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EDITORIAL

FUTURE CHALLENGES FOR THE BANK OF ALBANIA

The Bank of Albania has, since April 1992, enjoyed the attributes of a modern central bank. In these 20 years, the central bank has served the Albanian citizens as the institution supporting economic growth sustainability, structural reforms and pace of Albania’s integration into global markets and economy.

The fact that financial integration is one of the key elements of Albania’s general integration into the European Union is now publicly known. In this context, the role of the banking system and, in broader terms, of the financial system, is fundamental and the challenges in this regard are numerous.

In terms of macroeconomic stability, the role of the Bank of Albania remains ensuring the existence of sound financial institutions and promoting financial integration in co-operation with other institutional structures. To this end, the Bank of Albania shall continue to contribute to policies providing for a sound architecture for the Albanian financial stability.

Monetary Policy

In pursuing its primary objective, the maintenance of price stability, the Bank of Albania shall undertake the necessary economic and monetary analyses, and adopt and implement appropriate monetary policies. The Bank of Albania has, since 1999, defined the medium-term inflation target as a numerical value of 3%, with a tolerance band of +/-1.0 percentage point. Monetary policy strategy has been associated with the implementation of a free floating exchange rate regime and the employment of monetary policy instruments to help steer short-term interest rates. A similar monetary policy framework is successful in achieving and maintaining price stability and it has been coupled with further strengthening of macroeconomic balances.

Bank of Albania’s inflation target supports EU integration process, allowing for a reasonable time span for real and nominal convergence of the Albanian economy. To this end, it shall continue to keep the maintenance of price stability, within the above-mentioned tolerance band, as its primary objective in the years ahead.

Monetary policy decision-making process is based on a thorough series of research analyses, surveys and forecasts assessing the monetary situation and economic developments in Albania. The primary objective of research is to assist decision-makers in having an accurate understanding of the
Albanian economic reality in order to formulate and implement monetary policy in compliance with its primary objective. It also contributes to making a self-assessment of the Bank of Albania’s ability to meet its price stability maintenance commitment.

Research

So far, research analyses have focused on studying monetary policy transmission, economic growth, and the fiscal and external sectors. However, the crisis and post-crisis period brought forward the need to re-assess the monetary policy framework and the contributing research analyses. Consequently, Bank of Albania’s compass will continue pointing towards the enhancement of technical capacities in order to improve the analysis and forecasting models further, and ultimately enhance their reliability.

In view of improving research analyses and forecasting models, the Bank of Albania will for the first time use DSGE models\(^1\) for macro modelling the economy, fiscal policy and the financial sector.

Statistics

In order to make research analyses and studies, the central bank needs accurate and reliable data. The Bank of Albania is an important source of statistical information to different institutions and the public at large. It collects information on a number of economic sectors and releases relevant statistics after careful compilation. In the medium run, the Bank of Albania’s priority will be to approximate the legislation, methodology and statistical products to the standards of the relevant EU structures, like the European Commission, European Central Bank and Eurostat.

In pursuing this priority, the Bank of Albania is investing in human and financial resources in order to automate the statistical reporting and processing process. The project for the design and establishment of a long-term technological solution will enable the electronic reporting and control. It will also contribute to the considerable improvement of the statistical product, both for banking supervision needs and in terms of producing Bank of Albania’s official statistics. The project for the automation of the reporting system envisages the revision of the regulatory basis, revision and harmonization of reporting forms, training of reporting institutions, establishment and testing of the application in parallel with the current system.

Payments System

In order for a modern economy to function properly, the economic agents should be able to carry out safe and efficient transactions. Payments, clearing and settlement arrangements are essential for the well-functioning of the financial system and carrying out of transactions between economic agents. In Albania, the central bank is responsible to guarantee the smooth operation\(^1\) DSGE Models - Dynamic Stochastic General Equilibrium Models.
of the payments system as a condition for an effective implementation of its monetary policy. In pursuing this task, the Bank of Albania manages and regulates two interbank payment systems – Albanian Interbank Payments System (AIPS) and Albanian Electronic Clearing House System (AECH) –, which make up the basis for domestic payments and connection to the international payments systems.

Guided by the best international practices, the Bank of Albania is working on approximating the Albanian legislation on payments to the European one. To this end, it will, in the medium run, set up a modern regulatory framework for payment services and electronic money. In the period ahead, the Bank of Albania will also apply, for the first time in the Albanian market, new rules and procedures in order to establish an out-of-court complaint system to resolve disputes between users and providers of these services, thereby strengthening consumer protection.

Communication

The Bank of Albania’s communication strategy is based on three pillars: reliability, transparency and accountability. It is through these three pillars that the central bank communicates with the Albanian citizens and the media effectively. The Bank of Albania will continue to inform the public on the developments affecting the financial markets and will be attentive to public interests and market needs.

Bank of Albania’s communication in the recent years has made significant steps, particularly towards transparency of monetary policy decision-making, which in turn approximates it further to the European Central Bank.

In accomplishing its mandate, the Bank of Albania has, in the last seven years, also engaged in the financial literacy of all economic agents, namely institutional and market entrepreneurs, media and educational system representatives in Albania etc., aiming at enhancing institutional credibility in the framework of well-defined objectives and responsibilities.

Though not a legal requirement, the Bank of Albania engages in financial literacy projects and programmes designed for the public, and particularly for the young-aged one, in order to create a financially-aware environment that understands the Bank of Albania and its decisions rightly and accurately.

In the medium run, the Bank of Albania will aim to extend its financial literacy programmes to pre-university curriculum, beginning from 9-year basic education to high-school level. This Bank of Albania strategy is in line with OECD recommendations, according to which – financial literacy should start at an early age.

In view of enhancing transparency and public literacy, the Bank of Albania will for the first time open its own Museum, where it will exhibit its numismatic collection to the public at large. It does not intend to establish a museum in its
classical form, where visitors can only see exhibitions of coins and banknotes dating from antiquity to present day. Following the example of other European central banks, it will be interactive providing the visitors more insights into the objectives, role and activities of the central bank in Albania.

The establishment of a summer school is another initiative related to public literacy, where Bank of Albania experts will share their know-how with students interested in learning more about the application of empirical approaches in the areas of economic research. The contents of the summer school curriculum will be similar to the ones applied in universities and will be developed with the support of Bank of Albania experts. Central bank’s library fund, scientific research and statistical information available at the Bank of Albania will serve as a basis for the academic curriculum literature.

The Bank of Albania also aims to take concrete steps toward the design and implementation of a national strategy for the financial education of the public. Upon its initiative, as a first step in this regard, it will gather all Albanian stakeholders in a joint roundtable. A complete strategy, where each actor provides his/her own contribution to enhance the financial literacy of the public at any age, is the best investment to increase the country’s welfare.

Technological and infrastructure conditions

Technological and infrastructure conditions play a role in the normal and efficient operation of work. Technological infrastructure development projects aim at facilitating a number of work processes further, while enhancing the security of systems remains top priority. With a view to carry out its day-to-day work activity, two of the most outstanding buildings of the Albanian capital, Bank of Albania’s Headquarters in Scanderbeg Square and former Dajti Hotel are being subject to reconstruction projects, under the pronounced commitment of the Bank of Albania to preserving cultural heritage and improving the environment of Tirana.

Despite the multiplicity of challenges, their accomplishment aims at achieving a single goal: the aspiration to join the big European family with dignity, walking in the same steps with its counterparts. This aspiration delineates Bank of Albania’s path in the years ahead.
ADDRESSES AND PRESENTATIONS
BY BANK OF ALBANIA’S
ADMINISTRATORS IN ACTIVITIES
IN ALBANIA AND ABROAD
Dear bank representatives,
Dear guests,

It is a special pleasure for me to address the periodic Bank of Albania forum, which this time will discuss on “Collateral, loans, market and legislation”. Today’s round table will aim at a careful analysis of all factors that affect qualitative and secure lending to the economy. For that reason, we have an added presence of state institutions. I take this opportunity to thank and welcome their representatives to this round table.

Over the last three years, we have witnessed some events that have gone beyond normal limits of expectations, imposing a series of changes. Consequently, markets, structures, institutions and even economic concepts have been affected in all aspects. Nevertheless, while the Albanian economy has been influenced by global financial developments, we are proud to say that it has demonstrated high resilience and stability.

I have stated many times that Albania is one of the countries that:

• Did not experience bank bankruptcy or capital injections from the state;
• Handled courageously the crisis of trust and confidence in the banking system; financial intermediation never halted;
• Continued to mark positive, though decelerated, growth rates;
• Continued to keep well-anchored inflation expectations all the time;
• Experienced inconsiderable and fully absorbable additional costs following the shocks generated by the global crisis.

This performance and immunity is not a product of accidental circumstances. The growing economic activity and financial sector stability reflect the following:

• Successful coordination of economic policies before and during the crisis;
• Structural reforms before and during the crisis;
• Special attention by the Bank of Albania, particularly in the period preceding the crisis, as regards strengthening the financial stability through a series of regulatory and administrative banking supervision actions;
• Market consolidation and expansion through including all non-bank financial operators in banking supervision scheme, as well as through licensing new factoring operators.
The actual positive economic development provides us with the possibility to take structural reforms further in the long run, in order to consolidate the country’s comparative advantages in the national, regional and global context. Return to previous growth rates, on a global perspective, is a difficult challenge that requires a combination of high productivity of land, capital and labour.

In concrete terms, economic growth for 2010 was at 3.9%. This growth relied mainly on foreign demand and increased exports, while domestic demand slowed down. The Albanian economy is expected to reach 5% growth for the two years ahead, thus reflecting optimistic expectations. The Bank of Albania has also informed in its earlier statements that the inflation rate is in check and, by the end of the year, it will be within the Bank of Albania’s target band.

Developments in the banking system indicate that its activity continues to grow although at lower rates compared to the pre-crisis period. Since 2010, banking system activity has grown significantly, relying on higher deposits and increased lending to the economy, which were up respectively by about 18% and 10% in annual terms, as at May 2011. The banking system continues to be adequately liquid and well-capitalised.

The capital adequacy ratio is about 15%; considerably higher than the legal regulatory benchmark of 12%, showing banking system adequate capacity to cope with future development challenges.

The Bank of Albania has constantly conducted periodic stress tests. According to the latest test results, all the banks operating in Albania are capable to continue with their activities even in the event of extreme shocks to the economy. Conclusions drawn from the stress tests are not accidental. Our supervision model is prudent, proactive and preventive.

It has been uniform throughout the pre-crisis period, following its outburst, and up to this day. We, deliberately, in the years of loan expansion, paid particular attention to:

- Cover every single lent Albanian Lek with adequate collateral;
- Complete on time the credit registry;
- Not lend in unprotected foreign currencies, such as in Swiss franc and Japanese yen;
- Apply a very prudent policy on loan provisioning, especially in terms of unprotected foreign currencies;
- Improve governance, internal control and risk management;
- Create the required flexibility to restructure existing loans and supply the economy with new loans.

Allow me to recall our first open forum in the spring of 2008, when, in my address to the forum I said, and I quote: “...monetary policy and financial stability are inseparably related to each other. It is difficult for me to
establish which one weighs more nowadays. However, I am convinced that any investment made today to guarantee the financial stability will turn into greater efficiency of monetary policy.”

This leads us to the conclusion that these achievements are not by mere chance. They are the outcome of long, persistent, visionary and comprehensive efforts. Another argument I would like to focus on is lending to the economy, one of the key factors to promote economic development. It should be seen not only as an economic catalyst, but also as a source of future stability for banking operators. In this process, special emphasis should be placed on lending quality, the analysis that should be associated to it, and the management quality of risks related directly to this process or other banking activities.

One of the first shocks generated by a financial crisis, among other, targets lending. Financial crises pose more difficulties, because they are lengthy and affect every cell of the economy. There are no exceptions to this “rule”, neither for advanced nor for emerging economies, which include the countries of our region as well.

Therefore, the current leitmotif of structural reforms, in the global context, is market regulation, expansion and further development.

The real estate and corporate stock and securities markets should be open round the clock, to anyone who wishes to buy or sell. This is the basic concept of the market economy. Without this function, the market is fragmented, stands still, does not function, thus affecting the activity of the economic agents and leading, in turn, to more non-performing loans.

The latest data reveal that non-performing loans have reached the level of about 15%. This increase reflects the struggle for liquidity on a part of businesses and households, leading to their incapability to repay regularly their obligations to the banks. The Bank of Albania finds that the banking system is paying increasing attention to the customer relation management, especially with those customers in difficult financial situations.

In many cases, negotiations between the banks and their clients have led to loan restructuring, in order to infuse a fresh spirit to business performance.

Certainly, there have been cases of complete incapacity of a borrower to repay the debt, which case has been channelled in court procedures to an eventual execution of the mortgage.

It is this very phenomenon – execution of collateral – which has been a key concern for the banking sector and led the Bank of Albania to call this round table. In addition to legal difficulties, often a bureaucratic attitude is observed in relevant institutions. The Bank of Albania has analysed these difficulties in cooperation with stakeholders, such as banks and private and public bailiff services.
Allow me to list a few of these problems as per their categories:

Objection of bailiff procedures

For a considerable number of cases, banks pose the following claims:

• prolonged obligatory execution procedure;
• courts suspend bailiff procedures without evidence submitted by the debtor and ignore arguments presented by banks;
• courts have failed to call in banks as third parties in the process, thus violating the principle of the appropriate legal process.

Moreover, it is noted that the chances to suspend a court proceeding until a final decision increase relative to the amount subject to execution or objection.

Securing the claim

Another concern of banks relates to the court decision on securing the claim. Examination and decisions of the court are often made in the absence of the creditor, and, consequently, its loss is not examined, violating therefore the principle of equality between the parties and prolonging the suspension of execution procedures for months.

The situation worsens since conform to provisions of the Code of Civil Procedures, action to secure a claim should be based on written evidence and not on estimates at the time the loan is granted, which vary substantially from the estimates at the time of the court proceeding.

Deadlines of case decisions

The banking community claims that delays in issuing execution orders consist in the publication of these decisions and, subsequently, in breaches of legal deadlines envisaged for deciding on a case.

Unfortunately, it is found that delayed decisions and procrastinated processes have encouraged debtors not to return the debt, favouring thus the problematic borrowers.

In addition to court-related concerns, there are a number of issues faced during bailiff procedures as summarised below:

• fictitious sequestration or recovery of the object;
• speculative reduction of the object’s price, to the disadvantage of creditors’ interest;
• lack of procedures on immovable property built without a construction permit;
• lack of transparency and guarantee for a process with integrity for objects under execution.
The list of concerns is even longer, which indicates that the problems faced are numerous. However, it seems that the relationship with bailiff services has seen qualitative improvement after the approval of the legal framework and introduction of private bailiff officers in the market.

Cooperation of the banks with these services demonstrates that there is:

- clear rising tendency to respect execution deadlines and better use of legal provisions;
- increased effectiveness in notification procedures;
- increased assistance in dealings with relevant public institutions, and active and specialised participation in court sessions, initiated by the debtor;
- impartiality, professionalism, and transparency in handling the cases.

With a unified position of all participating institutions, today’s round table will convey a clear message to raise the awareness of all stakeholders in the process: the general public, businesses, individuals and potential borrowers that execution of collateral remains an important pillar to preserve banking system stability, and in a wider context, financial stability.

In the framework of this forum, and in order to have an overall picture on this matter, information has been obtained from the banking system and the private and public bailiff services. Additionally, preliminary technical meetings have taken place with representatives of stakeholders on the execution of collateral.

In these meetings, some ideas were shared, which may be subject to further discussion in the near future to address the raised concerns and may be subject to discussion in today’s table as well.

More specifically, it is necessary to:

- organise training of various groups participating in the collateral execution process, with a view to identify problems arising from the legislation, as well as to better the understanding of legislation;
- promote unification of decisions on conflicting cases. For that reason, interest groups need, through their legal representatives, to encourage the presentation of the cases to the Supreme Court to request a unified decision procedure;
- see the possibility of revising the relevant regulatory legislation so as to eliminate all identified difficulties;
- have various stakeholders assist with the development of an awareness-raising campaign on this issue;
- draft a manual on practical issues on execution of collateral, with the assistance of EURALIUS mission in Albania.

These measures will be subject to following discussions. It is important that, after agreeing, they are translated into an action plan to find a timely solution for problems related to the execution of collateral.
Ladies and gentlemen,

The Bank of Albania has played an important role as the guardian of the country’s macroeconomic and financial stability. Macroprudence has been the dominant word in our communication with the market, authorities and the general public.

We have translated it as a necessity for more capital, liquidity, and paying capacity of the banking system. Hence, the Albanian banking sector has never reached an impasse. The Bank of Albania has provided and will continue to provide the necessary liquidity to the banking system, injecting a fresh spirit to the market and the entire economy.

Prudential policies and timely legal regulations have guaranteed an effective banking supervision and have provided adequate access of businesses to bank loans.

Banks are surely created to lend but, above all, they need to bear in mind that stability of the public, i.e. individuals’ deposits, is more important than lending to a specific business, or the portfolio of a specific bank. Moreover, businesses need to recalibrate their position vis-à-vis the latest developments in the domestic and external economies.

Businesses need to aim at higher productivity, through identifying all competitive advantages, in relation to overall global changes.

Bank of Albania has been vocal about the role of lending and support to the economy, and it will continue to be so. Its vision for the future is: more stability, foreign investments, and loans to ensure sustainable development and natural integration in the European family.

Thank you.
SPEECH BY THE GOVERNOR OF THE BANK OF ALBANIA MR. ARDIAN FULLANI
At the Press Conference on the Monetary Policy Decision-Making of the Bank of Albania’s Supervisory Council
27 July 2011

Today, on 27 July 2011, the Supervisory Council of the Bank of Albania reviewed and approved the Monetary Policy Statement for 2011 H1. Based on the analysis of Albania’s latest economic and financial developments and following discussions on their performance outlook, the Supervisory Council of the Bank of Albania decided to leave the key interest rate unchanged at 5.25%. The Supervisory Council holds that the actual monetary conditions are appropriate for meeting the inflation target and for continuing to stimulate the economic activity.

Let me now proceed with an overview of economic developments and main issues discussed at today’s meeting of the Supervisory Council.

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The Albanian economy continued to grow during 2011 H1, although in the presence of added challenges generated by the internal and external economic developments. Tensions in global economies and financial markets, as well as increased prices of raw materials and foodstuff led to shrinkage of Albania’s economic activity. The first factor raised the uncertainty of economic agents and risk premiums in financial markets, while high inflation imported from world markets decelerated domestic demand and increased inflation expectations at home. Despite the unfavourable factors, Gross Domestic Product posted growth and main macroeconomic balances and financial stability remained stable.

According to INSTAT data, Albania’s annual economic growth was 3.4% in the first quarter, supported by the fiscal stimulus of this period and foreign demand for Albanian products and services. On the other side, private consumption and investments continue to be slow, reflecting cautious consumer behaviour and existence of spare production capacities in the economy respectively.

The Bank of Albania deems that economic activity posted similar growth even in the second quarter, with higher contribution of the private sector and downward public sector and foreign demand.

Consumer prices were under added inflation pressures during 2011 H1, mainly due to foreign price increase in global markets. Average annual inflation during the first and second quarters of the year was 4.0% and 4.1%, respectively.
As regards the consumer basket items, prices of processed foodstuffs had the main impact on the formation of annual inflation. Their contribution to headline inflation floated around 55%, close to this indicator’s all-time record. Inflation of non-food consumer goods, such as oil and other day-to-day consumer goods and services, was an added contribution to consumer price hike. On the other hand, the contribution of non-processed foods to inflation was stable.

The gradual upsurge of domestic food products supply during the second quarter balanced the effect of these items’ price increase in international markets. Lastly, administered prices and increased excise on some products had an increasing impact on annual inflation, albeit lower compared to a year earlier.

Concerning the macroeconomic aspect, a number of factors contributed to inflation over the period under review, with various degrees of intensity and opposite directions of action. Upward inflation pressures were generated mostly by conjunctures of raw material and primary commodity prices in international markets. Imported inflation was transmitted directly to increased consumer goods prices in Albania. It exercised additional pressures on producer prices and inflation expectations, but these second-round effects remained controlled. Furthermore, the negative output gap continued to exercise downward pressures on prices, balancing, in part, the effect of foreign price increase. The expansion of economic activity continues to be below the potential of the economy, leaving unutilized capacities in the labour and capital markets. Under these conditions, inflationary pressures from the real sector of the economy remain controlled. This is reflected also on the core inflation performance, which, although upward, remains anchored close to the Bank of Albania’s medium-term inflation target.

Moreover, monetary indicators generated contained inflation pressures, reflecting also a prudent monetary policy of the Bank of Albania. In March, the Supervisory Council of the Bank of Albania decided to increase the key interest rate by 0.25 percentage points, to 5.25%. This decision was made in response to added inflation pressures of foreign origin. It aimed at retaining the anchoring of economic agents’ expectations on inflation and minimising second-round effects. Even after this increase, domestic monetary conditions remained stimulating and provided the economy with the appropriate support at this stage of its development. In line with the action time-span, this measure is considered to have been effective in signalising the commitment of the Bank of Albania to comply with its inflation target and keep inflation expectations under control. In addition, it kept unchanged the stimulating characteristic of the monetary policy and conditions as reflected in comparatively low interest rates, banking system ample liquidity and exchange rates favouring Albanian exports.

Let me now focus on economic highlights defining the inflation performance as well as their expected development.
In line with its past year’s performance, the expansion of the Albanian economy during the first and second quarters of 2011 relied mostly on the industry and services sectors growth. Owing to foreign demand, industrial output increased by 12.3% in annual terms, providing major contribution to the expansion of the economy in the first quarter. The services sector, topped by “Trade, hotels and restaurants”, continued to support economic growth, although less than last year’s quarters. This sector’s annual growth marked 1.8% in the first quarter of 2011. The services sector performance is closely connected to consumer spending performance, which I will address later. After five quarters of contraction, the construction sector posted an annual growth of 4.6%, triggered by higher public investments during this period. Lastly, agriculture maintained growth and contribution rates similar to the last quarter of 2010.

Indirect data obtained from business surveys and monetary indicators suggest that this performance is and will continue to be along the same lines even during the second quarter and beyond.

On the demand side, economic activity relied mostly on foreign demand and public spending, while private sector contribution was low.

Indirect data support the assessment for a weak private consumption performance during 2011 H1. In spite of increased available income and improved bank lending – as indicated by higher employment, real wage and consumer and house-purchase loans – consumer confidence was low. The Albanian consumer continues to be cautious in spending, displaying added saving preference over a number of quarters. Naturally, this behaviour is a structural correction of the consumption model shown over the past years, but the slow performance of consumer spending reflects, also, added uncertainty about the future.

While the first component is welcomed, in the context of preserving macro- and micro balances, the second component may and should be corrected: household consumption has the potential to grow and be stimulated in the short and medium run. Taking into account the significant share of consumption in GDP, its performance will substantially condition economic growth during this time span.

Private investments increased at a moderate pace during 2011 H1 as illustrated by higher loans for investment and imports of capital goods. Although financial terms – availability, liquidity and bank interest rates – have significantly improved, the existence of spare capacities in the economy limits the demand of businesses for investment. In the short run, the position of economic activity operating below its potential conditions a slow performance of investments. In the medium run, investments performance will reflect developments in domestic and foreign demand performance. Given the need for a more competitive Albanian economy and its further orientation towards exports, stimulation of investment, increase of production capacities and adoption of more advanced processes and technologies should be priorities
Public expenditures provided a positive contribution to the aggregate demand of 2011 H1. Following the consolidated behaviour of last year, fiscal policy was stimulating during this period. Public spending increased by 7.4% in annual terms, led primarily by current expenditures, with an added positive contribution of capital expenditures as well. On the other hand, budget revenues were slow, increasing by 1.1% in annual terms. The differences of growth rates for revenues and public spending materialised in the expansion of the budget deficit. In GDP terms, budget deficit at the end of 2011 H1 stands at 4.1% or about 1.5 percentage points higher than a year earlier. Expansionary fiscal policy was more present during the first quarter of the year, while in the second quarter it was more moderate. Revenue and spending growth rates reduced during the second quarter, leading to the need for the revision of the 2011 budget, in order to retain the parameters of public finance soundness in the short and long run. On the other hand, measures to control budget deficit through reducing public spending implies modelling the fiscal stimulus during the second half of 2011.

Foreign demand continued to provide a positive contribution to the aggregate demand. Nevertheless, as expected, its positive impact was lower than a year earlier. During the first five months of the year, Albanian exports increased by 23.3% y-o-y, which is lower compared to 2010. On the other hand, deterioration of trade terms and domestic demand performance triggered the increase of imports in the first half of the year.

Value of imports increased 14.1% y-o-y during January-May, thus, leading to higher trade deficit. Following its narrowing in 2010, this deficit expanded by approximately 8.8% y-o-y during this period.

Trade deficit expansion, negative foreign currency flows in the services account and lower remittances were reflected in the expansion of the current account deficit in the first quarter, at the end of which, this deficit was at 11.8% of the GDP, illustrating the fragile position of the external sector of the economy.

The performance of the four demand components led to positive, but below potential, economic growth during 2011 H1. Unutilised capacities in the economy controlled production costs and generated controlled inflation pressures.

