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1 GOVERNOR’S SPEECH

The Albanian economy has been characterized by positive development tendencies over the last years, expressed in stable growth rates, in the constant improvement of macroeconomic stability and in the gradual approximation of our economy structure to the developed economies’ ones. The structural reforms and the stability of macroeconomic indicators have sustained the economic potential of the private sector by generating stable economic growth rates at the level of 5-6 per cent.

This course of development was also maintained over the second semester of 2006. According to producer and consumer indices, the performance of economy was in line with the country’s economic development. The improvement of the economic situation in the Euro area and the holding back of the oil price rise have favoured the performance of the Albanian economy. Considering the third quarter developments and the trends observed over the fourth quarter, it is concluded that the situation of production continued to be satisfactory and was generally in line with the projections. Unlike the first semester developments, the fiscal balance recorded a deficit over the second semester of 2006, as a consequence of the budget expenditure acceleration. The external sector of economy displayed signs of improvement, manifested in the slight reduction of current deficit. Foreign exchange market developments have pursued the international market performance, causing the domestic macroeconomic balance not to be jeopardized.

Domestic demand has remained in proper levels to sustain the economic growth, while the seasonal growth effect of demand over the consumer prices was more moderate in December compared to the previous years. The recurrent energy supply shortages over the second half of December makes up a new occurrence. The same shortages over the first month of 2007 lay down the necessity of a complete analysis, in order to reach into reliable conclusions on the possible negative effects, be they direct or indirect. The Bank of Albania deems as necessary the taking of concrete steps in finding alternative sources of energy, in order to minimise our country’s great dependence on the atmospheric conditions. The Bank of Albania believes that the chronic recurrence of similar crises would convert this issue into a permanent factor, which would as a consequence affect the production or service costs.

As far as the previous year’s economic activity is concerned, based on the available statistical information, it is assessed that the performance of
production over 2006, according to the economic enterprises’ sales index, was satisfactory. In annual terms, the sales’ growth rate was about 11 per cent over the first nine months, being close to the average growth rate of the last five years. The data on production signal that the sector of industry is displaying great signs of recovery, observed in particular in the processing industry. The latter grew under rapid rates over 2006, recording one of the highest rates of sectoral growth, by 27 per cent, in the third quarter of the year. Trade sector continues to grow rapidly. It has constantly recorded high annual growth rates, providing at the same time the highest contribution to the growth of sales in economy. Despite the annual positive growth in the third quarter, the sector of construction displayed signs of slowdown compared to the previous years. An economic slowdown was also observed in the sector of transport, while telecommunication services and other services have recorded growth over the second semester of 2006, both in annual and quarterly terms.

Labour market recorded the same figures as in the two previous quarters over the third quarter of 2006. Unemployment rate reached 13.8 per cent, while there has been a shift of employed from the public sector to the private non-agricultural sector.

Consumer prices inflation over the second semester of 2006 was close to the Bank of Albania objective, fluctuating to the low tolerance interval. On average, consumer prices rose by 2.7 per cent over the second semester, while the average annual inflation reached 2.4 per cent. The fact that the average annual inflation has fluctuated to around 2-3 per cent in the last four years indicates that inflation has now been stabilized in constant and relaxing levels for the performance of the Albanian economy. The profile of the rise of prices over the second semester was dominated by the energy price rise. Its annual rise by 13.7 per cent was also accompanied by the rise of rent prices, in particular over September and October. “Alcoholic beverages and tobacco” group also exerted pressure on the increase of inflation, as a result of the excises rise in September. The balancing effect over this period was provided by foodstuffs, the prices of which fell over September and October and recorded low positive rates in the other months. Worth emphasizing is that the consumer price rise remains under control and close to the targeted level of the Bank of Albania, even if we would exclude the administered prices’ effect.

In general, the budget deficit financing through the domestic borrowing was low over the second semester of 2006. Government demand for monetary assets has provided a controlled influence on the expansion of monetary sources. The fiscal indicators have been within the projected amounts for this period, even under revised figures. In this context, the fiscal policy has not infringed the preservation of macroeconomic balances.

Current account developments until the third quarter of 2006 indicate an intensive activity of the external sector of economy. The volume of current account transactions reached EUR 5 billion over the first nine months, which is 17 per cent higher than the same period the previous year. Current transfers,
as in the previous years, were shaped by workers’ remittances. The latter represent one of the main sources of deficit financing in the trade in goods and services. Over the first nine months of 2006, they were estimated at EUR 683 million or EUR 24 million more than the same period the previous year. This mitigating tendency requires a prudent monitoring and proper measures to be taken for the generation of more stable foreign currency sources in a longer term perspective.

In response to these economic developments, the Bank of Albania has pursued a prudent monetary policy, aiming at balancing the financial incentive of economy with the need of maintaining monetary stability and controlling the inflationary pressures on economy. The economic and financial developments generated focal challenges for the formulation and implementation of monetary policy over the second semester of 2006. The inflationary pressures over this period mainly originated from the shocks of supply; however, the component of demand began to constitute an important factor in the setting of inflation rate. The latter has been ever-increasingly influenced by the banking system boomed crediting over the last three years, sustaining the increase of business investment and consumption.

In order to precede the generation of inflationary pressures and their manifestation in the expectations of economy, the Bank of Albania raised the cost of money in economy. This raise occurred in July and November and brought about the increase of the core interest rate from 5.0 to 5.5 per cent. The increase of the cost of money aimed at keeping appropriate monetary conditions for guaranteeing price stability in the long-term. The ridimensioning of incentives for consumption and saving in economy and the reassessment of the exchange rate sustaining factors will allow the maintenance of price stability over the coming months within the parameters set out by the Bank of Albania. Moreover, the tightening of monetary conditions is in line with the monetary policy pursued by large central banks and with the increase of interest rates in the international foreign currency markets. Following the tightening signals, the interest rates in the money market have been increasing over this period.

The monetary developments in the second semester of 2006 were conditioned by the gradual growth of Government demand for monetary assets. In response, money supply growth rate increased to 12.7 per cent in November, compared to 9.7 per cent in June. However, the current rates of monetary aggregates’ annual expansion are evidently lower than the rate of 17-18 per cent of the last two years. Moreover, the gradual reduction of the share of currency in circulation favours the monetization of economy, the increase of the financial intermediation level and of the banking system role.

Credit to economy remains the main contributor to the growth of monetary assets in economy. It continued to record a rapid growth over the second semester of 2006. The banking system credit portfolio to economy amounted to ALL 179.5 billion in November 2006, accounting for 28.1 per cent of the economy monetary assets. In relation to the gross domestic production, this
portfolio stands in the highest historical level of the last ten years, - 20.1 per cent.

However, the annual expansion rate of credit to economy has decreased in relative terms, declining from 67.1 per cent in June to 57.8 per cent in November. The growth rate slowdown came as a result of the high credit level for a two-year period, of some market segments satisfaction and of the Bank of Albania signalling for the tightening of regulative measures which control the portfolio quality. The Bank of Albania expects the application of this regulative set over 2007 to contribute to the control of credit expansion rate, in line with the country’s macroeconomic stability in the long run.

The Bank of Albania remains an accountable and transparent institution. The legal commitment for the maintenance of price stability and the institutional motivation for boosting and developing the financial markets are at the heart of the Bank of Albania tasks. In this context, the Bank of Albania has formulated and approved its policy and operational framework for 2007, finalized in the Monetary Policy Document and the Monetary Programme for 2007. Both these documents clearly outline our strategic objectives related to the economic and financial stability in the country.

The Bank of Albania deems that the country’s economic and financial development objectives for 2007 are realistic. However, they impose their prudent pursuit by the responsible institutions, in particular in the field of structural reforms in economy, and a sound coordination of the macroeconomic policies.

2 ECONOMIC DEVELOPMENTS OVER THE SECOND SEMESTER

2.1 WORLD ECONOMY

World economy continued to record positive developments over the second semester of 2006. The growth impulse generated by the Asian economies, in particular from China and India, continued to be strong, while the USA economy displayed signs of economic slowdown. The economic developments in the Euro area and Japan signal an improvement of the economic situation. In a general view, it is assessed that the world economy growth will somehow slow down in the coming period; however, the growth rates will continue to remain in satisfactory levels.

The rise of the oil and by-products price has increased the inflationary pressures on most economies. However, both the direct and secondary effects were limited. The effect of the high oil price on core inflation was moderate over 2006 in most countries. The tightening monetary policy pursued by many central banks has played a key role in the prices performance. The actualization of the monetary policy tightening effects and the dropping of oil
price over fall 2006 are expected to contribute to the reduction of inflationary pressures in the coming period.

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<th>GDP annual growth, Q3</th>
<th>Unemployment rate</th>
<th>Consumer prices inflation, November 2006</th>
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</thead>
<tbody>
<tr>
<td>USA</td>
<td>+3.0</td>
<td>4.5 (December)</td>
<td>2.0</td>
</tr>
<tr>
<td>Euro area</td>
<td>+2.7</td>
<td>7.6 (November)</td>
<td>1.9</td>
</tr>
<tr>
<td>Germany</td>
<td>+2.3</td>
<td>8 (November)</td>
<td>1.5</td>
</tr>
<tr>
<td>France</td>
<td>+1.9</td>
<td>8.6 (November)</td>
<td>1.6</td>
</tr>
<tr>
<td>Italy</td>
<td>+1.9*</td>
<td>6.9 (June)</td>
<td>2.0</td>
</tr>
<tr>
<td>Japan</td>
<td>+1.0</td>
<td>4.0 (November)</td>
<td>0.3</td>
</tr>
</tbody>
</table>

* Second quarter

Source: Eurostat; Bureau of Economic Research; Bureau of Labour Statistics; ECB, Report for December

**Euro area Economy**

According to the preliminary data provided by the Eurostat, the Euro area annual real growth for the third quarter of 2006 was 2.7 per cent. Although the growth rate was not as high as over the first semester of 2006, the economic developments are considered satisfactory and extensive. Domestic demand was the impelling force of the economic activity for the third quarter. Its contribution to annual growth marked 0.6 percentage points. The contribution of net exports, which reflects the developments in external demand, was negative. Various surveys and the industry and services confidence indices signal that the economic developments in the Euro area are assessed as stable. Despite the fact that not all the indicators have grown under the same rate, the growth rates are above their historical average.

The Euro area labour market has recorded positive developments throughout 2006. The increase of the employment rate continued to be high over the third quarter of 2006, while the unemployment rate stabilized over November to the lowest rate of the last ten years. There are positive expectations for the coming quarter, based on the projection for stable growth in employment in the short run.

Harmonized index of consumer prices inflation fluctuated to the average rate of 2.2 per cent over 2006. The developments in the oil and its by-products’ price have defined the course of total inflation over most of the year. Meanwhile, production prices performance continues to show inflationary pressures, as a result of the past oil and other goods’ price rise. Labour cost pressures remain limited.

In its meeting in December, the Governing Council of the ECB decided to increase the core interest rate by 0.25 percentage points to 3.5 per cent.
The Council took this decision in order to avoid upside risks to price stability over the medium term. According to the ECB, the Euro area monetary policy continues to be accommodative, with the interest rates remaining at low levels, strong credit growth and liquidity ample by all plausible measures.

**USA Economy**

The high growth rate of the USA economy has displayed signs of slowdown over 2006. Annual real growth of gross domestic production was 3 per cent over the third quarter. This was the lowest rate recorded since the third quarter of 2003. The main reason behind this downward tendency relates to the dropping of residents’ investment by about 8 per cent. The negative effect of the apartments’ market is expected to be partly balanced by the growth of corporations’ investment. The business situation remains sound, suggesting for a positive climate in the following periods.

After the continuous deepening over the first months of the year, trade balance deficit has been narrowing since September. In November, it amounted to USD 58.2 billion. The increase of exports and the decrease of imports supported by the oil price falling and by the limitation of the imported quantity, have contributed to the trade balance improvement.

The high level of the use of sources in the American economy may favour the inflationary pressures. However, the control of the oil price rise, the expectations for moderate inflation rates and the accumulated effect of monetary policy operations have held the domestic demand back, being reflected in a downward tendency of consumer prices inflation. After August, which recorded a peak inflation rate of 3.8 per cent in annual terms, this indicator has been marking continuous decrease. In November, annual inflation marked 2.0 per cent. In its last meeting on 12 December 2006, the FOMC decided to leave the core interest rate unchanged at 5.25 per cent.

**Exchange Rate**

In the last months of 2006, the Euro area currency appreciated against the USD, following some period of several months’ stability in the spot exchange rate. The USD also depreciated against the British Pound and the Japanese Yen over the last months of 2006. The signals for a slowdown in the USA economic activity and for stable growth rates in the Euro area seem to have affected the international markets expectations, influencing on the depreciation of the USD against the EUR and the USA’s main trade partner countries’ currencies.

**Oil price**

Oil price reached peak levels over summer 2006. At the beginning of August, oil price reached USD 78 per barrel. The considerable price rise came as a consequence of the panic deriving from the possible reduction of
production by the oil exporting countries following the intensified geopolitical tension over this period. Oil price has considerably fallen over the last months, mainly because some of the factors affecting the price rise over summer did neither actualize, nor had the expected effect. The high inventories level, the decrease of demand for oil and the slowdown of the American economic activity were all reflected in the decline of demand for this product. Oil price over the last two months of the year was also influenced by the favourable atmospheric conditions, leading to the reduction of demand for fuels.

However, OPEC countries have clearly indicated that they will try to keep the oil and its by-products’ price in high levels. At the end of October, OPEC decided to reduce production by 1.2 million barrels per day. This is the first decision since 2003, which concludes for a reduction of production.

2.2 ALBANIAN ECONOMY OVER THE SECOND SEMESTER OF 2006

The Albanian economy was generally characterized by positive developments over the second semester, both in the real sector and in the other sectors of economy. Economic growth is assessed to have marked satisfactory levels, while production and consumer prices have recorded a moderate growth. Unlike the first semester, fiscal balance recorded a deficit over October and November, as a result of the budget expenditure acceleration. Domestic foreign currency market recorded an appreciation of the lek against the American dollar and a stable performance of the lek against the euro. Oil price fall in the international market was reflected in the fall of domestic market oil price, though not under the same rates. The seasonal rise of consumer prices over December was manifested less than over the previous years. The influence of the aggravated energy situation over the performance of production over the end of 2006 and the beginning of 2007 is to be assessed in the future. The economic growth over 2006 was impelled by the performance of some key sectors of the economic activity, such as construction, industry and services.

<table>
<thead>
<tr>
<th>Table 2 Economic growth by sectors of production for 2005-2006*</th>
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<td></td>
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<tr>
<td>Agriculture</td>
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<tr>
<td>Industry</td>
</tr>
<tr>
<td>Construction</td>
</tr>
<tr>
<td>Transport</td>
</tr>
<tr>
<td>Services</td>
</tr>
<tr>
<td>GDP</td>
</tr>
</tbody>
</table>

Source: Ministry of Finance and Bank of Albania estimates
*Preliminary data
According to the sales index, the sector of industry, the sector of hotels and restaurants and other services have recorded the highest annual growth rates over the third quarter of 2006. The sector of construction and that of telecommunication have recorded positive annual growth rates over the same quarter, marking a return from the negative growth rates of the second quarter.

The general economic enterprises sales index had an annual growth of 12.4 per cent over the third quarter, which is higher than the previous quarter, but lower than the average annual growth level since the early 2005.

Based on the performance of some domestic demand and investment indicators, it is assessed that by the end of the third quarter of 2006, demand remained in satisfactory levels, while investment recorded low levels.

### Table 3 Annual growth of sales in some sectors of economy¹ (in percentage)

<table>
<thead>
<tr>
<th>Sector</th>
<th>Q1 - 06</th>
<th>Q2 - 06</th>
<th>Q3 - 06</th>
<th>Share</th>
<th>Contribution</th>
</tr>
</thead>
<tbody>
<tr>
<td>Industry</td>
<td>22.9</td>
<td>3.4</td>
<td>19.9</td>
<td>24.5</td>
<td>4.6</td>
</tr>
<tr>
<td>Extracting industry</td>
<td>34.2</td>
<td>5.8</td>
<td>28.4</td>
<td>2.1</td>
<td>0.5</td>
</tr>
<tr>
<td>Processing industry</td>
<td>24.3</td>
<td>7.2</td>
<td>26.6</td>
<td>17.4</td>
<td>4.1</td>
</tr>
<tr>
<td>Electricity, water and gas</td>
<td>17.7</td>
<td>-7.5</td>
<td>-1.3</td>
<td>5.0</td>
<td>-0.1</td>
</tr>
<tr>
<td>Construction</td>
<td>5.8</td>
<td>-1.1</td>
<td>6.8</td>
<td>14.2</td>
<td>1.0</td>
</tr>
<tr>
<td>Trade</td>
<td>17.4</td>
<td>9.5</td>
<td>9.5</td>
<td>44.5</td>
<td>4.3</td>
</tr>
<tr>
<td>Hotels and restaurants</td>
<td>48.0</td>
<td>33.4</td>
<td>17.4</td>
<td>0.7</td>
<td>0.1</td>
</tr>
<tr>
<td>Transport</td>
<td>-2.3</td>
<td>-16.9</td>
<td>-3.7</td>
<td>3.0</td>
<td>-0.1</td>
</tr>
<tr>
<td>Telecommunication</td>
<td>21.4</td>
<td>-7.2</td>
<td>11.4</td>
<td>7.3</td>
<td>0.8</td>
</tr>
<tr>
<td>Other services</td>
<td>31.7</td>
<td>26.3</td>
<td>33.6</td>
<td>5.7</td>
<td>1.6</td>
</tr>
<tr>
<td>Total economy</td>
<td>17.9</td>
<td>5.1</td>
<td>12.4</td>
<td>100</td>
<td>12.4</td>
</tr>
</tbody>
</table>

Source: INSTAT, Economy sales index, Bank of Albania estimates

### Table 4 Performance of some indicators of domestic demand and investment over the third quarter of 2006

<table>
<thead>
<tr>
<th>Item</th>
<th>Annual change (in %)</th>
<th>Quarterly change (in %)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Fuels consumption</td>
<td>57</td>
<td>51</td>
</tr>
<tr>
<td>Import of vehicles</td>
<td>37</td>
<td>77</td>
</tr>
<tr>
<td>Import of TVs</td>
<td>131</td>
<td>36</td>
</tr>
<tr>
<td>Import of washing machines</td>
<td>10</td>
<td>27</td>
</tr>
<tr>
<td>Import of machinery and equipment</td>
<td>-15</td>
<td>-11</td>
</tr>
<tr>
<td>Cement consumption</td>
<td>3</td>
<td>19</td>
</tr>
</tbody>
</table>

Source: INSTAT, Conjecture, third quarter, 2006

#### 2.2.1 Performance of economy by sectors

**Sector of industry and electricity**

Following the slowdown in the second quarter of 2006, the activity of the sector of industry grew by 20 per cent in the third quarter of the same
year, mainly as a result of the growth in the processing industry. The growth recorded in this sub-sector was pushed by the vitalization of the metallurgy and the materials processing activity over the third quarter. Processing industry has recorded the highest contribution of the last four years to the Albanian economy. The great performance of this industry was also accompanied by the increase in the number of employed. On the other hand, extracting industry has made a lower contribution to the general annual economic growth over the third quarter, despite the high annual growth compared to the previous quarter. The increase of sales in the sub-sector of energy, water and gas has been decreasing over 2006, making a negative contribution to the sales of economy over the third quarter by 0.3 percentage points.

Table 5 Main indicators of electricity balance sheet (in GWh)

<table>
<thead>
<tr>
<th></th>
<th>S1 ’06</th>
<th>July-November ’05</th>
<th>July-November ’06</th>
<th>Annual change (in %)</th>
</tr>
</thead>
<tbody>
<tr>
<td>I. SOURCE (a+b+c-d)</td>
<td>3,016</td>
<td>2,084</td>
<td>2,274</td>
<td>9.14</td>
</tr>
<tr>
<td>a. Domestic production</td>
<td>3,056</td>
<td>1,759</td>
<td>1,900</td>
<td>8.00</td>
</tr>
<tr>
<td>b. Exchange balance</td>
<td>12</td>
<td>372</td>
<td>404</td>
<td>8.43</td>
</tr>
<tr>
<td>c. Total production in distribution</td>
<td>67</td>
<td>38</td>
<td>50</td>
<td>30.24</td>
</tr>
<tr>
<td>d. Loss and consumption in transmission</td>
<td>120</td>
<td>86</td>
<td>79</td>
<td>-7.90</td>
</tr>
<tr>
<td>II. USES (e + III)</td>
<td>3,016</td>
<td>2,084</td>
<td>2,274</td>
<td>9.14</td>
</tr>
<tr>
<td>e. Invoiced consumption</td>
<td>1,800</td>
<td>1,401</td>
<td>1,462</td>
<td>4.34</td>
</tr>
<tr>
<td>f. Household consumption</td>
<td>1,111</td>
<td>836</td>
<td>829</td>
<td>-0.81</td>
</tr>
<tr>
<td>g. Non-household consumption</td>
<td>689</td>
<td>566</td>
<td>633</td>
<td>11.94</td>
</tr>
<tr>
<td>III. LOSSES (Uninvoiced consumption)</td>
<td>1,216</td>
<td>682</td>
<td>812</td>
<td>19.01</td>
</tr>
</tbody>
</table>


Compared to the same period the previous year, domestic production of energy increased over July to November 2006, in contrast to the first semester of the year when it recorded a slight decrease. Invoiced consumption marked an annual increase of about 4 per cent, while the largest share of this increase is attributed to the increase of consumption by non-household consumer, by about 12 per cent. The ratio of losses to distributed energy was higher than the same quarter the previous year, but lower than the first semester of 2006. Energy exchange balance for the first five months of the second semester was positive and higher than over the first semester.

Sector of construction

Sales for the sector of construction were about 4 per cent higher over the first nine months of 2006 than the same period the previous year. There was a positive annual growth, although it was relatively low in the first and third quarters of 2006. The statistics on sales indicate that the performance of this sector is less positive than the one projected at the beginning of the year. The construction sales have provided only 4 per cent of the growth in the sales of economy for the nine-month period. Moreover, the cement consumption has increased under slow rates. The accomplishment of the projection for a growth of 10 per cent will strongly depend on the performance of this sector over the last quarter of 2006.
With regard to the expected investment in the sector based on the construction permits statistics, over the first nine months of 2006 there has been a decrease by 3.6 per cent, in annual terms. This figure is a significant indicator for the projection of this sector’s growth in the near future. There has been a considerable decrease in the number of residence construction permits by 14 per cent and an increase by 3.3 per cent in the projected amount for transport infrastructure.

Other services
Trade activity continued to provide a strong impetus to the performance of economy, contributing by about half of total sales over 2006. Following a considerable growth in the first semester of 2006, trade index grew by 9.5 per cent over the third quarter. The sales performance of hotels, café and restaurants was fairly positive for the third quarter of 2006. Transport and telecommunication recorded an annual growth of 6.5 per cent over the third quarter, following its economic slowdown over the second quarter. This growth is attributed to the positive performance of the sector of telecommunication, which contributed by 0.83 percentage points to the growth of sales index over the third quarter of 2006. On the other hand, the growth of this sector over 2006 was less considerable than the one recorded the previous year, despite the vitalization of transport over the third quarter.

Sector of agriculture
According to the projections of the Ministry of Agriculture, Food and Consumer Protection, production in the sector of agriculture is expected to grow by 2.55 per cent over 2006. The lack of final data on production impedes the analysis of its performance. Agro industrial production, which shares about 20 per cent of total agricultural production, is projected to grow by about 6 per cent, while agricultural production by about 1.8 per cent. Agro industry has marked positive developments over the first nine-month period of 2006, recording an annual growth of 9 per cent, despite the slowdown observed over the third quarter of the year. The performance of agricultural production remains to be assessed in the following months.

The growth of agro industrial production over the third quarter of 2006, in particular the processing of fruit and vegetables, has influenced on the increase
of their exports by 54 per cent, compared to the same quarter the previous year. On the other hand, the imports of this group have increased only by 15 per cent. The progress in the ratio of agricultural exports to imports over the third quarter reflects the growth of agricultural production over this part of the year.

2.2.2 Labour market

Labour market over the third quarter of 2006 confirms the revival of the economic activity for this period. The positive developments over this quarter, mainly observed in the sectors of trade, processing industry and construction, added to the mitigation of unemployment. The decrease in the number of unemployed over this period does not entirely correspond with the increase recorded in the number of employed, suggesting that part of the labour supply occurred out of the formal labour market.

The structure of employment over the first three quarters of 2006 was presented similar to the previous year structure. Unemployment rate has been decreasing over the quarters, recording 13.8 per cent in the third quarter, which is the lowest historical rate of the last nine years. At the end September 2006, labour force totalled about 2 thousand people fewer than at the end of the third quarter 2005. Moreover, the total number of employed increased by only about 3 thousand people, while the number of people recorded as unemployed has decreased by about 5 thousand. Over a time-span of a year, public sector labour force has decreased by about 5 thousand people, while the private non-agricultural sector has recorded an increase of the number of employed by about 8 thousand people.

According to the latest data provided by the Ministry of Labour, Social Affairs and Equal Opportunities, the number of unemployed registered in the labour offices by November 2006, was 149.6 thousand people or 2.8 per cent lower than the number recorded at the end 2005. An evident characteristic of the labour market is the fact that long-term unemployed share about 70 per cent of total unemployed in economy.

