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I. GOVERNOR’S SPEECH

The Albanian economy has just left behind a difficult year. The deep global economic crisis was soon felt even in Albania, testing the foundations of the economy: the financial stability and the macroeconomic balances. However, the good initial state of our economy and the proper response of macroeconomic policies helped to successfully cope with this test. During the first three quarters of the year, the Albanian economy ensured a positive growth, thus preserving the financial stability and the key indicators of macroeconomic stability: price stability, public debt level and balance of payments sustainability.

The global economic and financial crisis, which was significantly intensified during the first half of the year, put in question the financial system sustainability, the macroeconomic stability and the long-term development prospects of the world economy. The determined response of public authorities, increased coordination of economic policies and keeping open the world trade channels, helped preventing any negative economic spirals. The latest data on the global economy indicate a recovery of economic activity in the third quarter onwards. The monetary and fiscal stimulus packages resulted successful in terms of stabilising the global economy. The recovery of economic growth in the main developed countries and the positive performance of the largest emerging countries are accompanied by the upsurge of the demand at world level and the reduction of uncertainty in financial markets. These positive signals, confirmed by the improvement of confidence sentiment, are reflected on more optimistic forecasts for the future.

However, the sustainability of global economic growth will remain fragile, as long as the economic activity continues to rely on significant monetary and fiscal stimuli. In particular, the public debt sustainability, which is burdened by fiscal stimulus bill to exit the crisis, is becoming a more and more aggravated problem for many countries. In this complex situation, choosing the right moment for withdrawing the economic incentive will have a decisive importance in the future economic performance.

In a more structural aspect, the recent crisis is expected to leave visible traces in the economic development. In a long-term horizon, it seems that new economic and strategic balances are being determined, thus re-dimensioning the poles of global economic growth. In a medium-term horizon, the global economic growth rate is expected to converge in a lower balance than the one that has prevailed over the last two decades. This slowdown may be accompanied by economic and social problems for those countries, which would not know how
to figure out their relevant implications. In a short-term horizon, discussions on the state’s role in the economy, on economic development and growth patterns, on the philosophy and appropriate practices regulating the financial markets, will dominate the political round-table debates. In particular, the economic growth model will be a sensitive topic for economies significantly affected by the crisis, including many Eastern European countries. Promoting competitive advantage and increasing competitiveness in global markets will be the subject of discussions and intended reforms.

Turning to domestic economic developments, the analysis of available indicators shows that the Albanian economy has had a positive economic growth during the first nine months of the year. However, these indicators suggest that the growth rate was characterized by a progressive slowdown during 2009. Such performance was conditioned by reduced foreign demand and slowed domestic demand, in the presence of a tight liquidity situation, financing restriction and increased uncertainty. According to preliminary data from INSTAT, the economic growth for the first nine-month period of the year was 4.9 percent, against 7.8 percent recorded for the same period of the previous year. In sectoral terms, the sectors that benefited most from the economic growth are the services and construction one, while the industry sector underwent a more problematic performance.

The positive growth rate has been supported by the fiscal stimulus, while consumer demand and the contribution of external sector to the economy have been relatively stable. At the same time, private investments have declined. Consumer demand has been supported by a slight rise in employment and wages, while the mortgage and consumer credit contraction, as well as reduction of remittances have given the reverse effect. Private investments have been contracted, as a consequence of limited financing resources, reduced lending support by the banking system and limited access to international capital markets. Increased uncertainty, slowed progress of the final demand for their products and reduced capacity utilization rate have impacted on such performance. Effects of domestic economic slowdown and the global economic crisis have appeared even in the foreign trade. Foreign economic activity is characterized by a simultaneous decline in both, exports and imports of goods and services, thus impacting significantly on the economic growth for 2009. On the other hand, fiscal stimulus, injected mainly during the first half of the year, has contributed to rapid increase of budget spending and public debt.

The economic growth below the potential has created an environment of generally reduced inflationary pressures. The annual inflation for December recorded 3.5 percent, while the average annual inflation rate was 2.2 percent. Both these indicators are in line with Bank of Albania’s target on price stability. The economic activity slowdown, low main products prices in the world markets, low monetary expansion in the economy and controlled inflationary expectations offset the inflationary pressures coming from exchange rate depreciation during 2009.
The upward inflation trend during the last quarter of 2009 was expected by the Bank of Albania. It was formed mostly by transitory factors, which are not expected to generate steady inflationary pressures. In particular, this performance was influenced by rising food prices, which reflect the lagging effect of exchange rate depreciation, international markets conjunctures and structural problems of the Albanian market. These factors are expected to exert inflationary pressures during the first half of 2010, possibly added by expected reduction of agricultural products supply, as a result of the flooding that has lately occurred. However, stable core inflation trend and low inflation rate of non-traded goods confirm that inflationary pressures exerted by domestic demand are moderate. In the absence of other supply shocks, the slow progress of domestic demand, low growth of monetary supply and anchored inflationary expectations, are premises for keeping inflation within the target in the medium run.

The Bank of Albania pursued a prudent monetary policy during 2009, creating a suitable environment for a balanced development of the economy and for keeping inflationary pressures under control. In the presence of downward inflationary pressures and steady expectations, the hints for slow domestic demand in the next period have motivated the progressive growth of monetary stimulus during 2009. The Bank of Albania cut the key interest rate by one percentage point, down to 5.25 per cent during this period. It also steadily increased liquidity injection, according to banking system needs for liquidity and the economy demand for funding. Concerning liquidity injection, the Bank of Albania has made use of the entire range of monetary policy injecting instruments, facilitating at the same time the access to and easing the cost of operation of the banking system with Bank of Albania. Hence, we have also cut the overnight credit interest rate, raised the allowed level of mandatory reserve use and we have increase the accepted collateral base in our transactions.

in the presence of the exchange rate depreciation, such policy has brought about easing monetary conditions, serving the promotion of the economic activity. However, the pass-through of easing monitoring policy on interest rates of banking products has been limited, due to liquidity constraints of the banking system and weakened demand of the public sector for funds. On the other hand, the banking system itself has been reserved with regards to lending, as a result of the increased risk in the economy and performance of loan portfolio quality. The alleviation of these problems would help to more fully transmit the monetary policy and enhance its effectiveness.

The country’s external position continues to be characterized by a high and upward current account deficit. During the first three quarters of the year, the deficit was fully covered by capital and financial account inflows, resulting in increased foreign exchange reserves of the Bank of Albania. However, the inflows have been significantly favoured by privatization receipts and by public sector borrowing. Both these items are limited in time and size, making necessary a steadier correction of the external position of our economy. This correction should aim at covering the trade deficit with stable funding resources, in the form of foreign direct investments and promoting export industries in branches that may constitute a competitive advantage for Albania.
However, short-term developments in foreign trade for October to November show a somewhat different performance compared with the first nine months of the year, testifying a modification of the trends observed earlier. Thus, the country’s exports fell in annual average terms by about 7.4 percent, recording a slowdown in comparison with the average decline by about 19 percent during the first nine months of the year. On the other hand, imports recorded an annual average decline of 17% over these two months, compared with the average annual decline of 7 percent recorded in 2009. These developments contain encouraging signs for sustainability of the balance of payments in the short run.

Fiscal policy had an expansionary nature during most of the year, being materialized in a budget deficit of 6 percent of GDP. The increase of budget deficit reflects both the action of automatic stabilizer in the form of decreased revenues, and the intended countercyclical character of fiscal policy, through increased wages and capital expenditures. The country’s economic activity slowdown has dictated a slow pace in budget revenue growth, especially after the first quarter of the year. In late November, the annual growth of budget revenues was only 2 percent, almost entirely reflecting the low pace of generating the tax revenues. On the other hand, public expenditures have maintained high growth rates, accounting for 16.4 percent in November. The deficit has been mostly financed through foreign borrowing and privatization receipts, dampening the pressures in the domestic financial market.

Rapid growth of expenditure and budget deficit during 2009 has further increased the public debt level, accounting for 58 per cent of GDP at the end of November. The Bank of Albania deems that the future budget policy orientation towards fiscal consolidation, aiming at reducing the public debt, is now a prerequisite for the macroeconomic stability in the country. As we have constantly stated, the public debt reduction will mitigate the pressure of the public sector on the financial markets, creating more room for the private sector. Consolidation of public finances will also lower the risk premiums in the economy and will raise the monetary policy effectiveness.

Monetary supply slowed down further in the second half, reflecting to a great extent, the ever lower credit growth. Annual growth of private sector loan portfolio slowed down to 10 percent in November. Unlike the first six months of 2009, when credit growth curbing was more affected by the tightened supply, in the second half of the year the credit performance was dictated by decreased demand for loans. The economic activity slowdown and uncertainty about the future, in the face of still tightening lending terms by banks, have guided the economic agents’ decisions to postpone the investment plans and to less finance consumption from borrowing.

However, monetary developments confirm an improved situation of deposits during the second half of 2009. The change in depositors’ behaviour, in the context of measures taken to prevent the spread of global crisis effects, and the foreign currency inflows in the form of remittances during summer, have contributed to stabilizing the liquidity situation of the banking system.
Financial markets were characterized by a more relaxed situation during the second half of the year. The banking system continued to be featured by liquidity constraints, which were remedied by central bank liquidity injections. Improved liquidity situation due to increased deposits in the system and fostered certainty in the market created a suitable environment for transmitting the monetary policy signal to the interbank market. The key interest rate cut at the end of October is followed by reduced yields on government securities, after the upward trend characterizing them throughout the year. In the meantime, the Bank of Albania, in accordance with time lags that characterize the monetary policy transmission mechanism, expects and requires that the key interest rate cut be transmitted to credit markets.

II. DEVELOPMENTS IN THE WORLD ECONOMY

The positive signals transmitted from the developed and emerging economies markets, from some months now, have strengthened the opinion on the return of economic growth at positive values. The most recent data reveal that after the economic slowdown of the first half of year, economies of the main developed countries and of a number of emerging countries have recorded an economic growth in the third quarter and onwards. The improvement of economic situation owes to the successful encouraging monetary and fiscal policies undertaken since the beginning of global economic recession in the world. The core effect of high prices of the previous year imposed inflation to remain at low rates, but in the recent months, it entered into a positive territory owing to the increase of oil price.

II.1 ECONOMIC GROWTH AND MACROECONOMIC BALANCES

The economies of the main developed countries and of a part of emerging countries after the economic slowdown of the first half of year, experienced an economic growth in the third quarter and onwards. The improvement of confidence sentiments, the demand and trade growth at world level are some of signals which show the positive momentum of the world economy. However, the temporary nature of a number of stimuli staying behind this positive performance provide an advice for a more cautious and mature interpretation of many of the indicators.

<table>
<thead>
<tr>
<th>Countries</th>
<th>GDP change Q3-09/Q3-08</th>
<th>Unemployment rate Q3-09/Q2-09</th>
<th>November 2009</th>
<th>Inflation rate December 2009/December -08</th>
</tr>
</thead>
<tbody>
<tr>
<td>USA</td>
<td>-2.6</td>
<td>2.2</td>
<td>10.0</td>
<td>1.81</td>
</tr>
<tr>
<td>Euro-Zone</td>
<td>-4.0</td>
<td>0.4</td>
<td>10.0</td>
<td>0.9</td>
</tr>
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<td>Germany</td>
<td>-4.8</td>
<td>0.7</td>
<td>7.6</td>
<td>0.8</td>
</tr>
<tr>
<td>Greece</td>
<td>-1.7</td>
<td>-0.4</td>
<td>9.12</td>
<td>2.6</td>
</tr>
<tr>
<td>Italy</td>
<td>-4.6</td>
<td>0.6</td>
<td>8.3</td>
<td>1.1</td>
</tr>
<tr>
<td>Japan</td>
<td>-3.7</td>
<td>0.3</td>
<td>5.2</td>
<td>-1.92</td>
</tr>
</tbody>
</table>

Source: Eurostat, Respective statistical institutions
1 Data for December 2 Data for September 3 Data for November
The economic activity in the Euro-zone, during the third quarter 2009, grew by 0.4 percent relative to the previous quarter, while in annual terms it shrank by 4 percent. This increase marked the Euro-zone exit from recession and comes after five quarters of economic activity negative growth. It is mainly grounded on the upsurge of the trade activity and government expenditures mainly due to the economic incentives packages undertaken from the governments of these countries. While consumer spending and investments affected negatively the economic growth rate. Surveys data reveal that the same behaviour is expected to show up even in the forth quarter of 2009 and in 2010 where the growth shall continue to remain a positive one, but at controlled rates. Unemployment rate continued its increasing trend pointing to 10 percent in November 2009. This rate shows amongst the highest of this decade. In accordance with preliminary data, annual inflation in Euro-zone pointed to 0.9 percent, in December, pursuing its climbing trend. The average rate for the forth quarter points to 0.4 percent, while in the third quarter, the latter recorded negative values. The base effect reduction of the high prices in the previous year caused that only in last months of year, inflation rate shifted to positive values.

Economic activity in United States of America has been improved progressively since the third quarter of 2009. Therefore, final estimations on GDP performance denote an economic growth of about 2.2 percent in quarterly basis. Consumer spending, aggregate investments and exports were the main economic indices which impacted the GDP growth. These indicators increased by 2.8, 5.0 and 17.8 percent, respectively in quarterly terms. Imports grew as well, thus providing a negative impact on GDP calculation. As regard the economic performance during the forth quarter of year, indicators about production industry in USA show a more accelerated upsurge trend relative to its third quarter. Annual average inflation rate, (during July-November) pointed to -2.9 percent, while the average unemployment rate pointed to 9.8 percent in the second half of year.

Economies of BRIC countries after a weakening of the economy growth paces until to its contraction, as in case of Brazil and Russia, recorded an improvement of economic conditions during the second half of year. Economy of China, during second half of year, is supported by the accelerated expenditures of Government and the improved production indicators. While, production growth in the Indian processing industry has effected the recovery of the increasing tendency industry at the rate noted prior to the crisis. In Russia, the rise of oil price, during the second half of year, has assisted the country to exit the crisis. In Brazil, the growth of both the domestic demand and exports supported the moderate expansion of GDP during the third quarter of year compared to the previous quarter.

<table>
<thead>
<tr>
<th>Countries</th>
<th>Annual change of real GDP</th>
<th>Annual inflation</th>
</tr>
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<tbody>
<tr>
<td></td>
<td>Q3-09</td>
<td>2009&lt;sup&gt;1&lt;/sup&gt;</td>
</tr>
<tr>
<td>Brazil</td>
<td>-1.2</td>
<td>-0.7</td>
</tr>
<tr>
<td>Russia</td>
<td>-9.4</td>
<td>-7.5</td>
</tr>
<tr>
<td>India</td>
<td>7.1</td>
<td>5.4</td>
</tr>
<tr>
<td>China</td>
<td>8.9</td>
<td>8.5</td>
</tr>
</tbody>
</table>

Source: IMF, OECD, Respective Statistical Institutes
<sup>1</sup> IMF estimations, October.<sup>2</sup> Data for December
<sup>3</sup> Data for October
During the first half of year, economic activity in Italy recorded the first signs of recovery. Therefore, GDP marked a positive growth pace during the third quarter of year, after fifth quarters of consecutive contraction. GDP expanded by 0.6 percent in annual terms meanwhile the consumer expenses and investments’ upsurge provided the main contribution. In the meantime, the Italian Government expenditures recorded a fall. The latest economic data on the activity performance during forth quarter of year reveal a further improvement of some of the main indicators. Unemployment rate pursued the increasing trend and in November pointed to 8.3 percent. The average annual inflation rate was 0.5 percent in the second half of year.

Economy of Greece, during second half of 2009, manifested signs of economic slowdown, after a relatively sufficient growth period, during the first half of year. Thus, third quarter of year recorded a contraction of GDP by approximately 1.7 percent relative to the same period of previous year. The fall of aggregate investments and the drop of exports provided the main contribution to this reduction. They reduced by 18.6 and 21.7 percent, respectively in annual terms. Regarding the forth quarter of year, the latest data show a further deterioration of the economic activity. The largest risk being manifested during the last quarter of year originates from the accelerated growth of the budget deficit and public debt ratio against GDP. The latter pointed to 112 percent during 2009 and is expected to raise onwards during the next year. Unemployment rate for September was 9.1 percent, while the average annual inflation rate pointed to 1.5 percent in the second half of year.

During third quarter of 2009, the economy in Turkey recorded a negative annual economic growth of -3.3 percent, while compared to the previous quarter, it recorded a growth by 2.7 percent. Consumer expenses provided a positive impact by adding about 0.5 percentage points to the annual growth. Private investments, notwithstanding their negative impact, recorded a slowdown of the falling pace. Preliminary data denote a lower demand and restricted production, which suggest that the forth quarter shall maintain the same rates of the third quarter. Unemployment for February remained at 13.4 percent, equal to the value of August, however it is increased by 2.7 percentage points relative to the previous year. Inflation recorded the annual rate of 5.7 percent in the forth quarter of year 2009.

The economy of the former Yugoslavian Republic of Macedonia pursued the declining trend during the third quarter of 2009, therefore it shrank by -1.8 percent relative to the same period of previous year. This fall owes to the decline of consumer spending and the accelerated reduction of investments, whose impact is loosened somewhat by a high decline of imports and growth of public expenditures. Given the deteriorated economic situation, the increase of public expenditures caused that unemployment recorded a drop in the third quarter pointing to 31.7 percent from 33 percent in 2008. Annual inflation rate in the forth quarter pointed to -2.1 percent, thus reducing the average annual rate of 2009 to -0.8 percent from 8.3 percent in 2008.
According to statistics of Kosovo Statistics Office, economic growth in 2009 was 6.1 percent. Consumer spending and investments grew considerably, while exports are reduced significantly. IMF forecasts reveal a growth of 4 percent in 2009. Consume Index Price continue to remain at negative values, recording the annual value of -1.3 percent in November 2009, meanwhile in the third quarter it pointed to -3.1 percent. These low rates were present since January 2009, meanwhile the lowest rate was recorded in May (-4.4 percent). These deflationary developments owed to the fall of foodstuff and transports prices, whereas the electric energy and fuels price recorded a slight increase.

### Table 3 Economic indicators for the regional economies

<table>
<thead>
<tr>
<th></th>
<th>Change of GDP</th>
<th>Annual Inflation</th>
<th>Unemployment rate</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Q3:09</td>
<td>December-09</td>
<td>November-09</td>
</tr>
<tr>
<td>Italy</td>
<td>-4.6</td>
<td>1.1</td>
<td>8.3</td>
</tr>
<tr>
<td>Greece</td>
<td>-1.7</td>
<td>2.6</td>
<td>9.1</td>
</tr>
<tr>
<td>Macedonia</td>
<td>-1.8</td>
<td>-1.6</td>
<td>31.7</td>
</tr>
<tr>
<td>Serbia</td>
<td>-2.3</td>
<td>6.6</td>
<td>16.6</td>
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<tr>
<td>Croatia</td>
<td>-5.7</td>
<td>1.9</td>
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<tr>
<td>Turkey</td>
<td>-3.3</td>
<td>6.5</td>
<td>13.0</td>
</tr>
<tr>
<td>Kosovo</td>
<td>:</td>
<td>-1.3</td>
<td>13.0</td>
</tr>
<tr>
<td>Albania</td>
<td>4.1</td>
<td>3.5</td>
<td>12.8</td>
</tr>
</tbody>
</table>

Source: Respective Statistical Institutes, EuroStat, EcoFin, IMF

1 Data for November
2 Data for September. 3 Data for the third quarter
4 Data for October: Unavailable data

### II.2 MONETARY POLICY, FINANCIAL MARKETS AND THE EXCHANGE RATE

During the second half of year, none of central banks change the key interest rate. These banks deemed the current rates appropriate to establish an encouraging environment for the economic growth.

The European Central Bank has kept its rate at 1 percent, whereas it decreased the latter 4 times during the first half of year. Federal Reserve kept its interest rate at 0-0.25 percent throughout the year. Bank of England kept the key interest rate at 0.5 percent during the second half of year, whereas it cuts the latter three times in the first half of year. The Bank of Japan did not change its reference interest rate (the over-night interbank interest rate), keeping it at 0.1 percent throughout 2009.

The financial markets have manifested positive development and controlled volatility during these months. The interest rates in these markets pursued the fall started since the beginning of year, by confirming the neutralisation of tensions and the
overall improvement occurring in all segments of the market. The developed and emerging economies markets are transmitting positive signals from some months now. These positive signals have strengthened the recovery of the economic growth at positive rates. Notwithstanding the main part of this growth owes to the stimuli and encouraging policies implemented by the main central institutions of the world, the current positive performance reflects the sustained improvement in the context of controlled risks.

Since July, Libor and Eurobor interest rates continue to fall in the money market, thus transmitting the neutralisation of pressures for liquidity and the decrease of risk primes. 1-, 3- and 6-month Euribor interest rates at the end of this year fell averagely by 43, 55 and 44 basis points relative to the end of first half of year, whereas the 3-month Libor rate reduced by 37 basis points. The 1-, 3- and 6-month Euribor interest rates recorded 0.48, 0.68 and 0.99 percent respectively in average terms, during this month. The 3-month Libor rate diminished to 0.25 percent.

The appreciating performance of Euro against US dollar, British pound as well as against many Asian currencies related to the US currency is distinguished during this half of year in the exchange market. Euro is also appreciated against Japanese yen and other European currencies. At the end of this year EUR 1 was equal to USD 1.44, while at average terms in this half of year it was estimated 9.1 percent relative to the preceding period.

II.3 OIL AND COMMODITY PRICE DEVELOPMENT

Oil price per barrel in the international market increased during the second half of year compared to its first half, pointing to values close to those of year 2005. Thus, the average price pointed to USD 70.9 for the analysed period, approximately 40 percent higher than the average of the first half of year. The improvement of economic environment in the developed countries,
mainly the positive performance in USA, and the high demand of the emerging countries impacted the strengthening of the oil price climbing trend.

In the meantime, during the recent months of year, the ambiguities as regards to the future economic growth paces in OECD countries, the problems in respect of the high accumulated debt in some of Persian Gulf countries and the strengthening of US dollar versus some of main international currencies affected the fall of oil price. Regarding the supply, the latter increased during the second half of year relative to the first half, mainly during October-December. This is due to the production growth in Russia and in OPEC member countries.

The main indices manifested negative changes during the second half of year relative to the same period of previous year, while they reveal positive growth when compare with the first half of year 2009. Considering that the quarterly changes manifest an upsurge tendency throughout the year for almost all indicators, the negative values of annual growth are due to the base effect of previous year high prices. Commodity Price Index showed an annual growth of 16 percent in the forth quarter 2009, and compared to the third quarter of year increased by 8.4 percent. The increase of food, fuels and metals’ prices were the main incentives of this upsurge, which show an improvement of the world economic conditions. Food Price Index in the forth quarter of year raised by 10 percent relative to the forth quarter of 2008, while the quarterly increase was 1.3 percent. Fuel Price Index climbed by 17.1 percent annually and by 10.2 percent quarterly.

III. PRICE STABILITY AND BANK OF ALBANIA TARGET

The achievement and maintaining of price stability is the main objective of the Bank of Albania. This is the major contribution the central bank can give to stimulating savings and attracting productive investments to sustain a consistent economic growth. In line with its strategy, the Bank of Albania is committed to achieving and maintaining an annual inflation of 3.0 percent, with a +/- 1 percentage point tolerance. The publication of the qualitative objective on inflation aims at anchoring the economic agents’ expectations and the decrease of inflation risk primes.
III.1 CONSUMER PRICE, INFLATION TARGET AND MONETARY POLICY

The inflation rate recorded the value 3.5 percent at the end of 2009. Average annual inflation pointed to 2.2 percent, close to the lower limit of 3.0 percent Bank of Albania’s targeted band. Average annual inflation rate appears 1.2 percentage points lower relative to the previous year, displaying moderated inflationary pressures. The fall of raw materials price, the statistical effect of managed prices and the weak pressures conducted by the demand at home, provided a contribution to the low inflation rates within an environment with a depreciating tendency of the exchange rate.

Macroeconomic developments at home during 2009 were shaped in the context of the global economic downturn. These developments were characterised by a progressive slowdown of economic growth pace owing to the reduction of both external and domestic demand and under the presence of liquidity tightening conditions. They were also accompanied by reduced inflationary pressures. According to INSTAT preliminary data, economic growth for the first 9-month period of year pointed to 4.9 percent, thus slowing down from 5.4 percent in the first quarter to 4.1 percent in the third quarter. The economic growth in the previous year pointed to 7.8 percent for the same period. Private investments contracted along with the fall of the external demand\(^4\). The restricted external and domestic funding sources and the increased attention on the conduction of expenses, mainly for investments in an uncertain context regarding the accomplishment of future revenues- contributed to the tightening of the private investments.

Trade deficit narrowed by about 6 percent annually in the first 9-month period of year. The sustainability of consumer demand\(^5\) and the fiscal stimulus\(^6\), along with the easing monetary conditions, supported the positive rates of the domestic demand growth notwithstanding at lower paces than in the previous years. The slowdown both the demand and economic activity led to the slight raise of unemployment. Different indicators of costs in economy signal a slight declining trend in labour cost per produced item and a fall in imports and production prices\(^7\). The operation of demand and supply factors lead to the expansion of production negative gap\(^8\), that has balanced the inflationary pressures of the exchange rate deprecation. ALL depreciation during this year is transmitted considerably to the tradable consumer prices. Tradable goods inflation increased progressively since June recording the highest growth rate of 4.9 percent in December. Based on empiric studies\(^9\), the transmission degree of the exchange rate effect on consumer prices pointed the maximum after 9 months.
The Bank of Albania implemented a cautious monetary policy, during the year 2009, by providing adequate conditions for an equilibrated development given the considerable uncertainty situation. Given that inflation, the forecasts and economic agents’ expectations remain within the tolerance band around the target of 3 percent, the signals on the slowdown of the domestic demand in the forthcoming period encouraged the upsurge of monetary stimulus. Bank of Albania decided to cut the key interest rate in two cases, in January and October 2009, pointing to 5.25 percent from 6.25 percent at the end of 2008. Along with the cut of the key interest rate, Bank of Albania has employed its entire operating framework to inject liquidity in economy. The return of exchange rate on the depreciating direction, at the end of third quarter and almost throughout the forth quarter of year, being strengthened from the easing measures of interest rate decrease, supported the dropping trend of the monetary conditions’ index. The easing of monetary conditions, in the presence of slowing tendencies of the economy, has established the needed premises for the encouragement of aggregate demand and the observation of inflation target.

The recent data regarding the world economy signal a stabilisation of forecasts on the economic growth and raw materials prices in the international market. Risks against price stability at home for the ongoing period are estimated to be relatively balanced, in absence of unexpected shocks from the supply side. The slowdown of monetary supply, the softening of fiscal stimulus, the estimates for the slowdown of the domestic demand and economic activity paces and the low rate of producing capacities utilisation are assessed to have balance the inflationary pressures generated by the supply factors, such as the exchange rate and the projected rise of the administered energy price.
III.2 PRICE PERFORMANCE OF MAIN CPI BASKET ITEMS

The monthly inflation rate of December recorded the highest annual inflation rate of 3.5 percent for the year 2009. This rate resulted 1.3 percentage points higher relative to the average inflation rate during 2009, thus confirming the strong climbing trend during the last quarter of this year. An increase of the foodstuffs inflation rate is observed during the second half of year, especially of vegetables and fruits. This growth is more highlighted in the last months of year, which are deemed to have been characterised by the typical phenomenon of food price increase in the Albanian market during holidays.

Annual headline inflation, during this half of year, is almost completely shaped by the contribution of “unprocessed food” item, meanwhile the contribution of other inflation basket items has provided a low contribution to the construction of headline inflation rate.

The performance of “unprocessed food” item inflation rate has a special importance in explaining and forecasting the short-term volatilities of inflation. The contribution of this item increased progressively during this year until December, peaking to 2.8 percentage points. The inflation of this item showed at a doubled value since June of this year, recording the highest rate in December of 15.1 percent. Components of this item are mainly affected by the prices of fruits and vegetables, which are considerably volatile and of seasonally nature. The inability of the domestic product to meet the demand for these goods, and the fact that the imported part of these products remains under the pressure of the exchange rate behaviour, is translated into higher prices for them. This category has also reflected the considerable growth of these goods’ prices during the last quarter, in the main trading partner countries of Albania.

<table>
<thead>
<tr>
<th>Items</th>
<th>Q3-08</th>
<th>Q4-08</th>
<th>Q1-09</th>
<th>Q2-09</th>
<th>Q3-09</th>
<th>Q4-09</th>
</tr>
</thead>
<tbody>
<tr>
<td>Processed foods (pp)</td>
<td>2.3</td>
<td>1.7</td>
<td>0.9</td>
<td>0.3</td>
<td>-0.1</td>
<td>-0.1</td>
</tr>
<tr>
<td>Bread and cereal (pp)</td>
<td>1.3</td>
<td>1.0</td>
<td>0.6</td>
<td>0.2</td>
<td>-0.1</td>
<td>-0.3</td>
</tr>
<tr>
<td>Alcohol and tobacco (pp)</td>
<td>0.0</td>
<td>0.1</td>
<td>0.1</td>
<td>0.1</td>
<td>0.1</td>
<td>0.2</td>
</tr>
<tr>
<td>Unprocessed foods (pp)</td>
<td>-0.9</td>
<td>-0.1</td>
<td>0.1</td>
<td>1.8</td>
<td>2.3</td>
<td>2.5</td>
</tr>
<tr>
<td>fruits* (pp)</td>
<td>-0.1</td>
<td>-0.1</td>
<td>0.0</td>
<td>0.3</td>
<td>0.5</td>
<td>0.6</td>
</tr>
<tr>
<td>vegetables* (pp)</td>
<td>-1.3</td>
<td>-0.7</td>
<td>-0.3</td>
<td>1.4</td>
<td>0.9</td>
<td>1.0</td>
</tr>
<tr>
<td>Services (pp)</td>
<td>0.5</td>
<td>0.5</td>
<td>0.4</td>
<td>0.3</td>
<td>0.1</td>
<td>0.1</td>
</tr>
<tr>
<td>Administered prices (pp)</td>
<td>0.8</td>
<td>0.3</td>
<td>0.1</td>
<td>-0.4</td>
<td>-0.4</td>
<td>0.1</td>
</tr>
<tr>
<td>Fuels and energy (pp)</td>
<td>0.6</td>
<td>0.7</td>
<td>0.4</td>
<td>0.0</td>
<td>0.0</td>
<td>-0.1</td>
</tr>
<tr>
<td>Housing (pp)</td>
<td>0.0</td>
<td>0.0</td>
<td>0.1</td>
<td>0.2</td>
<td>0.2</td>
<td>0.2</td>
</tr>
<tr>
<td>Non-food consumer goods</td>
<td>0.3</td>
<td>0.2</td>
<td>-0.2</td>
<td>-0.2</td>
<td>-0.2</td>
<td>-0.1</td>
</tr>
<tr>
<td>Durable consumer goods</td>
<td>0.0</td>
<td>0.0</td>
<td>0.0</td>
<td>0.1</td>
<td>0.1</td>
<td>0.2</td>
</tr>
<tr>
<td>Consumer Price Index (year/year, %)</td>
<td>3.0</td>
<td>2.5</td>
<td>1.9</td>
<td>2.1</td>
<td>2.1</td>
<td>2.9</td>
</tr>
</tbody>
</table>

Source: INSTAT and Bank of Albania estimates
The “unprocessed food” item recorded a drop of prices during year 2009, thus manifesting a completely different performance relative to the previous year. Annual inflation of this item during 2008 pointed to 2.3 percent, whereas at the end of 2009 recorded the value of 0.3 percent. In the meantime, the imported share of these products has maintained a stable period owing to the considerable fall of their prices at world market since one year ago. The descending trend of inflation appears to have set out a downward “shifting” of prices as a result of cancelling out the effect of bread price increase in February and March 2008.