Monetary indicators analysis confirms our assessments for contained inflation pressures suggesting that money supply growth rates are moderate and in line with the economy’s demand for real money. In average terms, M3 annual growth was 11.3% in January-May triggered by a steady growth of deposits in the banking system. Demand for money is dominated by public sector demand for funding, while the private sector’s demand was more moderate. Lending to the private sector increased on average by 11.5%
during the first five months of the year, about 1.5 percentage points higher than in 2010 H2. In contrast to previous years, lending is oriented more towards the national currency: ALL-denominated loans increased by about 14% as at May. Lending continues to be impacted by a moderate demand for loans while the banking system has adopted prudent lending practices, with tightened lending standards for certain market segments.

Financial markets were calm reflecting low risk premiums and a good liquidity situation. In the interbank market, interest rates fluctuated around the key interest rate, following its latest increase in March. The increase in the key interest rate is also followed by the yields in the Government securities primary market and is reflected less in the ALL-denominated deposits and loans, due to factors of liquidity and risk that accompany financial intermediation. The yields curve has retained its slope, indicating low inflation premiums in financial markets.

Summing up the expected economic performance, our projections and assessments suggest that economic growth will continue even in 2011 H2. Aggregate demand will be supported less by the public sector and foreign demand, while the private sector is expected to provide a larger contribution to the economy. Nevertheless, economic growth is not expected to fill completely the negative output gap. The Albanian economy will continue to have spare capacities in the capital and labour markets, avoiding potential wage-inflation spirals and producing contained inflation pressures in the medium run.

In addition, imported inflation is expected to decline and administered price rise effects are expected to be eliminated in the medium run. In the presence of anchored inflation expectations by economic agents, the Bank of Albania expects consumer price inflation to gradually settle close to its target of 3% in the period ahead.

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Drawing on the information above, the Supervisory Council of the Bank of Albania deemed that inflationary pressures remain, in the short run, high. However, they are controlled and in the medium run they are expected to follow a downward trajectory. In the absence of unexpected shocks, inflation is expected to be within the target band of the Bank of Albania over the monetary policy-relevant horizon. Inflationary expectations of economic agents continue to be within the inflation target range, which is essential under the conditions of the simultaneous presence of the negative output gap and high foreign prices. The Bank of Albania is fully committed to anchoring inflationary expectations in compliance with its inflation target and stands ready to accomplish its mandate, by preventing the materialisation of constant pressures on inflation.

We deem that the monetary conditions are appropriate to stimulate economic growth, without generating additional inflationary pressures. Given the fragile equilibriums of the Albanian economy, this philosophy will continue to lead our activity in the period ahead.
At the end of discussions, the Supervisory Council concluded that the monetary conditions remain appropriate for meeting the medium-term inflation target and decided to leave the key interest rate unchanged at 5.25%.
Today, on 31 August 2011, the Supervisory Council of the Bank of Albania reviewed and approved the Monthly Monetary Policy Report. Based on the analysis of Albania’s latest economic and financial developments and following discussions on their performance outlook, the Supervisory Council of the Bank of Albania decided to leave the key interest rate unchanged at 5.25%. The Supervisory Council holds that the actual monetary conditions are appropriate for meeting the inflation target and for continuing to stimulate the economic activity.

Let me now proceed with an overview of actual and expected economic developments and main issues discussed at today’s meeting of the Supervisory Council.

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Annual inflation in July was 3.6%, following the downward trend noted in the second quarter of the year. Consumer price performance continues to be under the pressure of rising prices in global markets, although lower than in previous months. Annual inflation was primarily formed by the contribution of processed food prices, most of which are imported. Decline of the annual inflation rate reflects the downward contribution of unprocessed foods as a result of increased supply of domestic agricultural products, a seasonal development, which in July 2011 appeared to be stronger than a year earlier. On the other hand, regulated price goods and non-food goods had a low and downward contribution to this month’s inflation.

In line with Bank of Albania’s expectation, controlled inflationary pressures by the domestic economy and anchored inflation expectations created a favourable environment for a rapid reduction of imported inflation effects.

Consumer prices during 2011 were mainly affected by supply shocks, materialised in higher prices of imported goods and some products subject to excise, or with regulated prices. These effects appeared to be more moderate in July. In the absence of sudden shocks, they are expected to decrease further in the months ahead. Below-potential economic growth continued to generate controlled inflationary pressures on the demand side. Core inflation stopped increasing and is set around the Bank of Albania’s target of 3%. Moreover, stabilisation of inflation expectations of economic agents and the prudent policy of the Bank of Albania regarding their anchoring are reflected in moderate second-round effects on inflation.
Following, I will describe in more detail economic highlights defining the inflation performance and their expected development.

Although amidst an unfavourable external environment characterised by added uncertainties in our trade partners, the Albanian economy continued to grow during the second quarter of 2011.

In the absence of direct data, the Bank of Albania deems that economic growth during this period is similar to the one recorded in the preceding quarter, thus remaining below Albania’s potential growth rate. Economic activity relied on the public sector and external demand, although more moderately than in the first quarter of the year. In the meantime, the private sector demand appears sluggish, also conditioning our projections for economic growth for the rest of the year.

Private investments continue to be slow, compared with their historical rates and the country’s needs for quantitative and qualitative production capacities. This conclusion is suggested by the performance of capital goods imports, low confidence indices of construction and industry sectors – the most intensive in using capital – and low bank lending for investments. Moreover, there are signals for improved private consumption performance in the second quarter, as suggested by improved consumer confidence indices and increased consumer credit.

The expected easing of funding terms during the second half of the year and the decline of perceived uncertainty by businesses and individuals are expected to be accompanied by a somewhat more positive performance of private consumption and investments in this period.

The stimulating nature of fiscal policy during the first half of the year is reflected in a positive contribution of public expenditures to economic growth. For the first seven months of the year, public spending increased by 5.9% in annual terms. Moreover, the performance of fiscal revenues was slow, reflected in their annual growth of 2.3% during this period. This behaviour of revenues and expenditures is materialised in a higher budget deficit than a year earlier. Fiscal impulse to the economy was consistent throughout this period. It showed tendencies of moderation during the second quarter, which are expected to strengthen further during the rest of the year, in conformity with the revised budget of 2011.

Contribution of foreign demand to economic growth was lower during the second quarter of the year. Trade deficit in the second quarter was 20% higher compared to a year earlier.

Our exports shrank by about 2.8% year-on-year for this period, a reflection of reduced exporting of energy, which is a volatile component in exports. Despite this development, the core basis of exports continues to maintain more sustainable growth rates. On the other hand, imports continued their annual growth, albeit at a lower rate compared to the first quarter of the year.
Aggregate demand performance triggered economic activity growth but was insufficient to fully utilise Albania’s output capacities. Developments in the labour market seem sluggish and do not have premises for emergence of stable inflationary pressures.

Signals from economic information are also confirmed by the monetary indicators analysis. In June, the annual growth of M3 aggregate was 11.8%, close to the average rates of the past 12 months. Our assessments show that the expansion of monetary supply is in line with the performance of the economy’s demand for monetary assets.

In June and throughout the second quarter, the public sector demand for funding was high, in line with the intensity of the fiscal activity during that period of the year. Furthermore, the private sector demand for funding continued to be moderate. Lending to private sector posted an annual growth of 11.6% in June, in line with the second quarter’s performance.

Financial markets are characterised by a serene environment with contained risk premia. Interbank market experienced increased trade volume; interest rates were close to the key rate and had low volatility. In the primary market, government demand for funding is reflected in the increased yields of government securities. However, the trajectory of yields retained its slope, showing low inflation expectations by market agents.

As regards the economy’s performance outlook, our projections and assessments suggest a continuation of economic growth, in terms relative to those of the first quarter.

Composition of aggregate demand is expected to be different to the one of the first half of the year. Private sector of the economy is expected to be more vivacious in the second half, while the contribution of the public and external sectors are expected to be more moderate. Size and speed of the private sector recovery will define the stability of economic growth in the future. In spite of assessments for increased aggregate demand, economic activity in Albania is expected to remain below its potential, thus conditioning the continuation of spare capacities in the economy in the period ahead. Subsequently, inflationary pressures originating from the aggregate demand are expected to be contained. In addition, foreign prices effect is expected to be more moderate in the upcoming months while inflation expectations of economic agents continue to be within the target band. Consumer price inflation is expected to continue its downward trend in the next months, gradually approaching the Bank of Albania target.

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Taking into consideration the information above, the Supervisory Council concluded that inflationary pressures in the medium term are contained.
In the absence of abrupt shocks, inflation is expected to drop further and stay within the target band of the Bank of Albania over the policy-relevant horizon. Distribution of risks remains overall symmetric: slower than projected economic growth would lead to a rapid decrease of inflation, while a further consolidation of imported inflation could keep inflationary pressures high for a longer time.

At the end of discussions, the Supervisory Council concluded that the monetary conditions remain appropriate for meeting the medium-term inflation target and decided to leave the key interest rate unchanged at 5.25%.

In the near future, the downward inflation trend and shift to the downward section of the risks balance may establish the premises for a revision of the monetary policy. In any case, its future position shall factorise the new information obtained, aiming to adopt monetary conditions to respect our objectives.

The Bank of Albania remains fully committed to anchor inflation expectations in accordance with its inflation target and to support sustainable and long-term development of the Albanian economy.
Dear Minister of Finance,
Dear Deputy Minister of Education,
Your Excellencies Ambassadors,
Dear NBS Governor Šoškia,
Dear Mr. Passacantando,

It is a special pleasure for me to open the 9th Conference of the Bank of Albania, which this time is dedicated to financial education. I take this opportunity to wish a warm welcome to all the participants in this room and in particular to our foreign guests.

If you asked me directly what I mean by financial education, I would summarise it as: the ability of consumers and investors to understand financial concepts and products; ability to understand how to protect oneself against unwanted developments; ability of people to make sound decisions about their money in accordance with their life’s circumstances.

Financial education should start with understanding the role of finance in a free market economy. Finance “lubricates” the economic growth process. It also provides opportunities for all those who do not have sufficient financial resources. In 1911, the renowned Austrian economist Joseph Schumpeter said: “...that the structure of modern industry could not be erected without finance, that it makes the individual to a certain extent independent of inherited possessions, that talent in economic life “rides to success on its debts” even the most conservative orthodoxy of the theorists cannot well deny.”

If you asked me why is financial education important, I would say it in these words: because it contributes to Albanians’ financial welfare.

The more literate we are financially, the more capable we are to make decisions that contribute to our improved welfare. This is true for everyone, regardless of who we are or where we come from. As Friedman, the Nobel Prize winner, says: “Economic freedom is an essential condition for political freedom.” Our exercising rights that result from economic freedom would be unavailing in absence of financial literacy and equality in the marketplace. This implies not only the same information at the same time, but also the capacity to use this information.

Finances create an added value not only for the rich, but also for the entire society. It is necessary to create equal access for all citizens. Equal access to
Finances, equality before the law and law above all are the foundations of modern market economy. Finance and financial education walk side by side. While literacy may turn a poor man into a rich man, illiteracy, on the other hand, may conduct a rich man into misery. Finances are dangerous when you are not financially literate enough. That is why I consider this conference as highly important.

The Bank of Albania has devoted constant attention to financial education. Our education agenda is integral and comprehensive both in terms of geography and age groups, full of interactive elements and modern communication methodology. Further on, I would like to refer to some of the elements that constitute the philosophical grounds of our educational work.

First, I would like to recall that financial welfare is inextricably related with the country’s economic progress.

It has been already proven that individual’s welfare is proportionate to economic activity and prices of financial assets. The cause-effect relation is true on both directions. Our economy and financial institutions are strong when employment increases and income and wealth grow. Financially healthy individuals are inclined to increase their consumption and, therefore, boost their spending, consequently pushing the economy forward. Moreover, financially successful people boost bank lending potential by channelling their savings into deposits.

Therefore, they are in a position to access crediting by the banking system, giving life to new businesses which, in turn, provide higher employment and welfare.

To most people, having a job and a salary or estate is essential to personal financial welfare. However, the fact that you may have a job or a salary does not imply that you automatically have the capacity to make wise decisions on effective money utilisation.

This is the point where our relation with financial education is subjected to the test of truth. Is this test passed? The sub-standard credit crisis in the US revealed that individuals in most cases did not manage to pass this test. Consequently, the debt load on individuals grew even heavier, while access to crediting became tighter, resulting in a big risk for their financial future. A similar analogy may be drawn for lending in foreign currency in some Eastern European countries.

Second, financial education should be seen as a public good that brings about positive externalities to the society. It not only increases individuals’ financial welfare, but also affects directly economic policy efficiency undertaken by relevant authorities.

The more educated the public, the higher economic policy efficiency is. Keeping inflation and economic activity under control is almost impossible...
in a society ailing from financial illiteracy. Macro-economic balances are achieved and maintained through monetary and fiscal policies instruments. The society needs to be aware of these instruments, understand them, evaluate stimuli and incentives, and properly respond to them.

The important role of consumer behaviour for the policies success is clearly evidenced in the “rational expectations” theory. A simple intuition behind this theory is that rational individuals shape their expectations using the available information optimally. They respond to new information by adopting their behaviour to maximise welfare.

In this case, individuals “equipped” with financial literacy read and understand developments in economic policies and respond to them rationally. This mutual understanding would drive the economy towards the desired direction. The central bank adjusts its policies in response to the actual behaviour of agents, who would adjust their behaviour in line with the central bank’s policy. For this interaction to happen, both the public and the central bank need to speak the same language and understand each other unequivocally. Monetary management needs this two-way understanding and the active role of individuals. Consequently, the trust and confidence of the public is earned, monetary policy objectives are achieved and its reliability is enhanced.

Third, I would like to underline that financial education of individuals establishes a more stable society on one hand and a stronger and secure banking system on the other.

Efficient and ongoing financial education is a path trotted by millions of individuals and families in their endeavour to achieve financial goals and accumulate wealth.

The positive effect of this process is reflected in a stronger economic and financial stability for the entire society. The banking system has its role to play in this process, mainly through lending to businesses and households. As a regulator, the Bank of Albania gives its share of contribution ensuring that banks strictly abide by legal and regulatory obligations in relations with their customers. On the other hand, financially literate customers contribute to the development of the banking system with their increasing demand for financial products and services. Therefore, the result is clear: higher efficiency, lower charges, better services and healthier and safer banking system.

Fourth, I would like to highlight that financial education, over time, improves the standard of living in the long run, including retirement age.

In a recent analysis, the essential reason why an individual needs to amplify his/her financial literacy is that this investment will help him/her to reach his money management objectives.

Although personal objectives may vary from an individual to another, from
financial education point of view, the improvement of society’s living standard is guaranteed and confidence in the future is boosted.

Financially literate individuals are capable to make healthy financial plans from an early stage of their career. Their knowledge enables them to plan their finances for retirement, children’s education and accumulation of financial assets. These individual behaviours, seemingly irrelevant, bring about great benefits in the national perspective.

Fifth, I would like to underline that financial education is a long-term process, extended over time, and that the presence of specialised institutions is indispensable.

Although in financial crisis individuals incur large damage, they continue to be involved in future crisis. The number of individuals, who are familiar with interest rates they either receive or pay in financial transactions, remains low.

The same can be said about investment strategies, financial risk identification and assessment, and other elementary money management concepts.

Many people do not think in financial terms and do not perceive accurately profits and costs resulting from bank loan use, or wealth-related effects originating from home ownership and other similar long-term assets.

Reasons behind this behaviour are understandable and related to the fact that the majority of the society acquires information circumstantially, hoping that the actual failure becomes a lesson for the future.

One way to eradicate circumstantial learning is the introduction of financial reading at an early stage of education. In this view, I would proudly say that the Bank of Albania has provided an outstanding contribution. Allow me to briefly make a résumé of our work in this aspect.

The first strategic station of financial education provided by the Bank of Albania was the assessment of needs and identification of training priorities. From this point of view, we assessed that it was indispensable to open the Bank “de facto” to the public. More frequent communications with the market and its important participants, as well as periodic explanations of monetary policy decision-making and risks balance related to inflation and financial stability, are some initiatives that we consider as a very effective education process.

I am proud to say that now we have:

- A public opinion that builds up expectations as regards our decision-making;
- A media sector, which has admirably enhanced understanding, interpretation and expectations related to our decision-making;
- A banking sector, which reads accurately and responds with high
flexibility to the direction oriented by us;
• A qualified public critique, where Bank of Albania finds a mirror of alternative opinions on its adopted decisions and practices.

Another important aspect is the identification and division of the population according to their demographic, geographic and cultural characteristics. To us, financial education is a public good intended for all. In line with the best international experience, we identified financial education for young people as highly important, targeting not only students but also their educators. Its practical realisation has been a complex process requiring adequate human and financial resources.

For that purpose, the slogan adopted by us is very meaningful: “Education may be costly, but it is priceless”. The implementation methodology is widely known: meeting face-to-face, interactive games that intrigue children’s imagination, a series of publications with a flexible level of difficulty, training of teachers of Economics, and a tour in various schools of the country.

In this regard, I would like to point out to the recent contribution of the Bank of Albania to high-school students for the book on: “Personal finance in your hands”, which is conceptualised as an elective subject for high schools.

Dear guests,

Education is a never-ending process. Learning is lifelong. It is deep, immense, and comprehensive. Therefore, I have to say that in spite of what we have done so far, we still have a long way to go. The Bank of Albania deems as imperative the drafting and implementation of a national strategy on contemporary financial education. The Bank of Albania stands ready to join any initiative at national level, which aims at promoting literacy across the country.

Thank you.
SPEECH BY THE GOVERNOR OF THE BANK OF ALBANIA MR. ARDIAN FULLANI
At the Press Conference on the Monetary Policy Decision-Making of the Bank of Albania’s Supervisory Council
29 September 2011

Today, on 29 September 2011, the Supervisory Council of the Bank of Albania reviewed and approved the monthly Monetary Policy report. Based on the analysis of Albania’s latest economic and financial developments and following discussions on the performance outlook, the Supervisory Council of the Bank of Albania decided to cut the key interest rate by 0.25 percentage points. Following this decision, the interest rate on one-week repurchase agreements is 5.00%. This cut in the key interest rate reflects contained inflationary pressures, anchored expectations of economic agents, and a more prudent fiscal policy during the period ahead. The easing of monetary policy aims at providing appropriate monetary conditions to meet the medium-term inflation target and promote economic activity through stimulating consumption and investments in Albania.

Let me now proceed with an overview of economic developments and main issues discussed at today’s meeting of the Supervisory Council.

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August was characterised by a sharp decline in inflationary pressures. Annual inflation rate was 3.1%, or 0.4 percentage points lower than in July. In addition to decreased foreign price shocks, during this month, inflation contribution to regulated prices dropped and contribution of prices of bread and grains curbed. Furthermore, the seasonal effect of domestic agriculture production supply was stronger this year, leading to further reduction of food items annual inflation.

During 2011, consumer prices in Albania were subject to supply shocks, materialised in high import prices. This effect was more moderate during July-August and, in the absence of sudden shocks, it is expected to subdue even further in the months ahead. Moreover, second-round effects are contained, under the influence of controlled expectations of economic agents on inflation. The domestic economic setting produced controlled inflationary pressures. Aggregate demand slowdown led to spare capacities of production factors and controlled long-term inflationary pressures on the economy.

Therefore, core inflation was 2.9% in July, showing a downward trend, and was close to our inflation target.

New economic data obtained in September are scarce. Following our earlier analyses and based on new available information, the Bank of Albania deems that the Albanian economy continued to grow during 2011. Economic
activity relied primarily on public spending and exports surge, while the private sector demand had a slow positive performance. Consumption and investments were supported by crediting, but their upsurge is conditioned by hesitation to spend.

Following the revised budget, the fiscal behaviour during the last two months is characterised by lower spending pace and lower budget deficit increase. Fiscal stimulus was more present in the first quarter, while in the following months the fiscal policy was more contained, which is reflected in lower annual deficit increase.

Until August, public spending posted an annual growth of 5.2% in annual terms, while revenues slowed down, growing only by 2.2%. Budget deficit was ALL 30.6 billion as at end-August.

Foreign demand continues to support Albania’s economic growth. Exports’ annual growth was 28.8% in July. On the other hand, imports continued their downturn trend that had started in the second quarter of the year, increasing by 4.6% in annual terms. Export uptrend and import slowdown materialised in narrowed trade deficit in July, contracting by 6.0% year-on-year. However, the economy’s external position remains a structural weakness of the Albanian economy, which reflects the need for higher competitiveness of our products in global markets and conditions the effectiveness of stimulating macroeconomic policies.

Indirect indicators analysis of private consumption reveals its moderate performance. Consumption continues to suffer from perceived uncertainty by Albanian families, leading to higher saving although aggregate income increased. Private investment slowed down in this period, but it retained positive growth rates.

This is supported by the good performance of foreign direct investments, up by 38% during the second quarter, and higher import of capital goods, which suggest higher private investment in the economy. Nonetheless, this hike is conditioned by the fact that many businesses are operating below their production capacities, limiting their needs for new investments.

Monetary inflationary pressures remain controlled in the medium run. Annual growth of money supply, M3, which resulted 11.2% in July, retained the average rates recorded last year. Money demand was affected by a moderate upward private sector demand for funding. Lending to private sector increased by 12.5% in July, triggered by the relatively stable increase of lending to private businesses and resurgence of lending to households. Although the banking system has eased lending standards, the Bank of Albania deems that there is still room for further easing, especially as regards credit for private investments.

Developments in financial markets indicate downward risk premiums and liquidity. In the interbank market, trade volume expanded further and interest
rates dropped, remaining closer to the key rate and displaying low volatility. More moderate government demand for funding is reflected in refrained upward trend of government bill yields in the primary market. Additionally, the yields curve retained its slope, showing low inflation expectations by financial market agents.

At the end of 2011 H1, the situation of the financial system and banking sector was stable. The banking sector expanded its activity and broadened its share in the country’s economy. Liquidity situation is good while the deposits by the public increased at satisfactory rates; they cover more than once the value of credits and borrowing from non-residents is low.

Data indicate that lending growth rate is improving, but the credit portfolio quality continued to drop. The banking sector retains stable growth rates of net interest income and gross operating profit.

However, the required increase in provisioning to cover credit risk led to lower net profit of the banking sector compared to a year earlier. However, profit continues to be positive and concentrated. The capital adequacy ratio followed a downward trend, even though it remains clearly above the minimum level required by the regulatory framework.

The analysis of resilience to various shocks and risks indicates that credit risk is the primary source of banking sector risk. Furthermore, the banking system is more protected from direct market risks, but it continues to be exposed to the effect, on credit quality, of adverse exchange rate and interest rates fluctuations. Therefore, in its supervisory capacity, the Bank of Albania requested commercial banks to timely and properly identify non-performing loans, establish relevant reserve funds and take determined action to recover loans through execution of collateral. These actions, combined with reduced operating costs, would establish gradually the conditions for a positive and stable profit, which would support better the banking sector’s need for capital.

In a shorter term, the Bank of Albania has requested the banking sector to strengthen activity capitalisation through increased shareholders’ capital. The Bank of Albania has oriented and monitored this process closely, so that it takes place in compliance with the development strategy and relevant risks performance. The process to strengthen capitalisation indicators in the banking sector includes creation of adequate capital above the required minimum. The process continues in line with the specifications that the Bank of Albania has discussed and communicated with the banking sector. As a result of these measures, the banking sector would remain stable and establish conditions for its higher contribution to Albania’s economic growth.

Our assessments on economic outlook suggest a continuation of economic growth for the rest of the year. Foreign demand and public sector demand will continue to provide positive contribution to aggregate demand upsurge, although more moderately than in the first half of the year. Private sector demand remains an important factor in determining economic growth in the future.
Fiscal consolidation measures and the unfavourable situation in global markets and our trade partners will shift the short-term focus of economic growth to the domestic demand: private consumption and investments.

The capacity of these aggregates to compensate for the slowdown of the two main drivers of the insofar growth will condition Albania’s economic performance over the upcoming 2-3 quarters. In the longer run, the performance of the Albanian economy shall be determined by its competitiveness and productivity as well as expansion of Albanian goods and services in foreign markets. This requires intensification of structural reforms at macro- and microeconomic level as well as financial and macroeconomic stability in the country.

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Taking into account the information set out above, the Supervisory Council of the Bank of Albania deemed that inflationary pressures are downward and remain controlled in the medium run. Developments in the Albanian economy will continue to generate weak inflationary pressures, as a result of the negative output gap action. On the other hand, pressures generated by developments in global economy are expected to be downward. Economic agents’ inflation expectations remain anchored around the Bank of Albania’s target.

At the end of discussions, the Supervisory Council decided to cut the key interest rate by 0.25 percentage points, down to 5.00%. This decision serves to comply with the inflation target in the medium run and provides the necessary monetary conditions to stimulate economic activity. The Bank of Albania remains heedful to future economic and financial developments, with a view to take the right steps for the fulfilment of its mandate.
Today, on 26 October 2011, the Supervisory Council of the Bank of Albania reviewed and approved the Monetary Policy Report for the third quarter of 2011. Based on the analysis of Albania’s latest economic and financial developments and following discussions on the performance outlook, the Supervisory Council of the Bank of Albania decided to leave the key interest rate unchanged at 5.00%.

Let me now proceed with an overview of current and expected economic developments, as well as main issues discussed at today’s meeting.

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Overall, the Albanian economy had a positive performance in 2011, although in the presence of an unfavourable external environment.

Domestic economic activity posted growth and some of the main macroeconomic and financial balances are controlled and have further improved.

Nevertheless, certain challenges have had their impact on the Albanian economy. More specifically, during the last two years, economic growth has been characterised by hesitating behaviour of economic agents towards consumption and investment. Similarly, reassessment of risk in financial markets has been coupled with added prudence and heightened risk premiums in domestic and international credit markets. Furthermore, high prices of oil, food and other products in global markets have led to higher import prices for Albania along with strong inflationary pressures during the first half of the year. Finally, the increased attention of financial markets towards public finance soundness has limited the possibility of fiscal authorities to pursue strong and stimulating policies.