<table>
<thead>
<tr>
<th></th>
<th>2005</th>
<th>2006</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Q1</td>
<td>Q2</td>
</tr>
<tr>
<td>Total labour force</td>
<td>1,087</td>
<td>1,086</td>
</tr>
<tr>
<td>A. Total employed</td>
<td>931</td>
<td>931</td>
</tr>
<tr>
<td>i) in the public sector</td>
<td>176</td>
<td>176</td>
</tr>
<tr>
<td>ii) in private non-agricultural sector</td>
<td>213</td>
<td>213</td>
</tr>
<tr>
<td>iii) in private agricultural sector</td>
<td>542</td>
<td>542</td>
</tr>
<tr>
<td>B. Unemployment</td>
<td></td>
<td></td>
</tr>
<tr>
<td>i) Total unemployed</td>
<td>156</td>
<td>155</td>
</tr>
<tr>
<td>ii) Unemployment rate (in percentage)</td>
<td>14.3</td>
<td>14.3</td>
</tr>
</tbody>
</table>

Source: INSTAT, September 2006
2.2.3 Fiscal sector

Fiscal indicators have generally been close to the level projected in the supplementary budget over January to November 2006. The most considerable deviation in the fiscal indicators is observed in the budget deficit, resulting from the non-realization of expenditure plan. According to the data provided by the Ministry of Finance, over the first 11 months of 2006 were collected 97.8 per cent of projected revenues and carried out about 92.6 per cent of projected expenditure. As a consequence, budget deficit by the end November was about ALL 1.5 billion from the projected ALL 13.2 billion. Total revenues for January to November 2006, reached the highest level in the last seven years in relation to the Gross Domestic Production. Meanwhile, budget deficit has been characterized by a downward trend over the recent years, proceeded over 2006 as well.

Table 7 Main fiscal indicators as a share to GDP (in percentage)

<table>
<thead>
<tr>
<th></th>
<th>11M-99</th>
<th>11M-00</th>
<th>11M-01</th>
<th>11M-02</th>
<th>11M-03</th>
<th>11M-04</th>
<th>11M-05</th>
<th>11M-06</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total revenues</td>
<td>20.2</td>
<td>20.7</td>
<td>19.7</td>
<td>21.2</td>
<td>22.0</td>
<td>21.8</td>
<td>21.7</td>
<td>24.4</td>
</tr>
<tr>
<td>Tax revenues</td>
<td>12.6</td>
<td>14.5</td>
<td>13.3</td>
<td>14.8</td>
<td>19.5</td>
<td>19.7</td>
<td>19.6</td>
<td>22.2</td>
</tr>
<tr>
<td>Total expenditure</td>
<td>29.5</td>
<td>27.7</td>
<td>25.5</td>
<td>26.3</td>
<td>25.8</td>
<td>25.1</td>
<td>23.7</td>
<td>24.5</td>
</tr>
<tr>
<td>Current expenditure</td>
<td>24.3</td>
<td>22.4</td>
<td>19.8</td>
<td>21.6</td>
<td>22.1</td>
<td>21.2</td>
<td>20.3</td>
<td>20.5</td>
</tr>
<tr>
<td>Capital expenditure</td>
<td>5.2</td>
<td>5.1</td>
<td>5.5</td>
<td>4.7</td>
<td>3.7</td>
<td>3.9</td>
<td>3.4</td>
<td>4.0</td>
</tr>
<tr>
<td>Deficit</td>
<td>(9.4)</td>
<td>(6.9)</td>
<td>(5.9)</td>
<td>(5.1)</td>
<td>(3.8)</td>
<td>(3.3)</td>
<td>(2.0)</td>
<td>(0.2)</td>
</tr>
<tr>
<td>Domestic financing</td>
<td>3.8</td>
<td>4.2</td>
<td>3.2</td>
<td>2.2</td>
<td>2.9</td>
<td>2.6</td>
<td>1.4</td>
<td>(0.7)</td>
</tr>
<tr>
<td>Foreign financing</td>
<td>5.6</td>
<td>2.7</td>
<td>2.6</td>
<td>2.9</td>
<td>0.9</td>
<td>0.7</td>
<td>0.5</td>
<td>0.9</td>
</tr>
</tbody>
</table>

Source: Ministry of Finance and Bank of Albania statistics

Compared to the same period the previous year, revenues and expenditure have increased by 12 and 3.5 per cent, respectively. Over the first months of 2006 was observed a considerable contraction of expenditure. This period was accompanied by their gradual acceleration over the following months. Budget deficit was until November mainly covered by foreign financing. The latter was carried out at 164 per cent of the projection\(^4\).

Table 8 Annual growth rates of main fiscal indicators (in percentage)

<table>
<thead>
<tr>
<th></th>
<th>11M-00</th>
<th>11M-01</th>
<th>11M-02</th>
<th>11M-03</th>
<th>11M-04</th>
<th>11M-05</th>
<th>11M-06</th>
<th>Average 99-05</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total revenues</td>
<td>14.3</td>
<td>5.7</td>
<td>15.7</td>
<td>12.8</td>
<td>11.3</td>
<td>9.3</td>
<td>12.0</td>
<td>12.1</td>
</tr>
<tr>
<td>Tax revenues</td>
<td>28.8</td>
<td>1.8</td>
<td>19.7</td>
<td>43.2</td>
<td>13.2</td>
<td>9.0</td>
<td>14.4</td>
<td>18.5</td>
</tr>
<tr>
<td>Local government revenues</td>
<td>57.9</td>
<td>39.7</td>
<td>32.0</td>
<td>252.1</td>
<td>13.3</td>
<td>16.0</td>
<td>(6.5)</td>
<td>60.7</td>
</tr>
<tr>
<td>Independent budget revenues</td>
<td>10.7</td>
<td>3.3</td>
<td>23.1</td>
<td>11.5</td>
<td>12.7</td>
<td>10.6</td>
<td>10.2</td>
<td>12.4</td>
</tr>
<tr>
<td>Non-tax revenues</td>
<td>(26.2)</td>
<td>29.5</td>
<td>(9.3)</td>
<td>(6.6)</td>
<td>(10.4)</td>
<td>(6.7)</td>
<td>(2.1)</td>
<td>(1.5)</td>
</tr>
<tr>
<td>Total expenditure</td>
<td>4.3</td>
<td>2.7</td>
<td>10.4</td>
<td>6.8</td>
<td>9.1</td>
<td>3.7</td>
<td>3.5</td>
<td>7.5</td>
</tr>
<tr>
<td>Current expenditure</td>
<td>3.0</td>
<td>(1.9)</td>
<td>17.1</td>
<td>11.5</td>
<td>7.4</td>
<td>5.0</td>
<td>1.3</td>
<td>7.4</td>
</tr>
<tr>
<td>Capital expenditure</td>
<td>9.1</td>
<td>21.1</td>
<td>(8.6)</td>
<td>(15.1)</td>
<td>19.9</td>
<td>(3.7)</td>
<td>16.6</td>
<td>10.4</td>
</tr>
<tr>
<td>Deficit</td>
<td>(17.4)</td>
<td>(6.0)</td>
<td>(7.1)</td>
<td>(18.6)</td>
<td>(3.3)</td>
<td>(34.2)</td>
<td>(91.0)</td>
<td>(10.1)</td>
</tr>
<tr>
<td>Domestic financing</td>
<td>24.9</td>
<td>(14.7)</td>
<td>(27.7)</td>
<td>43.5</td>
<td>1.3</td>
<td>(39.1)</td>
<td>(148.5)</td>
<td>(3.0)</td>
</tr>
<tr>
<td>Foreign financing</td>
<td>(45.9)</td>
<td>7.5</td>
<td>18.1</td>
<td>(65.3)</td>
<td>(17.8)</td>
<td>(15.6)</td>
<td>68.5</td>
<td>(10.8)</td>
</tr>
</tbody>
</table>

Source: Ministry of Finance

Budget revenues

Budget revenues, over January to November 2006, were about 12 per cent higher compared to the same period the previous year. The level of tax revenues at the end November amounted to about ALL 186 billion, out of
which tax collected by the customs totalled about ALL 12.9 billion, realizing the projected budget level by 99.2 and 99.6 per cent, respectively. Among the main indicators of tax revenues, it is observed that revenues from the independent budget have increased by 10.2 per cent compared to the same period over 2005, realizing the budget plan at 103.6 per cent. While, revenues from the local government and non-tax revenues decreased by 6.5 and 2.1 per cent, respectively, compared to the previous year.

Tax revenues continue to constitute the main source of budget revenues, accounting for about 92 per cent of total revenues. Tax on profit revenues, value added tax revenues and excises revenues provided the main contribution to the realization of tax plan. Compared to the same period the previous year, they increased by 20.4, 14.9 and 23.5 per cent, respectively. Tax on personal income and customs tax provided 13.9 and 6.2 per cent, respectively, more than over 2005. Meanwhile, non-tax revenues decreased by 2.1 per cent, realizing 86 per cent of the projection for this period.

| Table 9 Main indicators of budget revenues (in billions of ALL, progressive data) |
|---------------------------------|-----|-----|-----|-----|-----|-----|-----|-----|
|                                 | July| August| September| October| November| 11 M Plan, in %| Annual plan, in %|
| Total revenues                  | 125.2| 143.4| 162.3| 182.1| 202.5| 97.8| 88.1|
| Tax revenues                    | 114.0| 131.2| 149.2| 168.1| 186.1| 99.2| 89.7|
| Value added tax                | 39.3| 45.7| 52.4| 59.6| 67.1| 98.5| 88.3|
| Tax on profit                   | 13.2| 14.9| 16.7| 18.6| 20.5| 106.0| 97.8|
| Excises                         | 11.8| 14.2| 16.5| 18.7| 20.9| 97.5| 86.5|
| Tax on personal income          | 4.5| 5.2| 5.8| 6.6| 7.3| 91.3| 81.0|
| Customs duties                  | 8.2| 9.3| 10.5| 11.7| 12.9| 99.6| 91.1|
| Local government revenues       | 6.7| 7.2| 8.1| 9.2| 9.9| 96.7| 89.2|
| Independent budget revenues     | 22.7| 25.9| 29.2| 32.7| 35.5| 103.6| 95.1|
| Non-tax revenues                | 9.3| 10.2| 11.0| 11.8| 12.6| 85.9| 76.1|

Source: Ministry of Finance, November 2006

Budget expenditure

Budget expenditure for January to November 2006 amounted to ALL 203.9 billion, which is 3.5 per cent higher than over 2005. The growth rate of budget expenditure for this period was nearly half the average growth of the last seven years. Personnel expenditure, which account for about 29 per cent of current expenditure, were realized at 96 per cent. Current expenditures were concentrated in personnel expenditure, social insurance expenditure and local budget expenditure. These items have recorded an annual growth of 5.2, 7.7 and 4.4 per cent, respectively.
Capital expenditure continues to be realized below the level projected in the revised budget. For the first 11 months of the year, they were realized at 86.9 per cent. About 66 per cent of capital investment, totalling ALL 33.4 billion, was carried out over the last three months of the period. As far as expenditure financing is concerned, those covered by foreign and domestic financing were carried out at 98.2 and 81.7 per cent, respectively.

Table 10 Composition of current expenditure (in billions of ALL)

<table>
<thead>
<tr>
<th></th>
<th>July</th>
<th>August</th>
<th>September</th>
<th>October</th>
<th>November</th>
<th>11 M Plan, in %</th>
<th>Annual plan, in %</th>
</tr>
</thead>
<tbody>
<tr>
<td>TOTAL EXPENDITURE</td>
<td>114</td>
<td>133</td>
<td>152</td>
<td>176</td>
<td>204</td>
<td>92.6</td>
<td>76.4</td>
</tr>
<tr>
<td>Current expenditure</td>
<td>104</td>
<td>121</td>
<td>137</td>
<td>154</td>
<td>171</td>
<td>94.1</td>
<td>83.5</td>
</tr>
<tr>
<td>Personnel</td>
<td>30</td>
<td>35</td>
<td>39</td>
<td>44</td>
<td>49</td>
<td>96.1</td>
<td>83.0</td>
</tr>
<tr>
<td>Interests</td>
<td>15</td>
<td>18</td>
<td>19</td>
<td>21</td>
<td>23</td>
<td>94.3</td>
<td>91.9</td>
</tr>
<tr>
<td>Domestic</td>
<td>14</td>
<td>16</td>
<td>18</td>
<td>20</td>
<td>22</td>
<td>96.9</td>
<td>94.2</td>
</tr>
<tr>
<td>Foreign</td>
<td>1</td>
<td>1</td>
<td>1</td>
<td>1</td>
<td>2</td>
<td>70.2</td>
<td>70.2</td>
</tr>
<tr>
<td>Operative maintenance expenditure</td>
<td>11</td>
<td>12</td>
<td>13</td>
<td>15</td>
<td>17</td>
<td>89.6</td>
<td>80.2</td>
</tr>
<tr>
<td>Social insurance expenditure and other related</td>
<td>33</td>
<td>38</td>
<td>43</td>
<td>48</td>
<td>53</td>
<td>97.2</td>
<td>88.0</td>
</tr>
<tr>
<td>Local budget expenditure</td>
<td>9</td>
<td>11</td>
<td>13</td>
<td>15</td>
<td>17</td>
<td>92.2</td>
<td>73.7</td>
</tr>
<tr>
<td>Other expenditure</td>
<td>6</td>
<td>6</td>
<td>7</td>
<td>8</td>
<td>9</td>
<td>82.5</td>
<td>73.6</td>
</tr>
<tr>
<td>Capital expenditure</td>
<td>10</td>
<td>11</td>
<td>15</td>
<td>22</td>
<td>33</td>
<td>86.9</td>
<td>58.3</td>
</tr>
<tr>
<td>Domestic financing</td>
<td>7</td>
<td>8</td>
<td>11</td>
<td>18</td>
<td>21</td>
<td>81.7</td>
<td>57.8</td>
</tr>
<tr>
<td>Foreign financing</td>
<td>3</td>
<td>3</td>
<td>4</td>
<td>5</td>
<td>12</td>
<td>98.2</td>
<td>59.3</td>
</tr>
</tbody>
</table>

Source: Ministry of Finance, November 2006

Fiscal balance

Fiscal deficit over January to November 2006 was nearly as much as 11.8 per cent of planned deficit. The sluggish performance of expenditure and the satisfactory growth of revenues caused the deficit to record the highest decrease in the last eight years. As far as distribution of deficit over 2006 is concerned, it is observed that the period over October and November recorded the highest level of deficit by ALL 11.5 billion, while the first quarter resulted in a surplus of ALL 9.2 billion. It is observed that the government budget has by October resulted in a surplus of ALL 6.2 billion. This situation improved over November, causing the fiscal balance to result in a deficit of ALL 1.5 billion for the first time over 2006. The accomplishment of this objective was accompanied by the rapid increase of expenditure in the last two months of the year.

2.2.4 External sector of economy

Current account developments until the third quarter 2006 indicate an intensive activity of the external sector of economy. The volume of current account transactions over the first nine months of the year amounted to EUR 5 billion, which is 17 per cent higher than the volume amounted over the
same period the previous year. Current account deficit deepened by about 15 per cent compared to the previous year. The deepening of deficit in the trade in goods, as a result of the higher increase of imports as opposed to the increase of exports, affected the aggravation of the current account balance. However, the negative influence of the trade balance was offset by the positive developments in all the other items of current account.

The third quarter of 2006, as opposed to the third quarter of 2005, recorded a current deficit of about 74 per cent higher. The decrease of the current transfers’ inflows provided the main influence on the aggravation of current deficit. Goods, services and revenues’ account recorded in the third quarter a deficit of almost as high as the one recorded in the third quarter of 2005, which equals EUR 375 million. Compared to the same period the previous year, the deficit on the trade in goods deepened by about 8.5 per cent; the deficit on the trade in services reduced by about 60 per cent; while the surplus recorded in the item of revenues was about 28 per cent higher.

Over the first nine months of 2006, the lek displayed a slight downward tendency against the three currencies of our five main trade partners. The depreciation fluctuated around the level of 1-2 per cent. As a consequence, the influence on the performance of foreign trade is assessed to have been limited.

Over January to September 2006, the Albanian economy was developed dynamically. This performance was also observed in the advanced trade relationships with the rest of the world. By the end September, the exports of goods increased by 16 per cent, while the imports increased by 17 per cent compared to the previous year, causing the deficit on the account of goods to amount about EUR 1.2 billion. The high growth rate and the wide range of imported products reflect the orientation of the domestic market towards the foreign production.

The most required commodity groups from the domestic market relate to the final consumption, foodstuffs, intermediate consumption, mineral products, chemical industry, plastic, base materials, as well as to the machinery and appliances item, which reflect the performance of capital investment in economy. The import of textiles and leather, which is related to the performance of re-export production, has increased under steady rates. This development has been reflected in the constant increase of exports upon orderer’s material. Worth mentioning are the positive developments in vegetable products and prepared foodstuffs, in particular over the third quarter. This group has not only recorded a decrease in the import growth rate, but also an increase of exports by about 20 per cent, over the period
when domestic agricultural production recorded the highest levels. A stable growth has been also recorded in the exports of mineral products and of base metals.

Year 2006 did not mark evident changes in the distribution structure of imports and exports of goods by countries of origin and destination. European Union countries continue to constitute the most significant group of trade partners. Other important trade partners, apart for Italy and Greece, are Turkey, Ukraine, Russia, China and South Korea. Trade with the regional countries shares about 8 per cent of total volume of trade in goods for this period.

Over the first nine months of 2006, the developments in the balance of services are considered as satisfactory, since they have had a positive influence on the reduction of current account deficit. Both the imports and exports of services have increased under high rates. At the end of the period, trade in services deficit was about EUR 64 million or 26 per cent lower than the first nine months’ deficit of 2005. The higher growth rate of exports of transport services and other services, compared to the increase of imports, provided the main influence on the reduction of deficit on this account. Personal travels are one of the main items of services account, which to a large extent, displays the performance of tourism in and out of the country. The available data indicate that there has been a slowdown in the activity of tourism in the country for 2006. Over July to September, which represents the main period of tourism in Albania, non-residents have spent about EUR 221 million or about 12 per cent more than over the previous year. Meanwhile, for the same period, residents have spent EUR 216 million abroad or 20 per cent more than the previous year.

Current revenues account continued to record a positive balance over the first three quarters of 2006. In September, this account recorded a surplus of about EUR 159 million, or about 73 per cent higher than the previous year. The increase in revenues has been a consequence of the increase of revenues from the compensation of seasonal workers, and of the increase of interests from the portfolio investment and the foreign reserve. In September, the surplus in current transfers account amounted to EUR 690 million, which is about 4 per cent higher than the net flow of transfers over the same period the previous year. Workers’ remittances, the main item in this account, grew by 17 per cent, amounting to EUR 683 million. The decrease of remittances over the third quarter may be a temporary occurrence. They have covered about 54 per cent of trade in goods and services deficit.
3 INFLATION PERFORMANCE

Annual inflation rate over the second semester of 2006 fluctuated around the Bank of Albania objective of 3 per cent. In December, inflation reached 2.5 per cent, being 0.5 percentage points higher than in December 2005. The average rate of 2.4 per cent of annual inflation over 2006 was similar to the average rate of 2005, which provides evidence for a stable inflation in periods longer than a year.

The dynamics of the monthly inflation performance for July to December 2006 is in line with the historical performance of the last years. The monthly inflation changes over the second semester in general display an upward tendency peaking in December with the speculative rise of prices over the end-year holidays. This phenomenon was quite moderate at the end 2006, being comparable to the two previous end-years. The monthly inflation of 1.7 per cent, recorded in December 2006, was the lowest rate in the last four years.

### Table 11 Main items in the current account (in millions of EUR)

<table>
<thead>
<tr>
<th></th>
<th>July</th>
<th>August</th>
<th>September</th>
<th>Q3-06</th>
<th>Q3-05</th>
<th>9M-06</th>
<th>9M-05</th>
</tr>
</thead>
<tbody>
<tr>
<td>Current account</td>
<td>-30.2</td>
<td>-28.6</td>
<td>-70.7</td>
<td>-129.4</td>
<td>-76.8</td>
<td>-410.6</td>
<td>-355.5</td>
</tr>
<tr>
<td>Goods, services and revenues</td>
<td>-110.9</td>
<td>-109.3</td>
<td>-150.6</td>
<td>-371.0</td>
<td>-377.3</td>
<td>-1100.0</td>
<td>-1017.9</td>
</tr>
<tr>
<td>Goods</td>
<td>-133.5</td>
<td>-143.5</td>
<td>-138.2</td>
<td>-415.3</td>
<td>-382.3</td>
<td>-1200.0</td>
<td>-1022.7</td>
</tr>
<tr>
<td>Exports</td>
<td>59.3</td>
<td>37.0</td>
<td>56.9</td>
<td>153.2</td>
<td>133.7</td>
<td>463.3</td>
<td>398.5</td>
</tr>
<tr>
<td>Imports</td>
<td>-192.8</td>
<td>-180.5</td>
<td>-195.2</td>
<td>-568.5</td>
<td>-516.1</td>
<td>-1663.2</td>
<td>-1421.3</td>
</tr>
<tr>
<td>Services</td>
<td>-1.1</td>
<td>17.5</td>
<td>-31.4</td>
<td>-15.1</td>
<td>-39.0</td>
<td>-60.7</td>
<td>-87.0</td>
</tr>
<tr>
<td>Exports</td>
<td>112.3</td>
<td>135.5</td>
<td>89.1</td>
<td>337.0</td>
<td>270.8</td>
<td>895.5</td>
<td>714.1</td>
</tr>
<tr>
<td>Imports</td>
<td>-113.5</td>
<td>-118.1</td>
<td>-120.5</td>
<td>-352.0</td>
<td>-309.9</td>
<td>-956.2</td>
<td>-801.1</td>
</tr>
<tr>
<td>Revenues</td>
<td>23.7</td>
<td>16.7</td>
<td>18.9</td>
<td>56.3</td>
<td>44.1</td>
<td>158.5</td>
<td>91.8</td>
</tr>
<tr>
<td>Current transfers</td>
<td>80.8</td>
<td>80.7</td>
<td>80.1</td>
<td>241.6</td>
<td>300.5</td>
<td>689.5</td>
<td>662.4</td>
</tr>
<tr>
<td>Remittances</td>
<td>79.2</td>
<td>79.2</td>
<td>79.2</td>
<td>237.7</td>
<td>259.5</td>
<td>689.5</td>
<td>582.6</td>
</tr>
</tbody>
</table>

Source: Bank of Albania, Statistics Department

### Table 12 Annual inflation rate (in percentage)

<table>
<thead>
<tr>
<th></th>
<th>2001</th>
<th>2002</th>
<th>2003</th>
<th>2004</th>
<th>2005</th>
<th>2006</th>
</tr>
</thead>
<tbody>
<tr>
<td>January</td>
<td>2.2</td>
<td>6.5</td>
<td>0.0</td>
<td>3.3</td>
<td>3.3</td>
<td>1.4</td>
</tr>
<tr>
<td>February</td>
<td>1.5</td>
<td>7.6</td>
<td>1.1</td>
<td>4.4</td>
<td>1.8</td>
<td>1.3</td>
</tr>
<tr>
<td>March</td>
<td>2.9</td>
<td>7.5</td>
<td>1.3</td>
<td>4.0</td>
<td>1.6</td>
<td>1.5</td>
</tr>
<tr>
<td>April</td>
<td>3.0</td>
<td>6.5</td>
<td>2.3</td>
<td>3.2</td>
<td>1.3</td>
<td>2.4</td>
</tr>
<tr>
<td>May</td>
<td>2.5</td>
<td>4.6</td>
<td>2.8</td>
<td>2.6</td>
<td>2.0</td>
<td>3.1</td>
</tr>
<tr>
<td>June</td>
<td>4.0</td>
<td>3.7</td>
<td>2.6</td>
<td>2.9</td>
<td>2.9</td>
<td>2.4</td>
</tr>
<tr>
<td>July</td>
<td>5.6</td>
<td>4.2</td>
<td>3.0</td>
<td>3.1</td>
<td>1.8</td>
<td>3.2</td>
</tr>
<tr>
<td>August</td>
<td>4.1</td>
<td>5.5</td>
<td>3.0</td>
<td>2.7</td>
<td>2.3</td>
<td>2.9</td>
</tr>
<tr>
<td>September</td>
<td>3.5</td>
<td>5.3</td>
<td>2.8</td>
<td>2.0</td>
<td>3.1</td>
<td>2.6</td>
</tr>
<tr>
<td>October</td>
<td>1.8</td>
<td>5.8</td>
<td>2.9</td>
<td>2.0</td>
<td>3.3</td>
<td>2.3</td>
</tr>
<tr>
<td>November</td>
<td>2.8</td>
<td>3.7</td>
<td>3.4</td>
<td>2.2</td>
<td>3.0</td>
<td>2.9</td>
</tr>
<tr>
<td>December</td>
<td>3.5</td>
<td>1.7</td>
<td>3.3</td>
<td>2.2</td>
<td>2.0</td>
<td>2.5</td>
</tr>
<tr>
<td>Average</td>
<td>3.1</td>
<td>5.2</td>
<td>2.2</td>
<td>3.0</td>
<td>2.4</td>
<td>2.4</td>
</tr>
</tbody>
</table>

Source: CPI, INSTAT, 2006

The developments in the general level of prices over the second semester of 2006 occurred within a balanced macroeconomic framework, in which the inflationary pressures, despite being present, have been kept under control. Both
the monetary and fiscal policies have controlled the demand and supply pressures in economy, allowing for the observance of the inflation objective. Annual inflation did not exceed the tolerance band of 1 percentage points around the 3.0 per cent objective over this period.