“Administered prices” items recorded important developments in the performance of prices during this half of year. Annual inflation rate of this item was negative (averagely -2.2 percent) until September, owing to the statistical effect of the comparison at a higher base, as a result of energy price increase during 2008 and the drop of mobile tariffs during 2009. The annual inflation of this item marked a slight increase of 0.5 percent during this quarter, providing a positive contribution by 0.1 percent, against the negative contribution (averagely -0.4 percent) this category provided on the headline inflation rate. The inflation of this group is expected to fall considerably starting from January 2010 with the new increase of energy price.

Contribution of “Services”, “Housing” and “Durables” items to annual inflation rate, is fluctuated within the band 0.1 – 0.2 percentage points during the last months. Within these items, it is worthy to mention that the payments of taxes for education, mainly of private universities, have recorded a growth of 4.7 percent in November.

Prices of non-food consumables continued to have a negative impact on the headline inflation (-0.1 percentage point). However, the observed fall of “Transfers against personal assets” sub-item, including oil price since November of previous year, is almost cancelled out in the last quarter of year,
in addition for the first time in December, fuels prices have been increased by 4.4 percent at annual rate. During December 2008- September 2009, this item prices cut averagely by 11 percent. This factor, assuming that the growth paces shall pursue to be alike those of December, is thought to steam new inflationary pressures, particularly on the daily consumer goods prices.

III.3 MAIN INFLATION TRENDS

The annual core inflation during the second half of 2009 fluctuated averagely around 1 percent, by observing the declining trend of its first half of year. Its values during the months of last quarter of this year, recording 0.9, 1.0 and 1.2 percent, respectively, highlighted the convergence towards the long-term average of inflation permanent component.

Non-core inflation component, as representative of short-term volatilities in consumer price, resulted with a relatively high increasing contribution to the annual headline inflation, during June-December 2009. The relevant average contribution for the referring period pointed to about 1.7 percentage points, while in December 2009, it pointed to 2.7 percentage points. The notable rise of annual and monthly prices of unprocessed food item, mainly in November and December, are the main “responsible” factors of the high rates relevant to both non-core and headline inflation. Notwithstanding the developments of the last months of year, its second half resulted with a lower annual core inflation rate relative to the same period of previous year (1.6 percentage points lower).

The average annual inflation rates of non-tradable goods and services of CPI basket, were 3.5 and 1.1 percent, respectively, in the second half of year 2009. The price upsurge in tradable goods sector was more evident in the last quarter of the referring year. The inflation of this sector pointed to the maximum rate of 5 percent in December 2009, contributing by about 3 percentage points to the annual headline inflation.

Net tradable inflation in average annual terms for the second half of 2009, resulted about 0.6 percent or 2.9 percentage points lower than the tradable inflation in the respective period. The high seasonality of unprocessed products and the added effects of prices behaviour at the end of year, were considerably amplified in the presence of the relatively depreciating long...
behaviour of the exchange rate during the end of year. Estimates reveal that the relatively deep depreciating effect of ALL/EUR\textsuperscript{16} is transmitted considerably on the inflation rate of tradable goods sector, as the most exposed sector to the risk of the exchange rate volatility.

Developments in the annual inflation of non-tradable goods and services of CPI basket, helped to cancel out the rates of headline inflation close to 2.5 percent in the second half of 2009. Both, this sector’s inflation and the net non-tradable one\textsuperscript{17}, continue to stay at historical low rates until the last month of the referring year.

The analysed trends in consumer prices suggest that inflationary pressures from the side of domestic demand have been moderate, helping to smooth down the pro-inflationary effects caused by the depreciating exchange rate, during January – December 2009.

IV. MACROECONOMIC DEVELOPMENTS AND THEIR EFFECTS ON INFLATION

Developments in indirect indicators of aggregate demand in the Albanian economy show its contraction during the third quarter of 2009 and the period to follow. The indicators regarding consumption, private investments and exports continue to record lower rates than in the previous year. The expansionary fiscal policy pursued during June- November 2009 on the short-term expenses and public investment direction is assessed to have provided the main incentive to aggregate demand in economy. The contracted demand affected the slowdown of the economic activity growth paces at home, during the second half of 2009 relative to the previous year.
IV.1 GROSS DOMESTIC PRODUCT AND PERFORMANCE OF AGGREGATE DEMAND

Albanian economy recorded a positive economic growth during the first 9-month period of the year, notwithstanding at increasing paces which have been slowing down. Thus, GDP recorded an annual growth rate of 4.9\(^{\text{18}}\) percent, or about 2.3 percentage points lower than the average annual rate of previous year. Based on preliminary data of INSTAT\(^{19}\), the gross domestic product in the third quarter climbed by about 4.1 percent in annual terms, while the paces recorded in the two first quarters of year were 5.4 and 5.3 percent, respectively. This indicator’s dynamic, based on the quarterly paces of its growth, during January-September 2009, is in line with the annual trend. The performance of turnover figure for the economy as a total displays the same trend with GDP performance in the first three quarters of year, thus confirming the slowing down of growth rates.

Chart 12 Contribution of sectors to GDP annual growth (in p.p)

Source: INSTAT (GDP, second and third quarter 2009) and Bank of Albania estimates

Box 1. What do confidence indicators reveal regarding the economic development at home during 2009?

Confidence indicators constructed from Bank of Albania at the end of elaborating process of business and consumer confidence survey, summarise at a sole indicator the opinions regarding different aspects for each sector and the confidence of business and consumers on the economy in general\(^{20}\). Employment of confidence indicators in periodic analysis regarding the economic developments are based on assumptions that, the stated judgements and opinions of businesses and consumers shall be reflected on concrete operations, with economic consequences on their activity and thus on the country economy. The connection of confidence indicators to official quantitative real economy indicators depends on this level of opinions’ reflection into concrete operations.

Economic Sentiment Indicator (ESI), which summarises the developments in industry, services and consumer sectors, has clearly affected the slowdown of quarterly GDP climbing paces during 2009 (chart 1). Businesses and consumer confidence indicators recorded a deep fall in the third quarter of this year, affected by the slowness of the demand and the negative expectations in face a world economic crisis. Economic Sentiment Indicator drooped by 28 percentage points in this quarter, remaining below its historical average by 27 percentage points. Notwithstanding, businesses and consumers’ confidence resulted at a higher rate in the two forthcoming quarters relative to the first quarter of year, confidence indicators for all sectors of the economy remain below the long-term average rates. Production balances being aggregated for the production sectors and the balance of the perceived demand aggregated for the economy have recorded negative rates in the first three quarters of 2009 (Chart 2).

In line with the production fall and the slowdown of the demand, the utilisation of current business capacities, as an indicator of the economy situation, has declined considerably during 2009. At economy level, business have utilized averagely 69
percent of their capacities during the 9-month period of this year, 10 percentage points lower than in 2008 (chart 3). The lowest capacities utilisation rate during the 9-month period of 2009 is recorded for industry sector, accounting for 65 percent at average terms. As a result of the low producing capacities utilisation, the slowdown of consumer demand and the credit tightening, private investments are contracted during 2009. Investments balance, according to businesses estimations, was negative and has been dropping during 2009. This is expressed also on the annual fall by 13% of capital goods’ import during January–October 2009.

Financial position of businesses at economic level, observed the declining trend during the first three quarters of 2009, owing to the shrink of the external and domestic demand, being reflected also on the fall of the growth pace of the tax income (chart 4).

The performance of consumer confidence indicator during 2009 has reflected, on one side, their estimation on the overall economic and financial situation, and on the other side, the positive developments in the savings situation. The latter balance increased by 4.5 percentage points in the third quarter of 2009.
Private consumption, based on its measuring indirect indicators, recorded a modest increase during 2009. The moderate employment growth, the slowdown of wages rise rates in the private sector, the decrease of remittances and consumer loan, and the upsurge of uncertainty, throughout the year 2009, have affected the consumer stabilisation over the course of year. According to indirect qualitative data, retail trade indices and consumer goods import have been relatively stable during 2009. In particular, retail trade index, recorded a negative annual growth in the first quarter of year, a slight annual increase in the second quarter and fell by 2.3 percent in the third quarter. Based on the surveys’ qualitative data, the consumer confidence sentiment, after a slight improvement in the second quarter, declined in the third quarter of 2009. Expectations on business and consumer surveys suggest that the growth paces of private consumption shall remain at modest rates even during the forth quarter of 2009.

Indirect indicators reveal a contraction of private investments during 2009, imposed by the demand slowdown, the low rate of business confidence, the low rate of capacities utilisation and by the tightened lending standards. Capital goods import, as an approach of investments in economy, has been reduced annually by 12.8 percent during January-November 2009. The survey data about business confidence, regarding investments whose balance remained negative and decreased during the first three quarters, confirm this fall. Public investments, on the other hand, climbed by 23 percent during January – November 2009, relative to the same period of previous year. Qualitative indicators from business surveys for the second consecutive quarter show a decline of inventories in the third quarter of 2009, after a series of consecutive quarters when businesses have reported their accumulation.

Government expenditures provided a positive contribution to the aggregate demand during 2009, compared to its other components. Public expenditures recorded an annual growth of 16 percent during the 11-month period of 2009. This upsurge is reflected on the increase of budget deficit and is financed through the external borrowing and the use of proceeds from privatisation.

Net exports continued to provide a negative contribution to GDP during the first three quarters of 2009, given that imports rate exceeds considerably the exports rate. However, net exports contribution of goods and services, during this period, in the current economic rate has maintained the same share of the previous year.
IV.1.1 Production performance by sectors

During the fourth quarter of 2009, at sectoral rate\(^{23}\), activities of services provided the highest contribution to GDP annual growth, mainly affected by the high rates of annual increase in the branches of post & telecommunication (about 34.3 percent), transport (about 15.5 percent) and trade, hotels and restaurants, (about 6.4 percent). Activities included in other services rose by about 2.3 percent in annual terms or averagely 7 times lower relative to the first and second quarter of year.

Industrial production activity pursued the contraction in the third quarter of year, notwithstanding at a lower annual rate than in the second quarter, by recording an annual fall of 4.5 percent. Construction shrank also at 0.7 percent in annual terms, differently from the increase recorded in the first half of year.

PRODUCTION SECTORS IN ECONOMY

Based on the turnover index as a volume, the industry branch recorded an annual modest rise in the third quarter by about 0.2 percent, recording the lowest annual rate since 2004. The non-household consumption indicator of electric energy reflects also this development in the industrial activity. The extracting industry, after the contraction recorded since the fourth quarter of 2008, increased in this quarter by 1.8 percent annually. During this quarter, at turnover figure terms, another branch showing a deterioration was the processing industry, declining by 5.7 percent, while “Electric energy, gas, water” item recorded a better performance, thus increasing by about 20 percent in annual terms.

The high annual growth paces of construction sector slowed down, by generating a turnover figure as a volume of 24.5 percent higher than the third quarter of previous year, however it recorded a contraction at quarterly terms, of 8.3 percent. Construction volume, during this period has slowed down the annual increase paces, as denoted by the other indirect indices, such as the rise by lower paces of cement consumption.

Box 2. Performance of housing prices\(^{24}\)

Housing price index in Tirana recorded higher rates in the second half of 2009 relative to the first half. In the third and fourth quarter of 2009, this index pointed to 17.3 percent and 11.6 percent, respectively. The quarterly changes for these periods pointed to 5.6 and 5.8 percent, respectively. This upsurge has mainly reflected the depreciating performance of ALL during this period.

Production prices at construction sector, based on businesses estimations collected from confidence survey, increased in the third quarter 2009, after a declining trend started in the second quarter of 2008 (chart 2). As regards to these data survey, assessment of constructing businesses regarding ordering contracts is improved and the lowering of inventories continued for the second regular survey during the third quarter of 2009.
Rent price index, differently from house prices index, declined again during the fourth quarter of 2009, by 15.5 percent, compared to the fourth quarter of 2008. House price index is 1.2 percent lower relative to the third quarter of 2009. Price index to rent ratio rose in the fourth quarter remaining by 0.2 percentage points upper its historic average.

Production of electrical energy during January – November 2009 grew by 35.2 percent relative to the same period of previous year. Available data reveal that during November 2009, electrical energy production increased 94.8 percent in annual terms and by about 5.7 percent relative to the previous month.
Energy import and export balance was improved during January – November 2009. Thus, the energy export volume amounted to 438.5 GWh, during this 11-month period. Energy import volume, for the same period, fell by 97.2 percent compared to the same period of previous year (53.1 GWh from 2232.5 GWh in January – November 2008). The level of exported energy for the 11-month period was 385.5 GWh higher than the level of imported energy. Electrical energy consumption in January – November 2009 climbed by 5.65 percent relative to the same period of previous year. This upsurge owes mainly to the rise of electrical energy household consumption. On the other hand, electrical energy consumption by businesses increased insignificantly, by 0.04 percent, respectively.

Table 5 Annual indicators of the electrical energy balance (in GWh)

<table>
<thead>
<tr>
<th></th>
<th>11M '05</th>
<th>11M '06</th>
<th>11M '07</th>
<th>11M '08</th>
<th>11M '09</th>
<th>Annual change 11M '09/ 11M '08 (in %)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Net production</td>
<td>5089.0</td>
<td>5163.9</td>
<td>2591.8</td>
<td>3423.5</td>
<td>4628.8</td>
<td>35.21</td>
</tr>
<tr>
<td>Import ( - )</td>
<td>149.8</td>
<td>507.4</td>
<td>2517.8</td>
<td>2232.5</td>
<td>53.1</td>
<td>-97.2</td>
</tr>
<tr>
<td>Export ( + )</td>
<td>0.0</td>
<td>0.0</td>
<td>0.0</td>
<td>0.0</td>
<td>438.5</td>
<td>-</td>
</tr>
<tr>
<td>Losses in distribution</td>
<td>1793.0</td>
<td>2028.3</td>
<td>1513.7</td>
<td>1520.4</td>
<td>1881.1</td>
<td>23.73</td>
</tr>
<tr>
<td>Losses/ Production</td>
<td>35.2%</td>
<td>39.3%</td>
<td>58.4%</td>
<td>44.4%</td>
<td>40.6%</td>
<td>-3.8</td>
</tr>
<tr>
<td>Consumed Energy</td>
<td>4075.0</td>
<td>5151.4</td>
<td>4931.8</td>
<td>5422.4</td>
<td>5729.0</td>
<td>5.65</td>
</tr>
<tr>
<td>Billed consumption</td>
<td>3225.6</td>
<td>3123.1</td>
<td>3278.2</td>
<td>3736.1</td>
<td>3847.9</td>
<td>2.99</td>
</tr>
<tr>
<td>Unbilled consumption</td>
<td>849.4</td>
<td>2028.3</td>
<td>1653.5</td>
<td>1686.3</td>
<td>1881.1</td>
<td>11.55</td>
</tr>
<tr>
<td>Household consumption</td>
<td>1943.1</td>
<td>1939.9</td>
<td>1870.1</td>
<td>2072.8</td>
<td>2183.9</td>
<td>5.36</td>
</tr>
<tr>
<td>Non-household consumption</td>
<td>1282.5</td>
<td>1183.2</td>
<td>1408.1</td>
<td>1663.3</td>
<td>1664.0</td>
<td>0.04</td>
</tr>
</tbody>
</table>

Source: KESh, OSSh

SERVICES SECTOR

The volume turnover index derived from services branch has recorded a positive growth pace in annual terms, however this pace was lower relative to the first two quarters of year. According to this index, retail trade activity
rose by about 12.6 percent annually, pointing to 5.2 percentage points less than the average of the two preceding quarters. Post and telecommunication branches have also recorded positive annual rates of these indices and hotels activity as well, notwithstanding at lower paces in this quarter relative to the previous quarters.

IV.1.2 Performance of the External Sector of the Economy

The overall balance of payments denote the increase of foreign assets by about EUR 44 million for the period July-September 2009. The main developments in the external sector of the economy consisted on:

- the decline of inflow and outflow current transactions;
- the further deepening of current deficit and the modest narrowing of trade deficit;
- the contraction of net inflows in the capital and financial account;
- the growth of foreign reserves of the monetary authority.

**CURRENT ACCOUNT**

Current transactions carried out during July-September 2009, amounted to about EUR 2.68 billion, 7.4 percent higher than the transactions of the same period in the previous year\(^7\). The deficit of current account balance amounted to EUR 330.6 million during this period, recording an annual growth of about 43 percent.

Current deficit deepening owed to the direction change of the revenues balance from surplus to deficit\(^9\), and to the narrowing of current transfers\(^9\) surplus. As a result, current deficit ratio to GDP\(^9\) increased considerably in annual terms being estimated to about 17 percent. Trade exchanges in goods
and services represent the major part of current transactions of our country. More than 90 percent of the period current expenses served for the purchase of goods and services, while about 22 percent of current revenues have entered as transfers. Goods and services exports provided respectively about 17 and 57 percent of current incomes. While, goods trade deficit shrunk to EUR 591 million or about 2 percent in annual terms and its ratio against GDP is estimated to 28.4 percent.

Table 6 Balance of payments indicators, in years

<table>
<thead>
<tr>
<th></th>
<th>In EUR million</th>
<th>In percentage to GDP</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Current account</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Q3’06</td>
<td>-106.9</td>
<td>-1.7</td>
</tr>
<tr>
<td>Q3’07</td>
<td>-170.1</td>
<td>-2.2</td>
</tr>
<tr>
<td>Q3’08</td>
<td>-230.7</td>
<td>-3.3</td>
</tr>
<tr>
<td>Q3’09</td>
<td>-330.6</td>
<td>-4.6</td>
</tr>
<tr>
<td>Q3’06</td>
<td>-8.2</td>
<td>-0.1</td>
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<tr>
<td>Q3’07</td>
<td>-8.4</td>
<td>-0.1</td>
</tr>
<tr>
<td>Q3’08</td>
<td>-13.9</td>
<td>-0.2</td>
</tr>
<tr>
<td>Q3’09</td>
<td>-17.3</td>
<td>-0.3</td>
</tr>
<tr>
<td><strong>Trade balance</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Q3’06</td>
<td>-415.3</td>
<td>-4.0</td>
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<tr>
<td>Q3’07</td>
<td>-527.4</td>
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</tr>
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<td>-601.9</td>
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<td>-590.8</td>
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<td>Q3’06</td>
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<tr>
<td>Q3’08</td>
<td>-27.9</td>
<td>-0.4</td>
</tr>
<tr>
<td>Q3’09</td>
<td>-28.4</td>
<td>-0.5</td>
</tr>
<tr>
<td><strong>Exports</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Q3’06</td>
<td>153.2</td>
<td>1.8</td>
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<tr>
<td>Q3’07</td>
<td>197.3</td>
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<td>Q3’08</td>
<td>242.0</td>
<td>2.7</td>
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<td>Q3’09</td>
<td>201.8</td>
<td>2.5</td>
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<td>Q3’06</td>
<td>8.3</td>
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<tr>
<td>Q3’07</td>
<td>9.7</td>
<td>0.1</td>
</tr>
<tr>
<td>Q3’08</td>
<td>10.9</td>
<td>0.1</td>
</tr>
<tr>
<td>Q3’09</td>
<td>9.2</td>
<td>0.1</td>
</tr>
<tr>
<td><strong>Imports</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Q3’06</td>
<td>-568.5</td>
<td>-5.2</td>
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<tr>
<td>Q3’07</td>
<td>-724.7</td>
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<td>Q3’08</td>
<td>-843.9</td>
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<td>Q3’09</td>
<td>-792.6</td>
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<tr>
<td>Q3’06</td>
<td>-31.0</td>
<td>-0.3</td>
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<tr>
<td>Q3’07</td>
<td>-34.9</td>
<td>-0.4</td>
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<tr>
<td>Q3’08</td>
<td>-38.7</td>
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</tr>
<tr>
<td>Q3’09</td>
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<tr>
<td><strong>Services (net)</strong></td>
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</tr>
<tr>
<td>Q3’06</td>
<td>-18.6</td>
<td>-0.2</td>
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<td>Q3’08</td>
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<td>88.1</td>
<td>0.9</td>
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<tr>
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<td>-1.3</td>
<td>-0.0</td>
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<td>Q3’07</td>
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<td>Q3’08</td>
<td>1.0</td>
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<td>Q3’09</td>
<td>0.5</td>
<td>0.0</td>
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<tr>
<td><strong>Income (net)</strong></td>
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<td></td>
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<tr>
<td>Q3’06</td>
<td>50.5</td>
<td>0.4</td>
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<tr>
<td>Q3’07</td>
<td>74.4</td>
<td>0.6</td>
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<tr>
<td>Q3’08</td>
<td>54.8</td>
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<td>Q3’06</td>
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<td>Q3’08</td>
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<td>Q3’09</td>
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<tr>
<td><strong>Current transfers (net)</strong></td>
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<td>Q3’06</td>
<td>276.4</td>
<td>2.8</td>
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<td><strong>Capital &amp; financial account</strong></td>
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<td>Q3’06</td>
<td>298.8</td>
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<td>Q3’08</td>
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<td>11.5</td>
<td>0.1</td>
</tr>
<tr>
<td>Q3’09</td>
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<td>Q3’06</td>
<td>3.6</td>
<td>0.0</td>
</tr>
<tr>
<td>Q3’07</td>
<td>0.2</td>
<td>0.0</td>
</tr>
<tr>
<td>Q3’08</td>
<td>3.3</td>
<td>0.0</td>
</tr>
<tr>
<td>Q3’09</td>
<td>0.8</td>
<td>0.0</td>
</tr>
<tr>
<td><strong>Balance of payments</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Q3’06</td>
<td>76.1</td>
<td>0.7</td>
</tr>
<tr>
<td>Q3’07</td>
<td>135.1</td>
<td>1.0</td>
</tr>
<tr>
<td>Q3’08</td>
<td>118.5</td>
<td>1.0</td>
</tr>
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<td>Q3’09</td>
<td>43.9</td>
<td>0.7</td>
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<td>Q3’08</td>
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</tr>
<tr>
<td>Q3’09</td>
<td>1.7</td>
<td>0.0</td>
</tr>
</tbody>
</table>

Source: Bank of Albania and IMF estimates

FOREIGN TRADE

Data of the foreign trade for the period July-November 2009 denote a weakening of trading inflows and outflows. Trade exchanges for this period amounted to EUR 1.7 billion, about 11 percent lower relative to the same period of previous year. Trade deficit narrowed by about 10 percent in annual terms. Imports’ coverage by exports remain at 24.6 percent and reveals a decline by about 2.4 percentage points.

Table 7 Exports and imports (in EUR millions) and the annual change by commodity groups (in %)

<table>
<thead>
<tr>
<th>Category</th>
<th>Exports (EUR, million July-November)</th>
<th>Annual change (in %, July-November)</th>
<th>Imports (EUR, million July-November)</th>
<th>Annual change (in %, November)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Foods and live animals</td>
<td>16.1</td>
<td>-2.7</td>
<td>170.5</td>
<td>2.1</td>
</tr>
<tr>
<td>Beverages and Tobacco</td>
<td>0.5</td>
<td>-58.1</td>
<td>62.4</td>
<td>20.4</td>
</tr>
<tr>
<td>Raw materials</td>
<td>43.8</td>
<td>-24.0</td>
<td>43.2</td>
<td>31.6</td>
</tr>
<tr>
<td>Fuels</td>
<td>39.1</td>
<td>-5.4</td>
<td>185.2</td>
<td>-28.5</td>
</tr>
<tr>
<td>Vegetable and animal fats and oils</td>
<td>0.2</td>
<td>94.6</td>
<td>1337.1</td>
<td>-19.5</td>
</tr>
<tr>
<td>Chemical products</td>
<td>6.3</td>
<td>37.7</td>
<td>148.5</td>
<td>-4.7</td>
</tr>
<tr>
<td>Processed goods</td>
<td>61.0</td>
<td>-33.3</td>
<td>353.9</td>
<td>-7.2</td>
</tr>
<tr>
<td>Machinery and appliances</td>
<td>18.1</td>
<td>8.7</td>
<td>287.5</td>
<td>-15.7</td>
</tr>
<tr>
<td>Other processed goods</td>
<td>157.1</td>
<td>-5.2</td>
<td>121.3</td>
<td>-18.9</td>
</tr>
<tr>
<td>Miscellaneous</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td>342.2</td>
<td>-13.1</td>
<td>1,389.1</td>
<td>-10.9</td>
</tr>
</tbody>
</table>

Source: Bank of Albania

Given that a considerable high percentage of domestic exports have as final destination the EU countries- mainly Greece and Italy, the weakening
of external demand in these countries has affected considerably the exports performance. Notwithstanding, the depreciation of the domestic currency against EUR has softened the demand decline in these countries. The fall of prices in the respective markets has exercised pressures on the reverse direction for exporters at home. Therefore, exports dropped by 13.1 percent during July-November ‘09 relative to the same period of previous year. Exports categories “raw materials” and “processed goods” provided the main impact by recording a decline of 24 and 33 percent, respectively in annual terms. While, the group of highest share in exports, “Other processed goods”, recorded an annual fall of about 5 percent. The combined share of these three categories against total exports for this period is about 77 percent.

Imports to our country, during July-November, reduced by approximately 11 percent in annual terms. The “machinery and appliances” and “processed goods” sub-items provided the main contribution to this drop, being reduced by 16 and 7 percent, respectively in annual terms. “Fuels” item also recorded an annual decline of imports, affected also by the high rate of prices this sector encountered in the previous year. By contrast, imports of “Foods and live animals” rose by about 2 percent in annual terms.

The performance of exports measured by volume (ton), attests a more moderate annual downward compared to the decline in the value. Thus, imports volume reduced by approximately 1.5 percent. Albania exports’ volume to other countries recorded a fall of 9.3 percent in annual terms, during July-November’09. The analysis of imports performance in terms of their final destination, “capital goods”, “intermediate goods” and “consumer
goods”, show an upward trend of the last item and a downward trend of the two first items.

Thus, in terms of the above mentioned period, imports of “capital goods” and “intermediate goods” reduced by 20 and 14 percent, respectively in annual terms. By contrast, imports of “consumer goods” recorded an increase of approximately 1.6 percent in annual terms.

The EU countries continue to remain Albania’s main trading partners. Hence, trade exchanges with these countries account for about 68 percent of total trade activity of our country. In terms of exports, Italy continues to be their main destination accounting for averagely 61 percent of total exports, during the period July-November. By contrast, geographical span of imports origin to our country is diversified. Here it is highlighted the decline of imports from China and regional countries and the increase of imports from EU countries.

### Box 3. Remittances, a developing possibility

The economic crisis’ effects and lessons, which involved the world markets during 2008-2009 should be considered in the compilation of economic policies and strategies which relate the migration to the stable economic development of a country. The expected performance of remittances and their ability to support the reduction targets of poverty and the country economic development is an important dimension of remittances. In Albania, remittances – which are estimated to about 9-10 percent of GDP, represent a quite important inflow to both households and to the entire economy. Along with the foreign direct investments and revenues from goods and services export, they compose one of the main items for the financing of imports and the meeting of economy needs for consumption and investments. The ratio rates of remittances to GDP have been higher than those of foreign direct investments, acting as an incentive to the economic and financial development of the country.

Remittances’ effects on the economy are complex. In case of Albania, these flows compose a revenues source to meet the consumer needs of living conditions, and a potential possibility to finance investments and the creation of new work positions. On the other hand, the benefiting of remittances from emigrants families may potentially establish pressures on labour market, through the establishment of dependences and encouragement of long-term unemployment. These factors should be taken into account in dealing with remittances, in their current and expected context as well.
Remittances during the first 9-month period of 2009 to Albania decreased by about 6 percent against the same period of the previous year and by about 19 percent relative to the same period of 2007, by fluctuating the supply demand ratio for foreign currency and thus affecting the performance of exchange rate. The slowing down of remittances during 2009, notwithstanding was mainly a direct reflect of global crisis effects, may be considered as a primary signal of their effects in the future. The progressive reduction of their relative value and share is mainly related to the seasonal character of remittances, which as widely accepted from by different studies (Docquier, Rapoport 2005), have a long-term downward trend. Emigrants, by the time, are stabilised in the hosting country, establish their families and consequently come across with different pressures to lower the remittances level to the country of origin. The same tendency is expected to occur also for Albania, and for that reason, the attempt to find out alternative sources, which generate foreign-exchange denominated inflows, and their channelling in producing economic sectors and investments as well.

Annalists at World Bank, International Monetary Fund and World Bank for Migration have accomplished the same results: remittances currently are designated for the financing of daily consumption, for they represent a restricted capital source for investments and for the financing of the stable economic development of the countries of origin. Nowadays, when countries have a long migration history, the attention, higher than on remittances flows, should be concentrated on the development of financial instruments adequate for the attraction of immigrants’ savings. Immigrants’ savings are assessed to be 4.2 times higher than the remittances rate in case of Albania.

<table>
<thead>
<tr>
<th>Monthly income (familiar) – (Euro)</th>
<th>Albania</th>
<th>Kosovo</th>
<th>BiH</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>2300</td>
<td>3900</td>
<td>2288</td>
</tr>
<tr>
<td>Monthly expenses - (Euro)</td>
<td>1477</td>
<td>2324</td>
<td>1938</td>
</tr>
<tr>
<td>Value of monthly savings (Euro)</td>
<td>835</td>
<td>1578</td>
<td>350</td>
</tr>
<tr>
<td>Rate of monthly savings (in %)</td>
<td>38</td>
<td>41</td>
<td>15</td>
</tr>
<tr>
<td>Annual value of remittances per family - (Euro)</td>
<td>1664</td>
<td>3212</td>
<td>1752</td>
</tr>
<tr>
<td>Annual savings – Euro</td>
<td>10260</td>
<td>15724</td>
<td>2448</td>
</tr>
<tr>
<td>Savings in 2008 - (Euro million)</td>
<td>3473</td>
<td>2340</td>
<td>1175</td>
</tr>
<tr>
<td>Remittances in 2008 (Euro million)</td>
<td>833</td>
<td>479</td>
<td>841</td>
</tr>
<tr>
<td>Savings/Remittances</td>
<td>4.2</td>
<td>4.8</td>
<td>1.4</td>
</tr>
<tr>
<td>No, of migrant families</td>
<td>404.000</td>
<td>149.000</td>
<td>480.000</td>
</tr>
</tbody>
</table>

Source: IOM, IASCI and Bank of Albania

On the other hand, immigrants represent also an important channel for the transmission of new knowledge, new ways of production, work ethic, new technologies and a new culture of doing business. The intertwining of both components, savings and new knowledge, shall represent a highly considerable potential source for the development of the countries of origin in general.

**PERFORMANCE OF OTHER CURRENT ACCOUNT ITEMS**

Transactions rate in services amounted to ALL 1.25 billion or 31.4 percent higher in annual terms, for July-September 2009. The balance sheet of services account recorded a suffice of EUR 88.1 million, for the third quarter of 2009, remaining almost at the same level compared to the same period of previous year (EUR 87.2 million). In the meantime, the annual growth of
exports and imports in services pointed to 28.8 and 34.5 percent, respectively. Travel services covered the main share of both services export and import, contributing by 81.5 and 78.2 percent, respectively on the overall share of services. Net balance of travel services, during this quarter, recorded a surplus of about EUR 91 million compared to the surplus of about EUR 94 million amounted in the previous year. Foreign exchange inflows from travel services amounted to EUR 543.4 million during this period, recording an annual growth of about 40 percent, related also to the increase of visitors’ number during summer season. Exchange inflows from travel services were about 2.7 times higher than goods exports’ revenues. Residents’ consumption outside Albania is estimated at about EUR 453 million, 54.2 percent higher compared to the same period of July – September 2008.