All these factors are reflected in economic growth rates, bringing them to below the potential level and creating spare capacities in the economy.

Moreover, these challenges have identified the need to continue with structural reforms and pursue prudent macroeconomic policies. Structural reforms, at macro and micro level, should be oriented towards increasing the competitiveness of our labour force, products, and services in the global market. In addition, these reforms aim at enhancing foreign interest in the Albanian economy, as a business destination. Macroeconomic policies are facing a new reality, at the national, regional and international level. They
should not, however, shift the focus away from safeguarding macroeconomic and financial stability.

This stability controls long-term risk premiums and is a prerequisite for stimulating sustainable investments in the economy.

Analysing these issues and coping with these challenges has been the focus of the Bank of Albania’s work during 2011.

In the following paragraphs, I will present a more detailed overview of economic developments in Albania, focusing on inflation performance and Bank of Albania’s work to accomplish its mandate of maintaining price stability.

In the third quarter, average annual inflation rate was 3.2%, down by 0.9 percentage points compared to the rates of the first half. Annual inflation had also pursued a declining trajectory during the second quarter but it appeared more pronounced during the third quarter.

This trajectory is determined primarily by the reduced contribution of food items inflation, as a result of price increase slowdown for these goods in international markets. Additionally, the increase of domestic agricultural products supply beyond the seasonality that characterises this period had an impact on the reduction of food items inflation. Furthermore, this quarter evidenced the full cancelling out of the effect of administered price increase from a year ago.

Inflation in 2011 was mainly affected by supply shocks, which are materialised in higher import prices. As expected, this effect was more moderate in the third quarter. Its downward dynamic was shaped mostly by the more moderate growth rates of raw materials and commodities in international markets. Supply shocks were balanced by downward pressures originating from aggregate demand. The Albanian economy continued to grow in the second and third quarters of the year; however, it continues to operate below its potential.

Below-potential growth has conditioned partial utilisation of production capacities and has prevented the creation of wage-inflation spirals. Furthermore, controlled expectations of economic agents on inflation have kept second-round effects at minimum levels.

Public sector demand and foreign demand continued to support economic activity, although at a more moderate rate. Meanwhile, private sector demand had positive but slow growth rates. Private consumption rates remain contained, influenced by uncertainty about the future and hesitating consumer behaviour. Nonetheless, employment indicators stabilisation and increased aggregate disposable income suggest a growing potential of consumption during this period.
Private investments remain slow. Increasing foreign demand has supported the expansion of investment in the industry sector, but slow domestic demand has not favoured investment increase in services and construction sectors. Below-average capital utilisation rates, which are present almost across all the sectors of the economy, are expected to dictate low demand for investments in the near future as well.

Public sector demand stimulated economic growth this year, but its contribution has been declining since the first quarter. The performance of this aggregate demand element has been dictated by the conduct of fiscal policy, which, although on the stimulating side for 2011, has been more prudent over the last two quarters. Budget deficit at the end of the first months of the year was ALL 30.7 billion, remaining almost unchanged for three consecutive months.

In GDP terms, it is estimated to be at 3.1%, or 0.5 percentage points higher than a year earlier. Budget deficit performance has been defined primarily by the slowdown of public spending, while public revenues retained slow growth rates. Public spending and revenues growth at the end of the first nine months of the year was 3.5% and 1.0%, respectively.

Foreign demand continued to support Albania’s economic growth. In real terms, net export deficit in the second quarter narrowed compared to a year earlier, materialising in a positive contribution of this component to aggregate demand. The latest data on foreign trade suggest a similar trend for the third quarter as well. Trade deficit in July and August narrowed on average annual terms by 0.2%, as a result of increased exports and slight slowdown of imports. Exports increased on average by 31.7% during July-August.

Good performance of exports, beyond the positive impact of temporary factors related to energy sector, is stimulated by exports of processed goods and mineral raw materials. Imports marked an average annual rate of 8.2%. Regardless of positive developments, the reduction of the current account deficit demonstrates the need to continue with structural reforms in order to enhance domestic products competitiveness.

Monetary indicators confirm the assessment for contained inflationary pressures in the Albanian economy. Expansion of money supply is considered to be in compliance with the economy’s demand for real money. Annual M3 growth was 10.6% in July-August, retaining its rates noted during 2011. Private sector demand for monetary assets pursued the rising trend of previous months. Lending to the private sector was up by 12.6% in July and August, or about 1.1 percentage points higher than the average rates recorded in the second quarter of the year.

This growth relied primarily on private businesses demand for funding, while lending to households is also pursuing a rising trend. Annual growth rates of lending to households settled at 5.7% at the end of August, from 1.5% at the end of last year.
Bank of Albania analyses suggest that the moderate credit growth is primarily due to lower demand from the economy for credit. This stance is confirmed by business surveys, which display a weak investment inclination as well as by the reduced number of credit applications to commercial banks. Against this setting, the banking system is liquid and well-capitalised to conduct its financial intermediation activities. In response to the monetary policy of the Bank of Albania, credit interest rates have reached their historic low. Nevertheless, the banking system has added its prudence as regards lending, with more critical assessment of business plans and tightened requirements for collateral.

This approach is a reaction to the uncertainty about the economy in general or its specific sectors and reflects a more prudent development model of crediting and banking business. In the long run, it will yield a more sustainable growth for the Albanian economy and will guarantee a solid and reliable banking system.

Financial market developments reveal low liquidity and inflation premiums. Trade volume in the interbank market increased further, while, in the presence of a good liquidity situation, interest rates in this market followed the decrease of the key interest rate and displayed low volatility. In respect of time lags in the monetary policy transmission mechanism, the decrease of interest rates is expected to be transmitted also into the deposit and credit market. Bond yields retained their rates of the second quarter, in the presence of moderate government demand for short-term funding.

Looking ahead, our assessments and projections suggest continued economic growth for the rest of the year. Foreign demand is expected to support aggregate demand, but at slower rates compared to the first half of the year. Domestic demand performance remains pivotal to economic growth, while contribution of public stimulus is expected to moderate even further, as a result of the need to retain stability of fiscal indicators. Under these circumstances, private sector demand will condition the size and velocity of domestic demand recovery in the future.

The performance of fundamental factors that define private demand suggests that there will be a potentially better performance of consumption and investments in the economy compared to the estimated insofar materialisation.

Bank of Albania deems that, within the parameters of macro and microeconomic soundness, there is room for a more rapid growth of consumption and investments, as well as a more realistic behaviour of economic agents towards projections for the future. The Albanian economic outlook remains sound; development policies and further structural reforms will free new development potentials, which need to be explored far-sightedly and attentively by the private sector.

Analysing the factual and expected inflation performance, in September, the Bank of Albania eased the monetary conditions, lowering the key interest rate by 0.25 percentage points to 5.00%. The easing of monetary conditions,
in addition to maintaining price stability, enables a higher support to domestic demand.

In the absence of unexpected shocks, inflationary pressures appear to be downward in the medium-term horizon. The reduction of foreign price effects on inflation and the impact of negative output gap make the inflationary pressures balance to remain controlled and downward over the policy-relevant horizon. Inflation is expected to range around our target in the medium run. It will be under the balanced influence of internal and external inflationary pressures. Aggregate demand is expected to remain below the economy’s potential, thus carrying forward the negative output onto the upcoming period. Subsequently, inflationary pressures originating from the demand side will remain contained. Additionally, foreign price effects will continue to be present in consumer prices performance and is expected to pursue its downward trend.

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At the end of discussions, the Supervisory Council decided to leave the key interest rate unchanged at 5.00%. The monetary policy position in the future will aim continuously to adjust monetary conditions with a view to respecting our objectives, in the presence of downward inflation trends. Without affecting price stability and external balances of the economy, the clarification of the situation in the euro area over the coming days and confirmation of our expectations on Albania’s economic performance may create room for further easing of the monetary policy.
SPEECH BY THE GOVERNOR OF THE BANK OF ALBANIA MR. ARDIAN FULLANI
At the Press Conference on the Monetary Policy Decision-Making of the Bank of Albania’s Supervisory Council
30 November 2011

Today, on 30 November 2011, the Supervisory Council of the Bank of Albania reviewed and approved the monthly Monetary Policy Report. Based on the analysis of Albania’s latest economic and financial developments and following discussions on the performance outlook, the Supervisory Council of the Bank of Albania decided to cut the key interest rate by 0.25 percentage points. Following this decision, the interest rate on one week repurchase agreements fell to 4.75%. This key interest rate cut was triggered by contained inflationary pressures over the policy-relevant horizon and expectations for a more prudent fiscal policy over the period ahead. The Supervisory Council judged that this decision would provide appropriate monetary conditions to meet the inflation target over the medium run. It would also increase monetary stimulus and promote economic activity in Albania.

Let me now proceed with an overview of economic developments and main issues discussed at today’s meeting.

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Annual inflation rate was 3% in October, slightly up compared with the previous month’s figure. Annual consumer price rise continues to be influenced substantially by high food, oil, and primary commodity prices in global markets. These prices have been reflected in a higher contribution of imported inflation to domestic inflation throughout 2011. However, the increase in domestic agricultural production, stable exchange rate and price stabilization in global markets have reduced its impact in recent months. These factors, along with the cancelling out of regulated price inflation have led to a continuous slowdown in the inflation rate in recent months.

From the macroeconomic aspect, consumer prices were influenced by drivers of a different impact and intensity. The shocks arising from high prices in global markets, the increase in several regulated prices in 2010 and excise taxes in early 2011 were offset on the downside by the below-potential performance of economic activity and sluggish demand-side pressures. In the presence of anchored inflation expectations and low monetary inflationary pressures, the overall macroeconomic environment has favoured the reduction of inflationary pressures during the second half of the year.

In the absence of direct data, the Bank of Albania’s assessments on the country’s economic performance, based on indirect qualitative and quantitative indicators, suggest a moderate increase in aggregate demand
over the second and third quarters, in line with the one registered over the first quarter. Economic activity has continued to be supported mainly by foreign demand and growth of exports, whereas the public sector’s impact has been downward and private consumption and investments have remained weak. In particular, the private sector demand is assessed as sluggish. Notwithstanding the positive performance of real income, consumer spending is estimated as weak, affected by the uncertainty surrounding the future and increased propensity of Albanian consumers to save. On the other hand, the need of private businesses to carry out new investments has been low, against the backdrop of a moderate demand for goods and services and the existence of spare capacities in production.

Fiscal policy has been stimulating during 2011. For the first ten months of the year, budget deficit posted ALL 30.9 billion or about 33.0% higher than a year earlier. The performance of budget deficit has been determined by the sluggish increase in expenditures and revenues at an annualized rate of 3.9% and 1.4%, respectively. The stimulating fiscal policy has been winding down steadily following the first quarter of the year, as also shown by the decelerated increase in public spending and budget deficit. This fiscal stance has contributed to maintaining the level of public debt under control. The Bank of Albania assesses the latter as one of the most essential indicators of macroeconomic stability at home. In this context, we encourage fiscal authorities to take appropriate measures, in order to ensure long-term sustainability of public debt.

Foreign demand has supported the Albanian economic growth, notwithstanding the concerns surrounding the global economy and especially our trading partners. Albanian exports continue to grow, albeit at decelerated paces compared with the previous year. Exports grew 27.3% in the third quarter of the year, while imports grew 8.6% over the same period. Trade deficit increased 6.8% in the first nine months of the year. The Bank of Albania is very heedful to external balances of the Albanian economy, considering their correction as one of the main priorities of the country’s macroeconomic policies. This objective assumes more importance against the backdrop of recent developments in global financial markets. In the long run, its attainment requires ongoing structural reforms, which will enhance the competitiveness of the Albanian economy and will generate higher revenues from the export of goods and services.

Monetary inflationary pressures remain subdued in the medium run. Monetary expansion has maintained stable annual growth rates during the year, resulting 10.4% in September. Public sector demand for funding has been downward in recent months, making the private sector’s demand to provide the largest contribution to money supply growth. Private sector credit grew 14.0% in September, marking a slight acceleration compared with the first half of the year. However, as we have constantly stated, the relatively sluggish performance of private sector credit reflects mostly its weak demand. The banking sector appears liquid and well-capitalized to credit the Albanian economy, but it has increased its prudence in terms of lending, thus reflecting
the new reality of the Albanian economy and global financial markets. The Bank of Albania assesses that, within the parameters of prudence, there is room for a more rapid growth of credit and for supporting sound investment projects by the banking sector. On our behalf, we will continue to support the financial system with liquidity and monetary stimuli in order to boost lending.

Financial markets continue to highlight downward liquidity premiums and inflation. The interbank interest rates have declined further, remaining closer to the key interest rate and displaying low volatility. A more moderate government demand for funding and the short-term interest rate cut in the money market have been reflected in an overall decline in the yields on primary market government securities.

Our assessments on economic outlook suggest a moderate economic growth for the remainder of the year and for the next year. Heightened uncertainties surrounding the global economy provide their impact on current and expected developments of the Albanian economy. In particular, the situation of our trading partners is expected to be reflected in a sluggish foreign demand for Albanian goods and services. Also, the need for maintaining budget deficit and public debt parameters is expected to materialize in the public sector’s lower contribution to aggregate demand over the period ahead. Under these conditions, the performance of economic activity at home will be determined substantially by the extent and speed of recovery of the private sector demand - consumption and private investments. Despite the positive growth, aggregate demand is expected to remain below the potential of the Albanian economy, determining the incomplete capacity utilization in the economy and generating demand-driven low inflationary pressures. Considering the materialization of these expectations and projections for further weakening of inflationary pressures from global conjuncture, annual inflation is expected to be within the Bank of Albania’s target in the medium run.

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Taking into account the above overview, the Supervisory Council of the Bank of Albania deemed that inflationary pressures are downward and remain subdued over the policy-relevant horizon. Also, economic agents’ inflation expectations remain anchored around the Bank of Albania’s target.

At the end of discussions, the Supervisory Council decided to cut the key interest rate by 0.25 percentage points, to 4.75%. This decision serves to comply with the inflation target in the medium run and provides appropriate monetary conditions to stimulate the economic activity. The Bank of Albania remains heedful to future economic and financial developments at home and abroad, with a view to take the right steps for the fulfilment of its mandate.
Dear Chairman,
Dear colleagues,
Dear guests,

It is a privilege and a responsibility for me to deliver a keynote speech today amongst colleagues, researchers and other distinguished participants. The cooperation of the Bank of Albania with Oxford University focuses on developments in South-East Europe. In this regard, today’s strategic and scientific discussion will focus on mid- and long-term perspectives of growth and welfare in this region.

These are important moments since, perhaps for the first time in modern history, the future of global economy lies in the hands of developing countries. The United States and Europe are struggling with their problems, victims of their financial excesses and political paralysis. Their heavy debt burdens constrain them to years of stagnation or slow growth, widening inequality, and possible social discontent.

These are important times for the countries of our region, too. While focusing on themselves to solve their own problems, the developed economies have now less time and resources to commit to the Euro-periphery. The current situation in the developed Europe, especially in the SEE closest partners, has potential implications for this region. Several euro countries are facing with a situation, which was once unthinkable even for the euro periphery.

With these almost reversed roles, it would be reasonable to expect less economic support in terms of investments, foreign demand and technical assistance towards South East Europe from its traditional developed partners. Therefore, it is important that the countries of the region focus more on their internal resources for economic growth. Moreover, it is possible that the political focus on internal affairs will weaken the role of the EU as a political, moral and social anchor for the region. In conclusion, it is the first time that the South-East European countries will have to find more resources within rather than outside the region.

In my opinion, recently, the world has witnessed a new wave of regionalism, which is in contrast with the globalization trend that has been in full swing over the last two decades. Almost all countries have sought integration with other countries, and not necessarily always with their neighbours. Preferential trade arrangements have been the central element of regional cooperation. Analytically, preferential trade arrangements give rise to two important effects
on trade flows, trade creation and trade diversion. Trade creation is the replacement of domestic expensive production by cheaper imports from a preferred partner and trade diversion takes place when a country switches its source or origin of imports from more efficient producers who are excluded from the preference to less efficient but preferential producers.

Currently, additional evidence suggests that support for globalization is withering in developed societies. Economic literature is more frequently referring to the side effects of globalization and technological innovation on labour markets and income distribution. Public support blames deteriorating conditions on the globalization and the rise of once fragile emerging countries. During these times of high anxiety, the leading economies, which once used to be the promoters of globalization and free trade, are now barely mentioning the Doha Round and are trying to turn to regional cooperation not only as a solution to economic problems but also as a counter balance to the shifts in economic power. In almost every part of the world, long-term problems and imbalances are being solved through closer cooperation among neighbouring and other countries forming new economic regions.

Regional cooperation is becoming the rule more than an exception. Therefore, each region will have to secure its own future. Of course, this should occur in a context of cooperation both across and within the regions. Regional integration is traditionally seen as harmonisation of trade policies leading to deeper economic integration with political integration (a spill-over effect) as a potential future outcome.

These are topics that we have already discussed before. Today, I would like to focus on particular reforms that would help regional cooperation. I would like to draw your attention to the fact that regional cooperation is usually entrusted with contributing to greater economic prosperity only when cooperation and democracy-building political dialogue leads to more cooperative attitudes and mentalities among governments and peoples alike. This is a concept that has repeatedly been advanced and promoted by the EU as a successful example and development model for other regions of the world. In contrast, the region’s history is full of unpleasant episodes.

The SEE region is the last group of transition countries lagging behind both in economic and political criteria relative to the CEE region. In my opinion, this reflects the difference in political and economic choices made by the authorities and the public at large. The long-run developments of our region are best described by the famous quote of Sir Winston Churchill: “The Balkans produce more history than they can consume”, instigated by a centuries-long history of conflicts in the region. I believe that economics has the right tools to explain this behaviour. In my opinion, the trace of these conflicts, regarded as one of the reasons that stopped and slowed down the prosperity of the region, and accurately referred to by Churchill, has its roots in a strong rent-seeking behaviour in the region. The prosperity is seen in possessions rather than in trade, cooperation and technology. It seems that the region is not aware of the existence of modern economic thinking.
It is a common habit to refer to the case of the Balkans as something different and unique. The region is home to three monotheistic religions and a melting pot of civilizations, cultures, waves of migration and trade. It may seem like the history of this region is distinct from that of the rest of Europe. Well, I do not think so. All that is happening in SEE is not unique to this region. The whole European continent can claim the same “historical achievements”; the latest two shattering ones less than one century ago. This has been a defining pattern, more a rule than an exception, since ancient Rome: countries fighting for possessions and resources, first in Europe and then worldwide. The behaviour is not unique to Europe; it is found across all civilizations.

Later, as the understanding of economics evolved, the developing countries of the world found out that they could achieve the same results from trade and reliance on well-organized markets. EU is a good example to illustrate my point. Economics, markets and regional economic cooperation achieved, within a short time, the unified markets of resources and final goods that had not been achieved before because of centuries of conflicts.

It is probably the same rent-seeking behaviour that pushed the region into a different trade model from that of the CEE. The engine of growth has relied mostly on the non-tradable rather than the tradable sector. Wealth accumulation in different forms, most of all in the real estate, created the illusion of wealth and capital gains and resulted in large trade and current account deficits.

The absorption-led growth model adopted during the second half of the last decade only made our model less sustainable. This is, however, one of the few examples where the region outperformed its developed partners. This excess consumption was far more evident in Europe than in the region, as the SEE region, in particular its central banks, could foresee the problems of this consumption based on faster credit growth.

Both examples illustrate that financial and economic illiteracy is one of the problems, and probably one of the most important ones that motivates the particular Balkan history of the past and the present. Therefore, combating financial and economic illiteracy is one of the solutions not only to the heated temper of the Balkan nations but also to the success of the regional cooperation and new growth agenda. It is not enough to recognize that financial literacy is poor; we must also understand whether financial literacy matters in decision-making. Addressing this issue is particularly difficult because financial literacy is delivered randomly in the population. Traditionally, there are two ideal venues for financial education: schools and the workplace. My question is then why not extending it to the political environment.

These problems used to be evident in the behaviour of political and community leaders. This seems to be less of a concern today, as the leaders in the region not only understand but also contribute to the idea of regionalism in SEE. However, unless the community shares the same beliefs with their
political leaders, efforts for regional cooperation will not be successful. Therefore, these are times that call for leadership. The region’s leaders need to combat financial illiteracy, push for reforms, do what is right and not yield to the political will of less literate communities.

The leaders in the region have already started to move in this preferred direction. This is mostly due to the fact that the political and legal developments are motivated by the single European target to reinforce and integrate regulatory and structural reforms. This can be done through external treaty obligations and visible political commitments. Often, small countries participating in Preferential Trade Arrangements have made, or are trying to push ahead, major reforms. Political negotiations to form new regional institutions necessitate political, ideological, and social affinity among members. If states share similar ideological preferences over economic policy objectives as well as political and cultural values, they will likely be more willing to accept their neighbours’ policies and cooperate with them. Regional infrastructure is improving and several infrastructure projects are either connected or constructed with a regional focus in mind.

However, the leaders and the entire region must understand that physical infrastructure will not open economies and support regional cooperation unless it is supported by a linked virtual infrastructure. With this concept, I mean an effective, practical, and fundamental infrastructure. Without this virtual infrastructure, markets and institutions in the region will not be connected as a human and capital formation; legislation and regulation will potentially evolve in different directions, failing to provide scope and support for regional exchanges and cooperation. This virtual connection is the only force that will eventually transform the region into a closed endogenous system that seeks a single and unique long-run solution. This view of the region, as a single interconnected system, has been characterized and driven by many “explosive trends”, which, in the past, have prevented the region from achieving sustainable prosperity in the long run.

Unfortunately, these trends define past and present unresolved problems and challenges of individual countries and communities of the regions. During the last 15 years, these explosive trends have been overridden by the European integration process with its promise of economic and social prosperity. However, while the European model is currently withering, the rising economies of BRIC countries are providing alternative and competing models with potential negative effects for the region.

I belong to that group of observers who are sceptic on the model that relies on exploitation and export of regional natural resources for its large dependence on foreign demand and international markets price volatility. In addition, these new models have the potential to fuel and reinforce the “explosive trends” leading to potential competition for country-based projects, motivated by short-run political choices and pragmatic short-run solutions.

That contradicts the progress and positive developments of the last decade
in the South East European Region and may slow, if not damage, the speed of economic convergence and integration of the region as a whole with the group of developed countries. This current situation represents a crossroad, an important moment that requires the leadership to act as a driving force that counterbalances all the other trends that prevent our common sustainable and successful future. To this end, education, open minds, and rich diversity are potentially successful development strategies.

Wishing success to this conference, I would like to thank you once again for the established collaboration and the invitation to hold a keynote speech today.

Thank you for your attention.
SPEECH BY THE GOVERNOR OF THE BANK OF ALBANIA MR. ARDIAN FULLANI
At the 2011 End-Year Reception
19 December 2011

Dear Minister,
Your Excellencies Ambassadors,
Dear Members of Parliament,
Dear representatives of the banking system and the media,
Dear guests,

I would like to welcome and thank you for your participation.

Your presence today is a special pleasure for me personally and the Bank of Albania.

My special thanks go to the former members of the Supervisory Council of the Bank of Albania, whose term in office has ended. I personally appreciate the seriousness and commitment they have dedicated to their work, a precious contribution to Bank of Albania’s institutional furtherance.

Thanking them once again for their professional work, allow me to welcome the newly appointed members of the Supervisory Council of the Bank of Albania, renowned public figures with an unquestionable professional career. They come from diverse fields of professional careers and will bring in added value to the Bank of Albania, contributing to a wider coverage of the institution’s functions.

I am confident that the Bank of Albania, in its activity, will continue to incorporate the best international standards as regards decision-making, independence, accountability, transparency and governance.

I believe that a healthy economy that generates stable growth needs a developed financial sector in terms of its depth and width; a flexible banking system, which manages public deposits cautiously and channels them efficiently to fund the economy. Today, from this modest ceremony, I would like to assure you that we are fully responsible for this as useful as difficult mission. The Bank of Albania will be always attentive to ensure macroeconomic and financial stability for the country.

In the spirit of end-year celebrations, I cannot help but focus on the Albanian young generation, an inspiration to our work and a fruit of our investments for a better future.
Following its established tradition, the Bank of Albania has the pleasure to announce the Governor’s Award for the Best Diploma Thesis in 2011. This year, we decided to announce this award in this important activity, in the presence of friends and colleagues. This is an expression of our appreciation for research by these today’s students – tomorrow’s colleagues.

The Bank of Albania pays particular attention to the young generation, especially to its education.

When I look back and see how we started financial education five years ago, I recall what may be a naive but a significant comparison; Neil Armstrong’s landing on the moon. In addition to his famous quote “...That’s one small step for (a) man, a giant leap for mankind” he said “…the surface is fine and powdery. I only go in a fraction of an inch, maybe 1/8 of an inch, but I can see the footprints of my foot from the trail.”

Looking back, we may spot our footprints. The reward of an excellent work in an unknown domain is the 6900 students who have chosen to attend as an elective subject “Personal finance in your hands” published by the Bank of Albania. In cooperation with the Ministry of Education and Science, we are endeavouring to make this book available in every school and to each student with the ultimate goal for them to be educated financially and empowered to manage personal finance. Only in this academic year, high-school students in 36 districts of Albania chose this book as an elective subject, making us optimistic and forward-looking.