3.1 INFLATION PERFORMANCE BY MAIN GROUPS

Inflation performance over the second semester of 2006 was affected by the influence of a number of factors, such as the energy price rise in August, the deviation of domestic agricultural production from the seasonal framework, the rise in the prices of some excise goods and the oil price performance. Among these factors, “Foodstuffs and non-alcoholic beverages”, “Rent, water, fuels and energy” and “Alcoholic beverages and tobacco” were the main groups which defined the inflation rate for this period.

Foodstuffs prices have played a pivotal role in the definition and performance of the general level of prices over this semester. This group’s annual inflation has on average contributed by 0.3 percentage points to total inflation for this period. The increasing pressures were considerably higher than those of the previous year or of 2004, when the contribution of this group to total inflation rate was 0.0 and -0.6 percentage points, respectively. A number of internal and external factors have conditioned the change of this group’s contribution. The unfavourable atmospheric conditions over spring had a negative impact over the supply of agricultural production, pushing the entry of import goods into the domestic market at high prices. The positive annual inflation rates of “Foodstuffs and non-alcoholic beverages” over most of the year reflect the presence and the share of import goods. September and October make up an exception, over which domestic agricultural production may have coped better with the domestic demand for agricultural products, causing the annual inflation for this group to be negative. The seasonal effect, despite being late and short, was reflected in the monthly inflation rates. Being in line with the seasonal performance, foodstuffs monthly inflation and total inflation recorded negative rates over May to August.
Foodstuffs prices were also influenced by the upward tendency of these goods’ prices in the European markets. The favourable behaviour of the exchange rate between the lek and the euro toned down the influence of foreign prices until June, but did not manage to compensate the rise of foodstuffs prices over the second semester. Over this semester, the lek depreciated against the euro by 0.4 per cent, compared to the appreciation by 2.4 per cent and 2.2 per cent over the same period the previous year and over the first semester 2006.

Table 13 Annual inflation of “Foodstuffs and non-alcoholic beverages” (in the country and abroad) and its contribution to total inflation

<table>
<thead>
<tr>
<th></th>
<th>Annual inflation ’05</th>
<th>Contribution (pp)</th>
<th>Annual inflation ’06</th>
<th>Contribution (pp)</th>
<th>Italy’s Annual inflation ’06</th>
<th>Greece’s Annual inflation ’06</th>
<th>Euro area’s (12 countries)</th>
</tr>
</thead>
<tbody>
<tr>
<td>March</td>
<td>-1.7</td>
<td>-0.7</td>
<td>0.4</td>
<td>0.2</td>
<td>1.0</td>
<td>2.8</td>
<td>1.3</td>
</tr>
<tr>
<td>June</td>
<td>1.6</td>
<td>0.7</td>
<td>1.9</td>
<td>0.8</td>
<td>1.3</td>
<td>3.0</td>
<td>2.0</td>
</tr>
<tr>
<td>July</td>
<td>-1.6</td>
<td>-0.7</td>
<td>4.7</td>
<td>1.9</td>
<td>1.8</td>
<td>5.4</td>
<td>2.6</td>
</tr>
<tr>
<td>August</td>
<td>0.0</td>
<td>0.0</td>
<td>1.3</td>
<td>0.5</td>
<td>2.2</td>
<td>4.6</td>
<td>2.9</td>
</tr>
<tr>
<td>September</td>
<td>1.5</td>
<td>0.6</td>
<td>-1.1</td>
<td>-0.5</td>
<td>2.5</td>
<td>4.6</td>
<td>3.3</td>
</tr>
<tr>
<td>October</td>
<td>1.7</td>
<td>0.7</td>
<td>-1.5</td>
<td>-0.6</td>
<td>2.7</td>
<td>5.1</td>
<td>3.0</td>
</tr>
<tr>
<td>November</td>
<td>0.2</td>
<td>0.1</td>
<td>1.1</td>
<td>0.5</td>
<td>2.9</td>
<td>4.5</td>
<td>3.0*</td>
</tr>
<tr>
<td>December</td>
<td>-1.9</td>
<td>-0.8</td>
<td>0.2</td>
<td>0.1</td>
<td>2.7</td>
<td>4.3</td>
<td>--</td>
</tr>
</tbody>
</table>

Source: Bank of Albania; General Secretariat of National Statistical Service of Greece; ISTAT-Italy

(“) Preliminary rates

“Rent, water, fuels and energy” continued to provide the main influence on the definition of annual inflation rate over the second semester of 2006. The average contribution of this item to annual inflation rate for this period was 1.8 percentage points. Following the cessation of the energy price rise effect at the beginning of 2006, the annual inflation rates of this item increased moderately until August, when the energy price increased by 13.7 per cent, in annual terms. All this item’s constituents marked positive growth rates. Apart from the energy price rise, rent and imputed rent market prices also increased. The highest annual inflation rates of this item over the second semester were recorded in September (8.5 per cent) and in October (8.0 per cent), reflecting the growth of demand for apartments at the beginning of the school academic year.

Table 14 Total annual inflation rate and annual rate of “Rent, water, fuels and energy”, and its contribution to total inflation

<table>
<thead>
<tr>
<th></th>
<th>March</th>
<th>June</th>
<th>July</th>
<th>August</th>
<th>September</th>
<th>October</th>
<th>November</th>
<th>December</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total annual inflation (in percentage)</td>
<td>1.5</td>
<td>2.5</td>
<td>3.2</td>
<td>2.9</td>
<td>2.6</td>
<td>2.3</td>
<td>2.9</td>
<td>2.5</td>
</tr>
<tr>
<td>Inflation of “Rent, water, fuels and energy” (in percentage)</td>
<td>3.2</td>
<td>3.9</td>
<td>3.2</td>
<td>6.5</td>
<td>8.5</td>
<td>8.0</td>
<td>7.0</td>
<td>7.0</td>
</tr>
<tr>
<td>Contribution to total inflation (in percentage points)</td>
<td>Rent 0.9</td>
<td>1.0</td>
<td>0.9</td>
<td>1.8</td>
<td>2.3</td>
<td>2.2</td>
<td>1.9</td>
<td>1.9</td>
</tr>
<tr>
<td></td>
<td>Rent 0.1</td>
<td>0.1</td>
<td>0.1</td>
<td>0.1</td>
<td>0.1</td>
<td>0.1</td>
<td>0.1</td>
<td>0.1</td>
</tr>
<tr>
<td></td>
<td>Imputed rent 0.7</td>
<td>0.9</td>
<td>0.8</td>
<td>0.8</td>
<td>1.2</td>
<td>1.1</td>
<td>0.9</td>
<td>0.9</td>
</tr>
<tr>
<td></td>
<td>Fuels and energy 0.0</td>
<td>0.0</td>
<td>0.0</td>
<td>0.9</td>
<td>0.9</td>
<td>0.9</td>
<td>0.9</td>
<td>0.9</td>
</tr>
</tbody>
</table>

Source: Bank of Albania, INSTAT, 2006

Total prices level over the second semester was overwhelmingly influenced by the inflation of “Alcoholic beverages and tobacco”. The information on the increase of the excises for these goods’ prices was reflected in their sale.
prices starting from August, preceding the entry into force of this decision in September 2006. This rise reflects the speculative features of the domestic market. Despite the small share by 3.1 per cent of “Alcoholic beverages and tobacco” in the consumer basket, its contribution to annual inflation rate was 0.3 percentage points, or as much as the contribution of “Foodstuffs and non-alcoholic beverages”.

The second semester of 2006 was characterized by low annual inflation growth rates of “Transport” and “Hotels, café and restaurants”. Their average contribution to annual inflation was 0.1 and 0.2 percentage points, respectively. The low inflation growth rates of “Transport” were mainly headed by the moderate rise of oil price. In annual terms, the oil price in the country rose by 0.1 per cent over this semester, which is lower than the rise of 0.3 per cent, recorded over the previous semester and over the same period the previous year. Apart from the more considerable appreciation of the domestic currency to the dollar over this period, the positive developments in the international markets oil price pushed the fall of oil price in the country.

The goods’ prices of other basket groups displayed diverse tendencies over the second semester. The combined contribution of their inflation was almost insignificant, since the groups with a positive contribution balanced the groups which contributed negatively. The fall in the prices of tradable goods, which are part of “Clothes and footwear”, “Furniture, household and maintenance appliances”, is quite a long phenomenon, being present since 2000. Their decreasing contribution was offset by the rise of services prices, which are part of “Health service” and “Education Service”.

3.2 MACROECONOMIC ENVIRONMENT AND CONSUMER PRICES

Domestic macroeconomic developments over the second semester of 2006 have by and large provided a favourable environment for keeping the inflation rate under control. The inflationary pressures mainly derived from the supply-side, which at times, were intensified. Among them, the energy price rise in August, the excise goods price rise and the oil price rise until October 2006 were most evident. Under these conditions, the tightening monetary policy reaction at mid-July and end November is assessed to have begun to control the upward inflationary pressures in economy. In particular, the mitigation of these pressures was observed over the last month of the year, which has been historically perceived as a high inflation month. The stable lek in the foreign exchange market, the absence of inflationary pressures deriving from the external environment and the oil price fall in the domestic market are assessed to have provided their impact over this period. Budget expenditure and budget deficit have been in controlled levels, despite their concentration
in the last period of the year. This has caused the aggregate demand to remain within the projections, not transmitting inflationary pressures to the economy. However, part of the impact over demand and inflation will be carried out in the first quarter of 2007.

**FACTORS OF DEMAND**

**Domestic demand indicators**

The signals deriving from various indicators provide evidence for a growth in domestic demand over the second semester of the year. The sales index for the first nine-month period recorded an annual growth of 12.4 per cent. For the same period, foreign trade indices indicate a growth of exports and imports by 16 and 17 per cent, respectively, compared to the previous year. These indices, along with the rapid growth of lending activity, provide evidence for an expansion of consumption and investments. However, given the dynamics of inflation indices, this growth of domestic demand did not prove sufficient to transmit inflationary pressures to the economy.

**Fiscal policy**

In general, budget deficit financing though domestic borrowing was low over the second semester. Government demand for monetary assets did not exert pressure for the growth of monetary sources. The fiscal indicators did not exceed the amounts projected for this period, even under the revised figures. In this context, the fiscal policy has not infringed the preservation of macroeconomic balances. On the other hand, the data on November provide evidence for a concentration of budget expenditure at the end of the year. Despite the accelerated growth rate of carrying out the expenditure, they are still far from the realization of plan. The concentration of expenditure over the fourth quarter increased the possibility of generating inflationary pressures in the short and medium-term.

**Monetary policy and monetary conditions**

Under the conditions when the supply-side inflationary pressures were more intensively present over the second semester of the year, monetary policy accommodated these developments by pursuing a tightening policy. The increase of the core interest rate aimed at creating adequate monetary conditions for the control of these pressures. Money supply grew gradually, meeting the increasing demand of both the public and the private sector. The Bank of Albania continued to be present in the money markets, aiming to provide the necessary liquidity and to minimize interest rate fluctuations. On the other hand, the ratio of currency outside banks to money supply fluctuated around the lowest historical levels. The meeting of market’s demand for liquidity and the maintenance of low levels of currency outside banks aided the maintenance of price stability in the medium-term.
FACTORS OF SUPPLY

External environment and exchange rate

Exchange rate developments enabled the mitigation of inflationary pressures over the second semester of 2006. Our domestic currency appreciated distinctly to the dollar, while remaining at stable levels to the euro. Such a performance of the exchange rate is assessed to have been one of the main factors to have controlled the strong supply-side pressures and to have influenced on the maintenance of the inflation rate within the Bank of Albania objective. On one hand, it influenced on the reduction of cost for import goods, and on the other, it provided a status quo of the oil price in the country, while in the international market there was an oil price rise (in particular over the third quarter).

Table 15 Annual inflation rates in Italy, Greece and the Euro area and the exchange rate annual change (in percentage)

<table>
<thead>
<tr>
<th></th>
<th>Q1*-06*</th>
<th>Q2*-06*</th>
<th>Q3*-06*</th>
<th>Q4*-06*</th>
</tr>
</thead>
<tbody>
<tr>
<td>Greece</td>
<td>3.2</td>
<td>3.2</td>
<td>3.4</td>
<td>2.9</td>
</tr>
<tr>
<td>Italy</td>
<td>2.2</td>
<td>2.2</td>
<td>2.2</td>
<td>1.8</td>
</tr>
<tr>
<td>Euro area</td>
<td>2.3</td>
<td>2.4</td>
<td>2.1</td>
<td>1.8</td>
</tr>
<tr>
<td>Lek/Euro</td>
<td>-2.9</td>
<td>-1.4</td>
<td>0.1</td>
<td>0.7</td>
</tr>
<tr>
<td>Lek/Usd</td>
<td>5.7</td>
<td>0.1</td>
<td>-4.1</td>
<td>-7.0</td>
</tr>
</tbody>
</table>

Source: CPI, INSTAT
Note: (*) The quarterly figures are the average monthly indicators.

Imported inflation

The performance of consumer prices in Albania’s main trade partners was an important factor for the transmission of decreasing tendencies to the domestic consumer prices. As a result of the oil price fall, the inflation rate in our two main trade partners, Greece and Italy, and in the Euro area, recorded distinct lower rates at the end of 2006, compared to the previous year. Meanwhile, there was a fall in the prices of “Foodstuffs and non-alcoholic beverages”,

Table 15 Annual inflation rates in Italy, Greece and the Euro area and the exchange rate annual change (in percentage)
resulting from the late entry of domestic production into the market over the end of summer 2006.

**Oil price and energy situation**

The downward oil price tendency starting from October pushed the fall of prices in the domestic market. As a result, the forewarned risk for inflationary pressures over summer and the first part of the second semester, pushed by the oil price rise, did not actualize. On the other hand, the oil price effects on the domestic market are reinforced by the situation of energy supply, which began to be displayed as problematic starting from December. The consequences of the interaction between both these factors, as well as the second round effects over prices, continue to remain among the priorities of monetary policy.

**Agricultural production**

The fluctuations in the prices of goods and services of consumer basket main groups compensated one another, causing the inflation rate to be kept below the objective of 3 per cent, but within the tolerance band. The energy price rise in August, the price rise of excise goods and of education service contributed to total inflation by 1 percentage points. On the other hand, the favourable behaviour of foodstuffs prices until the end 2006 balanced the high inflation rates of special goods and services. The dropping of this group’s goods prices was favoured by the favourable climate conditions and the growth of agricultural production, almost until the end of the year.

**Unemployment and wages**

The labour market situation continued to improve. Moreover, the wages in the public sector, the minimal wage and pensions increased according to the budget programme. These elements did not transmit strong inflationary pressures to economy over July to December 2006; not even in the year end when the demand for goods and services grows overwhelmingly.

**4 MONETARY DEVELOPMENTS AND FINANCIAL MARKETS**

**4.1 MONETARY POLICY OF THE BANK OF ALBANIA**

The overall economic and financial environment introduced some important challenges for the formulation and implementation of monetary policy over the second semester of 2006. There were increasing inflationary pressures
over this period, mainly resulting from the influence of supply factors. The likelihood of high oil prices being transmitted to the costs of production and their effect on the economic agents’ inflationary expectations was persistently monitored by the Bank of Albania, aiming at providing a rapid and complete reaction to it. On the other hand, the rapid growth of credit to economy and the concentration of budget expenditure in the last quarter provided evidence for a more complete inflationary pressures context, including in it the factors of demand as well. Under these conditions, the Bank of Albania reacted by increasing the core interest rate in July and November, from 5.0 per cent to 5.5 per cent over the second semester.

The raise of the cost of money aimed at keeping appropriate monetary conditions for guaranteeing price stability in the long-term. The tightening of monetary conditions is in line with the monetary policy pursued by large central banks and with the increase of interest rates in the international foreign currency markets. The Bank of Albania decision was reflected in the monetary markets’ interest rates.

On the other hand, the increase of Government borrowing and the maintenance of high crediting rates in lek caused liquidity shortages in the system over the last quarter of the year. This situation was reflected in the increase of Treasury bills yield and in a higher fluctuation of the interbank market. Under these conditions, the Bank of Albania injected liquidity in the system, aiming at reducing the interest rates fluctuations and at meeting the market’s short-term demand for liquidity. The injection of liquidity in the system was carried out through the use of reverse repos, totalling ALL 6.5 billion by the end of 2006. This injection affected the mitigation of pressures over the Treasury bills yield. Along with the money market operations, the interventions in the foreign currency market supported the meeting of economy’s demand for liquids and the observance of the Bank of Albania quantitative objectives.

Table 6 Realization of the Bank of Albania quantitative objectives

<table>
<thead>
<tr>
<th>December'05</th>
<th>March'06</th>
<th>June'06</th>
<th>September'06</th>
<th>November'06</th>
<th>December'06*</th>
</tr>
</thead>
<tbody>
<tr>
<td>Net international reserve of the Bank of Albania (in millions of USD)</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Objective</td>
<td>1,172</td>
<td>1,117</td>
<td>1,112</td>
<td>1,252</td>
<td>1,262</td>
</tr>
<tr>
<td>Current</td>
<td>1,172</td>
<td>1,202</td>
<td>1,224</td>
<td>1,296</td>
<td>1,305</td>
</tr>
<tr>
<td>Difference (C-Obj)</td>
<td>--</td>
<td>85</td>
<td>112</td>
<td>44</td>
<td>43</td>
</tr>
<tr>
<td>Net domestic assets of the Bank of Albania (in billions of ALL)</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Objective</td>
<td>82.0</td>
<td>85.0</td>
<td>90.0</td>
<td>82.9</td>
<td>85.6</td>
</tr>
<tr>
<td>Current</td>
<td>76.9</td>
<td>61.9</td>
<td>67.8</td>
<td>71.2</td>
<td>72.7</td>
</tr>
<tr>
<td>Difference (C-Obj)</td>
<td>-5.1</td>
<td>-23.1</td>
<td>-22.2</td>
<td>-11.7</td>
<td>12.9</td>
</tr>
<tr>
<td>Net domestic credit to the Government (in billions of ALL)</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Objective</td>
<td>317.8</td>
<td>325.8</td>
<td>329.8</td>
<td>335.8</td>
<td>340</td>
</tr>
<tr>
<td>Current</td>
<td>317.8</td>
<td>311.8</td>
<td>306.6</td>
<td>307.4</td>
<td>312</td>
</tr>
<tr>
<td>Difference (C-Obj)</td>
<td>--</td>
<td>-14.0</td>
<td>-23.3</td>
<td>-28.5</td>
<td>-28</td>
</tr>
</tbody>
</table>

*Operative data
Source: Bank of Albania
4.2 PERFORMANCE OF MONETARY AGGREGATES

The monetary developments over the second semester of 2006 continued to reflect at large the dynamics observed in the private sector’s economic activity, despite the gradual growth of Government’s demand for monetary assets. Credit to economy remains the main contributor to the growth of monetary assets in economy. Moreover, workers’ remittances made a positive contribution to the seasonal growth of deposits in foreign currency and of the system’s net foreign assets. The growth of Government’s demand for financing, in particular over the last quarter, influenced on a more rapid monetary expansion compared to the first semester. In November, money supply recorded an annual growth of 12.7 per cent, against an annual growth of 9.7 per cent in June.

However, the relatively low demand of the public sector over 2006 contributed to the shrink of monetary growth rates as opposed to the two previous years. The current annual expansion rates of monetary aggregates result distinctly lower than the last two years’ rates of 17-18 per cent. Moreover, the slowdown of lending growth rate adds to the argument for a more sluggish monetary expansion and for the maintenance of macroeconomic balances. The gradual reduction of the share of currency in circulation tends to favour a more rapid circulation of money and the monetization of economy, being in line with the tendencies observed in more developed economies.

The creation of money in economy found an evident reflection in the growth of the level of deposits, while the share of currency outside banks to money supply displayed a decreasing tendency. The ratio of currency outside banks to monetary aggregate M2 decreased to 32.5 per cent in November, compared to 32.9 per cent at end June. Moreover, the high level of deposits in foreign currency deepened further the decrease of the share of currency outside banks to broad money by about 0.8 percentage points over July to November 2006. Such a performance is in line with the positive tendency of the banking system development. The reduction in the use of cash in economy provides the grounds for the fall of the financial intermediation cost in economy.

The banking system deposits recorded an annual growth of 15.3 per cent in November, compared to the annual growth by 11.7 per cent at the end of the
first semester. ALL inflows have by and large been channelled in time deposits, while foreign currency inflows, mainly the share of the private sector, were in the form of both time and demand deposits. The more rapid growth of time deposits to demand deposits was reflected in the ratio of time deposits to M3, which marked 54.1 per cent in November or 0.7 percentage points more than in June and 1.9 percentage points more than the previous year. The level of deposits in foreign currency maintains the highest growth rates as opposed to the annual growth rate of deposits in lek. ALL deposits grew by 5.5 per cent compared to June, while foreign currency deposits grew by 13.6 per cent. Under these conditions, the foreign currency structure of broad money maintained the shifting tendency towards deposits in lek and in foreign currency.

The creation of money in the form of deposits in foreign currency was favoured by the high borrowing rates of the private sector in foreign currency and by the increasing rates of euro and dollar interests. The increase of the interest rates by the European Central Bank and the Federal Reserve had a pivotal influence on their upward tendency. Such an increase led to the narrowing of differences between ALL time deposits rates and time deposits in foreign currency. However, the increase of the lek core interest rate contributed to the maintenance of positive differences between the ALL and foreign currency interests.

<table>
<thead>
<tr>
<th>Table 17 Performance of monetary indicators (in billions of ALL)</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>November</strong></td>
</tr>
<tr>
<td><strong>2006</strong></td>
</tr>
<tr>
<td>Currency outside banks</td>
</tr>
<tr>
<td>Total deposits</td>
</tr>
<tr>
<td>- in lek</td>
</tr>
<tr>
<td>- in foreign currency</td>
</tr>
<tr>
<td>M1</td>
</tr>
<tr>
<td>M2</td>
</tr>
<tr>
<td>M3</td>
</tr>
<tr>
<td>Monetary base</td>
</tr>
<tr>
<td><strong>Shares to broad money (in percentage)</strong></td>
</tr>
<tr>
<td><strong>December ’05</strong></td>
</tr>
<tr>
<td>Currency outside banks/M3</td>
</tr>
<tr>
<td>Deposits in lek/M3</td>
</tr>
<tr>
<td>Deposits in foreign currency/M3</td>
</tr>
</tbody>
</table>

Source: Bank of Albania

4.3 DEMAND FOR MONETARY ASSETS

4.3.1 Credit to economy

Credit to economy continued to record rapid growth rates over the second semester of 2006. The banking system credit portfolio amounted to ALL 179.5
billion in November 2006, accounting for 28.1 per cent of the economy monetary assets. As a share to the gross domestic product, it stands at its highest historical levels, accounting for 20.1 per cent. However, the annual growth rate of credit to economy marked a decrease over this semester, declining from 67.1 per cent in June to 57.8 per cent in November. The growth rate slowdown is a result of the high credit level for a two-year period. Moreover, the new market segments not covered with credit have been decreasing, not allowing the maintenance of such growth rates. The application of a set of rules in the beginning of 2007, which aims at controlling and maintaining the credit portfolio quality, is expected to affect the further reduction of credit growth. The continuous credit growth rates slowdown in the future will bring it to stable levels, in line with the macroeconomic stability in the country.

The extension of loans maturity terms of banks’ portfolio and the increase of new extended loans are the main factors to support the stable growth of credit in the banking system. Over July of November 2006 was extended a total of ALL 13.4 billion of new credit per month or 20 per cent above the monthly average of the first semester. The positive developments over summer constituted the particular of the credit historical performance to date. Moreover, the new disbursed credit of ALL 15.9 billion in November marked the historical maximum extended credit within a month.

Credit in lek accounted for 29.7 per cent of credit portfolio in November, marking a slight growth in its share to total credit. The growth of credit in lek for more than a year was reflected in the reduction of the annual growth rate to 82.4 per cent in November, from 140 per cent the previous year. In August and September, the contribution of credit in lek reached to 40 per cent of credit growth, being later reduced to the rates featuring year 2006, to about 36 per cent. The supply of some large banks with low-cost consumer loan over summer seems to have pushed the acceleration of credit in lek over this period. Despite the rapid growth of credit in lek, credit in foreign currency dominates the banks’ portfolio by 70.3 per cent. This type of credit displayed a positive performance over the second half of 2006. Its annual growth rate recorded 48 per cent in November, constituting the highest rate for July to November. Credit in foreign currency had an upward tendency in September, which is not only related to the increase of business crediting in foreign currency, but also to the financing of household purchases in foreign currency.
Credit to households accounted for 7 per cent of the GDP in November. Banks have almost maintained the share of this type of credit to total credit unchanged over the last months of 2006, around the level of 33 per cent. The annual growth rate of credit to households recorded 65 per cent in November, getting close to the lowest levels of the last three years. More than half of credit to households is extended for the financing of real estate acquisitions. However, there has been an increasing crediting of households for the financing of consumer goods purchases over 2006. The share of consumer loan to total households’ portfolio accounted for 30 per cent in November, from 20 per cent the previous year.

