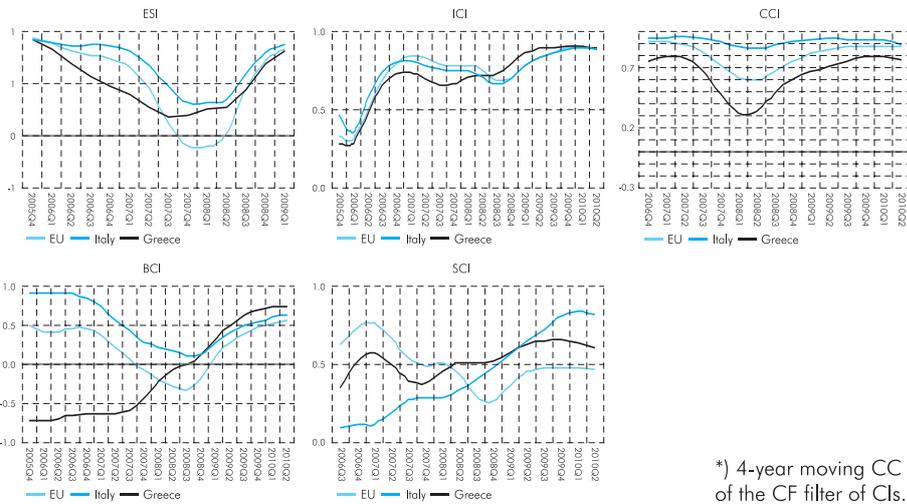
Table 6
Granger-
Granger
Causality Test
results for CIs
and GDP

	Probability	Basic hypothesis is rejected	Opposite test ²¹
Basic hypothesis: CIs do not Granger-cause the GDP, y-o-y changes			
ICI	0.0273	Yes	No
BCI	0.0103	Yes	No
SCI	0.0779	Yes	No
CCI	0.9596	No	No
Basic hypothesis: CIs do not Granger-cause the GDP, q-o-q changes			
ICI	0.2674	No	No
BCI	0.2841	No	No
SCI	0.6223	No	No
CCI	0.6341	No	No



²¹ Basic hypothesis: GDP does not Granger-cause the CIs.

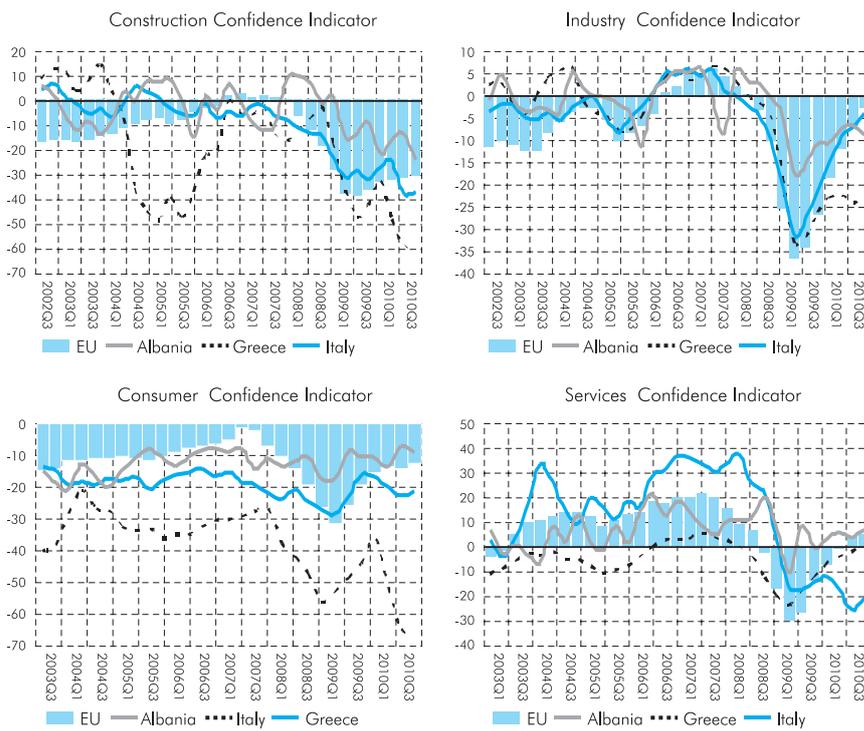
Chart 8 Moving correlation between CIs*



*) 4-year moving CC of the CF filter of CIs.

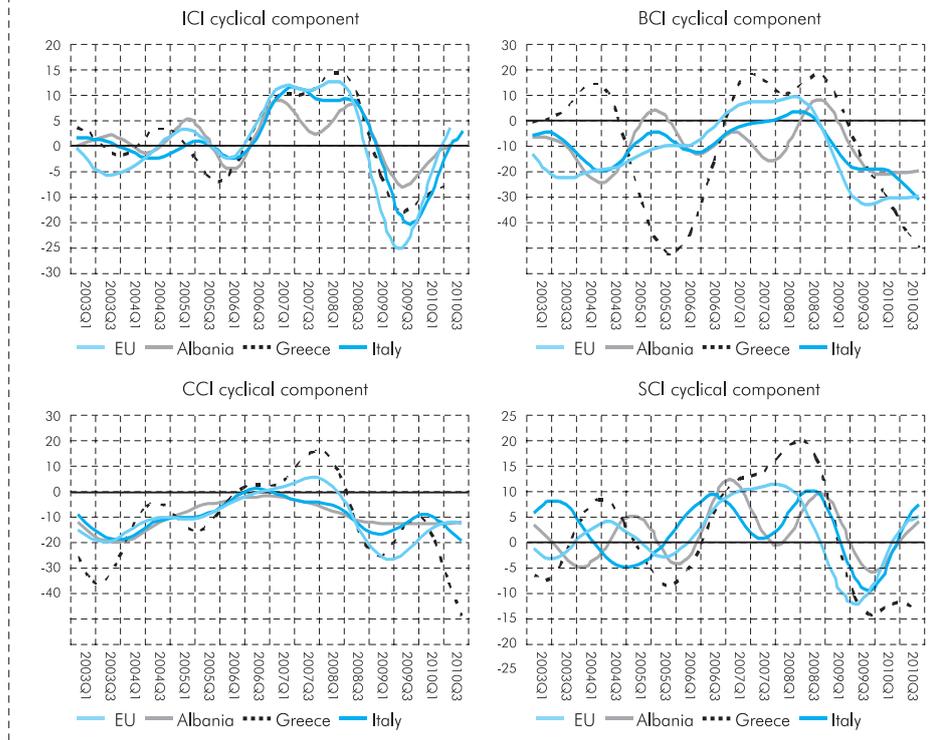
Source: Bank of Albania and European Commission

Chart 9 CIs in Albania and EU countries



Source: Bank of Albania and European Commission

Chart 10 Cyclical components of CIs



Source: Bank of Albania and European Commission

BALANCE OF PAYMENTS DEVELOPMENTS

MERITA BOKA AND EGLENT KIKA *

INTRODUCTION

The Balance of Payments is a statistical statement that systematically summarises for a specific time period the economic transactions of an economy with the rest of the world. These transactions, which in most cases occur between residents and non-residents, involve economic transactions recorded in two main accounts: in the current account and in the financial and capital account. If inflows into these accounts are lower than outflows, then the account will be in deficit, and it leads to the respective change in the foreign reserve of the country. This material provides an analysis of the performance of the main balance of payments accounts, in order to identify the dynamics of the current account deficit adjustment and the reduced financing requirement.

* Monetary Policy Department.

The views expressed in this publication are the views of the authors and do not necessarily reflect the views of the Bank of Albania.

The overall balance of payments for the third quarter of 2010 recorded a growth of foreign assets by about EUR 53.3 million. The current account deficit narrowed by about 45.3% y-o-y over this quarter and followed a trend which commenced in the fourth quarter of 2009. A higher net surplus in the services account by 32.2% y-o-y, a narrowing merchandise trade deficit by about 1.8% y-o-y and a shift into positive territory of the net income account position contributed to the narrowing of current account deficit. This deficit was valued to 9.1% of nominal GDP in the third quarter. In addition, the cumulative analysis of all three quarters of 2010 reveals a contraction of the current account deficit by 5.1 pp relative to the same period of the previous year. The capital and financial account surplus failed to finance fully the current account deficit for a fifth quarter in succession, thus covering about 73% over the third quarter of the year. Net foreign direct investments (foreign direct investments – privatisations) recorded a y-o-y growth of 43.1%, accounting for 9.3% of GDP.

Table 1 Balance of payments

Key items	In EUR million				
	Q3 2009	Q4 2009	Q1 2010	Q2 2010	Q3 2010
CURRENT ACCOUNT	-383.1	-324.6	-246.6	-216.7	-209.6
Trade balance	-606.6	-601.3	-419.0	-482.9	-595.9
- Export	186.0	205.5	254.9	340.5	270.3
- Import	-792.6	-806.9	-673.9	-823.4	-866.2
Services (net)	126.2	34.5	-19.3	-0.1	166.8
Income (net)	-60.7	-30.5	-19.2	-16.1	28.9
Current transfers (net)	158.1	272.8	210.9	282.5	190.6
CAPITAL AND FINANCIAL ACCOUNT	218.3	109.6	125.3	183.7	153.0
Capital account	32.1	17.0	10.0	22.7	23.4

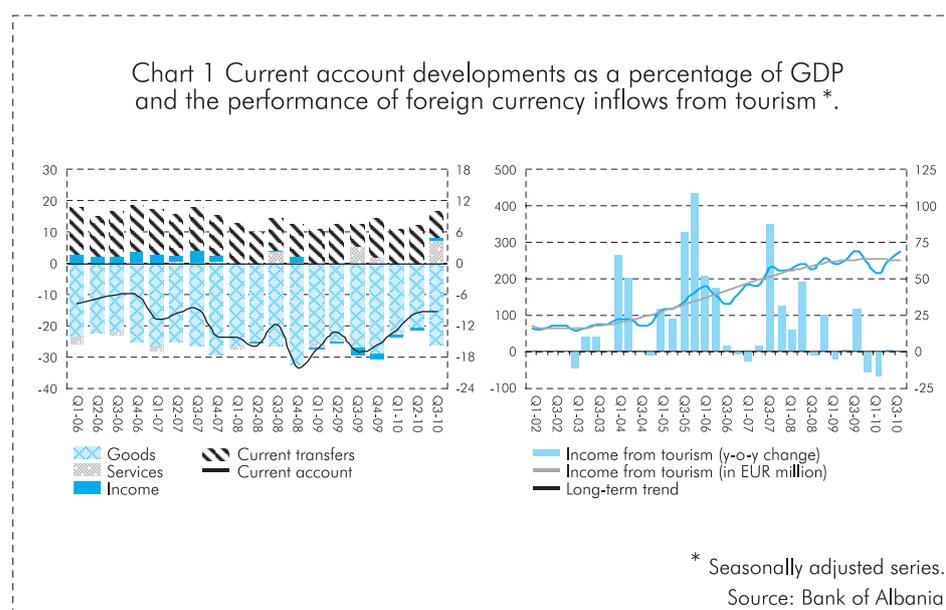
Financial account	186.2	92.6	115.3	161.0	129.6
Foreign Direct Investment (inflows)	168.3	108.5	177.8	175.8	202.9
Government borrowing	136.0	8.0	41.0	18.6	29.0
Private borrowing	22.0	1.0	3.0	23.2	13.0
ERRORS AND OMISSIONS	208.7	128.3	102.5	48.7	109.8
OVERALL BALANCE	43.9	-86.7	-18.8	15.7	53.3

Source: Bank of Albania

SERVICES, INCOME AND CURRENT TRANSFERS

The net exports deficit narrowed by about 10.7% y-o-y over the third quarter of the year, and accounted for 18.7% of GDP. Although goods and services import increased by about 4% y-o-y, the more expansive results of exports in goods and services by 12.7% y-o-y provided the impetus to this performance. The goods exports continued to increase rapidly over this quarter following a tendency started in the fourth quarter of 2009. As a share of GDP, merchandise exports were estimated at 11.8%, about 3.6 pp higher than the ratio registered in the same quarter the previous year¹.

The services account recorded a positive net position and accounted for 7.3% of GDP, about 1.7 pp higher than the same quarter of the previous year's ratio. This quarter, which corresponds to the tourist season at home, is characterized by a high amount of foreign currency inflows. Nevertheless, the y-o-y fall of foreign currency outflows from outbound tourism provided the main contribution to the y-o-y growth of the services account surplus by about 32%. Thus, while foreign currency inflows from tourists decreased by 0.1% y-o-y, Albanians spent abroad around 30% less for tourism purposes over this quarter compared with the same period of the last year.



¹ The y-o-y growth of Albanian goods exports was 45.3%.

The income account recorded a positive net position of EUR 28.9 million, after a deficit net position for a period of six quarters in succession. Although it continues to record a negative net position, it is worthy to mention the considerable drop of foreign direct investments² profit repatriation. This development signals the recovery of foreign investors' confidence in the potential of the Albanian economy in the short run. It is also imperative to emphasize the annual fall of interest payments on the loans disbursed to public and private sectors as well as the annual increase of profits derived from the interest paid on residents' invested assets and on the foreign reserve.

The surplus in current transfers was valued 20.6% higher relative to the same period of the previous year. Meanwhile, although workers' remittances revealed a y-o-y upward trend over this quarter, their significance to financing current account deficit remains considerably below the historical average³. Lastly, the combined surplus in services account, income account and current transfers financed around 64.8% of trade deficit for the quarter in analysis.

CAPITAL AND FINANCIAL ACCOUNT

The capital and financial account recorded a positive balance of EUR 153.0 million over the third quarter of 2010, declining by about 29.9% y-o-y. As a percentage to GDP⁴, net capital and financial flows accounted for about 6.7% of GDP from 9.6% in the same period of the previous year. The lower surplus in capital and financial account owes to the annual decline in both capital and financial account flows by about respectively 27.0% and 30.4%. Currently, their combined surplus financed about 73.0% of the current account deficit during this period.

Albania's financial liabilities to the rest of the world, albeit higher than the previous quarter, amounted to EUR 261.2 million, about 18.1% lower compared to the previous year. The lower level of financial liabilities is mainly due to the lower private and public borrowing and the banking system's short-term borrowing. Public borrowing dropped by about 78.7% y-o-y over the third quarter, whereas private borrowing declined by about 40.9% y-o-y. In addition, the banking system's short-term borrowing declined by EUR 96.4 million relative to the decline by EUR 16.4 million in the same period of the previous year. On the other hand, a considerable increase of non-resident bank deposits held with Albanian banks is noticeable during the current quarter by about EUR 98.9 million compared with the same period of the previous year. Foreign direct investment inflows amounted to EUR 202.9 million in the third quarter, accounting for about 8.8% of GDP and recording a y-o-y

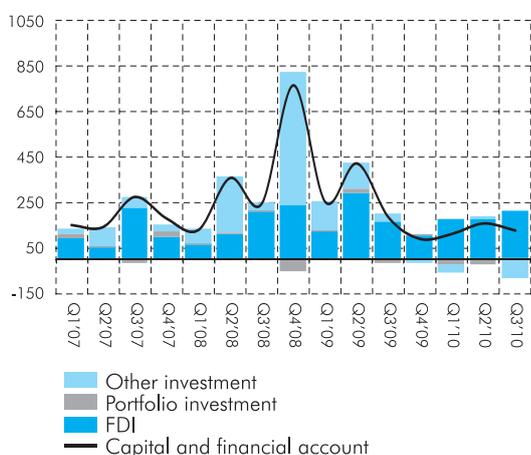
² This sub-item deficit was EUR 9 million over this quarter versus EUR 87.2 million in the third quarter of 2009.

³ Remittances were estimated at EUR 135.2 million during this quarter and the trade deficit financing indicator pointed to 23%, about 25 pp below the historical average of this indicator over 2003-2010.

⁴ The GDP used for the period 2003-2008 is published from INSTAT. IMF's GDP projections have been employed for the years 2009 and 2010, according to "IMF Article IV Consultation, 2010", July 2010.

growth of 20.5%. Excluding privatisation receipts, foreign direct investment grew by 32.8% y-o-y relative to the third quarter of 2009.

Chart 2 Financial account and key items – net flows in EUR million



Source: Bank of Albania

Domestic financial assets invested abroad amounted to EUR 131.6 million in the third quarter of 2010, down by about 0.7% y-o-y. After two quarters in succession of higher portfolio investments, in the third quarter, their contribution to the increase of our financial assets abroad was only EUR 4.3 million. Domestic banking system deposits held with non-resident financial institutions amounted to EUR 138.9 million, up by about 33.0% y-o-y.

Reserve assets grew by EUR 53.3 million over the third quarter of 2010, about EUR 10 million higher than the same period of the previous year. At the end of September 2010, foreign reserve stock pointed to EUR 1,777.0 million, sufficient to cover 4.6 months of imports of goods and services.

FINANCIAL INTERMEDIATION ANALYSIS

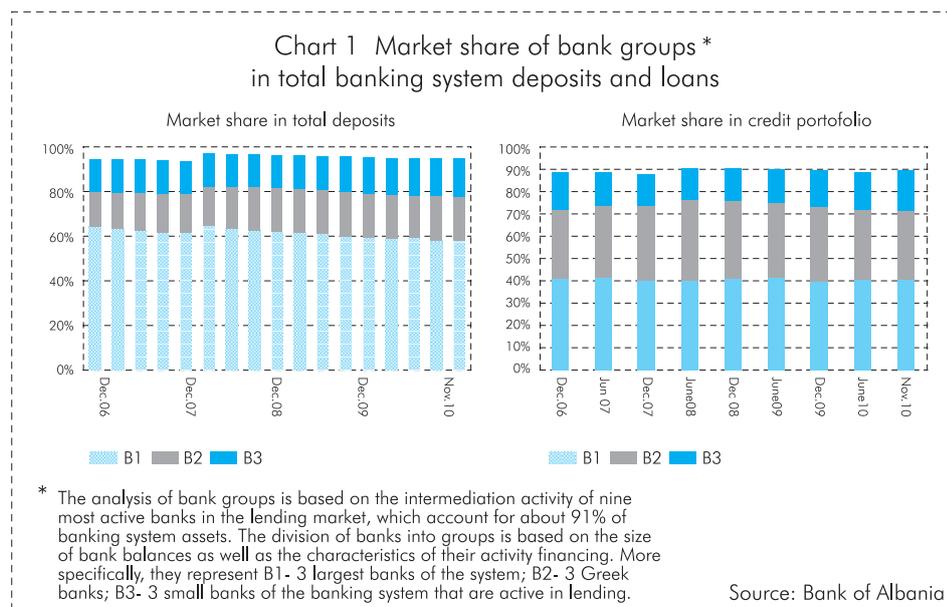
ERJONA SULJOTI & OLTA MANJANI *

INTRODUCTION

Due to the limited development of the financial and capital markets in most Central and Eastern European (CEE) countries, including Albania, the financial system is dominated mainly by the banking system, which plays a key role in the financial intermediation for the private sector. The financial system in Albania is highly dominated by the banking sector, in comparison to other CEE countries. The weight of the banking system assets to total financial system¹ assets stands at about 95%, compared to the level of almost 81% of CEE countries².