We strongly believe that today’s young generation will be the protagonists of tomorrow’s economic life. For this purpose, we need to make our utmost investment for their formation, in order to ensure not only their future, but also the country’s future.

The youth are eager and capable to assimilate, process and convey information, habits, or new products in any field of life. They are the transmitters of innovation, the most energetic and progressive segment of the society. It is our moral, professional and institutional responsibility to invest for a qualitative education of the young generation.

To us, enhancing financial literacy is crucial. A well-educated nation guarantees its country’s welfare and progress. Therefore, we have decided to choose the young generation as our strategic partner to realize this challenge. We believe in their idealism, positive energy and pure spirit.

I take this opportunity to extend my special thanks to the media and congratulate this community for its work. The media has transmitted the decision-making and activity of the Bank of Albania in a timely and reliable fashion to the public.

Year 2011 was a complex year for the entire global economy, especially the European one, to which the Albanian economy is more sensitive. From this
perspective, the role of the media takes special significance. I am happy to affirm that in Albania, the media has expanded its broadcast time dedicated to economy and finance-related issues, and especially to transmission of information from the Bank of Albania, whose decisions were covered professionally. The media has been active also in promoting the reflection by stakeholders.

Media has supported Bank of Albania policies, forestalling dissemination of uncertainties amongst the public. The self-adjusting attitude has been another important element in media’s activity. The alarming effect has been cancelled successfully by thorough analysis of news items, providing nuances of the truth beyond excesses and speculations.

A fresh example of this responsible behaviour is the EUR/ALL exchange rate fluctuation at the beginning of December this year. Some “panic” was caused amongst the public by earlier media reports and analyses, which were later considered by the media itself as an unreal exchange rate volatility.

Dear guests,

At the end of my address today, I would like to draw your attention on a consolidated annual publication of the Bank of Albania - our 2012 Calendar, the jubilee year of the 100th anniversary of Albania’s Declaration of Independence.

2012 Calendar features a cycle of contemporary works of art, which elegantly combine traditional and modern elements. This artistic ingenuity provides a varicoloured and loyal depiction of the long and toilsome journey of the Bank of Albania and the Lek through good and bad days, times of war and peace, subtle and radical changes. These fellow travellers have always succeeded in renewing and strengthening their shared foundation, which is your trust and confidence. This thread sews together in this calendar, art and the Bank of Albania, as two components that create, uphold and promote values.

The Calendar is an artful portraying of our central bank’s traits such as stability, independence, confidence, transparency and financial literacy, which nourish our dream of a common European future. This future rests in our hands like a golden globe of prosperity and happiness.

Thanking you for your attention, allow me to announce the winners of the Best Diploma Thesis for 2011:

The third prize is awarded to Ardit Azizaj, an MA student of the New York University in Prague, for his dissertation “What Albania’s possibilities are, in future, regarding the world division of labour?” His dissertation focuses on the impossibility of a country to transform its economy successfully from a poor and centralised to a developed economy.
The second prize is awarded to Ledia Sulejmani, a student of the University of Tirana for her dissertation “Economic developments in Western Balkans, future challenges.” Her dissertation describes distinctions and characteristics of Western Balkan countries as regards economic indicators, in light of a common area and its future challenges.

The first prize is awarded to Borana Angjeli, an MA student of Marin Barleti University in Tirana for her dissertation “Pension systems”. Drawing on results from a survey to employees close to their retirement, the thesis points out some of the shortcomings of the pension system in Albania and makes recommendations on changes to the actual pension scheme, in line with European principles, without being a heavy burden for the state budget.

Thank You.
Dear bank executives,
Dear guests,

This end-year event with the Albanian Association of Banks, turned into a tradition of communication between the banking sector and the Bank of Albania, provides an excellent opportunity to make a short resume of the results achieved by this sector in this year and to identify its challenges in the upcoming year.

The banking sector managed to finish off 2011 successfully. Its role in supporting Albania’s economic activity was crucial, while prudence was made to guarantee its financial soundness.

In this regard, the supervisory role of the Bank of Albania has provided an extraordinary contribution. Banking supervision has been proactive and preventive by creating, at the same time, the necessary space for flexible banking activity management. Amendments to the law “On banks in the Republic of Albania”, a number of amendments to the banking regulatory framework as well as the physical interaction through on-site inspections have contributed to enhanced immunity and dampened negative effects generated by the global crisis. The Bank of Albania has periodically conducted stress tests on specific banks to ensure that the banking sector’s security and functionality is never put in doubt.

Currently, we are working for this project to be transformed into regional cooperation taking into account that the same banking groups operate across the entire region.

According to banks reporting at end-September 2011, banking sector total assets expanded 9.5% from year start and about 13% from the corresponding period of a year earlier. The banking sector credit portfolio widened 9.6% during the year or about 15% year-on-year, constituting 49.1% of total assets. During the year, Lek-denominated loans increased more rapidly than foreign currency-denominated loans. The activity increase was sustained mainly by the growth of deposits, which account for 81.4% of total liabilities. During the year, they were up 9.7% or 14.1% higher than the corresponding period of 2010. Liquidity ratios are stable and are expected to consolidate following recent regulatory requirements introduced by the Bank of Albania. As at September 2011, banking activity made a profit of ALL 1.3 billion and return on assets and equity were 0.2% and 1.9%, respectively. Capital adequacy
ratio was 15.1%, better than at the end of 2011 H1. This was due to capital increase by some banks, following the Bank of Albania’s requirement.

These developments confirm stable public confidence in the Albanian banking sector and the significant contribution of the banking sector to fund the Albanian economy in this year. These may be considered as precious achievements in light of the challenges facing the Albanian economy and its economic agents in 2011. Loan portfolio worsening and credit risk management requirements were matched by higher provisions by banks, which in turn contributed to worsened profit. In response, banks managed to optimise their operating costs and improve their capital ratios. In this regard, the Bank of Albania has emphasised the accurate identification of the credit portfolio situation, asking the banks to take firm action and recover their non-performing loans value.

This may be realised through support to qualitative borrowers in temporary difficult situations and through execution of collateral in the case of hopeless borrowers. Execution of collateral and the need to improve the relevant legal and operational framework are considered as a priority by the Bank of Albania. Following recommendations from an earlier forum organised on this topic, the Bank of Albania is fully committed so that other public authorities address the issue with priority.

Furthermore, in cooperation with the banking sector, the Bank of Albania has identified and undertaken a number of other supervisory and regulatory actions, aiming at improving operational capitalisation situation and minimum liquidity requirements both in the national and foreign currency.

Next, some amendments to the Law “On banks in the Republic of Albania” were drafted and approved, which, in essence, complete and improve banking activity supervisory framework. These actions were pivotal for addressing an added risk perception due to international and regional financial developments. I take this opportunity to thank you for your cooperation and concrete actions with regard to the implementation of these new requirements, being confident that you will fully accomplish them within the required timeframe.

Dear bank executives,

More than three years on from the crisis start, global economy’s perspective to exit this crisis remains unclear. Nonetheless, this is a gradual and long process.

Overall, financial institutions, in Europe and beyond, continue to face with the following:

- High uncertainties as regards exposure value to sovereign debt securities;
- Difficulties to ensure liquidity in wholesale markets;
- Reduction of crediting volume and tightening of its terms to fund the domestic economy;
• Higher capital requirements arising mainly from new regulatory rules by supervisory authorities.

The need to reduce investment risk in sovereign debt is accompanied by huge efforts on fiscal consolidation in many countries, especially in Europe. Hence, EU economic growth expectations, including those for countries that had, insofar, posted above-average economic growth, were markedly down. It appears that the best solution for this situation will come only as a result of various countries’ ability to undertake, at this point, vital social and economic reforms as well as to provide financial support so that, on the one hand, financial stability is maintained and, on the other hand, private enterprises are provided with some relief, thus affecting their future economic development expectations.

Albania’s economy maintained its positive growth rates during this period, to absorb external shocks.

This flexibility is a precious characteristic that will continue to support the country’s economic development and buffer effects from various shocks, even in the future. It is important for the banking sector to utilise and support this valuable attribute of economic agents, both private and public, offering them a constant satisfaction of their needs for funding and other services. This action should rely not only on the insofar-successful experience, but also on an economic logic, while only a few countries in the region have retained their positive economic growth rates. Nevertheless, the economic environment will remain a challenging one and it should be assessed pragmatically. Various actions that may be taken should be oriented by the concept of prudence and in respect of regulatory and supervisory framework requirements.

I would like to underline that a responsible bank management during this period will be recognised by its ability to control and administer operational risks in general, and your swiftness to develop institution’s capacities to test the resilience and performance in various scenarios of potential future developments in particular. International standards require that the focus be not placed on planning highly probable events, but on assessing the institutions’ resilience to relatively extreme and unfavourable developments.

Moreover, this process should be part of a broader and constant analysis that you need to conduct with a view to assess your needs for stable operational capitalisation and define hedging measures. These requirements are actually present in the regulatory and supervisory framework and the Bank of Albania stands ready to share with you its experience for effective development.

In conclusion, allow me to say that the Bank of Albania is in the process of perfecting the regulatory framework and supervisory practice, in the context of its cooperation with the European System of Central Banks.

However, full and timely observance of legal and regulatory framework requirements on operational capitalisation and liquidity, as well as bank’s...
overall operational risk management methodology will continue to be an ongoing supervision priority.

This process is oriented by the common objective to safeguard banking and financial systems stability. The Bank of Albania remains committed to cooperate with the banking sector to achieve successfully this objective.

As in previous years, the Bank of Albania will make the appropriate decisions to ensure that its fundamental objectives to maintain price and banking system stability are constantly accomplished for the country’s stable growth in the long run.

Thanking you for your valuable work, I wish you a New Year full of successes in your work and happiness in your families!

Thank You.
Today, on 28 December 2011, the Supervisory Council of the Bank of Albania reviewed and approved the monthly Monetary Policy Report. Based on the analysis of Albania’s latest economic and monetary developments and following discussions on their performance outlook, the Supervisory Council of the Bank of Albania decided to leave the key interest rate unchanged at 4.75%. The Supervisory Council deemed that the actual monetary conditions are appropriate to meet the inflation target and provide the necessary monetary stimulus and to support economic activity in Albania.

Let me now proceed with an overview of economic developments and main issues discussed at today’s meeting.

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Inflation rate in November was 2.9%, slightly down by 0.1 percentage point from the previous month. Most of inflation in November was formed by higher prices of processed foods and non-food consumer goods, whereas other items of the consumer goods basket had low inflation rates.

Recent months were characterised by the progressive reduction of inflationary pressures on the economy. On the supply side, price rise slowdown for main products in international markets and national currency stability were reflected in dampened imported inflation. Moreover, the cancelling out of direct administered price increase effects contributed to lower inflation rates during this period. On the demand side, below-potential growth of the Albanian economy and under-utilised capacities in the labour and capital markets were reflected in limited pressures on production costs and final prices in the economy. Furthermore, the Bank of Albania’s positive experience in inflation control and its reliable monetary policy have contributed to controlling inflation expectations and mitigating transmission of supply shocks on headline inflation. Overall, this trend is expected to continue in the period ahead.

The absence of direct data on real economy indicators makes a comprehensive analysis of the Albanian economy difficult. Our judgement is thus based on indirect data, which proxy developments in various sectors of the economy, as well as information filtered from monetary indicators, fiscal indicators, external sector indicators, and business and consumer confidence surveys.

The analysis of these indicators supports the assessment for positive-but-below potential performance of the Albanian economy in the second and third
quarters. Economic growth was supported by external demand and public sector demand, whereas private consumption and investments continued to be sluggish. Production growth was mainly driven by the industry and services sectors, whereas the construction sector continued to suffer from low demand for residential properties.

Performance of private consumption and investments was sluggish. In line with the performance of the economy, disposable income of Albanian households were assessed as growing at lower rates in this period. The sluggish consumption has reflected mostly higher inclination of Albanian households towards savings. Private consumption was more supported by consumer credit in 2011. Nevertheless, banks report feeble demand for consumer credits, while consumers continued their hesitation for large purchases in 2011.

Moreover, investments in the economy are restricted by the final demand, existence of spare capacities in production and added prudence by banks in lending.

In this context, monetary policy easing of the second half of 2011 is expected to be reflected in better lending terms to Albanian businesses and households to support their consumption and investment. I have often reiterated that their performance will condition economic growth in the short and medium run.

Fiscal policy has been stimulating in 2011, though this stimulus has fluctuated over the quarters. As indicated by the expenditures and budget deficit performance, the fiscal stimulus was stronger in the first quarter and moderate in the second and third quarters. Data on the fourth quarter point to its acceleration.

Budget deficit in the first eleven months was ALL 38 billion, reflecting mainly public spending. Their annualised increase rate for the first eleven months was 5.6%, with added contribution by capital expenditures during October-November. On the other hand, fiscal revenues continue to display slow annual increase, at 0.7% for this period.

Foreign demand continued to contribute to aggregate demand growth in the economy, albeit less than in earlier periods. Its performance was affected by the unfavourable economic situation of our main trade partners. In October, exports were up 16.3%, recording slower annual growth rates.

On the other hand, under the effect of high prices in international markets, annualised import rates remained high and were materialised in Albania’s trade deficit expansion, which in October was 11.6% higher than a year earlier.

Monetary sector’s analysis indicates contained inflationary pressures of monetary nature in Albania’s economy. Broad money expansion was 10.6% in October, lower than the average rates of 2011. In real terms, monetary supply growth rates were stable and are deemed to be in line with economic
agents’ demand for real money. During the last months, public sector demand decelerated, whereas private sector demand for monetary assets increased. Private sector credit growth rates were upward and settled at 14.0% in October.

Credit demand was higher both by businesses and households; however, this growth is slow. Overall, lending terms offered by the banking system and parameters of capitalisation, liquidity and soundness are appropriate for funding higher demand for private consumption or investments in the future.

Latest developments in financial markets continue to be characterised by controlled risk, liquidity and inflation premiums. Successive key interest cuts appear to have been transmitted forthwith into the money market. Government securities yields in the primary market dropped further, reflecting the key interest rate cut in the economy and the low public sector demand for funding. The key interest rate cut is expected to be transmitted in the future to interest rates on deposits and loans, in accordance with the time lags of the monetary policy transmission mechanism.

Lastly, a positive development in financial markets at home is the reconfirmation of the actual government bond rating and the country’s stable outlook by Moody’s and Standard & Poor rating agencies.

Projections for the economic outlook remain subject to high uncertainties, dictated mainly by developments in the global economy. Our analyses and estimates suggest the continuation of moderate economic growth rates for the remainder of the year and the next year.

Economic slowdown in our trade partner countries may be reflected in weaker foreign demand and further deceleration of Albanian exports.

In addition, rooms for implementing fiscal stimuli narrowed in response to the growing need for maintaining fiscal sustainability and controlling public deficit and debt levels. Consequently, public sector contribution to aggregate demand growth is expected to be downward in 2012. Under these circumstances, the extent and speed of recovery of private sector demand will be crucial for the country’s economic growth. As we have stated in earlier communications, the actual monetary conditions are appropriate to encourage private consumption and investments.

***

Taking into consideration the information set out above, in the Supervisory Council assessment, inflationary pressures remain controlled over the policy-relevant horizon.

The presence of the negative output gap in the period ahead will be accompanied by low inflationary pressures originating from domestic demand.
In addition, inflationary pressures from global economy developments are projected to be more moderate, while inflation expectations are anchored. These assessments are materialised in annual inflation projections ranging within the target band of the Bank of Albania for the medium run.

At the end of discussions, the Supervisory Council decided to leave the key interest rate unchanged at 4.75%. This decision serves to comply with the medium term inflation target and provides the appropriate monetary conditions for Albania’s economic activity.

Bank of Albania remains heedful to future economic and financial developments, both at home and internationally, as well as vigilant to fulfil its mandate.
PERIODIC ANALYSES*

* The views expressed in these materials are those of the authors and do not necessarily reflect the views of the Bank of Albania.
I. BANKS AND FINANCIAL INTERMEDIATION

In 2011 Q4, intermediary activity took place against the setting of slow but upward performance of economic activity in the country and heightened uncertainties surrounding the euro-area economy. Economic activity was well below its potential, leading to slow and unsteady improvement of bank loan portfolio and further deterioration of loan portfolio quality. As at end-Q3, the ratio of nonperforming loans to total loan portfolio was 18%, from 14% at end-2010. Against this setting, banks tightened lending conditions further by pursuing prudent lending policies. Moreover, the business financing demand was low, due to existence of spare productive capacity. The heightened uncertainty about internal and external development fosters the businesses’ and households’ reluctance to invest. Moreover, during the third and fourth quarters, many banks in the system raised their capital in response to meeting regulatory requirements. Overall, it is estimated that the banking system is well capitalized and liquid, capable of increasing the financial intermediation.

Developments in deposits were positive, owing to households’ preference for using less cash and money creation from the financial intermediation system. The increased fiscal stimulus in the economy in the final quarter of the year, along with the private sector demand for financing, contributed to money creation, especially in ALL. In November, the deposit-to-GDP ratio amounted...
to 68%, from 64% in 2010. Developments in deposits reflected the shifting of monetary assets towards less liquid instruments. Over the same period, currency outside banks fell by about 1% compared with year-end 2010. Building confidence in the banking system, coupled with economic agents’ orientation toward long-term instruments, led to increased monetization of the economy. The M3-to-GDP ratio increased further, to 82%.

Developments in banks peer-group intermediation reflected an increase in the big and small-sized bank market, while Greek banks continued to contract their intermediation. The largest banks in the system, offering promotional products for savings collection and attractive loan rates, increased their deposit and loan market share. The share of large banks in the deposit market amounted to about 69.5%, from 58% as at end-2010. In the meantime, their loan portfolio for the same period increased by 1.5 percentage points. Greek banks’ loan portfolio and their market share contracted, down to 25% as
at end-November, from 30% as at end-2010. Moreover, their share in the deposit market went down to 17.9%, from 19.3% in December 2010. Small-sized banks were more aggressive in increasing their loan portfolio, hence their market share grew by 3 percentage points. In November, their share in the loan market amounted to 22.1%.

Intermediary activity of the banking system in October and November continued the decelerating trend that had started since August. Loan-to-deposit ratio reached 61.2%, or 2 percentage points less than a year ago, driven by higher growth of deposits in the system and slow improvement of credit to the economy. This dynamic is attributed to the slowdown in foreign-currency intermediation, while the national-currency intermediation has been upward. Also, intermediation costs by currency performed differently over this period. They were up for the national currency and down for the euro. The analysis of lending conditions indicates their overall tightening in Q4, with a significant contribution by non-cost elements.

1.1 Developments in intermediation

In October-November, the national-currency intermediation performed in line with the previous months of 2011 H2, characterized by a slight increase in the loan-to-deposit ratio. In end-November, this ratio stood at 40.3%, from 39.9% in end-Q3 and 39.3% in end-Q2. This performance is attributed to continuation of faster increase in ALL-denominated loans, while ALL-denominated deposits have shown stable paces of increase.

Developments in foreign-currency intermediation during October-November continued the decelerating trend that had started since August. Loan-to-deposit ratio reached 83.7% in both months, from 84.5% in end-Q3 and 88.3% in end-Q2. Both foreign-currency deposits and foreign-currency loans slowed down over this period, but the impact of the latter was determinant to the downward trend of foreign-currency intermediation.
I.2 Intermediation costs

ALL intermediation cost increased in October and November, unlike the downward trend that had been observed in the first three quarters of the year. In October-November, it resulted 6.8 percentage points, from 6.3 percentage points on average in the third quarter. The higher intermediation cost is attributed to increase in the average loan interest rate, which over this period registered 11.8%, up by 0.3 percentage points from the third quarter. In spite of the increase taking place in November and beyond monthly volatility, the loan interest rate has trended down over the past two years. Also, the average deposit interest rate fell slightly by 0.16 percentage points over these two months, down to 4.91% in November. In spite of an increase in the months under review, the intermediation cost is lower, on average, compared with the first half of the year and the previous year’s figure.

Despite the decrease in 12-month T-bill yield, which was used as a reference rate for ALL- credit cost, the margin applied on them increased during October and November, leading to a higher average interest rate on loans. The spread between the loan interest rate and 12-month T-bill yield was 3.91 and 4.85 percentage points, respectively, in these two months, from 3.39 percentage points in September.

Euro intermediation cost1 appeared slightly lower in October-November, compared with the second and third quarters. It averaged 4.79 percentage points in these two months, or about 0.16 percentage points lower than in the third quarter. Its performance is attributed to instantaneous decrease in the average interest rate on deposits and loans, with a higher influence by the latter.

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1 The banks’ activity in foreign currency is dominated by their activity in euro, which accounts for more than 80% of their activity in foreign currency.
The price of euro-denominated loans continues to be significantly higher than the interbank market reference rates for the euro, factoring into the high cost of euro-denominated deposits in the country. The spread between the latter and the Euribor rates has increased again since August, reflecting the banks’ aggressive policy to attract foreign-currency liquidity. In October-November, this spread for the 12-month maturity averaged 1.07 percentage points. The spread between the average loan interest rate and EURIBOR rate fell slightly, averaging 5.19 percentage points in these two months.

1.3 Developments in non-cost intermediation elements

Developments in banking intermediation have been influenced not only by the interest rate but also by non-cost lending elements, which determine the credit supply. The analysis of lending activity in Q4 indicates a further tightening of lending conditions, using mainly the non-cost elements.
Banks continued to tighten their conditions for business loans in 2011 Q4 and are expected to tighten them further in 2012 Q1. All the non-cost elements led to tightening in Q4, with an added effect of the maximum loan maturity and collateral requirements. The tightening of non-cost conditions was associated with higher commissions and an easing effect leading to decline in the margin on average-risk loans.

Conditions for household loans, after having been tightened in 2011 Q3, remained unchanged in Q4. The loan-price elements (average margin, margin on risky loans and commissions) influenced on the easing side. Among non-cost elements, the criteria for loan size, collateral requirements and requirement for reporting loan instalment to income, remained tight, while the criterion for loan maturity has provided a neutral effect on the performance of household lending conditions.

II. DEVELOPMENTS IN DEPOSITS

Banking system deposits were 12.7% higher y-o-y, in nominal terms, in November. During 2011, their annual growth rates were downward. It is pointed out that the annual deposit growth rate, adjusted for the exchange rate effect, was slightly improved in October to November, to 13.8%. Also, the average monthly flows in 2011 were down by 20% y-o-y. The slowdown in deposit growth rates has reflected the developments in foreign-currency deposits, whose increase averaged about ALL 3.4 billion per month, from about ALL-5.5 billion in 2010. ALL-denominated deposits manifested higher flows on a year earlier. Developments in ALL-denominated deposits, besides shifting toward higher maturity assets, have also been helped by money creation in the national currency by the public and private sectors. These developments have affected the maintaining of deposit structure by currency. Thus, the ratio of ALL-denominated deposits to total deposits remained at the same level as a year earlier, at 52%.
According to maturity term, deposit growth was supported by positive developments in time deposits in both currencies. Time deposits increased by about 15% on a year earlier, while demand deposits increased by 5%. Throughout the year, the paces of time deposit growth were slow, driven mainly by performance of business deposits. Positive developments in time deposits contributed to increasing their ratio to total deposits, at 82%, compared with 79% in the previous year. In the meantime, demand deposits were influenced mainly by the performance of foreign-currency business deposits.

ALL-denominated deposits showed steady growth rates in 2011. Positive developments, particularly in monthly flows over October-November, contributed to improving their growth rate to 11.2%. Seasonally adjusted, quarterly deposit flows improved in ALL deposit flows into the system over the last two months, especially in November. Similarly, households’ time deposits were higher than in Q3, confirming their tendency to invest savings in long-term maturities. The ratio of demand deposits to total deposits in ALL reached 18%, or down 2 percentage points from end-2010. In the meantime, household deposits account for about 89.5% of total deposits in ALL, slightly increasing their share on a year earlier.

Foreign-currency denominated deposits showed significantly slower annual growth rates following the third quarter of the year. The annual growth rate fell to 14.1% at end-November, from about 20.8% in the first half of the year. Foreign-currency deposit index, measured at a fixed rate, shows that their annual growth rate has remained constant following September, at about 14%. However, the slowdown observed after July, together with lower money creation in foreign currency have been affected by the previous year’s significant deposit growth effect. Quarterly foreign-currency deposit inflows were downward in the third and fourth quarters, compared with a year ago, mainly due to less time deposits by households. The reduction in household foreign-currency deposits has reflected the previous year’s lower remittances from neighbouring euro-area countries. In contrast to the
previous year, businesses’ demand deposits have not contributed positively to foreign-currency deposit inflows. Developments in business time deposits have provided a lower contribution than in the previous year.

Demand deposits showed higher growth rates over the last two months of the year, but due to their small share in deposit structure, they made a low impact on the performance of foreign-currency deposits. The ratio of demand deposits to total foreign-currency deposits reached 20.3%, about 2.3 percentage points less than in December 2010. The ratio of households’ foreign-currency deposits to total foreign-currency deposits increased during the year, peaking 84% in November, from 80% at year-start.

3. DEVELOPMENTS IN LOANS

Private sector credit performed positively in 2011. Monthly net flows, adjusted for the exchange rate effect, averaged 10% higher than in 2010 and its annual change has trended up, reaching 14.0% in October (12.7%, exchange rate effect adjusted). In November, the annual credit growth rate decreased to 10.9%, mainly due to the base effect stemming from high credit growth in previous year’s November and its pass-through to annual growth rates in the subsequent months. By currency and borrower, this effect was present in businesses’ foreign-currency loan portfolio.