Business loan maintained increasing annual rates over the second semester of 2006, accounting for about 55 per cent. The structure of its distribution by use attempted to be more harmonized compared to the previous year. The largest share of business loan is used for the purchase of appliances and machinery, accounting for 33.3 per cent. Meanwhile, the financing of business investments for the expansion of their activity had a remarkable performance over 2006, accounting for 24 per cent of business loan in November.

The sector of trade continued to constitute the most attractive sector for the banking system, accounting for 23.4 per cent of loans, and reflecting a slight increase from the end of the first semester. Meanwhile, the sector of agriculture continued to reduce its share to total to 0.7 per cent from 2.4 per cent the previous year. The performance of loan index by sector indicates that real estates loan had the most remarkable performance for 2006, being stabilized in high growth rates. The positive borrowing performance in the apartments market is followed by the sector of trade. Meanwhile, the loan growth rates for this sector have been decreasing over the recent months.

4.3.2 Net foreign assets

The banking system net foreign assets have increased considerably over the second semester, amounting to USD 260 million. This increase was
mostly influenced by the Bank of Albania foreign currency operations and by
the growth of deposits in foreign currency held with commercial banks. On the
other hand, a share of this growth is attributed to the appreciation of the euro
against the dollar by about 3.8 per cent, increasing the amount of investment
in euro, expressed in dollar. In the absence of this effect, the growth of the
banking system net foreign assets for this period totals USD 198.8 million.

The developments in net foreign assets over this period have by and large
been in line with their historical performance. The increase of deposits in foreign
currency and the slowdown of credit over the third quarter have provided a
positive influence on the level of commercial banks net foreign assets. Despite
their decrease in the last quarter, their increase totalled USD 113.5 million
over the second semester of 2006. In the absence of the exchange rate effect,
the growth of these assets amounts USD 96.2 million.

The Bank of Albania net foreign reserve increased by USD 146.5 million over
July to November. This increase came due to the continuous interventions of
the Bank of Albania in the foreign currency market, in order to accomplish its
objective related to the net international reserve and to lower the fluctuations
in the foreign currency market. In the absence of the exchange rate effect,
the increase of the Bank of Albania net foreign reserve amounts USD 102.5
million.

As far as the foreign currency structure of commercial
banks’ foreign assets is concerned, the USD shares
most of this structure, accounting for about 50 per
cent, over the second semester of 2006. Most of non-
residents’ securities held with banks and time deposits
held with foreign banks are denominated in USD.
Most of non-residents cash and credit are in EUR. On
the other hand, about 70 per cent of foreign currency
liabilities are denominated in EUR, most of which is
shared by credit extended by foreign banks.

4.3.3 Government demand for money

The Government maintained the fiscal balance
in positive levels for most of the second semester
of 2006. Following June, budget surplus has been
decreasing, recording negative levels in November. As a result of these
development, Government demand for money was concentrated in the
last quarter of 2006. In this period, total financing recorded positive levels,
marking a growth of ALL 16.6 billion. The fiscal projections for 2006 projected
the level of domestic financing to reach to ALL 22.8 billion. By November, this
financing resulted to about ALL 6.7 billion.

Over the second semester of 2006, the Government was oriented towards
the issue of long-term debt and reduced the issue of Treasury bills. Domestic
financing was mostly covered through the issue of bonds of 2, 3 and 5-year maturity. Bonds of 5-year maturity were issued for the first time in November, totalling ALL 6.36 billion. With regard to bonds of 2 and 3-year maturity, their portfolio for July to November grew by ALL 9.8 and 6.5 billion, respectively.

Over the same period, the net level of Treasury bills purchased in the primary market decreased to the negative level of ALL 22 billion or about ALL 12.8 billion more than over the first semester of 2006. The Treasury bills’ portfolio decreased by ALL 14.8 billion. About 90 per cent of this decrease is a consequence of the reduction of commercial banks Treasury bills’ portfolio.

The Government continued to invest the surplus in the form of reverse repos to commercial banks over the second semester. However, over this period, the excess liquidity invested in reverse repos decreased, reaching ALL 5.8 billion or about ALL 5.2 billion less than in June. For the same period, the level of Government’s deposits held with the Bank of Albania increased by ALL 7.3 billion.

**4.4 PERFORMANCE OF FINANCIAL MARKETS**

**Money and securities market**

The second semester was characterized by the tightening of the monetary policy. The Bank of Albania increased the core interest rate twice, in July and in November, by 25 basis points, respectively, causing it to reach 5.50 per cent. Following the tightening signals, the interest rates in the money market have been increasing over this period.

While in the third quarter the Bank of Albania continued to withdraw the liquidity through the regular auctions of weekly repos (ALL 2.9 billion on average), in the fourth quarter the course of operations shifted. Under the absence of liquidity in the market, the Bank of Albania intervened by injecting liquidity through reverse repos. In order to provide for its stable level, there were auctions for reverse repos of one-month and three-month maturity, besides the weekly reverse repos. These kinds of structural operations totalled ALL 6.5 billion.

The average daily volume of transactions in the interbank market decreased to ALL 1.6 billion in the second semester, compared to ALL 1.7 billion in the first semester. The weekly transactions recorded ALL 0.9 billion, on average,
maintaining the same level as in the previous semester. The interest rate for these transactions increased by 9 basis points, reaching to 5.24 per cent by the end December. The overnight transactions interest rate was influenced by the change of demand/supply ratios. It decreased from 5.00 per cent in the third quarter to 4.52 per cent in the fourth quarter, when the volume of transactions was higher (ALL 0.9 billion on average, against ALL 0.6 billion).

The issues of Government securities in the primary market increased in the second semester, in particular for maturities of longer than one year. The banking system treasury bills’ portfolio decreased by ALL 10.8 billion, while the bonds’ portfolio of two- and three-year maturity increased by ALL 19.5 billion. For the first time in November, were issued bonds of five-year maturity, whose yield resulted in 9.68 per cent.

The tightening of monetary policy and the occasional non-accomplishment of Government demand for liquidity from the banking system, caused the treasury bills yield to increase significantly compared to the first semester, when they decreased to historical minimum levels. By the end of December, the treasury bills yield of 12-month maturity increased to 7.88 per cent or 214 basis points above the yield in June. For bonds of two- and three-year maturity, the yields increased to 8.40 per cent and 8.80 per cent from 6.38 per cent and 7.50 per cent, respectively, in June.

Banking system interest rates

According to the most recent data for November, there has been an increase of ALL deposits and loan interests of all maturities, except for interests of 2-year deposits and credit from 6 months to 1 year. The increase of interests was a reaction of these markets to the tightening policy pursued by the Bank of Albania, and to the increase of interests for loans and liquidities. As opposed to June, the increase of loan interests exceeded the increase signalled by the Bank of Albania, while ALL deposits interests did not pursue the same trend. The banks were more reserved in increasing the ALL deposits interests, since the system has in general resulted in excess of liquidity from June to November 2006. The more rapid increase of loan interests than deposits interests brought about the increase of intermediation cost.

<table>
<thead>
<tr>
<th></th>
<th>November-05</th>
<th>June-06</th>
<th>November-06</th>
</tr>
</thead>
<tbody>
<tr>
<td>6-month loans-deposits</td>
<td>8.47%</td>
<td>6.93%</td>
<td>11.1%</td>
</tr>
<tr>
<td>1-year loans-deposits</td>
<td>7.84%</td>
<td>6.75%</td>
<td>8.7%</td>
</tr>
</tbody>
</table>

Source: Bank of Albania
The tightening monetary policy pursued by the European Central Bank over the second semester 2006 influenced on the increase of loan and deposits interests in euro of all maturities. In November, the average weighted interest of EUR loans reached 8.02 per cent from 7.75 per cent as of the end of the first semester.

As far as USD interests are concerned, under the conditions of a tightening monetary policy signalled by the Federal Reserve at the end of June 2006, the overall tendency was their increase both for deposits and loans. USD loan interests of all maturities increased from 9.85 per cent in June to 9.96 per cent in November 2006. Over the second semester of 2006, USD deposits interests increased in almost all maturities, exceeding, in most cases, the increase signalled by the Federal Reserve. The expectations for the decrease of the core interest rate by the Federal Reserve in the following months, caused in November to be displayed cases of decrease in the interests of demand deposits, 1-month deposits, 2-year deposits, up to 6-month loans and loans from 6 months to 1 year.

The difference of lek and foreign currency interests of deposits of 3-month, 6-month and 12-month maturity had, in general, a downward tendency. The increase of the core interest rate by the Bank of Albania in November is expected to influence on the increase of this difference.

The following chart displays the spread of ALL deposits real interests to foreign currency ones for deposits of 12-month maturities, which continues to have a downward tendency.

**Exchange rate performance**

The developments in the lek exchange rate over the second semester of 2006 confirmed the slowdown of its appreciating trend against the main currencies. In annual nominal effective terms, the lek appreciated by 1.1 per cent, on average, against the appreciation by 2.8 per cent over the previous year. The USD depreciation in the international foreign currency market continued to favour the appreciating trend of the lek against the dollar over the second semester. On the other hand, the lek was more stable against the EUR, displaying a slight depreciating tendency.
Over summer, the lek was confronted with a less moderate seasonal effect, compared to the previous years. Despite the higher fluctuation of the lek against the euro over the second semester, it followed the downward trend observed over the years. The lek stability was a result of the improvement in the functioning of the foreign currency market and of a number of macroeconomic developments, such as the stable economic growth, the low inflation, the transparency and the moderation of the lack of confidence related to the performance of these indices in the future.

5 EXPECTED PERFORMANCE OF ECONOMY OVER 2007

The economic activity has been displaying positive development tendencies over the recent years. The economy has grown by about 5-6 per cent in real terms, while the investment rate in economy has increased to more than 25 per cent of the GDP, against the 23-24 per cent rates over the previous years. The current macroeconomic framework takes into account the performance of both fiscal and monetary indicators, while the trends of external sector indicators have been in line with the projected economic growth. The macroeconomic situation as a whole remains favourable for 2007, while the accomplishment of the projected indicators for this year is projected to provide for an economic growth of about 6 per cent.

<table>
<thead>
<tr>
<th>Real economy indicators</th>
<th>2002</th>
<th>2003</th>
<th>2004</th>
<th>2005</th>
<th>2006*</th>
<th>2007•</th>
</tr>
</thead>
<tbody>
<tr>
<td>GDP growth</td>
<td>2.9</td>
<td>5.7</td>
<td>5.9</td>
<td>5.5</td>
<td>5.0</td>
<td>6.0</td>
</tr>
<tr>
<td>Annual CPI (average)</td>
<td>5.2</td>
<td>2.4</td>
<td>2.9</td>
<td>2.5</td>
<td>2.4</td>
<td>3.0</td>
</tr>
<tr>
<td>Nominal GDP (in billions of ALL)</td>
<td>624.7</td>
<td>682.7</td>
<td>766.1</td>
<td>836.6</td>
<td>896.3</td>
<td>978.9</td>
</tr>
</tbody>
</table>

Fiscal indicators (as a share to GDP)

| Fiscal deficit (with grants) | -6.6 | -4.5 | -5.1 | -3.6 | -3.1 | -3.9 |
| Domestic borrowing          | -3.3 | -2.9 | -2.3 | -2.7 | -2.2 | -2.0 |
| Revenues                    | 24.7 | 24.5 | 24.1 | 24.4 | 25.7 | 25.9 |
| Expenditure                 | 31.4 | 29.0 | 29.2 | 28.0 | 28.9 | 29.8 |

External sector

| Trade deficit (in millions of EUR) | -1,214 | -1,248 | -1,307 | -1,617 | -1,707 | -1,853 |
| Current account deficit (% to GDP) | -10.0  | -8.1   | -5.5   | -7.5   | -7.2   | -7.5   |

Monetary indicators (as a share to GDP)

| Monetary supply | 65.3 | 65.0 | 65.7 | 68.4 | 73.3 | 75.0 |
| Credit to private sector | 6.4  | 7.7  | 9.4  | 14.9 | 20.8 | 25.5 |
| Interest of 12-month treasury bills | 12.0 | 9.5  | 8.1  | 6.9  | 7.8  | --   |

* Preliminary data, • Projections
** Primary deficit excludes expenses of Government debt interests.
Source: Bank of Albania, Ministry of Finance, INSTAT
Macroeconomic balance and fiscal sector

The macroeconomic framework for 2007 projects a slight increase of domestic savings in economy, accounting for about 19.9 per cent of the GDP, against 19.2 in the previous year, mainly from the private sector. This increase in savings is expected to be entirely channelled in the financing of supplementary investment. The average level of investments over the recent years varied to about 24 per cent of the GDP and their growth of 26 per cent in 2007 is projected to improve the performance of exports in economy for the upcoming periods. Under these conditions, the savings-investment balance is projected to about 6.2 per cent. This high ratio implies the aggravation of the current account (in the same level of 6.2 per cent), although the exports-imports balance varies to 23.3 per cent, as in 2006.

Positive is the fact that the increase of the savings-investments macroeconomic balance and the aggravation of the current account are a result of the higher growth rate of investments, a tendency which promotes the economic and exports growth in the long run. Moreover, the higher level of savings is entirely based on the increase of the private sector’s savings, while the level of public sector’s savings is projected to account for about 2.5 per cent of the GDP, as in 2006.

The fiscal account contribution to the increase of savings-investments balance is projected to account for about 4.6 per cent of the GDP, while the rest makes up the private sector’s deficit. The Government fiscal projections provide for the financing of the fiscal deficit through domestic borrowing to 2.5 per cent and external sources finances to about 2 per cent.

Monetary sector

Based on the projections related to the growth of credit to the private sector and of Government borrowing, broad money is expected to grow by about 11.9 per cent in 2007. Moreover, the growth of M2 monetary aggregate is projected to about 11.4 per cent.

Money supply growth over 2007 will be a result of the growth of credit to economy by about ALL 63.3 billion and of the Government borrowing financing by the banking system, by about ALL 12 billion. The other share of domestic borrowing for the financing of deficit is projected to be covered by other financial institutions and households. The current projections concerning money supply and credit indicators are conditioned by the monetary policy stance related to inflation forecasts. The projected growth of money supply for 2007 is in line with an average inflation rate of about 3 per cent. The financial markets development and further deepening is expected to be positively influenced by the presence of Government securities of long-term maturity. The dynamics of demand for money requires the maintenance of an upward tendency of interest rates in the market. Moreover, the stable current account and the projections for an inflation rate being close to the objective are expected to provide a positive contribution to maintaining exchange rate stability.
ENDNOTES

1 FOMC - Federal Open Market Committee.
2 Real effective exchange rate calculated as the weighted average of a country’s currency relative to a basket of the country’s main trade partners.
3 Agriculture not included. Agro industry is included in ‘Processing industry’.
4 According to the supplementary budget.
5 Referring to the nominal effective exchange rate calculated by the Bank of Albania.
6 Source: ISTAT; web page: http://www.istat.it
7 Source: National Statistical Service of Greece; web page: http://www.statistics.gr
8 Source: Eurostat, web page: http://epp.eurostat.cec.eu.int
9 Source: National Statistical Service of Greece; web page: http://www.statistics.gr
10 Source: Italian National Statistics Institute; web page: http://www.istat.it
11 Source: EUROSTAT; web page: http://epp.eurostat.cec.eu.int
12 The Bank of Albania quantitative objectives are part of the new PRGF/EFF 2006-2008 arrangement, signed between the Albanian Government, the IMF and the Bank of Albania in January 2006.
13 The significant reduction of credit to agriculture observed from June 2006 mainly reflects the changes in reporting, according to the reassessment of one of the largest bank’s credit portfolio in the banking system.
14 The operative data for December indicate that the Government only issued bonds of 2-year maturity, amounting to ALL 3 billion.
15 See: Statistical Annex; Financial Markets; Table 10 “End-month interest rates and their change to previous periods”.
16 Issued for the first time in April 2006.
17 See: Statistical Annex; Financial Markets; Table 10 “End-month interest rates and their change to previous periods”.
18 Difference of ALL credit and deposits interests of 6- and 12-month maturity.
19 The most recent data refer to November 2006.
20 Excluding demand deposits interests and credit interests of 1-3 years maturity.
21 See: Statistical Annex; Financial Markets; Table 12 “Interest rates of deposits in foreign currency”.
22 Excluding the ALL and EUR deposits interests of 3-month maturity, whose difference has increased compared to June.
23 NEER – nominal effective exchange rate measured against two currencies according to an approximate share they have in trade with abroad, EUR (80 per cent) and USD (20 per cent). December 2001: NEER = 100. An increase of the NEER implies the lek appreciation.
24 Calculated as the quarterly average of the exchange rate volatility. Exchange rate volatility is measured as the standard deviation \( \sum (x_i - \bar{i})^2/n - 1 \), where \( x_i \) is the exchange rate in period \( i \), \( \bar{i} \) is the average of period \( i \) (for example, the exchange rate in a day of a given month in year \( i \) minus the average rate of
the month in year i).

25 The difference corresponds with the aggravation of the balance of revenues from transfers from abroad.

26 According to the Government budget data approved by the Parliament, which projects privatization revenues to account for 0.1 per cent of the GDP.
### Inflation

#### Table 1 Annual Inflation Rates (in Percentage)

<table>
<thead>
<tr>
<th>Month</th>
<th>2001</th>
<th>2002</th>
<th>2003</th>
<th>2004</th>
<th>2005</th>
<th>2006</th>
</tr>
</thead>
<tbody>
<tr>
<td>January</td>
<td>2.2</td>
<td>6.5</td>
<td>0.0</td>
<td>3.3</td>
<td>3.3</td>
<td>1.4</td>
</tr>
<tr>
<td>February</td>
<td>1.5</td>
<td>7.6</td>
<td>1.1</td>
<td>4.4</td>
<td>1.8</td>
<td>1.3</td>
</tr>
<tr>
<td>March</td>
<td>2.9</td>
<td>7.5</td>
<td>1.3</td>
<td>4.0</td>
<td>1.6</td>
<td>1.5</td>
</tr>
<tr>
<td>April</td>
<td>3.0</td>
<td>6.5</td>
<td>2.3</td>
<td>3.2</td>
<td>1.3</td>
<td>2.4</td>
</tr>
<tr>
<td>May</td>
<td>2.5</td>
<td>4.6</td>
<td>2.8</td>
<td>2.6</td>
<td>2.0</td>
<td>3.1</td>
</tr>
<tr>
<td>June</td>
<td>4.0</td>
<td>3.7</td>
<td>2.6</td>
<td>2.9</td>
<td>2.9</td>
<td>2.4</td>
</tr>
<tr>
<td>July</td>
<td>5.6</td>
<td>4.2</td>
<td>3.0</td>
<td>3.1</td>
<td>1.8</td>
<td>3.2</td>
</tr>
<tr>
<td>August</td>
<td>4.1</td>
<td>5.5</td>
<td>3.0</td>
<td>2.7</td>
<td>2.3</td>
<td>2.9</td>
</tr>
<tr>
<td>September</td>
<td>3.5</td>
<td>5.3</td>
<td>2.8</td>
<td>2.0</td>
<td>3.1</td>
<td>2.6</td>
</tr>
<tr>
<td>October</td>
<td>1.8</td>
<td>5.8</td>
<td>2.9</td>
<td>2.0</td>
<td>3.3</td>
<td>2.3</td>
</tr>
<tr>
<td>November</td>
<td>2.8</td>
<td>3.7</td>
<td>3.4</td>
<td>2.2</td>
<td>3.0</td>
<td>2.9</td>
</tr>
<tr>
<td>December</td>
<td>3.5</td>
<td>1.7</td>
<td>3.3</td>
<td>2.2</td>
<td>2.0</td>
<td>2.5</td>
</tr>
<tr>
<td>Average</td>
<td>3.1</td>
<td>5.2</td>
<td>2.2</td>
<td>3.0</td>
<td>2.4</td>
<td>2.4</td>
</tr>
</tbody>
</table>

Source: INSTAT

#### Table 2 Contribution of Basket Constituent Groups to Total Inflation

<table>
<thead>
<tr>
<th>Month</th>
<th>March-06</th>
<th>April-06</th>
<th>May-06</th>
<th>June-06</th>
<th>July-06</th>
<th>August-06</th>
<th>September-06</th>
<th>October-06</th>
<th>November-06</th>
<th>December-06</th>
</tr>
</thead>
<tbody>
<tr>
<td>Foodstuffs and non-alcoholic beverages</td>
<td>0.16</td>
<td>1.03</td>
<td>1.51</td>
<td>0.80</td>
<td>1.86</td>
<td>0.51</td>
<td>-0.45</td>
<td>-0.59</td>
<td>0.45</td>
<td>0.09</td>
</tr>
<tr>
<td>Rent, water, fuels and energy</td>
<td>0.85</td>
<td>0.84</td>
<td>1.00</td>
<td>1.04</td>
<td>0.88</td>
<td>1.78</td>
<td>2.32</td>
<td>2.19</td>
<td>1.91</td>
<td>1.87</td>
</tr>
<tr>
<td>Transport</td>
<td>0.14</td>
<td>0.13</td>
<td>0.23</td>
<td>0.24</td>
<td>0.19</td>
<td>0.13</td>
<td>0.10</td>
<td>0.09</td>
<td>0.08</td>
<td>0.05</td>
</tr>
<tr>
<td>Hotels, café and restaurant</td>
<td>0.20</td>
<td>0.22</td>
<td>0.22</td>
<td>0.22</td>
<td>0.16</td>
<td>0.18</td>
<td>0.18</td>
<td>0.15</td>
<td>0.15</td>
<td>0.14</td>
</tr>
<tr>
<td>Other</td>
<td>0.11</td>
<td>0.12</td>
<td>0.10</td>
<td>0.15</td>
<td>0.15</td>
<td>0.24</td>
<td>0.40</td>
<td>0.40</td>
<td>0.32</td>
<td>0.40</td>
</tr>
<tr>
<td>Total</td>
<td>1.48</td>
<td>2.35</td>
<td>3.1</td>
<td>2.45</td>
<td>3.24</td>
<td>2.84</td>
<td>2.55</td>
<td>2.24</td>
<td>2.91</td>
<td>2.55</td>
</tr>
</tbody>
</table>

Source: INSTAT, Bank of Albania

### Monetary Aggregates

#### Table 3 Performance of Monetary Aggregates (in Billions of ALL)

<table>
<thead>
<tr>
<th></th>
<th>November-06</th>
<th>Monthly change</th>
<th>Annual change</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Absolute</td>
<td>Percentage</td>
<td>Absolute</td>
</tr>
<tr>
<td>Currency outside banks</td>
<td>146.3</td>
<td>0.5</td>
<td>0.3</td>
</tr>
<tr>
<td>Total deposits</td>
<td>491.7</td>
<td>2.2</td>
<td>0.5</td>
</tr>
<tr>
<td>- in lek</td>
<td>303.3</td>
<td>3.2</td>
<td>1.1</td>
</tr>
<tr>
<td>- in foreign currency</td>
<td>188.4</td>
<td>-1.0</td>
<td>-0.5</td>
</tr>
<tr>
<td>Demand deposits</td>
<td>146.9</td>
<td>-3.4</td>
<td>-2.3</td>
</tr>
<tr>
<td>- in lek</td>
<td>80.5</td>
<td>0.8</td>
<td>1.1</td>
</tr>
<tr>
<td>- in foreign currency</td>
<td>66.3</td>
<td>-4.3</td>
<td>-6.1</td>
</tr>
<tr>
<td>Time deposits</td>
<td>344.9</td>
<td>5.7</td>
<td>1.7</td>
</tr>
<tr>
<td>- in lek</td>
<td>222.7</td>
<td>2.4</td>
<td>1.1</td>
</tr>
<tr>
<td>- in foreign currency</td>
<td>122.1</td>
<td>3.3</td>
<td>2.7</td>
</tr>
<tr>
<td>M1</td>
<td>226.9</td>
<td>1.3</td>
<td>0.6</td>
</tr>
<tr>
<td>M2</td>
<td>449.6</td>
<td>3.7</td>
<td>0.8</td>
</tr>
<tr>
<td>M3</td>
<td>638.0</td>
<td>2.7</td>
<td>0.4</td>
</tr>
<tr>
<td>Monetary base</td>
<td>209.3</td>
<td>3.6</td>
<td>1.7</td>
</tr>
</tbody>
</table>

Source: Bank of Albania
Table 4 Performance of NFA indicators by main groups (in millions of USD)

<table>
<thead>
<tr>
<th></th>
<th>November - 06</th>
<th>Monthly change</th>
<th>Annual change</th>
</tr>
</thead>
<tbody>
<tr>
<td>Net foreign assets</td>
<td>2,440.7</td>
<td>35.7</td>
<td>393.4</td>
</tr>
<tr>
<td>Foreign assets</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Bank of Albania</td>
<td>1,700.0</td>
<td>45.0</td>
<td>332.5</td>
</tr>
<tr>
<td>ODC</td>
<td>1,105.6</td>
<td>18.6</td>
<td>196.1</td>
</tr>
<tr>
<td>Foreign liabilities</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Bank of Albania</td>
<td>108.8</td>
<td>1.9</td>
<td>3.1</td>
</tr>
<tr>
<td>ODC</td>
<td>256.1</td>
<td>26.0</td>
<td>132.1</td>
</tr>
</tbody>
</table>