* Monetary Policy Department,
January 2011

The views expressed in this publication are the views of the authors and do not necessarily reflect the views of the Bank of Albania.



The Albanian banking system is composed of 16 private universal banks with a dominating foreign capital, accounting for 92% of the capital held by the banking system. As at end of November 2010, the loan portfolio amounted to 47% of the banking system assets, while deposits accounted for about 77% of liabilities. The banking system intermediation is broadly covered by the group of the three largest and market dominant banks (group B1 in the chart). Developments in the recent years indicate a continuous shrinking on the deposit market for the first group of banks, B1. Their market share fell from

¹ The financial system, in addition to depository banks, includes savings and credit associations, private pension funds, leasing associations and other financial institutions.

² This ratio for CEE countries in 2007 was about 81% according to Dubravko Mihaljek 2010, "Domestic bank intermediation in emerging market economies during the crisis: locally owned versus foreign-owned banks", BIS papers, No.54.

64% in 2006 to 58% in November 2010. The group of small banks was more active in the market by slightly increasing their share of deposits to 17%. Only 9 banks of the system are active in lending and their portfolio accounts for about 95% of the total stock. Meanwhile, the credit market manifests a higher competition compared to the deposit market, with more uniform distribution among bank groups. The portfolio of the first group accounts for 41% of the market and has remained unchanged in recent years. In the meantime, the second bank group, including the Greek banks, has experienced a reduction of their loan portfolio from 36% in mid-2008 to 30.5% in November 2010. Their market share of deposits has remained almost unchanged. The group of small banks shows rapid credit growth, expanding their market share from 14% in 2007, to 18.2 % in November 2010.

BANKING SYSTEM INTERMEDIATION

The withdrawal of deposits during the last quarter of 2008 and the first quarter of 2009 exposed the banking system to a reduction of financial resources. During this period, the first pressures on liquidity were noticed, leading to the slowdown of intermediation³ and, consequently, the growth of money supply. Meanwhile, in order to support the banking system with the necessary liquidity, the Bank of Albania was present in the inter-bank market during 2009 and 2010. The accommodating policy pursued by the monetary authority contributed to reducing interest rate fluctuations in the financial markets, thus guaranteeing their normal functioning as well as sending monetary policy signals for the support of domestic economic activities.

The re-monetisation of the economy and the improvement of liquidity during 2010, thanks to a reduction of the currency outside banks and the recovery of deposits in the banking system, led to a lower presence of the monetary authority in the inter-bank market compared to the preceding year. Nevertheless, the supply of the banking system with monetary instruments remains at high levels. The monthly average of liquidity injections by the monetary authority has averaged at ALL 26 billion⁴ during the last two years. Meanwhile, the pre-crisis banking system was characterised by excess liquidity and the Bank of Albania intervened with its market instruments by withdrawing an average of ALL 2.3 billion a month.

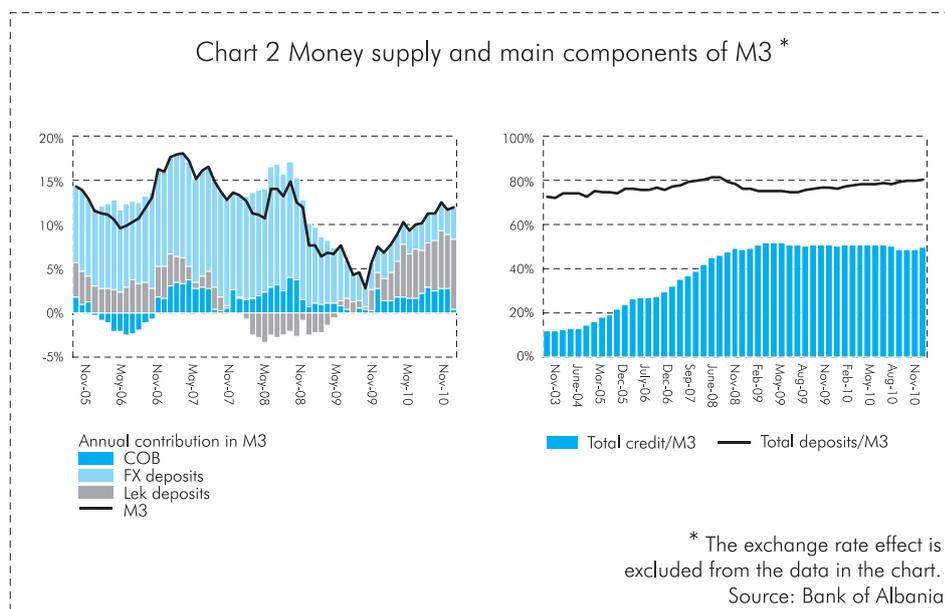
Supply-side developments confirm a full return of deposits in the system during the first half of 2010. The strengthening confidence of economic agents' in the banking institutions, thanks to the measures taken to overcome the financial crisis, has affected the re-monetisation of the economy. As such, the rapid recovery of deposits (on average by 15.2% y-o-y) was accompanied by a continuous growth of deposits to GDP ratio, standing at 63.4% in the third quarter compared to 57.3% at the end of 2009. Deposits developments by economic agents confirm the stable growth of household deposits compared

³ In this analysis, intermediation refers to private sector intermediation, as measured by the loan to deposit ratio for the private sector.

⁴ The interval of these injections varies from ALL 13 to 37 billion.

to the fluctuating growth of business deposits depending on their economic activity.

The level of re-monetisation is reflected in the share of the total stock of deposits to the broad money indicator, which stands at around 80% in November 2010, against 76% at the end of 2009. The growing tendency of deposits was followed by a reduction of currency outside banks. Its share to the M2 aggregate declined to 31.9% at the end of the period from 36.2% at the end of 2009. Historically, this ratio has fluctuated within the interval of 25-40%, reflecting the preference of economic agents for liquid monetary instruments in various periods, as well as the development level of the banking services.



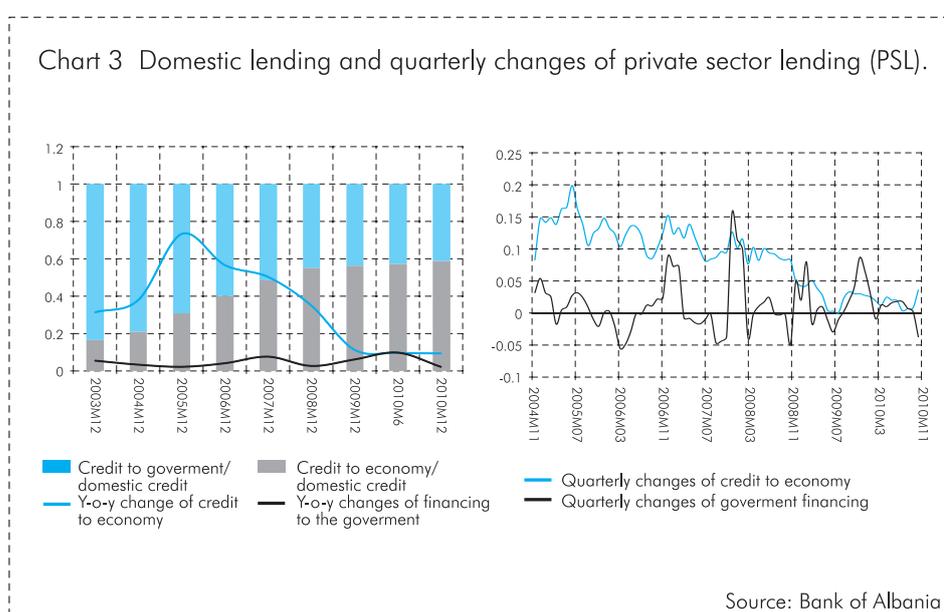
Despite the liquidity improvement, the banking system intermediation for the economy continued to be low. The total loan to deposit ratio in November 2010 was 62%, compared to its peak of 69% in July 2009. This decline in intermediation rates was mostly due to a rapid return of deposits into the system as well as a moderate credit growth. However, compared to the pre-crisis period, the intermediation rate is around 5.2 pp higher. The slowing tendency of the loan portfolio growth, which started in 2007, was a welcomed phenomenon to ensure a balanced and sound credit expansion. The effects of the global financial crisis that affected Albania towards the end of 2008 and during 2009, led to a rapid reduction of the credit annual growth rate, reaching a historic low of about 2.5%⁵ in November 2009. December 2009 marked a turning point in the declining trend. During the first half of 2010, the annual growth rate of outstanding loans increased by about 5.5% on average. In the second half⁶ of the year, credit growth continued to improve gradually until October 2010, by 6.3% on average. In November, the loan portfolio marked a significant improvement, with around ALL 11 billion monthly

⁵ Excluding the exchange rate effect.

⁶ The analysis covers July-November 2010.

growth, reaching as such an annual growth rate of 9%. The substantial credit growth in November was mainly due to an increased demand by the private sector as well as eased credit standards⁷.

In absolute terms, the credit portfolio of the private sector enlarged by ALL 29 billion for the period of January-November 2010 compared to the ALL 15 billion increase in 2009. The positive performance of credit to the private sector during this period was oriented mainly towards corporate credit. In contrast to 2009, during 2010, corporate credit was mainly oriented towards investments, primarily in foreign currency. Furthermore, credit to households continued to decline, similar to 2009, but at a significantly slower pace than before.



The lower credit growth during 2010 was mainly related to a lower credit demand by economic agents due to their financial situation, uncertainties about the future outlook, and a slowdown of domestic economic activity. According to Bank of Albania's bank lending surveys, despite the tendency of easing credit standards in 2010, they remained tighter compared to the period prior to September 2008. A further deterioration of the loan portfolio quality has driven banks to be more cautious in expanding their lending activity. Similarly, in the last months (September-November), some of the banks in the system intensified the loan write off process, thus influencing the moderate increase of their loan portfolio.

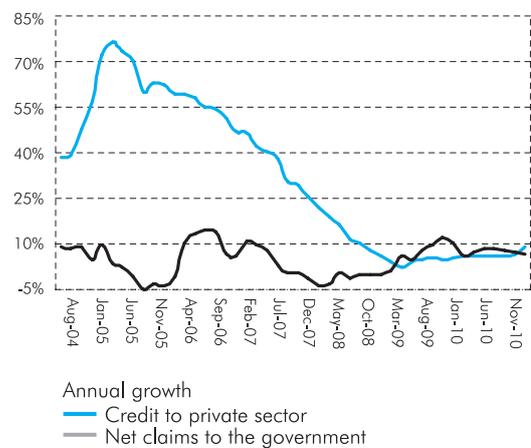
Regardless of the fiscal consolidation in 2010, public sector borrowing was higher than the previous year. The improvement of the liquidity situation, especially in the local currency, has also been reflected in the increased participation of banks in the T-bill and security auctions since October 2009. At the end of October, the first Albanian Eurobond was issued at a value of around EUR 300 million. The issuance of the Eurobond affected

⁷ For more refer to "Lending Survey Results, Q4 2010".

the currency structure of government financing activity in November, thus reducing the bank claims on the fiscal sector. During 2010, the high foreign currency inflows from the improved external position, the good performance of foreign currency loans to the economy and the shift to external borrowing to finance the budget deficit contributed to a higher growth of broad money against the moderate growth rates of the M2 aggregate. The foreign currency component highly contributed to the expansion of money supply, hence offsetting the significant reduction of the credit contribution during the entire 2010.

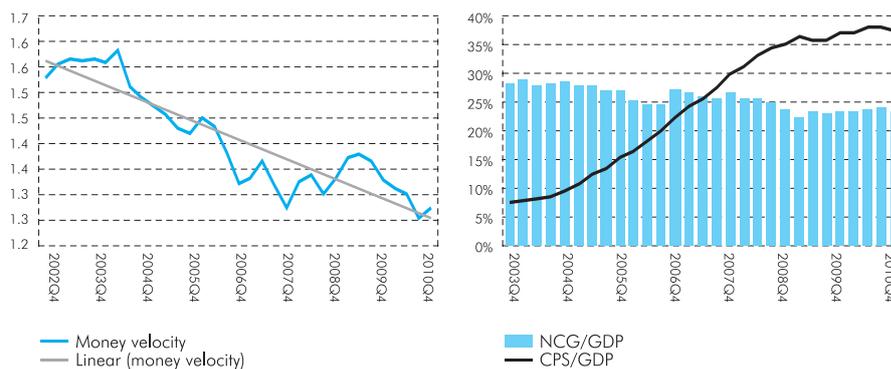
A deceleration of credit to the economy was reflected in the slowing money velocity during the second half of 2009 and for the most part of 2010, compared to the increasing tendency of this indicator during 2008. As a share of GDP, credit to the private sector experienced substantial reduction of growth rates. At the end of the third quarter of 2010, credit to the private sector accounted for about 38% of the GDP. The annual change of 2 pp in this ratio, as an indicator of the loan impulse to economic growth, has been falling during the last two years and is substantially lower than the pre-crisis period (7 pp).

Chart 4 Annual growth of private sector loans and net claims on the government



Source: Bank of Albania

Chart 5 Money velocity, net claims to the government and credit to private sector to the GDP



Source: Bank of Albania

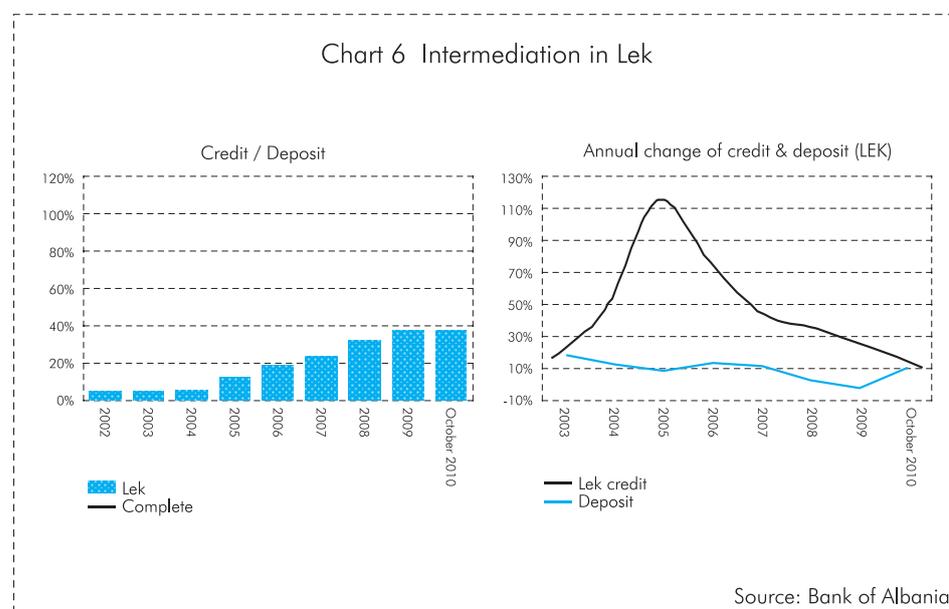
BANKING INTERMEDIATION BY CURRENCY

Most of 2010 was characterised by a slowdown of lending in Lek and an improvement of lending in foreign currency, which in turn led to the improvement of banking system's liquidity in foreign currency. These

developments were reflected on the banking intermediation as well as on its costs according to currencies.

INTERMEDIATION IN LEK

As at the end of November 2010, loan to deposit ratio in Lek reached 38.3%, marking a reduction compared to the peak of 38.8% in July 2010. This performance reflected a slowdown in Lek credit growth rates and a rapid improvement of Lek deposits, with the latter exceeding the pre-crisis levels since the early months of 2010. The long-term performance of Lek deposits displayed higher stability compared to foreign currency deposits. Meanwhile, Lek loans accounted for 35.7% of the loan portfolio, against 34.7% in 2009. Credit in Lek experienced a low demand for money by economic agents, in particular households, as the main borrowers of credit in Lek. The perceptions of still high uncertainty for the future (influenced by labour market developments) as well as households' increased propensity to save⁸ seemingly have influenced the reduction of households' demand for credit. Moreover, despite banks' easing lending standards for households during 2010, they still remain tight, discouraging as such households' marginal demand for loans. On the other hand, businesses, depending on their economic activity characteristics, increased their borrowing in foreign currency. Despite showing a slightly decreasing trend, the intermediation costs in Lek continued to be higher than foreign currency costs, hence making borrowing in Lek less attractive. On the other hand, the high government demand for funds influenced the banks' financing in government securities, thus reducing banks' initiatives to lend in Lek.

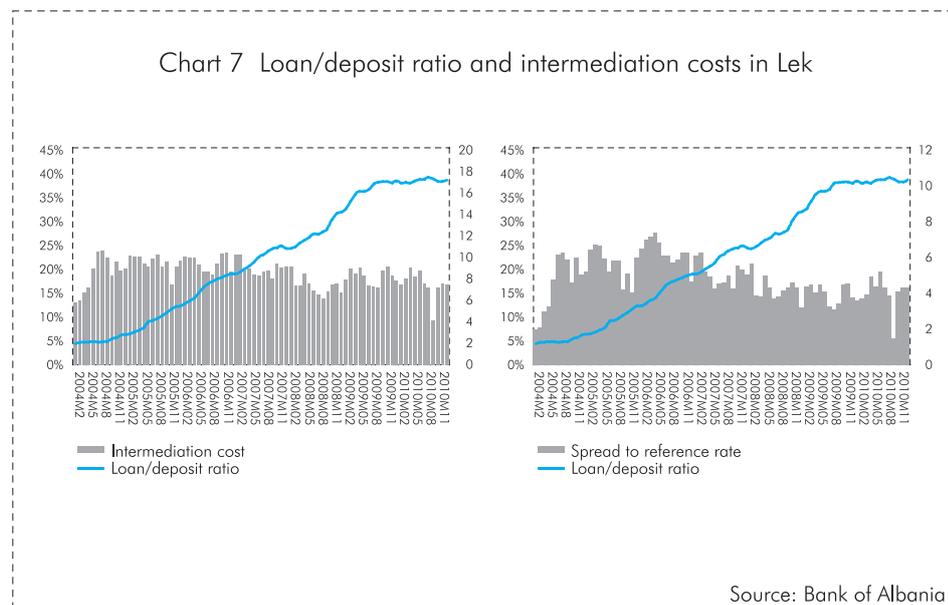


The annual growth rate of 12.5% of the loan portfolio fell significantly compared to the previous year when the same portfolio increased on average

⁸ In addition to a high growth of Lek deposits, survey results on consumer confidence are another indicator that indirectly confirms consumers' propensity to save. Read more in "Consumer Confidence Survey, 2010" at www.bankofalbania.org.

by about 33%. As of November, the net flow of Lek loans was about 40% lower than the previous year⁹. In addition, net claims to the government for the same period confirmed continuous and increased bank participation in the primary market. Banks' portfolio in government securities increased by ALL 16 billion, while for the same period in the previous year it increased by ALL 6 billion. Meanwhile, the high demand by fiscal agents contributed to the money creation in Lek and positive developments of Lek deposits. The total stock of Lek deposits reached the pre-crisis level as early as the first quarter. Lek deposits growth was constant and stable during the entire 2010 with an average growth of around ALL 3 billion per month. As at end November, annual growth rate of deposits in Lek was 10.2%.