Transport services recorded a surplus of EUR 0.2 million, after a period of subsequent negative rates quarters. “Other services” category closed with a surplus of about EUR 12 million, being narrowed in the time span of one year. The positive signals within this category are noted for both construction and government services, while services in communication and financial sector record negative developments.

Net result of transactions in revenues is negative during this quarter and estimated to about EUR 34 million against the positive value of EUR 55 million of the same period in the previous year. Foreign currency denominated inflows of this category fell by about 49 percent, while outflows are almost doubled, relative to the third quarter of previous year. The work of seasonal and border workers and investments’ proceeds, in the form of banking system deposits interests abroad, were the two main sources of revenues. Work inflows decreased by 35 percent. While, outflows from direct investments as dividend payments and re-invested profit are doubled. During the third quarter of 2009, Albania paid the amount of EUR 5 million to settle interest on its external debt.

Net current transfers balance, during July-September 2009, recorded a surplus of about EUR 206 million with a drop of EUR 24 million relative to the previous year. Remittances continue to maintain the highest share (around 90 percent) of this category incomes. These transactions amounted to EUR 187.5 million, during this period, covering about 32 percent of goods trade deficit. Relative to the same period of 2008, these transfers are assessed 6.6 percent lower. Their ratio to GDP is assessed to 9.4 percent relative to 10.2 percent in the previous year.

CAPITAL AND FINANCIAL ACCOUNT

Albania recorded a net inflow of EUR 187.1 million in the capital and financial account during the third quarter of 2009. Around EUR 32 million entered in the form of capital investment transfers, while EUR 155 in the form of net financial flows. Capital inflows financed 57 percent of the current account deficit. Albania’s financial liabilities to the rest of the world grew by EUR 285 million, during the above stated period, while residents’ assets
abroad raised considerably (about 19 percent). The highest shifts in this account are recorded in borrowing items. The granting of long-term and soft loans from abroad amounted to EUR 162 million. Public sector borrowing amounted to about EUR 140 million, while private borrowing amounted to EUR 22 million. The increase of this type of liabilities led to higher future external debt-service payments. External-debt service for the third quarter of 2009 reduced residents’ liabilities by EUR 20 million. While, the Foreign Direct Investments inflow, in the Albanian economy, for the third quarter 2009, amounted to about EUR 143 million against EUR 178 million recorded in the previous year. It is worthy to mention, that for the first time, after some consecutive quarters, it is recorded an increase of residents’ claims against non-residents. Foreign exchange assets invested abroad recorded a growth of EUR 130 million, mainly in the form of portfolio investments (EUR 15.8 million) and banking system reserves investments in the international market as deposits (EUR 104.3 million). Long-term lending increased as well (EUR 10.5 million).

Reserve assets rose by EUR 44 million. Foreign reserves amounted to EUR 1,736 million in third quarter-end of 2009. This level is considered sufficient to cover 4.2 months of imports of goods and services.

IV.1.3 Developments in fiscal indicators and fiscal policy

Fiscal policy manifested an expansionist character during 2009, particularly in the second quarter of year. Primary deficit experienced sharp expansionary paces during this year, by reflecting the uprise of current and capital expenditure.

Primary deficit has reflected on its major part the growth of budget deficit. At the end of November, budget deficit amounted to about ALL 64.5 billion, exceeding by about 6 percent the projected level for this period. Deficit financing relied primarily on proceeds from privatisation, syndicated loan and the borrowing through the issuance of debt instruments in the Government securities market.

<table>
<thead>
<tr>
<th>Revenue</th>
<th>To the plan35 (in %)</th>
<th>Annual change (in %)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Revenue</td>
<td>11-month 2009 11-month 2009 11-month 2007 11-month 2008 11-month 2009</td>
<td>268.2 92.3 11.8 15.9 2.2</td>
</tr>
<tr>
<td>Tax and customs</td>
<td>192.0 95.8 13.9 16.7 2.7</td>
<td></td>
</tr>
<tr>
<td>VAT</td>
<td>99.9 96.0 19.3 21.9 2.3</td>
<td></td>
</tr>
<tr>
<td>Tax on profit</td>
<td>15.8 100.1 -7.9 -11.4 -5.7</td>
<td></td>
</tr>
</tbody>
</table>

Table 9 Accomplishment of main fiscal indicators for the 11-month period of 2009 relative to the previous years
Excises | 30.5 | 91.3 | 24.8 | 14.8 | 1.8
- Local government | 11.1 | 72.8 | -12.8 | 19.8 | 7.4
- Independent budget | 45.5 | 94.4 | -4.2 | 16.8 | 5.5
- Non-tax income | 17.1 | 78.1 | -53.4 | 5.9 | -16.5
- Grants | 2.5 | 51.8 | -68.8 | 24.6 | 68.8
Expenditure | 332.6 | 94.7 | 9.8 | 28.6 | 16.4
- Current expenditure | 247.7 | 97.1 | 8.1 | 15.4 | 16.4
Personnel | 55.9 | 102.7 | 4.2 | 14.0 | -3.6
Interests | 32.3 | 98.9 | -1.2 | 24.5 | 13.1
Social insurance and pensions | 86.8 | 99.8 | 17.0 | 9.8 | 27.4
Local government expenditure | 29.3 | 90.4 | -2.1 | 34.1 | 31.1
- Capital expenditure | 84.9 | 90.5 | 3.4 | 110.7 | 22.8
Budget balance | -64.5 | 106.1 | 2,031.8 | -664.9 | 175.2

Source: Ministry of Finance

BUDGET REVENUE

Budget revenue manifested a slowing trend, particularly after the first quarter of 2009. This tendency is reflected almost on all main items of tax revenues. In more concrete terms, annual increase of revenues for the 11-month period pointed to about 2 percent, against 14 percent recorded at the end of the third quarter of 2009. This behaviour of revenues is mainly posted by VAT revenue, whose annual increase pace fluctuated within the interval 2-5 percent. The same interval constructed for 2008, has as lower and upper limits the values of 21 and 25 percent, respectively.

Budget revenue during the first half of year, along with the slowdown trend, have manifested differences to the projected level. Their performance during first half of year imposed as indispensable the review of budget for the year 2009. As revealed from the reviewed budget of 2009, revenue dropped by ALL 8.7 billion, while expenditure rose by ALL 16.1 billion, relative to the rates being projected at the beginning of year. Consequently, budget deficit grew by ALL 24.8 billion from the initial projected rate.

At the end of 11-month period, total revenue were realised by about 92.3 percent of the projection for the same period. Almost all revenue items have manifested differences to the projection, excluding revenues from profit tax, customs and national tax.

BUDGET EXPENDITURE

Fiscal policy has manifested signs of fiscal expansion, being led at the same time by short-and long-term expenditures, throughout the 11-month period. The realised budget expenditure, in annual terms, during the 11-month period, recorded a growth by about 16 percent, where capital expenses contribution is about 4 percentage points. Contribution of capital expenditure to the total...
of expenditure growth has been highlighted in the two last years, mainly owing to the expenditures for the construction of Durrës-Kukës way.

There are realised a total of 332.6 billion expenditures, until the end of November, which represent about 95 percent of the projection compiled for this period. Short-term expenditure cover about 74 percent of total expenditure. After the first quarter of year, almost all components of this item have been increased considerably, where there are highlighted local government expenditure and operative expenditure of maintenance.

**BUDGET DEFICIT AND ITS FINANCING**

Budget deficit has pursued an uprising trajectory starting from February of this year due to a more active fiscal policy on the expenditure side. The performance of budget revenue and expenditure, in terms of growth rates and meeting of projection provided the expansion of budget deficit, which at the end of November is estimated around 6.2 percent of GDP.

Budget deficit at the end of November 2009, is 2 times higher than the rate recorded in the same period of the previous year. At the same time, the face value recorded for the 11-month period amounted to ALL 65 billion, represents the higher rate recorded during the last 10-year period. Budget deficit experienced considerable growing paces during the last two years, by being deviated somewhat from the trajectory of fiscal consolidation followed during 2005-2007.

A higher rate of budget deficit is accompanied by higher needs for (external and domestic) borrowing, relative to the previous years. As a result, along with the widely employed instruments in the financing of budget deficit, the syndicated loan has been used throughout the previous years, in 2009. This new instrument (amounting to ALL 24.6 billion) has financed about 38 percent of the 11-month budget deficit. About 75 percent of syndicated loan was provided by non-resident banks and the rest by resident banks and institutions operating in Albania.
Privatisation receipts provided considerable contribution to the financing of budget deficit for the 11-month period (by about 43 percent)\(^47\). Government borrowing policy until the end of September was considerably oriented towards long-term instruments of debt. 5-year bonds covered a considerable part of total debt being issued during 2009. The focus of the Ministry of Finance shifted towards shorter-term instruments of debt in the third quarter, mainly towards 12-month T-bills. The borrowing shift was mainly based on the main actors’ preferences in securities market of government, who have showed a trend to shorten the lending span, relative to the previous years\(^48\). Consequently, until the end of this year, the percentage of long-term debt to total debt is expected to reduce at moderated terms relative to 2008. Total of public debt until the end of third quarter of 2009, is estimated to about 58.3 percent of GDP against 56 percent of GDP at the end of 2008.

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Revenues</td>
<td>202.5</td>
<td>226.4</td>
<td>262.4</td>
<td>268.2</td>
</tr>
<tr>
<td>Expenditures</td>
<td>202.3</td>
<td>222.3</td>
<td>285.9</td>
<td>332.6</td>
</tr>
<tr>
<td>Budget balance</td>
<td>0.2</td>
<td>4.1</td>
<td>-23.4</td>
<td>-64.5</td>
</tr>
<tr>
<td>Financing</td>
<td>-0.2</td>
<td>-4.1</td>
<td>23.4</td>
<td>64.4</td>
</tr>
<tr>
<td>Domestic financing</td>
<td>-5.8</td>
<td>-6.8</td>
<td>-9.7</td>
<td>37.5</td>
</tr>
<tr>
<td>Domestic borrowing</td>
<td>4.6</td>
<td>11.8</td>
<td>2.7</td>
<td>14.3</td>
</tr>
<tr>
<td>Treasury bills</td>
<td>-29.7</td>
<td>-20.9</td>
<td>-13.2</td>
<td>8.9</td>
</tr>
<tr>
<td>Bonds</td>
<td>34.3</td>
<td>38.4</td>
<td>15.9</td>
<td>8.4</td>
</tr>
<tr>
<td>Eurobond</td>
<td>0.0</td>
<td>-5.8</td>
<td>0.0</td>
<td>0.0</td>
</tr>
<tr>
<td>Direct Loans</td>
<td>0.0</td>
<td>0.0</td>
<td>0.0</td>
<td>-3.0</td>
</tr>
<tr>
<td>Privatisation receipts</td>
<td>2.1</td>
<td>13.2</td>
<td>1.0</td>
<td>27.6</td>
</tr>
<tr>
<td>Others</td>
<td>-12.5</td>
<td>-31.8</td>
<td>-13.3</td>
<td>-10.6</td>
</tr>
<tr>
<td>Syndicated loan</td>
<td>0.0</td>
<td>0.0</td>
<td>0.0</td>
<td>24.6</td>
</tr>
<tr>
<td>Foreign financing</td>
<td>5.6</td>
<td>2.6</td>
<td>33.1</td>
<td>26.9</td>
</tr>
<tr>
<td>Projections with foreign sources</td>
<td>5.6</td>
<td>2.6</td>
<td>33.1</td>
<td>8.5</td>
</tr>
</tbody>
</table>

Source: Ministry of Finance and Bank of Albania

Box 4. World crisis and its financial costs to Eastern European countries

The economic and financial global crisis extended its effects also on Eastern European countries. Notwithstanding at different dimensions, the crisis impact on these countries was shown on the reduction of economic activity, the increase of unemployment rate, financial sectors problems as well as in the deterioration of both fiscal positions and the balance of payments.

The encountering of crisis imposed the commitment of a range of measures mainly focused on the recovery of financial system and the encouragement of aggregate demand. The reaction of fiscal policy against the crisis consists on the fiscal simulation of economy to encourage aggregate demand and to provide explicit guarantees to the financial stability. The free movement of automatic stabilisers and the different discretionary programs of fiscal stimuli were accompanied by the considerable growth of budget deficit and of the public debt.\(^49\) Countercyclical fiscal policies increased the borrowing needs, making many countries apply for the assistance of international institutions, as IMF and EU, to cut their cost.
Chart 1 illustrates the fact that countries which were affected mostly by the economic crisis, reacted more considerably through the transmission fiscal stimuli. The experience acquired during this period identifies two important lessons.

Firstly, countries enjoying a good macroeconomic and financial stability prior to the crisis encountered the latter with lower consequences. Chart 2 illustrates the fact that the countries with macroeconomic misbalances, approximated by high deficits of current account, were affected to a greater extent from the world crisis.

Secondly, countries with better fiscal position, expressed at low rates of public debts and budget deficit, had possibilities to provide a stronger reaction. The anti-crisis measures have been directly related to the available fiscal spaces of each country; those countries with more controlled rates of public debt, have had possibilities to implement broader projections of fiscal stimuli, as denoted in chart 3.

In light of these lessons, these countries made more considerably highlighted attempts for fiscal consolidation and the strengthening of macroeconomic stability. The meeting of these targets cuts the risk primes and promotes the attraction of foreign investments, softens the macroeconomic shock risks and increases the possibility against contingencies. Regarding the Western Balkan countries, Albania owns a relatively comparative rate of the public debt. As a ratio to GDP, this indicator pointed to about 56 percent in 2008, thus increasing to about 58.3 percent in the third quarter of 2009. In this view, the recent initiatives for the decrease of budget deficit and the control of public debt rate in Albania sustain the stable and long-term growth of the country.
IV.1.4 Monetary developments

Monetary developments were characterised by a further slowdown of monetary supply until September 2009. In the meantime, in October it is noted a considerable increase of M3 growth paces, mainly as a consequence of the cancellation of the deposits withdrawal effect. However, the slowdown of monetary expansion mostly expresses the interruption of the sharp growth of the credit portfolio. Notwithstanding the liquidity improvement of banking system, economy lending is restricted by the deterioration of portfolio quality, the uncertainties in terms of the future of the economic activity at home and by the decrease of the demand. Money creation in economy is mainly realised through the component of ALL-denominated-monetary stock. While, the improved situation of deposits and lack of lending in foreign currency led to the improvement of foreign exchange –denominated component of money demand, by increasing its positive contribution to monetary expansion in economy.

**PERFORMANCE OF MONETARY AGGREGATES**

Performance of monetary indicators, excluding the exchange rate effects, has reaffirmed the slowdown trend of the lending activity. M3 broad aggregate recorded a growth of about 2 percent in average annual terms in the second part of year, relative to 4 percent in the second half of year. The neutralisation of statistical effect of deposits outflow from the banking system is reflected on the higher paces of monetary supply of averagely 3.7 percent in November-October against 1 percent in the third quarter of year.

In the meantime, ALL denominated money indicators, M2 and reserve money, have persisted to manifest slowdown signs in annual terms. Annual average rate of M2 aggregate pointed to about 8 percent in the end of half of year relative to the rate of 10 percent in the first half of year. Monetary base
pursued also the downward trend, climbing to only 11 percent in November relative to the annual average pace of 25 percent in the first half of year. Performance of these indicators has mainly reflected currency reduction outside banks during this period and the slowdown of ALL denominated lending. The uprising participation of households in financing budget deficit has imposed the use of currency outside banks to meet the demand of fiscal agent for financing. High demand for T-bills instruments from households, which in statistical terms is excluded from the calculation of ALL M2 aggregate, has affected the reduction of M2 growth paces for the second part.

The slowed paces of foreign lending have created spaces for foreign exchange reserve accumulation of banking system. This latter is more emphasised in the last quarter of year. Net foreign assets of commercial banks, during October-November, resulted 3.5 percent against broad money, relative to about 0.1 percent this ratio composed in the first half of year. While, to meet banking system need for liquidity in ALL, Bank of Albania, through reverse Repo agreements have increased the amount of liquidity being injected into the market. In the second part of year, the injected liquidity from Bank of Albania composed about 6 percent of M2 aggregate, thus supporting the intermediation in ALL from banking system.

PERFORMANCE OF DEPOSITS

The dynamic of recent developments in the monetary supply affirms an improvement of deposits situation during the second half of 2009, mainly concentrated at the end of the period. Statistical effect of deposits withdrawal at the end of 2008 has impacted the negative annual pace of deposits growth in the third quarter. The neutralisation of this effect in October is reflected on the expansion of total deposits in annual terms where in November recorded an annual growth of 5 percent. The change of depositors’ behaviour in the
framework of the measures taken for the prevention of global crisis effects allocation as well as the foreign exchange flows in the form of remittances during the summer months, are thought to have effected mostly the recovery and growth of ALL -and foreign currency-denominated deposits in the second half of year.

Developments in deposits stock excluding exchange rate effects displays a continued improvement of the system deposits’ situation, which in November resulted 1.2 percent higher in annual terms, relative to the reduction of this stock of higher 6 percent at the end of first half year. ALL-denominated deposits provided the highest contribution to its broadening, which have continued to return to the system more quickly than deposits. ALL denominated-deposits, during the last quarter, increased gradually, by 1 percent and 3.5 percent in annual terms, in October and November, respectively. Foreign currency-denominated deposits stock, excluding exchange rate effect, at the end of the period resulted around 1.6 percent lower than in the previous year, recording however an improvement against a higher drop in the first half of year.

A gradual trend of demand deposits shift to time deposits is noted in the second half of year. This fact is reflected on the increase of time deposits share to total stock by 78 percent at the end of the period. Demand deposits experienced an annual average fall by 5 percent during October-November, while time deposits rose by 1.2 percent, thus transmitting positive signals about the restore of confidence in banking system.

Developments of deposits, according to economic agents, affirm a higher growth of households’ deposits, mainly in ALL denominated time accounts. Households’ stock of foreign currency-denominated deposits continues to remain lower than in the previous year, owing also to the higher outflow of this category from the banking system. Monthly developments in business’ deposits
resulted more unstable, incurring fluctuation according to their activity. While in annual terms, business’ deposits have been cut during the second half of year, owing to the reduction of time deposits, starting since September and a considerable shift is noted regarding business’ foreign currency demand deposits to time deposits. During this period, demand deposits of business reduced averagely by about 14 percent in annual terms, while time deposits incurred a rise by about 12 percent. Developments in the performance of businesses’ deposits signal their expectations for a possible slowdown of the economic activity at home, a fact which is supported also by all available data of the real sector.

PRIVATE SECTOR LENDING

Developments in lending to the private sector during the second half of 2009, reveal a further slowdown of loan increase. Annual growth of loan
portfolio to the private sector slowed to 10 percent in November. This rise, excluding the exchange rate effect, was only 3 percent, 4 times lower than the one of June 2009. Unlike the first half of 2009, in its second half the decline of the demand for credit is reflected on the ever-increasing lower paces of lending to the private sector. The slowdown of economic activity and uncertainty for the future in the light of relatively tightened lending standards, have imposed the decisions of economic agents to postpone the investments plans and to lower the financing of their activity through borrowing.

The highlighted deceleration of credit, like in the first half of year, is considerably imposed by the slowdown and later on by the tightening of foreign exchange loan. After the deceleration at sharp paces throughout the year 2009, foreign denominated credit portfolio during September-October, started to reduce, being contracted averagely by 3.5 percent in annual terms. The ever-decreasing foreign currency lending has reflected a more cautious behaviour of banks, which factorise more the indirect risk of exchange rate in the non-payment of loan. Moreover, customers should become more aware regarding the risk they undertake while attaining a loan denominated in a currency different from the currency they generate incomes.

ALL-denominated loan continues to maintain relatively high growth paces. However, in the last three months there are noted signs of its deceleration. ALL-denominated loan portfolio is broadened by about 28 percent during September – November, against the relative average pace of the annual growth at 34 percent, maintained during the preceding months of year.

Annual growth of credit to businesses during the second half of year has pursued the uniform fall during the second half of 2009, pointing to 5 percent in November. Credit for liquidity continues to increase at higher paces relative to the loan for investments. Both have maintained the same downward
trend, and their annual growth remains at 10 and 2 percent, respectively in November. New credit for liquidity purposes has maintained high rates throughout year 2009, comparable to those of 2008. In the meantime, the loan for investing purposes has been declining continuously, particularly in the last three months of year.

According to surveys with bank’s specialists, the ever-decreasing demand of economic agents led to the highest slowdown for investments, as well as of more conservative policies of banks itself, particularly in terms of this type of loan. Trade remains the most important sector in lending, although it has manifested a slowdown of growth paces, the latter continues to maintain relatively high rates of credit surplus expansion by about 11 percent. Lending activity contraction is more considerable for the construction sector. Credit portfolio to this sector, in the second half of year, shrank by 1% relative to year

![Chart 40 Contributions to the annual growth of loan to businesses (left-hand) and annual growth of loan to liquidity and investments (right-hand)](chart40)

Source: Bank of Albania

![Chart 41 Credit portfolio and NPL performance by sectors of the economy (in %)](chart41)

Source: Bank of Albania
2008, compared to the annual average increase of 24 percent, it manifested during the first half of 2009. The considerable deterioration of this sector portfolio quality, the perception on surplus investments in this sector, and the uncertainty on the performance of real estate market in future, have made banks more conservative to finance this sector. While, industry sector has manifested a deceleration of growth paces averagely at 14%, compared to the average of 24% in the first half of year.

Unlikely the loan to businesses, the slowdown of the loan to households has appeared since two years already. Following a modest expansion during the first half of 2009, the portfolio of this loan has started to tighten during the last month, remaining at about 1 percent lower in November than in the previous year. These developments of the loan to households reflects both the drop of consumer loan and the slowdown of housing market, as well as the continuing tightened conditions kept from banks.

Consumer loan, whose performance was weak over the year 2009, is contracted in annual terms, recording in the two last months a negative annual change of 10 percent. Households have manifested an ever-increasing conservative conduct against the consumption and particularly regarding its financing with loans, as shown by the climbing rate of payments in the portfolio of this loan.

Housing credit, accounts for about 77 percent of loan to households, has been slowed down uniformly during the second half of year. In November, its portfolio increased at annual terms only by 2 percent, 8 percentage points lower than in June. The average rate of new loans, granted from banks for housing purchase purposes, during the last 5-month period, is about 30 percent lower than in the first half of 2009.
Box 5. Summary of lending activity surveys’ results

Surveys’ results of lending activity support the concluded performance of this indicator and provide some available indices regarding its future.

Survey aggregate results suggest that standards applied on lending are tightened further during the forth quarter. The major part of banks (7 out of 10 banks) have not changed these standards during this period, whereas other banks have conducted this change mainly on the tightening direction. In sectoral terms, the standards applied on loans granted to businesses are strengthened at a lower rate than in the third quarter. Standards applied on loans granted to households are tightened at a higher rate. Standards applied on small-and-medium sized enterprises continue to be more tightened relative to corporations (the respective balances are -7.9 and -6.6 percent). According to the purpose of loan use, the tightening degree of standards reveals higher for the loan for investments purposes than for the loan for working capital purposes.

All the considered factors have affected the tightening of lending standards in the third quarter of 2009, regarding both businesses and individual loans, but at a lower rate. Banks tightened the lending standards mainly through the terms regarding the borrowing cost; banks increased the average margin of credits, the margin for loans with higher risk and the loan commissions.

According to bank experts’ estimations, the demand for loans from businesses and households, is decreased, however at a lower rate in comparison to the third quarter of previous year.

Expectations for the first quarter of 2010 reveal optimistic, in terms of easing the lending standards for both categories, business and households as well as on their expected increasing demand.

Business Loans
During the forth quarter of 2009, the tightening of business loan standards continued to decrease, maintaining the trend started in the second quarter of 2009. Thus, the net percentage of banks reporting a lower rate of loan standards tightening increased in comparison to the previous quarter: net balance of loans standards to business increased to -2.3 percent from -7.6 percent in the third quarter of 2009.

The softening of tightening degree of loan standards during forth quarter of 2009 is reflected on the standards applied to small-and-medium-sized enterprises: net balance increased to -7.9 percent from -12.2 percent in the third quarter of this year. Net balance of loan standards to corporations was about 2 percentage points higher than that of third quarter. According to the purpose of the loan use, the tightening of lending standards was higher for the loan for working capital than for investments loan. All factors considered in the survey of the forth quarter of 2009 have impacted the reduction of the tightening standards degree for the loan to business.

In the forth quarter 2009, banks have strengthened lending standards through the terms regarding borrowing

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Note 1. The positive balance indicates easing of lending standards or that the factor has impacted the easing of lending standards; whereas the negative balance indicates tightening of lending standard or that the factor has impacted on the tightening of lending standards.
cost; banks increased average margin of loans, the margin on loans with higher risk and raised the commissions. Unlikely, terms which are not related to loan cost have affected the implementation of a more easing lending policy; banks grew averagely the amount of loan and its maximum maturity term.

Demand for loan. Net demand for loan is assessed to decline as revealed by the survey of lending activity for the forth quarter of 2009, however at a lower rate than in the third quarter of this year. The main factors affecting the fall of the demand are the reduction of need for the financing of fix investments as well as the current and expected macroeconomic situation. Net balances of these indicators are -30.4 and -27.7 percent, respectively.

Expectations. Banks’ experts expect an easing of the loan standards in the first quarter of 2010. Net balance of expectations is +15.2 percent. The easing of loan standards granted to businesses is expected in terms of the loan granted to small- and-medium sized enterprises as well as for the loan accorded to corporations (net balance 20.0 percent and 12.2 percent, respectively).

Households loans
Lending standards applied on individual loans are tightened further in the forth quarter of year, relative to the previous quarter (net balance point to -4.0 percent from the balance of 0.0 percent in the previous quarter). Standards on consumer loans are tightened more than for the housing loans; the net balance of consumer loans pointed to -8.7 percent relative to the net balance for housing loan -1.7 percent. Banks have tightened the lending standards during the forth quarter of year through the increase of higher risk loan margin, whose balance grew to -7.8 percent relative to -3.8 percent in the previous quarter.

These developments in consumer loan are mainly impacted by the individual financial situation, which was the factor with the highest impact on the strengthening of loan standards during the forth quarter of 2009.

Loan demand. The households’ demand for loan, according to banks experts’ opinion, is estimated to have been decreased during the forth quarter of 2009, but at a lower rate than in the previous quarter (net balance of banks stating for an increase of the demand points to -18.7 percent, relative to -21.2 percent in the previous quarter). Households’ demand for housing loans is assessed to be lower than their demand for consumer loans. In real terms, households’ need to finance consumption is ranked as the most important factor encouraging the households’ demand, whose balance climbed to 25.0 percent, relative to 17.0 percent in the previous quarter.

Expectations. Banks expect a slight easing of lending standards to individuals in the first quarter of 2010 compared to those applied in the forth quarter of 2009. This easing will reveal higher for housing loans than for consumer loans (net balances points to +13.7 percent and +4.4 percent, respectively). In the meantime, banks’ experts expect a growth of the demand for loans during the first quarter of 2010 (balance +14.8 percent).
IV.2 LABOUR MARKET AND WAGE

During the third quarter of 2009, labour force grew by about 0.3 percent, whereas the number of unemployed persons recorded an uprise about 0.2 percent in annual terms. Average number of recorded unemployed persons increased slightly during the year, where the highest annual rate is recorded in the third quarter, about 1.4 percent. Thus, given these developments, unemployment rate in this period pointed to 12.76 percent, fluctuating close to the average rate of 2008.

Employment by non-agricultural private and public sector has not recorded considerable changes during the third quarter of year. In more concrete terms, employed persons in non-agricultural private sector increased their number to 0.7 percent compared to the same period of previous year recording the lowest rate since 2004.

### Table 11 Performance of labour market indicators

<table>
<thead>
<tr>
<th>Some indicators of labour market</th>
<th>Q1 2009</th>
<th>Q2 2009</th>
<th>Q3 2009</th>
<th>Difference (*)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Labour force</td>
<td>1,114,161</td>
<td>1,114,166</td>
<td>1,113,580</td>
<td>0.33</td>
</tr>
<tr>
<td>Total number of employed persons</td>
<td>972,851</td>
<td>972,831</td>
<td>971,518</td>
<td>0.17</td>
</tr>
<tr>
<td>Number of employed persons in public sector</td>
<td>166,563</td>
<td>166,453</td>
<td>166,453</td>
<td>-0.06</td>
</tr>
<tr>
<td>Number of employed persons in non-agricultural private sector</td>
<td>230,739</td>
<td>237,829</td>
<td>236,516</td>
<td>0.73</td>
</tr>
<tr>
<td>Number of employed persons in agricultural private sector</td>
<td>568,549</td>
<td>568,549</td>
<td>568,549</td>
<td>0.00</td>
</tr>
<tr>
<td>Registered number of unemployed persons</td>
<td>141,310</td>
<td>141,335</td>
<td>142,062</td>
<td>1.42</td>
</tr>
<tr>
<td>Unemployment rate (in %)</td>
<td>12.68</td>
<td>12.70</td>
<td>12.76</td>
<td>0.14</td>
</tr>
</tbody>
</table>

Source: INSTAT Conjuncture Main Economic Indicators, July-September 2009

(*) Annual change of Q3:2009 to Q3:2008 in percent, for the unemployment rate is in pp

Performance of employed persons in non-agricultural economic enterprises displayed different dynamics compared to sectors level during the third quarter of 2009, whereas as aggregate indicator, it did not record...
any growth. In more concrete terms, the highest growth of employed persons was recorded from hotels activity, about 18.3 percent. On the other hand, other activities of services experienced a slowdown of growth annual paces of employment indicator, recording the rates of 9.6 percent in the retail trade branch, 3.2 percent in “post”, -8.7 percent in “telecommunication”. As regards to production sector, employed persons’ number in industry continued to decline at annual rate, by about 4.6 percent. Unlike, construction recorded the highest rate of annual growth of this indicator during 2009, about 9.5 percent, however it remains at lower rate than in the previous year.

![Chart 46 Employment index performance by economic activity](chart)

**WAGES IN ECONOMY**

Performance of wages\(^5^7\) in economy, during the third quarter of year, continued to record a climbing trend in public sector and accelerated the growth pace in production and services sector. The monthly average wage in public sector during the first three quarters of 2009 increased averagely by 12.7 percent, about 3.8 percentage points higher, compared to the same period of previous year. This performance of wage has reflected the decisions taken from Government regarding the increase of wage in public sector for some categories of profession. In the third quarter, this indicator recorded the highest annual growth rate for the year 2009; 16.4 percent in nominal terms or about 13.9 percent in real terms.

The nominal average wage\(^5^8\) in production and services sector recorded the highest annual growth rate in the third quarter of 2009, about 8.4 percent, 5.5 percentage points lower than the average annual growth of 2008. In real terms, the average wage of production sector increased by 6.2 percent in the third quarter of previous year.
The performance of average wage by economic activities accelerated its climbing pace in services sector, while it increased at lower rates in production sector, in the third quarter of 2009. Thus, the average wage continued to record the highest pace of annual growth in transport and telecommunication, about 17.2 percent, to be followed by the trade activity where this indicator raised by 14.7 percent. In production sector activities, the average wage slowed the raise, by recording an annual growth of about 6.9 percent in industry and 2.9 percent in construction.