ALL-denominated loans continued to perform positively in October and November, similarly as in the previous months. About 80% of private-sector loan portfolio expansion over these two months was in ALL. Its annual growth rate averaged 17.6%, from 16.9% and 15.6%, respectively, in Q3 and Q2. ALL-denominated loans to businesses and households registered upward

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2 The figures presented in the credit analysis presented in this session are adjusted for the exchange rate effect.
3 Private sector credit accounted for 97% of total credit.
annual growth rates. The major share of ALL-denominated loans was extended in the form of working-capital loans to businesses.

The increased preference for ALL-denominated loans has been present for 2-3 years from now, encouraged mainly by banks in the function of good management of exchange rate risk, but also by borrowers’ awareness. This behaviour has been manifested in all types of loans, but particularly in business investment and mortgage loans, which have traditionally been dominated by foreign currency. As a consequence, the share of ALL loans in total private sector loans reached 37% in November, up about 2 percentage points from end-2010 and 8 percentage points from end-2008.

Annual growth of foreign-currency credit to the private sector, after peaking 10.5% in August-September, slowed down to 9.9% and 7.2%, respectively, in October and November. Besides the afore-mentioned base effect, this
slowdown has also reflected the more contracted performance of this portfolio in the last two months. In general, in 2011, foreign-currency credit grew less than the previous year and was volatile among quarters. It performed positively in Q1 and Q3, while its growth was low in Q2 and in October-November.

Business demand is the main source of its growth, while foreign-currency lending to households is limited. Besides the banks’ approach, households appear more prudent in terms of using foreign-currency denominated loans.
1. SELECTED ECONOMIC FIGURES AND MONETARY POLICY ORIENTATION IN ADVANCED ECONOMIES

Global economic growth rates have decelerated in the recent months. The severe tensions in the financial markets arising from the sovereign debt crisis in many advanced economies have impacted the overall confidence climate of businesses and consumers, thus curbing the economic recovery further. The advanced economies in the euro area recorded modest growth rates, signalling the possible return of the economic downturn in later periods. The delay in finding a solution to the debt crisis acknowledged and supported by all major political and economic actors has conditioned the economic performance and is expected to affect it in the following year as well. CEE\(^1\) countries recorded low economic growth rates. The high growth rates recorded by many of these countries in the previous periods have now been replaced by moderate growth rates and below the agents’ expectations. The combined effects of the 2008-09 crisis and the sovereign debt concerns emerging in a number of euro-area countries have affected many important economic sectors the recovery of these countries was relying on. The inflationary pressures were subdued in the euro area and in most CEE countries. The exchange rates of the currencies of many CEE countries are pursuing a depreciation tendency, whilst investor perception of government debt securities in the financial markets is becoming more critical. The frail equilibriums characterizing many of these economies increase the perceived risk from the pass-through of euro area’s crisis effects.

Euro area

The sovereign debt crisis in the euro area has had an adverse impact on the economic performance of Europe and beyond, and has fuelled heightened uncertainty in the financial markets. The latest key policy rate cuts by the ECB have been interpreted as efforts to boost economic activity and need to offer more convenient financing conditions for the banking system. Direct and indirect indicators show that euro area’s economy is likely to have contracted in the last quarter of 2011. Unemployment has edged upwards starting from mid-2011 to later stand at 10.3% in the last months. Inflation marked 3% in the third quarter and in December, it slightly fell to 2.8%. With the deceleration in the economic growth, the underlying price pressures should remain limited. Euro area’s economic recovery in the last two years has been mainly driven by exports, fiscal stimulus, investment and domestic consumption. The

\(^1\) Central and Eastern Europe.
deterioration in the sovereign debt crisis has had an adverse impact on these items since obligatory rigorous fiscal policies leave no space for governments to stimulate the growth. The rising uncertainty has dampened consumer spending and demand for investment and lastly, the euro area sovereign debt crisis spillover effects on the global economy have contributed to a moderate growth of external demand. Concerning the financial markets, the sovereign debt crisis has had an adverse impact on the banking system’s soundness, since it has raised banks’ financing costs and has generated instability in the world stock markets.

Table 1 Key interest rates and use of instruments in advanced economies

<table>
<thead>
<tr>
<th>Inflation target</th>
<th>Euro area (ECB)</th>
<th>USA (Fed)</th>
<th>UK</th>
<th>Japan</th>
</tr>
</thead>
<tbody>
<tr>
<td>Key interest rate changes</td>
<td>03.11.11 (-0.25)</td>
<td>20.09.11 (0.00)</td>
<td>09.11.11 (0.00)</td>
<td>07.10.11 (0.00)</td>
</tr>
<tr>
<td></td>
<td>05.12.11 (-0.25)</td>
<td>01.11.11 (0.00)</td>
<td>07.12.11 (0.00)</td>
<td>15.11.11 (0.00)</td>
</tr>
<tr>
<td></td>
<td>12.01.12 (0.00)</td>
<td>13.12.11 (0.00)</td>
<td>11.01.12 (0.00)</td>
<td>20.12.11 (0.00)</td>
</tr>
<tr>
<td>Actual interest rate</td>
<td>1.00%</td>
<td>0-0.25%</td>
<td>0.50%</td>
<td>0-0.1%</td>
</tr>
<tr>
<td>Latest inflation rate</td>
<td>2.7%</td>
<td>3.4%</td>
<td>4.2%</td>
<td>-0.50%</td>
</tr>
<tr>
<td>Expected MPC meetings</td>
<td>9 February</td>
<td>24 January</td>
<td>8-9 February-8 March</td>
<td>23-24 January</td>
</tr>
<tr>
<td></td>
<td>8 March</td>
<td>13 March</td>
<td>4-5 April</td>
<td>13-14 February</td>
</tr>
<tr>
<td></td>
<td>4 April</td>
<td>24 April</td>
<td>12-13 March</td>
<td></td>
</tr>
<tr>
<td>Future events</td>
<td>16 February</td>
<td>29 February</td>
<td>16 February</td>
<td>15 February</td>
</tr>
<tr>
<td></td>
<td>15 March</td>
<td>11 April</td>
<td>Inflation Report</td>
<td>14 March</td>
</tr>
</tbody>
</table>

1 December 2011 for the euro area and UK, and November 2011 for USA and Japan.

2 Source: “Understanding of Medium- to Long-Term Price Stability”, Bank of Japan

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

Source: Respective central banks

The ECB cut its key rate twice during the last quarter and it has re-employed unconventional monetary policy instruments. Purchases of Government bonds in the secondary market and the conduct of long-term refinancing operations with a 3-year maturity were some of the ECB’s actions in order to relax and stabilise the financial market and support bank lending activity. In December, the EBA published the results of the stress tests for the major European banks. The results showed that these banks need to strengthen their regulatory capital by issuing new shares or bonds. This is expected to take place by June 2012 and the required amounts for capital enhancement are considerable. Greece tops the list of countries, where banks are recommended to enhance their capital by EUR 30 billion, followed by Spain, Italy and Germany. The difficult situation that the European stock markets are going through, the combination and the rapid pass-through of tensions from one market segment to another, and the perceived fragility of many countries with respect to sovereign debt management are some of the factors that hinder European banks’ approach in the financial market during this period. Euro area political leaders’ efforts in establishing automatic mechanisms and instruments to weather these crises are facing natural challenges arising from these treaties. In the meantime, the long time perceived by the market agents in reaching an agreement is fuelling uncertainty among the international investors.

2 European Banking Authority.
USA

The U.S. economy performed positively during 2011, although slightly lower than projections in early 2011. The U.S. economy recorded positive growth rates in 2011 Q3, and direct and indirect indicators show that it will continue to be positive in Q4 as well. The recently published Beige Book\(^3\) shows that the U.S. economy has recovered and has recorded positive growth rates. The declining unemployment rate, the higher private consumption and the industrial production provide evidence for a positive momentum of the U.S. economy over these months. Worth noting is that the residential sector continues to remain weak, while the inflationary pressures have, by and large, been subdued. Balance of payments figures for the third quarter have improved and the current account deficit has narrowed. The Federal Reserve has not changed its key policy rate during this period. At the end of September, it decided to sell, by the end of June 2012, the short-term debt securities of the U.S. Government holding in its portfolio and to later shift the sales toward long-term securities.

The sovereign debt crisis facing the old continent extended its effect to the U.S. stock markets. The U.S. market agents fear that EBA’s capital enhancement requirement for euro area banks will tighten lending to the economy further, which in turn may result in a negative spiral and pass through to the U.S. economy as well. U.S. banks’ exposure to the debt securities of euro area’s peripheral countries is considered manageable, while their interconnection with euro area’s banks appears more challenging.

2. SELECTED ECONOMIC FIGURES, INFLATION AND MONETARY POLICY ORIENTATION IN SELECTED CEE COUNTRIES\(^4\)

Similar to other EU member states, the economic growth rates in the CEE countries have begun to decelerate. GDP growth rates in the third quarter provided evidence for a non-uniform performance of the three CEE countries. The economic growth decelerated considerably in the Czech republic and Hungary, while maintaining almost the same rates in Poland.

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Czech Republic</td>
<td>1.7</td>
<td>2.9</td>
<td>2.0</td>
<td>1.8</td>
</tr>
<tr>
<td>Hungary</td>
<td>2.8</td>
<td>2.8</td>
<td>1.8</td>
<td>1.7</td>
</tr>
<tr>
<td>Poland</td>
<td>3.8</td>
<td>3.6</td>
<td>3.8</td>
<td>3.0</td>
</tr>
</tbody>
</table>

These countries are all export-oriented and the Western European countries are their main market. The lower demand from the latter and the respective tight fiscal policies in the CEE countries are expected to decelerate their economic growth.

\(^3\) Beige Book, January 2012
\(^4\) This region includes the Czech Republic, Hungary and Poland.
\(^5\) World Economic Outlook, April, September, IMF.
economic growth. These expectations are reflected in the IMF’s downward revision to their GDP growth forecast in September.

The inflation rates are showing an increasing trend. In the Czech Republic, the inflation rate has been within the central bank’s target most of the times, whilst in the other two countries inflation still remains above the target. However, the inflation dynamics does not appear a risk for the moment considering the weak economic growth in this region, although Hungary’s central bank has begun to take measures with regard to this tendency.

2.1 Economic Activity

**Rating CZECH REPUBLIC**

<table>
<thead>
<tr>
<th>Rating</th>
<th>Moody’s</th>
<th>S&amp;P</th>
<th>Fitch</th>
</tr>
</thead>
<tbody>
<tr>
<td>A1 (stable)</td>
<td>A (positive)</td>
<td>A+ (positive)</td>
<td></td>
</tr>
</tbody>
</table>

The Czech Republic’s GDP expanded by 1.2% in 2011 Q3 compared to 2.2% in the previous quarter. Among other factors this deceleration reflected mainly the fall in private and public consumption beyond expectations as well as the tightening of fiscal conditions and the sluggish improvement of the labour market conditions. In addition, the euro area’s crisis effect on net exports and investments has provided downward pressures to the economic activity. The export growth was lower than projected reflecting the fall of demand from the Czech Republic’s trading partners. This component was, however, the main driver of economic growth in the third quarter. The fiscal measures are expected to decelerate domestic demand further and increase the level of spare capacities. Economic growth is assessed to have been driven by non-inflationary factors.

**Rating HUNGARY**

<table>
<thead>
<tr>
<th>Rating</th>
<th>Moody’s</th>
<th>S&amp;P</th>
<th>Fitch</th>
</tr>
</thead>
<tbody>
<tr>
<td>Ba1 (negative)</td>
<td>BB+ (negative)</td>
<td>BB+ (negative)</td>
<td></td>
</tr>
</tbody>
</table>

Hungary’s GDP expanded by 1.4% y-o-y in 2011 Q3 compared to 1.5% in Q2 and 2.3% in Q1. Net exports had been the main driver of economic growth in the previous periods. They dropped due to the unfavourable economic developments outside Hungary, while in real terms the other components – private consumption, private investment and public spending – were lower than in the previous year. The depreciation of the domestic currency is seen to be also a potential source of vulnerability of the domestic financial system and the broad economy, since a considerable portion of the Hungarian private debt is denominated in foreign currency.

**Rating POLAND**

<table>
<thead>
<tr>
<th>Rating</th>
<th>Moody’s</th>
<th>S&amp;P</th>
<th>Fitch</th>
</tr>
</thead>
<tbody>
<tr>
<td>A2 (negative)</td>
<td>A- (stable)</td>
<td>A- (stable)</td>
<td></td>
</tr>
</tbody>
</table>

The data on Poland’s economy continue to be positive. GDP expanded by 4.2% in 2011 Q3 compared to 4.3% in Q2. What is most important is that
the economic growth has been balanced by both private consumption and the accelerated growth rate of investments. Despite the sluggish economic growth in Poland’s trading partners, domestic demand has been relatively high, thus offsetting the lower foreign demand. Nevertheless, the deceleration in the European growth rate is expected to affect Poland’s economy, which has also led to the downward revision of growth forecasts for 2013\(^6\).

2.2 Inflation and Monetary Policy

Compared to the other CEE countries, inflation in the Czech Republic is low and within the tolerance band of the central bank’s target. Since October, it has ranged between 2.3% and 2.5%. According to the central bank, the inflationary pressures are balanced; thereby no monetary policy changes are required to be made. The Czech National Bank kept the two-week repo rate unchanged at a record low of 0.75%. A change in the inflationary expectations, due to the fiscal measures projected to be taken by the Government, is a factor that may jeopardise the performance of inflation. The central bank projection of one-year-ahead inflation put the inflation rate in a range between 2% and 3%. It is expected to fall below 2% in 2013, due to the fading-out effect of the VAT rise in the beginning of 2012.

In Hungary, the inflation rate marked 4.1% in December, which is above the central bank’s projections. The Hungarian National Bank raised the key interest rate for the second month in a row to 7.0% from 6.0%. Due to Hungary’s elevated risk premium assigned by the rating agencies and the weakening of the exchange rate, there was heightened risk for the central bank to miss the inflation target. In addition, the central bank has stated in its statement that output is expected to remain below its potential for the next two years. Concerning core inflation, as projected in the quarterly inflation reports, it is expected to be balanced by the weak demand and the high level of the unemployment rate.

\(^6\) Poland’s central bank projects that GDP will grow by 3.0% in 2013.
In Poland, the annual inflation rate showed an increasing trend in the last quarter of 2011. In November and December, it marked 4.8% and 4.6% respectively, remaining, however, below the maximum rate of 5% of May. The National Bank of Poland kept the key interest rate unchanged at 4.50% (since June 2011). The inflationary pressures will remain high due to the immediate price rise in the previous period (VAT rise by 1% and the low comparative base) and the depreciation of the Polish zloty in the recent months. According to the central bank, the introduction of the severe fiscal measures in 2011 and the deceleration in the global economy will lead to the decrease and balancing of the inflation rates in the periods ahead.

3. SELECTED ECONOMIC FIGURES, INFLATION AND MONETARY POLICY ORIENTATION IN SELECTED SEE COUNTRIES AND TURKEY

SEE countries recorded lower economic growth (though slightly higher than expected) in 2011 Q3. Turkey’s GDP expanded by 8.2% y-o-y, hence continuing to top the list of countries in this region with the highest GDP growth. Romania’s GDP also expanded by 4.4% compared to 1.7% and 1.4% in Q1 and Q3, respectively. At more negative tones, Bulgaria and Serbia registered lower annual growth rates, confirming the deceleration in their economic activity during this quarter.

It seems that this region will be affected in the fourth quarter by the difficulties facing the trading partners in the rest of Europe. The strong economic and financial linkages between this region and the advanced Western European countries have exposed it to challenges caused by the retardment in finding a definitive solution for the sovereign debt crisis. Figures on sales and production show that they are moving into negative territory. Confidence survey data appear also non-optimistic, whilst the tightening of lending conditions in these

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*This region includes Bulgaria, Macedonia, Romania, Serbia, and Turkey for study purposes.*
countries is expected to affect investment and domestic consumption. The deceleration in the economic growth is also expected to be affected by the contraction in fiscal spending, while the economy is expected to be driven by the monetary easing and other measures for supporting lending activity. The former is considered hard to take place in countries where the currency is continuously depreciating (Turkey).

3.1 Economic Activity

**Rating BULGARIA**

<table>
<thead>
<tr>
<th>Baa2 (stable)</th>
<th>BBB (stable)</th>
<th>BBB-(positive)</th>
</tr>
</thead>
<tbody>
<tr>
<td>(Moody’s)</td>
<td>(S&amp;P)</td>
<td>(Fitch)</td>
</tr>
</tbody>
</table>

Bulgaria recorded the lowest GDP growth rate in the last four quarters in 2011 Q3. According to official data, Bulgaria’s GDP expanded by 1.6% in Q3, compared to 2.0% in Q2 and 3.3% in Q1 y-o-y. Unlike the previous periods, when net exports had provided the major contribution to economic growth, in 2011 Q3, this indicator was negative (The growth rate of exports is considered positive due to the fast diversification of Bulgarian exports to non-EU member states. These countries’ share increased to 40% in November). Investments decreased during this period, although Bulgaria has withdrawn considerable investment funds from the EC. The construction sector, in particular, does not seem to have exited the recession phase following the collapse in the real estate market in 2008. Private consumption, the largest GDP component, grew by 1.6% in 2011 Q3, compared to 1.4% in Q2 y-o-y. The growth in private consumption was driven by the increase in real disposable income following the continuous decrease of the inflation rate.

In December, the IMF revised Bulgaria’s GDP growth forecast downward to 1.9% for 2011 (from 2.5%) and to 1.3% for 2012 (from 3.0%).

**Rating MACEDONIA**

<table>
<thead>
<tr>
<th>- (Moody’s)</th>
<th>BB (stable)</th>
<th>BB+ (stable)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>(S&amp;P)</td>
<td>(Fitch)</td>
</tr>
</tbody>
</table>

Macedonia’s GDP growth rates decelerated to 2.3% in 2011 Q3, compared to 5.0% in Q2. The economic performance was mostly determined by industrial production, which recorded downward annual growth rates. The same trend seems to have persisted in the fourth quarter as well. External sector data were positive. The current account balance was more positive than expected (0.6% of GDP) due to the improved private transfers. According to the central bank, the monetary data and the performance of inflation are within the monetary authority’s projections and in line with other real economy data.

**Rating ROMANIA**

<table>
<thead>
<tr>
<th>Baa3 (stable)</th>
<th>BB+ (stable)</th>
<th>BBB-(stable)</th>
</tr>
</thead>
<tbody>
<tr>
<td>(Moody’s)</td>
<td>(S&amp;P)</td>
<td>(Fitch)</td>
</tr>
</tbody>
</table>

With its 4.4% y-o-y growth rate in 2011 Q3, Romania recorded the highest GDP growth among the EU member countries (EU-27 average is 1.4%).
agriculture sector made the major contribution to the GDP growth, while the other sectors also showed better-than-expected performance. Economic activity was driven by the improvement in private consumption and investment. Both these components recorded positive annual growth rates for the first time since 2008. The fall in food and energy prices contributed to the increase in real income, thus driving the private consumption up. Investments were supported by the recovery in the construction sector, which, however, remains highly volatile. By contrast, net exports provided an adverse contribution due to the fast increase in imports.

### Rating SERBIA

<table>
<thead>
<tr>
<th>Unrated (Moody’s)</th>
<th>BB (stable) (S&amp;P)</th>
<th>BB- (stable) (Fitch)</th>
</tr>
</thead>
</table>

Serbia’s GDP growth rates continued to decelerate considerably in 2011 Q3. It expanded by 0.7% y-o-y compared to 2.2% in the previous quarter. The sector breakdown shows that the contraction of private consumption, despite the real increase in income, played a negative role in this performance. Private consumption was largely affected by the relatively high food prices, high unemployment rates (22% in April) and the tight lending standards. In addition, the fiscal stimulus was weak during this period, net exports’ contribution during this quarter was 0, compared to the positive contribution by 0.6 pp in the previous quarter. The dynamics of export growth were negatively affected by the appreciation trend of the domestic currency in the third quarter and the fall of external demand from the EU countries. Private investments provided positive contribution to Serbia’s economic activity.

### Rating TURKEY

<table>
<thead>
<tr>
<th>Ba2 (Moody’s)</th>
<th>BB (positive) (S&amp;P)</th>
<th>BB+ (stable) (Fitch)</th>
</tr>
</thead>
</table>

Turkey’s relatively high economic growth persisted in 2011 Q3 as well. GDP expanded by 8.2% (y-o-y) during this quarter, compared to 8.8% in the previous quarter, recording, however, higher-than-expected growth rates. Data on domestic demand show that it slowed down and the lower imports data confirm part of this. By contrast, the increase in exports led to a positive contribution of net exports for the first time since 2009 Q3. Consequently, the current account deficit corrected further. Data on retail sales show the further deceleration of domestic demand in 2011 Q4. The tightening of the monetary conditions by the central bank will affect the domestic demand with time lags, which, coupled with the fall of foreign demand (since the main destination of Turkish exports is the EU) lead to a lower projected GDP growth in 2011 Q4.

The higher current account deficit and inflation, as well as the signals for the deterioration of the economies in the region, pushed the Fitch rating agency to downgrade Turkey’s rating from “positive” to “stable”. Fitch’s move, however, kept Turkey’s rating at BB+.
Table 3 Key interest rate and use of monetary policy instruments

<table>
<thead>
<tr>
<th></th>
<th>Czech Republic</th>
<th>Poland</th>
<th>Hungary</th>
<th>Romania</th>
<th>Serbia</th>
<th>Turkey</th>
</tr>
</thead>
<tbody>
<tr>
<td>Inflation target</td>
<td>2.0% (± 1%)</td>
<td>2.5% (± 1%)</td>
<td>3.0% (± 1%)</td>
<td>3.5% (± 1%)</td>
<td>4.9% (± 1.6%)</td>
<td>5.5% (± 2%)</td>
</tr>
<tr>
<td>Latest meetings and changes in the key interest rate</td>
<td>02.11.11 (0.00)</td>
<td>07.12.11 (0.00)</td>
<td>29.11.11 (+0.50)</td>
<td>03.11.11 (-0.25)</td>
<td>10.11.11 (-0.75)</td>
<td>23.11.11 (0.00)</td>
</tr>
<tr>
<td>Actual interest rate</td>
<td>0.75%</td>
<td>4.50%</td>
<td>7.0%</td>
<td>5.75%</td>
<td>9.75%</td>
<td>5.75%</td>
</tr>
<tr>
<td>Latest inflation rate*</td>
<td>2.4%</td>
<td>4.6%</td>
<td>4.1%</td>
<td>3.14%</td>
<td>7.0%</td>
<td>10.45%</td>
</tr>
<tr>
<td>Expected MPC meetings</td>
<td>02.02.12</td>
<td>08.02.12</td>
<td>10.01.12</td>
<td>02.02.12</td>
<td>09.02.12</td>
<td>24.01.12</td>
</tr>
</tbody>
</table>

*December 2011
Source: Respective central banks

3.2 Inflation and Monetary Policy

The inflation rate in Bulgaria continued the downward trend as a result of the fall in food and energy prices, which have the largest share in households’ consumer basket. The downward pressures on inflation were backed also by the low consumption. At the same time, deposits growth in the banking system recorded relatively high rates evidencing thus the private sector’s propensity to save.

![Chart 4 Annual inflation rate](source)

The return of the annual inflation rate to within the target band of 3.0% +/-1% in 2011 Q3 supported the National Bank of Romania decision to cut the key interest rate by 0.25% to 6.00% in November. As explained in the inflation report, the performance of inflation was affected by the fall in food prices, which had shown high volatility, and the fading-out of the first-round effect of the VAT rate hike. In view of the weak domestic inflationary pressures and in order to anchor the inflationary expectations within the central bank’s target, the NBR Board decided to take this measure in order to alleviate the monetary conditions. In December, the annual inflation rate fell to 3.1%.
After reaching a peak rate in April (14.7%) due to supply-side factors, inflation in Serbia pursued a downward trend in the next quarters and stabilized at single-digit rates. Food price items contributed to lowering the annual inflation rates during this period. Subsequently, the inflation rates got closer to the central bank’s target. The lower inflation was driven by the decelerated domestic demand and the decrease in inflation expectations. In December, the annual inflation rate marked 7.0% compared to 9.3% in September.

Since June 2011, when the National Bank of Serbia signalled the beginning of a cycle of monetary policy easing, the key interest rate has been cut six times by a total of 275 basis points from 12.50% to 9.75% in December. The last two changes, by -25 basis points each, were made in November and December.

According to the central bank, the easing of monetary conditions precedes the projection for the decrease of inflation to within the target tolerance band of 2.5%-5.5% in the first quarter of 2012. The disinflationary pressures are expected to be generated from a weak domestic demand, decrease in inflation expectations and the decision to change some administered prices at a later period. On the other hand, the central bank evidenced two sources of risk that may condition the monetary policy in the future: developments in the external environment and developments in the fiscal sector, which precede the parliamentary elections of May 2012.

The inflation rate in Turkey increased to 10.45% in December, markedly above the central bank’s target of 5.5%. It was largely driven by the base effect in unprocessed food prices and the rise in energy prices coupled with the depreciation of the Turkish lira, and the rise in some administered prices. The central bank had projected and knew that it would miss the target. In October, it signalled the tightening of monetary conditions by widening the standing facilities corridor (the overnight lending rate was increased by 350 basis points). Within this corridor, the central bank supplies the banking
system with liquidity in days when it does not conduct regular one-week repo auctions. Parts of this strategy are also the efforts to curb the depreciation of the Turkish lira through foreign exchange market interventions. Given the time lags in the monetary policy transmission mechanism, the second-round effects are expected to be contained in the period ahead. Inflation is forecasted to maintain a descending tendency and converge towards the 5.0% target during 2012. The central bank has also stated that the monetary policy tightening will persist in order to contain the inflation expectations.