Chart 7 Loan/deposit ratio and intermediation costs in Lek



In spite of substantial monthly fluctuations, Lek intermediation costs in the last 3 years have maintained a decreasing trend, reflecting an increased interest of banks in Lek crediting. In 2010, intermediation margin¹⁰ in Lek was lower by 0.7 pp compared to the 2009 average, but remained slightly higher than in 2008. The January-November developments reflected a decline in the price of Lek crediting, from an average of 13.7% in 2009 to 12.7%, as well as a moderate decline in the interest rate on new Lek deposits by 0.26 pp. Cost reductions of Lek loans, in addition to the decline of the reference rate of 12-month T-bills by 1.7 pp, have also reflected the preferential bank's lending policy to large clients.

INTERMEDIATION IN FOREIGN CURRENCY¹¹ - EURO

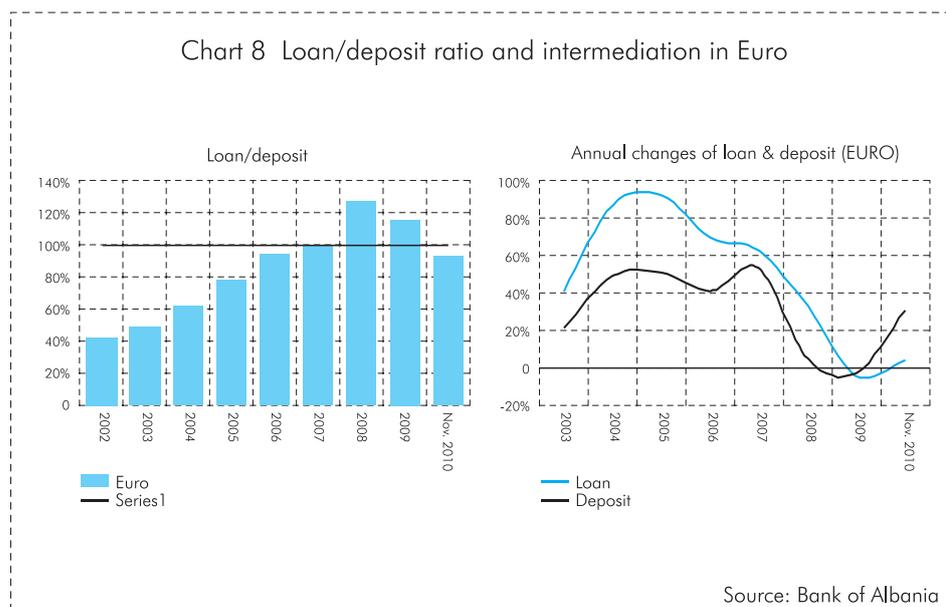
Euro intermediation during 2010 experienced a decline reflecting a rapid

⁹ ALL 14 billion compared to ALL 24 billion.

¹⁰ Intermediation margin refers to the spread between loan and deposit interest rates.

¹¹ Banks' activity in foreign currency is dominated by their activity in Euro, which accounts for more than 80% of foreign currency activity.

growth in deposits and slow increase of lending in Euro. In November, the loan-deposit ratio in Euro reached 94.4%, compared to 116% of the previous year. Intermediation rate in Euro has been shrinking month after month for more than a year. The spread of the global financial crisis effects was followed by a higher withdrawal of foreign currency deposits compared to Lek deposits, encouraged by exchange rate instability. Following the increased confidence in the banking system and the retrieval of the deposits in the banking system, the annual growth rate of deposits in foreign currency thus recovered, marking higher growth rates than Lek deposits since January. Deposits in Euro account for 84% of foreign currency deposits of the system, or 40% of total deposits. During 2010, the annual growth of deposits in Euro averaged 23% compared to the reduction in 2009 by around 4%. Remittances are the main source for deposits in Euro, which are channelled into the banking system and usually characterised by seasonal fluctuations. Foreign currency deposits are generally higher during August-September and December-January, corresponding to the seasonal inflows of remittances into the economy. Moreover, the higher levels of foreign currency lending encouraged the circulation of banking system's foreign assets as well as the creation of foreign currency in the economy.

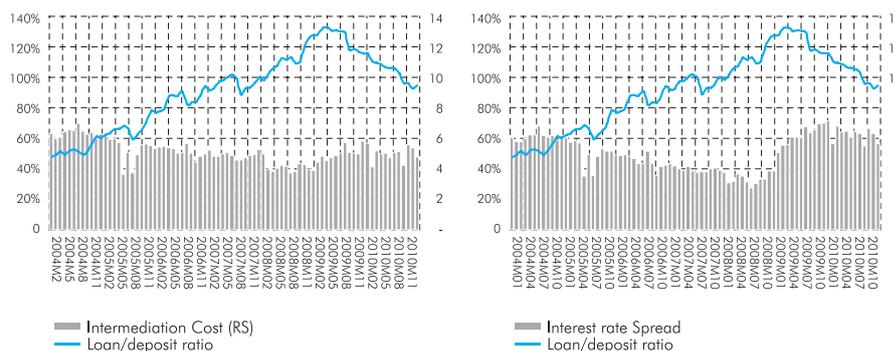


Lending in foreign currency demonstrated a more positive trend compared to the previous year, boosted by eased bank lending standards in response to improved foreign currency liquidity as well as the business demand for foreign currency loans, especially for investment purposes. In particular, the slowdown of credit in Euro appeared more evident for households, mainly for mortgage loans. Loans to households in foreign currency are estimated to bear higher risk (compared to businesses) because, in most cases, they do not have a natural hedge against exchange rate movements. During 2009, due to the depreciation tendency of Lek to Euro, banks applied strict terms on lending to households in Euro. During 2010, especially during the last quarter, banks offered favourable terms in lower interest rates for mortgages.

However, credit experts hold that, despite all favourable offers (low price) for lending to households, demand for loans from this group continues to be low. This behaviour reflects their consumption/saving behaviour as well as their expectations for price correction in the real estate market. The sluggish real estate market is another factor that has led banks to reassess their lending to households more cautiously, particularly in terms of collateral.

Despite temporary monthly fluctuations, during 2010 banks maintained the same intermediation margin as in 2009, at around 5.3 pp. This level is higher than the average 4.5 pp intermediation margin for 2008. The high levels of intermediation costs in Euro indicate that banks continue to account for the risk of exchange rate fluctuations, tightening of supervisory criteria and, in general, the uncertainties over future economic and currency outlook. Interest rates of deposits in Euro, although constantly declining in 2010, have continued to be obviously higher than rates in international markets.

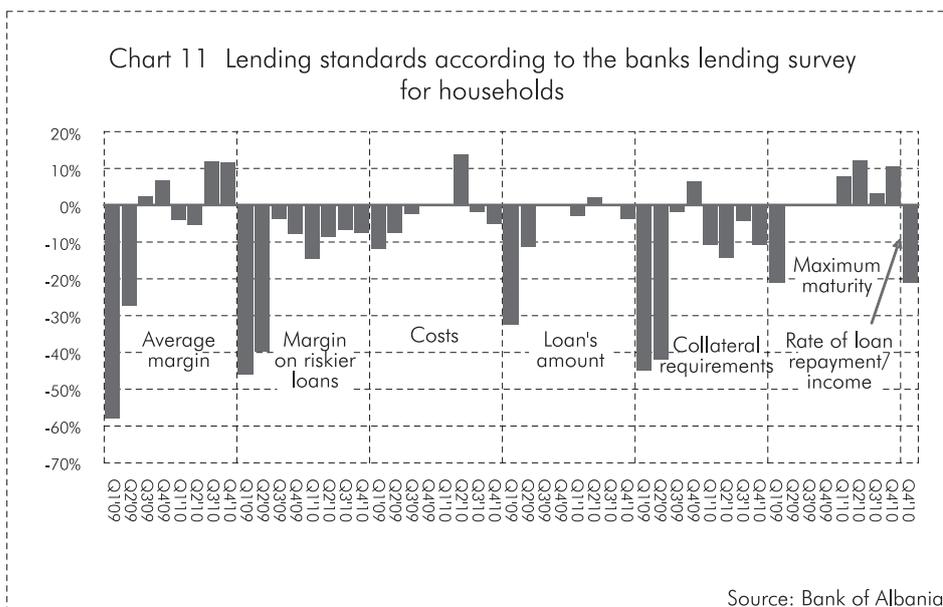
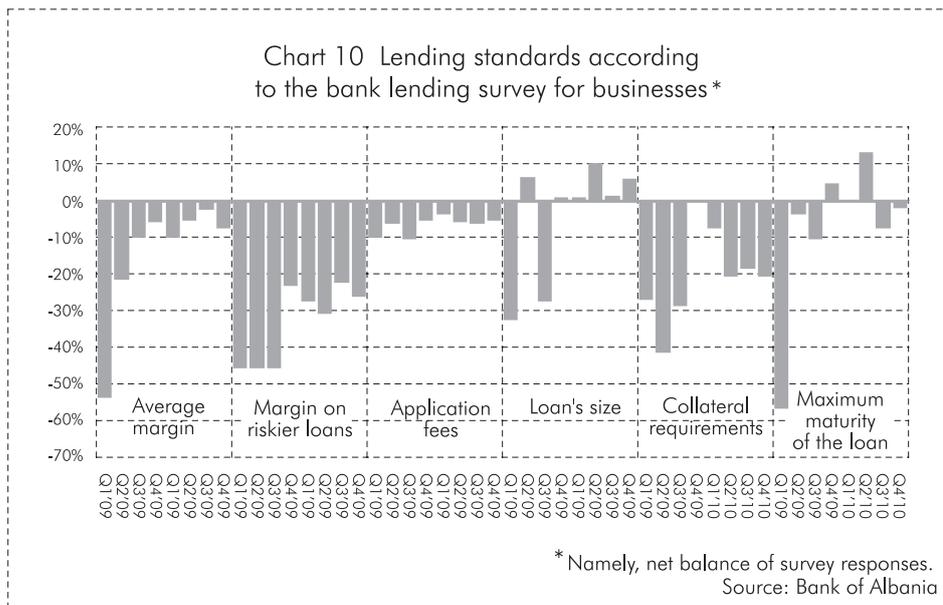
Chart 9 Loan/deposit ratio and intermediation costs in Euro



Source: Bank of Albania

NON-PRICE CONDITIONS OF LENDING

Bank lending surveys show that, during 2010, banks had a tendency to ease some of the non-price lending conditions. The chart of net balances indicates that towards the end of 2008 and in 2009, banks reported significant tightening of non-price conditions of lending. According to banks, tightening of collateral has been apparent both in terms of covering the loan with collateral and the quality of collateral required (type and location). In 2010, substantial improvement was noticed in net balances. Conditions such as loan size and payoff time were eased significantly compared to the previous year. Despite the seasonality of responses, there appears to be a tendency for easing and, in general, these conditions are not tight. Collateral requirements seem to have eased following their substantial tightening in 2009. In the last two quarters, there was a tendency of relative tightening, mainly on the type and location of collateral.



BANKING INTERMEDIATION IN THE COUNTRIES OF THE REGION¹²

The year 2009 proved to be a difficult year for the world economy, with the global financial crisis effects spreading to Central and South-Eastern Europe, Albania included. Crisis effects were present in all sectors of the economy, initially with the slowdown of financial intermediation and later with the reduction of international trade volume and transmission of these effects on the growth of the real economy. The financial crisis hit Central and South-Eastern Europe countries while the lending cycle was experiencing high and continuous growing rates.

¹² A Deutsche Bank periodical on Eastern Europe, October 2010. The countries of the region include: FYROM, Serbia, Bosnia and Herzegovina, Croatia, Turkey, Romania, Bulgaria, Poland, Czech Republic and Hungary.

However, some recovery signs in financial markets and financial and monetary indicators were observed in 2010, thanks to interventions of central banks and the accommodative fiscal policies. All Central and South-Eastern European countries are recovering from the crisis at a satisfactory pace, while formally overcoming recession. This includes countries such as Romania or Baltic countries characterised by a slower recovery compared to other CEE countries. These countries, in general, have recorded consecutive positive rates of economic growth for the first two quarters of 2010, projected to be stable despite being below the historical average rates.

Monetary expansion in these countries continues to be low. According to Deutsche Bank research for the first quarter of the year, recovery from the last global financial crisis and low economic growth were not supported by bank lending, as many of these countries recorded reduction or slowing trends of credit growth. Meanwhile, data for the second quarter and onward experienced a slow improvement of lending rates, showing the first signs of recovery after having reached the lowest levels. Although in real terms it may not be realistic to speak of an apparent annual private sector credit growth, the lending growth in many places has bottomed out. Availability of domestic or foreign financial resources, the performance of non-performing loans and risks related to capital and profitability of the banking system will continue to remain among the main causes of this slow recovery in lending. In addition, countries with a fixed exchange rate regime, actually undergoing a difficult period of local currency depreciation, do not foresee any rapid revival of credit to the economy.

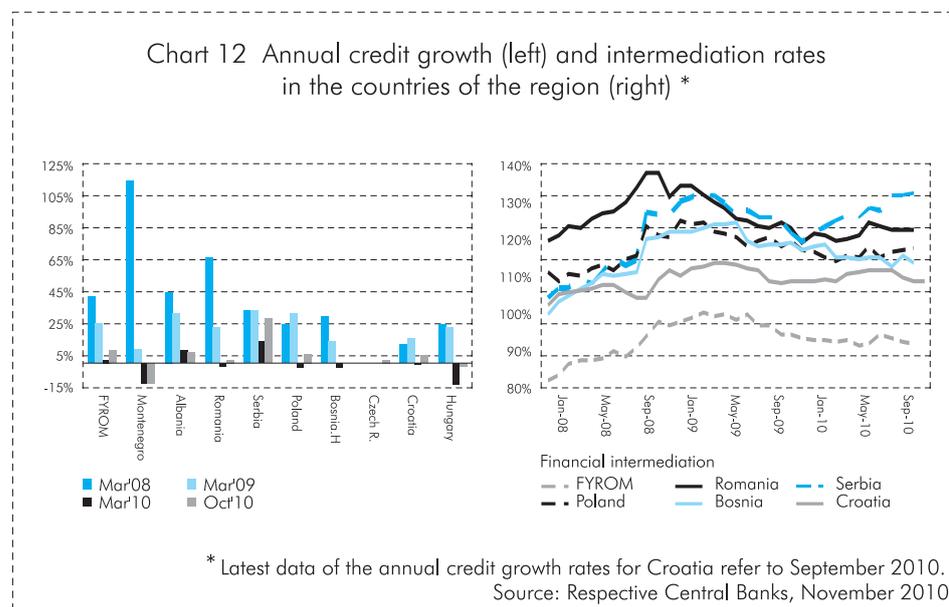
Stimulation of the economy by lending to the private sector is reflected in the credit impulse index¹³, which marked substantial improvement during the first half of 2010 compared to 2009, recording positive values in countries such as Ukraine, Hungary and Romania. On the other hand, intermediation rates which had been soaring during the pre-crisis period in Montenegro, have undergone severe reduction during the global financial crisis. Credit growth in Montenegro remained in negative territory, clearly below the historical average. Bosnia and Herzegovina experienced a slow recovery of credit to the economy¹⁴, marking a slight growth in August-September 2010. In the meantime, Hungary, in spite of the positive growth rates in June-September 2010, recorded again a drop in lending rates in October. In most countries of the region such as, Poland, Czech Republic, Croatia and Romania, the continually decreasing credit growth rates during the previous year, have reached their trough and started to grow again, thus demonstrating signs of a moderate and stable recovery during 2010 (see Chart 11). Serbia has clearly recorded higher average rates than other countries of the region. Credit rates to these economies have not decreased substantially, while remaining at relatively high levels on average even during the global financial crisis, mainly due to the government loan subsidising programmes to the agricultural sector and the household mortgages. Intermediation rates¹⁵ have been generally

¹³ Measured as a net difference in the loan portfolio as a percentage to GDP.

¹⁴ Figures in the chart represent nominal growth rates.

¹⁵ Represented by the ratio of total loans for the economy to total deposit stock.

decreasing during the global financial crisis, reflecting the substantial slowdown in loans versus the faster growth in deposits. Most CEE countries have been witnessing a growth in intermediation rates, mainly during the first half of 2010, therefore retaining almost the same figures in the third quarter.



Lending slowdown in most CEE countries was more distinguished for corporate credit. In countries such as Romania, FYROM and Croatia, loans to households experienced a sharper decline, hence affecting the developments in the total loan portfolio. In the context of recovering from the crisis, the banking sector has mainly supported businesses with short-term loans, initially to help them cover their liquidity needs, as well as for short-term investment purposes. In the case of Serbia, loans to important sectors, such as trade, industry and transport, have increased.

External funding of CEE countries has remained sluggish. On the other hand, outflowing funds for most of these countries turned out to be lower than expected. This situation reflected the entrance of CEE countries into a stage of deleveraging¹⁶, suggesting that banks may take advantage of ECB's facilitating monetary policy rates and abundant liquidity in the market. According to the Deutsche Bank Research, a comparative analysis with the Latin America crisis of 1983 and Asian crisis of 1997 suggests that deleveraging may continue up to 5 years. Nevertheless, the actual financial crisis consequences are thought to be comparatively smoother for a number of reasons. First, CEE countries are financially more integrated than Latin American countries prior to their 1983 crisis, enabling countries of this region to have stronger creditor-borrower relationship and a higher financial interdependency. Second, foreign claims on most of CEE countries have now reached their trough and have established growing trends¹⁷, partly also due to the exchange rate effect. A wider interest

¹⁶ Reduction of foreign bank claims as a percentage to GDP of recipient countries.