**IV.3 IMPORTED INFLATION**

Inflationary pressures from the economy outside Albania on the overall price rate of consumption showed weak during the year 2009. The global
economic fall along with the drop of raw materials costs compared to the high rates of 2008, provided the conditions for a decline of inflation in the world. In line with the global trend, the average annual inflation at home (2.2 percent) dropped by 1.2 percentage points relative to the previous year. This drop was lower than the one noted abroad, as attested by the positive spread of inflation at home to the inflation average of Italy and Greece. This measuring has manifested a highlighted increasing trend since the beginning of year. In average terms, for this year, this indicator pointed to 1.3 percentage points, while one year ago pointed to -0.3 percentage points. The broadening of this gap, particularly in the second half of year (averagely by 1.8 percentage points), mainly reflects the transmission at a higher degree of the exchange rate depreciation inflationary effect.

Domestic currency is depreciated in the same period averagely by 7.6 percent against the European currency and by 13.8 percent against USD, leading to an increase of imported inflation. The latter performance is of a high importance in shaping the inflation rate at home, particularly of tradable goods component. This component shares about 60 percent of consumer goods basket and represents that part of consumer goods which derive mainly from imports. While for a period of some years, ALL strong position against European currency has softened the inflationary pressures coming from abroad. In the last year this factor provided an inflationary effect. Imported inflation was 6.9 averagely in 2009. This figure reveals 3 times higher than its historic average (2.4 percent). The action of this factor became more sensible in the forth quarter. The transmission share of exchange rate, based on empirical studies as well, points to its maximum rate (99%) after three consecutive quarters.

In the meantime, ALL exchange rate against US dollar has not imposed increasing pressures on oil price during the second half of year. ALL is appreciated by 5.2 percent compared to the first half of year.
The international conjectural developments are estimated to have completely triggered oil price performance in the domestic market. Oil price in the domestic market, after recording a fall in the two first quarters, showed a climbing trend until the end of year. Average price of a litre of oil in the retail market amounted to ALL 114.8 in the second half of year increasing by about 10 percent against the average recorded during the first half of year. However, this price continues to be lower (about 20 percent) than in the previous year, time when the price of this product experiences a sharp growth. Developments at this market are mirrored on the sub-item index “Services to personal transport vehicles” in CPI goods basket. Annual inflation of this index recorded 5.5 percent relative to the first half of year. While sub-item index “transport services”, which relates indirectly to the domestic oil market, remained unchanged in average terms.

IV.4 EXPECTATIONS FOR INFLATION IN ECONOMY

The expectations of different economic agents regarding inflation remained at low rates during 2009. Expected inflation of consumers pursued the fall during the two first quarters of year, started since the last quarter of 2008. In the third quarter, these expectations displayed an upraising turn, but however remaining too close to the lower limit of the Bank of Albania’s target band.

Unlike, business’ expectations for inflation after one year perused the fall even in the third quarter of 2009. The survey organised with banks’ experts reveal that the rate of expected inflation after one year in the forth quarter of year of 2009 remains unchanged since the previous quarter, respectively 2.7 percent.

V. FINANCIAL MARKETS, INTEREST RATES AND THE EXCHANGE RATE

Bank of Albania cut the key interest rate by 50 percentage points in October, thus transmitting a signal on the easing of monetary conditions. A declining trend of interest rates in the money market observed this direction.
in addition to the improvement of liquidity situation and the strengthening of security in the market. The cut of key interest rate is transmitted in the primary market of the Government securities, along with the reaction of interests in interbank market, where yields raised on ongoing basis since the beginning of year. These positive signals are still not reflected on the lending activity of the economy. ALL denominated loans interest rates remain at relatively high and volatile levels, thus reflecting high risks rates, giving rise to uncertainty about the economy performance at home.

**INTERBANK MARKET**

The second half of year is characterised by a declining performance of interest rates in interbank market and an improvement of banks’ liquidity situation. On the other side, the exchanged volume among banks recorded lower values during this period and has manifested a climbing trend only in the last quarter. Interest rates during these months have manifested a falling trend and more controlled volatility than in the previous half of year\(^6\). Banking system continued to lack liquidity during this period, and the Bank of Albania injected liquidity by employing its transactions in the open market, through the reverse repurchase agreements of one week maturity term. Bank of Albania, in addition to this instrument, employed the longer–term maturity REPO agreements, particularly in the last months there are employed the 1- and 3-month REPO agreements. The supplied liquidity was high, while deposits level at commercial banks recorded the values of the period prior to November 2008, thus confirming the signals of their improvement. Bank of Albania continued to employ the reverse repurchase auction at fixed price and unlimited amount. The average volume of one-week reverse repurchase auctions, during this half of year, amounted

<table>
<thead>
<tr>
<th>Chart 52</th>
<th>Interest rates in the inter-bank market (left-hand) and daily lending volume (left-hand)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>![Chart Image]</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Quarter</th>
<th>Daily interest rate</th>
<th>1-week interest rate</th>
<th>Daily volume</th>
<th>Weekly volume</th>
</tr>
</thead>
<tbody>
<tr>
<td>Q 2-09</td>
<td>5.08</td>
<td>5.65</td>
<td>1,620</td>
<td>712</td>
</tr>
<tr>
<td>Q 3-09</td>
<td>5.30</td>
<td>5.67</td>
<td>1,319</td>
<td>228</td>
</tr>
<tr>
<td>Q 4-09</td>
<td>4.93</td>
<td>5.35</td>
<td>1,214</td>
<td>649</td>
</tr>
<tr>
<td>October-09</td>
<td>5.10</td>
<td>5.68</td>
<td>905</td>
<td>325</td>
</tr>
<tr>
<td>November-09</td>
<td>4.90</td>
<td>5.19</td>
<td>1,281</td>
<td>817</td>
</tr>
<tr>
<td>December-09</td>
<td>4.78</td>
<td>5.17</td>
<td>1,472</td>
<td>650</td>
</tr>
</tbody>
</table>

Source: Bank of Albania
to averagely ALL 21 billion from ALL 14 billion in the previous period, by meeting the demand of participating banks. The allocation of liquidity has been uniform, leading to lower interest rates volatility.

At the end of October, Bank of Albania by estimating inflation performance within the target band, with the purpose to promote economic activity and the reduction of credit cost, decided to cut the ALL key rate by 50 basis points to 5.25 percent. Trade volume in interbank market, after the lower values of September and October, recorded a growth during the last months of year. The improvement of liquidity conditions should have been reflected on a cut of interest rates in interbank market, whereas banks financing in money market has manifested a more efficient behaviour. The interest rates in interbank market have transmitted the cut of key rate and the neutralisation of pressures for liquidity. Daily lending decreased slightly, amounting to ALL 1.21 billion relative to the previous quarter, while the total volume of interbank transactions increased by 0.27 billion amounting to ALL 1.76 billion, notwithstanding it is lower than first half of year, in half of year terms. Banks continue to prefer daily transactions while weekly transactions have been climbing during the last months affecting positively the growth of total transactions volume. In average terms, the daily interest rate fell to 4.93 percent from 5.30 percent, it was in the previous quarter, while the one-week is reduced to 5.35 percent, or 32 percentage points lower. In December, the exchanged volume in interbank market recorded an increase and interest rates have pursued the dropping trends affected mainly by the supply and demand factors.

**PRIMARY MARKET**

Primary market yields maintained the upward trend in the major part of this half of year, to change direction onwards, during November and December, as a reaction against the monetary policy easing. Yields increase is attested for all maturities and has been present since the beginning of year, being highlighted at definite periods. The cut of key interest rate at the end of October has been transmitted at yields in the primary market, in meantime the

![Chart 53 Government securities’ yields in the primary market (left-hand) and yield curve (right hand)](chart)

Source: Bank of Albania
The banks participation in the Government securities auction has been high, during this period, however it is has not affected the smoothing of the uprising pressures, thus denoting an increase of their assessment about the risk. The growth of issuances during this period is an other factor which has not helped the hampering of climbing trends. The more highlighted growth of T-bills yields are observed for the longer maturity, being then transmitted to the bonds yields, as measured by this indicator. At the end of October, the 12-month T-bills interest pointed to 9.43 percent declining afterwards at 9.06 percent or at a rate equal to the average of first half quarter. Notwithstanding yields performance has manifested a downward trend, They remain at higher rates relative to the preceding period in average terms. At an average rate the one-year T-bills yield is 0.22 percentage points higher than in the first half of year.

Other 6 and 3-month maturities yields attested the same performance, but at a more controlled rate. The 6-month yield, after pointing to 7.73 percent in October, continued to drop, thus recording the rate of 7.52 percent at the end of December or 0.15 percentage points lower than the end of June. 3-months T-bills yield displayed a more controlled volatility and has approximately remained at the same level.

Bonds in primary market manifested similar trends to T-bills. Bonds yields increased mainly during the third quarter of year affected by the increase of risk assessment from banks while banks’ participation in auctions appears plausible. 2-years bonds yield, at actions held in November and onwards, dropped by observing the overall fall displayed by the T-bills. At the end of this quarter, 2-year bond yield was assessed at 9.30 percent or 0.05 percentage point less than the average of the first half of year. Yield of 3-and 5-year bonds have observed the same performance (at flexible interest rate).Thus at the end of this year, it points to 9.60 and 10.93 percent, respectively. It is worthy to underscore that the yield raise of flexible interest rate bonds was mainly affected by the performance of instruments, by which it is pre-measured, as the accepted margin has always followed a downward trend during this period. Yields rates among different maturities denote a growth mainly for the short and medium-term rate, therefore making the slope of curve be more emphasised in its first part.

**INTEREST RATES ON NEW DEPOSITS**

In the second half of 2009, interest rates for both main currencies, ALL and EUR, continued to maintain higher rates relative to the key rates. Data reveal that the cut of key interest rate by 0.50 percentage points from the Bank of Albania is not implemented from all banks of the system, owing to the high competition to maintain the market shares.
Average interest rate on ALL-denominated deposits was approximately 5.56 percent in the second half of 2009, by 0.18 percentage points higher relative to the first half of this year. The 1-and 12-month term recorded an increase of the average weighted interest rate. After the end of summer season, banks proceeded to complete at high margins (even after the cut of the key interest rate) through the prior implementation of end-year supplies. However, the average trend of ALL deposits after August 2009 has been declining, pointing to 5.28 percent in November. This rate is 0.15 percentage points lower than November 2008 (ALL core rate is cut by 1.00 percent in this period).

The interest rate of Euro-denominated time deposits maintained in general a reverse shifting trend with that of the domestic currency. They recorded a fall by 0.28 percentage points in the second half of year. Reductions of interests rate are recorded for all the usage terms. However, the interest rates of Euro-denominated deposits continued to maintain high values relative to ECB key rate, which pointed to 1.00 percent throughout the second half of 2009, being conditioned by the liquidity situation and the individual orientation of banks policies regarding the interest rates. Banks continue to employ deposits interest rates as reference rates for Euro-denominated time deposits. The weighted average interest rate of Euro-denominated deposits was cut considerably in November (2.00 percent). Since October, this rate reflected high values, affected by the reduction of
INTEREST RATES ON NEW LOANS

The average interest rates are characterised by a high volatility during July – November. The business seasonal effect for working capital to increase inventories was one of the main factors. Their effect continued until October, while November recorded a decline of interest rates on new ALL–denominated loans. The tightening trend on lending is emphasised in European currency, which has expanded the spreads with the benchmark rates (as euribor, libor euro and funds cost).

The weighted average interest rate on new ALL–denominated loans decreased 0.04 percentage points, in average terms, during July-November of 2009. This performance reflects the observation of the tightened lending conditions during this period.

According to maturity terms, it is noted the trend to tighten more both the long-term and investments loans as a reaction to banks perception on the increased uncertainty, regarding the economy development at home. Interest rates on short-term (0-6 month) displayed increasing trend until October, owing to the high seasonal demand for the growth of inventories for business, and decreased onwards, returning to normality in November. Average interest rate on new Euro-denominated loans revealed an increase in this period compared to the benchmark rates. It resulted averagely 8.05 percent or 0.37 percentage points higher than the previous half of year. The overall perception on uncertainty, the close monitoring of foreign–denominated lending and the factorization of exchange rate volatility, imposed an increase of prices from banks. Euribor rate in international markets is cut during this period, Euro-

![Chart 58 Weighted average interest rate on 12-month EUR, EURIBOR and loans](chart58.png)

Source: Bank of Albania

![Chart 59 Average intermediation margin in ALL and EUR (left-hand); and the spread between average interest rate on ALL and EUR loans (right-hand)](chart59.png)

Source: Bank of Albania
denominated credit increased for all terms. The interest rates (working capital to businesses) observed the same behaviour with the domestic currency, in the short-run, highlighting the tightening trend of banking system to provide seasonal liquidity denominated in foreign currency.

Intermediation cost (loan/deposit spread) maintained a high rate during July – November 2009. This spread observed opposite directions, being increased in terms of ALL by 0.22 percentage points and in terms of EUR by 0.66 percentage points. This indicator pointed to 8.23 percent for ALL and 6.25 percent for EUR. The interest rates spread of ALL loans to EUR changed direction in November. It recorded a drop of 0.98 percentage points pointing to 5.27 percent.

**EXCHANGE RATE**

The second half of 2009 experienced a depreciation of ALL at effectively nominal terms, by relatively stable paces. In annual terms, the changes in the NEER during this period, fluctuated within a narrow band (from 7.42 percent to 8.78 percent) comparable to the one of the first half of year (-4.2 percent to -10.2 percent). The performance of ALL during this half of year in the domestic exchange market has resulted on the depreciating direction. In average terms, the domestic currency depreciated against both currencies, EUR and USD, by 9.57 and 2.36 percent respectively, relative to the same period of the previous year.

Developments in EUR/ALL ratio, beyond the already known factors which impacted the misbalance of supply demand, reflected at a considerable rate the effects of seasonal nature. Therefore, at the begging of the second half, the domestic currency was strengthened owing to the remittances which characterise this period. This effect seems to have posted a preliminary neutralisation, leading to a shift of the preceding behaviour against the end of the seasonal supply since August. In the succeeding months, ALL positions
against foreign currency continued to fluctuate at depreciating direction. This performance owes to the volatile supply demand ratios, which are also accompanied by an uncertainty of market agents, which was reflected at a historic volatility in the last quarter of year. The confidence growth to the domestic currency combined with the seasonal effect of the end-year have supported the gradual reduction of ALL depreciating positions.

ALL performance as a ratio to USD, resulted on the declining side relative to the same period of 2008. However, at half of year terms, USD/ALL ratio displayed an appreciation of 5.17 percent. This ratio performance, during this half of year, partially resulted in line with EUR/USD ratio developments in the international market, for the transmission of USD weak positions against EUR (a depreciation of 9.17 % in 6-month terms) was not a completed one.

EUR/ALL ratio after the accelerated rise in favour of European currency during the third quarter, seems to have been stabilised and has pursued almost the same performance with that of the other countries.

VI. EXPECTED ECONOMIC DEVELOPMENTS DURING 2010

Economic activity during 2009 took place in face of unfavourable demanding and financing conditions. Overall, macroeconomic indicators
are affected, by the contraction of regional and world economies, as well as by the developments in the domestic market. The slowing down of the world economy is transmitted to Albanian economy in the form of the external demand reduction for goods and services and a contraction of other financial capital inflows. The trend of monetary aggregates and credit to economy confirms also the slowdown of the domestic demand.

Developments in the external sector of economy reflect the intertwined of financial and capital foreign inflows and of competitiveness of the Albanian economy. The trade opening during the two last years was encouraged by the financial inflows in the form of foreign direct investments and external borrowing. Along with the sustained economic growth and high pace of investments, their injection into the economy provided a higher consumption and an increase of trade and current deficit of the country. The gradual tightening of the external financing during 2009, accompanied by a strong slowdown of lending activity in the financial market, hampered the maintaining of investments pace in economy, while consumption rate manifests an inertia trend. The reduction of domestic and external investments’ sources has affected the economic growth throughout this period.

Indirect data of last quarters denote a contraction of domestic demand relative to the previous years owing also to the slowdown of the lending activity. Economy lending by banking system in annual terms is slowed by one figure rate against the average pace of higher than 40 percent in the two previous years. Lending to economy, in its major part, is financed by foreign assets stock at commercial banks balance-sheet. In presence of this stock reduction after the withdrawal of a part of deposits at the end of 2008, the funding of economic growth through financial intermediation is becoming more difficult. For 2010, lending credit growth extended to private sector of economy from banking system is forecasted to be about 1/3 of the one injected in 2008. The performance of credit portfolio quality and the higher risk prim, in presence of other factors, shall make difficult the recovery of banking system lending to the economy private sector, to be characterised by the previous paces.

External financing sources of the economic growth for the current year are also lower relative to the two previous years. External financing through capital and financial inflows has contributed on the continuance of aggregate demand expansion during 2008-2009. Financial flows in 2009 are expected to be at about 11-12 percent of GDP, while 2008 financing from external financial flows accounted for about 17 percent of GDP. In general, these flows consist on foreign direct investments, partially as privatisations of state-owned companies, as well as the external borrowing mainly of public sector. Further lowering of theses flows during the current year, as a consequence of the reduction of foreign direct investment and the tightening of financial borrowing standards in international markets, is expected to impose an increasing impact on the country economy during this year.

Along with the developments in the financial markets, long-term factors that have contributed on the economic growth reveal more reduced during 2010.
Macroeconomic development and economic growth during the last years is enhanced by the high rate of remittances which shall remain low during 2010, as a result of the difficult situation in our trading partners. In terms of GDP, remittances foreign-denominated inflows fluctuate at 12-15 percent, while during 2008 and 2009, their rate dropped by 8 percent each year pointing to lower than 10 percent of GDP. The further drop of remittances during the forthcoming year shall have a negative effect on the economy aggregate demand. The decreasing trend observed during the last two years, is neutralised by high financial flows of foreign investments and external borrowing. Their ongoing contraction tends to be transmitted at consumer rate and on the climbing opportune costs of investments in economy being reflected on the fall of the economic strengthening in the medium-term period.

In presence of these developments, during 2010, the economy is expected to encounter reduced financing possibilities of aggregate demand and a moderated performance of consumer and investments. Real economy is expected to remain under its long-term potentiality in presence of restrictions in terms of consumption financing sources. This shall transmit reduced inflationary pressures generated from the domestic economy. On the other side, the lowering of the domestic demand shall be reflected on a gradual improvement of the economy external balance.
Endnotes

1 Consumer spending and investments dropped by 0.1 and 0.8 percent, respectively in the third quarter 2009 relative to the previous quarter.
2 Brazil, Russia, India and China
3 Calculated from the spread of the monthly average of these indicators in June with December.
4 Exports during January –November 2009 fell by 17% in annual level.
5 Retail trade dropped by 1.4% in the first 9-month period of 2009, consumer loan recorded lower increasing rates since the beginning of year, import of consumer goods maintained the rates of the previous year. Wages in economy have recorded a slight increase while remittances dropped by 6.6%.
6 Current and capital expenses during January-November increased by 16 and 23% respectively in annual terms.
7 See the analyse in Chapter IV.3 for more details
8 Production gap is measured as the spread between current production of economy with the production it would potentially generate under the complete exploitation conditions, with maximum efficiency.
10 In case of Albania, Monetary Conditions Index (MCI) is a weighted average of the key interest rate changes and the Nominal Effective Exchange Rate, against their respective values in a basic period. Since the second quarter of 2009, the basic period is December 2005. MCI ratio in case of Albania points to 1.82:1, implying that the effect of an appreciation 1.82 percent of NEER on aggregate demand, would be neutralised by a cut of the key interest rate by 1.0 percentage points. Index is monitored to see the monetary conditions direction and not as an operational target.
11 The share of this item on total shares in calculating consumer price index is approximately 19 percent.
12 Oil price in the domestic market is almost affected by the oil price in the world market, which have been increasing recently.
14 Average of core inflation in annual terms for the last decade points to about 0.8 percent.
15 CPI tradable sector basket, are excluded the process effects of “Fruits” and “Vegetables and potatoes” items’ prices.
16 The estimate takes into account the tradable sector share (0.62%), average annual inflation for the ALL/EUR Exchange rate for 2009 (+7.5%), average inflation of tradable sector during July-December 2009 (3.5%) and historic average (0.8%).
17 Which are excluded from CPI non-tradable sector, sub-items by administered process.
20 The confidence indicators for the industry, construction, services and consumers sectors, which summarise in a sole indicator the judgements expressed from all the above mentioned groups, based on the confidence survey results.
21 According to the data from lending activity survey at banks, lending standards are contracted at a higher rate in terms of the loan for investments purposes, relative to the loan for inventory and working capital purposes.
22 Annual fall of exports and imports during this period provided an impact on an expansion by 0.12 percent of net exports.
23 Analysis at sectoral rate referring to publications “Quarterly Gross Domestic Product”, September 2009 and December 2009, INSTAT.
24 Housing price index is calculated based on the hedonic way of indices calculation, which provides an index cleaned from the effect of quality change, based on the process of announcements for housing sale in “Çelësi” newspaper. The major part of announced process are issued in the European currency. The major part of notices relate to the re-sail from owners and sales for the
first time. Index also might not trigger in time the change of selling price as an effect of its change from housing constructers.

25 Selling price ratio to house rent is a simple indicator that shows if housing price is appreciated, from the comparison of ratio current values with its historical rates.

26 Data of electrical energy balance are available until November.

27 Both current revenues and expenses recorded an annual growth of 3.7and 10.4 percent, respectively during July – September '09.

28 Deficit of revenues amounted to about EUR 34 million relative to the surplus of EUR 55 million recorded in the previous year.

29 The latter amounted to about EUR 206 million relative to the amount of about EUR 229 million, it recorded during the Q3'08.

30 The calculations of nominal GDP for the year 2009 are based on IMF estimates for nominal GDP: ALL 1,129,000 million(6th review of PRGF agreement, February 2009, http://www.imf.org/external/pubs/). The rates of different indicators expressed as a percentage of GDP refer to cumulative data for Q4’08- Q3’09.

31 The values of the following ratios refer to cumulative data, which include the period from Q4 of the previous year to Q3 of the referring year.

32 Due to the shortfall of data for December, foreign trade shall be considered on the above-mentioned period.

33 Source: Bank of Albania relevant data and “Maximising the development impact of migration related Financial Flows and Investment from Austria to BiH “, IOM (International Organization for Migration), IASCI (International Agency for Source Country Information).

34 This balance recorded a surplus of about EUR 34.5 million during July-September ’08.

35 Communication services sector recorded a narrowing of this category surplus from EUR 19.3 million during Q3’08 to EUR 6.6 million during Q3’09; while the financial ones record a further expansion of the above mentioned account deficit: from EUR 2.0 million during Q3’08 to EUR 6.4 million in Q3’09.

36 According to the reviewed 2009 projection, approved on September 2009.

37 This rate represents the lowest increase of the decade for the 11-month period.

38 The rate of 14 percent represents the highest annual growth recorded for the year 2009.

39 VAT contribution to the growth of total revenues throughout this year appeared at modest levels (lower than percentage point), meanwhile in the previous years, given that this item has the main share on revenue (35%), this item contributed averagely with about 5 percentage points on the increase of total revenue.

40 The review and approval of the 2009 budget, is carried out in September of this year.

41 The initial rate projected by the Ministry of Finance amounted to 74.8 billion.

42 According to the reviewed projection.

43 Increasing contribution during the last two years of capital expenses is clear from the chart.

44 Growth of this items, for the 11-month period was 27, 31 and 18 percent, respectively.

45 Referring to the 11-month budget deficit ratio against 11-month (IMF) GDP.

46 Syndicated loan is a form of loan provided from a group of resident and non-resident banks in the territory of the Republic of Albania to the Albanian Government by, to finance budget deficit. The maturity of this loan does not take too long.

47 These proceeds refer to privatisation of ARMO (a portion of which were transferred to the 2009account), OSSh, a part of AMC and of the United Bank of Albania stocks, and the licence granted to the forth mobile telephony.

48 In the meantime, Government borrowing policy aimed the increase of Bonds issuance of all maturities, against T-bills.

49 Almost all Western Balkan countries, manifested a deepening of budget deficit owing to the realisation of budged revenue lower to the estimated rate, as well as a high rate of expenses as a reaction to the last economic and financial crisis.

50 The change of GDP real growth at horizontal axe and of budget deficit against 2009 GDP in vertical axe.

51 Horizontal axel shows public debt stock against GDP for the year 2009, while vertical axe shows the difference of fiscal balance to GDP for the year 2009 with 2008. Data for Albania refer to Q3 2009.

52 Excluding the Exchange Rate.
The displayed figures in the lending analysis are excluded from the foreign exchange rate.

During the first half of the year, lending growth hampering was mostly affected by the supply tightening, lending standards from banks, and the difficult liquidity situation.


Based on short-term statistics (INSTAT), indicator of employed persons with wage.

Referred data from “Short-term statistics”, INSTAT, excluding agriculture and “The main Economic indicators Conjecture, July-September 2009”, INSTAT.

Average payment index is calculated as a index of payments funds ratio to employed persons’ number index.

Expectations of economic agents for inflation are measured based on business survey data, consumers confidence survey and the monthly survey of banks’ experts for the forecast of some macroeconomic indicators.

Standard deviation of interest rates in interbank market during this half of the year was 0.36 relative to 0.46 in the first half of year.

At the end of January 2009 the key rate reduced at base rate cut by 50 basis points.

The weighted average interest rate on Euro-denominated deposits was 2.35 percent.

NEER – Nominal Effective Exchange Rate measured against to currencies according to an approximate share they have in trade with abroad, EUR (80 percent) and USD (20 percent). An increase of the NEER implies the appreciation of ALL.

Measured as the quarterly average of exchange rate volatility. The latter is measured as the standard deviation indicator.

The complete data for the year 2009 are still unavailable.
SPEECH BY THE GOVERNOR OF THE BANK OF ALBANIA, MR. ARDIAN FULLANI
At the joint press conference of the IMF Mission, the Ministry of Finance and the Bank of Albania
27 October 2009

At the beginning, I would like to thank the IMF Mission and especially the IMF Mission Chief, Mr. Gerwin Bell on the huge work they have carried out during the last week.

This regular visit of IMF, in the framework of Article IV consultations, coincides with a rather difficult period, as regards to the pressures streaming from the big crisis, which has blown up throughout the world economy since last year.

We have concluded with pleasure that, Bank of Albania shares equal appraisals regarding a lot of developments the Albanian economy has been going through during the first half of 2009. I take advantage to flag once more the conclusion articulated for some time: (1) that Albanian economy and its financial system showed sufficiently resistant; and (2) the policies undertaken from both authorities, the Bank of Albania and the Ministry of Finance, resulted useful for both the establishment and transmission of the right incentives towards financial stability and economic activity at home.

Speaking in more concrete terms about the monetary policy of the Bank of Albania, I would like to emphasise that it has been measured throughout this period, by prudentially reflecting the latest macroeconomic developments, the banking system developments and the agents’ expectations. Also, the strategies used by the Bank of Albania in the money market, are part of this prudence, with the purpose to increase liquidity injection in the system.

Overall, turning the attention to the short-term and long-term horizon, briefly I would like to deal with two or three issues that Bank of Albania has decided to have in its agenda of priorities, for the succeeding months.

First, I would like to emphasise, once more, my idea launched during the Third Forum of the Bank of Albania with the banking system, as regards to the shift of the economy towards a new equilibrium, different from the pre-crisis one. This is an argument which dominates the today debate, and I share the opinion we should factorise this conclusion on our macro- projections of the country development for the forthcoming years.

Second, Bank of Albania considers indispensable to increase the attention and financial vigilance during the succeeding periods. This may imply a further strengthening of macro-financial stability, particularly as regards to the best harmonisation of both basic policies in economy, to pursue the required simulation of the country’s economic activity.
Third, I would assess as highly important the continuance of lending to economy, the attraction of foreign investments and the deepening of structural reforms. The Bank of Albania is committed to provide long-term stability of prices and for that purpose, its decision-making shall continue to be anchored by this legal target. Under the circumstances of a new post-crisis reality, we are not going to draw the attention away from the structural processes of the economy, to further customise the Albanian economy in encountering the post-crisis effects and to turn the latter on a vibrant economy, not only in the region but even more broadly.
In today’s meeting of 28 October 2009, the Supervisory Council of the Bank of Albania, after analyzing the latest economic and financial developments in the country, the macroeconomic projections and the balance of risks for the months to follow, decided to reduce the key interest rate by 50 basis points to 5.25 percent.

The Supervisory Council of the Bank of Albania concludes that the third quarter of 2009 witnessed positive signs in the Albanian economy and financial markets. It particularly marked a turning point in terms of restoring confidence in the Albanian banking system. The stable liquidity situation, the preservation of financial stability and the banking system’s capitalization parameters constitute a solid platform for restoring its intermediation and financial role in economy. In tandem with the latest positive tendencies of the global economy, which still remain frail in terms of their nature and permanence, these developments prompt us to consider the future Albanian economic activity under the optics of a prudent optimism.

Over the course of the year 2009, the Albanian economy has been affected by the global economic and financial crisis primarily through the decline of foreign demand and remittances, higher risk premiums and reduced and high-cost financial support. However, our economy continued to record positive economic growth rates during this period, while the domestic inflationary pressures remain contained. Economic activity at home has been sustained by the fiscal stimulus and the preservation of relatively high consumer demand rates. In the meantime, investments and export demand have recorded lower growth rates in the first nine-month period.

At a global level, the second quarter of 2009 and the following period witnessed stable economic activity. Although the world economy continued to contract in annual terms, the consumed stock cycle replacement set a floor on the downturn of Euro area and US economies. Moreover, this cycle served as a short-term catalyst for the reactivation of their industry and production sectors. In a longer-term perspective, the stable economic activity of the Asian countries -China in particular,- and the global trade growth will fuel the global economic growth. However, the world economy path to a sound and stable growth is a long one. The existing model of global economy has relied on the high consumption and the severe debt situation of the USA, against an Asian countries’ strategy that favours exports and savings. Coupled with below potential economic growth and downward inflationary pressures for a relatively long period of time, the addressing of these imbalances at a global level requires time.
The global financial system, the capital markets, the banking sector and other financial intermediaries seem to be recovering. The monetary and fiscal stimulus has provided its effect at a global level, helping first the recapitalization of the financial system and restoring the lending system. Despite the high risk perception and low risk readiness across the financial agents, the resumption of global financial flows will provide assistance to emerging countries through higher available funds.

Amidst the global development challenges, the Albanian economy recorded positive economic growth during the first half of 2009. According to preliminary data reported by the INSTAT, the GDP grew at an annual rate of 5.3 percent in the second quarter, maintaining similar growth rates as in the preceding quarter. Activity in services provided the main contribution to the GDP growth. The production sector provided additional contribution to the annual GDP growth, mainly owing to the performance of the construction sector. By contrast, industry deepened the downward growth rates that began in early 2009.

The economic growth tendency, albeit at lower magnitude, is also present in several indirect indicators of the economy, namely the higher budget revenues, higher lending to the economy and more stable labour market indicators. However, these indicators, particularly monetary and business and consumer confidence indicators, reflect slower economic growth rates relative to the previous year.

In a macroeconomic context, the slowdown is mostly a reflection of the fall in investment and foreign demand, while consumption and public expenditure have led to higher economic activity.