Source: Bank of Albania

Table 5 Net Claims on the Government by main groups (in millions of ALL)

<table>
<thead>
<tr>
<th>Net claims of the Government</th>
<th>November - 06</th>
<th>Monthly changes</th>
<th>Annual changes</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bank of Albania</td>
<td>275,738.3</td>
<td>1,258.5</td>
<td>3,014.5</td>
</tr>
<tr>
<td>ODC</td>
<td>225,509.2</td>
<td>3,461.7</td>
<td>28.7</td>
</tr>
<tr>
<td>Deposits held with the Bank of Albania</td>
<td>10,655.9</td>
<td>3,448.2</td>
<td>11,845.6</td>
</tr>
</tbody>
</table>

Source: Bank of Albania

Table 6 Performance of some main indicators

<table>
<thead>
<tr>
<th></th>
<th>2003</th>
<th>2004</th>
<th>2005</th>
<th>2006</th>
</tr>
</thead>
<tbody>
<tr>
<td>Money supply (in billions of ALL)</td>
<td>448.4</td>
<td>507.2</td>
<td>541.8</td>
<td>578.04</td>
</tr>
<tr>
<td>Domestic credit (in percentage to M3)</td>
<td>71.5</td>
<td>68.9</td>
<td>69.9</td>
<td>70.03</td>
</tr>
<tr>
<td>Credit to Government (in percentage to M3)</td>
<td>60.2</td>
<td>55.1</td>
<td>52.2</td>
<td>48.94</td>
</tr>
<tr>
<td>Credit to economy (in percentage to M3)</td>
<td>11.3</td>
<td>13.8</td>
<td>17.7</td>
<td>21.10</td>
</tr>
<tr>
<td>Credit to economy (in percentage to total assets)</td>
<td>13.7</td>
<td>16.9</td>
<td>20.8</td>
<td>25.11</td>
</tr>
<tr>
<td>Credit to economy (in percentage to GDP)</td>
<td>6.8</td>
<td>9.0</td>
<td>11.2</td>
<td>14.57</td>
</tr>
<tr>
<td>Credit/deposits ratio (in percentage)</td>
<td>15.7</td>
<td>19.0</td>
<td>23.6</td>
<td>28.47</td>
</tr>
</tbody>
</table>

Source: Bank of Albania

Table 7 Outstanding credit indicators as a share to total

<table>
<thead>
<tr>
<th>Outstanding credit (in billions of ALL)</th>
<th>2003</th>
<th>2004</th>
<th>2005</th>
<th>Q1 '06</th>
<th>Q2 '06</th>
<th>Q3 '06</th>
<th>October '06</th>
<th>November '06</th>
</tr>
</thead>
<tbody>
<tr>
<td>Credit to households</td>
<td>50.7</td>
<td>69.3</td>
<td>121.6</td>
<td>134.6</td>
<td>152.8</td>
<td>165.3</td>
<td>172.8</td>
<td>179.5</td>
</tr>
<tr>
<td>Credit to private sector</td>
<td>75.5</td>
<td>69.4</td>
<td>67.7</td>
<td>68.1</td>
<td>67.6</td>
<td>66.7</td>
<td>66.7</td>
<td>66.6</td>
</tr>
<tr>
<td>Short-term credit</td>
<td>46.0</td>
<td>34.0</td>
<td>32.3</td>
<td>32.5</td>
<td>31.1</td>
<td>30.0</td>
<td>29.6</td>
<td>28.8</td>
</tr>
<tr>
<td>Medium-term credit</td>
<td>33.3</td>
<td>36.0</td>
<td>29.7</td>
<td>30.0</td>
<td>31.2</td>
<td>32.6</td>
<td>32.3</td>
<td>33.2</td>
</tr>
<tr>
<td>Long-term credit</td>
<td>20.7</td>
<td>30.0</td>
<td>37.9</td>
<td>37.5</td>
<td>37.7</td>
<td>37.4</td>
<td>38.1</td>
<td>37.9</td>
</tr>
<tr>
<td>Lek</td>
<td>19.6</td>
<td>19.5</td>
<td>26.6</td>
<td>26.0</td>
<td>28.2</td>
<td>29.8</td>
<td>29.4</td>
<td>29.7</td>
</tr>
<tr>
<td>Foreign currency</td>
<td>80.4</td>
<td>80.5</td>
<td>73.4</td>
<td>74.0</td>
<td>71.8</td>
<td>70.2</td>
<td>70.6</td>
<td>70.3</td>
</tr>
</tbody>
</table>

Source: Bank of Albania

Table 8 New credit indicators as a share to total

<table>
<thead>
<tr>
<th>New credit (in billions of ALL)</th>
<th>2004</th>
<th>2005</th>
<th>2006</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total</td>
<td>99.7</td>
<td>32.8</td>
<td>32.9</td>
</tr>
<tr>
<td>Q1</td>
<td>22.1</td>
<td>32.1</td>
<td>32.9</td>
</tr>
<tr>
<td>Q2</td>
<td>53.2</td>
<td>47.4</td>
<td>48.7</td>
</tr>
<tr>
<td>Q3</td>
<td>22.4</td>
<td>31.0</td>
<td>25.6</td>
</tr>
<tr>
<td>Q4</td>
<td>14.93</td>
<td>22.2</td>
<td>25.7</td>
</tr>
<tr>
<td>Credit in lek</td>
<td>32.5</td>
<td>30.1</td>
<td>32.8</td>
</tr>
<tr>
<td>Credit in foreign currency</td>
<td>67.4</td>
<td>70</td>
<td>69.8</td>
</tr>
</tbody>
</table>

Source: Bank of Albania
### Table 9 Distribution of credit by sectors of economy (as a share to total)

<table>
<thead>
<tr>
<th>Sector</th>
<th>2004</th>
<th>2005</th>
<th>2006</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Total</td>
<td>Q1</td>
<td>Q2</td>
</tr>
<tr>
<td>Agriculture, Hunting and Silviculture</td>
<td>1.5</td>
<td>1.3</td>
<td>1.5</td>
</tr>
<tr>
<td>Fishing</td>
<td>0.1</td>
<td>0.01</td>
<td>0.1</td>
</tr>
<tr>
<td>Extracting Industry</td>
<td>0.3</td>
<td>2.35</td>
<td>0.6</td>
</tr>
<tr>
<td>Processing Industry</td>
<td>17.1</td>
<td>15.8</td>
<td>15.6</td>
</tr>
<tr>
<td>Production, Distribution of Energy, Gas and Water</td>
<td>2.8</td>
<td>6.27</td>
<td>2.9</td>
</tr>
<tr>
<td>Construction</td>
<td>9.8</td>
<td>10.6</td>
<td>11.2</td>
</tr>
<tr>
<td>Trade, Repair of Vehicles and Household Appliances</td>
<td>23.3</td>
<td>20.5</td>
<td>19.1</td>
</tr>
<tr>
<td>Hotels and Restaurants</td>
<td>8.3</td>
<td>2.5</td>
<td>4.7</td>
</tr>
<tr>
<td>Transport and Telecommunication</td>
<td>2</td>
<td>2.5</td>
<td>1.7</td>
</tr>
<tr>
<td>Financial Activities</td>
<td>0.2</td>
<td>0.2</td>
<td>1.1</td>
</tr>
<tr>
<td>Health and Social Activities</td>
<td>0.5</td>
<td>0.1</td>
<td>0.4</td>
</tr>
<tr>
<td>Collective, Social and Personal Services</td>
<td>4.8</td>
<td>8.3</td>
<td>7.4</td>
</tr>
<tr>
<td>Other*</td>
<td>29.1</td>
<td>29.6</td>
<td>33.7</td>
</tr>
<tr>
<td>Total</td>
<td></td>
<td>100</td>
<td>100</td>
</tr>
</tbody>
</table>

*Source: Bank of Albania*

*“Other” includes credit extended to some sectors sharing a small weight in the country’s economic activity and credit to households. Upon the introduction of new credit forms was required to review the credit distribution by sectors, where the new classification was introduced.*

### FINANCIAL MARKETS

#### Table 10 End-month interest rates and their change compared to previous periods (in percentage points)

<table>
<thead>
<tr>
<th>Sector</th>
<th>December ’06</th>
<th>Change December ’06 -November ’06</th>
<th>Change December ’06 – June ’06</th>
</tr>
</thead>
<tbody>
<tr>
<td>Core interest rate*</td>
<td>5.50%</td>
<td>+0.25</td>
<td>+0.50</td>
</tr>
<tr>
<td>Interbank market</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Overnight interest</td>
<td>4.52</td>
<td>+0.42</td>
<td>+0.31</td>
</tr>
<tr>
<td>Weekly interest</td>
<td>5.24</td>
<td>+0.26</td>
<td>+0.09</td>
</tr>
<tr>
<td>3-month Treasury bills yield</td>
<td>6.25%</td>
<td>+0.01</td>
<td>+1.02</td>
</tr>
<tr>
<td>6-month Treasury bills yield</td>
<td>7.18%</td>
<td>+0.31</td>
<td>+1.76</td>
</tr>
<tr>
<td>12-month Treasury bills yield</td>
<td>7.88%</td>
<td>+0.34</td>
<td>+2.14</td>
</tr>
<tr>
<td>Bonds market</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2-year bonds yield</td>
<td>8.40%</td>
<td>0.00</td>
<td>+2.01</td>
</tr>
<tr>
<td>3-year bonds yield</td>
<td>8.80%</td>
<td>-</td>
<td>+1.30</td>
</tr>
<tr>
<td>5-year bonds yield</td>
<td>9.68%</td>
<td>-</td>
<td>-</td>
</tr>
</tbody>
</table>

*Source: Bank of Albania and commercial banks*

*Core interest rate throughout November was 5.25 per cent. On 30 November, it was increased to 5.50 per cent.*
### Table 11 Interest rates and their change in the lek deposits and credit market (in percentage points)

<table>
<thead>
<tr>
<th></th>
<th>November '06</th>
<th>Change November '06 – October '06</th>
<th>Change November '06 – June '06</th>
</tr>
</thead>
<tbody>
<tr>
<td>Core interest rate</td>
<td>5.25%</td>
<td>0.00%</td>
<td>0.25%</td>
</tr>
<tr>
<td>Interest of deposits in lek</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>3-month</td>
<td>3.86%</td>
<td>0.01%</td>
<td>0.12%</td>
</tr>
<tr>
<td>6-month</td>
<td>4.51%</td>
<td>0.01%</td>
<td>0.16%</td>
</tr>
<tr>
<td>12-month</td>
<td>5.33%</td>
<td>0.13%</td>
<td>0.28%</td>
</tr>
<tr>
<td>24-month</td>
<td>5.59%</td>
<td>-0.19%</td>
<td>-0.31%</td>
</tr>
<tr>
<td>Interest of credit in lek</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Up to 6-month credit</td>
<td>15.61%</td>
<td>0.41%</td>
<td>4.33%</td>
</tr>
<tr>
<td>6-month to 1 year credit</td>
<td>13.99%</td>
<td>-1.23%</td>
<td>2.19%</td>
</tr>
<tr>
<td>1-3 years credit</td>
<td>17.26%</td>
<td>0.42%</td>
<td>1.37%</td>
</tr>
<tr>
<td>Over 3-year credit</td>
<td>13.03%</td>
<td>0.68%</td>
<td>1.61%</td>
</tr>
</tbody>
</table>

Source: Bank of Albania and commercial banks

### Table 12 Interest rates of deposits in foreign currency (in percentage points)

<table>
<thead>
<tr>
<th></th>
<th>November – '06</th>
<th>Change November '06 – October '06</th>
<th>Change November '06 – June '06</th>
</tr>
</thead>
<tbody>
<tr>
<td>Fed – Core interest rate</td>
<td>5.25%</td>
<td>+0.00%</td>
<td>+0.25%</td>
</tr>
<tr>
<td>Interest of deposits in USD</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>1-month</td>
<td>3.01%</td>
<td>-0.07%</td>
<td>0.67%</td>
</tr>
<tr>
<td>3-month</td>
<td>3.61%</td>
<td>0.09%</td>
<td>0.08%</td>
</tr>
<tr>
<td>6-month</td>
<td>3.81%</td>
<td>0.05%</td>
<td>0.40%</td>
</tr>
<tr>
<td>12-month</td>
<td>4.79%</td>
<td>0.20%</td>
<td>0.97%</td>
</tr>
<tr>
<td>24-month</td>
<td>4.72%</td>
<td>-0.04%</td>
<td>0.34%</td>
</tr>
<tr>
<td>ECB – Core interest rate</td>
<td>3.25%</td>
<td>+0.25%</td>
<td>+0.75%</td>
</tr>
<tr>
<td>Interest of deposits in EUR</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>1-month</td>
<td>2.71%</td>
<td>0.24%</td>
<td>0.58%</td>
</tr>
<tr>
<td>3-month</td>
<td>2.85%</td>
<td>0.08%</td>
<td>0.42%</td>
</tr>
<tr>
<td>6-month</td>
<td>3.10%</td>
<td>-0.07%</td>
<td>0.19%</td>
</tr>
<tr>
<td>12-month</td>
<td>3.45%</td>
<td>0.03%</td>
<td>0.41%</td>
</tr>
<tr>
<td>24-month</td>
<td>4.13%</td>
<td>0.07%</td>
<td>0.50%</td>
</tr>
</tbody>
</table>

Source: Bank of Albania and commercial banks

### Table 13 Interest rate spread of deposit – credit in lek and in foreign currency

#### Spread of deposit interest

<table>
<thead>
<tr>
<th></th>
<th>ALL-USD</th>
<th>ALL-EUR</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>June ’06</td>
<td>November ’06</td>
</tr>
<tr>
<td>3-month</td>
<td>0.21%</td>
<td>0.25%</td>
</tr>
<tr>
<td>6-month</td>
<td>0.94%</td>
<td>0.70%</td>
</tr>
<tr>
<td>12-month</td>
<td>1.23%</td>
<td>0.54%</td>
</tr>
</tbody>
</table>

#### Spread of credit interest

<table>
<thead>
<tr>
<th></th>
<th>ALL-USD</th>
<th>ALL-EUR</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>June ’06</td>
<td>November ’06</td>
</tr>
<tr>
<td>6-month</td>
<td>2.00%</td>
<td>6.82%</td>
</tr>
<tr>
<td>6-month – 1 year</td>
<td>0.58%</td>
<td>2.42%</td>
</tr>
<tr>
<td>1-3 years</td>
<td>6.25%</td>
<td>7.25%</td>
</tr>
<tr>
<td>Over 3 years</td>
<td>2.64%</td>
<td>3.87%</td>
</tr>
</tbody>
</table>

Source: Bank of Albania and commercial banks
EXTERNAL SECTOR DEVELOPMENTS OF THE ALBANIAN ECONOMY OVER THE FIRST NINE MONTHS OF 2006
JANUARY 2007

The overall balance of payments for the first nine-month period of 2006 resulted in a surplus of EUR 121.1 million. Capital inflows financed 71.4 per cent of the current deficit.

The main developments in the external sector of the Albanian economy may be summarized in:

• Intensive activity in the external sector, expressed in the increase of current revenues and expenditure.
• Current and trade deficit deepening.
• Increase of the country’s financial assets to non-residents, mainly expressed in the increase of financial assets held by the banking system in the form of deposits abroad.
• Increase of the monetary authority foreign reserve.

I. CURRENT ACCOUNT

The volume of current transactions is assessed to have grown by about 14.5 per cent, in annual terms, recording a total of EUR 5 billion. More than 96 per cent of current expenditure was used for the purchase of goods and services from non-residents. Around 30 per cent of current revenues were in the form of current transfers, while the exports of goods and services have provided 20 per cent and 38 per cent of revenues, respectively.

Trade deficit, a permanent feature of foreign trade developments, continued to affect the high levels of current account deficit. As opposed to the previous year, current deficit recorded an increase of about 51.6 per cent, amounting to EUR 410.6 million. The increase of trade deficit in goods and services was partly offset by the increase of net revenues and of net factorial revenues in transfer accounts.

I. 1. FOREIGN TRADE

Albania’s trade activity over the first nine months of 2006 recorded EUR 2.1 billion, accounting for 42 per cent of current transactions volume carried out over the period. The overwhelming import-orientation of the Albanian economy continues to be considered a characteristic of this period, resulting in further deepening of trade deficit (18 per cent). The coverage of the high demand for consumption and investment by import goods, the continuous
expansion of credit to economy over the recent years, and the rise of several products’ prices in the international markets remain among the most significant factors for the high imports over this period.

Imports expenditure amounted to EUR 1.7 billion, while exports contributed by EUR 463 million. From the dynamics viewpoint, the growth rates of both imports and exports were almost in the same levels, accounting for 17.3 per cent and 16.3 per cent, respectively. Exports managed to cover only 27 per cent of imports over this period, which is similar to the corresponding period the previous year.

According to an analysis in harmony with the system of national accounts, our country continues to remain oriented to intermediate goods, which share almost half of our imports (47 per cent), while capital and consumer goods shared 11 and 32 per cent, respectively.

Active processing industry, which dominates Albania’s trade activity with the rest of the world, was characterized by upward tendencies over this period, following the slowdown displayed over the last two years. Regardless of the continuous increase of global competition from low-cost production countries (China, in particular), of the lek and of the economic slowdown of Italy and Greece (our main exports’ markets) over this period, almost all domestic processing sectors have expanded. Exports experienced the most rapid growth by 17 per cent, while raw material imports grew by 13 per cent, compared to the same period the previous year. The share levels of exports and imports for further processing were 70 per cent and 14 per cent, respectively, to the total.

The geographical structure continues to show significant representation of European markets, sharing about 81 per cent of all trade transactions. Except the traditional partners (Italy and Greece), Turkey, China and Germany are among the countries Albania has established import-relations with.

Free trade agreements with the regional countries seem to have provided their effects on exports, as well. Bosnia and Herzegovina, Serbia and Montenegro are among the new markets, while exports with Kosovo have maintained constant trends and a moderate growth.

I. 2. DEVELOPMENTS IN OTHER ITEMS OF CURRENT ACCOUNT

Trade in services, which has been characterized by upward growth rates over the recent years, is ever-increasingly becoming a pivotal factor of Albania’s integration with abroad. Trade transactions in services amounted to about EUR 1.9 billion, which is 22 per cent higher than the same period the previous year. Services account ended up with a negative balance of EUR 61 million, representing a decrease of about 30 per cent to the previous year deficit. The upgrade of services’ deficit position came mainly as a result of the reduction of deficit in “Other services”, due to the expansion of exports for this category of services.
This year’s deficit in services is attributed to the negative balance in “Transport services” and in “Other services”; while “Travel” maintained its surplus position.

“Tourism” (travel) services continue to make a considerable contribution to this item’s inflows and outflows, sharing 69 and 61 per cent, respectively, of the total for this nine-month period. Currently, tourism represents to the Albanian economy one of the main sources of foreign inflows. According to the Bank of Albania estimates, exports on travel services generated about EUR 614 million over the first nine months of 2006, which is about 33 per cent higher than the exports of goods. Income from tourism is assessed to be 19 per cent higher than the same period over 2005, mainly influenced by the increasing number of foreign visitors and expatriates visiting the country over the first months and by the slight increase of daily expenditure estimating coefficients. The number of foreign citizens visiting Albania over the first nine months of 2006 increased by 26 per cent compared to the same period the previous year.

Tourism expenditure has also had an accelerated activity, being characterized by higher annual growth rates. Albanian residents have spent in their travels abroad around EUR 583 million or 85 per cent of total workers’ remittances. The increase of Albanian travellers’ expenditure abroad is higher than the increase of income, causing the positive balance of this item to reduce from EUR 38 to 30 million over the first nine months of 2006.

The developments in “Other services”, accounting for 21 per cent to total volume, provide evidence for an increasing trade activity, both in terms of income and of expenditure.

This period has recorded a deficit of EUR 29 million, against the deficit of EUR 56 million recorded over the same period the previous year. The export of these services increased by 50 per cent, while the import by 20 per cent to the previous year. This category of services is headed by trade transactions in communication, cultural and business services.

The positive balance of income at the end of the period is assessed to have totalled about EUR 161 million or EUR 60 million more than the same period the previous year. Unlike the previous years, when revenues from labour constituted the main contribution to the country’s net factorial revenues, over the first nine months we observe an acceleration of investment revenues flow. Net revenues from portfolio investment are assessed to have increased by about four times as high as compared to the first nine months of 2005, contributing to the increase of revenues surplus by 80 per cent for this period. The rest of revenues, provided by revenues from labour, increased by about 17 per cent.

As in the previous years, current transfers were in the form of workers’ remittances. The latter represent one of the main sources of financing the deficit in the trade of goods and services. Over the first nine-month period of
2006 they amounted to EUR 683 million, which is EUR 24 million more than the same period the previous year.

Workers’ remittances were also accompanied by official transfers, mainly in the form of technical assistance (EUR 42 million), which are assessed to have maintained the previous year level.

II. CAPITAL AND FINANCIAL ACCOUNT

Net capital flows amounted to about EUR 293 million over the first nine months, enabling the financing of current deficit at 71 per cent and contributing to the increase of foreign reserve. Behind this positive figure rest the incoming capital transfers totalling EUR 143.7 million and the positive balance of financial account amounting to about EUR 150 million.

Financial account for this period may be defined in the increase of Albania’s financial liabilities with the rest of the world (by about EUR 320 million) and in the increase of our assets abroad (about EUR 171 million). As opposed to the same period the previous year, financial liabilities flow is assessed to have increased by 39.3 per cent, while Albania’s financial claims on the rest of the world were assessed as increasing by twice as high. However, the net flow of financial liabilities is estimated to have increased by only EUR 5 million, compared to the previous year.

The increase of financial liabilities to the rest of the world over the first nine months was mainly a consequence of the capital inflows in the form of direct investment (EUR 201 million) and of borrowing from abroad (EUR 101 million).

Foreign direct investments are assessed to be 5.3 per cent higher than the same period the previous year. These capital flows have now turned into a dominating factor in the increase of financial liabilities and in the development of the country’s capital and financial transactions.

The borrowing of long-term and soft loans from abroad, which remain another important factor in the increase of Albania’s financial liabilities to the rest of the world, recorded EUR 101 million, out of which only 91 per cent flows from public borrowing. Unlike the previous year, when there was an increase of private sector’s liabilities through borrowing, they have increased by only EUR 8.6 million over the first nine-month, which accounts for only 18 per cent of the previous year increase.

Foreign debt services in the form of principal and interest payments totalled about EUR 45 million, which is equal to 9.7 per cent of the exports of goods.

On the other hand, Albania’s financial claims on the rest of the world increased by EUR 171.1 million. The increase of these assets was mainly
determined by the increase of financial assets held by the banking system in the form of deposits abroad. Meanwhile, portfolio investments of resident entities abroad have been decreasing.

Financial assets stock in the form of portfolio investment recorded EUR 90.6 million as of end period, representing a decrease of EUR 23 million. In terms of structure by denomination, 78 per cent is shared by the USD and 17 per cent by the EUR.

Foreign assets held by the banking system in the form of deposits abroad increased by about EUR 191 million, over the first nine months. Such an increase came due to the increase of residents and non-residents’ deposits held in our banking system, which were invested in the international financial institutions. This increase also derives from the shift of assets from portfolio investment to deposits with abroad. In terms of structure by denomination, USD deposits share 60.2 per cent, while EUR deposits share 35.2 per cent.

Foreign assets inflows in the form of financial capital were reflected in the increase of the monetary authority’s foreign reserve by about EUR 121 million. The level of gross foreign reserve, as of end period, amounted to EUR 1.294 billion, fully sufficient to cover 4.4 months of imports of goods and services.

<table>
<thead>
<tr>
<th>Table 1 Balance of payments</th>
</tr>
</thead>
<tbody>
<tr>
<td>In millions of EUR</td>
</tr>
<tr>
<td>Current account, nie.</td>
</tr>
<tr>
<td>Merchandise: exports, fob</td>
</tr>
<tr>
<td>Merchandise: imports, fob</td>
</tr>
<tr>
<td>Trade balance</td>
</tr>
<tr>
<td>Services: credit</td>
</tr>
<tr>
<td>Services: debit</td>
</tr>
<tr>
<td>Income: credit</td>
</tr>
<tr>
<td>Income: debit</td>
</tr>
<tr>
<td>Private unrequired transfers</td>
</tr>
<tr>
<td>Official unrequired trans., Nie</td>
</tr>
<tr>
<td>Capital account</td>
</tr>
<tr>
<td>Financial account</td>
</tr>
<tr>
<td>Direct investment, nie</td>
</tr>
<tr>
<td>Portfolio investment, nie</td>
</tr>
<tr>
<td>Other capital, nie*</td>
</tr>
<tr>
<td>Net errors and omissions</td>
</tr>
<tr>
<td>Overall balance</td>
</tr>
<tr>
<td>Reserve and related items</td>
</tr>
<tr>
<td>Reserve assets</td>
</tr>
<tr>
<td>Use of Fund credit and loans</td>
</tr>
<tr>
<td>Memorandum items</td>
</tr>
<tr>
<td>Total change in reserve assets</td>
</tr>
<tr>
<td>Of which: revaluation</td>
</tr>
</tbody>
</table>

* is not included use of IMF credit and loans
Source: Bank of Albania
GREETING SPEECH BY MR. ARDIAN FULLANI, GOVERNOR OF THE BANK OF ALBANIA
Sheraton Hotel, 30 October 2006

Honorable Mr. Prime Minister,
Honorable Colleagues,
Honorable participants

It’s a great pleasure and a privilege to open the proceedings of the Sixth Annual Conference of the Bank of Albania and to welcome you in Tirana.