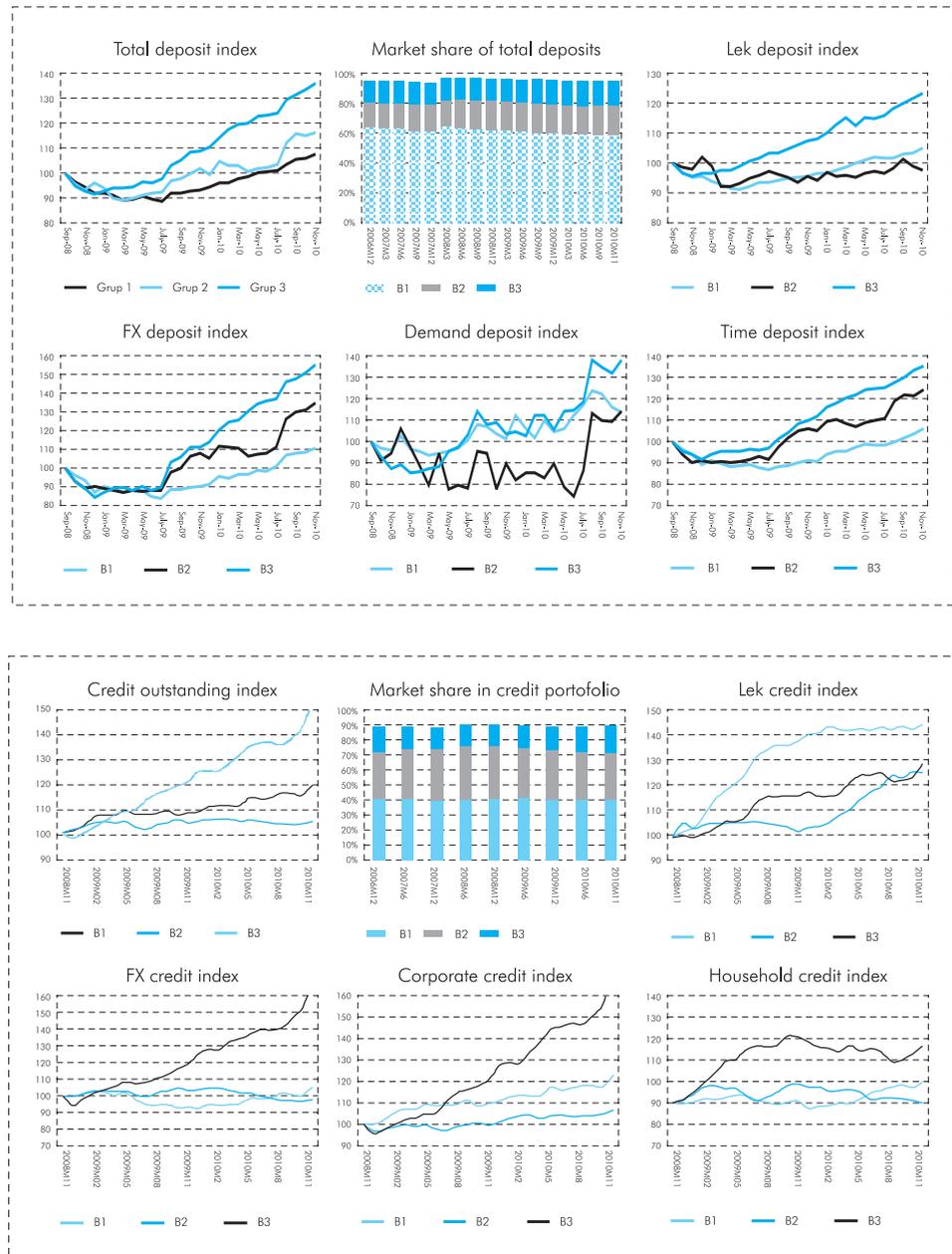
¹⁷ With the exception of Romania and Baltic countries.

rate margin favours concentration of retail banking in East European markets versus western markets.

Along with the weak economic performance and high unemployment rates, non-performing loans have marked an increase during 2009, retaining the same levels during 2010. Countries like Romania, Bulgaria and Hungary have recorded a deterioration of non-performing loan ratios, which have remained high since the beginning of the crisis. Non-performing loans in this region are expected to follow a rising curve and mark peak levels during the next 3-6 months. A fall in the ratio of non-performing loans to the total is envisaged to be gradual as restructured loans may also turn out to be non-performing. Moreover, the statistical effect of the higher numerator, in the presence of lower lending, increases the ratio of non-performing loans to the total. Rising non-performing loans may discourage the acceleration of lending to the economy in the short run.

Under the circumstances of high unemployment rates and low consumption levels, the sectors of the economy will continue to operate below their economic potential, thus generating slow economic growth rates. The low positive rates of the economic growth during the first half of the year, for most of the countries in the region, are not expected to be totally stimulated by lending to the economy. This stimulus is expected to be revived after a revitalisation of the demand by the private sector, primarily businesses.

ANNEX



INFORMATION ON RECENT MONETARY DEVELOPMENTS AND SELECTED ECONOMIC INDICATORS IN THE MAIN ADVANCED AND CENTRAL AND EASTERN EUROPEAN COUNTRIES

MEDVIN SHEHU, PRIAM RAMAJ & VALENTINA SEMI *

1. SUMMARY

The following material focuses on the description of the performance of the main indicators in advanced economies, some regional countries and Central European countries.

Global economic activity continued to recover, but the pace of the recovery remains uneven. The worldwide economic growth pace was slower over the third quarter relative to the first six months of the year. In developed economies, the growth pace has been more moderate, while in emerging economies this rate continued a dynamic pace. Overall, it is assessed that the ongoing negative pressures of unemployment and labour market, amid lower fiscal stimulus, have given rise to lower economic growth rate. The renewed concerns about the sustainability of public finances in some euro area countries have worsened the situation. Preliminary estimates suggest a growth of GDP in euro area for the third quarter of 2010, affected by the increase of consumption, while exports provided a somewhat moderate contribution compared with the first half of the year. The uncertainty related to the fiscal crisis in Greece and Ireland and the higher price risk for many countries with similar problems contributed to increasing instability in global financial markets.

In addition, the unsustainable situation arising from sovereign debt-related concerns in the euro area has been reflected in the foreign exchange market. In this context, after a 5-month period (July-October), the appreciation of Euro against USD reached a turning point in November and December, thus benefiting the appreciation of USD. Depreciating pressures appear to have been generated in most CEE and SEE countries as well as in Balkan countries, due to the higher sensitivity of the market agents with regard to risk perception.

* Monetary Policy Department, January 2011.

The views expressed in this publication are the views of the authors and do not necessarily reflect the views of the Bank of Albania.

2. SELECTED ECONOMIC INDICATORS, INFLATION AND MONETARY POLICY ORIENTATION

Key interest rates and use of instruments in developed economies

	Euro area (ECB)	USA (Fed)	UK	Japan
Inflation target	< 2%	n.a.	2%	0-0.1% ^{1 2}
(Key interest rate changes)	07.10.10 (0.00) 04.11.10 (0,00) 02.12.10 (0.00)	21.09.10 (0.00) 2-3.11.10 (0,00) 14.12.10 (0.00)	6-7.10.10 (0,00) 3-4.11.10 (0,00) 8-9.12.10 (0,00)	04-05,28.10.10 (0.00) 04.11.10 (0,00) 20.12.10 (0,00)
Current interest rate	1.00%	0-0.25 %	0.50%	0.10 %
Latest inflation	2.2 % (December)	1.1% (November)	3,3% (November)	0,20% (October)
Expected MPC meetings	13.01.11 03.02.11 03.03.11	25.01.11 15.03.11 26.04.11	12,13 January 9,10 February 9,10 March	24,25 January 16,17 February 14,15 March
Expected events	20 January,10 February Monthly Bulletin, March, ECB Forecast	12 January, 3 March Beige book	06 January Credit Conditions Survey - Q4 IR 1-16 February	January, February, Monthly Report of Recent Economic and Financial Dev./2010 Q4

Source: Respective Central Banks

ECB

In the euro area, the pace of economic growth slowed down over the last quarter. The third quarter recorded an economic growth of 0.3% relative to the quarter ahead, manifesting an uneven performance across euro area countries. This figure attributes to the decline in investment, the lower contribution of trade, and consumption, which recorded some modest growth. Euro area countries' public balance-related concerns increased further while Ireland submitted the request for financial assistance to both IMF and EU in November. Over the same month (November), the results of the second inspection carried out in Greece by EU, ECB and IMF authorities regarding the performance of the Greek government fiscal adjustment plan appeared positive, but they re-emphasised the need to continue implementing the consolidating measures. In the meantime, the ECB kept the key policy rate unchanged and in the early days of December, it decided to continue conducting the one and three-month refinancing operations over the year 2011. The financial markets in euro area have transmitted the heightened uncertainty of these months and featured higher risk premium. This setting was also present in the money markets, which recorded slight growth, being in line with the beginning of liquidity excess reduction by the central bank. The analysis of credit and monetary aggregates growth noted that inflationary pressures will remain contained during the second half of this year.

- On 13 December, the ECB's Governing Council decided to increase the ECB's subscribed capital by EUR 5 billion. This increase in capital aims to provide an adequate capital base in a financial system that has grown considerably, as stated out at the press release.

¹ Bank of Japan has not adopted Inflation Targeting and the rate considered as price stability from this bank points to the band 0-2% or precisely the midpoint of 1.00%.

² Source: "Understanding of Medium- to Long-Term Price Stability", Bank of Japan.

- On 16 December, in Brussels, the European Commission members agreed on the establishment of a future permanent mechanism to prevent and reduce the probability of a crisis in the future. This facility (European Stability Mechanism – ESM) will replace the temporary stability tool (EFSF) put in place earlier this year, and will provide financial assistance packages to euro area Member States, under strict conditionality functioning. The main agreed principal sets out the activity of this fund as lender of last resort and conditions its employment with the implementation of sustainable fiscal policies by the respective countries.

FED

Latest data for USA, published in December, show an improving economic situation, with an economic growth rate higher than the market agents' expectations for the third quarter. U.S. Department of Commerce published the figure of 2.5% relative to 2.0% published in the month ahead. The U.S. economic growth has been supported by the increase of consumption and investments, while net exports, albeit benefiting from USD depreciation over this period, have provided a negative contribution. The U.S. monetary policy continued to pursue a similar approach as that started since the last year by not changing the reference rates. The November decision about the re-entry of Federal Reserve into the securities market was an important development. Accordingly, the Federal Reserve will purchase bonds of the U.S. Government amounting to USD 600 billion up to June 2011. This decision was taken under the assessment that, notwithstanding the positive signals coming from the U.S. economy, it finds itself far from its growth potential. With this movement, the Federal Reserve hopes to provide a further incentive to the economic growth and to lowering the unemployment rate, which at the current juncture is expected to grow higher. The fiscal stimulus appears to have followed the monetary one in mid-December, being channelled through the reduction of taxes from the U.S. Government. The U.S. financial markets have, over these months, reflected the re-dimensioning of expectations for a rapid economic growth, which in turn has given rise to a moderate increase of the yields in these markets.

Key interest rates in both areas have been kept unchanged over this period. This has also been supported by the contained inflationary pressures, against a background where the growth of credit indicators increase still remains below the pre-crisis level.

2.1 SELECTED ECONOMIC INDICATORS IN CEE AND SEE COUNTRIES

Macroeconomic data:

	GDP (%)			Unemployment (%)			Inflation (%)			Current account deficit in % of GDP		
	2008	2009	Q3 '10 annual	2008	2009	Q3 2010	2008	2009	Q3 2010	2008	2009	Q3 2010
Hungary	0.5	-6.3	2.1	7.8	10.0	10.9	6.1	4.2	3.8	-7.3	-0.5	1.7 ³
Turkey	0.9	-4.8	6.4	11.0	14.0	11.1	16.0	8.8	8.4	-5.4	-2.3	-5.5 ⁴
Serbia	5.5	-3.1	2.1 ⁵	13.6	16.1	19.2 ⁶	8.6	9.4	7.7	-21.1	-6.9	-6.7
Poland	5.1	1.7	4.7	7.2	8.2	9.5	4.2	4.0	2.1	-4.7	-5.5	-1.7
Czech Rep.	2.5	-4.2	3.3	5.4	8.0	6.9	6.4	1.1	1.6	-0.6	-1.0	-2.7
Romania	7.3	-7.1	-2.5	4.4	7.8	7.35	7.85	5.6	7.5	-11.8	-4.3	-7.8 ⁷
Macedonia	5.0	-0.9	0.4 ⁸	33.8	32.2	32.1	8.3	-0.8	1.1	-12.8	-7	-0.6
Albania	7.8	3.0	3.3 ⁹	0.8 ¹⁰	2.2	13.5	3.4	2.2	3.4	-15.5 ¹¹	-15.1	-9.1

Source: Respective Central Banks and Statistical Offices

ECONOMIC ACTIVITY

Preliminary data released from Czech Statistical Office showed an improved economic growth over the third quarter of this year. This economic growth of 1.1% q-o-q and 3.3% y-o-y was mainly supported by the upsurge in trade and manufacturing industry. The forecast for the quarters ahead and for 2011 appears more optimistic based also on the fact that Czech Republic's main trading partners¹² have manifested positive and increasing economic developments. The ongoing recovery of investments, against a background of fiscal consolidation and a more optimistic household consumption outlook, is expected to be another positive factor. Labour market developments have been positive and the unemployment rate continued to lower over the last two quarters. According to CNB, future risks mainly arise from the external economy of Czech Republic due to the measures implemented from central banks of the main countries in view of weathering the crisis and the uncertainty reigning in the financial markets. GDP forecast shows an average growth by 2.3% in 2010 and 1.2% in 2011.

Latest data on Poland's economy show the persistence of positive economic growth rates. In the last quarter, its y-o-y and q-o-q growth rates were 4.7% and 1.3%, respectively. Domestic demand, private and public consumption provided the main contribution. Overall, industrial production, construction and capacity utilisation have improved throughout the year and enterprises

³ MPD calculations with preliminary data for Q2 GDP.

⁴ MPD calculations with preliminary data for Q3 2010 GDP and deficit.

⁵ Preliminary data from Statistical Office of the Republic of Serbia.

⁶ Q2 2010.

⁷ Q2 2010, current and capital account deficit.

⁸ Preliminary rate of Q2 2010.

⁹ Q2 2010.

¹⁰ The unemployment rate is for December 2008 and 2009. Source: Ministry of Labour, Social Affairs and Equal Opportunities.

¹¹ Revised figure.

¹² Germany, Poland and Slovakia.

show a good liquidity situation. With regard to the labour market, the growing employment in corporate sector has reflected this improvement, while wage rise rate dropped during this quarter. Business lending has not grown over this period, although banks report lower interest margins applied on loans. According to the National Bank of Poland, the possible risks for the future in general, and with regard to monetary policy in particular, derive from the external developments and the performance of public finances, where their disciplining is considered necessary to achieve macroeconomic stability.

According to Hungarian Central Statistical Office, economic growth pointed to 2.1% y-o-y and 0.8% q-o-q over the third quarter of 2010. These figures were higher than experts' expectations and forecast and confirmed the economic recovery shown during this year. Export, production sector and domestic consumption provided positive contribution in this quarter. The higher external demand contributed to the increase of employment in export-related sectors, which along with the cut in personal income tax are expected to impact the increase of domestic consumption. The Hungarian National Bank experts expect the Hungarian economy to continue to be positive, although the overall product will be below potential. Lending to enterprises continues to record moderate rates while lending terms and conditions are considered as tightened. With regard to wages, their rate is not expected to change due to the higher room and flexibility in the labour market. The Hungarian National Bank experts consider the external economy developments, and particularly the increase of risk perception from foreign investors with regard to the sustainability of Hungarian economy, as risk factors for Hungary's economic development. Risk premium in October increased and exceeded the required levels for the countries similar to Hungary. The implementation of a responsible and stable fiscal policy is deemed indispensable to hedge against external shocks, and also to support the economic recovery and growth.

Economic data from Turkey confirm the improvement of this year, though the growth pace slowed down in the last quarter. Economic growth in the third quarter posted 6.4% y-o-y and 1.1% q-o-q. Turkish economy ranked the first with regard to economic growth in Europe and it appears to progress convincingly toward the economic recovery. According to Central Bank of the Republic of Turkey's experts, the second half of this year will be characterised by more moderate growth rates. Indirect indicators reveal that exports, services and investments grew during July and August, but at a lower rate relative to the second quarter. These items, along with the decline of agriculture output, have affected the slowdown of the economic growth pace over the third quarter. Domestic demand is expected to manifest stable upward tendency, sustained by the stability of political factors and the improving labour market conditions. In the meantime, the perspective of external demand remains vague owing to the uncertainty about the global economic recovery.

According to the National Bank of Serbia, economic recovery is expected to continue over the third quarter, although preliminary data attest to a slight

slowdown of the economic growth (from 2% to 1.4%¹³ in this quarter). This growth is mainly supported by the positive performance of trade and overall industrial production, while the contraction of agriculture, construction and electricity sectors provided a negative contribution. The rise of nominal gross wages slowed down during the third quarter, while real wages fell in both sectors¹⁴. This factor, combined with the unchanged industrial output, gave rise to lower unit labour costs over this period. The freezing of wage rise until April 2011 will change in January and is expected to provide positive effects to domestic consumption over the period ahead. Lending slowed down over this quarter due to the fall of demand, particularly from businesses. Worth noting however is the fact that for the first time after two years, the growth of business loans for investment purposes was higher than loans for liquidity and working capital purposes. The forecast for 2010 remains similar to the previous NBS's forecast, forecasting an economic growth by 1.5%, whereas for 2011 it is forecast to grow by 3-3.5%. External demand is considered the underlying growth factor. The role of investments has been also considered as highly positive.