The economic performance of the first half of 2009, albeit positive, attests to a slowdown of about 1.4 percentage points compared with the same period in 2008. In addition to the general slackening of global inflationary pressures, this situation has been translated into the gradual reduction of inflationary pressures on the Albanian economy. Average inflation marked 2.0 percent in January to September 2009, fully reflecting the exclusion of the first round effects generated from the rise in raw material prices during 2007-2008 and the cessation of effects arising from the latest administrative rise in the energy price. The downward trend of core and non-traded goods’ and services’ inflation attest to the fact that the inflationary pressures generated from the domestic demand-side are subsiding. On the other hand, the relatively strong depreciating movements of the domestic currency, the ALL, during 2009 have pushed the traded goods’ inflation higher to about 3.1 percent in the third quarter. Developments in the labour market and wages do not signal higher future inflationary pressures on the supply-side. Unemployment rate was 12.7 percent in the first half of 2009, similar to the year-end 2008 level. For the same periods, the growth rates of average real wage in economy have been more contained.

The Bank of Albania forecasts and the anchoring of economic agents’ expectations for consumer prices support the preservation and firming up
of consumer price stability in the medium run, expressed in low and stable inflation rates.

Current account deficit narrowed slightly by 1 percentage point y-o-y in the second quarter of 2009, reflecting slower imports and exports in the Albanian economy. In the meantime, workers’ remittances have reduced at relatively lower rates than in the preceding quarters. However, the current account deficit remains high, reflecting the high levels of consumption in the Albanian economy and the unfeasibility of the production capacities at home to meet it. Privatization receipts and the public sector’s foreign currency borrowing led to a positive balance of payments; however, its future stability should rely on longer-term factors.

The government ran an expansionary fiscal policy in the first eight months of 2009. In annual terms, budget expenditure increased by 23 percent, reflecting primarily the rapid increase of capital expenditure. Budget revenues maintained a slower rate than expenditure due to the slower economic growth rate during this period. Consequently, the additional budget expenditure was financed through the use of privatization receipts and the higher public borrowing. This policy has exerted pressure over the increase of Government debt securities’ interest rates of long maturity term.

The influence of fiscal policy on the domestic monetary markets was more moderate during this period since the public debt was to a large extent borrowed from the international capital markets. However, the future persistence of this policy will face less funding potentials of both the Albanian and the international market. This fact calls for the quick return to the consolidating trajectory that the fiscal policy pursued in the pre-crisis years.

The monetary indicators of the third quarter of 2009 attested to the slow money growth tendency. Money supply, M3, recorded an annual growth of 4.5 percent in August vis-à-vis the average growth rate of about 7 percent in the first half of 2009, owing mainly to the lower credit flows to the private sector. Deposits grew substantially in August – about ALL 25.4 billion in monthly terms – in line with their seasonal performance during this period of the year. As at end of period, about 70 percent of the total deposits’ stock growth was time deposits, hence signalling the higher confidence in the banking system.

Private sector credit maintained its slower growth rates in July and August 2009, reflecting both the tightening of credit supply and the contraction of credit demand. Coupled with the reduced use of capacities as reported by businesses in the Bank of Albania survey, this performance signals that the private sector’s investments in economy are downward. Banks continue to apply tight lending standards, while consumer demand and private sector investments have fallen.

In nominal terms, private sector credit grew by an annual average of 16 percent in June to August, markedly lower than the first five months’ average (29 percent). Despite the low growth rates, business credit provided the main
contribution to the private sector credit growth, accounting for about 65 percent. The downward trend of credit attributes to the deceleration of foreign currency lending, whose growth rate was zero in August. In the meantime, ALL lending continued to maintain its average growth rate of 30 percent throughout the year 2009. As a result, the share of foreign currency credit in the private sector’s loan portfolio dropped to 67 percent. The understanding of the consequences of exchange rate movements and the greater tightening of lending for loans denominated in a currency other than that of the borrower’s income, caused the individuals to borrow less foreign currency credit than businesses.

The financial markets attested to an improved liquidity situation and the recovery of the agents’ confidence in these markets. The persistent Bank of Albania’s liquidity supply to the money market helped to calm the market participants down and to supply the market with funds, which served to the private sector’s domestic currency intermediation. The liquidity needs in the interbank market have been declining, hence exerting no pressure over the short-term interest rates. By contrast, the Government securities’ primary market experienced a reverse situation, with the T-bill yields of long-term maturity going up despite the ample liquidity. In September’s last auction, the 12-month yield was 9.40 percent, up by 0.64 percentage points from the year-end 2008.

The high risk premium on long maturity terms and the existence of a shallow financial market were the rationale behind the high Government securities’ long-term yields. On the other hand, the high yields attracted the individuals’ investment in this market, hence providing them with an alternative instrument to keep their savings and at the same time, increasing the share of budget deficit financing from this item. The individuals’ deposits held in the banking system have had a satisfactory return. Weighted average interest rate on ALL deposits marked 5.94 percent in August or up by 0.48 percentage points from the end of the second quarter. This increase led to lower intermediation cost for the ALL during the recent months. Interest rates on new ALL loans declined to an average of 12.86 percent in July and August, down by 0.79 percentage points from the average rate of the first half of 2009. The banking system’s inclination to relieve the cost of ALL loans is attested by the narrowing of its margin and the corresponding reference rate, the T-bills. The spread declined to an average of 3.6 percentage points in summer, from 4.8 percentage points in early 2009.

Going back to today’s decision of the Supervisory Council of the Bank of Albania, allow me to underline that the long-term development perspective of the Albanian economy is positive. Macroeconomic stability and the confidence in the Albanian financial system are the product of our responsible macroeconomic and financial policies undertaken continuously over the course of the recent years. Macro financial stability is a solid foundation for boosting the country’s development in the future.

This development will to a large extent depend on the capacity of the Albanian economy to attract funds, which will buttress its growth. The monetary
conditions are relaxed in line with the dynamics of economic and financial developments in Albania, in our main trading partners and broader in the global economy. This decision represents a new incentive for the economic developments at home, aiming at reducing the financing cost of the economy further.

The performance of lending to economy will be of prime importance in the medium run. The Bank of Albania deems that the stabilization of the banking system’s liquidity and balance sheet indicators will pave the way for the lending process. In this context, the Bank of Albania has been engaged in an active role in terms of stimulating demand and supply with funds. The relaxation of monetary conditions will fuel the growth of business and consumer demand for funds, while the Bank of Albania’s injection of liquidity will assist the banking system in meeting the demand for funds in quantitative terms. The Albanian banking system should understand its role rightly and transmit the relaxation of monetary policy in economy completely and rapidly. On the other hand, a lower pressure of the fiscal sector over the domestic financial markets will in the future lower the risk premium in economy, will create more room for private sector lending and will facilitate the smoothing out of the interest rate curb in favour of lowering the cost of credit further. The efficiency of the monetary policy decision will depend on the market and its participants’ behaviour, wherein fiscal policy plays a key role.

In the long run, the attraction of foreign direct investments and other forms of stable capital inflows should be at the core of our development policies. These funds will not only improve the external position in terms of its stability, but also sustain the country’s long-term growth. Time is ripe for all the actors to carefully analyze the country’s economic growth model in the decade we are approaching. The future economic growth model should in particular consider the competitive advantages of the Albanian economy more, mitigating its reliance on short-term capital inflows and expanding the economic basis, which generates stable and long-term capital flows. In this context, the Bank of Albania remains committed to playing a key role in the periods to follow.

In compliance with our legal and institutional commitment, the Bank of Albania’s monetary policy will aim at creating the proper conditions for a balanced development, characterized by low consumer price inflation environment, moderate fluctuations of monetary indicators and sound macroeconomic agents’ balance sheets.
Dear Governor Rexhepi,

Distinguished ladies and gentlemen,

It is a pleasure for me to participate in this Conference which is perfectly organized by the Central Bank of the Republic of Kosovo, and to witness the amazing progress this institution has achieved in such a short but intense period of time. The energy and desire of the local staff to contribute to the history of this institution, has been rightly channeled by the vision and experience of several managing professionals that have given a valuable contribution in chairing this institution in the last years. I am sure this story will continue to be a successful one, based on the commitment of the management of the Central Bank of Kosovo to achieve and comply with the best work organizational and efficiency standards, by pursuing a clear long-term policy of investing in the quality of its personnel, and by supporting actions that contribute to maintaining fruitful inter-institutional cooperation.

In addition, I want to thank the organizers for giving me the honor to speak in front of you today, regarding a topic that has become so relevant in the last year, following this unprecedented international financial crisis. Given the fact that the causes and consequences of this crisis have been broadly identified and discussed, in the first part of my speech I will focus more on the main findings of the professional discussion that is taking place nowadays to identify a new financial supervision approach. I am sure you will elaborate on these issues further during this Conference. In the second part of my speech, I will try to give you more detailed information on how we at the Bank of Albania are thinking about the future approach of the public authorities and of the financial industry, in relation to necessary measures to strengthen financial stability.

Very shortly I want to reiterate what has now become clear to many: the recent crisis was a consequence of wrong incentives which supported unbalanced financial activity development and misconception of risk assessment, pricing and management. Such wrong incentives were present not only to the financial industry and markets, but also to the balance sheet of households, businesses and entire countries. Given the nature, the size and the impact of this crisis, not only to the financial industry and markets but also to the real economy, public authorities in many countries were forced to adopt swift, coordinated and extraordinary measures, both in the area of monetary and fiscal policies. Central banks abandoned almost any restriction and even adopted unconventional measures in providing ample and low-cost liquidity to the financial markets. Governments showed a strong commitment...
to reduce systemic risk by saving important financial institutions, by providing guarantees for inter-bank lending, by raising the level of deposit guarantees for the public etc. Such measures, most of the times designed as temporary, appear to have been successful in restoring the market confidence and steering the world economy back in the gradual recovery path.

Focusing on the financial markets and institutions in the aftermath of the crisis, a number of issues, previously known but many times neglected, have re-appeared forcefully to request a serious and thorough response by the authorities. Many of these issues relate to the financial activity itself, others are connected more with the surrounding economic environment.

It can be said now that the supervisory authorities of the financial markets and institutions are partly responsible for what happened. Despite the rhetoric, they failed to properly and timely identify and control the risk in the financial industry. Here one can mention the soft-hand on bank wholesale borrowing that financed the foreign currency credit in a certain jurisdiction, the neglect for the special purpose entities that were created to by-pass balance sheet prudential requirements etc.. There are many reasons for this weakness and a number of them, in my opinion, go beyond the legal and resource capabilities of the supervisory authorities to act. On their own, the supervisory authorities were wrong in basing their work on the misconception that strong individual financial institutions are sufficient for the entire financial system stability. By doing so, they missed the negative effects and excesses that arise from the herd behavior of the financial institutions, many times a consequence of the pro-cyclicality that is inherent in the financial activity and the regulatory framework itself. The attention of the supervision was focused on the banking sector, but insufficient attention was given to its interaction with the non-banking financial sector, that by being much less regulated, in the meantime was increasing in size and importance. Also, as part of their general and commendable goal to focus their supervisory approach on the most important risk sources of the financial industry, but also as a sign of their objective difficulty to keep the pace with the financial markets developments and innovations, the supervisory authorities relied more and more on the market discipline and on the sophisticated and unclear risk models of the financial industry, that also proved to be deficient. Some times, the structure of the supervisory authorities has proven to be fragmented or too complicated, giving rise to regulatory arbitrage by the market players. Other times, the resources needed to effectively perform the supervisory role have been limited, negatively affecting the supervisor’s performance.

But this crisis showed that risk came also from other sources, out of the direct control of the supervisory authorities in a given jurisdiction. For example, the increasing asset prices were fueled by ample liquidity and credit conditions, which were often affected by international developments and financial flows. The borrowing in the international markets by the financial institutions was also affected by increasing fiscal and current accounts deficits, arising due to wrong policies that created imbalances in the saving-consumption behavior of most important economic players in the economy, including the households.
It is now a question, whether some of these issues could be addressed by a more powerful role of the monetary policy. Financial integration, among other things, has also contributed in the rapid expansion of the financial activity, and many financial institutions have become too big for a single country. This has occurred at a time when, for the same reason, the “de facto” power of regulation has shifted away from the local supervisors toward their host counterparties. Hence, despite a steady trend of convergence between financial legislation in many countries, there are still marked differences that, particularly at a crisis situation, create strong tensions between public authorities in different countries.

A very strong effort by the public authorities in the world to address the abovementioned issues in order to improve the supervisory standards and superstructure is now underway. Both in the United States of America and in the European Union, the creation of special institutions is being envisaged, whose role will be to identify and control systemic risk through a different supervisory approach for financial institutions with systemic importance. At the same time, such financial institutions are expected to become subject of a more stringent regulatory framework in terms of capital and liquidity requirements, balance sheet composition and expansion, and governance relationships. Revising the liquidation procedures for similar financial institutions with cross-border presence is another area that will confront the public authorities in the world with a stronger challenge.

The main purpose of the reform of the financial regulatory framework will be to accommodate new incentives that will create a stronger environment for risk management in the financial industry. The main principle here is “prevention is the better cure”. In this regard, the perimeter of the supervision regulatory framework will be extended to include other important non-bank financial institutions and probably the bank holding companies. At the same time, the approach in the regulatory framework is expected to feature more automatic requirements (and less discretionary ones), as it tries to move toward more simplicity and clarity. The move toward simplicity and clarity, will certainly reduce manipulability and enhance transparency and credibility of the banking and financial activity. These changes will be complemented by similar ones in the area of customer protection and market transparency. The regulatory framework of the financial industry is also expected to be less pro-cyclical, as new interesting proposals are being identified to adopt a countercyclical approach for capital requirements, provisioning and accounting. Ensuring responsible governance for the banking and financial institutions is going to be another area of developments. New regulatory requirements and instruments to seek more involvement and higher responsibility of boards of directors for risk management and discourage uncontrolled risk undertaking are being identified. On the other hand, the supervisory authorities will need to strengthen their macro-prudential risk assessment capacities, by focusing more on systemic behaviors of the financial institutions. The central bank is expected to take a larger responsibility in this area, particularly in those countries where it did not use to have a strong supervisory role. Whatever the approach in this direction, the supervisors will need stronger legal powers...
which will ensure their ability to act in a timely and flexible way. As mentioned also above, procedures for managing distressed financial institutions and for crisis management will need to be revised to ensure stronger and more effective inter-institutional and cross-border cooperation, and in general to better address the potential conflict between ex-ante supervision and ex-post intervention.

This important process of financial regulatory reform is not without risks. I believe that the public authorities will pay particular attention to control the tendency for over-regulation, and to avoid a “blind” adoption of the regulatory changes as well as asymmetric/unilateral approach. Regulating more should mean regulating better. Undertaking risks is a natural thing for the financial industry in their valuable role of financial intermediation. Such undertaking of risk, when well identified and properly managed, is useful for increasing efficiency and returns of the activity, two important elements for a viable and solid on-going financial performance. Every country should certainly follow with particular attention the discussion and the changes that are being proposed for the financial regulatory reform, as this process will affect them for sure. In this regard, it is important for the public authorities to start a process that would analyze and assess the impact in their financial industry of the expected and well identified proposed changes. Clearly, the practical adoption of the proposed changes should be driven by the goal for achieving a higher convergence with international standards, but it should be determined by the characteristics of the national or regional financial system, and their development goals. In addition, focusing only at better regulating the financial industry, without addressing other important and probably unsustainable economic developments, is an asymmetric approach that will not deal properly with the risks to financial stability. In this regard, governments, businesses and households, should identify measures and adopt actions to reduce imbalances in their own balance sheets, as this will, on the other side, improve the quality of the financial industry and reduce risk.

Dear participants,

Let me now focus more on how the Albanian economy and our financial system was challenged by the international crisis, and what are some of the future measures the Bank of Albania believes are important to strengthen the stability of the financial system and of our economy.

The recent international crisis showed that at the time of continuing financial integration and economic globalization, small economies like Albania’s or other countries’ in the region, should not count only on some natural protection coming from less developed financial markets and a much lower level of indebtedness from the households and businesses, to compensate over time for potential risks coming from less diversified economic growth, overreliance in remittances, insufficient culture of risk management in financial institutions and other economic agents - in particular for the exchange rate and liquidity risk, and very limited space from the public authorities to introduce anti-crisis financial measures similar to those in the developed countries. Hence,
policy measures should address these and other deficiencies to find a proper solution in the medium-term. Such measures should reflect the preference for preventive approaches.

In fact, over the last 4 to 5 years the Bank of Albania was vigilant over time to point out areas of the banking activity that required attention from the industry. We have expressed our concern regarding the rapid increase in lending, as we believed that this could negatively affect the credit quality. The composition of the loan portfolio, which is dominated by the euro-denominated loans, has also been identified as a point of concern. Despite the fact that this position is supported by a strong presence of foreign currency denominated liabilities in banks balance sheets and very close economic links to Euro-area countries like Italy and Greece, Bank of Albania has been consistent in its approach to introduce gradually regulatory measures that would discourage rapid increase in lending, encourage banks to lend more in domestic currency and increase transparency toward clients on banks products and services. On the other side, the monetary policy has successfully anchored expectations of very moderate growth in the price level and has supported demand for local currency financial assets by offering sufficient positive real return.

As the crisis hit, the first impact in our economy was shown on the balance of payments, reflecting the relationships of our economy with the world. The increase of unemployment and the tightening of financing conditions in the neighboring countries of European Union were followed by the decline of Albanian emigrants’ remittances that live and work in those countries. While the gap between the domestic and external demand was widened, this was accompanied with an increase of current account deficit and the mounting pressure on the exchange rate. At the same time, the banking sector, which heavily dominates the financial system in Albania, reduced its funding contribution to the domestic economy as a response to the increasing demand for liquidity, following the deposit withdrawal from the public and an increasing borrowing demand from the Government. The combined effect of these developments affected negatively the real sector of the economy, mainly the business sector. In the first quarter of this year, business confidence index fell under its historic average, reflecting a more difficult financial situation. The latter was also shown by the lower-than-planned realization of fiscal revenues as well as by the decline of loan portfolio quality that banking sector has encountered throughout the period.

In the short-term, the public authorities took measures to lessen the impact of the global financial crisis in the economy. Through the significant increase of the fiscal expenditures share designated for investments, mainly in infrastructure, the government supplied an important impetus for the support of the real sector of economy to cope with the global crisis effects. The Bank of Albania has also been active to provide liquidity in the interbank market, with the aim to preserve the stability of the banking sector and to lessen the expected decrease of its intermediation role. We removed quantitative limits in the size of the liquidity injections through our week-long reverse repurchase agreements, and extended the maturity of our injection operations up to three
months. Following a cut of the policy rate by 0.5 percentage points in January and the subdued inflationary pressures at home, the monetary policy paid an important attention to the financial stability, by keeping the policy interest rate unchanged throughout the period[1]. Through this policy, we intended to maintain strong incentives that would support the public demand for financial assets denominated in the national currency, in the short term. At the same time, along with the Ministry of Finance, the Bank of Albania initiated legislative changes to increase the deposit insurance level, as a necessary measure to restore the public confidence for the safety of their banking deposits. From the supervision point of view, the Bank of Albania established a stronger day-to-day monitoring of the banking sector developments, focusing particularly in the liquidity situation. This was part of a broader approach that included also changes in the regulatory framework, better analysis through improving stress-test methodologies, stronger communication with the banking sector, increasing number of publications and more presence in the media. We believe that such policies were important for the effective management of the banking sector liquidity needs, provided an orientation of lending in national currency and maintained strong capitalization parameters for our banks. The situation entered into a qualitative improvement phase after the return of public deposits growth in the banking sector. This process, which was developed gradually and in a stable way in the second quarter of 2009, continues with a steady pace.

We believe that, after coping with the short-term effects of the international financial crisis and following the improvement of the international economic situation, it is the time for the public authorities at home to initiate a process of assessment for the legal and financial operations framework, with the goal to re-establish appropriate balances in the fiscal, monetary and banking activity, to further sustain a stable economic growth and maintain financial stability. In this regard we consider important for the fiscal policy to take respective correcting measures in order to keep the confidence of the resident and non-resident market agents and investors. At the same time, the monetary policy should assess the possible effects on inflation of the financial incentives it provided to the banking sector and to the economy, and later analyze the possibilities to support the financial intermediation of the banking sector in the economy at a lower cost. To provide a longer-term response to the stable economic growth, public authorities should insist on the compilation and implementation of the strategies for future economic development, which in a medium term shall provide for:

a) the establishment of a better balance on the contribution that different sectors give for the economic growth. In this regard, it is important to increase the support for economic sectors with strong growth potential, like agriculture and tourism;

b) the increase of our economy’s competitiveness and its further formalization. In this regard, the debate should focus on finding the incentives to increase the domestic production and support domestic savings. Over the time these would improve our current account balance, and improve the availability of our foreign currency assets;
c) the expansion of the economic agents’ funding sources. In this regard the authorities should implement policies that support the development of the non-banking financial sector and that sustain the establishment of capital and debt market for private entities. The accomplishment of these targets shall firstly require the strengthening of the financial reporting standards; the completion and improvement of the legal framework for the developments of business relationships and the improvements in the protection of creditors and consumer rights, regarding the financial institutions and products. In more practical terms, these measures are expected to improve the availability of the funding sources for the economic growth, and gradually decrease its dependence from the banking sector;

d) the improvement and the completion of the legal and operational framework to strengthen the crisis management capacities of the public authorities. In this regard, the authorities should identify the necessary measures for the prevention, the treatment and the elimination of financial crisis consequences. Bank of Albania believes it is important that each public authority carry out an assessment of its legal, financial, human and technological capabilities, to perform its role in the crisis-prone situations. Needless to say, throughout this process, the coordination among the public authorities should be at the highest level.

The banking industry itself is required to carry out a process of reassessment of its development objectives and models for the future, so as to ensure consistent and stable profits. In this regard, the managing structures of the banks are expected to undertake a process with the purpose of: a) re-assessing the development priorities; b) establishing a better balance regarding income sources and focus on cost control; c) enabling a higher specialization of their business and identify competitive priorities; d) achieving a better balance regarding the composition of their assets and liabilities according to the currency, maturity structure, etc.; e) implementing more active policies to approach and maintain the public (customers) close to the institution; f) strengthening the internal audit structure and risks management and research capacities.

Bank of Albania is now working with the goal that, within the needed time frame and after properly consulting with the financial industry, to support this process through the introduction of changes in the regulatory and supervisory framework. With this in mind, we shall aim at strengthening the internal mechanisms of the banking activity that incentivize its more controlled and balanced expansion, with adequate characteristics of liquidity and capitalization. At the same time, Bank of Albania shall assess the need for a new supervisory approach for the banks with systematic importance. The transparency of banking activity in its relationships with customers and public in general, shall remain at the centre of our supervisory activity. In general, in this process the Bank of Albania, shall consider the alternations that shall occur in the European standards, by supporting the strong collaboration with other central banks and supervisory authorities.
In conclusion, let me point out that the ultimate goal of the new financial regulatory changes that is being identified in the international level is to provide the right incentives, which over time will ensure a more balanced, risk-averse and stable financial markets and institutions activity in the future. On a global and national level, such changes should be complemented by other more general economic measures that should enable an adjustment process to ensure a better alignment of asset and liabilities in the balance sheets of the various economic agents. All this should be achieved, as we still want the social benefits of economic and financial integration. This means the path ahead will witness a continuous and challenging effort to find and strike a new and more appropriate balance between risk appetite and more stable returns by the economic agents, and between short-term national concerns and long-term regional economic and political integration objectives.

Once again, I wish to the Central Bank of the Republic of Kosovo, to its management and staff, a successful future!

Thank you for your attention!
SPÆECH BY THE GOVERNOR OF THE BANK OF ALBANIA, MR. ARDIAN FULLANI
At the Bank of Albania’s forum with representatives of main businesses operating in Albania
23.11.2009

Dear Ladies and Gentlemen,

It is my pleasure to be among you today, to share with you our views on the current performance and development prospects of the Albanian economy. As the most dynamic part of the Albanian economy, your contribution has been tangible in the country’s economic development during transition. Your incentive, your willingness and devotion have brought about tangible results in the country’s development. In a single figure, the Albanian economy performance may be summarized in the growth of above 65 percent of gross domestic product and well-being per citizen during these years of transition. Our development prospect remains as much positive. The country’s macroeconomic stability, the continuation and deepening of structural reforms as well as the geopolitical reality of approximation to developed economies of the European Union, would help in a fuller release and remuneration of your potential and energies.

Today’s forum aims to highlight the economic development of the country and initiate a broad public discussion on alternatives of the future economic growth models.

Now, let me start by making a brief statement of the latest developments of the Albanian economy, and further dwell upon our viewpoints on the country’s economic development in the future.

ECONOMY PERFORMANCE DURING THE CRISIS

The developments over 2009 have indicated that the Albanian economy has been impacted by the recent global crisis, mainly as a consequence of decreased foreign demand and remittances, higher risk premiums, reduced and high-cost financing resources. However, our economy continued to record positive economic growth rate during this period, while the domestic inflationary pressures remain subdued. The country’s economic activity has been sustained by the fiscal stimulus and the preservation of steady consumer demand, while investments and exports have recorded lower growth rate in the first nine-month period of the year.

The economic performance over the first 9-month period of the year, albeit positive, attests to growth rate slowdown, reflected even in the gradual slackening of inflationary pressures. In spite of a slight improvement during 2009, the current-account deficit remains high, reflecting high levels of
consumption in the Albanian economy and unfeasibility of production capacities to meet it. The fiscal policy has had an expansionary nature during 2009, reflected mainly in increased budget spending, mainly due to rapid growth of capital expenditures. Budget revenues maintained a slower-than-projected rate, due to slow-down in the economic growth rate during this period.

Consequently, the additional budget spending has been financed through the use of privatization receipts and the higher public borrowing.

This policy has exerted pressure over the increase of government debt securities’ interest rates of long-term maturity. Financial markets attested to an improved liquidity situation and agent’s recovered confidence in these markets. The persistent Bank of Albania’s liquidity supply to the money market helped to calm the market participants down and supply the market with funds, which served to the private sector’s domestic currency intermediation. The needs for liquidity in the interbank market have decreased, hence exerting no pressure on short-term interest rates.

The prudent monetary policy of the Bank of Albania has helped relieve the tension in the financial market, while the latest base interest rate cut should be translated into greater lending to the private sector.

As we have already stated even previously, the Bank of Albania regards the future Albanian economic activity with a prudent optimism. I mean, in spite of the great shock we have gone through, the macroeconomic and financial stability of the country has not been affected. Furthermore, the restoring of confidence in the banking system opens the way to recovery of the lending process and sustaining of the economy with funds. On the other hand, the Bank of Albania keeps on pursuing a prudent stance, because the financial risks on the economy have not been completely overcome. The banking system has still liquidity shortages, whereas the global economy continues to be frail. Therefore, the economic prospect will depend on our joint work and on the performance of global economic and financial markets.

Dear participants,

In the optics of historical developments and particularly of recent events, I would like to briefly dwell upon several vulnerabilities that we, as the politico-supervisory and regulatory authority, have highlighted, as well as the lessons we should draw and the issues we should address for the country’s further economic development.

LESSONS FROM THE CRISIS

Right from the beginning, I would like to emphasize that generally, the philosophy of the country’s economic development has been accurate. Market openness and increased competition have made the Albanian economy benefit the fruits of private sector initiatives. The practice of economies based
on free market principles has broadly indicated that this sector remains the most efficient engine of the economic activity.

This process has been sustained even by the constant reduction of the state’s share to the economy, as well as by its focus on procurement of public goods and infrastructure development. Positive financial market development has generated the necessary funds for supporting investments and consumption in the economy. Though chiefly for historical reasons, our banking system has based its activity on the intermediation of domestic funds of the economy, the recent developments indicated that it remains as much capable in generating foreign funds to provide capital and liquidity backstop to the Albanian economy. On the other hand, the integration of our financial system into the European one has raised the resilience of the Albanian economy to various shocks, of which the latest is still under operation. It has also brought about a necessary expertise in terms of financial and economic business administration, has developed the infrastructure and means of payments in the economy and has helped efficient risk transfer in the economy.

In spite of accomplishments, I think the country’s growth model needs modifications and improvements, aiming at enhancing its efficiency and stability. Under the conditions of an economy that requires dynamism for moving from a transition economy to an emerging one, the commitment for a sustainable and long-term development should be the subject of current and future economic reforms, at both, political and institutional level, and enterprise and consumer level.

WHICH ARE THE VULNERABILITIES NOTICED IN THIS REGARD?

First, domestic consumption and investments have been the main beneficiaries, while the Albanian economy has not yet succeeded in establishing a competitive export sector, capable of generating steady foreign currency income, which would enable the preservation of external economic balances. From another viewpoint, this development does not seem as balanced in sectoral terms. So, some sectors such as trade, construction and services have contributed disproportionally the country’s development while others, such as agriculture and industry have contributed less.

Second, Albanian economy continues to suffer from structural vulnerabilities, which contract its competitiveness in international markets of products and capital. This behaviour is illustrated even by international competitiveness indices compiled recently by the World Economic Forum, where Albania is ranked below regional countries. Some acute problems refer to the need for enhancing education and infrastructure, in all dimensions. Both these problems restrain the attraction of foreign investments and impede the country’s development.

Third, efficiency in using the economy funds should be improved even at micro level. This implies the need for improving private businesses’ management and control systems, enhancing analytic and forecasting capabilities, as well as transparency.
Allow me to further deal with some of the above-mentioned issues.

**STABLE ECONOMIC DEVELOPMENT OF THE COUNTRY**

As we have continuously underlined in our periodical reports, the economic growth over the recent years has been strongly supported by the banking system lending. The growth of banking lending has provided an impulse of about 7 percentage points of GDP in the last five years, making a pronounced and evident contribution to the growth of consumption and investments in economy. Their growth has provided room for expanding the production basis and improving the welfare. However, it has also generated macro and microeconomic imbalances.

At macroeconomic level, the high consumption and investments were followed by increasing inflationary pressures and higher trade and current account deficit. These signs of overheating were clear signals that that level of consumption could not be kept for a long time, hence calling for controlling measures by the monetary authority.

This is also the key to understand our prudent monetary policy during the period 2006-2008. The institutional investment we have made during these years in terms of consolidating macroeconomic and financial stability was rewarded with a much more moderate and milder impact of the global crisis than in the regional countries. In concordance with the modern philosophy of macroeconomic administration, the Bank of Albania remains committed to not allowing that rapid and short-term economic growth impair the long-term development perspectives of our country. At microeconomic level, the growth of consumption in economy was followed by increased indebtedness in Albanian households’ and businesses’ balance sheets and by over-investments in certain sectors of the economy. Both these indicators are either at lower levels than in the regional countries, or at similar levels; hence, they cannot be specified as problematic. However, their rapid growth rate creates the idea of a short-term vision of the economic agents, and in particular cases, even avoidance of rationality.

Dwelling upon household consumption, the Bank of Albania invites all economic agents to be more forward-looking and realistic in their consumption and savings plans. This invitation does not imply the contraction of consumption or the change of preferences related to it, but merely placing it in the context of long-term plans that equal income and expenditure at a household level. Beyond the time-related dimension, as we have continuously drawn the attention, borrowers should be cautious as regards their loan currency. This implies that the matching of their loan currency with that of their income would be their best protection. In a more pragmatic approach, this advice may be reduced into an appeal for a close consultation with the banking system and the financial market’s specialized agents.

The latest global crisis – in particular in the US and England – showed that the impaired households’ balances sheets create room for strong economic
shocks and condition the country’s long term growth. On the other hand, it showed that the countries that succeeded in preserving a clear certificate of consumer’s financial soundness, wherein Albania is part of, had a more moderate impact and enjoy good premises for a more rapid growth. In a philosophical approach, the key lesson of the market economy is that all consumption must be paid for. There is no free lunch.