4. EXCHANGE RATE

The countries under review have generally shown a depreciation trend of their domestic currencies. The downgrade in Hungary’s rating in November to Ba1 (speculative), being placed on a negative outlook by Moody’s, and the high exposure of public debt to the international market pushed the depreciation of the Hungarian forint further. In Poland, the central bank is facing the depreciation of the Polish zloty and has intervened in the foreign exchange market in favour of the domestic currency. The higher perceived risk on Poland, against a background of the deterioration of the sovereign debt crisis in Europe, has pushed investors to sell the Polish zloty. In the second half of the year, the Hungarian forint depreciated by 11.7% and the Polish zloty by 10.8%.

The Turkish lira has remained sensitive due to deepening of the current account deficit and the central bank’s hesitation to increase the interest rate and its differential with the advanced economies. While the foreign demand remains subdued and the deceleration effects of domestic demand become more pronounced, the cumulative depreciation of the Turkish lira has started to reflect considerably in the import prices. Turkey’s central bank has been present in the foreign exchange market in order to somehow curb the depreciation of the Turkish lira. Concerning Serbia, since mid-2011, the Serbian dinar has depreciated by 0.5%, hence considerably less than the other currencies in the
region. After the sudden decrease of the key rate in December, the Serbian dinar began to depreciate, pushing, in turn, the central bank to intervene in the foreign exchange market at the end of the year.

Chart 7 Daily Euro/domestic currency exchange rate in CEE countries (base index – January 2010)

5. MISCELLANEOUS

- In October, the ECB announced the modalities of the new covered bond purchase programme that will be carried out in the primary and secondary markets for a one-year period beginning from November 2011, for an intended amount of EUR 40 billion.

- In the beginning of November, Mr. Mario Draghi, former Governor of the Banca d’Italia, took up his duties as the President of the ECB. He succeeded Mr. Jean-Claude Trichet, whose term as the President of the ECB had terminated in October.

- In December, six central banks – Fed, ECB, Bank of Canada, Bank of England, Bank of Japan and the Swiss National Bank agreed to lower the pricing on the existing temporary US dollar liquidity swap arrangements by 50 basis points. They also approved the extension of the authorisation of these swap arrangements to February 2013 and agreed to establish temporary bilateral liquidity swap arrangements.

- In December, the ECB released a plan of additional enhanced credit support measures to support bank lending and relax the money markets. In particular, the ECB decided to:

  a. Conduct two longer-term refinancing operations with a maturity of 36 months and the option of early repayment after one year. These operations will be conducted in December 2011 (conducted) and February this year.
b. Temporarily discontinue the fine-tuning operations carried out on the last day of each maintenance period.

c. Reduce the reserve ratio from 2% to 1% starting from January 2012.

d. Increase collateral availability accepted in the liquidity injection operations.

- On 22 December, the Governing Council of the ECB adopted its opinion on the draft legislation regarding the Magyar Nemzeti Bank, proposed by the Hungarian Government and scrutinized and voted by the Hungarian Parliament. The Governing Council of the ECB expressed the concern that the provisions in this draft law could undermine the central bank’s independence and that they are not in line with the European legislation in this area. The Governing Council of the ECB requested the Hungarian authorities to bring their consultation practice into line with the requirements of European Union law and to respect the obligation to consult the ECB.

- In the last quarter of 2011, staff teams from the European Commission, European Central Bank, and the International Monetary Fund held their regular meetings to assess the fiscal and economic consolidation plans of Greece, Portugal and Ireland. The analysis of this mission made a positive assessment of the steps and commitment of the respective governments in terms of observing the fiscal consolidation objectives. It, however, pointed out that many indicators are out of reach for 2011, while they are more likely for 2012 and 2013. The acceleration in carrying out structural reforms in these countries and the rigorous approach towards public spending will enable the quick recovery of the debt level and fiscal deficit to within acceptable parameters. The results of these analyses confirmed the continuation of the loan facilities extended by these institutions (ECB, EC, and IMF).
I. BALANCE OF PAYMENTS HIGHLIGHTS\(^1\)

Over the third quarter of 2011, the overall balance of payments ended with an increase of foreign assets of EUR 56.4 million. The net position of the current account recorded a deficit of about EUR 272.4 million, about 13.1% higher compared to the same period of the previous year. The deficit was estimated at about 11.4% of nominal GDP\(^2\), or about 1.2 percentage points higher than the level of this ratio in the third quarter of 2010. Foreign currency inflows in the capital and financial account resulted about EUR 218.5 million, up by about 15.8% year-on-year. The surplus recorded in this account during the third quarter of 2011 financed about 80.2% of the current deficit recorded in this period.

Table 1 Balance of Payments items

<table>
<thead>
<tr>
<th></th>
<th>Q3 ’10</th>
<th>Q4 ’10</th>
<th>Q1 ’11</th>
<th>Q2 ’11</th>
<th>Q3 ’11</th>
</tr>
</thead>
<tbody>
<tr>
<td>Current account (EUR mln)</td>
<td>-245.2</td>
<td>-373.6</td>
<td>-229.6</td>
<td>-324.4</td>
<td>-272.4</td>
</tr>
<tr>
<td>Current account (% to GDP)</td>
<td>-10.2%</td>
<td>-16.7%</td>
<td>-10.9%</td>
<td>-13.5%</td>
<td>-11.4%</td>
</tr>
<tr>
<td>Trade balance</td>
<td>-595.9</td>
<td>-584.9</td>
<td>-408.5</td>
<td>-581.4</td>
<td>-593.1</td>
</tr>
<tr>
<td>Exports, f.o.b.</td>
<td>270.3</td>
<td>305.9</td>
<td>370.6</td>
<td>330.8</td>
<td>344.1</td>
</tr>
<tr>
<td>Imports, f.o.b.</td>
<td>-866.2</td>
<td>-890.7</td>
<td>-779.1</td>
<td>-912.2</td>
<td>-937.2</td>
</tr>
<tr>
<td>Services balance</td>
<td>180.0</td>
<td>5.2</td>
<td>-32.2</td>
<td>-11.0</td>
<td>119.7</td>
</tr>
<tr>
<td>Credit</td>
<td>661.0</td>
<td>412.5</td>
<td>304.4</td>
<td>367.8</td>
<td>615.8</td>
</tr>
<tr>
<td>Debit</td>
<td>-481.0</td>
<td>-407.2</td>
<td>-336.6</td>
<td>-378.8</td>
<td>-496.2</td>
</tr>
<tr>
<td>Travel - net</td>
<td>171.3</td>
<td>17.3</td>
<td>-43.5</td>
<td>-19.9</td>
<td>82.9</td>
</tr>
<tr>
<td>Income balance</td>
<td>-19.9</td>
<td>-31.6</td>
<td>14.7</td>
<td>22.2</td>
<td>17.6</td>
</tr>
<tr>
<td>Credit</td>
<td>70.8</td>
<td>73.1</td>
<td>60.0</td>
<td>69.5</td>
<td>74.3</td>
</tr>
<tr>
<td>Debit</td>
<td>-90.7</td>
<td>-104.7</td>
<td>-45.3</td>
<td>-47.3</td>
<td>-56.6</td>
</tr>
<tr>
<td>FDI income - net</td>
<td>-73.8</td>
<td>-73.7</td>
<td>-15.0</td>
<td>-9.5</td>
<td>-20.8</td>
</tr>
<tr>
<td>Current transfers</td>
<td>190.6</td>
<td>237.7</td>
<td>196.4</td>
<td>245.9</td>
<td>183.4</td>
</tr>
<tr>
<td>Credit</td>
<td>233.0</td>
<td>280.1</td>
<td>238.0</td>
<td>287.6</td>
<td>225.9</td>
</tr>
<tr>
<td>Debit</td>
<td>-42.4</td>
<td>-42.4</td>
<td>-41.6</td>
<td>-41.7</td>
<td>-42.5</td>
</tr>
<tr>
<td>Worker’s remittances - net</td>
<td>135.1</td>
<td>165.1</td>
<td>153.1</td>
<td>189.4</td>
<td>132.6</td>
</tr>
<tr>
<td>Capital and financial account (EUR mln)</td>
<td>193.7</td>
<td>433.1</td>
<td>184.6</td>
<td>192.7</td>
<td>218.5</td>
</tr>
<tr>
<td>Capital and financial account (% to GDP)</td>
<td>8.0%</td>
<td>19.2%</td>
<td>8.7%</td>
<td>8.0%</td>
<td>9.2%</td>
</tr>
<tr>
<td>Financial account</td>
<td>22.6</td>
<td>30.2</td>
<td>19.1</td>
<td>31.5</td>
<td>6.5</td>
</tr>
<tr>
<td>FDI - net</td>
<td>171.1</td>
<td>402.8</td>
<td>165.5</td>
<td>161.2</td>
<td>212.0</td>
</tr>
<tr>
<td>Portfolio investments - net</td>
<td>-6.6</td>
<td>286.8</td>
<td>-21.8</td>
<td>-23.2</td>
<td>-54.2</td>
</tr>
<tr>
<td>Other investments - net</td>
<td>-74.8</td>
<td>-134.9</td>
<td>145.2</td>
<td>-37.1</td>
<td>99.8</td>
</tr>
<tr>
<td>Errors and omissions</td>
<td>111.7</td>
<td>66.2</td>
<td>-32.1</td>
<td>130.1</td>
<td>110.3</td>
</tr>
<tr>
<td>Reserve assets</td>
<td>-60.2</td>
<td>-125.7</td>
<td>77.1</td>
<td>1.7</td>
<td>-56.4</td>
</tr>
</tbody>
</table>

Source: Balance of Payments, Bank of Albania

\(^1\) The latest data of the Balance of Payments cover 2011 Q3. Also, data of 2010 are reviewed.
1.1 CURRENT ACCOUNT

The net position of the current account during the third quarter of 2011 recorded a deficit of EUR 272.4 million. After the slight narrowing in annual terms over the first quarter of 2011, the current account deficit widened annually for the second consecutive quarter. During the quarter under analysis the current account deficit rose by about 13.1% y-o-y. The deficit was estimated at 11.4% to nominal GDP or about 1.2 percentage points higher than its level during the same period of the previous year. Unlike the two first quarters of year, over the third quarter the current account dynamics was broadly determined by the net exports and income account performance.

In the analysis of the current account according to its main items, net exports widening was the main factor behind its worsening over the third quarter of 2011. The narrowing trade deficit by 0.5% y-o-y failed to counterbalance the negative effect of services account balance worsening. Their combined net position largely contributed to the deepening of the net exports deficit by 13.8% y-o-y.

The external sector main indicators performance over the third quarter of 2011, shows a narrowing of the net exports deficit in real terms\(^3\), compared to the same period of the previous year. Net exports deficit narrowing was due to lower imports of goods and services in real terms by about 4.2% and higher exports by about 8.6% y-o-y. Developments in the import and export balance of goods and services in real terms are assessed to have been materialised in a positive contribution of this component to aggregate demand growth during this period.

Note: A positive value indicates that the factor contributed to the current account deficit widening and a negative value indicates that the factor contributed to the current account deficit narrowing.

\(^3\) To switch from nominal to real terms of goods imports and exports the Unit Value Index obtained from external trade data in volume was used. Whereas, Consumer Index Price of Services, estimated by the Bank of Albania, was used for services imports and exports.
As a result of trade flows in goods and services, the degree of economic openness of the country over the third quarter of 2011, pointed to 100.6%, 3.8 percentage points higher compared to the same period of the previous year.

After the deficit recorded over the first two quarters of 2011, services account ended with a surplus of EUR 119.7 million in the third quarter of the same year. The services account surplus narrowed by about 33.5% y-o-y, contributing by about 25.1 percentage points to the current account deficit widening.

Lower surplus registered in this account was mainly due to increased personal and business travelling expenses\(^1\) of residents abroad, by about 1 Travel services cover the highest share in services total income and expenses, by about 76.2% and 77.9%, respectively.
6.7% y-o-y. On the other hand, inflows from personal and business travelling services by non-residents in the country declined by about 12.0% during the period under analysis. In cumulative terms, the first nine months of 2011 were characterized by a notable decrease from EUR 177.6 million to EUR 19.5 million of net travel services balance. Developments in this sub-item of the services account in three- and nine-month terms for 2011 are estimated to be the effects of visa liberalization regime for Albania with Schengen countries. Other services (including mail, telecommunication, construction, computer, information and other services) recorded a positive balance of EUR 55.7 million from EUR 23.2 million in the previous year.

The net balance of income account resulted in a surplus of EUR 17.6 million during the third quarter of 2011, mainly due to lower foreign investment income outflows. After about two years that this account consistently recorded net deficit, in the first nine months of the year 2011 its balance resulted positive. The income account balance over the previous year resulted with a deficit of about EUR 45.2 million; during the first nine months of 2011 its surplus was about EUR 54.5 million. The improvement in the income account balance in three- and nine-month terms was mainly due to lower outflows of income, especially FDI incomes.

Over the third quarter of 2011, FDI’s income outflows decreased by about 70.3% y-o-y. Given the difficult current situation in European countries, particularly in Italy and Greece2, profits re-investment in Albania could be seen as more attractive than their repatriation to origin countries. Other investments net income continues to record negative values for the fourth consecutive quarter, mostly due to increased net interest repayments on public and private debt. In the third quarter of 2011, the net deficit of this sub-item of the income account resulted in deficit of about EUR -19.0 million, from the surplus of EUR

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2 According to 2008 available data, EU countries represent about 65.9% of foreign direct investments stock. Greece and Italy have the highest share of investments to total stock.
9.0 million in the previous year. Net interest payments to private and public debt in the considered quarter, have lowered country’s obligations by about EUR 23.3 million, while inflows decreased by about 78.7% in annual terms. Income from portfolio investment grew by about 46.5% y-o-y in the third quarter of 2011.

The surplus of current transfers account continued to narrow even during the third quarter of 2011, trend started since the fourth quarter of 2010. In the third quarter of 2011, this account surplus narrowed by about 4.2% in annual terms. Over the first nine months of 2011, current transfers account surplus decreased by about 8.6% relative to the same period in the previous year. The main sub – item of this account, workers’ remittances inflow, continued its annual downward trend for the fourth quarter on. In the current quarter, worker’s remittances (inflow) fell by about 2.0% y-o-y. The financing ratio to the trade balance was 22.9% or about 33.6 percentage points lower compared to the financing ratio registered in the same period of the previous year. Current transfers to the public sector have been falling as well by 51.4% y-o-y.

I.2 CAPITAL AND FINANCIAL ACCOUNT

During the third quarter of 2011, net capital and financial account surplus recorded EUR 218.5 million, or about 15.8% higher compared to the same period of the previous year. About Euro 6.5 million entered the country as grants for capital investments, and about EUR 212.0 million as financial inflows. Net capital and financial flows amounted to about 9.2% in terms of nominal GDP or about 1.2 percentage points higher than the ratio recorded in the same quarter of the previous year. In cumulative terms, over the first nine months of 2011, this account surplus was about 25.2% higher compared to the same period in the previous year.
Financial transactions during the third quarter of 2011 recorded a value of EUR 212.0 million, up by about 27.7% in annual terms. Residents’ financial liabilities to non-residents increased by about EUR 406.9 million during the analysed period, up by about 31.3% y-o-y. Our financial assets invested abroad grew by about EUR 194.9 million during the third quarter of 2011.

As a result of the financial flows in the items of assets and liabilities, the indicator of the country’s financial openness degree for the third quarter of 2011 was 25.3%, up by about 6.0 percentage points compared with its value in the corresponding period of the previous year.

Net foreign direct investments (inflow – outflow) during the third quarter of 2011 resulted in EUR 166.4 million, or about 32.8% lower compared to the same period of the previous year. In terms of nominal GDP net FDI’s represented about 7.0%. In cumulative terms, net FDIs during the first nine months of 2011 were 25.6% y-o-y lower compared to the same period of the previous year. According to FDI’s direction, similarly to the previous quarters, FDIs inflows prevailed. FDI’s inflows were about EUR 170.5 million, down by about 31.2% y-o-y. According to investment instrument, FDI inflows in the form of equity and re-invested earnings (shares) represented about EUR 202.6 million, about 20.0% lower compared to the same period of the previous year. During the third quarter of 2011, other capitals sub-item recorded a capital outflow in the form of inter-company loans of EUR 32.1 million. In the first quarter of 2011, this item recorded about EUR 115.1 million.

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3 The “Other capitals” instrument under foreign direct investments refers to borrowing and lending of funds, including debt and trade loans, between the direct investor and the direct investment enterprise, as well as between two direct investment enterprises having the same direct investor.
Excluding privatisation receipts during the third quarter of 2011, foreign direct investments inflows were about 31.2% lower y-o-y. Since 2010, receipts from privatization have given a lower contribution to the FDI’s growth in the country. Sectoral distribution of FDI in the third quarter of 2011 shows a concentration of them in hydro-carbon sector (about 46%), banking sector (about 16.0 %) and telecommunications (about 11%).

Net portfolio investments in the third quarter of 2011 increased domestic assets invested in foreign economies, by about EUR 54.2 million. In the quarter under analysis FDI’s outflows grew markedly by about EUR 57.1 million. Residents have mainly preferred to invest in debt securities. In cumulative terms, the first nine months of year 2011 recorded a growth of residents’ portfolio investments in foreign economies by about 50.5% y-o-y.

In the third quarter of 2011, other investments account marked a positive balance, contributing with about EUR 99.8 million to our liabilities toward the rest of the world. Financial flows direction in this account was determined primarily by non residential financial inflows invested in our country. Our financial liabilities (under other investments) increased by about EUR 233.4 million over the third quarter of 2011, mainly due to private and public borrowing. The latter resulted in EUR 109.6 million, from EUR 46.7 million in the same quarter the previous year. About 57.3% refer to the public sector and 42.7% to the private sector. Resident’s investments abroad increased mainly due to the improved liquidity situation in the banking system. The investments of the banking system in the form of currency and deposits and short-term loans rose respectively by EUR 114.8 and 21.6 million.

Reserve assets during the third quarter of 2011 increased by about EUR 56.4 million. At the end of September 2011, the stock of foreign reserves amounted to EUR 1,894.0 million, which is a sufficient level to cover up 4.4 months of imported goods and services.
* The views expressed in these materials are those of the authors and do not necessarily reflect the views of the Bank of Albania.
I. INTRODUCTION

Corporate Governance is a current topic that is gaining increasing interest from the enterprises and corporations, and also from banks in particular. This is due to the developments and recent challenges that have taken place globally, such as: the growing number of privatizations, the spread of stock investments, and the global integration of financial markets, which gives rise to the need for convergence towards a set of similar rules and practices in different countries.

Corporate Governance is the system of rules and restrictions that regulates the relations between managers and shareholders of a corporation, and ensures that the latter is managed in the interest of the shareholders.

Regarding the banking industry, a specific discipline of Corporate Governance is necessary, since these organizations have a special and greater significance compared to the others. The impact of their soundness or non-soundness affects many economic agents. As a matter of fact, a poor structure of Corporate Governance of a bank would lead to its bankruptcy, which would incur damage for both shareholders and depositors. The consequences could be even more severe, leading to a crisis in the economic system, which would reflect in the loss of public confidence in the real capabilities of banks to play their intermediation role. The experiences of bankruptcies in the recent years have given Corporate Governance an even greater role, turning it into an important and widely discussed topic.

Taking into account the importance of Corporate Governance in banks and the lessons drawn from the recent global crisis, this material seeks to identify the correlation between the level of bank governance in Albania and their financial performance. This analysis comes as an extension of a previous paper, from which we have used the Banking Governance Index. Since the data we possess are derived from a single survey, this material will focus only on a cross-section analysis. The inclusion of additional time series in the future will enable the assessment of correlations using more advanced methods.

But why does the main focus of many studies lie on the identification of the link between banks’ sound governance and their performance? Love and Rachinsky (2008) describe the reasons why better governed banks may display a better performance: “First, governance may reduce the incidence of bankruptcy and financial distress; second, good governance improves access to external finance, which is particularly important for small and medium-sized enterprises; third, good governance reduces asymmetric information and therefore increases investor confidence, reducing the cost of capital; fourth, good governance increases the chance of success of financial innovations, since it reduces the risk of fraud and regulatory arbitrage; and fifth, good governance reduces the risk of moral hazard.”

1 Refer to the paper of Ceca et al. (2010), “Corporate Governance in the Albanian Banking System: Analysis of a Corporate Governance Survey in the Albanian Banking System”. 
and amounts of related-parties transactions, as such transactions are usually sub-optimal in terms of efficiency and a reduction in these transactions would improve performance. Second, better governed banks may have lower cost of capital if they employ subordinated debt financing. Finally, better governance may translate into more efficient operations, as the functions of the supervisory board and the management are separated and modernized.”

II. STYLISTED FACTS

After the early 2000s, the Albanian banking system entered a new stage of development, characterized by the significant privatizations of state banks, the entry of renowned banking groups, and also a merger of two banks into a single bank. All these changes required the revision of the legal and regulatory framework, which culminated with the approval of a new banking law in 2006, and the continuous improvement and adaptation of the Bank of Albania’s regulations with the best international practices and banking market conditions. In the years 2004-08, the Albanian banking system underwent a rapid credit growth, high rates of return on assets and on equity, low non-performing loans rates, but also a growing competition for gaining market share in terms of loans and deposits. With the improvement of the supervisory framework, banks are increasingly paying attention to the compliance with this framework, by creating special functions in their structures to cover this aspect. They are not only being adjusted to the supervisory requirements. Many of them – being part of large banking groups or branches and subsidiaries of foreign banks – are adopting the best international practices that even go beyond the legal and regulatory requirements. One of the most important issues, which is being paid increasing attention from the banks operating in Albania, is Corporate Governance.

III. DATA AND METHODOLOGY

The following provides a brief overview of the Banking Governance Index (hereinafter referred to as “BGI”) as measured by Ceca et al. (2010)².

Box 1

Banking Governance Index (BGI) has been measured by Ceca et al. (2010). This index was first created for banks operating in Albania, deriving from the responses obtained from a questionnaire involving these banks.

This index measures the quality of governance in banks, by converting the qualitative responses of the questionnaire into quantitative variables, with numerical values in the segment [0;1]. A low value of this index shows a low level of governance in banks, while a value of 1 indicates the best level of governance. Various answers are weighted at specific shares based on their significance. The questions were grouped into 6 main topics and, by applying the simple average method of each bank responses, were constructed 6 sub-indices. The BGI is the indicator used in the following analysis.

² Since this is an unpublished study, you may contact the authors for a detailed explanation of the methodology used to measure the Index.
Chart 1 shows the value of the governance index for each bank, and an average for the entire Albanian banking system. Banks are represented by numbers in order to keep the data confidential. The chart shows that the quality of bank governance in Albania, compared to the base principles (which take the value of 1 unit), is satisfactory with an average BGI of 0.79. Banks generally show similar levels of governance, with half of them standing above the average level and the other half below this level.

Since the index value in the case of the Albanian banking system is calculated only for a year, and it will be extended even further with its measurement year after year, actually it is impossible to make an econometric assessment of the correlation between the index and the financial indicators. This material will, therefore, identify the links between the variables through a cross-section analysis.

This material takes into account the financial indicators analyzed by Love and Rachinsky (2008), where we could mention: RoA, RoE, the annual growth rate of average assets, the annual growth rate of average capital, interest income, interest expenses, the growth rate of non-performing loans, and an indicator for the bank size, measured as the natural logarithm of total assets.

Theoretically, the correlation between the BGI and RoA and RoE is expected to be positive, as a better governed bank should generate more net profits per unit of assets or equity invested. The indicator of interest income is an approximation of the income generated from lending, thus a kind of average interest rate generated by loans. Given that a better governed system reduces related-parties transactions (by not extending loans with preferential rates for them), this increases the average interest rate on loans granted. Consequently, the correlation between this indicator and the bank governance is expected to be positive, so the better a bank is governed, the more income per unit it is expected to generate from lending.
The correlation between interest expenses (which serves as an approximation of the cost of collecting deposits) and bank governance is expected to be negative, as the more defined are the governing rules and procedures of the bank, the more attractive and less risky it is, giving it the possibility to attract funds at lower costs.

The correlation between the growth rate of non-performing loans and the BGI is expected to be negative. Well-governed banks are expected to perform better and suffer less from the increase in non-performing loans, as they have the possibility to be equipped with better credit risk management techniques.

The bank size is also expected to affect their governance positively, under the assumption that big banks are better organized and have specific structures in place for different functions.

The following section makes a simple analysis of the correlation between the BGI measured in June 2010 and some variables of the Albanian banking system performance measured in June 2011. The inclusion of these data in the analysis with a time lag of one year aims at avoiding the possible problem of endogeneity between the BGI and bank performance variables.

IV. MAIN FINDINGS

The correlation between the BGI and the banking system’s financial variables is presented through the assessment of the fitted bi-variate regression line. Each of the following figures is a simple scatter plot, which presents in the horizontal axis the BGI, while in the vertical one the respective bank financial performance indicator.

Chart 2 shows a positive correlation between RoA and RoE and the BGI, hence confirming the fact that the better governed the banks are, the more net income they generate per unit of assets and capital invested.
The equation in Chart 3/a shows that the BGI is positively correlated with the annual growth rate of bank assets. A well-governed bank increases its assets faster than a bank with a lower level of governance, as it has a better image in the market and thus it is more capable to obtain funds.