Romania continued to record a negative economic growth over the third quarter. It pointed to -2.5% y-o-y and -0.6% q-o-q. The effects of the tight public balance policy and a further reduction of consumption affected negatively the GDP rates, where the increase of inventories only smoothed down the economic contraction during this quarter. Exports have been maintaining an upward tendency, but imports have also been increasing at higher rates, thus yielding a negative contribution of net exports to economic growth. The internal political concerns, mainly related to the implementation of tight fiscal measures are considered as possible factors that pose threat to the macroeconomic stability and market agents' confidence in Romanian financial assets. The bailout package provided by the IMF imposes the implementation of a prudent fiscal policy. Economic growth is expected to be positive only in 2012, whereas in the next year it is expected and aimed to subdue the contraction of economic growth.

The forecast of the National Bank of the Republic of Macedonia concerning GDP growth remains at around 0.6% for the year 2010. The recovery of economic activity has been progressing, albeit at a slower pace. The latest forecast expects investment and trade to provide a positive contribution to the economic growth over the third quarter of this year. Also, consumption is expected to increase as reported from the recent optimistic data on the labour market. At the end of September, the National Bank of Macedonia reported further growth of total loans by 7.7%, which showed an upward tendency in the previous months as well. Current account deficit is expected to yield a surplus of 0.5% as a share of GDP relative to 0.8% envisaged in July's forecast. The increasing trade deficit was one of the factors to have generated the previous deviation.

¹³ This preliminary estimation differs from that published by the Statistical Office of the Republic of Serbia, which estimates it at 2.1%.

¹⁴ Public and private sector.

INFLATION

Annual inflation in Czech Republic marked 2.0%¹⁵ in November, maintaining the same rate for the third successive month. Pressures deriving from domestic economy appear contained while import price pressures on consumer prices seem to show a slight deflationary nature owing to the positive performance of the domestic currency. The increase of primary commodity prices was the sole rationale behind the increase of inflation.

Annual inflation rate in Poland marked 2.8% in October, thus exceeding the central bank's target of 2.5%. The rise in electricity and food prices gave rise to the increase of inflation, while core inflation remained unchanged. The low inflation over this period has mainly expressed the impact of the comparative base effect (inflation increased considerably a year ago owing to excise and oil price). Inflation is expected to increase again in the months ahead, and in the beginning of 2011, it will also reflect the pre-announced VAT increase.

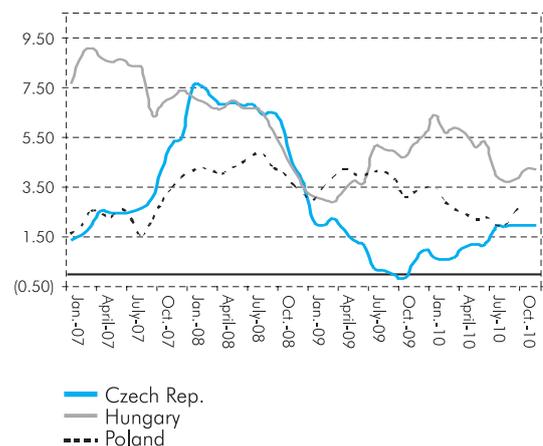
Inflation rate in Hungary remains above the central bank's target of 3%. Annual inflation did not change in November compared with the previous month and marked 4.2%. The high food prices are the rationale behind the unfavourable performance of inflation. The monetary authority assesses that, at the current juncture, inflation is expected to remain above the target (3%) for a considerable period of time, thus affecting the inflationary expectations in the period ahead.

In Turkey, annual inflation dropped to 7.29% in November from 8.62% in the previous month. The previous two months also featured lower inflation due to the comparative base effect. Although unprocessed food prices continued to rise considerably, inflation remained low for all other sub-categories, mainly for transport and services. Thus inflation is expected to fall in line with the medium-term expectations of the target (6.5% ± 2.0%).

Inflation in Serbia continues to increase, marking 10.3% in December, considerably above the target of 6.2% ± 2%. The continuous increase is mainly driven by administered prices, agricultural product prices and oil price in the world market. Combined with the depreciation of the Serbian Dinar, these developments have increased substantially the inflationary pressures on the

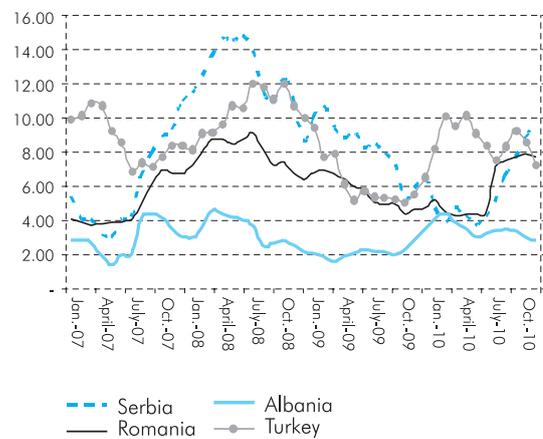
¹⁵ Czech National Bank's inflation target is 2.0%.

Chart 1 Inflation rates



Source: Respective Central Banks

Chart 2 Inflation rates



Source: Respective Central Banks

Serbian economy. Nevertheless, the outlook for the persistence of aggregate demand-side disinflationary pressures due to the more moderate rise of wages and pensions than projected, and supported by the tight measures undertaken by the monetary authority, are expected to bring inflation back to within the forecast range ($4.5\% \pm 1.5\%$) as at end 2011 and $4 \pm 1.5\%$ as at end 2012).

Annual inflation in Romania dropped to 7.73% in November from 7.90% in October, but it remains high relative to the $3\% \pm 1\%$ target. The rise of prices over the last five months owes mainly to the increase of VAT¹⁶ by the Government and the rise of agricultural food prices. The increase of inflation has been also factored in the forecasts of the central bank, leading the latter not to undertake further accommodating monetary policy measures. However, it is assessed that the VAT increase effects will terminate next year and the annual inflation rate is expected to fall to within the target.

According to the National Bank of the Republic of Macedonia, the disinflationary trend of 2009 has come to an end. Annual inflation has constantly been upward over the year 2010, pointing to 2.9% in November relative to 1.9% in August. Inflation is expected to continue to increase, but still remaining within the forecast, mainly owing to the easing of monetary policy, the rise of import and electricity prices, which will be offset by domestic demand.

2.2 MONETARY POLICY ORIENTATION IN CEE AND SEE COUNTRIES

Key interest rate in Central European and regional countries:

	Czech Rep.	Poland	Hungary	Romania	Serbia	Turkey	Albania
Inflation target	2.0%(±1%),	2.5 % (±1%)	3.0 %	3.0% (±1%)	7.0% (±2%)	6.5% (± 2%)	3.0% (±1%)
Latest meetings and changes of the key interest rate	23.09.10 (0.00)	27.10.10 (0.00)	29.11.10 (+0.25)	29.09.10 (0.00)	11.11.10 (+1.00)	11.11.10 (0.00)	27.10.10 (0.00)
	04.11.10 (0.00)	24.11.10 (0.00)	06.12.10 (0.00)	02.11.10 (0.00)	09.12.10 (+1.00)	16.12.10 (0.00)	24.11.10 (0.00)
Current interest rate	0.75%	3.5%	5.5%	6.25%	11.5%	7.0%	5.0%
Inflation	2.00%	2.7%	4.2%	7.73%	9.6%	7.29%	2.8%
Expected MPSC meetings	22.12.10	29.12.10	10.01.11	05.01.11	13.01.11	13.01.11	22.12.10
	03.02.11	26.01.11	24.01.11	03.12.11	10.02.11 10.03.11	17.02.11	26.01.11
Expected releases	February 11 (Inflation Report)	November (Inflation Report)	December (Inflation Report)	December (Inflation Report)	December (Inflation Report)	December (Inflation Report)	26 January (Monetary Policy Rep.)

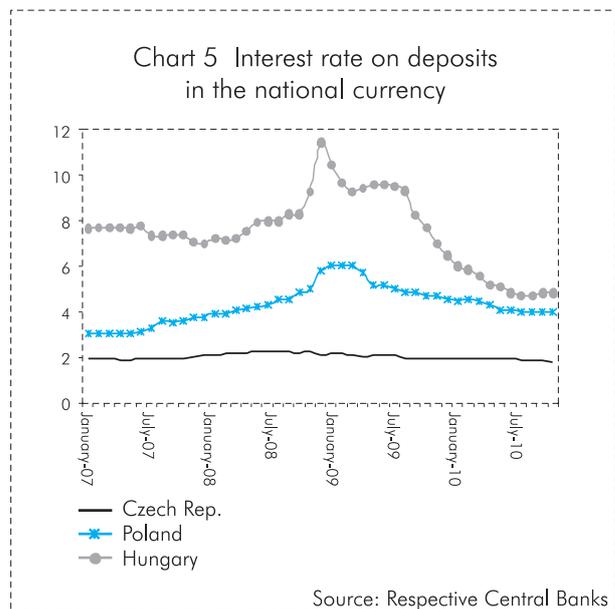
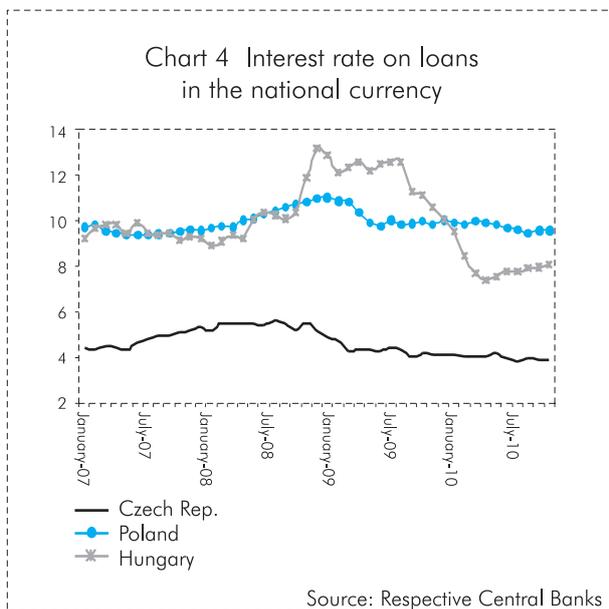
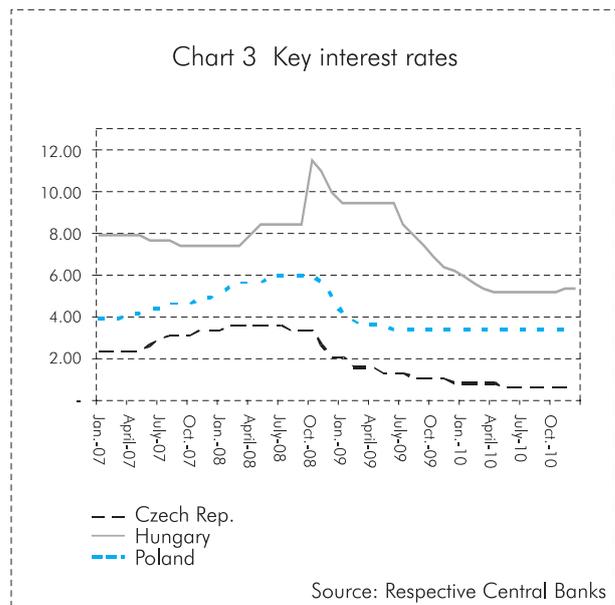
Source: Respective Central Banks

Czech National Bank kept the 2-week REPO rate steady at the historical minimum of 0.75% (it was last changed in May 2010). The stable inflation rate and the expectations for the persistence of this trend for the period ahead, have sustained this decision. Against a similar setting, the central bank is not expected to tighten the monetary conditions.

¹⁶ VAT changed by 5 bp (to 24%) in order to meet the budget targets under the Agreement with the IMF, in the framework of the bailout package solicited by Romania to counter the ongoing financial crisis (25 billion).

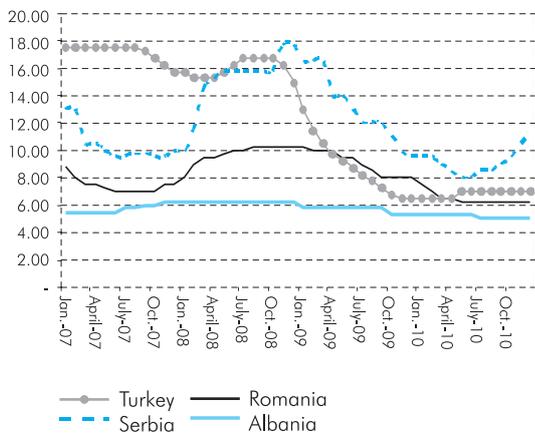
The National Bank of Poland kept the key interest rate unchanged at 3.50%. Although inflation exceeded slightly the bank target, core inflation did not undergo any changes. The low inflationary pressures on the Polish economy and the recurring concerns over the possible increase of capital inflows into advanced countries, due to the prolonged periods of the main central banks' easing policy, combined with the risk for the global economic activity slowdown, were the rationale behind this decision.

The Central Bank of Hungary raised the base rate by 25 bp to 5.5%. The monetary authority's reaction mainly owes to the latest developments in inflation. In more concrete terms, inflationary pressures have been persistently upward over the short run, which in turn is expected to affect inflation expectations over the period ahead. In addition, the price rise shock is expected to reflect second-round effects. In light of this, the Hungarian monetary authority declares that it will be open to increasing the base rate in the months ahead in order to keep the primary target of inflation.



At end December, the Central Bank of the Republic of Turkey decided to cut the key interest rate by 50 bp to 6.50%. This decision was followed by the increase of the required reserve ratio for deposits denominated in Turkish Lira from 0.6% to 8.0%. The Monetary Policy Committee highlighted in its statement that the implemented measures are not of an easing nature, but they aim to reduce the credit growth through the increase of the liquidity cost, thus ensuring the stability of prices and the financial sector. The combined central bank's policy aims to address the concerns arising from the balance of payments dynamics through the reduction of credit growth.

Chart 6 Key interest rates

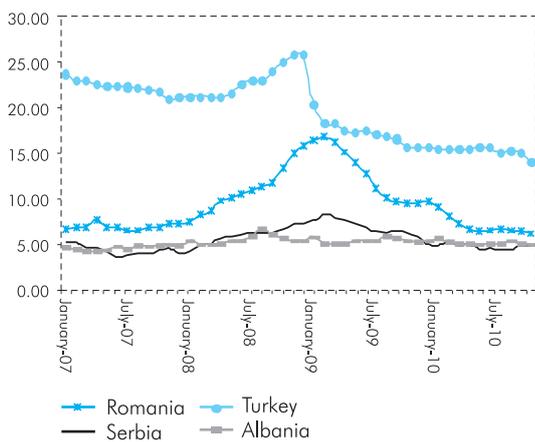


Source: Respective Central Banks

In January 2011¹⁷, the National Bank of Serbia raised the key policy rate for the 6th successive time by 50 bp, from 11.5% in November to 12.0%. The decision on the further increase of the key policy rate reflects the high inflationary pressures, which seem to have affected the inflation expectations. However, worth noting is that the raise by 50 bp compared to the previous month's 100 bp raise seems to have been affected by the lower-than-expected rise of pensions and wages, which generates expectations for the persistence of aggregate demand-side disinflationary pressures. Hence, after this decision, the National Bank of Serbia's Executive Board expects inflation to be brought back to within the target range only in the second half of the next year.

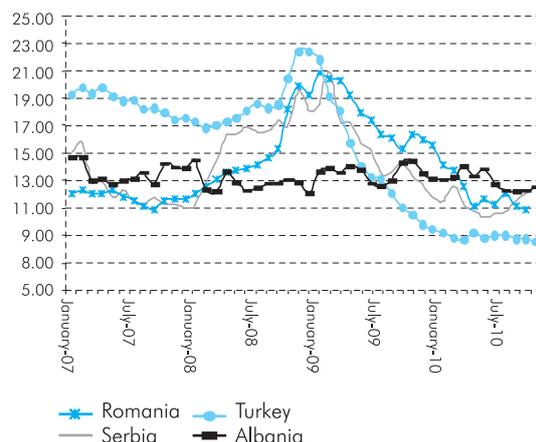
National Bank of Romania continues to keep the key rate unchanged at 6.25% (it last changed on 4 May 2010). The central bank's experts state that the return of inflation to a downward path will decisively hinge on the implementation of fiscal-structural reforms along with the absorption of EU and IMF funds, and it will serve as a prerequisite for recovering confidence in the financial markets. Thus, the NBR Board decided to adopt, as from 2013, a flat multi-annual inflation target of $2.5 \pm 1\%$.

Chart 7 Interest rate on deposits in the national currency



Source: Respective Central Banks

Chart 8 Interest rate on loans in the national currency



Source: Respective Central Banks

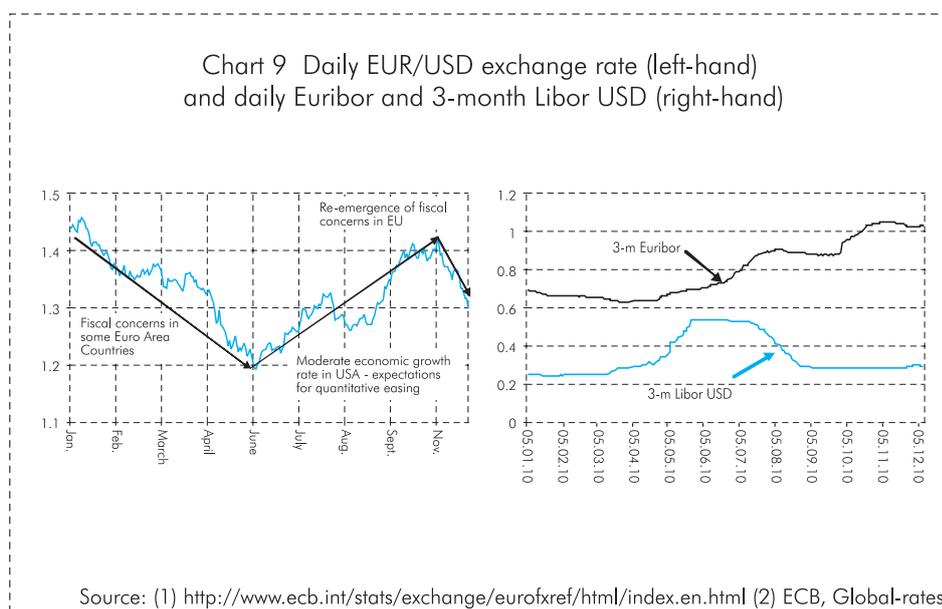
National Bank of the Republic of Macedonia, after a stable period, reduced the bills' interest rate from 4.5% in August to 4.0% starting from 9 December 2010. This decision came in response to the positive movement of the foreign exchange markets. Notwithstanding the positive trend, the economy needs incentives in order to use all its potentials.