This conference will focus on financial stability. The analysis and understanding of imbalances in the financial markets and of their causes is essential in central banking. The extent of social benefits and advantages that money, as a public good, creates for the society is dependent on the efficiency and capacity of financial markets to facilitate trade, production, capital accumulation, economic growth and social welfare.

Therefore, financial stability may be regarded as a “public good” and hence represents a public economic policy objective. The question is who is in charge of providing this good? Personally, my attention has been drawn by Paul Volker who describes the natural role of central banks in ensuring the financial stability. The central bank’s traditional role, as lender of last resort on one hand, and as monetary policy authority on the other, requires that central banks ensure financial stability in both standpoints as a provider and a beneficiary. Our role of monitoring the contagion process and financial and monetary crises, illustrates this idea very well. At the same time, the monetary transmission mechanism is another factor that witnesses the vested interest of the central bank in preserving the soundness of the financial system.

The developments observed in the last decades, and particularly in the ’90, brought the importance of financial stability to the fore and highlighted its key position among the most important economic policy objectives assigned to monetary authorities across the world. In spite of the emphasis and the vast literature on the issue, it is difficult to give a widely accepted definition of “financial stability”. Definitions of well-known academics and colleagues describe financial stability as a set of decisions and policies that deal with macroeconomic, monetary, supervisory aspects of economy and regulations of financial markets. I am confident, that those characteristics of financial stability will be widely covered in the proceedings of this conference.

After a long deliberation of literature, I chose Garry Schinasi (2005) to define the financial stability, and I quote him: “Financial stability is a condition, in which an economy’s mechanisms for pricing, allocating, and managing
financial risks are functioning well enough to contribute to the performance of the economy”¹. This definition implies that the financial system is capable of accomplishing appropriately its three main roles. Firstly, the financial system is capable to achieve effective distribution of economic resources over time. Secondly, it identifies and manages appropriately financial risks. Thirdly, it can softly absorb shocks and surprises that occur in the financial system and the real economy.

I think that the goal of this conference is to analyze financial markets concentrating on these three aspects, and to steer our efforts towards evaluating and guaranteeing the achievement of financial stability in our region. Our economies are quickly developing, and they are experiencing rapid changes, and we, as representatives of central banking in our countries, must adapt to these changes and promote growth without losing sight of prudential supervision. Latest trends towards expansion, liberalization and privatization of the financial system in the context of a fast-paced globalization of the world economy have put the goal of financial stability on top of the priorities in our region.

During the last few years, the financial sector has recorded positive growth rates in all countries in our region. However, I think that the merit for such a growth goes to the most vital segment of the financial system, that is, the banking system. The key factor to the successful growth and consolidation of the banking system has been the rapid privatization of banks, which is, at present, almost complete. This process has opened the way to the arrival of well-known international banks that have brought foreign capital, expertise and confidence in the region. The entry of those banks, besides the positive aspect of fostering growth and development, calls for higher prudence in the supervisory role of the central banks.

As a result of the above developments, the degree of financial intermediation in our region has further increased. Credit to economy has played a considerable role towards the deepening of financial intermediation. Albania has recently joined the group of countries experiencing a credit boom, as annual growth rates have been in the range of 60-70 per cent in the last two years.

An interesting indicator of banking system transformation is the EBRD indicator regarding “banking system reform and liberalization of interest rates”, which combines the quality of supervisory and regulatory base, the ownership structure of banking system and the degree of public access into the banking system. Based on latest data, Southeastern European Countries have progressed admirably with regard to their banking systems. It is crucial to understand that transformation of the banking system has been a key element in the long transition to a market economy. I want to emphasize that this process has brought development, has strengthened the macroeconomic stability, by positively influencing institution built-up and its consolidation, by encouraging faster structural reforms and the set up of regulatory frameworks related to economic policies.
Giving a glance at the Albanian banking system, I would emphasize that qualitative developments have taken place during 2006. The banking system assets during the first eight months of the year have been increased by 12 percent and are estimated at about 60 percent of Gross Domestic Product. The banking system results in profit, is liquid and capitalized. I would like to mention the entry of a new bank in our system, the Sao Paolo IMI Bank, which, besides its shares at the Italian-Albanian Bank, has preliminarily agreed with the owners of American-Albanian Bank to buy its 80 per cent of the shares. This opens the way to further consolidation of the banking system in Albania.

Now, let us give a glance at the rest of the financial system. It should be accepted that it still manifests problems of development and consolidation. The concerns relate to the magnitude of operators, the regulatory framework and particularly the supervision. In this way, their contribution to financial intermediation is low.

It should be understood that, besides our role, the establishment and consolidation of the financial stability cannot be ensured only through banking supervision. Therefore, further to FSAP recommendations for a more updated supervision and regulation, the new public agency of financial sector supervision is established. We as the Bank of Albania are deeply open to provide our assistance, so that the financial vigilance precedes the development. This will precede the expected developments in the insurance companies, pension funds, and financial mediators in general.

Elaborating this matter further, I would briefly bring up some weaknesses of the financial systems in the region.

Financial systems in all countries of the region are still dominated by commercial banks. Other segments play a second hand role. Capital markets, despite the recent developments, are still lagging behind. The number of banks in our region is relatively high. Taking into consideration the size of economies in our region, there is room for further consolidation, mainly through mergers and acquisitions. On a regional level, notwithstanding the credit growth rates, outstanding credit as a share of GDP is small compared to that of the new members of EU. This shows that banking sectors have a limited role in financing the needs of the economies for investments. One of the main factors slowing financial intermediation growth is the high intermediation margin of interest rates between loan and deposit rates.

This phenomenon could be the result of several developments, among which we can mention the lack of efficiency and competition among banks, the crediting risk that still remains high, problems with the collateral, and problems in the functioning of the rule of law as well as other issues of similar nature. The low level of efficiency and competitiveness in banking activities is also reflected even by the high capital adequacy ratios. The injection of foreign capital in our countries has remained low, showing, among other things, the inability of our financial systems to facilitate the absorption of
foreign investments in our national economies. The absorbing capacities can be improved significantly, if investors and banks conceive their strategies in regional level and not fragmented in separate countries. In this way, the financial system may serve as an accelerator of the inevitable process of the region’s integration into the European Union.

Dear honorable participants,

I believe our mission is vital to our future. What I have just said should not be linked only to the issues already mentioned above but to a greater goal, to that which for the moment has become the main aspiration of each country in the region, to the European integration. Mr. Trichet has emphasized that “the speed at which South-East European countries progress towards accession to the EU depends on the policies followed. It is the culture of stability and the exercise of the responsibility in economic policy making that are the crucial ingredients to achieve the bright prospects that lie ahead for the region”.

Personally, I have often mentioned in my public speeches that the opportunities of the region for quick and stable prosperity are linked, among other things, to our capability to act as a team. In line with that, we do not exclude financial stability in all its complexity.

It is a pleasure for me to observe that in the field of central banking, through our activity in the last couple of years, we have achieved a fruitful and productive cooperation. The presence of the regional Governors in the Conference of the Bank of Albania makes the case evident.

I am confident that I share the same opinion with my colleagues present in this room, that financial stability is a delicate matter that must always be part of our agenda. Today, the Bank of Albania is honored to act as the host of this event, but I am sure that in the future this forum will be hosted by other countries in the region.

I believe that this conference today opens a door, which I consider a door of the region. On this occasion, I would like to ask you to consider this conference not only as a sign of the willingness for cooperation. I think that it is our obligation and responsibility to identify future priorities for consolidating the financial stability in the region, as an important precondition towards its European integration.

NOTES

1 Safeguarding Financial Stability, Theory and Practice (2005), International Monetary Fund, page 83, last paragraph.
SPÉECH BY MR. ARDIAN FULLANI, GOVERNOR OF THE BANK OF ALBANIA
Sheraton Hotel, 31 October 2006

Distinguished Governors,
Dear participants,
Ladies and gentlemen,

When we thought about the topic of this annual conference, there was no doubt about the need to dedicate it to financial stability issues and the cooperation at a regional level. The current time seem to be appropriate because of the developments in the national financial markets and economic developments, as well as in the speed with which the region is moving ahead in adopting best international standards in good governance, market openness and integration, technological improvements and multilateral cooperation.

In my speech today, I will touch upon similarities and differences, but also uncertainties and risks that our financial markets are experiencing in the path toward modernisation and integration in the global financial markets, and will try to address the importance of regional cooperation in better facing these challenges. I will conclude with some thoughts about practical regional cooperation, which I am sharing with you, hoping to generate further discussions.

At a regional level, our countries are experiencing nowadays a higher growth rate of the financial markets, compared to that of the economic growth. As a consequence, the weight of the financial sector in the national economies, strictly from a quantitative perspective, is growing. At the same time, expansion is accompanied with changes in the market ability to better accommodate market participants needs for funding, diversification and risk appetite. Undoubtedly, institutional participants in the financial markets find themselves with a larger number of possibilities for business developments and financial specialization.

In addition, general public interest in using financial market products and services has increased dramatically based on the benefit they perceive from improved efficiency in everyday life activities. These developments highlight the importance of financial markets for our economic well-being, from a qualitative perspective. Let’s also recall that economic improvements trigger and support changes in social and cultural aspects of our life, bringing our nations closer to international values and principles, and to each other.

As expected, because of the historical background, our countries have differed in the speed and in the depth, with which they have moved along the transition phase in the last decade. While we had many similarities in
adopting the first basic and urgent reforms including price liberalization, enterprise restructuring and privatization in some economic areas, we were more distinctive in completing other reforms that would allow for institutional building capacities, which on the other hand, would make these changes root deeper in our societies.

Today, our countries enjoy stable macroeconomic environments. We are experiencing low inflation levels, stable exchange rates, a more prudent and responsible fiscal policy associated with limited and manageable budget deficits. National Central Banks have established their independence and are perceived in public as respectable and reliable authorities. There are also common efforts to fully open our economies and to attract foreign capital. As we are in the process of fully opening our markets, we are benefiting from increased competition, improved productivity and efficiency, and increasing quality of services for our citizens.

But, we are also facing several uncertainties and risks. Markets remain segmented and their infrastructure faces difficulties in supporting new and imposed developments. Market infrastructure deficiencies exacerbate their shallowness and make it difficult for various market participants to act in order to meet their business objectives and manage their risks. The technological improvements have to fully show their effect in meaningfully reducing costs of financial services. Regulatory gaps in different areas of local financial markets create the conditions for regulatory arbitrage and may adversely affect the supervisory work.

Therefore, erroneous and costly decisions are unavoidable. The financial situation of single market participants, due to market segmentation, is highly affected by their capacity to find financial support in the international financial markets. In reality, this leads to an increasing gap among so called “big” and “small” or among foreign and locally owned financial institutions. Real economy development is an additional source of risk for financial markets.

Such interaction should be carefully watched to better understand financial market trend in the future and identify financial imbalances in a country and regional level. Indeed, we are all experiencing a construction “boom”, where residential house prices have increased considerably. In some countries this is fuelled by credit expansion but in the whole region there are different views whether this is affordable. At the same time, the pace of general credit expansion, particularly for consumption and in foreign currency is alarming and is forcing us to think of several “what if” scenarios and take preventive actions.

It is our task as monetary and supervisory authorities, to provide a proper environment for a balanced and stable development of our financial markets. This is not an easy task for us, especially when there is no simple indicator to measure our success in achieving financial stability, and when we realize that this is a multifaceted issue that we do not fully control, and even can not fully predict. Above all, pursuing the target for financial stability is a never ending race, where the “finish line” is continuously moving ahead of us.
We have to find and implement appropriate policies, knowing that these policies represent a trade-off between making the system more resilient on one side and affecting its short-term efficiency on the other. In this challenge we must bring in the financial market industry through consistent communication and promote the adoption of the international standards in good governance a proportionate or risk-based supervision.

Based on our legal responsibilities, we have to approach these challenges in a national level. But, due to increasing liberalization of both labour and capital movement, and herd behaviour of financial market participants, we understand that that is not sufficient. We have nowadays in our countries the same financial institutions and the same behaviour of such financial institutions in response to a centralized business development policy, growing cross-border interaction among businesses and households, similar trends in social life.

Monetary and supervisory authorities in different countries in the region, to a large extent have responded to such developments with establishing formal cooperation with home country supervisory authorities, particularly in the area of banking system supervision, by signing bilateral Memoranda of Understanding (MoU). The fact that our countries are at the borders of the European Union (EU) has caused an increased presence of EU financial institutions, including banks.

Hence, the MoUs have been signed with these EU countries supervisory authorities. The quality of cooperation varies in different countries but one can say with reasonable confidence that the willingness of the host countries to cooperate has not always met the same interest from our counterparts. To an extent this is expected, because the assets of their banks in our single countries sometimes represent only a fraction of their total assets. Nonetheless, they should take notice of our concern that this cooperation is very important for us, particularly in cases where these foreign banks dominate our local markets.

The liberalisation of the financial markets in Albania has been a desirable move. We consider the inflow of foreign capital an important factor to upgrade the level of our banking system, improve its efficiency and the quality of its products, by improving competition conditions in the marketplace. In most cases, foreign banks have brought with them the expertise and the mentality of modern business development from the more developed countries they come from. As Mr. Bini Smaghi mentioned in his key note speech, the increase of foreign presence in our financial market has also triggered new ideas on how financial institutions and particularly banks intend to adjust their business volume and size to position themselves better in the marketplace. But this is something where we would like to see a more active and consistent approach, in both establishing active business development policies and bringing in good quality and experienced management in applying those policies.

It is indispensable for our supervisory authorities to be informed of the policy of different important financial or banking groups that operate throughout our
region. Host to host cooperation can help in this regard because some of us enjoy better communication links with the home country supervisory authority and they can share this information with the rest of the supervisory authorities in the region, within ethics and transparency principles. In practise, this can turn out to be a very valuable approach, because these regional foreign banks tend to adopt similar policies in countries with similar characteristics.

Another area where we could establish a strong cooperation is the discussion that should occur when any of us is adopting certain measures that are intended to control risks that appear from trends in the financial business developments. In return, we would be able to adopt similar supervisory policies, thus reducing damaging regulatory arbitrage possibilities and other risks associated with it.

One implication of the supervision/regulation heterogeneity across countries in the region is the ineffectiveness of indirect measures to control for credit growth. Therefore finding ways and pushing homogeneity in this regard would at the same time be also important to compensate the lost effectiveness of monetary policy and the eventual demand pressures.

There are also a few other ideas that stress the importance of pre-emptive regional cooperation, in bringing us as a region closer to fulfilling our target of European integration. By setting up and pursuing coordinated financial market development policies, we help to integrate our national financial markets into the international financial markets, and pave the way for other economic and social reforms to follow.

The modalities of such cooperation vary. Ad-hoc periodical meetings of Governors in the region, supported by more frequent meetings in a technical level to support the discussion agenda, could be one way of approaching the objective for stronger cooperation. In addition, through a more consistent communication, we can try to identify particular issues which are relevant for our regional financial markets, and pose those issues to our counterparties, being common home country authorities, other supervisory authorities where we turn for assistance, or even professional organizations where our supervisory authorities participate. I am sure our concerns can be taken more seriously if raised as a region. Furthermore, we must avail of the efficiency provided by the technology, in sharing our information.

A joint web-site can be established, where we can find important information, interpretations, or share its experience regarding supervisory issues or financial stability issues. When mentioning these ways of cooperation, I am not trying to neglect what is already happening and I am mindful of the fact that there is a trade-off between the advantages of such cooperation and its costs.

We should also point out that Memoranda of Understandings can not act as a substitution for cooperation in practice. It is important we maintain close contacts with our counterparts, on exchanging regular information on general trends and issues of respective banking systems in normal times, as it serves to
establish confidence for future cooperation, particularly during distress times. Otherwise, such official cooperation agreements will do little in making a real difference.

Let me conclude by saying that the objective of reaching and maintaining the financial stability is not an easy task but we could contribute a lot in its achievements by enhancing our efforts to make sure that financial market institutions are performing soundly in a stable macroeconomic environment. Our contribution can be much more effective if it is properly coordinated regionally.

Such cooperation will ease our efforts in improving supervision capacities, avoid cross-border regulatory arbitrage and will serve our efforts to meet our objective of integration into European financial markets. We can enrich the modalities of such cooperation, keeping in mind that the basis of good cooperation is established in normal times, through regular contacts.

Thank you.
SPEECH BY MR. ARDIAN FULLANI, GOVERNOR OF THE BANK OF ALBANIA
At the Press Conference with the IMF Mission
6 November 2006

In the meetings held with the IMF mission over the last two weeks, we have been sharing similar thoughts on the latest monetary and economic developments, as well as on the medium-term expectations.

The Albanian economy continues to remain within our expectations of the beginning of the year. Inflation has been kept under control within the BoA objective, though it has displayed an upward tendency compared to the previous year. The monetary policy pursued by the Bank of Albania was adequate to control the inflationary pressures. The increase of the core interest rate at end-July served to control the increase of demand and to signal our willingness for maintaining price stability. I would like to underline that the Bank of Albania is determined to continue pursuing a prudent monetary policy and to monitor those developments which may have a negative impact on the macroeconomic and financial stability.

The extension of Government securities’ maturity term (bonds of five year maturity were introduced today) increased the need and urge to develop their secondary market. In this context, the BoA is working rigorously to set up the necessary infrastructure in order to facilitate the Government securities operations in the secondary market. In more concrete terms, the implementation of Delivery-Versus-Payment system constitutes a pivotal step to be taken next year. Moreover, the Bank of Albania is making efforts to computerize the register of securities held within the Bank, which would at the same time further enhance and deepen the money market.

The stability of the banking system, in particular, and of the financial system, on the whole, makes up a priority of the Bank of Albania. Therefore, our commitment bears a special important in the context of credit market developments, which has continued to record further growth. The positive developments occurred over the last year in our banking system continued to be present over the present year. The BoA enhanced its cautiousness to provide stable positive developments. To this aim, the Bank is having an intensive communication with the banking system for the implementation of measures which aim at preserving the quality of the banking activity, in particular of the crediting one.

In conclusion, I would like to thank the IMF for the assistance and constructive ideas provided over this challenging period our economy is going through.
STATEMENT BY MR. ARDIAN FULLANI, GOVERNOR OF THE BANK OF ALBANIA
At the press conference following the Bank of Albania Supervisory Council’s decision on the increase of the core interest rate
Bank of Albania, 30 November 2006

In its meeting on 30 November 2006, after being introduced to the latest economic and financial developments, the Supervisory Council of the Bank of Albania decided to increase the core interest rate in economy by 0.25 percentage points (repurchase agreements rate of one-week maturity). Following this raise, the core interest rate reaches 5.5 per cent, from 5.25 per cent.

Annual inflation in October marked 2.2 per cent, being close to the inflation rate targeted by the Bank of Albania. Annual inflation for October was influenced by a number of positive transitory factors, such as the continuous high supply of agricultural products in the market and the oil price fall in the international markets. The controlled levels of budget expenditure and budget deficit, the preservation of money market stability, the stable lek relative to the other currencies and the proper administration of public expectations related to inflation have all had a positive impact on maintaining price stability.

The developments over the latest months have been characterized by higher monetary expansion rates, resulting from the growth of public sector demand over the recent months. However, credit to economy remains the main constituent of demand for monetary assets. Outstanding credit to the private sector amounted to ALL 165.6 billion in September, accounting for 18.7 per cent of the GDP. Credit to households grew under the most rapid rates, while the share of the lek to total credit continues to grow. The lek exchange rate was influenced by the increase of interest rates in the international markets. The latest months indicate a more diverse performance of the lek, characteristic of which was the absence of appreciating pressures. The Bank of Albania monetary operations have aimed at stabilizing the money market and at enhancing the monetary policy efficiency. In response to the growing demand of both the public and private sector for money, the Bank of Albania has reassessed the direction of operational instruments in the money markets, orienting them towards the injection of liquidity in the system over October.

The Bank of Albania assesses that the overall macroeconomic environment is favourable for maintaining price stability over 2007 and on. Despite the relative consumer prices stability, the analysis of the latest economic and monetary factors evidences that the balance of risks has shifted upward, bearing the possibility of inflation deviation from the desired trajectory. Therefore, it is necessary to take prudent measures for preserving this environment.

As we have already communicated to the public in our previous analyses, these factors would be summarized in:
• Performance of domestic demand. The rapid growth of credit to economy over the last two years has created the grounds for the quick revival of domestic demand in economy. Despite the slow growth rate in the last two or three months, it remains high. This effect becomes more evident under the rapid development of consumer loan. The moderation of the growth rate of credit to economy is not final yet, despite the regulative measures recently issued by the Bank of Albania. According to various studies, there is still a high potential of our economy to absorb credit in relation to what has been extended.

This fact is a clear signal indicating that the growth of credit will more or less be in the same levels with the current ones, implying that the pressures on domestic demand will be present. Moreover, worth mentioning is that, in line with the Government’s plans to increase domestic financing in the projected quota, domestic demand will be also supplied by the concentration of consumption and public investment.

In this context, it is assessed that today’s decision of the Bank of Albania Supervisory Council aims at absorbing the added pressures in the future, which may be generated by domestic demand in economy.

• Performance of agricultural prices. This factor has influenced on the moderation of total inflation over the last two years. Such a performance has, among others, been supported by the growth of domestic production and the enhancement of competition in the agricultural production market. The most recent data on the performance of agricultural prices provide signals for a downward shifting of agricultural prices, reflecting the prices performance of foodstuffs in partner countries, as well.

• Monetary developments and the exchange rate. In the presence of a high Government demand for financing, recently there has been a continuous fluctuation of liquidity and interest rates, in particular in the interbank market.

• Moreover, considering the constant narrowing of the spread between the ALL and foreign currency interest rates, the exchange rate performance may be put under the influence of depreciating tendencies. The expectations for another ECB decision by the end 2006 have a negative influence on saving in our domestic currency. Considering that the inflation influence channel (tradeable goods, in particular), as in most import-oriented countries, is too sensitive to shifts in the domestic currency, we assess that this increase will help in establishing a better balance of factors affecting our country’s external position.

• The inflationary expectations and the possible secondary effects of energy price rise. The level of economic agents’ development in transition economies affects the creation of adaptive inflation expectations, implying that they are overwhelmingly affected by the past and current performance of inflation. Such a characteristic may bring about the shifting of these expectations, even in the presence
of short-term inflationary impulses, leading to the extension of the inflationary cycle in economy.

The increase of the core interest rate aims to better control the pressures generated by domestic demand, better accommodate the supply-side fluctuations, stabilize the exchange rate, as well as to make a better orientation of inflationary pressures.

Its reflection in the financial markets and in the money market instruments will establish a more stable balance between the monetary stimulus of the economic activity and the deriving inflationary pressures. Moreover, the increase of the core interest rate aims to preserve the time and foreign currency structure of monetary assets, in line with their historical trends, and to reassess the incentives for maintaining the savings in our domestic currency.

The Bank of Albania will continue to be cautious at all contexts, making its best efforts to ensure that the decisions it makes are in line with the main objective, under a stable economic development.
SPEECH BY MR. ARDIAN FULLANI, GOVERNOR OF THE BANK OF ALBANIA
At the Regional Seminar “Development and Implementation of Business and Consumer Confidence Indices in Albania 2”
President Hotel, 1 December 2006

Dear participants,

Today’s seminar on confidence indices has a special importance as it touches upon the basic elements of assessment and decision-making in economic policies, information and its real dimension. As in any decision-making process, information is the first step to reach a sound judgment on the right monetary policy to be pursued by a central bank.

It is indispensable for the monetary authorities to prepare the analyses of macroeconomic indicators, in order to formulate a monetary policy that ensures the stability of the internal indicators, as well as the relations with the partner economies in trade relationships. On a more general view, the economy of a country cannot achieve competitiveness and international standards, if development policies are built on an incomplete information basis. The preparation of a complete information framework in the economic field is a challenge for the regional countries to reach occidental standards. At the current stage, this challenge is even more urgent for Albania.

The current situation of the national statistics has room for spreading the statistical basis and for providing stable statistics over time. However, the progress in the statistics field, as well as in other related ones, needs time, funds and the right legal ground for undertaking substantial projects. Meanwhile, our decisions have to rely on as much as possible sound basis. The formulation of confidence indices, as indicators of economic expectations, does not substitute the lack of statistical information on the current situation of an economy. These indices enable monetary markets and authorities to rearrange in time the strategies that preserve balances of related goals. Confidence indices enable a central bank to adjust the monetary policy stance timely, in order to preserve price stability, while the economy grows at potential rates.

The developed countries are in frontward regarding the preparation of confidence indices as indicators of expected performance of the economy. Integration of the markets and the globalizing process increase the necessity of preparing these indices in our region, because the objective of monetary policy, the price stability, reflects stability and economic openness towards regional countries and further. It has already been 4 years that the Bank of Albania has started to evaluate business and consumer confidence indices. These surveys are being run on a quarterly basis, with the help of INSTAT, and involve over 600 businesses of production, construction and services sectors and about 1500 consumers. The information collected covers the performance of prices, consumption, income, production, employment,
investments and some other indicators, which support the decision-making on the monetary policy stance.