The correlation between the BGI and the growth rate of the shareholders’ equity appears to be negative, implying that the most estimable banks in terms of the BGI have had a lower increase in their capital during the following period (1-year). However, Chart 3/b shows that this correlation is evidenced for the entire system as a whole, while a more detailed analysis of some individual banks shows that although some of them have had a good governance framework, they recorded negative capital growth over the following period of one year. If, from the total sample of banks, we exclude the two banks located in the extreme position in the chart (located inside the circle), the correlation becomes positive, implying that well-governed banks, despite the security they provide in this context, have taken measures to be also well-capitalized.
Interest income, which is used as a proxy of the average lending rate, show a positive tendency relative to the BGI, hence confirming the fact that banks with a better quality of governance have been able to generate higher profit rates on loans granted. While the correlation of the BGI with the interest expenses, which represent the average cost of collecting deposits, is negative as well-governed banks have managed to collect funds at lower costs, perhaps also due to the higher security they provide.

Another correlation identified is that between the BGI and the credit risk, which is measured as the annual growth rate of outstanding non-performing loans. Our analysis confirmed a negative correlation between these two indicators, being in line with the expectations that good bank governance has a better risk management, which is in turn reflected in a lower growth rate of non-performing loans.

Bank size, which is measured by the natural logarithm of banks’ assets, confirmed the positive correlation between this indicator and the BGI, giving us the perception that larger banks are those that have an even more complete and regulated governance framework. Larger banks, being part of renowned European banking groups, have paid greater attention to strengthening the legal, procedural and regulatory framework of their activity. This is has led to a higher BGI for these banks.

CONCLUSIONS

The purpose of this material was to analyze the correlation between the BGI in Albania and some bank financial performance indicators. The analysis showed that banks with a higher BGI were the ones that: generated more net income relative to their capital and assets; increased their assets faster and their equity slower during the period following the time of the measurement of their governance quality; had a lower growth rate of non-performing loans in their portfolio; had managed to provide funds at lower costs and to invest them in instruments that generate higher rate of return; and were the largest banks in terms of their total assets. We believe that these results may crystallize further once other time series are added in the future.

Based on the above analysis of the correlation between the BGI and the banking system performance indicators, we conclude that there is still room for the Albanian banking system to further improve the internal procedures and mechanisms of management and governance. A greater attention to these aspects would improve the value of the BGI and the performance of the Albanian banking system indicators.
REFERENCES


In the context of constantly assessing the banking system and addressing the concerns it is faced with, the Bank of Albania organized, on 12 July 2011, a roundtable on “Collateral, Loans, Market and Legislation”, with the Albanian Association of Banks and other stakeholders in the banking system. This roundtable was also attended by the Minister of Finance Mr. Ridvan Bode, Deputy Minister of Justice Ms. Brikena Kasmi, and representatives from the Supreme Court and the public and private bailiff service.

The purpose of this forum went beyond identifying the bottlenecks in the execution of the collateral. In conclusion, the parties agreed to establish an inter-institutional working group to draft a detailed action plan for the solution of collateral execution-related concerns.

The Bank of Albania, a promoter of macroprudence and financial stability, invites all institutions to pay maximum attention and commit to all legal initiatives or any other practices that may be proposed on collateral execution.

The Bank of Albania held on 1 September 2011 the presentation ceremony of the free-choice module for the financial literacy of high school students entitled “Personal Finances in Your Hands”. The opening address was delivered by the Governor of the Bank of Albania Mr. Ardian Fullani, and the Minister of Education and Science Mr. Myqerem Tafaj. This ceremony was attended by representatives of the Bank of Albania, Ministry of Education and Science, Education Development Institute and Regional Education Directorates.

The new educational module on financial literacy will be one of the free-choice subjects of the high school education curriculum for the academic year 2011-12. In accordance with the curriculum itinerary that each student has planned to make and with the personal interests, the students may choose to take this subject in one of the three high school years.

The contents of the module “Personal Finances in Your Hands” was formulated by the Bank of Albania in 2010, in cooperation with the Education Development Institute (EDI) and teachers of Economics. The key objective of this project was to formulate a format equipped with information based on the Albanian reality, and in line with the educational goal that this module intends to achieve didactically for the target group.

The project for the inclusion of a free-choice module on the financial literacy of high school students in the education curriculum was born as an initiative of the Bank of Albania, which has for several years now been engaged in creating and promoting the financial culture in the Albanian society. The endorsement of the Memorandum of Understanding, on 13 December 2007, between the Bank of Albania and the Ministry of Education and Science was a major step in this regard. It provided the opportunity to institutionalize the educational programme of the Bank of Albania designed for students in the fields of economics, finance and banking studies.
In order to be successful, this project also envisaged the training of trainers. Representatives of the Regional Education Directorates were offered a two-day training workshop by Bank of Albania experts that provided insights on how to teach this high school subject.

On 13 September 2011, the Governor of the People’s Bank of China, Mr. Zhou Xiaochuan, visited the Bank of Albania for an official visit at the invitation of the Governor of the Bank of Albania, Mr. Ardian Fullani.

Discussions in this bilateral meeting focused on the economic developments, where Governor Fullani presented Governor Zhou with an overview of the performance of the Albanian economy, and the banking system in particular. The Albanian Governor outlined the measures the Bank of Albania has taken in view of the prudential supervision of the banking system, and described the monetary policy framework in Albania. Governor Fullani also presented Governor Zhou with the policies pursued by the Bank of Albania to maintain price stability.

Mr. Fullani noted that the positive business climate, macroeconomic stability, the favourable geographical location, and the liberal legislation make Albania a very attractive destination for foreign investors. From this point of view, there is room for higher interest and presence of Chinese capital in Albania.

Governor Zhou commended the Bank of Albania’s work to preserve financial stability and expressed his willingness to expand bilateral cooperation.

On 15 September 2011, the Bank of Albania hosted its 9th International Conference on “Building our Future through Financial Literacy”. This Conference was organized in cooperation with Banca d’Italia, in the framework of the twinning project between the two central banks.

The opening address was delivered by the Governor of the Bank of Albania Mr. Ardian Fullani, who pointed out the importance of establishing financial literacy on a broad national level.

Welcome remarks were also delivered by the Minister of Finance Mr. Ridvan Bode, the Ambassador of the European Union to Albania H.E. Mr. Ettore Sequi, the Deputy Minister of Education and Science Mr. Halit Shamata, and Managing Director of the Bank of Italy Mr. Franco Passacantando. Keynote conference speaker was Mr. Dejan Soskic, Governor of the National Bank of Serbia.

This Conference was attended by many central bank representatives of the region, managers of commercial banks operating in Albania, prominent academics in the field of economics and finance, diplomatic corps accredited to Albania, representatives of international financial institutions, and many Albanian and foreign personalities.
This Conference was prompted by the increasing importance of financial literacy worldwide, especially following the latest economic developments and the global financial crisis. The latter evidenced the need for establishing financial literacy in order to reduce risks and improve consumer welfare as a result of a more accountable decision-making.

The Bank of Albania’s Governor Mr. Ardian Fullani concluded the proceedings of this Conference, emphasizing once more the importance of designing and implementing a national strategy on financial literacy. Governor Fullani pointed out that the Bank of Albania is willing to cooperate with the public and private sectors in Albania in order to design a national strategy on financial literacy in Albania.

Research Department of the Bank of Albania hosted, on 10-11 November 2011, the fifth regional workshop “Economic Research in South-Eastern Europe”. There were 25 participants (presenters and discussants) from Bank of Albania and other central banks of the region (European Central Bank, Bank of Italy, Bank of Austria, Central Bank of the Republic of Macedonia and Hungarian National Bank) who attended the workshop. Following the success of previous workshops, the aim of this workshop was to further improve cooperation and open dialogue among research economists, and also to further widen the knowledge of regional central banks over some characteristics and specific developments of the participant countries.

Some of the research studies dealt with issues related to public finances of the region, economic uncertainties and the way banks should optimally react to productivity, trade, financial stability, and price stability. These topics were of high interest against a background of the difficult situation most of the euro area countries are going through, caused by sovereign debt crisis problems, and negative potential effects they might pose to the economies of our region.

On 24 November 2011, the Bank of Albania held a roundtable on “Interbank Market Development”. This roundtable was attended by managers of commercial banks operating in Albania and representatives of the Albanian Association of Banks.

In the context of the European Integration process, the Bank of Albania has started to implement the Twinning Project between the Bank of Albania, Banca d’Italia and Banque de France. This project aims at strengthening the institutional capacity and approximating the legal and operational framework of the Bank of Albania with the best standards of the European System of Central Banks. “Interbank Market Development” is one of the modules in this project.

Interbank market development is a key objective of the Bank of Albania considering the important role it plays in improving the monetary policy transmission mechanism in the economy.
The Bank of Albania representatives pointed out the persistent efforts of the central bank in developing the interbank money market and the Government securities secondary market. They also noted that these efforts need to be supported with initiatives from the banking system.

During this roundtable, the commercial bank managers were introduced to the additional measures proposed by the Bank of Albania to develop the interbank market. In carrying out this process, cooperation with the market players is highly important.

On 19 December 2011, the Governor of the Bank of Albania, Mr. Ardian Fullani, hosted a reception to mark the end of 2011. This reception was attended by the Minister of Finance, Mr. Ridvan Bode, members of the Parliamentary Commission for Finance and Economy, representatives of the diplomatic corps accredited to Tirana, journalists and analysts of press and electronic media, and managers of the banking system in Albania.

In his speech, Governor Fullani commended the former members of the Supervisory Council of the Bank of Albania, whose term in office ended, for their contribution, and welcomed the new Council members. The Governor also commended the role of the media in transmitting the Bank of Albania’s decision-making and activity to the public in a timely and reliable fashion. During his speech, Governor Fullani also highlighted the Bank of Albania’s work in safeguarding macroeconomic stability in Albania.

The Governor placed special importance on the Bank of Albania’s commitment to public education. At the end of reception, Governor Fullani announced the three winners of the Governor’s Award for the Best Diploma Thesis for 2011.

The Research Department at the Bank of Albania organizes a fortnightly “Friday Seminar”. This initiative welcomes Bank of Albania experts, researchers from the academia and other financial, research and scientific institutions to present and discuss their theoretical and empirical research papers.

During the second half of 2011, the Friday Seminar Series welcomed seven presentations, mostly from Bank of Albania participants, and also from domestic scholars. These presentations covered various issues, like: the financial crisis and its impact on the economies of the region, the financial system and its performance, fiscal policy sustainability, exchange rate, trade relationships, etc.

“The Impact of Global Financial Crisis on the Economies of South-Eastern Europe”, by Evis Kopliku, Third Prize Winner of Governor’s Award for the Best Diploma of Year 2010 was the first study presented in the Friday Seminar for the period July-December 2011. The aim of this study is to investigate the impact of the global financial crisis on four South-Eastern European
countries: Albania, Bulgaria, Croatia, and Romania. This investigation is done by using Unit Root tests and Johansen Cointegration tests, and by employing quarterly time series data from 1990 to 2009. First, this study identifies the possible transmission channels of the crisis grounded on empirical research and theoretical approaches relevant to the crisis. Once the variables have been identified as possible transmission channels, the author investigates their significance on the economic growth of the sample of the South-Eastern European countries. Findings show that exports and credit have been significant transmission channels of the global crisis. Interestingly, FDIs are found to have a significant but negative effect on growth, while the impact of remittances is positive but not statistically significant. In the case of Bulgaria, all variables, but degree of openness, positively affect economic growth. In the case of Croatia, the results show that exports are the most significant transmission channel of the global crisis, whereas openness has a negative impact on economic growth. In the case of the new EU member, Romania, FDIs, credit and remittances are found to be statistically significant, indicating that being more integrated increases the significance of the global crisis on the growth. The findings of this study in the future might serve as a very useful source of reference in developing policies, which try to minimize the costs of the global financial crisis.

“The Impact of Trade on Growth: A Gravity Model-Based Instrument Approach on Post-Communist Europe”, by Endrit Yzeiraj, Research Department. The study is based on the literature initiated by Frankel and Romer (1999) on using instruments for predicted trade to analyze its effect on growth. It uses panel data to better control for possible time-invariant characteristics. The fall of communism is used as an exogenous shock to the system. The study finds that not all attempts at creating good instruments are successful. However, the successful attempts are the ones that have coefficient results comparable to the literature. Also, trade is found to have a positive and significant effect on a country’s income.

“Equilibrium Exchange Rate in a Developing Economy”, by Bledar Hoda, Research Department. This study aims to estimate the equilibrium level of the real exchange rate by employing “The Statistical Approach of the Exchange Rate”. This approach enables effects, such as Balassa Samuelson and terms of trade to play an important role in guiding equilibrium RER. The estimation also includes other factors, like: the real interest rate differential and the level of foreign currency reserves of the banking system. The estimation employs vector error correction among variables with unit root. Empirical findings show that all the above-mentioned factors but the foreign currency reserves enter significantly a long-run relationship with the real exchange rate. Also, the study shows that terms of trade and the Balassa-Samuelson proxy result to have the greatest impact to relatively affect the real exchange rate, while the other factors have only a marginal effect.

“Sustainability of Fiscal Policy: The Case of Albania”, by Gerti Shijaku, Research Department. This study aims to estimate the long-run sustainability of fiscal policy, while answering at the same time the question: “Does the government undertake the right policies to avoid the excess accumulation of
debt?" Empirical results show that developments in public debt-to-GDP ratio are sustainable, even though such behaviour lacks when such indicator is measured in real terms. These results are further confirmed by the statistical test, Phillips-Perron. Also, findings, under the assumptions of the reaction function, show that fiscal authorities react to increasing indebtedness by generating future surpluses, but not enough for debt to be mean-reverting in the long-run, leading to a non-Ricardian regime. Empirical analysis shows that fiscal policy has been relatively stable over time, even though economic and financial global crisis have had a negative impact. Lastly, evidence seems to suggest that fiscal policy is relatively volatile when public debt is close or above the 60% of GDP ratio.

“How is Financial Performance of Banks in Albania Influenced by Sound Corporate Governance”, by Oriela Kodra and Irini Kalluci, Research Department. This paper provides an overview on bank governance relation with their performance captured by several financial indicators. Among these indicators, we can mention: the return on assets and equity; the growth rate of assets and capital, interest income and expenses, and the size of banks. To measure the quality of banks governance, the study employs the values of Banking Governance Index, extracted from Ceca et al. (2010). All relations between this index and financial indicators proved with the expected sign. The testing of these correlations in the future will require other methods and additional time series.

“Free Trade Agreements and Trade Integration among South-Eastern European Countries: Gravity Model Estimations”, by Alban Pllaha, Research Department. This study aims to estimate the impact of bilateral free trade agreements on regional trade integration of South Eastern European Countries (SEE-9). The author analyses the trade flows between nine countries of South Eastern Europe. The study employs the GMM approach, which enables the incorporation of dynamics in panel data assessment into gravity model for trade. Findings of this study show that trade is impacted by GDP, free trade agreements, colonial links, neighbourhood, and physical transportation distance between countries.

“A Financial System Stress Index for Albania”, by Vasilika Kota and Arisa Saqe, Financial Stability Department. The latest financial crisis reflected the need to properly understand, to measure and possibly to project the systemic events, which have a high probability of causing the interruption of the normal functioning of the financial markets, resulting in a suffering of the economic growth. This paper presents a Financial System Stress Index for Albania, which aims to capture the level of financial stress of the economy in a single and comprehensive index (FSSIA). The authors assess the linkages of the different market segments through evaluating their impact on economic growth, providing in this way a clear method in discussing the evolution of the sub-indices of the banking sector, money market, foreign exchange rate, and housing market into financial stress. The results indicate that FSSIA captures the pressures in the form of the financial stress, not only from different market segments, but also from their interaction through cross correlation.
MONETARY POLICY DECISIONS

26 January and 23 February 2011
The Supervisory Council of the Bank of Albania decided to keep the interest rate unchanged at 5.00%.

23 March 2011
The Supervisory Council of the Bank of Albania decided to increase the key interest rate by 0.25 percentage points to 5.25%.

27 April, 25 May, 29 June, 27 July and 31 August 2011
The Supervisory Council of the Bank of Albania decided to keep the interest rate unchanged at 5.25%.

29 September 2011
The Supervisory Council of the Bank of Albania decided to decrease the key interest rate by 0.25 percentage points to 5.00%.

26 October 2011
The Supervisory Council of the Bank of Albania decided to keep the interest rate unchanged at 5.00%.

30 November 2011
The Supervisory Council of the Bank of Albania decided to decrease the key interest rate by 0.25 percentage points to 4.75%.

28 December 2011
The Supervisory Council of the Bank of Albania decided to keep the interest rate unchanged at 4.75%.
LEGAL EVENTS, JULY-DECEMBER 2011

BANKING SUPERVISION

On 13 July 2011, the Supervisory Council of the Bank of Albania approved by Decision No. 49 “The Supervision Annual Report for 2010”. According to this Report, the banking system’s total assets increased by about 11.8%, which is higher than in the previous year when they increased by only 6.3%. The loan portfolio grew moderately by 9.1%, hence decelerating the credit growth rates compared to the previous year when the loan portfolio grew by 13.4%. Credit risk in the system appeared higher in 2010 considering an elevated non-performing loan ratio. Banks’ overall risk level, however, remains moderate due to the preservation of a satisfactory bank capital adequacy ratio.

On 14 September 2011, the Supervisory Council of the Bank of Albania approved by Decision 62 the Regulation “On Credit Risk Management”. The purpose of this Regulation is to lay out the rules and requirements for credit risk management in banks’ activity. It also sets out the criteria for the assessment of risk and classification of loans and other assets, and for the calculation of reserve from loan loss as a result of their depreciation. This Regulation shall apply to banks and branches of foreign banks licensed by the Bank of Albania to conduct banking and/or financial activity in the Republic of Albania.

On 14 September 2011, the Supervisory Council of the Bank of Albania adopted the Decision No. 63 “On some Amendments to Regulation “On Capital Adequacy Ratio”. The amendments addressed in this Decision affect Article 8 of this Regulation, which stipulates the ways balance sheet assets are risk-weighted.

On 12 October 2011, the Supervisory Council of the Bank of Albania adopted the Decision No. 70 “On Granting Credins Bank sh.a. Preliminary Approval to Conduct Additional Activity”. Upon this Decision, Credins Bank sh.a. is granted preliminary approval to conduct trading activities, on its account or for the account of its clients, be it in a foreign exchange, over-the-counter or other negotiable instruments.

On 12 October 2011, the Supervisory Council of the Bank of Albania adopted the Decision No. 71 “On Granting Alpha Bank-Albania Preliminary Approval to Conduct Additional Activity”. Upon this Decision, Alpha Bank-Albania is granted preliminary approval to offer guarantees and receive commitments as additional financial activities.
On 26 October 2011, the Supervisory Council of the Bank of Albania adopted the Decision No. 75 “On some Amendments to Regulation “On Liquidity Risk Management””. The articles the amendments to this Regulation apply to regulate the liquidity ratios, the calculation of liquid assets to current liabilities, and the reporting requirements.

On 30 November 2011, the Supervisory Council of the Bank of Albania adopted the Decision No. 77 “On Granting Banka Societe Generale Albania sh.a. Preliminary Approval to Conduct Additional Activity”. Upon this Decision, Banka Societe Generale Albania sh.a. is granted preliminary approval to receive commitments, trade securities and other negotiable instruments and financial assets, intermediate monetary transactions, provide custody services, etc., as additional financial activities.

On 14 December 2011, the Supervisory Council of the Bank of Albania adopted the Decision No. 82 “On some Amendments to Regulation “On the Licensing, Organization, Activity and Supervision of Foreign Exchange Bureaus””. This Decision adds to this Regulation the self-declaration form, the declaration signed by the legal person’s administrator on the acknowledgement and implementation of the legal and by-law obligations to carry out the foreign exchange activity, and the information on the necessary technical/administrative equipment that the bureau has in place to conduct the foreign exchange activity.

ISSUE

On 13 July 2011, the Supervisory Council of the Bank of Albania adopted the Decision No. 50 “On Minting Coins for Numismatic Purposes in 2012”. The purpose of this Decision is to specify the technical information of non-circulating legal tender coins to be minted for numismatic purposes themed “100th Anniversary of the Declaration of Independence”. The coins will have a face value of 200, 100 and 50 Lek. They will be minted in different materials and there will be minted 1000, 1000 and 10000 pieces, respectively.

On 31 August 2011, the Supervisory Council of the Bank of Albania adopted the Decision No. 60 “On Minting Coins for Numismatic Purposes Dedicated to Mother Theresa, in 2012”. The purpose of this Decision is to specify the technical information, such as the weight, diameter and alloy of the non-circulating legal tender coins to be minted for numismatic purposes. The coins shall have a face value of 200 Lek and there will be minted 1000 pieces.

MONETARY POLICY

On 27 July 2011, the Supervisory Council of the Bank of Albania approved by Decision No. 52 “Bank of Albania’s Monetary Policy Statement on the First Half of 2011”. The Statement points out that in line with the past year’s
performance, the growth of the Albanian economy in the first and second quarter of 2011 was mostly driven by the growth in industry and services sectors. Owing to the impact of foreign demand, industrial output grew by 12.3% y-o-y. Consumer prices experienced added inflationary pressures in the first half of 2011, mainly due to the rise in global import prices. Annual inflation in the first and second quarter of 2011 averaged 4.0% and 4.1%, respectively. The developments in the financial markets were relaxed, reflecting the low risk premium and the satisfactory liquidity situation. Taking into account the future outlook for the Albanian economy, Bank of Albania’s projections and assessments suggest that economic growth will persist in the second half of the year.

On 29 September 2011, the Supervisory Council of the Bank of Albania adopted the Decision No. 68 “On Cutting the Interest Rate on Repo and Reverse Repos”. According to this decision, the Supervisory Council cut the interest rate on repo and reverse repos by 0.25 percentage points to 5.00%. The monetary policy accommodation aims at creating adequate monetary conditions to meet the medium-term inflation target, and driving economic activity by boosting consumption and investment in Albania.

On 26 October 2011, the Supervisory Council of the Bank of Albania approved by Decision No. 73 “Monetary Policy Report for 2011 Q3”. According to this Report, the Albanian economy displayed, overall, a positive performance during 2011, albeit in the presence of an unfavourable external environment. Annual inflation averaged 3.2% in 2011 Q3, down 0.9 percentage points from the first half of 2011. The developments in the financial markets in Q3 indicate low liquidity premium and inflation. Projections show that economic growth will persist in the remainder of the year. In September, the Bank of Albania eased the monetary conditions further by cutting the key interest rate by 0.25 percentage points to 5.00%. Inflation is expected to fluctuate around the Bank of Albania’s target in the medium run.

On 30 November 2011, the Supervisory Council of the Bank of Albania adopted the Decision No. 76 “On Cutting the Interest Rate on Repo and Reverse Repos”. According to this Decision, the Supervisory Council cut the interest rate on repo and reverse repos by 0.25 percentage points to 4.75%. This decision provides adequate monetary conditions to meet the medium-term inflation target and, at the same time, increase the monetary stimulus and boost the economic activity in Albania.

On 28 December 2011, the Supervisory Council of the Bank of Albania approved by Decision No. 85 “Monetary Policy Document for the Period 2012-2014”. According to this Decision, in quantitative terms, the Bank of Albania will, for the period 2012-2014, continue to target an inflation rate of 3.0%, with a tolerance band of ± 1 percentage point around this figure. The Bank of Albania considers that, by keeping inflation around 3%, monetary policy will continue to provide positive contribution to the development of the Albanian economy. The operational objective of the Bank of Albania’s monetary policy will be steering the short-term interbank rates close to the
Bank of Albania’s key interest rate, set by the Supervisory Council, and smoothing their movements.

FINANCIAL STABILITY

On 29 September 2011, the Supervisory Council of the Bank of Albania approved by Decision No. 69 “Financial Stability Report for 2011 H1”. According to this Report, at the end of the reporting period, the financial system and banking sector’s situation was assessed as stable. The banking sector, which continues to dominate the financial system’s activity, expanded its activity further and increased its share in the country’s economy. Liquidity situation appeared satisfactory and the public deposits continued to grow at similar rates as well. Credit growth rates are improving, however, the loan portfolio quality continued to deteriorate. Nevertheless, the financial profit remains positive and concentrated. Capital adequacy ratio has been downward, remaining, however, considerably above the minimum capital requirement. The Bank of Albania assesses and has required that banks strengthen the capitalization of their activity by raising the shareholders’ equity.

INFORMATION AND TECHNOLOGY

On 12 October 2011, the Supervisory Council of the Bank of Albania approved by Decision No. 72 the Regulation “On the Functioning of the SWIFT at the Bank of Albania”. The purpose of this Regulation is to lay out the functions and responsibilities of the organizational units at the Bank of Albania in relation to the SWIFT, and the rules and procedures for the management, operation, monitoring and control of this system.

SUPERVISORY COUNCIL

On 28 December 2011, the Supervisory Council of the Bank of Albania adopted the Decision No. 90 “On the Election and Appointment of the First Deputy Governor of the Bank of Albania”. According to this Decision, Ms. Elisabeta Gjoni is appointed the First Deputy Governor of the Bank of Albania.