Back to businesses and investment loans, whose portfolio is 2/3 of the total banking system credit, my message is the same in principle: expand the time span of your decision-making and foreign investment and base them on detailed and scrutinized business plans’ analysis. What I would like to underline is that this message should be perceived by you urgently, since you have the necessary financial and human resources to be more prudent in borrowing and investments. Time is ripe for the Albanian businesses to avoid the group behaviour, where one business idea is almost automatically followed and adopted by other businesses, without first studying the market size, the competitive advantages, the level of expertise or the financial efficiency of using the funds, according to all the chains a careful and prudent decision-making should go through.

The latest tendency for diversifying the Albanian businesses is useful in principle; however, it should not be made to the detriment of specialization and efficiency, or even less without first making the macroeconomic and sectoral analyses.

The inter-sectoral performance of the economy is another issue I would like to discuss with you today and which I briefly mentioned earlier in my speech. The country’s economic development has been characterized by a growth and investment model which has favoured the services and construction businesses, compared to the exporting industries or the competitive ones in imports. Although this performance somehow reflects the tendency to perform similarly to the economic structure of developed and advanced economies, it has resulted in over-investments in certain sectors. The economy development cannot be stable if the allocation of funds is not carried out by adhering to the principle of sector productivity and efficiency. The misuse of financial funds impairs the agents and the whole economy, providing severe and long-term consequences on corporate balances sheets and debts, on labour market and on capital and technology allocation among sectors of the economy.

To minimize such risks, the Bank of Albania advises you to discontinue the inertial moves in your behaviour and realistically assess the regional and European context in your choices. The competitive advantages of Albania should not be sought only in natural resources, or in meeting of yet unserved demands of the Albanian market, but also in the cheap work force of the country and in its position as a future EU member. The increasing interaction with the banking system would help to clarify your plans and reduce the financial risk, providing you with the opportunity to focus on business risk administration you are specialized in.
Completing my discussion related to stable development of the country, I would like to underline that the banking system can and should do more in this respect.

The financial system is the brain of a market economy; it determines the expected return and risk of investments in the economy, enabling later on the prioritized use of limited financial funds. Despite its good performance, the Albanian banking system should do more to incorporate macroeconomic and sectoral analyses, and also the country’s financial stability in decision-making. The development of research units within large banks is actually a requirement of the time we are living in. Moreover, more efforts should be made, to increase the support of small and medium-sized enterprises with funds. In addition, a more aggressive marketing of derivative instruments, which will lower the corporate financial risk, particularly of those operating in the export sector, requires a greater attention from the banking system.

What I just mentioned will be an important part of the future philosophy of the Bank of Albania in the field of structural reforms in the financial market and in developing and advancing its supervisory and regulatory function in it.

STRUCTURAL VULNERABILITIES AND THE NEED FOR REFORM

A useful lesson that the Bank of Albania has learnt from the crisis is the need to continue and deepen the structural reforms in the economy. These reforms, not only will create a more appropriate environment for promoting the private entrepreneurship, but will also increase the economy’s resilience to shocks. They also help to absorb foreign direct investments, which are the best support to the country’s development in the medium and long run. However, as stipulated even in the EBRD’s report, Albania is among the few countries that have continued structural reforms even during 2009.

In this regard, Albania has lagged behind the regional countries, attracting in total only about USD 1100 per capita of FDI during the 20 years of transitions.

In the entire broad framework of reform-related problems, I would like to dwell today upon the need for investments in education and infrastructure. A well-known business maxim is that: Employees are a company’s most precious asset. To the Bank of Albania it signifies that the higher the professionalism, the higher our institutional independence.

To a broader sense, this is also relevant for the national economy. Our country’s progress, the convergence with the developed countries of East Europe and even beyond, with the European Union countries, will depend on our level of education. Competition in national and international markets is above all based on the generation of ideas and their use in the final products. Referring again to the Global Competitiveness Index, Albania is ranked the 90th as regards the level of education and high-level training, and only the
109th and 126th respectively at the level of business sophistication and innovation. These vulnerabilities will ever-increasingly become an obstacle for the country’s economic growth in the future, unless addressed on due time.

Public reform in the education system and the need for more backup funds should be a priority of every development policy. On the other hand, I consider that the Albanian business can and should do more for supporting the Albanian education. First, the business can and should be more supportive to higher education institutions, at the same time cooperating with them in the area of market research and student training. The economic development history shows that the countries, which have invested in education, are currently in the group of most developed countries of the global economy. Second, I think that more efforts should be made in attracting and absorbing the brain in the administration and management of your businesses.

Investing in education, in enhancing professionalism and expertise, is the best investment we can make for the future of our country.

Parallel to this, the enhancement of our development infrastructure should be a priority issue. Beyond the road infrastructure development, which rightly is a priority of the public sector, the Albanian business can and should do more in this regard. The use of common business resources to resolve problems in supplying electricity, water and sanitation, and local roads, should be regarded as an effective option of overcoming these problems. Creating differentiated and specialized development areas will open more opportunities to them to benefit from scale economies and common solution of problems. Also, computer and telecommunication infrastructure are sectors, which can and should be addressed more efficiently by the private sector.

**BUSINESS ADMINISTRATION AND TRANSPARENCY**

Though I addressed some problems even earlier in my speech, now I would like to dwell briefly upon the problem of administration and corporate transparency enhancement.

Corporate administration is the linking bridge between ideas and results. It affects funds usage efficiency and differentiates profitable from non-profitable businesses.

In light of this, I think that the above-mentioned issues, the extended time span of investments, their support in market researches and prudent business-plans, the orientation of businesses’ positioning in national, regional and global context, the increase in specialization and professionalization, the fostering of cooperation with the financial system, require ongoing investments in terms of your management.

Finally, I think that transparency of your businesses is an aspect that deserves a greater attention. Its enhancement would help first of all the trading and financial transactions among businesses, fostering confidence and decreasing
their risk. Also, the long-term and ongoing relation with the financial system is conditioned by reciprocal transparency between parties. Beyond the banking system relations, transparency is a serious obstacle in the establishment and operation of capital market in Albania. In this regard, I think that the Albanian business should be aware of the fact that transparency enhancement and increased formalization are in its long-term interest.

Dear participants,

Long-term visions are translated into success achieved through work and short-term sacrifices. The Bank of Albania invites you to foster the cooperation in resolving these problems of mutual interest.

Thank you!
SPEECH BY THE GOVERNOR OF THE BANK OF ALBANIA, MR. ARDIAN FULLANI
At the Press Conference on the Decision of the Supervisory Council of the Bank of Albania
25 November 2009

In its meeting of November 25, 2009, The Supervisory Council of the Bank of Albania analysed “The Monetary Policy Report for November 2009”. After becoming acquainted with the latest economic and financial developments at home, and following the discussions related to their expected performance in the future, the Supervisory Council of the Bank of Albania decided to keep the key interest rate unchanged, at 5.25 percent. The Supervisory Council assessed that this interest rate is in line with Bank of Albania’s goal to keep inflation close to the target over the medium run.

Economic and monetary developments over the latest months are featured by low inflationary pressures. Annual consumer-price inflation for October recorded 2.3 percent, being almost in line with its performance over the last quarter. The steady and low inflation rate has been conditioned by moderate pressures from domestic economy, due to:

- Economic activity slowdown during this period;
- Low exchange rate pass-through of exchange rate depreciation on Lek prices of import goods; and
- Stabilized inflationary expectations.

Easing of monetary conditions by the Bank of Albania, through key interest rate cut in October and continuation of liquidity injecting operations have provided appropriate impulses for promoting the economic activity in the future. These impulses, as always, are administered under the conditions of an expected inflation performance close to the three-percent target of the Bank of Albania, and stabilized expectations of economic agents for it. The key interest rate cut by 0.5 percentage point by the Bank of Albania at end-October aimed at strengthening the domestic demand and reviving the lending activity. Its effect on the economy is not fully reflected yet, due to the short period of time and the time lags in transmitting the monetary policy. However, its pass-through to the money market, which constitutes the first link in the transmission chain, is a premise for its reflection to credit cost in a second round. In the meantime, our liquidity injecting operations have been successful in guaranteeing the backup of economy with funds, mainly short-term ones.

Allow me to make a more detailed description of the economic and monetary developments during this period.

At global level, the economic activity has been supported by improved overall economic climate, impacting on the improvement of the global economic
activity, reduction of risk premiums and stability of global financial markets. However, the global economy and the European one continue to reflect economic vulnerabilities, which are transmitted to low inflationary pressures. This situation conditions also the pursuit of a stimulating monetary and fiscal policy by keeping interest rates at the historical low and by high liquidity injections.

Back to the domestic economy, we should state that the new economic data were insufficient during October. Performance of inflation and of monetary and fiscal indicators, external trade data and consumer and business indices confirm that the Albanian economy continues to record positive growth rates. This growth is sustained by maintaining steady levels of the consumer demand and fiscal stimulus given during 2009. However, available data from the economy speak for an economic activity slowdown during the current year. Foreign demand for Albanian products has decreased, being illustrated by export slowdown along this period, while investments have declined.

The steady trend of core inflation and low non-traded inflation rate also indicate the presence of low aggregate demand-induced inflationary pressures in the country’s economy during January-October 2009. This performance has contributed to absorption of shocks generated from traded inflation, due to weakening of national currency’s position in the domestic foreign-exchange market.

Inflation during 2009 has fluctuated around the lower limit of the Bank of Albania’s target. Headline inflation in October was 2.3 percent, recording a slight rise in comparison to September, but resting below the record of the previous year. Average annual inflation recorded 2.1 percent, resting at the same level with that of September. Parallel to demand factors, inflation performance is influenced even from the development of several supply factors, such as slight downward trend in the labour cost per unit, reduced import and producer prices, statistical effect of administered prices, thus creating an overall environment with reduced inflationary pressures.

Fiscal policy during the third quarter of 2009 has revealed signs of mitigating its expansionary nature. Revenues have recorded a slight rise related to the previous months, while there is noticed a reduction in realised expenditure pace. In annual terms, during the first nine months of the year the budget revenues have recorded a growth of 6 percent, whereas the budget spending has increased by 22 percent. The budget deficit remains at comparably high historical levels, but within the budget limits reviewed lately.

To a great extent, this deficit reflects the high level of public capital expenditures during 2009. Public expenditures and fiscal policy have provided a tangible contribution to the maintaining of the economic activity along this period, but they have been associated with increased pressures over the money markets. The Bank of Albania considers that the fiscal policy should continue to be prudent towards these balances in the future, and should take into consideration the long-term fiscal stability while drafting and implementing mid-term and long-term budget plans.
External trade was featured by weakening in the trade volume during the first nine months of the year. However, trade exchanges value recorded during September is the highest recorded since 2009. After about three months of constant narrowing, the trade deficit enlarged during this month by about 9 percent in annual terms. Exports dropped by about 18 percent in annual terms, though the lek’s weak position vis-à-vis the Euro is a favourable factor for exports. Imports recorded positive growth rates for the first time since January of the current year. In annual terms, they grew approximately 1 percent, due to positive growth rate of consumer goods import, whereas import of intermediate goods and capital has declined.

Monetary indicators of September presented a slower performance of the banking system’s intermediating activity. In annual terms, broad money recorded a nominal growth of 2.8 percent in September, against 4.5 percent in August.

Foreign currency credit contraction and intermediation of the public sector credit by non-banking agents have influenced the slowdown of monetary indicators growth rate.

In September, loan portfolio of economy grew at lower rates than in the previous months. Annual credit growth rate decreased to 13.2 percent. The credit slowdown is totally a consequence of foreign currency credit tightening, while the ALL credit increased by 31 percent in annual terms. The major part of the new credit, around 85 percent of it, was absorbed by businesses and was used mainly for meeting the needs for liquidity, whereas credit for long-term investments decreased. Also, household loan portfolio growth decreased, chiefly due to consumer credit contraction. Housing loan to households continues to maintain positive growth rates, remaining at 5 percent in annual terms.

Domestic credit intermediation in ALL has raised the need for Bank of Albania’s presence by injecting liquidity. The banking system needs for liquidity have been met through open market operations of the Bank of Albania, preserving an appropriate time structure of this injection. Short-term interest rates in the interbank market have reflected decreased borrowing cost by the Bank of Albania and have been steady. Furthermore, the primary market was featured by agents’ response to loan pricing, reducing the T-bill yield. The 12-month yield, which serves as a reference rate in determining other costs, has decreased by 0.15 percentage points during November, down to 9.28 percent.

The supply for financing the government demand has been sufficient, without exerting upward pressures on interest rates. Interest rate performance of new deposits denominated in lek and in Euro has also been stable during September, enabling deposits return to the system. In the meantime, new ALL and Euro credit interest rates continue to carry over tightening lending policies by the banking system in general, and fluctuate around isolated preferential policies.
After discussions, the Supervisory Council agreed on keeping the key interest rate unchanged. This decision aims at further preservation and consolidation of macroeconomic balances, regarding the macroeconomic stability as an indispensable precondition for the long-term sustainable growth. It also guarantees appropriate monetary support for the economy during this stage of its development. In the future, the Bank of Albania is willing to operate in line with the actual and expected performance of economic indicators. The shifting to the downward side of inflationary risks balance and the consolidation of financial stability and inflationary expectations in the economy will be taken into consideration in Bank of Albania’s future decision-making.
Dear participants,

It is a very great pleasure for me to open the proceedings of this two-day workshop, entitled “Building Capacities for Policy Design and Implementation”, organised for the first time in Albania by the Bank of Albania, in co-operation with the Center of Excellence in Finance (CEF), Ljubljana, with support from the European Commission, European Central Bank, and International Monetary Fund. Welcoming you here in Tirana, allow me to express my gratitude for the excellent work done by the CEF in the course of these years, to the benefit of our region.

Since our Washington meeting last April, the effects of the global crisis increased their presence in our region; however, as I have already emphasised even earlier, they did not immediately concert to full blown economic and financial problems. The extension of crisis effects to the real economy, to the budgets of governments and to financial sectors of the region, was mitigated by sound macroeconomic policies pursued in the recent years and by the availability of International Monetary Fund funding on an unprecedented scale, in coordination with support from the European Commission and the EBRD.

Due to this intervention, and mostly due to prudential policies pursued by the central banks with regard to financial stability and financial supervision, the region prevented not only twin crises in our banking systems and foreign exchange markets, but also any kind of meltdown.

Nonetheless, this crisis has been a wake-up call. We agreed on this in our meeting last April, in Washington, among senior policy-makers from the region and from EU and IFIs.

Now that we have managed to prevent the crisis, we must start the evaluation of the collateral damage of our response to the crisis. In this respect, it is very important to assess not only the long run sustainability of our region’s equilibrium, but also the effectiveness of our short run response. It is crucial to plan and implement our future moves intelligently for its reversal in line with new normalities.

While we are not out of the woods yet, it is important to make sure that the past year’s fiscal appetite that characterised our region does not become part of this new normality. Actually, we need to do some deep thinking about aspects of our policy regimes – starting with the design of monetary policies,
continuing with the way they are anchored and the building of due capacities for a greater effectiveness of monetary policy in the future.

That is why we agreed to put in place today’s workshop, as part of a continuing process of reflection and reform.

In our discussions here in Tirana, we will begin with questions of policy design, which are fundamental to set the stage for the later topics we will come to. We have suggested in advance several questions that may help stimulate the discussion, covering some of the key questions that are certainly left in my mind, as a practitioner, after navigating through the crisis so far.

The issues of policy design include the questions how much room for manoeuvre there has been to use discretionary macro policy measures; how far fiscal policy in future should build up a buffer against macro-financial risks; how far national monetary and prudential regimes have been able to shield us from turbulence; and whether we now see a need to attract new kinds of capital flow – perhaps to change the growth model in the region.

This discussion of policy design will bring us to our second issue. It concerns the role of external anchors for monetary policy. One point of consensus in our Washington meeting was that we need to revisit some aspects of this anchoring process, and the way it interfaces with countries’ efforts to build up their own internal anchors over time.

There are several questions about the future role of external and internal anchors. They include some reflection whether there is a need for more co-ordination and synergy between our policy dialogues with the IMF and the Commission; how the Commission’s fiscal surveillance (through Economic and Fiscal Programmes, Pre-Accession Economic Programmes, Convergence Programmes) can be deepened and serve more as a commitment device; how far there are lessons to learn about monetary anchors and prudential coordination mechanisms for the EU accession of our region; and how we – including the external actors – can foster stronger domestic anchors in various forms, ranging from medium-term fiscal frameworks to more effective policy co-ordination mechanisms.

Finally, we will turn to the issue of capacity-building. This is a question on which we agreed, at this workshop, to already provide some operational input to the CEF as it develops its work programme in this area. There is a long lead-time in the effectiveness of capacity-building, although fortunately the CEF had already taken the initiative a few years ago to ramp up its contribution in areas such as financial stability and policy co-ordination, so it has a head-start.

In the field of capacity-building, we need to consider: what are the top priorities, and where are the gaps to be filled through initiatives in terms of training workshops, technical assistance, and cross-country exchanges of experience.
This will bring us to look carefully at the design and implementation of fiscal policy, among others, and the way policies come together through domestic co-ordination processes. And we also need to identify the needs in the areas of monetary and prudential policies, where the CEF’s member countries have urged it to continue expanding its activities.

This is a full agenda, and I am sure it will not be the last time we get together to exchange views on these issues.

I believe strongly that we stand to gain immeasurably from considering these challenges on a regional basis.

We can learn from each other’s experience; we can engage at times in a joint dialogue with the external actors in the region; and perhaps our political leaders can find some opportunities to launch reform initiatives in parallel — for example, in developing structural reforms to help promote a flow of new capital to, and within, this region.

In this spirit, I look forward to very fruitful discussions — now in Tirana and in the future!
SPEECH BY THE GOVERNOR OF THE BANK OF ALBANIA, MR. ARDIAN FULLANI
At the reception of the Albanian Association of Banks with bankers and representatives of banks operating in Albania
18.12.2009

On the occasion of 2009 year-end, the Albanian Association of Banks held a reception with bankers and representatives of banks operating in Albania. With invitation from the Albanian Association of Banks, the Governor of the Bank of Albania, Mr. Ardian Fullani, addressed a speech to the participants.

You will find below the speech held by the Governor of the Bank of Albania on this occasion.

Dear bank executive managers,
Dear colleagues and friends,

It is a pleasure to be here with you today, to celebrate the anniversary of the Albanian Association of Banks. It coincides with year-end and as such, it provides an additional reason to analyse the performance of the Albanian banking system over this year and the contribution of the Association in this regard.

In general, this period has had its ups and downs; however, it has witnessed a remarkable progress of the Albanian banking sector, which has become the main engine of our country’s economic growth.

Let me start by highlighting some of the main elements that show the progress of the Albanian banking sector over these years. The banking sector, which dominates the financial sector in Albania, has been moving from a sector with 3 banks, where all of them were state-owned and suffered various inefficiencies, into a sector that nowadays counts 16 banks, all in private hands, where the foreign capital dominates.

In the course of this time the banking sector has expanded its activity, accounting for 77% of the country’s GDP, has raised the number of branches, has increased its products to the public and has improved their quality, thus rendering a significant contribution to the country’s economic development. At the same time, the entrance of well-known European banking groups from Greece, Austria, Italy and France, has been associated with episodes of consolidation in the banking industry.

Higher standards have been adopted for a better governance of banks and for more transparent relationships with the public. During these years, the banking sector has been considerably profitable and has operated in compliance with the regulatory and supervisory framework in terms of capital and liquidity. The Board of Directors and shareholders have been prompt in
introducing the necessary measures to maintain a sound financial situation and support their banks’ expansion with additional capital. The supervisory work of the Bank of Albania has pursued and monitored the development of the banking sector along this time, in an effort to adopt the best international standards in the area.

But of course, nothing is absolute. The banking industry has been faced with a number of issues, many of which are part of our financial sector’s development phase towards its consolidation, towards the development of the economy and the society. We have been discussing these issues in many other occasions, but I could not help mentioning the importance of having good risk management frameworks, balanced expansion of activity, clear and transparent procedures, and many other issues.

However, I would like to reiterate the importance of a sole element that incorporates all of them: the good governance. For the management team of a bank, it means:

- Professionalism, or the ability to make the right business decisions after balancing the risks and benefits;
- Dedication, or the ability to instil a hard-working environment in the institution;
- Responsibility, or the ability to achieve the objectives in a qualitative manner;
- Vision, or the ability to adopt a long-term view in projecting your institutions performance; and
- Accountability, or the ability to establish an efficient system of controls and balances for the processes and structures at your institutions.

These elements, which are indispensable for the management philosophy, should be endorsed by the entire staff as its normal work culture. Certainly, we all agree that these issues should be further improved in our banking sector.

Dear friends,

During 2009, our banking sector faced a unique and challenging situation. The international financial and economic crisis affected considerably the public confidence in our banking sector. It showed how sensitive to financial shocks our social environment is. It also showed how important is to be prepared for the worse. Financial crises are the most difficult to be managed and their consequences need a long time to be absorbed.

Indeed, thanks to the liquidity of the banking sector, the support of the shareholders and the measures of the Bank of Albania, the banking sector has overcome the situation caused by deposit withdrawal at year-start. We have certainly left behind the short-term shock, but the skies are not yet clear. To manage the liquidity situation, you were forced to cut short on the lending supply. This has coincided with more pronounced difficulties in the real sector of the economy, which in turn, has affected the demand for credit. We are
now facing a deterioration of credit portfolio quality, which is going to weight on your financial result over the medium run.

The Bank of Albania acknowledges and supports the efforts of the banking sector to early recognize and quickly provision the non-performing loans. We urge you to keep exercising the necessary caution when assessing the credit quality. On the other hand, you must support your clients and continue lending to good borrowers, since this is beneficial to your clients, to you and to the whole economy. I will keep stressing this to you, because I do believe that there are real opportunities for you to do this in competitive terms, particularly for loans denominated in the national currency. The Bank of Albania will continue to provide the necessary support, by maintaining the liquidity flow, in order to satisfy your needs. Lending requires more work and analysis, not only off-site but also on site. It requires an in-depth knowledge and pursuit of the client and the market. But it is vital to bank balance sheets and to the country’s economic activity.

The international financial crisis impact on our banking sector should serve as a lesson we must learn for the future. As we have also mentioned in our recent publications, you should carry out a process of re-assessment of your development objectives and models for the future, so as to ensure a consistent, stable, and profitable activity.

Furthermore, you must develop policies and structures that improve your capacity to act under unusual circumstances and maintain “business as usual” for the most important areas. The Bank of Albania is now working with the goal to support this process, in due time and after proper consultations with you, by introducing changes to the regulatory and supervisory framework. With broader consideration, and following the changes to the supervisory standards at European level, we must work together to ensure a more balanced, risk-adverse and stable financial market and institutions’ activity in the future. I want to express my belief that the banking industry in Albania will be an active actor in meeting these objectives.

Let me now conclude with a sincere wish for a happy and successful New Year to you, your families and the institutions you manage! To the Association of Banks, I wish that the New Year represents yet another period of meaningful progress and achievements!

Thank you!
In its meeting of December 23, 2009, the Supervisory Council of the Bank of Albania analysed the Monthly Report of Monetary Policy. After dwelling upon the latest economic and financial developments of the country, their projections for the future and the expected balance of risks, at the end of discussions, the Supervisory Council of Bank of Albania decided to keep the base interest rate unchanged, at 5.25 percent.

Recent developments in the global economy have given positive signals for improvement in the economic activity performance. The main developed and developing countries have experienced an economic growth on a quarterly basis, while the world trade and confidence indices have shown improvement signs. The world economy is still far from full utilization of capacities, thus impacting on the maintaining of high unemployment rates. The limited capacity utilization rate impacts also on keeping inflationary pressures at low levels.

However, these pressures have lately been upward, due to optimistic news of oil and raw materials prices.

The latest data on the domestic economy performance indicate a slowdown in the economic activity. Unlike the first half of the year, when the economic growth was supported by the preservation of consumer demand and fiscal incentive provided over this period, the economic data for the third quarter and for the coming months indicate a more moderate pace of demand and production in the economy. This is evidenced by a number of indicators published in November, such as: the slow progress in retail sales index rise; data on external economy, which continue to be featured by decline in exports; performance of fiscal indicators, which seem to be below the projected level; and lending curbing, due to the decreased demand for it. The economy slowdown is also perceived by consumers and businesses, whose confidence indicators continue to be low. The future performance of the economy will significantly depend on the revival of consumer spending and investments in the country, the degree of their coverage from bank loans, foreign direct investments or any other form of long-term financing.

In general, the macroeconomic situation of the country has created an environment of weak inflationary pressures. Also, supply factors or those originating outside the Albanian economy have not produced strong inflationary pressures over this period.

Annual consumer price inflation recorded 2.8 per cent in November, close to the Bank of Albania’s target. Average annual inflation rate stood at 2.1 percent.
for the third consecutive month. Lack of pressure from domestic demand and low inflation rate in partner countries have balanced the pressures exerted by the domestic currency’s depreciation during 2009. This performance is manifested even by the steady performance of core inflation, whose low levels confirm the presence of a controlled inflationary environment.

Latest upward trend of consumer price inflation was an expected development for the Bank of Albania. It mostly reflects either the temporary or the technical factors, which, though operating for a short period of time, they do not comprise a persistent source of inflationary pressure.

The latest data on the external economy indicate trade deficit widening during the first nine months of 2009, recording a rise of 20 percent related to the previous year. In relative terms, the current deficit level accounts for 17.3 percent of GDP. On the other hand, foreign currency inflows to capital and financial account resulted 21 percent higher than in the previous year. Their share to GDP is estimated at 19.8 percent, making the country’s balance of payments turn out positive during the first three quarters of 2009. However, high and upward levels of current account deficit will require more quantities of foreign currency funds to finance it.

Therefore, long-term sustainability of the balance of payments requires a greater attention by policy makers, projecting also the political measures and structural reforms.

Short-term developments in foreign trade for October reflect a different performance compared to the first nine months of the year, showing correction attempts of the trends observed earlier. Country’s exports fell by about 9 percent in annual terms, while imports recorded an annual decline of 21.4 percent. In consequence, the trade deficit for the first ten months of the year contracted by 5 percent compared to the previous year, thus giving signals for its stable performance.

Fiscal policy continued to be expansionary during 2009, but this feature was diminishing during the second half of the year. The country’s economic activity slowdown is also reflected in the performance of fiscal indicators. Fiscal developments during the last two months were characterized by a smaller increase of budget revenues - only 4.5 percent in annual terms - mainly due to the declining contribution of VAT and profit tax revenues. Meanwhile, public expenditures continued to maintain high growth rates - by 16 percent. Most of the deficit is financed from foreign borrowing and privatizations receipts, without exerting any pressure on the domestic market.

Though the growth rates of the budget deficit have slowed down during the last two months and its level in late October was in line with the projected limit for this period, this deficit continues to be high compared to its historical levels.

The Bank of Albania deems that accomplishment of the medium-term fiscal target for reducing public debt (in relative terms) should guide the fiscal policy
over the coming periods. Its accomplishment will foster the public confidence in the country’s macroeconomic policies, will serve as a stable basis for the country’s macroeconomic stability, will reduce risk premiums in the economy and will create more breathing space to the private sector. This goal should be materialized into practice by pursuing prudent fiscal policies, always in line with the real economic developments.

Turning to monetary developments, the Bank of Albania deems that their overview for November is mixed. The pace of monetary supply growth has accelerated and interest rates have been falling, but credit to the economy has slowed down during this period. In November, the broad money increased by 5.6 percent in annual terms, reflecting the stabilization of banking system liquidity as a result of continuous return of deposits and improved foreign exchange position. Positive developments in deposits performance during the month and their time frame shifting towards time deposits confirm the tendency to restore confidence in the banking system.

Meanwhile, the lending activity of banks has slowed down, recording an annual growth of the loan portfolio by only 12 percent. Business credit has the major share to loan portfolio expansion, while consumer credit and mortgage loans are contracted.

Low levels of loan portfolio expansion reflect not only the liquidity constraints in the banking system, but also the decline, to a certain extent, of the demand for consumption and investment, as a consequence of weakening economic activity. The future credit performance will be an important determinant of the economic activity. The Bank of Albania deems that the banking system can and should make more efforts to transmit its easing monetary policy to a higher lending to the economy. Subject to fulfilling our mandate to control inflation, we are willing to help the banking system by taking the necessary measures to revive the lending market.

In this context, even during November, the Bank of Albania continued to fully meet the demand of the banking system for liquidity, through the repo instrument. Interbank market indicators attest to an increased trading volume, while interest rates have reflected a downward trend, following the base interest rate cut at the end of October. The base interest rate cut is also reflected in the primary market, when for the first time during 2009 the government securities yields have recorded a decline, for all maturity terms. The banking system has responded by reflecting it to Lek-denominated loan and deposit interest rates. The agents’ response to base interest rate cut is expected to be further conveyed to the credit and deposit market, keeping to time lags in monetary policy transmission.

Exchange rate performance continued its depreciating trend even during November, but at a slower pace. The Lek’s depreciation, which has been present throughout this year, is balanced by lower prices of imported goods, without comprising any material risk for exceeding the targeted inflation rate.
At the end of discussions on current and expected performance of economic developments, the Supervisory Council of Bank of Albania concluded that inflationary pressures are expected to be low in the medium run, being reflected in consumer price inflation around the lower limit of the Bank of Albania’s target. On the other hand, risks to price stability are currently estimated as relatively balanced. Restraining factors, such as the monetary supply slowdown, assessments regarding the slowdown of domestic demand and economic activity rates, low level of utilization of free capacities in the economy and low rates of price rise in the main partner countries, would balance the inflationary pressures deriving from the exchange rate and price rise in world markets.

The Supervisory Council decided to keep the base interest rate unchanged. This decision aims at preserving and further consolidating the macroeconomic balances, considering the macroeconomic stability as a necessary precondition for a sustainable and long-term growth. It also ensures the due monetary support to the economy during this stage of its development.

In the future, the Bank of Albania remains committed to operate in line with the actual and expected performance of the economic indicators. Aiming at curtailing the inflationary risks, the consolidation of financial stability and of inflationary expectations in the economy will be taken into consideration by the Bank of Albania’s decision-making.
DETERMINANTS OF NET INTEREST MARGIN IN THE ALBANIAN BANKING SYSTEM
Irini Kalluci

This material analyses the net interest margin as a measure of efficiency for the banks that operate in the Albanian banking system and the main focus is on the identification of factors that may affect this indicator. Net interest margin can be calculated as the proportion of net interest income to total assets or interest bearing assets. Nevertheless, a reduction of this indicator does not signal in all cases an improvement of efficiency. Under these circumstances, the study of factors that could bring about changes to the intermediation costs represents an interesting topic and broadly discussed by the foreign literature.

The banking system is the most important element of the Albanian financial system, whose assets account for 97 per cent of the financial system assets. For Albania, banks function as the main players in channelling funds from lenders to borrowers, therefore it is important that their intermediation role provides higher welfare for the society, possibly at lower costs. This study was inspired upon this context, aiming to identify the factors that impact the net interest margin for the Albanian banking system and wishing that it will contribute in the written literature dealing with this issue, since it represents the first attempt for the case of Albania.

Different stakeholders, but especially the policy-makers, are interested in the establishment and functioning of stabilized and efficient banking systems. Stability requires adequate profits, while the economic efficiency requires margins at acceptable levels, applied from banks. The results derived from the analysis of factors that impact the net interest margin may be useful for the compilation of specific measures of economic policies.