In this important process, the Bank has, from the beginning, been assisted by experts of Ifo Institute for Economic Research, which is internationally known in the field of business confidence indices. So far, the results of these surveys have been indirectly reflected in the periodical analysis and reports and in other different papers of the central bank. The further consolidation of these indicators, paves the way of their publication for the purpose of being used by the economic agents, as an extra way of communicating with the central bank. A preliminary step in this direction is also the consolidation of the applied methodology for calculating these indices, through a professional expertise as that of IFO.

The undertaken steps, in expanding and consolidating the statistical basis of the monetary authority in real time, will enable the timely management of the situations and challenges, brought about by the economic development and the further integration of the regional markets. Coordination of the work between regional central banks for adopting the methodology and the indices enables the maximal use of existing knowledge basis on the specific features of our region, against that of the most developed economies. The use of the same methodology for establishing the indices will make it easier to compare them to each other. In parallel, these indices will serve as a communication tool with the international institutions, specialized in best presenting and identifying the priorities by countries and with the foreign investors interested in our country.

Our purpose is to maximally adapt the indices we are building to the best international practices in this field, far from voluntarily solutions. Without any doubt, the main challenge remains their efficient use in our decision-making process.

We believe that the products we have been discussing during these two days, the confidence indices in general, will be a successful mean of communication for the Bank of Albania with the market’s actors and the public at large. I do not hesitate to state that the launch of these two products, especially in the context of our aspiration to adopt the inflation targeting regime, will further improve the decision-making process at the Bank of Albania.

Recently, the Bank of Albania has accelerated the development rates, both in the context of improving the decision-making process and of refining the mechanisms transmitted by its decisions. The issue is how quickly the market’s actors will pursue the current rates of the Bank of Albania. It is important that the difference between the two velocities reduces, in order for our dialogue with the market will be standardized and transparent. To enable an as much as possible contemporary communication, among others, our co-operation with the financial market, the Ministry of Finance, INSTAT and other institutions plays an important part. In addition, there should be a close co-operation with other groups of interest, such as the Chamber of Commerce, Konfindustria, the media and the public at large.
At this point, I would like to emphasize that the role the media plays is really exceptional. A professional media would be able to construct reliable and comprehensible communication models, easily understandable by the public.

The products we are getting ready to launch soon, that is, the confidence indices, have to justify their designation. Stated differently, the public should believe the product issued by the Bank of Albania is reliable, that the product is the real object and indicator of public expectations. In the meantime, we expect to have the echo of public’s trust back.

Wishing you all a fruitful working-day,
Thank you.
SPEECH BY MR. ARDIAN FULLANI, GOVERNOR OF THE BANK OF ALBANIA
At the Fifth International Banking Forum
Athens, Greece, 6 December 2006

Honorable Dr. Margret Doyle,
Dear Mr. Chairman,
Distinguished participants,

Before starting my speech, I would like to briefly address the perennial question that stands at the heart of our quest: “Are the prosperous times ahead of us?” It comes to my assistance an old saying of one of your ancient philosophers, Eupides: “Prosperity is full of friends”. As we are gathered here as friends, I believe we have a positive answer to this question.

I would like to thank “The Economist Conferences” for inviting the Bank of Albania in this very important forum. It is a great pleasure to be here today. The topic of my speech will be economic reforms. I will take this opportunity to express my views on past and future banking and financial reforms in Albania and the region. The topic is not new of course. However, reforms and their implementation are a dynamic process that must reflect changes and expectations for future developments in both domestic and global markets. Therefore, it will always be an open discussion in need for new ideas and solutions.

Central banks are important contributors to the economic reforms and their implementation. They do not only welcome and support, but also generate reforms in the capital, labor, and product markets. Such reforms have ripple effects that go beyond economic benefit of a long run stable growth and financial stability. I believe that positive spillovers will be materialized in the South East European region’s prosperity and its economic and political integration into the European Union.

The Bank of Albania has been a constant generator and supporter of reforms both institutionally and as the provider of stable prices, sound macroeconomic conditions and financial stability. It makes an undeniable fact that the financial integration which we are experiencing will be to the forefront of European Union integration process. It will ease the challenges and speed up the process of European integration which Albanians have embraced by wide popular consent.

Like in many other transition economies, banking reforms in Albania were implemented as an integral part of the structural reforms undertaken to transform the Albanian economy into a market oriented economy. Continuous improvement, along with approval and implementation of new banking legislation and supervisory regulation; liquidation and privatization process of
the state owned banks; and foreign ownership; have change of banking and financial markets.

Foreign banks have been an important push factor toward increasing efficiency, number, quality, and coverage of financial intermediation. New entries, mergers and acquisitions are recently altering the market structure in both asset and liabilities. Reforms that brought big European players and their capital in the market, have further increased confidence in our economy and in the region as a whole.

However, the presence of foreign banks does not replace the need for legal and institutional framework. Moreover, the latest developments in banking and financial markets might foster additional risk factors related to asymmetric exposure, issues of home host supervision and financial safety net with foreign banks dominance. These challenges and the expected financial developments in the region will outline the scope and the structure of reforms in the future. So, please allow me to briefly present my view on the future trends of regional financial markets.

Financial markets in the region are becoming part of broader global developments which fuels financial integration, liberalization, and financial innovation. The lucrative regional market and the consolidation process have imposed a vertical financial integration in the region. Less than ten European banks with headquarters in Vienna, Athens or Milan dominate the regional banking markets. The process of financial integration will continue, making the region more and more integrated into the European countries. Financial systems are leading the road to financial integration and the positive spillovers of such process will spread over.

Financial markets are and will continue to be bank dominated. Non banking financial sector will grow very rapidly, but banks will continue to be the major players. They will help to further build the needed financial infrastructure for non banking financial activities, and support growth in our economies. Not long ago, I asked a friend of mine who had recently returned from migration after 15 years: “Why did you come back”? His answer was simple but true: “It is not important for me where I like to live – he said – it is important where the opportunities are”. As the gap in living standards closes and Albanians see opportunities flourishing in Albania, they will come back. They will bring important human capital and managerial skills, which they have gained in the countries where they work. Many Albanian emigrants are at this stage of the migration cycle and we see potential benefits from such a process. It is the role of banks to match this human capital with necessary financial capital and provide financial services to develop their entrepreneur skills.

This role comes very naturally to Greek commercial banks that operate in Albania, which I take the opportunity to thank for their early confidence in Albania. They are natural partners for these new entrepreneurs who are familiar with the culture, and probably have a long history operating with respective Greek offices. The fact that such ventures could also involve Greek
capital in the case of pure joint investments makes one more argument in support of my observation. According to the Bank of Albania surveys, Greek companies are ranked first by the size of capital invested in the Albanian economy, while holding the second place for the number of Foreign Direct Investments.

The involvement of these banks in financing such activities will play a positive role in shifting the balance of the loans portfolio from retail and consumer crediting toward production activities in industry and agriculture. At the same time, it might also fuel the growth rate of credit to economy, which has already experienced very rapid growth during the last two years, raising concerns for macroeconomic and financial stability.

The results of reforms were not limited only to the openness and development of domestic financial market. They generated price and financial stability, sustained economic growth, assisted institutional building and increased confidence. These developments attracted interest of, and brought big financial groups in the region in general and Albania in particular. As I mentioned above, the entry of big financial groups, and the consolidation process that has followed since will continue to grow. What we are observing right now in the market is that the big fish is eating the small fish; the very big fish is eating the big fish in the European market with implications for the host countries. However, the process is far from over, gigantic fish (global player) might enter the region by eating the very big fish. Last but not the least, there will be mergers among domestic banks as well.

Despite the increase in the concentration ratio that comes with these mergers and acquisitions, we have started to observe increased competition in our market. This competition increases efficiency, introduces new services and products, lowers spreads and generates positive spillovers for economic activity. While this makes a good precondition to foster financial stability, it is not a sufficient condition to increase financial discipline.

Currently, the activities of financial institutions and commercial banks have a limited scope; however, we are starting to see the signs of financial conglomeration. We have no doubt that this trend will grow and continue in the future. It will bring innovation, new financial instruments and products in the market. Along with this, rapid growth of credit and debit cards as well as other systems of payments will continue to grow. While these instruments might not subside or even reduce the use of cash, this trend must be taken into account.

Transition economies of the region are lucrative markets. They are growing substantially faster than traditional European markets and offer impressive prospects for high profits and significant growth. To give you an example, return on banking activity in Albania during the last two years has been around 20 percent. These positive prospects and the eagerness to compete quickly and beyond rational limits for profits and market share may create potential risks. If managers were to lose sight of the entire picture, and financial
constraints, such competition might result in mismanagement, nonperforming loans, and other banking problems. Therefore, there is no room for sloppy managerial attitude. It is very important that managerial staff must be up to the challenges which, if materialized, could be more complex than in the self-regulated developed markets. It is important to act en bloc and engage in regional projects of infrastructure including here the financial ones.

We have great confidence in the ability of the banking system to promote the best banking and cautionary practices; however, I believe that preemptive action is needed to ensure that latest observed trends do not hamper financial stability. Therefore, we cannot neglect improving our legislative, regulatory and prudential measures as a major element of financial sector reforms in Albania.

In this regard, a new Draft Banking Law is prepared by the Bank of Albania; likewise, a new Law on Securities will be introduced shortly. In addition, efforts are underway to revise legislation on Pension and Investment Funds, and draft a Law on the Payments Systems, which will substitute several sub-legal acts issued by the Bank of Albania until now. This process aims at gradual harmonization of the banking legislation with that of the Acquis Communnautaire.

To address issues of increased competition, poor managerial practices and safeguard stability, the Bank of Albania is working toward establishing a Credit Registry, revising regulatory framework on capital adequacy ratio and credit risk management, increasing on-site supervision, and improving its stress-testing models. Following Financial Stability and Assessment Program (FSAP) recommendations, a separate entity “The Authority of Financial Supervision”, has been established recently to supervise the securities, insurance and pension funds markets.

Last but not the least, I would like to address the implementation of the Basel II accord. While it will shape the financial market, I believe it will pose challenges to our banking system and to us at the moment. We have initiated the implementation of the new accord, but we are currently being pragmatic to approve only the adoption of well understood elements of Basel II that can be implemented in a safe way.

Now, I would like to shift your attention to the other important pillar of banking reforms: the role of the central bank itself and its monetary policy. The contribution of the Bank of Albania to the economic reforms comes also through maintaining stable prices and helping to ensure financial stability. Over the last five years, the Bank of Albania stability oriented monetary policy has generated low and stable inflation; it has also ensured that medium and long run inflation expectations have been well contained. The economic growth has been robust at around 5-6 percent of GDP, while enjoying a high degree of financial stability. Reflecting broadly on the nature of the monetary policy I would say that it has always been focused on maintaining price stability and using the control of monetary aggregates as an intermediate target. Current account and foreign exchange transactions were liberalized
at the early stages of transition along with the adoption of the free floating exchange rate regime.

Indirect instruments are being used to transmit interest rate and liquidity signals to the market. Repo rate has become the signaling tool for short term interest rates while repo and reverse-repo operations are used to manage liquidity. Reforms in the conduct of the monetary policy have granted greater flexibility to banks to determine both the volume and terms of lending and deposits.

The Bank of Albania has provided all necessary conditions to ensure sustainable economic growth and stable prices; however it alone can not guarantee that the objectives will be fulfilled. All these positive developments have taken place in the presence of a well contained fiscal expansion, as an element of sound fiscal policy and bold structural reforms.

Banking system has become an important provider of domestic financing for the government. Commercial banks have played a major role in it, while direct financing from the Bank of Albania was limited to address issues of independence and deficit monetization. Recently, the Government introduced to market papers of five years maturity. In addition, with the consent of the IMF, the Government will shortly issue euro denominated government securities. The Bank of Albania welcomes such development as a certification of cautious and responsible fiscal policy. At the same time, we call for more prudence and proper addressing additional risks.

It is undeniable however, that these latest developments have been achieved under the watchful eye of the International Monetary Fund. IMF has been an important element of the reforms in Albania. Its presence and the memorandum of understanding signed under the framework of ESAF and current blend of PRGF and EEF Programs, enhanced credibility of our economic reforms and served as external anchors. However, as our economy grows and current agreement ends in 2009, we will soon get full ownership of our economic policies with a reduced role of IMF under article 4 of the Agreement.

The Bank of Albania has a proven track record of competence, credibility and professionalism in the service of our economy. These three elements provide necessary conditions to support and guarantee achievement of economic goal of stable prices and boost credibility in Albanian economy; but, we can not be hold responsible for the behavior of the other players. I am convinced that we need to find and implement clear domestic and foreign anchors to preserve the credibility of our reforms in the future.

For the way ahead we are focusing our efforts in the identification and utilization of key elements of the state, politics, markets, institutions and general public that could efficiently play the role of domestic anchors. As part of this preemptive action, the Bank of Albania is carefully considering the possibility to launch a fully fledged inflation targeting regime of monetary
policy in the midterm. This will be a conditional decision based upon results of current ongoing research, evaluation of the preconditions and building up of capacities. Other possible anchors, such as a memorandum of understanding with the Ministry of Finance and public education, are considered as well.

On the foreign side we see numerous prestigious partners who understand our concerns and appreciate the value of fiscal discipline. They enjoy the power and the virtues of an influential voice. Some of them have already been partners in reforms and will be shaping the future ones. European integration process and the Association and Stabilization Agreement that we just signed in provides nominal anchors. In addition, sovereign ratings and other independent country reports could also play this role. The Bank of Albania intends to establish open lines of communication and adopt instruments that will automatically start building up pressures before it is too late.

My personal conviction is that European Accession lies out as a natural process, where central banks have a vital role to play. This approach would be of mutual benefit and it will speed up the convergence toward European standards, making the political decision a natural outcome of our efforts. To make this process more effective the central banks and the European institutions should continue the dialogue, why not even by surveillance, supporting, assisting and guiding us in fundamentals and economic financial and legal infrastructure. This process would increase our responsibility and accountability to make Albania an eligible partner.

Let me conclude my discussion quoting Euripides who says: “Much effort, much prosperity”.

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

At the Round Table on Inflation Targeting 2
Tirana International Hotel, 8 December 2006

Ladies and gentlemen,

I want to conclude this Round Table by thanking you all for your contributions. We are really happy that you came to Tirana for discussing the monetary policy strategy of the Bank of Albania. This Round Table on Inflation Targeting was an excellent follow-up of the Open Forum. At the Open Forum last year in December we globally discussed the many preconditions for Inflation Targeting. During these two days of the Round Table, yesterday and today, we went far deeper on these complex issues. These issues need to be solved before the Bank of Albania can put a fully fledged Inflation Targeting regime into place.

At this Round Table we have discussed the progress that the Bank of Albania has been making during 2006. One of the discussed topics was the econometric modeling and forecasting. The Bank of Albania uses now a reliable analytical framework that provides information useful to the monetary policy decision making. Under Inflation Targeting more information would be needed about the expected inflation developments in the future.

As laid down in the central bank law, the primary objective of the Bank of Albania is to achieve and maintain price stability in Albania. For keeping prices stable we need to be able to forecast the development of prices in the future. Our current econometric models provide us information about these future developments. Our internal studies show now that the Bank of Albania is able to make reliable forecasts.

We also discussed the consequences of situations where the consumer price index increases, let us say, more than 3% at an annual basis. This may for instance happen due to higher electricity prices, or higher oil prices. These energy prices are a main share of our daily expenditures. Therefore, they are a main share of the total basket of consumer prices for the “average” Albanian household. However, the focus of our discussions was the analyses of the further impact on the Albanian macro-economy.

Higher prices will lead to a lower purchasing power. Households will buy less in case of a price increase, under the condition of unchanged household income. Then, if many households in Albania start consuming less, the Albanian economic growth will suffer. The Albanian production will slow down due to the overall lower demand for goods and services.

This process can take some time. But, anyhow, each economist will agree that strong increases in prices are bad for the economy. A high inflation,
that is another way of saying a strong increase in prices, will harm economic growth.

The Bank of Albania aims at an average increase of the consumer price index of 3%. The Bank of Albania will set the interest rate for keeping expected price increases to 3% plus or minus 1 percentage point. It has built a macro-econometric model with all these channels that transmit monetary policy in the Albanian economy. The main purpose of the model is to analyze the reaction of prices, private consumption and business investment and so on, in reaction to changes that may take place. We call these changes in analytical terms “shocks” to the economy.

Our macro-econometric model is promising. Very promising. But for building econometric models we need statistics. Albania has statistics, but we need better statistics. For the year to come, the Bank of Albania wants to improve the statistical framework. The Bank of Albania needs better statistics, I said. With “better” statistics I mean here “more” statistics, “reliable” statistics and “user-friendly” statistics.

We need to measure all macro-economic developments in the economy better. And we need to keep track of these developments. Our Albanian history is still short. We only have time series for about 15 years. In time we will logically have longer time series. Our time series need to become timely available and they should be fully understandable.

Inside the Bank of Albania we can work more on statistics. In the year 2007 the Bank of Albania will improve its own database on monetary and financial statistics, and on the balance of payments statistics. But, for other statistics we depend upon our national statistical office, INSTAT. We also depend on other institutions for providing us with relevant information.

Next to the broadening and deepening of the statistical framework the Bank of Albania will improve upon its communication with the public. We discussed during this Round Table the transparency of the Bank of Albania. We concluded that significant progress has been achieved.

But next to transparency, the Bank of Albania wants to improve upon the information that it provides to the public. The Bank of Albania aims at making monetary policy understandable to everyone. We know already that money matters. The more money we possess, the more we can buy, and the more our economy will grow. The more our economy grows, the more people can share. Poverty will be reduced. But what about monetary policy?

We all know that higher wages or lower prices are beneficial for our personal pockets. The higher the wages, or the lower the prices, the more we can buy. But for the Albanian economy as a whole, there is a flipside. This flipside is inflation.

More spending will lead to higher prices in the medium to long term. And these higher prices, I can also say “higher inflation”, is damaging for the
Albanian economic growth. For this reason the Bank of Albania safeguards price stability. Our main task is to keep prices stable. In order to do so, we set the main interest rate.

The Bank of Albania wants to communicate better on all these monetary policy issues. It wants to explain the monetary and financial benefits at the micro and at the macro level. It wants to explain better why it is aiming for an inflation rate of 3%. The communication strategy of the Bank of Albania is to explain the working of the monetary policy issues and its own tasks, to you all.

The understanding of the public is needed for a good conduct of Inflation Targeting. Credibility has to be gained. As said before, a solid statistical framework is also indispensable. Reliable statistics can tell us about the past and the present. On the basis of this, the Bank of Albania can use its econometric models to forecast the future. The Bank of Albania can conduct monetary policy, and can target inflation better, in case of better forecasts.

We can stress the preconditions. But the fulfillment of all preconditions for Inflation Targeting depends also on others in the Albanian economy. Under Inflation Targeting, the monetary policy aims at a precise inflation target in the medium term. The Bank of Albania can only reach this target in case the interest rate setting affects the deposits, credits, private consumption and business investment, GDP, like in a developed market economy. Only in this case can monetary policy be effective.

Therefore, some preconditions for putting fully fledged Inflation Targeting in place can not be met ONLY by the Bank of Albania. They depend upon the development of the Albanian economy, they depend upon the provision of statistics by INSTAT and others, they depend upon the understanding of the public. They also depend upon other key players like the Ministry of Finance and they depend upon the efficient working of the financial markets. Other preconditions for Inflation Targeting can partly be met by the Bank of Albania.

The full implementation of Inflation Targeting can therefore take place ONLY conditionally.

One can compare this situation with the tailoring of a suit for a special occasion. Let me make this comparison.

One can find a good tailor and ask him to make a suit for a special occasion. All measures can be taken, such as the length of the arms and the length of the legs. The suitable materials can be found. One needs the appropriate fabric, in the appropriate color. Upon all these preconditions of (1) the good tailor (2) the precise measures (3) suitable materials, the tailor can start the tailoring of the suit.

But, there is still no guarantee that the suit will fit you perfect. Or, it may happen that you look appealing in the tailor-shop, but not at the day of the
special occasion. For instance, the temperature may have fallen so that you need an additional coat, or even a different fabric. Or, the environment of the special occasion may make you look overdressed. You tried to make it perfect, but the environment is lagging behind. Factors that you could not influence yourself can make you look different from how you had wished to look with the new suit. Conclusion: The suit is not suitable, or better, the suit is not (yet) suitable.

For this reason we have to try the tailored suit regularly. All preconditions for Inflation Targeting need to be checked and re-assessed on a regular basis.

At this Round Table we discussed econometric modeling, statistics and communication, also the legal framework, the internal governance at the Bank of Albania and the arranged agreements with the Ministry of Finance and INSTAT. During this year we drafted the new Banking Law. This law increases customer protection, sets the legal grounds for credit information registry, introduces new rules for risk administration, bringing more confidence in the banking system as well. With the assistance of the IMF legal department we revised the agreement with the Ministry of Finance. These agreements were standardized to emphasize the role of the Bank of Albania as fiscal agent. Moreover, these agreements aim at creating a cooperative and partnership environment. We remain committed to further increase cooperation with major governmental agencies to ease their proper understanding of monetary policy process, its implications and the need for harmonized and coordinated policies.

Concluding, I would like to underline that we are carefully evaluating the degree to which these preconditions are met before shifting to fully fledged inflation targeting in the medium run. Such strategy will further increase the effectiveness of the monetary policy in Albania further consolidating the price stability and contributing to sustainable economic growth. We will re-assess all preconditions regularly through these types of meetings with foreign professionals. In the meantime, we are establishing a professional dialog among the central bank, INSTAT, Ministry of Finance and other government institutions.

Once more, ladies and gentlemen, I thank you very much for your contributions. I wish you a safe return back to your home countries.
SPEECH BY MR. ARDIAN FULLANI, GOVERNOR OF THE BANK OF ALBANIA
At the conference “The Mission of Contemporary Central Bank” organized by the National Bank of Poland.
Warsaw, 15 December 2006

CONCERNS OF THE PROSPECTIVE ERM II MEMBERS

Your Honor Mr. Balcerowicz,
Honorable Governors,
Dear Colleagues,
Ladies and Gentlemen,

I would like to take this opportunity to thank Mr. Balcerowicz and the National Bank of Poland for the invitation. It is an honor for me to take part in this discussion and to share my thoughts concerning the challenges facing prospective ERM II members.

The central theme of this conference – the mission of the contemporary central bank with the focus on euro adoption – is of crucial importance for countries aspiring to become members of the big EU family in the not-too-distant future. Drawing from the experience of current and prospective members, accession to this family is a complex and challenging process.

As a test of the nominal convergence of a country, the ERM II mechanism has attracted a lot of academic interest and criticism. Conceptually speaking, the ERM II directly precedes the full integration into the EMU.

ERM II AS A STEP TOWARDS EMU

To put the ERM II in a proper context, we need to be clear on the fact that it is an early necessary step before Euro adoption. Therefore, entry into ERMII is conditional on the economic and political readiness for entering the EMU. Several considerations need to be made. By adopting a single currency, the country foregoes independent monetary policy and the central bank can not act as a lender of last resort. The loss of monetary policy independence can be problematic if a country has achieved little in the way of real convergence (both structural and cyclical convergence) and is susceptible to asymmetric shocks. On the other hand, the loss of the lender of last resort function by the national central banks implies high and protracted fiscal costs in the case of financial crises. For this reason, a healthy and resilient financial system would be required for participating in the monetary union.

It is partly a reflection of these economic challenges that the new EU members appear to be following different trajectories towards EMU. On one hand, Slovenia, the Baltic countries, Malta, Cyprus and Slovakia have proceeded to join the ERM II with a view to enter EMU in the future. The other countries,
notably the larger Central European ones, have opted to stay out of the ERM II in order to have more time to do the necessary economic adjustments.

CHALLENGES OF THE ERM II

Once the economic argument and the political consensus are strong enough to support EMU membership, the acceding country can decide to enter the ERM II mechanism. What could go wrong for accession countries during the ERM II? Some often-cited issues are related to fiscal consolidation, financial stability and the choice of the central parity. Let me say a few words about these issues.

• The exchange rate stability is one of the five (nominal) Maastricht convergence criteria. Consumer price stability, long-term interest rate convergence and fiscal consolidation are the other conditions a country has to fulfill in order to gain EMU membership. Clearly, the burden of ensuring compliance with these conditions does not fall solely and exclusively on the monetary policy authorities. The fiscal and labor policies must be aligned with the monetary policy objectives and the achievement of political commitment to ERM II is of paramount importance. I find the practice of monetary and fiscal policies dialogue, as stipulated in Accession Strategies of some of these countries, a commendable achievement.

• Financial instability has been identified as a potential negative outcome of the bilateral fixing of the exchange rate for accession countries. Limited exchange rate flexibility under ERM-II and disinflation conditions expose the EU acceding countries to large ‘convergence play’ capital inflows. If the exchange rate in accession countries is forced to fluctuate within a relatively narrow band, the outcome might be additional and unnecessary inflation. The central bank’s reaction to increasing inflation would restrict economic growth. Such an outcome is even more likely in the presence of the Balassa-Samuelson effects, commonly experienced by the transition economies. In such a scenario, the dual task of preserving the domestic and international value of the currency can be jeopardized. It is on these grounds that the ERM II design has come under attack, as an unnecessarily lengthy period.