ECONOMIC POLICY

On 2 July 2011, the Council of Ministers adopted the Decision No. 471 “On Raising the Pensions”. According to this Decision, pensions are raised by 4% and 7%, for different categories of full, partial and early retirement pensions, full, partial and reduced invalidity pensions, payments for the insurance against accidents at work and occupational illnesses etc. The financial effects arising from the implementation of this Decision, estimated to amount to ALL 1,634 million, shall be covered by the contingency fund provided for in the 2011 State Budget.
On 2 July 2011, the Council of Ministers adopted the Decision No. 472 “On Disciplining the Use of Budget Funds for 2011”. The purpose of this Decision is to provide for different measures, such as: the public administration functions, approved in the organizational chart but not filled in yet, will freeze until the institutions are restructured; the special planned fund shall not be used for social and cultural activities; administration employees’ overtime hours shall be converted into leave hours/days; all budget funds subject to public procurement procedures, unprocured as at 1 August 2011, shall freeze.

On 4 July 2011, the Minister of Finance adopted the Instruction 12/3 “On some Amendments to Instruction No. 12, dated 18 May 2011 “On the Procedures for the Implementation of Law No. 10418, dated 21 April 2011 “On the Legalization of Capital and Cancellation of Part of Tax and Customs Liabilities””. These amendments mainly affect Section II of the Instruction, which sets out the provisions for the cancellation of tax and customs liabilities. They provide the details for the conditions when these liabilities are cancelled, the documentation to be completed by the debtors, and the procedures to be followed by the Cancellation Management Commission during the examination of applications.

On 7 July 2011, the Parliament of the Republic of Albania ratified by Law No. 10439 “The Agreement between the Council of Ministers of the Republic of Albania and the Government of the Republic of Serbia for the Settlement of the Debt of the Republic of Albania to the Republic of Serbia”. Through this Agreement, the parties agree that the final settlement amount of the Republic of Albania’s debt, including the accrued interest for the period 31 March 2006 - 30 September 2009 is USD 8,528,802.42. The interest for the period from 1 October 2009 to the signature date of the Agreement, that is 31 March 2011, amounts to USD 66,318.32. The debt will be settled through ten semi-annual payments of the principal and the interest, on 31 March and 30 September each year.

On 13 July 2011, the Council of Ministers approved by Decision No. 502 “The Uniform Regulation on the Control of Territory Development”. The purpose of this Regulation is to achieve uniform form and structure of national and local investment, and control of territory development, in order to discipline the control of development based on the effective planning instruments. This Regulation aims at providing for the general and specific rules on the form and structure of national and local regulations on the control of territory development.

On 14 July 2011, the Parliament of the Republic of Albania ratified by Law No. 10443 “The Loan Agreement between the Republic of Albania and the International Bank for Reconstruction and Development (IBRD) for the Financing of the Social Sector Reform Development Policy Loan Programme”. Through this Agreement, the IBRD agrees to lend EUR 18,100,000 to the Republic of Albania for carrying out the actions provided for in the programme. These actions include a number of amendments to the legal framework that
regulates social assistance and services, and the mandatory health care insurance.

On 14 July 2011, the Parliament of the Republic of Albania adopted the Law No. 10444 “On some Amendments to Law No. 9902, dated 17 April 2008 “On Consumer Protection””. The purpose of these amendments is to specify some definitions in Law No. 9902 and they affect the articles that provide for the unfair business practices, transparency requirements, indemnification of consumers, consumer loan and related obligations, Consumer Protection Commission and the handling of consumer complaints.

On 14 July 2011, the Parliament of the Republic of Albania adopted the Law No. 10450 “On some Amendments to Law No. 10355, dated 2 December 2010 “On 2011 Budget””. The Amendments affect the articles that set out the provisions for the state budget, local budget, social insurance and health insurance budget, the threshold level of budget deficit financing, the threshold level for the annual increase of total existing state and state-guaranteed debt, etc.

On 20 July 2011, the Council of Ministers approved the Decision No. 527 “On Establishing the National Minimum Wage”. According to this Decision, as from 1 July 2011, the base monthly minimum wage of employees, on a national level and required to be observed, is ALL 20,000, while the base minimum wage per hour is ALL 115.

On 20 July 2011, the Council of Ministers adopted by Decision No. 522 “Draft-Document on 2012-2014 Medium-Term Budget Programme”. The Medium-Term Budget Programme is an operational instrument for the management of public expenditure and it is a key component in the Integrated Planning System. It aims to encourage the efficiency in carrying out public expenditure, and establish a direct linkage between the Government priorities and the allocation of public resources and carrying out of public expenditure. It also seeks to promote fiscal discipline, enabling public expenditure to be planned within a realistic macroeconomic and fiscal framework.

On 21 July 2011, the Parliament of the Republic of Albania approved the Law No. 10457 “On some Amendments to Law No. 9632 “On Local Tax System”, as Amended”. The purpose of this Law is to abrogate those articles in Law No. 9632 that regulate the annual registration charges for road transport vehicles, and the cases exempt from these charges.

On 21 July 2011, the Parliament of the Republic of Albania approved the Law No. 10458 “On Some Amendments to Law No. 9975, dated 28 July 2008 “On National Taxes”, as Amended”. The purpose of this Law is to change the traffic tax on petrol and gasoil, and the carbon tax on petrol, gasoil, coal, coal-oil, solar and mazut. The traffic tax on petrol and gasoil shall be ALL 5 per litre until 31 December 2011. After this date, the traffic tax on petrol and gasoil shall be ALL 7 per litre, while the fixed tax on the type of fuel shall be ALL 25 for oil and ALL 20 for petrol.
On 25 July 2011, the Minister of Finance adopted the Guideline No. 17 “On the Accomplishment of Public Financial Inspection and Quality Control”. The purpose of the activity of public financial inspection is to protect the financial interests of public entities against serious financial mismanagement, fraud and corruption. This Guideline establishes the ways, conditions and procedures for the execution of public financial inspection and quality control.


On 3 August 2011, the Council of Ministers adopted the Decision No. 562 “On Establishing the Base Unemployment Benefit”. According to this Decision, the base unemployment benefit shall be ALL 6850 per month. The financial effects arising from the implementation of this Decision shall be covered by the 2011 state budget funds allocated to the Ministry of Labour, Social Affairs and Equal Opportunities, under “Household budget transfers and disability benefit” (unemployment income).

On 18 August 2011, the Council of Ministers adopted the Guideline No. 2 “Modalities on the Execution of Monetary Obligations in Treasury Accounts of Budgetary Institutions”. The purpose of this Guideline is to determine the modalities on the execution of monetary obligations in treasury accounts of general government entities arising from irrevocable judicial decisions. The execution of judicial decisions shall be carried out by the responsible spending entity, using the budget funds allocated for this purpose, and other income provided by the general government entity.

On 24 August 2011, the Council of Ministers adopted the Decision No. 602 “On the Approval of the Modalities on the Use of Counterparty Funds, Collected from Japanese Grants for Agriculture and Food Sector”. According to this Decision, the counterparty funds extended by the Japanese Government amounting to ALL 200,000,000 shall be used during 2011 to promote the growth and processing of agricultural and farming products. The monetary values that will be used to support agricultural development shall be proportional to the amount of beneficiary’s investment. They shall be extended to support the development of agricultural and farming activities in the form of interest-free loans of 7-year maturity term.
On 7 September 2011, the Council of Ministers adopted the Decision No. 615 “On Distance Selling Contracts Relating to Financial Services to Consumers”. The provisions set forth in this Decision regulate the distance selling contracts relating to financial services to consumers based on four articles of the Law “On Consumer Protection”, according to the European Parliament and Council Directives. The provisions in this Decision establish the rights and obligations of the consumer and trader of financial services, as well as the procedures to be followed during their trading.

On 7 September 2011, the Council of Ministers adopted the Decision No. 619 “On the Approval of the National Energy Efficiency Action Plan for the period 2011-2018”. This plan is based on EU Directives and it provides a description of measures to be taken to improve the efficiency of energy in the sectors of the economy, planned to achieve the short-term objectives until 2012, and the long-term ones until 2018, through the implementation of energy efficiency policies. The improvement of energy efficiency in all the sectors of the economy represents one of the main goals in the national energy strategy.

On 14 September 2011, the Council of Ministers adopted the Decision No. 643 “On the Approval of the Sectoral National Strategy for Water Supply and Sanitation Services”. The purpose of this strategy is to present Albania’s vision, mission objectives and action plans for this sector in a clear, specific, quantitative and timely fashion, along with the responsibilities pertaining to each institution. It aims at clarifying Albania’s directions and objectives as a co-sponsor of the United Nations Resolution, to turn access to safe drinking water and sanitation into a human right.

On 19 September 2011, the State Aid Commission approved the Decision No. 38 “On State Aid Allocation Plan on Promoting the Employment of Women Belonging to Certain Groups”. This scheme aims to promote and support the opening of new jobs through their subvention from the state budget. The cost shall be covered by the annual funds approved in the state budget law of the respective year. Beneficiaries of this scheme shall be those private enterprises or institutions that intend to hire, under regular contracts, unemployed women jobseekers from the employment office list. The intensity of the aid shall not exceed 75% of the wage cost for employees limited in their ability to work, and 50% of the wage cost for employees in difficulty.

On 19 September 2011, State Aid Commission approved the Decision No. 39 “On State Aid Allocation Plan “On Financing Amount, Criteria and Procedures for the Implementation of the Employment Promotion Programme of Unemployed Jobseekers Finding a Job for the First Time”. The aid allocation plan aims to help employers hiring young people aged 16-25 years, who do not have any previous work experience. This aid scheme shall enable the project-winning enterprises to be financed by the state budget. The intensity of the aid shall not exceed 75% of the wage cost for employees limited in their ability to work, and 50% of the wage cost for employees in difficulty.
On 28 September 2011, the Council of Ministers adopted the Decision No. 667 “On Establishing the Innovation Fund”. This Decision provides the provisions for the establishment of the Innovation Fund totalling ALL 40,000,000 over a 4-year implementation duration covering the period 2011-2014. This fund will assist micro, small and medium-sized enterprises through direct subsidies amounting to ALL 400,000. The Decision also establishes the conditions to be met for benefitting the assistance from this fund and the procedures for its extension.


On 20 October 2011, the Parliament of the Republic of Albania ratified by Law No. 10472 “The Agreement between the Council of Ministers of the Republic of Albania and the Government of the Republic of Kosovo on International Road Transport of Travellers and Goods”. By signing this Agreement, the two countries aim at taking a step forward toward the development of commercial and economic relations between them and promoting road transport cooperation in the framework of the market economy.

On 20 October 2011, the Council of Ministers adopted by Decision No. 725 “The Agreement between the Council of Ministers of the Republic of Albania and the Government of the Republic of Cyprus for the Promotion and Reciprocal Protection of Investments”. Through this Agreement, the two countries aim at intensifying economic cooperation and create favourable conditions for the investment made by the investors of each contracting party in the territory of the other party.

On 27 October 2011, the Parliament of the Republic of Albania adopted the Law No. 10475 “On an Amendment to Law No. 9901, dated 14 April 2008 “On Entrepreneurs and Commercial Companies”. The Amendment increases the minimum share capital of joint stock companies privately held to ALL 3,500,000.

On 27 October 2011, the Parliament of the Republic of Albania ratified by Law No. 10473 “The Agreement between the Council of Ministers of the Republic of Albania and the Government of the Republic of Italy on the Debt-for-Development Swap”. By signing this agreement, the parties agree that the funds arising from debt swap operations, amounting to EUR 20,000,000, shall be used to finance social development projects and particularly projects focused on generating education, health and employment.

On 2 November 2011, the Council of Ministers approved the Decision No. 752 “On the Approval of the Draft-Document on 2012-2014 Medium-Term Budget Programme”. This Document provides detailed description of the
purposes, objectives and products of the programmes of each line ministry, on a programme level for 2012, 2013 and 2014, as well as a summary of budget requirements of other budgetary institutions included in this process for the third time. Hence, it outlines the linkages between policy purposes and objectives and the allocation of budget resources in the medium run.

On 3 November 2011, the Parliament of the Republic of Albania approved the Decisions No. 134, No. 135, No. 136, No. 137, No. 138 and No. 139, on the appointment of the members of the Supervisory Council of the Bank of Albania. Accordingly, Mr. Ardian Fullani, Mr. Petraq Milo, Ms. Elisabeta Gjoni, Mr. Dhorë Kule, Ms. Ela Golemi and Ms. Ermelinda Meksi are appointed members of the Supervisory Council of the Bank of Albania. In addition, based on Decision No. 144, dated 15 December 2011, Mr. Adrian Civici is also appointed member to this Council.

On 3 November 2011, the Parliament of the Republic of Albania ratified by Law No. 10477 “The Agreement between the Council of Ministers of the Republic of Albania and the Council of Ministers of Bosnia and Herzegovina on the Solution of Republic of Albania’s Debt for the Settlement of Amounts in the Merchandise Trade Account between the Republic of Albania and former Socialist Federal Republic of Yugoslavia”. Through this Agreement, the parties agree that the final settlement of debt of the Republic of Albania to Bosnia and Herzegovina, including the regular interest, which amounts to USD 3,696,189.56, shall be made through six semi-annual payments, on 31 March and 30 September.

On 8 November 2011, the Minister of Finance approved the Guideline No. 25 “On Some Amendments to Guideline No. 17, dated 13 May 2008 “On Value Added Tax”, as Amended”. The purpose of this Guideline is to re-establish a number of points in the Guideline “On Value Added Tax”, which regulate the supply of services from abroad, the supply of medicaments, health-related services, education-related services, etc.

On 17 November 2011, the Parliament of the Republic of Albania adopted the Law No. 10481 “On some Amendments to Law No. 9662, dated 18 February 2006 “On Banks in the Republic of Albania”. The amendments to this Law aim at further approximation of the Law “On Banks in the Republic of Albania” to EU Directives in the area of banking and financial services and handling and solution of non-performing banks. In this context, banking activity is redefined by removing the exclusive right of banking institutions to issue means of payments in the form of electronic money. In addition, an important amendment is made to the existing Law relating to the definition of systemic risk as the risk related to factors that may threaten the stability, asset value and confidence in the banking and financial system or market. In view of supplementing the tools and techniques widely used by the supervisory authorities to handle and solve non-performing banks, this Law also introduces the term “bridge bank” as a temporary solution for a non-performing bank, allowing the latter to continue the operations until a permanent solution can be found.
On 17 November 2011, the Parliament of the Republic of Albania approved the Decision No. 142 “On the Appointment of the Governor of the Bank of Albania”. According to this Decision, Mr. Ardian Fullani is appointed Governor of the Republic of Albania.

On 5 December 2011, the Parliament of the Republic of Albania adopted the Law No. 10487 “On 2012 Budget”. According to this Law, State Budget revenues for 2012 are projected to amount to ALL 281,622 million and expenditures to ALL 322,785 million. Budget deficit is expected to be ALL 41,163 million. The threshold limit of the state budget deficit financing through domestic and foreign resources is ALL 41,163 million, of which ALL 300 million shall be financed through privatization receipts.

On 15 December 2011, the Parliament of the Republic of Albania adopted the Law No. 10489 “On Trade and Supervision of Non-Food Products Market”. The purpose of this Law is to determine the rights and obligations of economic operators in order to guarantee their compliance with the legal requirements. The Law also establishes the organization mode, rights and competences of the responsible structure, as well as the principles for the control of imported products entering the Albanian territory, in cooperation with the customs authorities.

On 27 December 2011, the Minister of Finance approved the Guideline No. 30 “On Asset Management in Public Sector Entities”. The purpose of this Guideline is to establish the standard procedures and the audit trail for the documentation, preservation, circulation and removal from use of assets in the public sector entities. The Guideline establishes that all public sector entities have the obligation to take the necessary measures for the documentation, protection, circulation and removal from use of assets, in order to manage them efficiently and preserve them from damage and misuse.
BANK OF ALBANIA MANAGEMENT, AS AT 31 DECEMBER 2011

SUPERVISORY COUNCIL

ARDIAN FULLANI Chairman
ELISABETA GJONI Vice Chairwoman
ADRIAN CIVICI Member
ARJAN KADAREJA Member
DHORI KUJE Member
ELA GOLEMI Member
ERMELINDA MEKSI Member
HALIT XHABA Member
PETRAQ MILO Member

GOVERNOR

ARDIAN FULLANI

DEPUTY GOVERNORS

ELISABETA GJONI First Deputy Governor

GENERAL INSPECTOR

ELVAR GOLEMI

GOVERNOR’S OFFICE

GENC MAMANI

HEAD OF COORDINATION

GRAMOZ 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 Klodian Shehu
INFORMATION TECHNOLOGY DEPARTMENT Xhilda Deliana
STATISTICS DEPARTMENT Diana Shtylla
ISSUE DEPARTMENT Dorian Çollaku
ACCOUNTING AND FINANCE DEPARTMENT Fatos Ibrahimimi
PAYMENTS SYSTEM DEPARTMENT Dashmir Halilaj
LEGAL DEPARTMENT Toni Gogu
AUDIT DEPARTMENT Elvar Golemi
FOREIGN RELATIONS, EUROPEAN INTEGRATION AND COMMUNICATION DEPARTMENT Oneda Andoni
ADMINISTRATION DEPARTMENT Agron Skënderaga
SECURITY AND PROTECTION DEPARTMENT Eduard Sinani

BRANCHES

SHKODRA Ermita Istrefi
ELBASANI Valentina Dedja
GJIROKASTRA Anila Thomaçi
KORÇA Liliana Zjarri
LUSHNJA Shpresa Meço
BANKS AND BRANCHES OF FOREIGN BANKS LICENSED BY THE BANK OF ALBANIA, AS AT 31 DECEMBER 2011

1. RAFFEISEN BANK SH.A.
Licence No. 2/1998, dated 11.01.1999
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 SH.A.
Licence No. 3/1998, dated 11.01.1999
Certificate No. 3 “On Deposit Insurance”
Director: Hikmet GÜLER
Address: Rruga e 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: www.uba.com.al

3. VENETO BANKA SH.A.
Licence No. 5/1998, dated 11.01.1999
Certificate No. 4 “On Deposit Insurance”
Director: Lucio Luigi GAITA
Address: Bulevardi “Dëshmorët e Kombit”, Ndërtesa Kullat Binjake, Tirana, Albania
Tel: +355 4 2280 555
Fax: +355 4 2280 356
E-mail: info@venetobanka.al
Website: www.venetobanka.al

4. NATIONAL COMMERCIAL BANK SH.A.
Licence No. 6/1998, dated 11.01.1999
Approved by the Bank of Albania Supervisory Council Decision 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
5. TIRANA BANK SH.A.
Licence No. 7, dated 12.09.1996
Approved by the Bank of Albania Supervisory Council Decision No. 9, dated 12.09.1996
Certificate No. 6 “On Deposit Insurance”
Director: Georgios CHARALAMPAKIS
Address: Rruga “Dëshmorët e 4 Shkurtit”, Tiranë
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 – ALBANIA BRANCH
Licence No. 8, dated 25.11.1996
Approved by the Bank of Albania Supervisory Council Decision No. 4, dated 14.03.1996.
Certificate No. 7 “On Deposit Insurance”
Director: Ioannis KOUGIONAS
Address: Rruga e 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 SH.A.
Licence No. 09, dated 20.02.1997
Approved by the Bank of Albania Supervisory Council Decision No. 9, dated 30.04.1996
Certificate No. 8 “On Deposit Insurance”
Director: Gideon van den BROEK
Address: Qendra e Biznesit, Rruga “Murat Toptani”, Tirana, Albania
Tel: +355 4 2254 372 / 2256 254
Tel/Fax: +355 4 2254 368
E-mail: info@icbank-albania.com
Website: -

8. ALPHA BANK - ALBANIA
Licence No. 10, dated 07.01.1998
Approved by the Bank of Albania Supervisory Council Decision, 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
Tel/faks: +355 4 2232 102
E-mail: tiranabanch@alpha.gr
Website: -

9. INTESA SANPaOLO BANK ALBANIA SH.A.
Licence No. 11, dated 10.08.1998
Approved by the Bank of Albania Supervisory Council Decision, No. 105, dated 10.08.1998
Certificate No. 10 “On Deposit Insurance”
Director: Stefano FARABBI
Address: Rruga “Ismail Qemalë” Nr. 27, P.O. Box 8319, Tirana, Albania
10. PROCREDIT BANK SH.A.
Licence No. 12, dated 15.03.1999
Approved by the Bank of Albania Supervisory Council Decision No. 22, dated 03.03.1999
Certificate No. 11 “On Deposit Insurance”
Director: Flutura VEIP
Address: Rruga e 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 - ALBANIA SH.A.
Licence No. 14, dated 28.10.1999
Certificate No. 13 “On Deposit Insurance”
Director: Luc BEISO
Address: Rruga e 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 SH.A.
Licence No. 15, dated 28.08.2002
Approved by the Bank of Albania Supervisory Council Decision 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 SH.A.
Licence No. 16, dated 31.03.2003
Approved by the Bank of Albania Supervisory Council Decision 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. SOCIETE GENERALE ALBANIA BANK SH.A.
Licence No. 17, dated 16.02.2004
Approved by the Bank of Albania Supervisory Council Decision No. 06, dated 11.02.2004
Certificate No. 16 “On Deposit Insurance”
Director: Hubert de SAINT JEAN
15. UNION BANK SH.A.
Licence No. 18, dated 09.01.2006
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 ALBANIA SH.A.
Licence No. 19, dated 06.07.2007.
Approved by the Bank of Albania Supervisory Council Decision No. 35, dated 27.06.2007
Certificate No. 12 “On Deposit Insurance”
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 at 31 December 2011 licensed the following entities:

<table>
<thead>
<tr>
<th>Nr.</th>
<th>ENTITIES</th>
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<tbody>
<tr>
<td>19</td>
<td>NON-BANK INSTITUTIONS</td>
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<tr>
<td>301</td>
<td>FOREIGN EXCHANGE BUREAUS</td>
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<tr>
<td>2</td>
<td>UNIONS OF SAVINGS AND CREDIT ASSOCIATIONS</td>
</tr>
<tr>
<td>126</td>
<td>SAVINGS AND CREDIT ASSOCIATIONS</td>
</tr>
<tr>
<td>1</td>
<td>REPRESENTATIVE OFFICE OF FOREIGN BANKS</td>
</tr>
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PUBLICATIONS ISSUED BY THE BANK OF ALBANIA OVER 2011

This list was designed to inform readers about publications issued by the Bank of Albania over the first half of 2011. 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 2011. This list does not include surveys carried out by the Bank of Albania as they are available only online (http://www.bankofalbania.org/web/Surveys_3405_2.php?kc=0,22,15,0,0).

ANNUAL REPORT:
Annual Report 2010

FINANCIAL STABILITY REPORT:
Financial Stability Report 2010 H2
Financial Stability Report 2011 H1

SUPERVISION ANNUAL REPORT:
Supervision Annual Report 2010

MONETARY POLICY PERIODICAL REPORTS:
Monetary Policy Report for the Fourth Quarter of 2010
Monetary Policy Report for the First Quarter of 2011
Monetary Policy Report for the Second Quarter of 2011
Monetary Policy Report for the Third Quarter of 2011

PUBLICATIONS ON STATISTICS:
Statistical Report (Published monthly)
OFFICIAL BULLETIN:
Official Bulletin - Volume 13, no. 1 Year 2011
Official Bulletin - Volume 13, no. 2 Year 2011
Official Bulletin - Volume 13, no. 3 Year 2011
Official Bulletin - Volume 13, no. 4 Year 2011
Official Bulletin - Volume 13, no. 5 Year 2011
Official Bulletin - Volume 13, no. 6 Year 2011
Official Bulletin - Volume 13, no. 7 Year 2011
Official Bulletin - Volume 13, no. 8 Year 2011
Official Bulletin - Volume 13, no. 9 Year 2011
Official Bulletin - Volume 13, no. 10 Year 2011
Official Bulletin - Volume 13, no. 11 Year 2011

BULLETIN OF THE BANK OF ALBANIA:
Bulletin of the Bank of Albania - 2010 H2
Bulletin of the Bank of Albania - 2011 H1

WORKING PAPERS:
Competitive Position of the Albanian Economy in Terms of Productivity and Labour Cost - Evelina Çeliku, Iris Metani
Estimation of Weights for the Monetary Conditions Index in Albania – Oriela Kodra
The Persistence of Inflation in Albania – Vasilika Kota
Analysis of the Albanian Banking System in a Risk-Performance Framework – Irini Kalluci
The Equilibrium Real Exchange Rate of Lek vis-à-vis Euro: Is it much Misaligned? - Ilir Vika, Erion Luçi
A Bayesian Estimation of a Small Structural Model for the Albanian Economy - Elona Dushku, Vasilika Kota
Macroeconomic Effects of Fiscal Policy in Albania: A SVAR Approach - Armela Mançellari

SCIENTIFIC NOVELTIES AT THE BANK OF ALBANIA:
Scientific Novelties at the Bank of Albania No. 5
Scientific Novelties at the Bank of Albania No. 6

EDUCATIONAL AND INFORMATIVE PUBLICATIONS:
Brochure “Significance of Albanian Banknotes”
Brochure “7 Short Lessons on Money”
Leaflet “The Journey of Currency”
Brochure “The European Central Bank; the Eurosystem; the European System of Central Banks”
Brochure “Credit Registry” (reprint)
Brochure “What is a Report on the Borrower?” (reprint)
Brochure “Research and Training Centre of the Bank of Albania in Berat” (available only in English)
Leaflet “Personal Finances in Your Hands”
OTHER:
“Economic Policies in SEE: Design, Performance and Challenges” - Edited by Ardian Fullani (available only in English)