NET INTERNATIONAL RESERVES IN ALBANIA: LEVEL AND MEASUREMENT, A COMPARATIVE ANALYSIS WITH THE REGIONAL COUNTRIES
Olta Manjani

The purpose of this material is to make a general description of the international reserves held by the monetary authority. The strategy of the Bank of Albania in managing international reserves has foreseen a continuous growth of reserves in accordance with the main features of the Albanian
economy: a high and growing current account deficit, a fast growth of short-term foreign debt and a considerable shift of broad money to its foreign currency component. Given the features of the Albanian economy, the application of reserve adequacy criteria based on conventional benchmarks is useful in the case of Albania. Adequacy benchmark of reserves covering 3-4 months of imports, covering one or up to one year of short-term foreign debt or 5-20 percent of broad money are required to forerun potential risk factors that might impinge the Albanian economy. Despite being widely used, conventional criteria are highly credible and provide good basis for comparison between different countries.

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MEASURING INFLATION EXPECTATIONS*
Gent Hashorva
Elona Bollano
Elvana Troqe

This paper attempts to apply some approaches in order to quantify the responses collected via the Consumer Confidence Survey conducted by the Bank of Albania. Moreover, it attempts to better understand the nature of consumer inflation expectations in Albania. The paper is organized as follows: Section one analyzes the testing of expected inflation indicator in order to derive conclusions related to the nature of consumer inflation expectations. Section 2 describes the importance of expectations in the inflation control process and the method of their measurement. Section 3 continues with the methodology of data conversion from qualitative to quantitative, using a number of functions of the probability approach to quantification of inflation expectations. Section 4 applies the methodology and testing in the case of Albania. The last section provides some preliminary conclusions.

THE INTERNATIONAL FINANCIAL CRISIS AND THE REGIONAL COUNTRIES*
Eglent Kika
Erblin Maçi
Medvin Shehu

The purpose of this paper is to provide a retrospective of the crisis evolution from the developed to the developing world, the primary focus being some of the Central Eastern European Countries, some of the regional countries and Albania. Within this context, exceptional interest is paid to the manner the crisis is reflected in these countries’ real economic indicators as well as fiscal, monetary and respective institutional operational developments according to their quintessential economic profile.
ANALYSIS OF FINANCIAL INTERMEDIATION
Erjona Suljoti
Sofika Note

The purpose of this material is to analyze financial intermediation in Albania. The Albanian banking system consists of 16 universal private banks, dominated by foreign capital, which constitutes about 92 percent of the capital held by the banking system. Though a considerable number of banks have been present in Albania since 2000, the genuine intermediary activity of the banking system has been livened up in the last 4-5 years. In 2004 banking financial intermediation was characterized by the accumulation of economic agents’ savings and low mobilization of funds for lending, particularly to the private sector. In the meantime, public debt financing accounted for 55% of assets, witnessing a high mobilization of funds for the public sector. This composition of the banking system assets was a consequence of the blow geographic expansion of the banking system, higher credit risk, lower integration of the real sector with the banking system, as well as the regulatory and supervisory elements present at the time.

SURVEY RESULTS OF REMITTANCE – RECIPIENT HOUSEHOLDS (2008)
Godiva Rëmbeci

The following material provides information on the general characteristics of remittance recipient households, the characteristics of Albanian emigrants and of their remittances to Albania, based on the quarterly data obtained from the Bank of Albania surveys conducted in 2008. The survey results do not only provide a good source of information to complete and replace (in the future) the estimation of workers’ remittances in the balance of payments, but they may be also used by the analysts as time series to monitor, understand and forecast remittances.
DETERMINANTS OF ECONOMIC GROWTH IN ALBANIA

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INTRODUCTION

The aim of this article is to analyse the sources of economic growth in Albania after transition. Determining the fundamental sources of economic growth is important in order to evaluate the role they have played in the past and what is the possible perspective of their development in the future. Economic growth in Albania compared to other countries of Central and Eastern Europe after ‘90s is impressive. Hence, excluding Poland and Turkey, which have showed a stable economic growth after ‘91, Albania is the first country amid the considered countries which in 1999 (along with Hungary) exceeded the real GDP level of 1990. For the rest, the transition shock resulted fairly strong and the recovery of the economy in order to succeed the level of 1990, begun only after the year 2003. In the meantime Macedonia, Bulgaria and Leetonia have not reached the real GDP level they had in 1990.

Chart 2 shows a more detailed outlook of economic growth in Albania. During the beginning of transition 1990-1992, the real GDP in Albania dropped by cumulative percentage of 39%. The policies implemented during 1993 aiming the macroeconomic stability of the country, helped the stable...
economic recovery and growth. Between 1993 until 1996 the average annual growth pointed to 9.3%. The crisis of pyramid schemes during 1997 triggered an economic fall of 11%. Nevertheless, economy recovered rapidly and the growth rate of real GDP for 1998 pointed to 8.6 percent. This growth was higher for the ongoing years and was stabilised during 2001-2002, at an average rate of 6.5 percent. During the economic crisis of 2002, economy grew only by 4.3 percent. In the meantime, starting from 2003, the average annual growth pointed to 6 percent. After the annual growth rate of 7.85 % in 2008, the global financial crisis was reflected on the slowing down of the economic growth recording only 3.3 % in 2009.

Due to the inefficient structure of the economy that Albania inherited from the communist regime, the transition process led to restructuring of the economy’s composition. Starting from 1990 the share of the industry sector has dropped from 39% to about 7.6% in 2009. Meanwhile, the construction sector experienced a considerably expansion, from about 3% of GDP in 1990, to 14.5% in 2009. The narrowing of industry sector provided usable resources to the other sectors. The services sector experienced a great expansion, whose share to GDP increased from 33 % in 1990 to 63% in 2009. The share of agriculture sector first climbed from 23% to 32% up to 1997 and then decreased to 19% of GDP in 2009. The financial crisis seems to have been reflected mostly on industry, which in 2009 reduced by 2.5 percentage points as a ratio to GDP, in the meantime the services sector continued to expand by 5.4 percentage points against GDP relative to year 2008.

After discussing the main development of economic growth in Albania, it is important to analyze the main sources of growth which have determined the economic development of the country. In order to explain the main determinants of economic growth, the empiric literature suggests two approaches (Khan, 2004):

- First, the neoclassic model sought to decompose economic growth into the contributions of a number of fundamental sources of growth, such as: human capital, physical capital stock and Total Factor Productivity growth (known as TFP).
- Second, cross country comparative analysis of economic growth, sought to identify a number of structural sources of economic growth, such as: investments rate, school enrolment, international trade integration; macroeconomic stability, infrastructure and quality of institutions. It is obvious that these structural variables provide a contribution to the development of one or some fundamental sources of economic growth, which are used in the first approach.
During the course of this article, economic growth in Albania shall be by identifying its fundamental sources through the first approach.

**METHODOLOGY AND DATA**

To identify the sources of economic growth, the first approach is based on the Solow model which is also known as the neoclassic model of economic growth. This model considers the labour productivity, the capital productivity and TFP rate, as determinants of the economic growth. TFP is determined as the residual of the model and it evaluates the change in Total Factor Productivity. TFP growth rate also reflect the methodological assumptions and errors in the measurement of production factors. This Solow residual is determined as the growth at output level occurring when factors of economic growth (labor and capital) do not change. Thus, its interpretation depends on the definition provided to labour and capital factors. Given that the basic Solow model does not identify variables such as education level or professional experience (which affects labour input) and the capacity of capital use (which affects the capital input), then automatically these latter are included in TFP assessment. Solow model is given as an aggregate output Cobb Douglass production functions as following:

\[ Y = A \cdot L^\alpha \cdot K^{1-\alpha} \]  

where \( A \) stands for Total Factor Productivity (TFP), \( L \) is the labour input, \( K \) stands for the capital stock and \( \alpha \) is labour elasticity (also the share of labour income to total income). The linearization of output equation is obtained as follows:

\[ \frac{dY}{Y} = \frac{\alpha dL}{L} + (1-\alpha) \frac{dK}{K} + \frac{dA}{A} \]

Due to the lack of data on the share of income arising from labor factor (\( \alpha \)), we use the broadly known assumption, that 70% of total income derives from labour input and only 30% from capital stock.

The second problem regards the assessment of capital stock, for in Albania there is a lack of data on this series. For this purpose, we use an assessment of initial capital stock of 1996\(^1\) and add data on investments obtained from INSTAT. The annual depreciation rate of capital is assumed 8% and the stock capital investment is given as following:

\[ 1 \text{ Data are an assessment and are provided based on the demand of the author submitted to Geoffrey B. Oestreicher, IMF.} \]
\[ K(t+1) = K_t + It - \delta^t K_t \] (4)

where \( K_t \) stands for capital stock in \( t \), \( I_t \) is investments and \( \delta \) stands for the capital depreciation rate. Kota (2009) presents more complete information as regards to the construction of these data.

The analysis of economic growth sources uses annual data for the period 1996-2009. Data on total employment for this period are obtained from INSTAT. Capital stock is assessed according to the methodology presented above for 1996-2007, as after this period no more data on investments are available from INSTAT. In the meantime the extrapolation of investments data for 2008-2009 has taken place by using calibration. The data provided by the Bank of Albania on the use of loans from banks’ customers, reveal that about 1/3 of total loans goes for investments. Data on private investments during this period is extrapolated using loan growth for 2008-2009, and then are used to assess capital stock. Given that, public investments share about 15 % of total investments, the performance of private investments is crucial to set out the developments in stock capital. However, this remains an assessment of the real performance of investments over the period 2008-2009. Therefore it may be used just to create an idea on the contribution of production factors and the analysis must be considered preliminary.

**SOURCES OF ECONOMIC GROWTH - RESULTS**

The contribution of production factors (labour and capital) on economic growth, as measured through the growth rate of these inputs weighted by their share on total income, is introduced in chart 3.

The results suggest that up to 2000, TFP growth rate is the main contributor to economic growth, meanwhile the expansion of lending to economy, which started after 2000 is reflected on the elevated contribution of capital stock during the second period taken in consideration. Broadly speaking, during the economic recovery after the crisis of 1997 (1998-2000), when economic growth rate averagely pointed to 9.7 %, TFP rose on average by 9.3 %, meanwhile capital stock during the same period increased by 1.4 %. During the period 2001-2007, the annual average growth of economy points to 5.8 % and the capital stock provides the main contribution to economic growth, averagely by 3 %, while TFP growth is the second determinant factor with an average increase of 2.45 %. Labour input, measured through the official employment, has provided a rather low contribution to economic growth and in some cases even a negative one (prior to 2000). The problem of statistical data related to employment may be one of the main reasons, as they do not include assessment for the informal labor market being considerably present in Albania. Also, we should take into account that, labour in our case includes
the employment contribution to the economic growth, whereas the possible improvements at labour quality are reflected on the TFP upsurge.

Other authors have proved similar outcomes as regards to the case of Albania. Here we may mention Khan (2004), who identifies the determinant role of TFP on the economic growth in Albania. As in the case of results presented above, Khan (2004) also concludes that TFP growth rates have been dropping recently. Lower TFP growth is accompanied by a modest improvement of labour and capital’s contribution. According to Khan (2004) the sources of TFP growth in transition countries may be three:

- Very substantial improvements in TFP due to production factors reallocation and economy’s transformation during transition.
- TFP improvement that occurs as a result of improvement of sources’ allocation due to the structural reforms.
- TFP improvement that occur as a result of innovation and learning on the part of entrepreneurs.

Findings suggest that the main contributor to TFP increase was the first source. At the beginning of transition, due to the reallocation of economy’s sources, it is expected that TFP plays an important role. But the contribution of this input decreases as time passed and both capital stock and employment begin to contribute more to the economic growth. A similar outcome appears also for Albania, as sluggish growth of TFP was accompanied by higher contribution of capital accumulation. However, the important role of production factors combination through TFP is returned during the world financial crisis 2008-2009. Due to the considerable reduction of the credit growth rate, from 53% in annual figures in 2007, to 44% in 2008, whereas during 2009 this rate declined to 25%. The contribution of capital stock slowed down.

Finally, the results of the analysis suggest that employment has not contributed to the economic growth (here we should remember again that labor quality improvement is reflected on TFP term). Also, an important process of supporting the economic growth through human resources is their use with productivity. Even though labour input has provided no contribution to total economic growth, according to Kota (2007) labour productivity in Albania is improved. This process is quite important for the convergence of the Albanian economy to more developed economies. Economies of countries with deferent development rate show a lot of heterogeneity and dynamic as regards to sectors or companies. These countries are characterised by different productivity levels whose upsurge is the main source of economic growth over the long - run.

If labour is concentrated in sectors of different productivity which is inefficient, then a re-structuring process will take place in order to enhance economic growth. Labor source will shift from less productive sectors to more productive ones. The process will lead to labour source reallocation resulting in higher aggregate and sectors’ labour productivity, thus in higher economic growth of the country.
As discussed in chart 2, transition process in Albania was accompanied by the restructuring of economic activities. Such a restructuring should be accompanied with the re-organisation of labour market. Chart 3 shows the performance of both employment and labour productivity by sectors. Labour productivity is determined as the ratio between the added value and employment in each sector.

Agriculture with the lowest productivity appears to have the highest rate of employment. The problem here originates from the data regarding the employment rate, as INSTAT uses the assumption that any person who owns a land is employed. Overall a similar behaviour is manifested by the other sectors as well. Thus, services sector with the highest rate of labor productivity counts about 60% of total employed persons. While, the construction sector, being listed the second one according to the high rate of productivity, covers only 6% of total employment. A simple observation of these data reveals that employment allocation by sectors is not efficient, at least by using the official data as regard to employment, which notwithstanding exclude the informal market. But at aggregate level (for the entire economy), labor productivity is averagely increased by 6.4% throughout the period 1996-2008. Therefore it is interesting to trigger the main sources that have determined developments in labor productivity.

**LABOR PRODUCTIVITY – ITS GROWTH SOURCES**

The methodology applied from Kota (2007) is used to identify the main sources of developments of labor productivity in Albania. According to the author, the determinant factors of labor productivity improvement are: the growth of labor productivity within the sector, the reallocation of employment among sectors and the convergence of sectors towards an average productivity...
level, which is considered as an equilibrium level. This methodology is originated by Maliranta and Ilmakunnas (2005) and is broadly used to analyse labor productivity growth (for example, Fagerberg, 2000; Timmer and Szirmai, 2000; Jalava and others, 2002; van Ark and Timmer, 2003). The decomposition of the growth rate of labor productivity is as follows:

\[
\frac{\Delta LP_i}{LP_i} = \sum_i LSH_i \cdot \frac{\Delta LP_i}{LP_i} + \sum_i LSH_i \cdot \left( \frac{LP_i}{LP_0} - 1 \right) \frac{\Delta LP_i}{LP_i} + \sum_i \frac{LP_i}{LP_0} \cdot \Delta LSH_i
\]  

where \(LP\) stands for labor productivity in economy at \(t\) time, \(LSH_i\) is the average employment’s weight of sector \(i\) for the periods \(1\) and \(0\), \(\Delta LP_i\) is the difference of labor productivity for sector \(i\) for the same period, \(LP_i\) is the average level of respective productivity and \(\Delta LSH_i\) is the difference of employment’s weight of sector \(i\), for the periods \(1\) and \(0\).

The data used are the labor productivity, calculated as the ratio of added value to employment for each sector and the employment level. INSTAT and the Ministry of Labour, Social Affairs and Equal Opportunities have provided the annual data for the period 1996-2008 for the employment by sectors in 2008.

Regarding the effects that have determined the main sources of labour productivity development, they are determined as follows:

- Intra sector effect – labor productivity growth due to the improvement of sector efficiency.
- Convergence term – labor productivity growth due to the convergence of sectors towards the equilibrium level (average productivity level of economy)
- Labour shift effect – labor productivity growth due to the shift of employment from non-productive sectors to productive ones.

Based on these definitions and given that the agriculture sector ranks the last in terms of productivity performance, it is expected the developments of two possible processes:

a) Low levels of agricultural productivity should lead to labor source reallocation from this sector towards more productive sectors.

b) If there is a sectors’ convergence process, then the agriculture sector should reflect higher productivity growth in order to catch the aggregate mean of labor productivity.
Meanwhile, as regards to the other sectors, the development of these processes would depend on the performance of labour productivity at sectors level, also on the overall developments in economy. The implementation of the methodology introduced in this section shall be presented below.

RESULTS OF LABOUR PRODUCTIVITY DECOMPOSITION BY EFFECTS

The results of aggregate productivity growth decomposition are presented in Chart 4, according to the intra sector effect, convergence term and the effect of labour reallocation across sectors.

The results suggest that Intra sector effect, that implies sector productivity growth, due to the improvement of sector’s efficiency, is the major contributor to the growth of labour productivity. In 2001 there is a structural break of data due to the change of employment measuring methodology from INSTAT, therefore this year is not considered during the analysis.

The results of analysis suggest that the reallocation effect of employment has not provided a high contribution to productivity developments. Official employment by sectors from year to year appears to be stable and this may result from the exclusion of informal labour market. Excluding the agriculture sector due to high share it has on total employment, the major contributor on the employment reallocation effect is the services sector. The high productivity rate of this sector is accompanied by the higher employment level in this sector. Also, construction sector shows a positive effect of employment reallocation, particularly prior to 2001. Owing to the upsurge of profitability in this sector, its share to employment has considerably climbed by providing a positive contribution to the total growth of labour productivity.

An explanation why the agriculture sector is not characterised by high rates of employment shift as expected, is that the labour force that is shifted, does not possess the relevant skills required in the more productive sectors. This problem emphasises the need for skills upgrading to induce higher productivity, and consequently, also the economic growth in Albania. However, given that the agriculture sector is the only sector with productivity level lower than average aggregate rate, it has continuously converged towards the average of economy, thus experiencing positive rates of productivity growth. But, on the other hand, the most productive sectors (construction and services) continue to show high annual growth rates of their efficiency, and regardless of the agriculture convergence, the economy has not achieved steady state level of productivity. The process of ongoing productivity growth of the productive sectors together with the convergence process of inefficient sector is expected...
to induce a further growth of labour productivity in Albania. This will be a good basis for the improvement of contribution of labor input to the economic growth in the future.

CONCLUSIONS

The improvement of TFP has been the main source of economic growth in Albania, whereas after 2000 the capital stock has played an important role. Consequently, given that after transition TFP improvement due to economy reorganisation will gradually slowdown, and the developments at investments growth rates have been fluctuating from y-o-y, it is important that Albania creates alternative sources of economic growth. In this view, the capital accumulation via the stimulation of investments becomes of a particular importance. Also, the establishment of other TFP improvements arising from alternative sources than that of economy’s reorganisation is important. Here we can mention improving the benefiting from technological knowledge, increasing the enterprising efficiency throughout the time, etc. Lastly, due to the convergence of sectors towards labour productivity growth in Albania, the improvement of this production factor quality is important to take place.

* The views expressed in this paper are those of the author and do not necessarily represent those of the Bank of Albania.
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INDEX OF MONETARY AND FINANCIAL CONDITIONS
ALBANIA

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1. INDEX OF MONETARY AND FINANCIAL CONDITIONS

The Monetary Conditions Index was first introduced by the Bank of Canada and has been used from many international banks and institutions. This index serves as a mechanism to interpret the direction of monetary policy and the related effects on the economy.

The Monetary Condition Index (MCI) assesses the combined effect of indicators, which represent the main channels of monetary policy transmission to an open economy: the real interest rates and the real exchange rate, where their coefficients represent the respective effects on aggregate demand. The main purpose of MCI is to provide additional information on the monetary conditions in a given economy. It considers the performance of both interest and exchange rates in real terms. We may say this index is a weighted average of both indicators stated above and determines if monetary conditions in a given economy are “loosed” or “tightened.” The result is displayed by a specific number that shows the grade of pressure that monetary policy exercises on economy and consequently on inflation. Given a situation characterised by “loosed” monetary conditions, it is expected that monetary policy supports economic growth. On the other hand, given neutral monetary conditions in the economy, the monetary policy is expected to have neutral effects.

It should be highlighted that the monetary conditions’ components do not necessarily affect the economy on the same direction. For example, exchange rate may be assessed as “loosed” and the interest rates as “tightened,” and vice-versa. The interest rate plays the main role in determining the monetary conditions, while the exchange rate adapts to the interest rates: lower interest rates, in a certain period of time, stimulate the depreciation of the domestic currency exchange, and vice versa. The monetary policy impacts inflation through two directions: interest rates and exchange rate. An increase in either of these rates is likely to slow down economic growth and decrease inflationary pressures. Likely, a cut of either interest or exchange rates stimulates economic activity, and therefore it may lead to higher inflationary pressures. Consequently, both channels should be taken into account when constructing MCI.

The Monetary Conditions Index for the period $t$ is determined as the weighted sum of interest rate changes ($i$) and the exchange rate ($e$) from their level in the base year ($t=0$), and may be introduced as following:

$$MCI = \theta_i (i - i_b) + \theta_e (e - e_b)$$
where, $\theta_1$ and $\theta_2$ represent the weights of real interest rates and of the real 
exchange rate, respectively.

Based on the research conducted by Manjola Tase (August, 2006), in the 
case of Albania, the Monetary Conditions Index is the weighted average of 
key interest rate changes (REPO) and the nominal effective exchange rate 
of ALL (NEER) against a base period. This index points to a ratio of 1.82:1, 
implying that the effect of exchange rate depreciation by 1.82 percentage 
points is compensated by a 1 percentage point shift in interest rates. The base 
period of the MCI assessment was September 2000.

This assessment of Monetary Conditions Index ratio for the case of Albania 
was accomplished through a calibration method based on IMF (2004). 
The assessment done using this method might be somewhat indirect and 
imprecise. Given the need for a new way of assessment and the available 
data for a period of about 10 years, I have calculated the average weights of 
real interest rates and the real exchange rate for Albania. The methodology 
is based on an OLS assessment and considers quarterly data for 1998Q1– 
2008Q4. The new ratio calculated by this method points to 3.8, implying that 
the effect of a real effective exchange rate (REER) by 3.8 percentage points 
might be neutralised by a shift of 1 percentage point in real interest rates.

Data used for the assessment of MCI ratio are the following:

- REER, real effective exchange rate of domestic currency, based on the 
domestic and international Consumer Price Index;
- 3-month T-bills real rates;
- 6-month T-bills real rates;
- 12-month T-bills real rates;
- Inflation;
- Gross Domestic Product;
- Output Gap, as a percentage of Real GDP deviation from potential 
  GDP.

Three separate equations are built in this study, where 3-, 6- and 12-month 
T-bills are used respectively for each, and where the output gap is the dependent 
variable. In these equations Adjusted R-squared is high and this shows that a 
high percentage of the model is explained by the variables considered, also 
F-statistic has a high value that certifies the model’s significance; the latter 
shows the model is statistically significant. Then, diagnostic tests of coefficients 
and residuals are conducted. Once it is certified that the models used do not 
show any problems, the coefficient ratio of each equation is calculated next. 
Later, the calculated values are simply averaged, pointing to -3.8. Given that, 
a numeric increase of REER shows a depreciation of ALL, then this value shall 
be multiplied by (-1) concluding that the new Monetary Conditions Index ratio 
points to 3.8.

Moving on to the Financial Conditions Index, this indicator assesses the 
financial conditions of a country. In this case the performance of real interest
rate for credit is considered when analyzing the financial activity. The same ratio used with the Monetary Conditions Index is used for FCI as well.

2. PERFORMANCE OF MCI AND FCI

**MONETARY CONDITIONS INDEX**

Monthly data from January 1996 to April 2010 were used subordinated indicator to build the Monetary Conditions Index for Albania. The base period of assessment for MCI is January 1996, and is expressed as follows:

\[
MCI = (\text{Real}_{TB} - \text{Real}_{TB_{(base)}}) \times 3.8 + (\log(\text{REER}) - \log(\text{REER}_{(base)})) + 100
\]

where:

- \( \text{Real}_{TB} \) stands for the average real rate of T-bills;
- \( \text{Real}_{TB_{(base)}} \) is the real rate of T-bills in the base year;
- \( \text{REER} \) is the real effective exchange rate;
- \( (\text{REER})_{(base)} \) is the real effective exchange rate in base year;

An increase in the Monetary Conditions Index shows a deterioration of monetary conditions; conversely, a fall in this index suggests that monetary conditions in the economy are improved compared to the base year. In the following chart we can see the MCI performance from January 2006 to April 2010, compared to the performance of REER and the real interest rates for T-bills.

In this chart we see that monetary activity from 2007 up to the third quarter of 2008 has seen considerable improvements, which was not customary for the preceding 15 years. These improvements arose due to the depreciation of the real exchange rate, which is interpreted into eased economic conditions and owes to the slight reduction of real interest rates. The beginning of the financial crisis is characterised by tight monetary conditions, mainly owing to the rise of T-bills’ interest rates. During the first months of 2010 we see that after a period of improved monetary conditions, starting from March, this index shows tightening of monetary conditions; this deterioration owes to the effect of the further raise of T-bills’ interest rates in real terms; meanwhile, the domestic currency continues to be characterised by an ongoing depreciation.
FINANCIAL CONDITIONS INDEX

Monthly data from August 2000 to April 2010 are used to build the Financial Conditions Index for Albania. The base period for the MCI assessment is August 2000, and it is expressed as follows:

\[
ICF = (Real_{LR} - Real_{LR\text{ (base)}}) \times 3.8 + (\log(REER) - \log(REER\text{ (base)}) + 100
\]

where:

- Real_{LR} is the real average rate of loans;
- Real_{LR\text{ (base)}} is the real rate of loans in base year;
- REER is the real effective exchange rate;
- (REER)_{\text{ (base)}} is the real effective exchange rate at base year;

This chart shows that, unlike the average rates of the last 15 years, the financial activity is characterised by important improvements in the period between 2007 and the third quarter of 2008. But at the beginning of the financial crisis, the financial activity is characterised by tight conditions owing to the increase of loans’ real interest rates. The financial conditions start to improve only after 2009 due to ALL depreciation and to the drop of interest rates.

* The views expressed in this paper are those of the author and do not necessarily represent those of the Bank of Albania.
REFERENCES


On 13 October 2009, the Bank of Albania organised the third Open Forum of the Albanian banking system, as a follow-up debate of the technical meeting held in August. Likely the previous forums, directors and experts of the Bank of Albania and of banks operating in the Albanian banking system attended this event.

The discussions addressed a number of important issues, not only for the moment, also as regards to the expectations for the future. Thus, the first line of discussion dwelled on during the Forum, related to the accountability in management, considered in the framework of strengthening the control systems, the improvement of risk management capacities, investments in human resources and technology, also the transparency with customers and the market. The second line of discussions dealt with the development of the activity, particularly the establishment of a better equilibrium in terms of assets–liabilities composition by currency, maturity, interest rate; stability of financing sources and the solution of liquidity challenges; the cyclical need to manage the latter. At the conclusion, whereas discussing the expectations of banking system for the future, it took place the discussion about the main developments occurring in the international standards and the level of their impact on the banking activity and the supervision regulatory framework, as well as the way expected these development affect banking activity over the short and medium run.

On 14 October 2009, the Governor of the Bank of Albania, Mr. Ardian Fullani held a meeting with the Deputy Minister for the Economic Development of the Republic of Italy, Mr. Adolfo Urso, who was heading a delegation composed by representatives of different Italian companies, who participated in the Fiera del Levante Exhibition organised in Tirana on October 14-17, 2009.

Governor Fullani made a general depiction of the main developments of the Albanian economy and the country’s macroeconomic performance. Mr. Fullani introduced to the Italian delegation the measures taken recently by the Bank of Albania in the framework of maintaining macroeconomic and financial stability at home and the work carried out to minimise the global crisis effects, thus affecting the stable performance of the economy and the establishment of a positive business climate.

The Deputy Minister Urso appreciated the reforms accomplished by the Bank of Albania, which has recently made strong and consolidated steps in
many directions, where undoubtedly a special contribution has been rendered by the Bank of Albania, as the monetary authority of the country, pursuing prudential and visionary policies. Availing this opportunity, Governor Fullani invited the Italian investors to pursue their support and investments in Albania, which offers a powerful potential, with well-unexploited natural resources, qualified human capital and modern developed infrastructure.

On 29 October 2009, in the framework of the Conference for the 10th Anniversary of the Central Bank of the Republic of Kosovo, the Governor of the Bank of Albania, Mr. Ardan Fullani delivered a lecture at the University of Pristina, entitled “The Albanian economy facing the recent challenges and the European Perspective”. The lecture was attended by students of Economics and Law Faculty of the University of Pristina and by the academic staff of this University.

On 16 November 2009, at the invitation of Mr. Drini Salko, Responsible of Finance and Accounting Department, the Governor of the Bank of Albania, Mr. Ardan Fullani, delivered a lecture entitled “Policies of the Bank of Albania in the framework of global crisis”. Speaking about the global crisis and its effects on the Albanian economy, Governor Fullani paid special attention to the importance and the need to pursue the appropriate agricultural policies to simulate the economy.

The lecture of Governor Fullani was accompanied with the organisation of “The Day of the Bank” at Agricultural University of Tirana. During this activity, the students and also the academics of university got more closely known with the publications of the Bank of Albania. At this occasion, there were delivered many periodic reports and bulletins, working papers and speeches of scientific conferences, educational brochures and informing leaflets, which are published from the Bank of Albania in the framework of transparency and responsibility for public informing.

In the framework of developing the open dialogue with different players of the economy and given the recent developments in the Albanian and global economy, on 23 November 2009, the Bank of Albania held a meeting with the main businesses operating in Albania.

As the most dynamic part of the Albanian economy, business’ contribution has been tangible in the country’s economic development during transition. The incentive, the willingness and devotion have brought about tangible results in the country’s development. Assessing the contribution of business sector, the Bank of Albania’s forum dealt with issues regarding the current situation of Albanian economy, the country’s exit from crisis and the potential difficulties of Albanian economy may encounter during 2010. Also, the forum aimed to start a broad public discussion about the alternatives of economic growth models in the future.
On 3-4 December 2009, the Bank of Albania, in cooperation with Centre of Excellence in Finance (CEF) – Slovenia, with support from the European Commission, European Central Bank and International Monetary Fund, organised the workshop on “Building Capacities for Policy Design and Implementation”. This workshop addressed the main challenges associated with policy design and policy anchoring, highlighting particularly the building of individual and institutional capacities in this very important area.

The meeting took place for the first time in Albania and gathered representatives from central banks and the ministries of finances of Southeast Europe, as: Bosnia – Herzegovina, Bulgaria, Kosovo, Croatia, Montenegro, Macedonia, Moldavia, Rumania, Turkey, Serbia, and Albania. The main speakers were from Centre of Excellence in Finance (CEF), European Commission, European Central Bank and International Monetary Fund.

In his opening speech, the Governor of the Bank of Albania, Mr. Ardian Fullani highlighted the importance of appropriate economic policies design to detect the new economic growth model, in the wake of crisis, with the focus on attraction of foreign capital inflows to the region. He suggested the need for risk-averse fiscal policies and proper structural reforms targeted to improving the business environment, which will help to increase new capital inflows and lead to their strong and sustainable growth.

While discussing with participants, Governor Fullani drew attention to the need for using the European institutions and integration process as a natural, sound and efficient external anchor in the medium run. According to Governor, the strengthening of external anchors over the medium run is a necessity, and the European policies or EU institutions can and should play such a role. Domestic anchors of regional countries are equally important, implying the compilation of sound financial economic policies on the one hand, and building of the appropriate capacities for their assimilation and implementation on the other hand.

On 13 December 2009, in the theatre of the Academy of Art in Tirana, was held the final stage of “Real Value of Money” competition for the academic year 2008-2009. The “Real Value of Money” competition is a challenge among the high schools’ teams, regarding their knowledge for the Bank of Albania, its monetary policy, the instruments it uses and the impacts of the central bank’s decisions on the country economy.