¹⁷ 17 January 2011.

3. EXCHANGE RATE

EUR/U.S. DOLLAR EXCHANGE RATE

The European currency continued to strengthen its position against the U.S. dollar during September and October. It has mainly reflected the market expectations about the continuation of easing quantitative measures implemented by FED in view of the less optimistic results for the U.S. economic activity over the second quarter of the year. Market trends with regard to the common European currency seem to have consolidated further owing to the positive results of some economic indicators in the euro area.

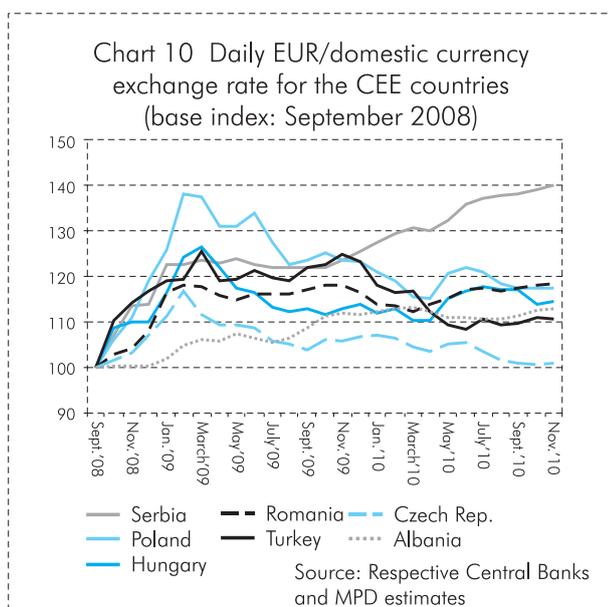


However, the statement of the Federal Reserve Chairman in the beginning of November, with regard to the quantity and period of interventions that this authority plans to implement and the positive results of U.S. businesses, put a halt to the market agents' reactions related to the performance of U.S. economy. On the other hand, the fiscal position deterioration in some euro area countries brings back the debates that characterised EUR depreciation over the first half of 2010 that were mainly related with the uncertainty about the sovereign debt. The depreciation pressures against the European currency, generated from the above mentioned factors seem to have been somewhat buffered out during December, due to unsatisfactory developments in the U.S. labour market in November and Moody's negative comments about the reduction of taxes by the U.S. Government.

The short-term perspective of both main currencies still shows high uncertainty. Thus, notwithstanding the efforts of both large economies to establish a favourable economic environment through the reduction of taxes in the U.S. economy and the agreement for the establishment of a permanent mechanism to cope with the problems related to EU's debt, there still remain

risks to be faced with. The still weak signals from the real estate market and labour market and the moderate growth of the global economic activity may be mentioned as such.

With regard to the exchange rate, worth noting is the performance of interest rates in the money market. The maintenance of the key interest rate at low levels, along with some unconventional quantitative measures implemented by ECB, is expected to reduce the interest rates spread in the money market, which reflects a considerable increase since the second half of 2010. In this view, the capital inflow incentive, which was expected to positively affect euro trading, is forecast to partially slow down over the period ahead. However, worth noting is that, although such a development may bring about unsatisfactory developments in terms of the exchange rate, it is expected to impact the export performance, the main contributor to Euro area's economic growth.



EXCHANGE RATE IN CEE AND SEE COUNTRIES

The performance of Euro/domestic currency exchange rate in CEE and SEE countries attest to divergences, not only geographically but also time-related for the period September-November. In concrete terms, the improved risk perception internationally during September-November benefited the trading of Central European currencies. In the meantime, Romanian and Serbian currencies continued to show depreciation pressures mainly owing to domestic economic developments.

However, the tensions in capital markets with regard to euro area countries' sovereign debt generated depreciation pressures in this region in November. EUR/Turkish Lira is an exemption to this behaviour, as it seems to have pursued the performance of the European currency in the international markets.

	Serbia	Turkey	Romania	Poland	Hungary	Czech Rep.	Albania
August 2010	105.385	1.9491	4.2434	3.9871	281.45	24.817	136.24
September 2010	105.541	1.9536	4.2653	3.9525	281.7	24.656	137.05
October 2010	106.424	1.9802	4.2808	3.9505	274.11	24.539	138.39
November 2010	107.087	1.9722	4.2933	3.956	275.77	24.65	138.820
December 2010	106.362	2.0127	4.2924	3.9934	277.36	25.152	138.81
Monthly change September 2010	0.15%	0.23%	0.52%	-0.87%	0.09%	-0.65%	0.59%
Monthly change October 2010	0.84%	1.36%	0.36%	-0.05%	-2.69%	-0.47%	0.98%

Monthly change November 2010	0.62%	-0.40%	0.29%	0.14%	0.61%	0.45%	0.31%
Monthly change December 2010	-0.68%	2.05%	-0.02%	0.95%	0.58%	2.04%	-0.01%

Source: Respective Central Banks and MPD estimates

CZECH REPUBLIC

Long-term currency rating		
A (stable) (Moody's)	A (stable) (S&P)	A+ (stable) (Fich)

Czech currency continued to strengthen its positions against EUR during September and October, traded at 24.43 Czech Koruna per EUR at the beginning of October, the peak rate over the last two years. The positive macroeconomic developments, the improvement of market sentiment in Central and Eastern European countries and the depreciation of USD were the main contributors to the strengthening of the Czech Koruna during this period. However, the announcement of easing measures by the Federal Reserve and the re-emergence of fiscal-related concerns facing the euro area countries seem to have negatively impacted the trading of Czech currency, manifesting a slight depreciation tendency during November, which worsened further in December due to the downward revision of GDP for 2011.

With regard to the short-term outlook for the Czech currency, the main factors that may exert depreciation pressures relate to the possible difficulties the Czech economy may encounter in view of implementing the consolidation measures in the public sector, the worsening of market agents' perception about Eastern and Central European countries and the deepening of fiscal-related concerns in the euro area. Nonetheless, the balance of trade surplus and the low foreign debt level may be seen as buffering factors against these risks.

POLAND

Long-term currency rating		
(Moody's)	-- (S&P)	A- (stable) (Fich)

The appreciation trend of Polish currency reported during the summer was also confirmed in September and October. Polish Zloty's positive performance has been supported by the positive developments this economy showed in the macroeconomic context, whose economic performance was ranked the best in the region. This fact seems to have encouraged the channelling of investment funds toward this economy. However, the uncertainty related to the fiscal-related concerns in the euro area has yielded depreciation pressures of this currency during November and December.

The EUR/Zloty exchange rate is expected to remain highly sensitive to developments in the euro area over the period ahead. Negative pressures on

this currency may be generated from the developments in the public finance sector, which according to the forecasts stated in the statement of the Polish Governor, is expected to exceed the level of 2009 and record a budget deficit of 7.9%¹⁸. However, positive signals from foreign trade, labour market and the difference of economic growth rates compared with EMU countries is expected to counterbalance the possible pressures arising from the above mentioned factors.

HUNGARY

Long-term currency rating		
Baa1 (negative) (Moody's)	BBB (stable) (S&P)	BBB (negative) (Fich)

The depreciation trend of Hungarian currency seems to have shown a temporary break in October, when HUF/EUR appreciated by 2.7% on average. The dynamics of the domestic currency seems to reflect the weakening of fiscal-related concerns facing the Hungarian economy owing to the fiscal consolidation plan for year 2011 introduced in October, and the Monetary Council's decision to raise the central bank base rate. The increase of international agents' demand seems to have contributed along the same line. Due to the turbulences facing the major currencies, they directed their investments towards the regional currencies. Nevertheless, the Hungarian currency resumed its depreciation trend in the following months, thus reflecting the global market agents' behaviour to risk on a regional level.

The performance of the Hungarian Forint over the period ahead will continue to largely depend on the developments in the fiscal sector. The Hungarian Government's solvency and the implementation of measures for fiscal consolidation will have a primary role in the performance of this currency. However, experts assess that the increase of interest rate spread and the recovery of global sentiment for this region may benefit the developments of the Hungarian currency.

ROMANIA

Long-term currency rating		
Baa3 (stable) (Moody's)	BB+ (stable) (S&P)	BB+ (stable) (Fich)

The Romanian currency continued to depreciate against the European currency during September-November. The negative performance of Romanian Leu mainly reflects the uncertainty arising from the political concerns. This factor seems to have been added to the rather low optimistic figures of public expenses and economic growth, thus hitting the investors' sentiment of this economy compared with other regional countries. On the other hand, this currency appeared stable in December, appreciating slightly by 0.02%.

¹⁸ Source: Inflation Report for October from the National Bank of Poland.

In light of these developments, the Romanian currency is expected in the period ahead to be largely affected by the fiscal developments and the frail external sector. However, the recent statements of the Romanian Central Bank, which highlighted the willingness of the monetary authority to intervene in the foreign exchange market whenever necessary, are believed to partially mitigate the depreciation pressures generated from the above mentioned factors.

TURKEY

Long-term currency rating		
-- (Moody's)	BB (positive) (S&P)	BB+ (positive) (Fitch)

Turkish Lira continued to maintain a depreciation trend against the European common currency over September and October, thus reflecting the increase of the reserve requirement ratio for foreign currency (-1 pp) at a higher degree compared with the TL reserve requirement ratio (-0.5 pp). The ongoing concerns of the Central Bank of the Republic of Turkey with regard to the balance of payments dynamics and its implications for price and financial stability have given rise to the reduction of the key interest rate coupled with an increase of the TL requirement ratio in December. Against this setting, after appreciating slightly in November, the Turkish Lira continued to reflect a depreciation trend in December.

The rapid recovery of domestic demand, coupled with a more moderate foreign demand, gave rise to a more accelerated growth of credit and wider deficit, thus posing a threat to financial stability. The main risks facing the Turkish economy relate closely to the external sector developments, their extent and pass-through to the economy from the monetary authority.

SERBIA

Long-term currency rating		
-- (Moody's)	BB- (stable) (S&P)	BB- (negative) (Fitch)

The depreciation tendency of the Serbian Dinar against the Euro, shown since the early 2010, persisted during September-November. The high demand for foreign currency and the rather unsatisfactory perception of international markets with regard to SEE countries are considered to be the rationale behind the depreciation pressures of the Serbian currency. The recovery of domestic demand during the last months has contributed to the widening of the current account, with the external debt also increasing. The depreciation pressures generated from the external sector of the economy seem to have been coupled with pressures of a seasonal nature. Against this setting, the consecutive raise of the key policy rate, as a response to the inflationary pressures manifested from this economy, are assessed to

have had a temporary and low impact on the exchange rate performance. Nevertheless, the Serbian Dinar appreciated slightly in December.

The exchange rate developments over the period ahead are expected to continue to reflect high sensitivity against the economic stability and fiscal developments. In light of this, the widening of the interest rate spread and the more optimistic-than-expected signs in the economic activity may fuel capital inflows and reduce the negative dynamics of the current account.

BANK OF ALBANIA
BULLETIN NEWS
JULY-DECEMBER 2010

Bank of Albania, in cooperation with the University of Oxford, organize a roundtable

On 8 September 2010, the Bank of Albania, in cooperation with the University of Oxford, organized a roundtable on “Economic and Political Challenges of Regional Cooperation”. Representatives of the academic circles in Albania, the banking system, public institutions, international organizations operating in Albania and the Bank of Albania attended this roundtable.

The Bank of Albania organized this roundtable as a follow-up to discussions held in the meeting “Economic Growth in Albania – Need for a New Model” in May 2010 in Berat. Discussions in this meeting focused on the analysis of economic growth models and regional cooperation, the identification of the main challenges facing the region, and the external anchors towards EU integration.

The roundtable began the proceedings after the signature of the cooperation agreement between the Bank of Albania, represented by the Governor, Mr. Ardian Fullani, and the University of Oxford, represented by Prof. Othon Anastasakis.

The cooperation between the partner institutions will be carried out through research studies on the Albanian and South-East European political economy. This cooperation will enhance the capacities of scientific research and education as two preconditions for establishing professional capacities in order to guarantee the success of these reforms. This objective is expected to be met within a three-year period. University of Oxford is one of the world’s leading academic institutions with extraordinary qualities in the field of scientific research and education.

Former Chairman of the Governing Board of the Swiss National Bank visits the Bank of Albania

At the invitation of the Governor of the Bank of Albania, Mr. Ardian Fullani, on 13 September 2010, the former Chairman of the Governing Board of the Swiss National Bank, Mr. Jean-Pierre Roth, had an official visit to Albania.

In the framework of this official visit, Mr. Roth delivered a lecture on “Switzerland: small country, monetary island”. The lecture was held in the Bank of Albania hall and it was attended by Bank of Albania representatives and commercial banks’ executives.

Deputy Governor of the Sveriges Riksbank, Mr. Lars Nyberg, visits the Bank of Albania

At the invitation of the Governor of the Bank of Albania, Mr. Ardian Fullani, on 14-15 September 2010, the Deputy Governor of the Swedish National Bank (Sveriges Riksbank), Mr. Lars Nyberg, had an official visit to Albania.

The discussions held during the meeting focused on the performance of the Albanian economy and the banking system in particular.

This is Mr. Nyberg’s second visit to Albania. The initiative undertaken by the Bank of Albania a few years ago on enhancing the dialogue between the regional central banks and the European Central Bank has also enjoyed the support of the Sveriges Riksbank. This initiative has assisted these banks in

their way towards the membership into the European System of Central Banks (ESCB). Sveriges Riksbank has also provided technical assistance in order to prepare the Bank of Albania in the approximation process with the ESCB.

On 30 September 2010, the Governor of the Bank of Albania, Mr. Ardian Fullani, held a regional meeting in the city of Gjirokastra with representatives of the business community, local government, banking sector and academics of Egerem Çabej University. In his speech, Governor Fullani focused on the identification of challenges facing the Albanian economy. Their identification will help steer debate on the economic growth model in the future.

The Governor of the Bank of Albania, Mr. Ardian Fullani, holds a Regional Meeting in the City of Gjirokastra

In the framework of Bank of Albania's commitment to economic and financial literacy, Governor Fullani also met with students and professors of Asim Zeneli High School in Gjirokastra. During this meeting, the Governor highlighted the important role the Bank of Albania plays in the country's economy and welfare of its citizens. The attendees were also informed of the novelties of the educational programme "Central Bank in Daily Life" for the academic year 2010-2011.

In view of building a constant partnership dialogue between the banking system and the Bank of Albania, on 2 November 2010, the Bank of Albania organized a discussion meeting with representatives and executives of the Albanian banking system and the Albanian Association of Banks.

Bank of Albania holds a Discussion Meeting with the Banking System and the Albanian Association of Banks

Bank of Albania representatives provided an overview of the financial situation at home, current developments and the challenges facing the Albanian economy in the future. The analyses indicate that the Albanian banking sector's financial situation has been positively affected by the marked improvement of the liquidity position due to the recovery of public confidence and stable growth of deposits. Lending to economy continues to record moderate growth rates, mostly due to demand-related concerns.

During this meeting, commercial banks' executives were introduced to the new draft package of measures proposed by the Supervision Department at the Bank of Albania. The new draft package of measures aims at ensuring constant improvement of the infrastructure required to support the economy. The development of the Albanian banking system in terms of the provision of new products and services, mainly internet and telephone banking, was another important topic discussed during this meeting.

On the occasion of the closing of the year, on 23 December 2010, the Governor of the Bank of Albania, Mr. Ardian Fullani, met with distinguished journalists of press and electronic media, political and economic analysts, executives and other representatives of the media in Albania. The Governor appraised the work of journalists for the significant contribution they have made in conveying the Bank of Albania's messages.

Governor of the Bank of Albania, Mr. Ardian Fullani, meets with journalists, analysts and media executives

In the beginning of his speech, Governor Fullani provided an overview of the Albanian economy, emphasizing that 2010 witnessed a lot of economic events and the media was always present to transmit the news to the public. The Governor underlined that the work made by the Bank of Albania enabled safeguarding and strengthening macroeconomic stability at home and the banking system's financial stability.

In addition to its contribution to safeguarding and strengthening the country's macroeconomic stability, the Bank of Albania is involved in a number of other projects that provide added value to the Albanian society. The Bank of Albania's initiative to promote Albania's cultural heritage is one of these projects. Governor Fullani presented the Bank of Albania's calendar for 2011. This year's calendar features bridges in Albania, translated into a virtual concept that links the Bank of Albania with the public.

The Governor also announced the three winners of the open competition "Governor's Award for the Best Diploma Thesis" for 2010. The first prize went to Ms. Lorena Skufi, the second to Ms. Fabiola Hysenbelliu, and the third to Ms. Evis Koplaku.

This competition is dedicated to Albanian students graduated during the academic year in Albania or abroad. The diploma thesis should represent a scientific research on topics related to monetary economics, financial stability, economic integration of the Balkans into Europe, Bank of Albania's activity, the Albanian banking system and the economy at large.

Friday Seminar The Research Department at the Bank of Albania organizes a fortnightly "Friday Seminar". This initiative invites Bank of Albania experts, researchers from academic and other financial, research and scientific institutions to present and discuss their theoretical and empirical research papers on the Albanian case and the application of the latest research methods.

During the period July-December 2010, the Friday Seminar Series welcomed several works from the Bank of Albania representatives, and other institutions. The main topics brought up in these seminars relate to issues of financial and monetary stability, fiscal policy, and the competitiveness of the Albanian economy in terms of labour productivity and cost.

The first paper presented during the second half of 2010 was "Stress-Testing on Indirect Credit Risk in Albania, based on Banks' Characteristics" by Kliti Ceca, Research Department, and Hilda Shijaku, Financial Stability Department. This study aims to analyze the response of the non-performing loans ratio to potential macroeconomic risks, such as: exchange rate, interest rates and economic growth. The estimation is enabled through the assessment of panel data, including data of 10 banks operating in Albania, during 2005Q1-2009Q4.

“Corporate Governance in Banks: Why is it Important and Peculiar? What does it mean?” by Sonila Biçaku, representative of IFC (International Finance Cooperation-Europe and Central Asia). Some of the issues in this study concerned the corporate governance in general, the reason of paying attention to governance in banks, and the peculiarities and problems that emerge while governing banks.

“Stabilization and Association Agreement with EU, Trade Integration and its Economic Implications” by Alban Pllaha, Research Department. The main issues of this study relate to the stabilization and association process and the regional integration in general. This study provides a viewpoint on the Albanian economy during the transition period and estimates the actual and potential level of Albania’s trade and its trading partners, based on the empirical assessments of the Gravity Model for Albania. A main conclusion of this paper is that European integration promotes further economic growth. Another conclusion shows that trade between the regional countries and Albania will enhance by further integration of our country towards the EU and the regional countries.