In front of the Competition Jury panel, chaired by the Governor of the Bank of Albania, Mr. Ardian Fullani, were the 5 winning schools at the district level: “Ali Demi’ High - School - Vlora; “28 Nëntori” High - School - Shkodra; “Themistokli Gërmenji” High-School – Korça; “Siri Shaplllo” High School – Gjirokastror; and “Tirana Jonë” High -School – Tirana. In addition to frequent questions, the competition’s finalists had to place on the shoes of the Supervisory Council of a central bank, to analyse the hypothetical situation of a country economy to decide on the key interest rate of the monetary policy.
At the conclusion of the competition, the Jury panel of the Bank of Albania assessed the teams not only for their knowledge, also about their analytical abilities of arguing the answers as a team work, and based on the scores, it announces as the winner of the competition, “Themistokli Gërmenj” school from Korça.

On the occasion of the closing of year, the Governor of the Bank of Albania, Mr. Ardian Fullani held a meeting with distinguished journalists of print and electronic media, politics and economics analysts, and with head of media and other representatives in Albania. Governor Fullani appraised the contribution of journalists to conveying the Bank of Albania messages and expressed his confidence that the media analyses and comments will remain objective and realistic in the period to follow.

At the beginning, Governor Fullani made a short overview of the development in the Albanian economy, underlying that year 2009 attested to a number of events among which the global crisis was the most striking one.

The Governor underlined that the efforts and work made by the Bank of Albania helped to safeguard and consolidate macroeconomic and financial stability in the Albanian banking system.

In addition, the Bank of Albania has been throughout the year 2009 committed in a number of other projects of special contribution to the Albanian society.

In this light, the Governor introduced some of the central bank’s commitments as regard public education, the inauguration of the research Institute of the Bank of Albania located in Berati and the launching of the Bank of Albania Calendar for 2010, to promote Albania’s antique cities and the respective coins minted and used during that period.

The Research Department at the Bank of Albania organises twice a month the “Friday Seminar”. This initiative provides a call to the Bank of Albania staff, analysts of academic field and of other financial, research and scientific institutions, to present and discuss their theoretical and empirical scientific works, having at their main focus the case of Albania and the application of new research methods.

Five working papers were part of the Friday Seminar during the last quarter of 2009. Lorina Green and Rezart Erindi, Monetary Operations Department of the Bank of Albania, presented the first paper entitled “Use of KMV-Merton Model to forecast the possibility of companies’ failure in terms of settling the issued debt”. An increasing interest has been shown, as regards to the models which forecast the failure possibility of companies in terms of their debt settlement, owing to the augmentation of issued debt products and the ever-increasing use of credit derivatives. A model introducing novelty
in forecasts, broadly applied in practice and in academic researches, is the special implementation of Merton (1974) model developed by KMV corporate. This paper aims to present this model and provides the possibility to exploit the latter at the Bank of Albania.

The next paper by Rezart Erindi and Valbona Luga, Monetary Operations Department of the Bank of Albania, entitled “Selection of strategic benchmark. Theoretical and practical aspects”. The selection of strategic benchmark might be described as a process through which a domestic institution might decide on the neutral allocation of investment (financial instruments) at any time, to achieve the long-term targets of investment. In this paper, the authors concentrate on the final steps of the process, by describing the methodology observed to build up the strategic benchmark and the timely assessment of this methodology. Also, they set out the instruments classes allowed for investment purpose.

In November, Armela Mançellari, Research Department at the Bank of Albania, introduced the paper “Nowcasting gDp – Short-term assessment of real GDP”. The purpose of this paper is to build up models for the short-term forecast of the country GDP value for the current quarter. Given that the data on quarterly GDP in Albania are published after 12 weeks, to accomplish a well-informed decision-making, it is needed the forecast of this indicator’s performance prior to its publication. The author makes use of data from: real sales, selling and repairing of vehicles and confidence index components, to forecast current quarterly GDP with the assistance of the econometric models.

“Does the fiscal multiplier exist? Fiscal and monetary reactions, credibility and fiscal multipliers in Hungary”, was the paper introduced by Zoltan Jakab, Director for Macroeconomic Analysis, Office of Fiscal Council, Republic of Hungary. The purpose of this paper is to assess the fiscal policy multipliers in Hungary by employing the DSGE model. Results show that the multipliers of different fiscal indicators vary from each-other. They do differ even when there are considered the ways the fiscal policy expansion shall be financed in the future. The perception of economic agents as regards to fiscal stimulus continuance considerably impacts the multipliers. Outcomes suggest that as regard to a small and open economy, where monetary policy mostly react against inflation, the accommodation it makes to fiscal policy has no effect on fiscal multipliers.

For the 2009, the “Friday Seminar” closed with the discussion of the working paper “Modelling the Quarterly GDP - Role of economic and surveys indicators”, by Evelina Çeliku, Ermelinda Kristo, Merita Boka, the Department of Monetary Policy, Bank of Albania. The purpose of this paper is to estimate the Albanian GDP trends in the short term by following three main approaches for this assessment: a set of ARIMA models with seasonal information; b. a set of Indicator models – bridge models; and c. a set of VAR models. These models have provided the obtaining of prior estimates regarding the dynamics of the economic activity, about the main trend for the referring quarter (nowcast) and
for two succeeding quarters (forecast). The paper concludes that variables obtained from the surveys contain valuable information for the quarterly GDP forecast in the short run. Also, the average of forecasts from various models is considered as the “best” forecast, (excluding ARIMA models). Finally, the forecast performance out of the sample period in the future would assist to identify the model or models with higher forecasting power.
CHRONOLOGY OF MONETARY POLICY DECISIONS

12 July 2006
The Supervisory Council of the Bank of Albania decides to increase the key interest rate by 0.25 percentage points, to 5.25%.

30 November 2006
The Supervisory Council of the Bank of Albania decides to increase the key interest rate by 0.25 percentage points, to 5.5%.

4 April, 2 May and 6 June 2007
The Supervisory Council of the Bank of Albania decides to keep the key interest rate unchanged at 5.5%.

27 June 2007
The Supervisory Council of the Bank of Albania decides to increase the key interest rate by 0.25 percentage points, to 5.75%.

19 July and 29 August 2007
The Supervisory Council of the Bank of Albania decides to keep the key interest rate unchanged at 5.75%.

26 September 2007
The Supervisory Council of the Bank of Albania decides to increase the key interest rate by 0.25 percentage points, to 6.00%.

31 October 2007
The Supervisory Council of the Bank of Albania decides to keep the key interest rate unchanged at 6.00%.

27 November 2007
The Supervisory Council of the Bank of Albania decides to increase the key interest rate by 0.25 percentage points, to 6.25%.
27 December 2007
The Supervisory Council of the Bank of Albania decides to keep the key interest rate unchanged at 6.25%.

The Supervisory Council of the Bank of Albania decides to keep the key interest rate unchanged at 6.25%, all through 2008.

28 January 2009
The Supervisory Council of the Bank of Albania decides to decrease the key interest rate by 0.50 percentage points, to 5.75%.

25 February, 25 March, 29 April, 17 May, 24 June, 29 July, 26 August and 30 September 2009
The Supervisory Council of the Bank of Albania decides to keep the key interest rate unchanged at 5.75%.
LEGAL EVENTS OVER OCTOBER - DECEMBER 2009

FINANCIAL STABILITY

On 14 October 2009, the Supervisory Council of the Bank of Albania approved by Decision No. 72, “The Financial Stability Report for the first half of 2009”. The report concludes that, the banking sector at home shrank the funding volume to the domestic economy as a response to the increased demand for liquidity, given the effects of the international financial crisis and due to the fall of deposits in banks and to the picking up of the Government demand to borrow. In the first quarter 2009, the financial system development, at home, was impacted from the ceasing of the banking system growth; in the meantime the other part of the financial market recorded a considerable growth of the activity. Notwithstanding, at the end of this period, the banking sector recorded a positive financial outcome, amounting to ALL 0.66 billion and the activity capitalisation remained stable and at adequate rates.

MONETARY POLICY

On 28 October 2009, the Supervisory Council of the Bank of Albania approved by Decision No. 76 “The cut by 0.50 percentage points of Repurchase and Reverse Repurchase Agreements interest rates”. Through the cut by 0.50 percentage points, with a key interest rate decreasing from 5.75 to 5.25%, the Bank of Albania aims to establish the premises for the lending of economy as well as to pursue the minimisation process of international financial crisis’ effects, by supporting the economic activity at home.

BANKING SUPERVISION

On 14 October 2009, the Supervisory Council of the Bank of Albania approved by Decision No. 71 the Regulation “On the management of risk liquidity”. The purpose of this regulation is to set out the requirements and minimum standards for the effective management of risk liquidity from banks, through the establishment of a system which must comprise the strategies and policies compiled from the bank to manage this risk; the organisational structure and internal audit, also the contingency plan.

On 11 November 2009, the Supervisory Council of the Bank of Albania approved by the Decision No. 78, the increase of Çalık Holding A.S. Turkey (indirect shareholder) qualifying holding, from 25.2 to 45.6 percent in the share capital of the National Bank of Turkey (Joint-Stock Company).

ECONOMIC POLICIES

On 14 October 2009, The Council of Ministers approved by Decision No. 1011 “The PHRD Grant Agreement, No. TF 093096, between the Government of Albania and the International Bank for Reconstruction and Development (IBRD), for the compilation of the project of government, finance and the providing the municipal services”. The grant amounting to USD 980,000 USD shall be used for the implementation of the project, which is the first phase of a long-term program for municipalities in Albania, which aims to accomplish stability on providing municipal services, through the strengthening of local government finances. The grant shall be exploited to fund activities which aim to sustain and improve waters, sewages, rural streets, management of inert residuals, etc.

On 15 October 2009, The parliament of the republic of Albania approved the Law No. 10 157 “On some changes and amendments to the Law No. 9663, dated 18.12.2006 “On concessions”, as amended. The amendments stipulate the establishment of the Concessions Agency, as a public budgeted institution, charged with the supervision and verification of implementation of the concession procedures, administrative investigation and the proposal of punishing measures in case of infringements.

On 15 October 2009, the Parliament of the Republic of Albania approved the Law No. 10 158 “On bonds of joint–stock companies and of local government”. The law sets out the types, ways of allocation and maturity of bonds issued from both the joint–stock companies and the local government. The law arranges the organisation and function of bonds’ owners groups, the conservatorship and the agent of bonds’ owners.

On 14 October 2009, the Council of Ministers approved the Decision No. 1020 “On the establishment of the Auditing Agency, accredited from the European Union”. The purpose of this Agency is to audit and control the implementation of assistance programs, granted from the European Union, the agency is responsible for the efficient and sound functioning of assistance management system and this latter is functionally independent from all players of this system.
On 15 October 2009, The Parliament of the Republic of Albania ratified by the Law No. 10 155 “The Agreement between the Republic of Albania and the Kingdom of Spain for collaboration to combat crime”. Through this Agreement, both countries commit to collaborate closely in the war against different shapes of the financial crime, as: contraband, money laundering, counterfeit and delivery of currency and other means of payments, and the criminal operations against public finances and fiscal evasion.

On 15 October 2009, The Parliament of the Republic of Albania ratified by the Law No. 10 162 “The Agreement between the Council of Ministers of Albania and the Government of Czech Republic for collaboration to combat the crime”. Through this agreement, the government of both countries aim to improve the collaboration for the prevention and detection of crime and its different shapes, as: crimes against life, terrorism and its financing, corruption and contraband, illegal financial transactions, etc.

On 21 October 2009, The Council of Ministers approved the Decision No. 1081 “On the organisation and functioning of National Food Authority”. According to this decision, the National Foodstuff Authority is responsible to plan and coordinate the official control of foodstuff, animal food and the defence of plants at national level.

On 22 October 2009, The Parliament of the Republic of Albania approved the Law No. 10 169 “On some amendments and changes in the Law No. 9482 “On legalisation, urbanisation and integration of illegal constructions”, as amended”. The amendments set out that the payment of constructing parcel of the illegal buildings during the legalisation process may take place via privatisation bonds, up to 50 percent of its value. This payment way is valuable for constructions built within the yellow line, outside the yellow line and in other territories as well.

On 27 October 2009, the Parliament of the Republic of Albania approved by the Law No. 1077, the national strategic document “On the investigation of financial crime”. The document aims to establish a long-term operational platform and to combat constantly the economic-financial crime, money laundering and terrorism financing through the compilation of the legislation in line with the European Standards, the increase of control efficiency of this legislation implementation and the strengthening of inter-institutional collaboration.


On 29 October 2009, The Parliament of the Republic of Albania approved the Law No. 10 183 “On some changes and amendments in the Law No. 9374 “On the Public Assistance”. This Law provides to the Law “On Public Assistance” the principles and procedures according to which it is allowed and controlled the public assistance for the disadvantaged employees, the assistance for the environment protection and the one for risk capital.

On 29.10.2009, The parliament of the republic of Albania approved the Law No. 10 179 “On the adherence of the Republic of Albania to the European Patent Treaty”. This Treaty decides, as regards to all the adhering countries, a common legal system on granting the patent for inventories, unique procedures and some standard rules which regulate the patents granted in this way.

On 5 November 2009, the Parliament of the Republic of Albania adopted the Law No. 10 186 “On the ownership regulation on state-owned land in the areas with tourism priority”. The Law aims to regulate the ownership relationships on the land and objects built in the areas simulated with tourism priority, which are granted for the realisation of facilitating activities, established prior to the entering into force of this Law.

On 20 November 2009, The Parliament of the Republic of Albania approved the Law No. 10 168 “On the approval of form and formula of INSIG privatisation, Joint-stock company”. As regards to this Law, the transfer of 100 percent to equities of the commercial company INSIG, Joint stock Company, which are owned from the Albanian Government, shall take place through the sale, to the benefit of investors, in line with the “Open International Tender” procedure.

On 20 November 2009, The Parliament of the Republic of Albania approved the Law No. 10 170 “On some changes and amendments in the Law No. 9643, dated 20.11.2006 “On Public Procurement”, as amended”. Amendments, inter alia, set out the establishment and the functioning of Public Procurement Commission as the highest authority in the field of public procurement, charged with the analysing of claims and procurement procedures, whose decisions are final in administrative terms.

On 25 November 2009, The Council of Ministers, approved the Decision No. 1151 “On the establishment and use of special fund”. In accordance with this decision, the special fund shall be established in the
units of general government, at the rate of 5% of the total wages fund, to be used for the compensation of employees, to provide subsequent grants in case of contingencies, etc.

On 25 November 2009, The Council of Ministers approved by the Decision No.1177 “The Agreement between the Council of Ministers of the Republic of Albania and the Government of the Republic of Kosovo on mutual collaboration and assistance dealing with customs issues. Through this agreement both countries aim to make more efficient the attempts to prevent the infringements of customs legislation and to provide the correct collection of imports-exports liabilities, taxes and other liabilities, through the close collaboration between their customs authorities.

On 29 November 2009, the Parliament of the Republic of Albania approved the Law No.10190 “On the budget of 2010”, given a deficit, which amounts to approximately ALL 50 billion, revenues, which exceeds ALL 360 billion and expenditures about ALL 410 billion, the budget of 2010 aims to guarantee the macro-economic stability of the country and the ongoing economic growth.

On 3 December 2009, the Parliament of the Republic of Albania approved the Law No.10 192 “On the prevention and the fight against the organised crime and traffic through preventing measures against assets”. The law sets out the procedures, competences and criteria to undertake the preventing measures against assets of persons suspected for participation in organised crime and trafficking. It aims the prevention and the fight of organised crime through assets ‘confiscation of persons, who owns an unjustified economic level, as a result of participation in criminal activities.

On 10 December 2009, The Parliament of the Republic of Albania approved the Law No. 10 196 “On some amendments and changes in the Law No. 9072, dated 22.05.2003 “On the electrical power”, as amended. The changes stipulated in this Law, deals mainly with the Article which arranges the sources of removable energy. Thus, the Council of Ministers is authorised to undertake encouraging and supporting initiatives for the construction of centrals, that uses the renewable energy for the production of electrical power, which shall be totally consumed at home.

On 10 December 2009, the Parliament of the Republic of Albania approved the Law No. 10 197 “On volunteer pension funds”. The purpose of this Law is to regulate the foundation, the activity and supervision of volunteer pension funds with determined contributions. It sets out the needed standards for the effective management and supervision of these funds, assigning the Financial Supervision Authority responsible for the implementation of this Law.

On 10 December 2009, the Parliament of the Republic of Albania approved the Law No. 10 198 “On collective investments schemes”. The purpose of this Law is to set out the conditions and criteria for the foundation, registration and functioning of collective investment schemes, providing the correct functioning
of capital markets and the simulation of their free movement. The Financial Supervision Authority shall supervise the activity carried out by the collective investments schemes, the managing companies, depositors and other persons involved in the sale of quotas and equities.

On 15 December 2009, the Commissioners Board of Power Regulatory Authority approved the Decision No. 100 “On establishing the selling prices of electrical power retail sale for the period 1 January -31 December 2010”. The decisions sets out the fees of electrical energy retail sale for the year 2010, by consumer groups. Thus, the price of electrical power during 2010 for households shall be 7.70 lekë/kWh for consumption up to 300 kWh and 13.50 lekë/kWh for consumption higher than 300 kWh.

On 16 December 2009, the Council of Ministers approved the Decision No. 1216 “On providing the subsequent economic assistance to persons, who benefit a pension”. In accordance with this decision, the persons benefiting an ancient, invalid or familiar pension, likely those benefiting a monthly compensation as war veterans or special financial treatment, shall benefit a subsequent economic assistance, amounting to ALL 2 500.

On 23 December 2009, The Council of Ministers adopted the Decision No. 1290 “On the establishment of the core criteria, of sectors to be assisted and the amounts of benefiting from the program fund for agriculture and rural development”. This decision shall set out the funds approved in the budget of 2010 designated for the Ministry of Agriculture and Consumer Protection, in the item “Transfers to household’s budget” be used for the assistance of agricultural, animal and agro-processing production. The provided funds aim to simulate the planting of olive woods, fruits and veins, the implementation of modern watering technology, production of vegetables in solar green houses, the production of bio productions, and the increase of banking credit to agricultural sector.
BANK OF ALBANIA MANAGEMENT, 31 DECEMBER 2009

SUPERVISORY COUNCIL

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<tr>
<td>FATOS IBRAHIMI</td>
<td>Vice Chairman</td>
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<td>ARJAN KADAREJA</td>
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<td>HALIT XHAFI</td>
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<td>BENET BECI</td>
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GOVERNOR

ARDIAN FULLANI

GOVERNOR’S OFFICE

GENC MAMANI

HEAD OF COORDINATION

GRAMOS KOLASI

DEPUTY GOVERNORS

FATOS IBRAHIMI  First Deputy Governor

GENERAL INSPECTOR

TEUTA BALETA

DEPARTMENTS AND OTHER UNITS

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<td>Roden Pajaj</td>
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<td>MONETARY POLICY DEPARTMENT</td>
<td>Erald Themeli</td>
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<td>Diana Shylla</td>
</tr>
<tr>
<td>ISSUE DEPARTMENT</td>
<td>Valer Miho</td>
</tr>
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<td>ACCOUNTING AND FINANCE DEPARTMENT</td>
<td>Artan Tora</td>
</tr>
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<td>PAYMENT SYSTEMS DEPARTMENT</td>
<td>Dashmir Halilaj</td>
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<td>LEGAL DEPARTMENT</td>
<td>Toni Gugu</td>
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<tr>
<td>AUDIT DEPARTMENT</td>
<td>Teuta Baleta</td>
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<tr>
<td>FOREIGN RELATIONS, EUROPEAN INTEGRATION AND</td>
<td>Agron Skënderaga</td>
</tr>
<tr>
<td>COMMUNICATION DEPARTMENT</td>
<td>(vacant)</td>
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<td>ADMINISTRATION DEPARTMENT</td>
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<td>SECURITY AND PROTECTION DEPARTMENT</td>
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BRANCHES

<table>
<thead>
<tr>
<th>Branch</th>
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<tbody>
<tr>
<td>SHKODRA</td>
<td>Ermira Istrefi</td>
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<td>ELBASANI</td>
<td>Valentina Dedja</td>
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<tr>
<td>GJIROKAstra</td>
<td>Anila Thomaj</td>
</tr>
<tr>
<td>KORÇA</td>
<td>Liljana Zjarri</td>
</tr>
<tr>
<td>LUSHNJAJ</td>
<td>Shpresa Meço</td>
</tr>
</tbody>
</table>
LIST OF ALL ENTITIES LICENSED BY THE BANK OF ALBANIA*

BANKS AND BRANCHES OF FOREIGN BANKS

1. RAFFEISEN BANK (JOINT-STOCK COMPANY)
   Licence No. 2/1998, dated 11.01.1999
   Certificate No. 2 “On Deposit Insurance”.
   Director: Oliver WHITTLE
   Address: Bulevardi “Bajram Curri”, European Trade Center, Tirana, Albania
   Tel.: 222 66 99, 222 45 40, 222 26 69, 222 54 16
   Fax.: 227 55 99, 222 35 87, 222 36 95, 222 40 51

2. UNITED BANK OF ALBANIA (JOINT-STOCK COMPANY)
   Licence No. 3/1998, dated 11.01.1999
   Certificate No. 3 “On Deposit Insurance”.
   Director: Abdul Waheed ALAVI
   Address: Rruga e Durrësit, Godina 14 katëshe Teknopjekt, Tirana, Albania
   Tel.: 222 84 60, 222 38 73, 222 74 08
   Fax: 222 84 60, 222 83 87

3. ITALIAN BANK OF DEVELOPMENT (BANCA ITALIANA DI SVILUPPO)
   Licence No. 5/1998, dated 11.01.1999
   Director: Libero CATALANO
   Address: Bulevardi “Dëshmorët e Kombit”, Ndërtesa Kullat Binjake, Tirana
   Tel.: 228 03 51 / 2 / 3 / 4 / 5
   Fax: 228 03 56

4. NATIONAL COMMERCIAL BANK (JOINT-STOCK COMPANY)
   Licence No. 6/1998, dated 11.01.1999
   Certificate No. 5 “On Deposit Insurance”.
   Director: Seyhan PENCAPlIgIL
   Address: Bulevardi “Zhan D’Ark”, Tirana, Albania
   Tel.: 225 09 55
   Fax.: 225 09 56

5. TIRANA BANK (JOINT-STOCK COMPANY)
   Licence No. 07, dated 12.09.1996
   Certificate No. 6 “On Deposit Insurance”.
   Director: Dimitrios SANTIXIS
   Address: Rruga “Dëshmorët e 4 Shkurtit”, Tirana, Albania
   Tel.: 226 96 16/7/8; 223 34 41/42/43/44/45/46/47
   Fax.: 223 34 17

* As of December 31, 2009.
6. NATIONAL BANK OF GREECE (JOINT-STOCK COMPANY) – TIRANA BRANCH
Licence No. 08, dated 25.11.1996
Approved by the Supervisory Council Decision of the Bank of Albania No. 4, dated 14.03.1996.
Certificate No. 7 “On Deposit Insurance”.
Director: Ioannis KOUGIONAS
Address: Rruga “Durrësit”, Godina Comfort, Tirana, Albania
Tel.: 227 48 02; 227 48 22
Fax.: 223 36 13

7. INTERNATIONAL COMMERCIAL BANK (JOINT-STOCK COMPANY)
Licence No.09, dated 20.02.1997
Certificate No. 8 “On Deposit Insurance”.
Director: Mahendra Sing RAWAT
Address: Qendra e Biznesit, Rruga “Murat Toptani”, Tirana, Albania
Tel.: 225 43 72 / 225 62 54
Fax.: 225 43 68

8. ALPHA BANK (JOINT-STOCK COMPANY) – ALBANIA
Licence No.10, dated 07.01.1998
Certificate No. 9 “On Deposit Insurance”.
Director: Andreas GALATOULAS
Address: Rruga e Kavajës, G – KAM Business Center, Kati II, Tirana, Albania
Tel.: 223 35 32; 223 33 59; 234 04 76/77
Fax.: 223 21 02

9. INTESA SANPAOLO BANK ALBANIA (JOINT-STOCK COMPANY)
Licence No.11, dated 10.08.1998
Certificate No. 10 “On Deposit Insurance”.
Director: Stefano FARABBI
Address: Rruga “Ismail Qemali”, Nr. 27, P. O. Box 8319, Tirana, Albania
Tel.: 224 87 53/4/5/6
Fax.: 224 87 62

10. PROREDIT BANK (JOINT-STOCK COMPANY)
Licence No. 12, dated 15.03.1999
Approved by the Supervisory Council Decision of the Bank of Albania No. 22, dated 03.03.1999.
Certificate No. 11 “On Deposit Insurance”.
Deputy Director: Borislav KOSTADINOV
Address: Rruga “Sami Frashëri”, Tirana e Re, P. O. Box. 2395, Tirana, Albania
Tel.: 227 12 72//4/5
Fax.: 227 12 76

11. EMPORIKI BANK OF ALBANIA (JOINT-STOCK COMPANY)
Licence No. 14, dated 28.10.1999
Certificate No. 13 “On Deposit Insurance”.
Director: George CARACOSTAS
Address: Rruga “Kavajës”, Tirana Tower, Tirana, Albania
Tel.: 225 87 55/ 56/ 57/ 58/ 59/ 60
Fax.: 225 87 52

12. CREDIT BANK OF ALBANIA (JOINT-STOCK COMPANY)
Licence No. 15, dated 28.08.2002
Certificate No. 14 “On Deposit Insurance”.
Director: Kamal Abdel MONÉIM
Address: Rruga “Perlat Rexhepi”, Al-Kharafi Group Administration Building, Kati 1&2, Tirana, Albania
Tel.: 227 21 68, 227 21 62
Fax.: 227 21 62

13. CREDINS BANK (JOINT-STOCK COMPANY)
Licence No. 16, dated 31.03.2003
Certificate No. 15 “On Deposit Insurance”.
Director: Artan SANTO
Address: Rruga “Ismail Qemali”, Nr. 21, Tirana, Albania
Tel.: 222 29 16, 223 40 96
Fax.: 222 29 16

14. POPULAR BANK (JOINT-STOCK COMPANY)
Licence No. 17, dated 16.02.2004
Certificate No. 16 “On Deposit Insurance”.
Director: Henri Maus de ROLLEY
Address: Bulevardi “Dëshmorët e Kombit”, Ndërtesa Kullat Binjake, Kulla 1, Kati 9, Tirana, Albania
Tel.: 227 27 88 / 89 / 90 / 91
Fax.: 227 27 81; 228 04 41

15. UNION BANK (JOINT-STOCK COMPANY)
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: 225 06 53; 225 80 81
Fax.: 225 06 54; 227 28 80

16. FIRST INVESTMENT BANK (JOINT-STOCK COMPANY)
Licence No. 13, dated 16.04.1999
Approved by the Supervisory Council Decision of the Bank of Albania No. 35, dated 27.06.2007.
Director: Bozhidar TODOROV
Address: Bulevardi “Dëshmorët e Kombit”, Kullat Binjake, Kulla 2, Kati 14, Tirana, Albania
Tel.: 225 64 23/4; 228 02 10
Fax.: 225 64 22
In addition to banks and branches of foreign banks, the Bank of Albania has as of 31 December 2009 licensed the following entities**:

<table>
<thead>
<tr>
<th>NO.</th>
<th>ENTITIES</th>
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<tr>
<td>13</td>
<td>NON-BANK INSTITUTIONS</td>
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<td>FOREIGN EXCHANGE BUREAUS</td>
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<td>UNIONS OF SAVINGS AND CREDIT ASSOCIATIONS</td>
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<td>135</td>
<td>SAVINGS AND CREDIT ASSOCIATIONS</td>
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<tr>
<td>1</td>
<td>REPRESENTATIVE OFFICES OF FOREIGN BANKS</td>
</tr>
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</table>
PUBLICATIONS ISSUED BY THE BANK OF ALBANIA SINCE 2008

This list was designed to inform readers about publications issued by the Bank of Albania since 2008. 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) 2223 558. 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 from January 2008 till August 2009. This list does not include periodical surveys carried out by the Bank of Albania as they are available only online (http://www.bankofalbania.org/web/survey_3405_2.php).

ANNUAL REPORT:
Annual Report 2007
Annual Report 2008

MONETARY POLICY PERIODICAL REPORTS:
 Monetary Policy Report for the First Quarter of 2008
 Monetary Policy Report for the Third Quarter of 2008
 Monetary Policy Statement for the First Half of 2008
 Monetary Policy Statement for the Second Half of 2008
 Monetary Policy Report for the First Quarter of 2009
 Monetary Policy Statement for the First Half of 2009
 Monetary Policy Document for 2008
 Monetary Policy Document for the 2009 - 2011 Period

PUBLICATIONS ON STATISTICS:
 Statistical Report (Published monthly)
 Balance of Payments Bulletin 2007
 Balance of Payments Bulletin 2008

OFFICIAL BULLETIN:
Official Bulletin - Volume 10, no.1 Year 2008
Official Bulletin - Volume 10, no.2 Year 2008
Official Bulletin - Volume 10, no.3 Year 2008
Official Bulletin - Volume 10, no.4 Year 2008
Official Bulletin - Volume 10, no.5 Year 2008
Official Bulletin - Volume 10, no.6 Year 2008
Official Bulletin - Volume 10, no.7 Year 2008
ECONOMIC BULLETIN:
Economic Bulletin - Volume 11, no.1 Year 2008
Economic Bulletin - Volume 11, no.2 Year 2008
Economic Bulletin - Volume 11, no.3 Year 2008
Economic Bulletin - Volume 11, no.4 Year 2008
Economic Bulletin - Volume 12, no.1 Year 2009
Economic Bulletin - Volume 12, no.2 Year 2009
Economic Bulletin - Volume 12, no.3 Year 2009

FINANCIAL STABILITY REPORT:
Financial Stability Report 2007
Financial Stability Report 2008

SUPERVISION ANNUAL REPORT:
Supervision Annual Report 2007
Supervision Annual Report 2008

INFORMATIVE PUBLICATIONS:
Publications Catalogue:
Publications Catalogue 2007
Publications Catalogue 2008

WORKING PAPERS:
Index of Foreign Prices/Unit Values of Albanian Imports
Exchange Rate Pass-Through in Albania
Measuring Import and Export Functions in Albania
New Core Inflation Measures: Their Usage in Forecasts and Analysis
The Role of Exchange Rate in an IT Framework, What do we do?
An Estimation of Balassa-Samuelson: Effect in Albania
Role of Banks in the Monetary Policy Transmission in Albania
Albanian Current Account Deficit: Does it Possess Mean Reverting Properties?
Monetary Policy Strategies for Small Economies - Editor, Ardian Fullani
Alternative Methods of Estimating Potential Output in Albania

SCIENTIFIC NOVELTIES AT THE BANK OF ALBANIA:
Scientific Novelties at the Bank of Albania No.1
Scientific Novelties at the Bank of Albania No.2

LEGAL PUBLICATIONS:

EDUCATIONAL PUBLICATIONS:
A Guide to Your First Bank Account*
Students’ Financial Guidebook*
Story of Ice-Cream (Reprint)*
Speaking Simply about Inflation (Reprint)*
Banknotes Withdrawal from Circulation (Leaflet)*
“The Real Value of Money”*
Bank of Albania - Our Central Bank
IBAN - The International Bank Account Number (Leaflet)*
Bank of Albania’s Monetary Policy Instruments and Procedures for their Execution (Reprint)*
Payments System (Reprint)*
“The Real Value of Money”, Vlorë, 2008*
Education - The New Challenge of the Bank of Albania