“Macroeconomic Effects of Fiscal Policy in Albania: The SVAR Approach” by Armela Mançellari, Research Department. The main purpose of this study is to assess the effect of fiscal policy on Gross Domestic Product, prices and interest rates in Albania through the Structural Vector Autoregressive model, for the period 1998Q2-2009Q4. The empirical findings show that fiscal policy in Albania has a considerable effect on the economy, while the analysis of fiscal multipliers confirmed that the tax cut policy is the most stimulating policy in economy.

“Key Macroeconomic Factors Defining Credit Risk: The Case of Albania” by Irimi Kalluci and Oriela Kodra, Research Department. The main purpose of this study is to identify the key determinants defining the non-performing loans ratio, disbursed to both businesses and households. The methodology employed is Ordinary Least Square, estimated over the period 2002Q2-2009Q4. Some of this study findings show that the non-performing loans ratio is influenced by the T-bills interest rates, REER, exports, M3 monetary aggregate, and the consumer price index.

“The Competitive Position of the Albanian Economy in terms of Productivity and Labour Cost” by Evelina Çeliku and Iris Metani, Monetary Policy Department. This study aims to measure, recognize and analyze the labour productivity and the unit labour cost while taking into consideration the importance and implications of these indicators to monetary policy. Based on the comparative analysis of the relative indicators of labour productivity and unit cost, we conclude that the fragility and the lack of competitive advantages of the Albanian economy arise from the high differences in labour productivity.

MONETARY POLICY DECISIONS

28 January 2009

The Supervisory Council of the Bank of Albania decides to decrease the key interest rate by 0.50 percentage points, to 5.75%.

25 February, 25 March, 29 April, 17 May, 24 June, 29 July, 26 August and 30 September 2009

The Supervisory Council of the Bank of Albania decides to keep the key interest rate unchanged at 5.75%.

28 October 2009

The Supervisory Council of the Bank of Albania decides to decrease the key interest rate by 0.50 percentage points, to 5.25%.

25 November and 23 December 2009

The Supervisory Council of the Bank of Albania decides to keep the key interest rate unchanged at 5.25%.

27 January, 24 February, 24 March, 28 April, 26 May, 30 June 2010

The Supervisory Council of the Bank of Albania decides to keep the key interest rate unchanged at 5.25%.

28 July 2010

The Supervisory Council of the Bank of Albania decides to decrease the key interest rate by 0.25 percentage points, to 5.00%.

31 August, 29 September, 26 October, 24 November, 22 December 2010

The Supervisory Council of the Bank of Albania decides to keep the key interest rate unchanged at 5.00%.

LEGAL EVENTS, 2010 H2

MONETARY POLICY

On 28 July 2010, the Supervisory Council of the Bank of Albania adopted by Decision No. 50 "The Monetary Policy Statement for the first half of 2010". According to this Statement, the Albanian economy performed positively throughout the first half of 2010, particularly when put in the context of the global economic developments and performance of the regional economies, as well as in relation with the dimensions of the challenges it encountered. Throughout the stated period of time, our monetary policy has been stimulating, maintaining low interest rates and injecting the necessary liquidity at appropriate maturity terms in order to support financial market activity and lending to the economy.

On 28 July 2010, the Supervisory Council of the Bank of Albania adopted the Decision No. 51 "On cutting the interest rate on repo and reverse repos by 0.25 pp". The absence of inflationary pressures in the medium run and the contained fiscal policy provided room for pursuing a stimulating monetary policy to support the economic activity. Hence, the Supervisory Council of the Bank of Albania cut the key interest rate by 0.25 pp to 5.00%.

On 26 October 2010, the Supervisory Council of the Bank of Albania adopted by Decision No. 75 "The Monetary Policy Report for the third quarter of 2010". According to this Report, the Albanian economic performance over the third quarter was characterised by the gradual improvement of aggregate demand, lower risk premium and consolidation of macroeconomic stability. In line with Bank of Albania projections, economic growth has strengthened and its base seems to have broadened; and consumer price inflation and its expectations have been anchored close to the Bank of Albania's inflation target. The external position of the Albanian economy has improved and the exchange rate appears more stable, while liquidity in the system has increased and interest rates have generally been downward. Against this setting, the Bank of Albania considers that monetary conditions in economy are adequate to ensure the maintenance of price stability over the medium run and at the same time, to support the further development of the domestic economy.

BANKING SUPERVISION

On 14 July 2010, the Supervisory Council of the Bank of Albania adopted by Decision No. 48 the Regulation "On managing open foreign position risk". This Regulation sets out the rules and criteria for the calculation, reporting and

supervision of banks' open foreign positions, in order to manage the foreign exchange risk. This Regulation shall be applied on banks, being granted a licence from the Bank of Albania to conduct banking and financial activity in the Republic of Albania. This regulation sets out, among other things, the way of determining the open foreign positions, thresholds and the risk management arising from these positions.

On 14 July 2010, the Supervisory Council of the Bank of Albania adopted the Decision No. 49 "On granting Raiffeisen Bank sh.a. preliminary approval to conduct additional activity". According to this Decision, Raiffeisen Bank is granted prior approval to conduct additional trading and financial activities, on its own account or for the account of its clients, be it in a foreign exchange, over-the-counter, other negotiable instruments and financial assets, and participation in the issuance of all types of securities. This bank may also carry out advisory and intermediation services and other auxiliary services for all activities included in the licence granted by the Bank of Albania.

On 31 August 2010, the Supervisory Council of the Bank of Albania adopted the Decision No. 56 "On granting Credins Bank sh.a. preliminary approval to conduct additional activity". According to this Decision, Credins Bank is granted the approval to carry out additional trading and financial activity, on its own account and for the account of its clients, be it in a foreign exchange, over-the-counter or gold operations.

On 29 September 2010, the Supervisory Council of the Bank of Albania adopted the Decision No. 65 "On some amendments to the Regulation "On the supervision of Savings and Loan Associations and their Unions"". The amendments affect Article 8 regulating the liquidity and it sets forth the terms and conditions that all savings and loan associations should meet when granting a loan.

On 13 October 2010, the Supervisory Council of the Bank of Albania adopted by Decision No. 67 the Regulation "On information content and functioning of Credit Registry at the Bank of Albania". This Regulation sets out the information content, principles and rules for the functioning of the Credit Registry at the Bank of Albania, and the terms and conditions to access and use the information held at this Registry. Credit Registry management aims at ensuring centralised handling and disclosure of information held at the Credit Registry, in view of carrying out the supervisory process and ensuring optimal credit risk management by the entities the Bank of Albania supervises. This Regulation sets out the contents and the way data in the Credit Registry are processed, and the way it operates.

On 13 October 2010, the Supervisory Council of the Bank of Albania adopted by Decision No. 68 the Guideline "On the issue of the Borrower's Report and the review of information held at the Credit Registry". This Guideline sets out the procedure for the issue of the Borrower's Report and the review of information held at the Credit Registry. It stipulates that the Borrower's Report is issued upon the request of the latter or other entities known as requestors

according to this guideline, the required accompanying documents as well as all the stages of this process and the data review.

On 13 October 2010, the Supervisory Council of the Bank of Albania adopted by Decision No. 69 "Fees charged for the use of information held at the Credit Registry of the Bank of Albania". This Decision sets out the fees charged for the successful query from banks, fees charged for the successful query from non-bank financial institutions and savings and loan associations' unions, as well as the fees charged for query from the registration entity.

On 13 October 2010, the Supervisory Council of the Bank of Albania adopted by Decision No. 71 "Banking Supervision Mission Document". According to this Document, the Bank of Albania's supervision mission is to ensure sound banking activities, by formulating and implementing policies and an adequate regulatory framework in order to influence on safeguarding the banking system's stability and broader; promote market discipline and develop fair competition among the supervised entities. The Bank of Albania fulfils its supervisory function by continuously developing and improving the regulatory framework, and by continuously conducting an effective and proactive supervisory process.

On 13 October 2010, the Supervisory Council of the Bank of Albania adopted the Decision No. 72 "On granting National Commercial Bank, sh.a. preliminary approval to conduct additional activities". According to this Decision, the National Commercial Bank may carry out a range of activities such as: factoring and the financing of trading transactions, trading on its own account or for the account of its clients, in an over-the-counter market of transferable securities, other negotiable instruments and financial assets, intermediation for a number of monetary transactions, etc.

On 22 December 2010, the Supervisory Council of the Bank of Albania adopted the Decision No. 88 "On some amendments to the Regulation "On managing risk arising from banks' large exposures"". The amendments affect articles that regulate the types of collateral, the maximum allowed limits of large exposure, the observation of these limits and the monitoring and supervisory requirements.

On 22 December 2010, the Supervisory Council of the Bank of Albania adopted the Decision No. 89 "On some amendments to the Regulation "On Capital Adequacy Ratio"". The amendments relate to Article 12 of this Regulation, where it is stipulated that the list of OECD member countries is the latest list published from this organisation on its official website.

On 22 December 2010, the Supervisory Council of the Bank of Albania adopted the Decision No. 90 "On an amendment to the Regulation "On risk management in the activity of non-bank financial institutions"". This amendment affects Article 23 of this Regulation, where it is stipulated that the list of OECD member countries is the latest list published from this organisation on its official website.

FINANCIAL STABILITY

On 13 October 2010, the Supervisory Council of the Bank of Albania adopted by Decision No. 74 "The Financial Stability Report – 2010 H1". According to this Report, the financial system and banking sector's financial situation has been stable, while capitalization level and operational liquidity positions are good. The main positive factors include the reduction of budget and trade deficit, exchange rate stability, moderate inflationary pressures and lower interest rates. The interbank market liquidity was sufficient to meet commercial banks' short-term liquidity needs and the financial market has operated smoothly. However, the Report highlights that banks should make ongoing and careful monitoring of the credit quality performance and they should timely establish reserve funds.

ISSUE

On 31 August 2010, the Supervisory Council of the Bank of Albania adopted the Decision No. 62 "On the withdrawal from circulation of legal tender banknotes". According to this Decision, it is approved the withdrawal of 1000 lekë denomination banknote, issue of 1992, 1994, 1995, 1996, having on the front side the portrait of Skanderbeg. These banknotes shall be legal tender till 31 March 2011. They may be collected and exchanged, versus the initial issue payment, with other legal tender banknotes and coins in circulation. Collection term expires on 31 December 2013.

On 13 December 2010, the Supervisory Council of the Bank of Albania adopted the Decision No. 84 "On re-minting the legal tender Albanian metallic coin of 5 lekë denomination". According to this Decision, it is approved the re-minting of 5 lekë denomination Albanian metallic coin, legal tender, originally minted in 1995 and re-minted in 2000. The issue year, 2011, shall be printed on the body of the coin.

ECONOMIC POLICY

On 15 July 2010, the Parliament of the Republic of Albania adopted the Law No. 10303 "On the establishment and way of organisation and functioning of the Albanian Investment Development Agency". According to this Law, the Albanian Development Investment Agency shall support and facilitate the direct investments in Albania through the identification and promotion of investment opportunities, by providing services and support to both existing and potential investors. This Agency shall commit to enhancing the competitive capacities of small and medium-sized enterprises and promoting the exports of goods and services.

On 15 July 2010, the Parliament of the Republic of Albania adopted the Law No. 10304 "On the mining sector in the Republic of Albania". This Law sets out the rules for the development of mining and post-mining activities

in the Republic of Albania, through the assurance of transparency and free competition in this activity, with the purpose of ensuring maximum public benefit from mining activity and protecting public health and environment from the mining risk and the mining industry residues.

On 23 July 2010, the Council of Ministers approved the Decision No. 591 "On disciplining budget funds use". This Decision sets out the measures taken to discipline the expenditures for 2010, such as: the non-allocation of the special fund planned for remunerations and social and cultural activities, the freezing of funds approved for trainings of government unit employees abroad for 2010, the freezing of budget funds that are subject to public procurement procedures and which result non-procured, etc.

On 28 July 2010, the Council of Ministers approved the Decision No. 588 "On the approval of the revised macroeconomic framework of macroeconomic and fiscal indicators, and the final ceilings of medium-term budget program, 2011-2013". This framework forecasts real GDP to grow by 4.1% in 2010, and 6.2% in 2013.

On 28 July 2010, the Council of Ministers approved the Decision No. 648 "On Taxpayer Lawyer". This Decision regulates the structure, authority and functions of Taxpayer Lawyer, and his relationships with other structures. According to this Decision, the main function of the Taxpayer Lawyer is to guarantee the protection and assurance of the taxpayers' rights, and the delivery of information on their rights and education. The Taxpayer Lawyer is appointed by the Minister of Finance upon the proposal of the General Director of Taxation and is directly accountable to the latter.

On 28 July 2010, the Council of Ministers approved the Decision No. 636 "On the approval of the Medium-Term Budget Plan". The Medium-Term Budget Plan is an operational instrument for the management of public expenditure and a key component of the Integrated Planning System. Its main purpose is to encourage the effectiveness, efficiency and the economy in carrying out public expenditure, the broadening of budget process vision by ensuring that expenditure plans are planned in a medium-term period (3-year).

On 18 August 2010, the Council of Ministers approved the Decision No. 697 "On establishing the base unemployment income". According to this Decision, the base unemployment income shall amount to ALL 6,565 (six thousand, five hundred and sixty-five) monthly. The financial effects arising from the implementation of this Decision shall be covered by the 2010 budget fund approved for the Ministry of Labour, Social Affairs and Equal Opportunities.

On 25 August 2010, the Council of Ministers approved the Decision No. 702 "On the approval, in principle, of the Agreement between the Republic of Albania and the United Arab Emirates, on the economic, trade and technical cooperation". This Agreement manifests the good will of both signatory parties

to strengthen their relationship, mainly in the economic and trade areas, also including industry, agriculture and transport. The parties shall encourage the respective specialised institutions and the authorised natural persons to consider the possibilities for the implementation of projects in the cooperation areas, including the financial resources of these projects.

On 25 August 2010, the Council of Ministers approved the Decision No. 713 "On establishing the rules for the terms and conditions of procedures for granting permits for the construction and use of natural gas systems' infrastructure and pipes". This Decision sets out the rules, procedures and criteria for the application, assessment and granting of permits for the construction and use of pipes and the respective infrastructure, for the transmission and distribution of natural gas. This Decision also regulates the connection of the Albanian natural gas system to the neighbouring countries, the installations of liquefied natural gas (LNG), underground natural gas storage, and direct lines.

On 25 August 2010, the Council of Ministers approved the Decision No. 717 "On the approval, in principle, of the Agreement "On the establishment of the International Anti-Corruption Academy, as an International Organisation"". The purpose of this Academy is to promote the prevention and effective fight against corruption, by ensuring anti-corruption education, facilitation of research and technical assistance, and by encouraging the international cooperation in this area.

On 1 September 2010, the Council of Ministers approved the Decision No. 760 "On the approval of intellectual and industrial property national strategy, 2010-2015". The period covered from this strategy is conditioned by the current situation in the area of intellectual property, which imposes rapid, but complex, measures, in order to effectively reform the system almost entirely, excluding the main parts of the legal framework considered as almost consistent with EU Acquis. The strategy is based on the Czech experience, and grounded on a long-term and deep study in the area of intellectual property in other European countries, in agreement with the Albanian partners.

On 7 September 2010, the Parliament of the Republic of Albania adopted the Law No. 10311 "On the ratification of the financial contract between the Republic of Albania and the European Investment Bank (EIB) for the financing of secondary and local roads project". According to this Agreement, the lender grants a loan of EUR 50,000,000 (fifty million) for carrying out the secondary roads project, which is part of an ongoing programme for the rehabilitation of secondary and local roads. This project will cover about 500 km of secondary and local roads.

On 7 September 2010, the Minister of Finance adopted the Guideline No. 30 "On the implementation of the Law No. 10270, dated 22 April 2010 "On the right of privatisation of state-owned land in use and tax on the right to use it"". This Guideline sets out the rules and procedures to be followed for paying the tax on the right to use state-owned land. The tax shall be paid

by individuals who use non-privatized land of buildings privatized by citizens, non-privatized land of buildings sold by state-owned enterprises, on which buildings have been constructed, based on construction permits issued from the councils' pluralism committees.

On 8 September 2010, the Council of Ministers adopted the Decision No. 796 "On some amendments to the Decision No. 787, dated 14 December 2005 of the Council of Ministers "On setting out the criteria, procedures and level of economic assistance"". The amendments set out the procedures and terms to be included in the economic assistance schemes of trafficking victims after they have terminated their stay at social care institutions and until their employment. The level of economic assistance shall amount to ALL 3,000 (three thousand) monthly.

On 16 September 2010, the Parliament of the Republic of Albania adopted the Law No. 10313 "On the ratification of ISTISNA'A Agreement and ISTISNA'A Agency Agreement between the Council of Ministers of the Republic of Albania and the Islamic Development Bank for the project "The reconstruction of secondary and local roads"". According to this Agreement, the Islamic Development Bank has agreed to carry out the works for the reconstruction of about 173 km secondary and local roads for a total amount that does not exceed USD 30,000,000 (thirty million) to be paid by the Council of Ministers within 11 (eleven) years after the maturity period of 4 (four) years.

On 16 September 2010, the Parliament of the Republic of Albania adopted the Law No. 10316 "On some amendments to the Law No. 7764, dated 2 November 1993, "On foreign investments"". These amendments set out the terms and procedures to be followed for the special state protection of foreign investments, their contents, deadlines for reviewing the application for special protection and coverage of expenses.

On 16 September 2010, the Parliament of the Republic of Albania adopted the Law No. 10317 "On some amendments to the Law No. 9121, dated 28 July 2003, "On the protection of competition", as amended". The amendments affect a number of articles in this Law that regulate the agreements between two or more enterprises and the dominant economic forces in the market. Further stipulations are made with regard to the concentration of enterprises and their control, abuses with the dominant position, preliminary and deep investigations in economy, etc.

On 16 September 2010, the Parliament of the Republic of Albania adopted the Law No. 10318 "On some amendments to the Law No. 9720, dated 23 April 2007, "On public sector internal audit"". This Law, among other things, changes the designation of the General Directorate of Audit to "Central Harmonisation Unit of Internal Audit" and the purpose of audit. As stipulated in this Law, the purpose shall be the conduct of internal audit of all structures, programmes, activities and processes, and the lowest level expense units within the public units, including the units spending European Union resources.

On 23 September 2010, the Parliament of the Republic of Albania adopted the Law No. 10320 "On the ratification of "The Loan Agreement between the Council Ministers of the Republic of Albania and the Islamic Development Bank (IDB) for the participation in the financing of the reconstruction project of the secondary and local roads"". The Islamic Development Bank, through this Agreement, grants the Council of Ministers an amount that does not exceed USD 10,000,000 (ten million) to be settled within a 25-year period. This loan shall be used to carry out the project that aims at improving the living conditions and reducing the poverty of people living in remote areas, by connecting the rural population centres and providing them access to basic services.

On 24 September 2010, the Council of Ministers adopted the Decision No. 775 "On foreign financing management in the Republic of Albania". This Decision aims to ensure and manage foreign financing, as an integrated and reported part in the Republic of Albania's budget system. According to this Decision, foreign financing shall include all loans, credits and grants provided to the Council of Ministers of the Republic of Albania, from other foreign governments, international organisations, international financial institutions, foreign banks and non-governmental organisations.

On 28 September 2010, the Council of Ministers adopted the Decision No. 764 "On the approval, in principle, of a Grant Agreement between the Council of Ministers of the Republic of Albania and the Government of the United States of America "On the fair and democratic governance and on investment in human resources and economic growth"". The purpose of this Grant Agreement is to establish understanding between the mentioned parties with regard to the accomplishment of functional objectives, in order to develop fair and democratic governance and to support the transformation of Albania into a stable, social and economic democracy. The objectives shall be accomplished through the implementation of activities that will be financed by the contribution of USD 75,000,000 (seventy-five million), under four programme areas: health, rule of law, good governance, and private sector growth, etc.

On 14 October 2010, the Parliament of the Republic of Albania adopted the Law No. 10335 "On the ratification of "The Financial Agreement between the Council of Ministers of the Republic of Albania and the Commission of the European Communities "On the financing program of Albania's participation in the ERDF trans-national programmes of the European territorial cooperation objective "South-eastern Europe and the Mediterranean" of Instrument for Pre-Accession Assistance (IPA), the cross-border cooperation component for 2009"". The purpose of the financial program, based on this Agreement, is to support the participation of partners from candidate or potential candidate countries in joint trans-national cooperation activities from EU member countries, and to familiarize them with territorial cooperation programmes under the EU structural funds.

On 21 October 2010, the Council of Ministers adopted the Decision No. 852 "On the organisation and functioning of the Bankruptcy Supervision

Agency". According to this Decision, the Bankruptcy Supervision Agency shall be a legal public person, accountable to the Minister of Justice. It shall be the responsible public authority to supervise the activity of bankruptcy administrators and to control the implementation of the bankruptcy law. The Agency shall be financed by the State Budget and the income arising from tariffs realized from its activity, etc.

On 21 October 2010, the Parliament of the Republic of Albania adopted the Law No. 10338 "On the ratification of "The Agreement between the Republic of Albania and the Kingdom of Spain for the avoidance of double taxation and the prevention of fiscal evasion with respect to taxes on income"". This Agreement shall apply on individuals, resident of one or both contracting states. It shall apply on income tax, placed on behalf of a contracting state, its political subdivisions or local authorities, notwithstanding the way they are collected. Income tax shall include all taxes applied on proceeds as a whole, or proceeds elements, including tax profit from the alienation of real estate or unfixed real estate, tax on salaries or wages paid from enterprises, and capital tax, etc.

On 27 October 2010, the Minister of Economy, Trade and Energy adopted the Guideline No. 721 "On the criteria for the organisation and management of consumer advisory centres". The purpose of this Guideline is to set out the criteria for the organisation and management of consumer advisory centres from consumer associations. Consumer advisory centres should be competent in providing advice on issues related to consumers, such as: the protection of consumers' economic interests with regard to the information about commodities and services, labelling, price index, guarantees, unfair trading practices, unfair contract terms and conditions, misleading publicity, financial services and consumer loans, etc.

On 28 October 2010, the Parliament of the Republic of Albania adopted the Law No. 10342 "On the approval of the actual state budget of 2009". According to this Law, the state budget revenue for 2009 amounted to ALL 249,169 million, whereas expenditure amounted to ALL 319,903 million. Budget deficit was estimated at ALL 808,83 million.

On 28 October 2010, the Parliament of the Republic of Albania adopted the Law No. 10343 "On some amendments to the Law No. 8438, dated 28 December 1998, "On income tax"". These amendments mainly concern the adjustment of data on gross income, the annual tax statement and other additional documents.

On 4 November 2010, the Parliament of the Republic of Albania adopted the Law No. 10346 "On some amendments to the Law No. 9874, dated 14 February 2008, "On public auction"". These amendments consist in the re-organisation of Public Procurement Agency and Public Procurement Commission duties. According to these amendments, the Agency shall supervise the implementation of auction sale procedures, while the Commission shall be responsible for the administrative review of bidders' complaints against the auction procedures or disqualification decisions.

On 5 November 2010, the Minister of Finance adopted the Guideline No. 37 "On the functions, responsibilities and procedures to be implemented by the Taxpayer Lawyer and the procedures to be implemented by the taxpayers". This Guideline shall provide, in a clear and detailed way, the role, responsibilities, competences and administrative procedures to be implemented by the Directorate of Taxpayer Lawyer. The mission of the Taxpayer Lawyer is to protect the taxpayers' rights by analysing any qualified claim submitted either by the taxpayer or his representative. This mission shall be mainly carried out through his right to order the conduct of verifications or investigations from the tax regional directorates and/or the functional departments of the General Tax Directorate, as well as through the advisory competences to the authorities competent to resolve the taxpayers' problems.

On 18 November 2010, the Parliament of the Republic of Albania adopted the Law No. 10354 "On some amendments to the Law No. 9632, dated 30 October 2006, "On local tax system"". The amendments mainly relate to the obligation of businesses to install fiscal equipment and the terms to benefit the compensation of fiscal printer up to ALL 44,000 (forty-four thousand). In the meantime, businesses operating in the transport area, and which have the obligation to be equipped with taxi meters, may benefit the reimbursement of the payment made for its purchase, up to ALL 30,000 (thirty thousand).

On 1 December 2010, the Council of Ministers approved the Decision No. 971 "On granting the fund to face the emergency situation in the district of Shkodra, due to the natural floods". Accordingly, the fund amounting to ALL 300,000,000 (three hundred million) was established, to be used by the Ministry of Interior, in the "Civil Emergencies" budget program, to face the emergency situation caused by the natural floods. This Decision also established that, under emergency situations, the local authorities of Shkodra district will be assigned by the Inter-Ministerial Committee for Civil Emergency to use this fund.

On 2 December 2010, the Parliament of the Republic of Albania adopted the Law No. 10355 "On the budget for 2011". According to this Law, budget revenue for 2011 are projected to amount to ALL 362,223 million, expenditure to ALL 409,035 million, and the budget deficit to ALL 46,812 million.

On 9 December 2010, the Council of Ministers adopted the Decision No. 989 "On the establishment and use of civil emergency fund in the district of Shkodra to face the situation caused by the natural floods". According to this Decision, the financial fund for civil emergencies in the district of Shkodra shall include the amount of ALL 300,000,000 (three hundred million) granted by the Albanian Electro-Energetic Corporation (KESH), the monetary donations collected from the banks' accounts opened for this purpose; and the material donations. These funds shall be only used upon the decision of the Inter-Ministerial Committee for Civil Emergency, and the payments shall be authorized by the Prefect of Shkodra district.

BANK OF ALBANIA MANAGEMENT, 31 DECEMBER 2010

SUPERVISORY COUNCIL

ARDIAN FULLANI	Chairman
FATOS IBRAHIMI	Vice Chairman
TEFTA ÇUÇI	Member
LIMOS MALAJ	Member
KSENOFON KRISAFI	Member
ADRIAN CIVICI	Member
ARJAN KADAREJA	Member
HALIT XHAFA	Member
BENET BECI	Member

GOVERNOR

ARDIAN FULLANI

DEPUTY GOVERNORS

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

GENERAL INSPECTOR

TEUTA BALETA

GOVERNOR'S OFFICE

GENC MAMANI

HEAD OF COORDINATION

GRAMOS KOLASI

DEPARTMENTS AND OTHER UNITS

HUMAN RESOURCES DEPARTMENT	Roden Pajaj
MONETARY POLICY DEPARTMENT	Erald Themeli
RESEARCH DEPARTMENT	Altin Tanku
MONETARY OPERATIONS DEPARTMENT	Marjan Gjermeni
SUPERVISION DEPARTMENT	Indrit Banka
FINANCIAL STABILITY DEPARTMENT	Klodion Shehu
INFORMATION TECHNOLOGY DEPARTMENT	Xhilda Kanini
STATISTICS DEPARTMENT	Diana Shtylla
ISSUE DEPARTMENT	Valer Miho
ACCOUNTING AND FINANCE DEPARTMENT	Vacant
PAYMENT SYSTEMS DEPARTMENT	Dashmir Halilaj
LEGAL DEPARTMENT	Toni Gogu
AUDIT DEPARTMENT	Teuta Baleta
FOREIGN RELATIONS, EUROPEAN INTEGRATION AND COMMUNICATION DEPARTMENT	Oneda Andoni
ADMINISTRATION DEPARTMENT	Agron Skënderaga
SECURITY AND PROTECTION DEPARTMENT	Eduard Sinani

BRANCHES

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

LIST OF ENTITIES LICENSED BY THE BANK OF ALBANIA, 31 DECEMBER 2010

BANKS AND BRANCHES OF FOREIGN BANKS

1. 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: Christian CANACARIS

Address: Bulevardi "Bajram Curri", European Trade Center, Tirana, Albania

Tel.: +355 4 2274 910

Fax: +355 4 2275 599

E – mail: info@raiffeisen.al

Website: www.raiffeisen.al

2. 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: Hikmet GÜLER

Address: Rruga "Durrësit", sheshi "Rilindja" (Zogu i Zi), Godina Teknoprojekt, P.O. BOX 128, Tirana, Albania

Tel.: +355 4 2228 460 / 2223 873 / 2227 408

Fax: +355 4 2228 460 / 2228 387

E-mail: info@ubaal.com

Website: -

3. ITALIAN BANK OF DEVELOPMENT (BANCA ITALIANA DI SVILUPPO)

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.: +355 4 2280 555

Fax: +355 4 2280 356

E – mail: info@bisbanca.com

Website: www.bisbanca.com

4. 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.: +355 4 2250 955

Fax: +355 4 2250 956

E – mail: info@bkt.com.al

Website: www.bkt.com.al

5. 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 SANTIXIS

Address: Rruga "Dëshmorët e 4 Shkurtit", PO BOX 2400/1, Tirana, Albania

Tel.: +355 4 2269 616 / 7 / 8, +355 4 2233 441 / 42 / 43 / 44 / 45 / 46 / 47

Fax: +355 4 2233 417 / 2369 707

E – mail: info@tiranabank.al

Website: www.tiranabank.al

6. 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: Ioannis KOUGIONAS

Address: Rruga "Durrësit", Godina Comfort, Tirana, Albania

Tel.: +355 4 2274 802 / 2274 822

Fax: +355 4 2233 613

E – mail: nbgalbania@icc-al.org

Website: -

7. 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.: +355 4 2254 372 / 2256 254

Fax: +355 4 2254 368

E – mail: info@icbank-albania.com

Website: -

8. 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: Rruga e Kavajës, G – KAM Business Center, Kati II, Tirana, Albania

Tel.: +355 4 2278 500

Fax: +355 4 2232 102

E – mail: tiranabranh@alpha.gr

Website: -

9. INTESA SANPAOLO BANK 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: Stefano FARABBI

Address: Rruga "Ismail Qemali", Nr. 27, P.O. Box 8319, Tirana, Albania

Tel.: +355 4 2248 753 / 4 / 5 / 6, +355 4 2276 000

Fax: +355 4 2248 762

E – mail: helpdesk@intesasanpaolobank.al

Website: www.intesasanpaolobank.al

10. 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: Flutura VEIPI

Address: Rruga "Durrësit", Laprakë, Tirana, Albania

Tel.: +355 4 2389 300

Fax: +355 4 2233 918

E mail: info@procreditbank.com.al

Website: www.procreditbank.com.al

11. 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", Nr. 59, "Tirana Tower", Tirana, Albania

Tel.: +355 4 2258 755 / 56 / 57 / 58 / 59 / 60

Fax: +355 4 2258 752

E – mail: headoffice@emporiki.com.al

Website: www.emporiki.com.al

12. 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: Sherine KAMEL

Address: Rruga "Perlat Rexhepi", Al-Kharafi Group Administration Building, Kati 1&2" Tirana, Albania

Tel.: +355 4 2272 168, +355 4 2272 162

Fax: +355 4 2272 162

E-mail: creditbkalb@icc-al.org

Website: -

13. 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.: +355 4 2234 096

Fax: +355 4 2222 916

E –mail: info@bankacredins.com

Website: www.bankacredins.com

14. BANKA SOCIETE GENERALE ALBANIA SH.A

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: Hubert de SAINT JEAN

Address: Bulevardi "Dëshmorët e Kombit", Ndërtesa Kullat Binjake, Kulla 1, Kati 9, Tirana, Albania

Tel.: +355 4 2280 442 / 3

Fax: +355 4 2280 441

Mobile: 068 (69) 20 60 974

E-mail: bp.info@socgen.com

Website: www.bpopullore.com

15. 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, Albania

Tel.: +355 4 2250 653 / 2258 081

Fax: +355 4 2272 880

E – mail: info@unionbank.com.al

Website: www.unionbank.com.al

16. FIRST INVESTMENT BANK (JOINT-STOCK COMPANY)

Licence No. 13, dated 16.04.1999

Approved by the Supervisory Council Decision of the Bank of Albania No. 35, dated 27.06.2007.

Certificate No. 12 "On Deposit Insurance", dated 18.07.2007.

Director: Bozhidar TODOROV

Address: Bulevardi "Dëshmorët e Kombit", Kullat Binjake, Kulla 2, Kati 14,
Tirana, Albania

Tel.: +355 4 2276 702 / 3

Fax: +355 4 2280 210

E – mail: -

Website: www.fibank.al

In addition to banks and branches of foreign banks, the Bank of Albania has as of 31 December 2010 licensed the following entities:

NO.	ENTITIES
17	NON-BANK INSTITUTIONS
284	FOREIGN EXCHANGE BUREAUS
2	UNIONS OF SAVINGS AND CREDIT ASSOCIATIONS
126	SAVINGS AND CREDIT ASSOCIATIONS
1	REPRESENTATIVE OFFICE OF FOREIGN BANKS

PUBLICATIONS ISSUED BY THE BANK OF ALBANIA OVER 2010

This list was designed to inform readers about publications issued by the Bank of Albania over the first half of 2010. By visiting our website (www.bankofalbania.org) you can subscribe to our mailing list by submitting a written request either by e-mail at public@bankofalbania.org or sending a fax to + 355 4 2419408. You can also subscribe to updates by signing up to receive free e-mail notices when new series items are posted on the Bank of Albania website. You will receive e-mail notices each time we post new items of the series you selected. Listed below you can find all the publications issued by the Bank of Albania over 2010. This list does not include periodical surveys carried out by the Bank of Albania as they are available only online (http://www.bankofalbania.org/web/survey_3405_2.php).

ANNUAL REPORT:

Annual Report 2009

FINANCIAL STABILITY REPORT:

Financial Stability Report 2009
Financial Stability Report 2010 H1

SUPERVISION ANNUAL REPORT:

Supervision Annual Report 2009

MONETARY POLICY PERIODICAL REPORTS:

Monetary Policy Report for the First Quarter of 2010
Monetary Policy Report for the Second Quarter of 2010
Monetary Policy Report for the Third Quarter of 2010
Monetary Policy Document for the 2009 - 2011 Period, revised in June 2010

PUBLICATIONS ON STATISTICS:

Statistical Report (Published monthly)
Balance of Payments Bulletin 2009

OFFICIAL BULLETIN:

Index of the Official Bulletin of the Bank of Albania (2009)
Official Bulletin - Volume 12, no.1 Year 2010
Official Bulletin - Volume 12, no.2 Year 2010
Official Bulletin - Volume 12, no.3 Year 2010
Official Bulletin - Volume 12, no.4 Year 2010

Official Bulletin - Volume 12, no.5 Year 2010
Official Bulletin - Volume 12, no.6 Year 2010
Official Bulletin - Volume 12, no.7 Year 2010
Official Bulletin - Volume 12, no.8 Year 2010
Official Bulletin - Volume 12, no.9 Year 2010
Official Bulletin - Volume 12, no.10 Year 2010

ECONOMIC BULLETIN:

Economic Bulletin - Volume 12, no.4 Year 2009

BANK OF ALBANIA BULLETIN:

Bank of Albania Bulletin 2010 H1

DOCUMENT:

Medium-Term Development Plan of the Bank of Albania for 2009 – 2011

PAPERS:

Monetary Policy Strategies for Small Economies - Editor, Ardian Fullani
Alternative Methods of Estimating Potential Output in Albania
Determinants of Net Interest Margin in the Albanian Banking System - Irini Kalluci
Modelling the Quarterly GDP - Role of Economic and Surveys Indicators - Evelina Çeliku, Ermelinda Kristo, Merita Boka
Monetary Transmission Mechanism in Albania - Gramoz Kolasi, Hilda Shijaku, Diana Shtylla
Measuring Inflation Expectations - Gent Hashorva, Elona Bollano, Elvana Troqe
Financial Development and Economic Growth: The Albanian Case - Elona Dushku
Monetary Policy: Institutional and Operational Framework Toward a Forward Looking Regime - Gramoz Kolasi, Bledar Hoda, Sofika Note
Macro Econometric Model of Albania: A Follow Up - Vasilika Kota, Elona Dushku

SCIENTIFIC NOVELTIES AT THE BANK OF ALBANIA:

Scientific Novelties at the Bank of Albania No.3
Scientific Novelties at the Bank of Albania No.4
Scientific Novelties at the Bank of Albania No.5

EDUCATIONAL PUBLICATIONS:

Brochure "Why should we have a personal budget?" (Reprint, available only in Albanian)
Brochure "What is Price Stability for You?" (Reprint, available only in Albanian)
Brochure "The Story of Ice Cream" (Reprint, available only in Albanian)
Brochure "Knowing the Treasury Bills" (available only in Albanian)
Leaflet and poster "Withdrawal from circulation of 500 lekë banknote" (available only in Albanian)