Thus, it is not surprising that some acceding countries prefer to stay there for the shortest time possible.

• The last issue I would like to discuss is the determination of the central parity rate. The potential implications of an exchange rate misalignment are large, as the corrective burden would fall on the real sector. An undervaluation or overvaluation of the exchange rate would result in higher inflation or lower economic growth until the real exchange rate returns to equilibrium. In the absence of a nominal exchange rate channel the adjustment process would tend to be slow.
Now let me briefly turn to the policy implications the aforementioned issues pose.

The ECB policy stance on ERM II (ECB, 2003) emphasizes the primacy of the inflation objective over the exchange rate stability. Approaching the EMU in the context of an IT regime seems quite a plausible option, and one which is even encouraged by the ECB. The period of residence in the ERM II needs however to be as short as possible, so as to avoid the inherent incompatibility of these two targets in the face of the Balassa-Samuelson effects and increased capital inflows. The countries approaching the EMU from a fixed exchange rate regime might have a different perspective on the subject. However, even these countries will experience the Balassa-Samuelson effects, facing a difficulty to reconcile the fulfillment of the exchange rate and price stability criteria. At the same time, given the wide fluctuation bands that are foreseen by the ERM II template, the credibility gain is likely to be marginal.

POLICY IMPLICATIONS

As a conclusion, let me re-emphasize the need for a careful approach to the EMU in that a certain degree of real economic and structural convergence is needed. The EMU membership can not be delayed by much however. First, a really high degree of economic convergence might require a lengthy period of time to be achieved and people could perceive an enlargement without EMU as incomplete. Second, in adopting the single currency the exchange rate risk will be eliminated, resulting in positive impulses to the financial market development. Thirdly, the endogeneity forces of trade and financial integration discussed in the literature might be an additional driver of real convergence that is worth exploring. Neither economic theory nor central banking practices offer an optimal approach to ERM II from the point of view of the monetary regime. The alternative theories agree however, on the need to stay there for the shortest time possible.

To conclude my speech, let me briefly say a few words on the Albanian case.

THE BANK OF ALBANIA APPROACH TO EU ACCESSION

The monetary policy of the Bank of Albania focuses on maintaining price stability through the control of monetary aggregates which are used as intermediate target. Indirect instruments are used to transmit interest rate and liquidity signals to the market. Repo rate is the leading indicator for short term interest rates while repo and reverse-repo operations are used to manage liquidity.

Over the last five years the Bank of Albania stability oriented monetary policy has generated low and stable inflation; it has also ensured that medium and long run inflation expectations have been well contained.

The economic growth has been robust at around 5-6 percent of GDP, while enjoying a high degree of financial stability. (In other words, it seems like we
are already close to the ERM II standards.) Such results reflect the opinion that economic convergence should not be held back by the political one.

Political processes dictate that ERM II and EMU should be preceded by entry into the EU. The Bank of Albania has a clear view of the EU accession process. The design of the current and future monetary policy strategies is in line with the ultimate objective of EU accession.

• On the policy side, it is striving to maintain monetary conditions in line with the Maastricht Criteria. In this respect, the Bank of Albania is carefully considering all available alternatives of monetary policy regimes, among which priority is given to fully fledged inflation targeting strategy.

This framework will provide a more sophisticated approach to decision-making and will create a better platform for communicating our commitment to price stability, ultimately leading to a better anchoring of inflation expectations. However, the choice of the new regime will be a conditional decision based upon results of current ongoing research, evaluation of the preconditions and building up of capacities. To this end, we are carefully refining our technical capacities and decision-making processes, following the necessary preconditions, working to achieve real independence for the monetary policy, upgrading our analytical capacities and designing appropriate internal processes.

• On the structural side, the Bank of Albania is also pushing the reform agenda in the financial sector. The reform agenda in the Albanian financial sector aims at gradual implementation of the Acquis Communautaire standards in banking legislation. We are revising the legal infrastructure.

In this regard, a new Draft Banking Law is prepared by the Bank of Albania; likewise a new Law on Securities will be introduced shortly. In addition, efforts are underway to revise legislation on Pension and Investment Funds, and draft a Law on the Payments Systems, which will substitute several sub-legal acts issued by the Bank of Albania until now. Prudential regulations have been tightened in response to rapid credit growth and intensified competition in the banking system. We are working to ensure proper supervision over the parts of the Albanian financial sector that are outside the Bank of Albania’s jurisdiction, while trying to preserve fair competition across the sector. The Bank of Albania is assisting the MoF to improve its debt-management capacities. I believe our hard work will be reflected in a satisfactory rating of our sovereign debt, due to be carried out early next year.

The competence, credibility and professionalism of our monetary policy provide necessary conditions to support and guarantee achievement of economic goals and successfully fulfill economic convergence toward ERM II preconditions. However, our achievements will not last in the absence of a careful fiscal policy and conservative fiscal expansion. The Bank of Albania is
not the only major economic player. Therefore, we must find and implement clear anchors to guarantee the compliance of other players’ economic policies. In this respect, we can transform ERM II preconditions into an important foreign anchor to preserve the credibility of our reforms in the future.

As a pre-accession country, Albania will be facing ERM II problems in the medium term. We are well aware of the difficult road ahead and the challenges we will face. Nevertheless, we remain committed toward economic and legal reforms considering it as a natural approach toward EU accession process.

ENDNOTES

1 See Begg et al., (2002).
2 It is worth remembering that the Maastricht criteria were designed to ensure the nominal convergence of industrial economies with roughly similar economic structures. Their validity in ensuring the convergence of transition economies is an issue that is hotly contested by several economists (see Buitel et al., 2002).
3 See Buitel and Grafe (2002) and Begg et al. (2002).
REFERENCES


SPÉECH BY MR. FÀTÔS İBRAHİMÎ, FIRST DEPÚTÝ GOVÈRNOR OF THE BANK OF ÁLBAÑÌA

At the Conference “Reducing the informal economy – a challenge of the Albanian Government”
Tirana International Hotel, 16 October 2006

THE REDUCTION OF CASH IN THE CONTEXT OF REDUCING THE INFORMAL ECONOMY

Since the inception of the programme undertaken by the Bank of Albania, in cooperation with the Ministry of Economy and the Ministry of Finance, on reducing cash, it came clear that the issue of cash in economy cannot be treated as separate from the issue of the informal economy. The companies, which try not to expose their activities to the third parties, will avoid banks and will find alternative sources of financing and payment, mainly in cash. Therefore, the Government initiative on reducing the informal economy is to be welcomed when bearing in mind the great impact it will have on reducing the cash economy. It needs to be said that the process of formalizing the economy has not been considered as an excuse for not undertaking a number of measures and initiatives, which may accelerate the progress of cash reduction. Among the actions undertaken in this context, I would mention:

1. The channelling of the state administration payrolls through the bank accounts.

At this moment, the entire public administration payrolls are channelled through the accounts with the commercial banks. Despite the initial reluctance of a part of the public administration employees, the withdrawal of payrolls through the bank accounts has now turned into as common as any other services provided by the private market. The channelling of pensions through the bank accounts has met with certain complications, since the small amounts and the high circulation do not make them very attractive for the commercial banks. The licensing of the post for carrying out certain banking services has resulted to be a good solution for this issue.

The larger involvement of the private business in this process remains a challenge. In this context, the encouragement of channelling the payments through the banking system is a crucial step to be taken. The requirement of a rigorous application of the obligation that (small, medium and large) businesses have to open and operate with the bank accounts would not only serve to reduce cash but also to reduce the informality.

2. Monthly utility payment (electricity, water, telephone) through the bank accounts.

The monthly utility payment is now made through banks. However, this is limited only to the clients of the bank the utilities have their account in.
The holding of these utilities’ accounts with all the banks in the system, or the finding of a kind of interbank cooperation would not only serve to increase the amount of payments channelled through banks, but also to enhance the competition. Another difficulty encountered in this context is the implementation of bank accounts direct crediting by the utilities. This has been due to the concentration of these companies in certain banks, and also because of the problems encountered in the standardization of the bills according to particular banks’ requirements. The Bank of Albania continues to be committed to finding a solution to these problems.

3. The expansion of the ATMs and the POS (point of sale).

Automated teller machines (ATMs) experienced a further development over 2005 - 2006. Most banks have established a number of ATMs in Tirana and in other main cities throughout the country. The number of electronic terminals has grown from 93 at the end 2004 to 266 in August of the present year, while the number of users has increased from 34,090 to about 295,250. ATMs are used through debit cards, but credit cards are also being widely used. Both Visa and MasterCard are actively being used in Albania and most banks are members in one of them, providing the respective cards. Although the use of cards is still limited, the growing number of service units accepting electronic payments (POS-Point of Sale) from 155 in December 2004, to 1073 in August 2006, and the gradual change of the attitude favouring the holding of cash will lead to the enhancement of the use of cards as a mean of payment.

The service of electronic transactions (e-banking) as a banking product began four years ago, although it may be said that it has not reached satisfying levels as far as its introduction and the use by the public is concerned. So far, two banks have been providing this service to particular clients (mainly businesses) for carrying out transfers, different payments etc. Over the present year, other banks have planned to provide this service.

<table>
<thead>
<tr>
<th>Table 1 Number of cards and ATM/POS</th>
<th>2004</th>
<th>2005</th>
<th>August 2006</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cash cards</td>
<td>26,736</td>
<td>173,161.00</td>
<td>220,657.00</td>
</tr>
<tr>
<td>Debit cards</td>
<td>6,552</td>
<td>50,066.00</td>
<td>70,176.00</td>
</tr>
<tr>
<td>Credit cards</td>
<td>806</td>
<td>2,550.00</td>
<td>4,245.00</td>
</tr>
<tr>
<td>Pre-paid cards</td>
<td>136.00</td>
<td>169.00</td>
<td>169.00</td>
</tr>
<tr>
<td>Total</td>
<td>34,094</td>
<td>225,913.00</td>
<td>295,247.00</td>
</tr>
<tr>
<td>ATM</td>
<td>93</td>
<td>205.00</td>
<td>266.00</td>
</tr>
<tr>
<td>EF/POS terminals</td>
<td>155</td>
<td>779.00</td>
<td>1,073.00</td>
</tr>
</tbody>
</table>

4. The network and services expansion through the bank offices

Over 2005 the banking system continued to expand its network rapidly within the Republic of Albania territory. It expanded with more than 50 branches and agencies throughout the country, although most of them were established in Tirana. A considerable number of branches and agencies have
been opening in small towns, indicating that a large share of the population is now being provided with banking services.

Almost all banks have established new branches and agencies, but just like in 2004, the opening of 29 branches and agencies by the small banks (G1 group) makes an impact. It mainly relates to the significant growing number of Banka Popullore branches, which opened 15 new branches throughout the territory of Albania over 2005, and to several other banks within this group, which expanded with some new branches and agencies after a period of long inactivity.

The number of employees grew considerably over 2005, by 24 per cent, from the growth of 26 per cent over 2004. This significant growth in the number of employees is mainly related to the expansion of the banking system network and to the extension of the banks’ activities, which requires a better division of work and a more complete organizational structure. By the end 2005, the Albanian banking system had 3,479 employees, from 2,816 over the previous year.

Compared to the previous year, the number of employees per banking unit decreased over 2005. In 2005, banks had 13.9 employees per banking unit, compared to 15 over 2004. Such a decrease has been a consequence of the growing number of branches and agencies with higher rates than the growth of the number of employees. A considerable number of branches and agencies have been established in sparsely populated areas; as a consequence, the number of employees in these branches and agencies has been quite small.

The number of loan officers has increased considerably, following the significant growth of lending over 2005 and in the upcoming period. A considerable number of banks have restructured their loan departments, aiming at a more distinct division of duties and responsibilities.

The increase in the number of banks, branches and their agencies, as well as the growing number of bank employees have caused the coverage of the population to improve significantly. Thus, the number of inhabitants per bank, banking unit and per bank employee has decreased considerably.

<table>
<thead>
<tr>
<th></th>
<th>2003</th>
<th>2004</th>
<th>2005</th>
</tr>
</thead>
<tbody>
<tr>
<td>Number of employees</td>
<td>2,236</td>
<td>2,816</td>
<td>3,479</td>
</tr>
<tr>
<td>Number of branches, agencies</td>
<td>161</td>
<td>188</td>
<td>250</td>
</tr>
<tr>
<td>Number of employees per:</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>bank</td>
<td>149</td>
<td>176</td>
<td>217</td>
</tr>
<tr>
<td>banking unit</td>
<td>13.9</td>
<td>15</td>
<td>13.9</td>
</tr>
<tr>
<td>Number of inhabitants per*:</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>bank</td>
<td>206,851</td>
<td>194,971</td>
<td>184,410</td>
</tr>
<tr>
<td>banking unit</td>
<td>20,815</td>
<td>16,593</td>
<td>12,539</td>
</tr>
<tr>
<td>bank employee</td>
<td>1,388</td>
<td>1,108</td>
<td>901</td>
</tr>
</tbody>
</table>


Table 2 Coverage with banking services
5. The implementation of the Automatic Electronic Clearing House (AECH) project.

After the introduction of the RTGS system for the settlement of gross payments, the payments infrastructure expanded with the Automatic Electronic Clearing House (AECH) system, which aims at reducing the processing time of small value payments considerably, encouraging as such the use of banking payments. Over the present year, significant improvements have been made in terms of the information technology and communication with commercial banks, which has been indicated by the programmes used and by the purchase of new programmes by several banks. These programmes constitute a better sustaining for the Banking Accounting Manual requirements and serve to the needs of the institution to expand the activity and introduce new services, such as e-banking.

6. The review of the legal framework related to the payment system in the country, paying a special attention to that part which supports the new payment instruments and actors in the country.

The abovementioned developments in technology and information have been supported by the Bank of Albania through the formulation of the Regulation “On the use of information technology and communication of the entities licensed by the Bank of Albania”, approved upon the Supervisory Council decision No. 32, dated 3 May 2006. This regulation will not only assist the provision of a more prudent and complete supervision of the information technology and communication used by banks, but at the same time it will help banks in their day-to-day work and in the use of this technology. Moreover, it will increase the security measures that banks should apply in order to provide the security and the good use of the information, the maintenance of the information and the continuity of work in cases of extraordinary events.

Table 3 The expansion of the banks’ network by the end of the 9-month period of 2006

<table>
<thead>
<tr>
<th>No.</th>
<th>Banks</th>
<th>No. of Branches</th>
<th>No. of Agencies</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Raiffeisen Bank</td>
<td>37</td>
<td>46</td>
</tr>
<tr>
<td>2</td>
<td>National Commercial Bank</td>
<td>22</td>
<td>9</td>
</tr>
<tr>
<td>3</td>
<td>United Bank of Albania</td>
<td>3</td>
<td>1</td>
</tr>
<tr>
<td>4</td>
<td>Italian Albanian Bank</td>
<td></td>
<td>6</td>
</tr>
<tr>
<td>5</td>
<td>Italian Development Bank (former Dardania)</td>
<td>1</td>
<td></td>
</tr>
<tr>
<td>6</td>
<td>Tirana Bank</td>
<td>31</td>
<td>4</td>
</tr>
<tr>
<td>7</td>
<td>National Bank of Greece (Tirana Branch)</td>
<td>4</td>
<td>8</td>
</tr>
<tr>
<td>8</td>
<td>International Commercial Bank</td>
<td></td>
<td>5</td>
</tr>
<tr>
<td>9</td>
<td>Alpha Bank (Tirana Branch)</td>
<td>9</td>
<td>1</td>
</tr>
<tr>
<td>10</td>
<td>American Bank of Albania</td>
<td>10</td>
<td>11</td>
</tr>
<tr>
<td>11</td>
<td>ProCredit Bank</td>
<td>20</td>
<td>1</td>
</tr>
<tr>
<td>12</td>
<td>First Investment Bank (Tirana Branch)</td>
<td>1</td>
<td>1</td>
</tr>
<tr>
<td>13</td>
<td>Emporiki Bank</td>
<td>3</td>
<td>4</td>
</tr>
<tr>
<td>14</td>
<td>Credit Bank of Albania</td>
<td>1</td>
<td>1</td>
</tr>
<tr>
<td>15</td>
<td>Credins Bank</td>
<td>10</td>
<td>4</td>
</tr>
<tr>
<td>16</td>
<td>Banka Popullore</td>
<td>29</td>
<td></td>
</tr>
<tr>
<td>17</td>
<td>Union Bank</td>
<td>1</td>
<td>3</td>
</tr>
<tr>
<td></td>
<td><strong>TOTAL</strong></td>
<td><strong>187</strong></td>
<td><strong>100</strong></td>
</tr>
</tbody>
</table>
Another crucial issue to be paid a special attention to and where certain deficiencies are present, is the SWIFT system. There needs to be a better administration of the users’ profile, in order to observe the three stages of sending the messages (creation, verification and authorization), and a division of security officers’ duties (left and right officer) from the different operational duties at the SWIFT.

It is also necessary that the internal bank audit (or external when provided by consultant companies) be expanded, including the information technology entirely. This audit, which currently is limited only to the system users’ profiles or to the access rights they have in the system, should include issues that relate to the functionality of these systems, the accuracy of generating the information, the changes in the system, the information security during the operation and in transmission (for on-line branches) etc.

7. The enhancement of transparency of the bank commissions applied for loan payments, and in particular the decrease or abolition of domestic commissions or of incoming payments, are another measure that the Bank of Albania is implementing in the context of attracting the public and businesses as far as the banking services are concerned.

Referring to the significant decrease of currency outside banks to total money – from 31 per cent in 2002 to 24 per cent over the present year – as an important indicator of the cash economy, it can be said that the abovementioned measures have provided their effect. However, the reduction of the informal economy remains a decisive factor in order to reach to the levels of cash in more developed economies, which is below 10 per cent. In this context, the establishment of Credit Information Bureau, initiated some time ago by the Bank of Albania and expected to finalize over the coming year, is believed to make an overwhelming contribution to reducing the business informality in the interbank level.
BANKING SYSTEM REFORMS, ACCOMPLISHMENTS AND CHALLENGES

Distinguished participants,

Allow me to express my pleasure for participating in this forum and for the opportunity to present some of the main developments that have taken place in one of the most important fields of the Albanian economy, the banking system.

My presentation will focus on two issues:

First, the main steps followed by the reform in the banking area, presenting the problems related to commercial banks, omitting monetary aspects.

Secondly, the current situation of the banking system and some of the main problems it is faced with, which need solution over the short-term and medium-term period.

The banking system reform was part of the structural reforms undertaken by the Albanian authorities after 1992, which aimed at macroeconomic stability and Albanian economy transformation into a market economy, by privatizing the economy and creating financial and social protection institutions.

The banking system transformation in Albania followed the same path as in other former socialist countries.

The first important phase started with the passing from the one-tier banking system into a two-tier system, in which the former Albanian State Bank was divided into two banks, with a qualitatively distinguished activity from each other. The Bank of Albania was given the conventional functions of central banks, such as: monetary policy, currency issuing, foreign exchange market; while the National Commercial Bank, together with other banks, were given the conventional banking functions, such as accepting deposits, extending loans and other banking services.

The Laws “On the Bank of Albania” and “On the Albanian banking system” adopted in 1992 constituted the grounds needed for this transformation.

It is worth mentioning that one of the fundamental elements of the Law “On the Bank of Albania” of 1992 was the granting of a relatively high degree of independence to the central bank, as a legal, institutional, financial and
personal independence. This independence has been increasing constantly throughout these years, not only as a legal and institutional independence, by amendments made to the Law in 1996 -1997 and after the approval of the Constitution, but also as an independence in the real aspect.

Under the Law of 1992, the dependence of the Central Bank passed from the Government to the Parliament, being given simultaneously the functions of determining the volume of credit, issuing, banking interest rate, the payment system, etc.

At that time, the reform in second-tier banks was focused on three main directions:

1. Introduction of a new regulatory and supervisory framework;
2. Institutional policies in treating the non-performing loans;
3. Plans related to the privatization of state-owned banks.

Notwithstanding the measures taken for the banking system transformation till 1997, when the collapse of pyramid schemes reached the climax, the banking system was not able to operate effectively in carrying out its intermediation function. Private banks, which consisted of small foreign banks or joint-stock banks and which did not have any subsidiaries, hesitated to extend loans and were focused on foreign exchange transactions and trade financing.

The state-owned banks were engaged in domestic lending, but they operated as government agencies, with soft restrictions in funds management and failed to apply the lending practices in compliance with international standards. Also, the Central Bank’s supervisory capacities of that time were limited. Some data indicate that the level of non-performing loans at end of 1996 reached to 60% of the total loan portfolio.

Besides the weak performance in credit intermediation, the range of services provided to the public was also limited.

Many financial activities in the economy were carried out outside the licensed financial institutions. The financial infrastructure, including the payment system of accounting and audit, was also rather weak.

Lack of a formal operational banking system, associated with an insufficient structure of regulations and supervision, contributed to the flourishing of pyramid schemes. The 1997 events served as an encouraging element for deeper reforms in the banking sector.

The Government of that time, in cooperation with the International Community and the Bank of Albania, affirmed the commitment to implementing a full program of reforms needed for the banking system. The Government’s commitment to carry out a full program of structural reforms in the banking sector served as an instrument for re-establishing the public confidence in financial institutions and services.
The program of that period was focused on four main objectives:

- Improving the legal and regulatory infrastructure;
- Building sound and reliable institutions;
- Strengthening the financial infrastructure; and
- Liquidating or privatising the state-owned banks.

Besides the adoption of new laws on the Bank of Albania, on the banking system, on bankruptcy, and on safe transactions, of importance was the program for a rapid change of the state-owned banks’ ownership, which led to the liquidation of the ANB and the establishment of the Bad Assets Resolution Trust. The NCB was recapitalised and privatised in 2000. During 2004, the privatization process of the Savings Bank was finalized, being purchased by the Raiffeisen International Bank Holding, thus recording the transfer of 94% of the banking capital to private ownership.

Currently, the Albanian banking system is composed of 17 banks, 14 of which are of foreign capital. The capital source is from different places, such as Greece, Italy, Austria, Germany, United States of America, etc.

After the privatization process of the former Savings Bank was over and a 100% of its stock was transferred to the Raiffeisen International Bank Holding AG in August, the capital ownership structure during that period underwent significant changes, having the share of “domestic government capital” estimated at 6% from 32.1% at end of 2003, and the “domestic capital” at 12.75 from 35.15% it was in the same period of the previous year.

Recently, the improved climate for the development of business and the economy, the Savings Bank’s privatization from the Raiffeisen Bank, the macroeconomic stability, and the low inflation, have all led to rapid development of the banking system. Hence, we can highlight that:

- During 2005 and onwards, considerable developments have occurred. The system was more oriented towards the lending activity. The latter one constituted 26% of the portfolio, from 16% in the same previous year period. In 2005, the outstanding credit of the banking system increased by ALL 57.6 billion or 82%, from ALL 19.3 billion or 38% in the previous year. In the meantime, the significant growth rate of outstanding credit compared to end of 2004 has been reflected even in the changed credit structure by terms. It comes out of the analysis that the short-term credit has maintained the same growth rate, while a shifting of the mid-term credit to long-term credit is noticed, particularly
when the comparison is made with year-end 2004. Banking system assets of the nine-month period of 2006 increased by ALL 71 billion or 14% more than at year-end 2005, maintaining almost the same growth rate with the previous year. The downward trend of the large banks’ contribution to the growth of the system indicates a reduction of the overall banking activity concentration. Meanwhile, the banking system assets performance in years, but particularly in 2005, expressed as a share of GDP, shows increased depth of the banking system intermediation. The ratio under discussion is estimated at about 59.3% for year-end 2005, versus around 52% at end of 2004 and 60.4% at end of the nine-month period of 2006.

Compared to end of 2004, the banking system appears with an increasing level of profit, to ALL 6.1 billion. Return on equity resulted to 22.24% at end of 2005 and 19.2% at end of the nine-month period of 2006, while the credit quality denominated as a ratio of the net non-performing loans to total loan portfolio is at 2.3%, from 4.2% at end of 2004. However, it is still soon to judge about the credit quality, because credits are still new and their quality has to be monitored prudentially.

Table 1 Banking system data in years

<table>
<thead>
<tr>
<th></th>
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<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Number of banks (out of which with foreign capital)</td>
<td>13 (12)</td>
<td>13 (12)</td>
<td>13 (12)</td>
<td>15 (13)</td>
<td>16 (14)</td>
<td>17 (14)</td>
<td>17 (14)</td>
</tr>
<tr>
<td>Total assets of the banking system (year-end)</td>
<td>270,851</td>
<td>318,457</td>
<td>339,333</td>
<td>373,635</td>
<td>426,440</td>
<td>496,561</td>
<td>567,743</td>
</tr>
<tr>
<td>Total loans (year-end)</td>
<td>28,213</td>
<td>28,277</td>
<td>38,941</td>
<td>50,824</td>
<td>70,148</td>
<td>127,056</td>
<td>171,484</td>
</tr>
<tr>
<td>Total deposits (year-end)</td>
<td>233,087</td>
<td>277,818</td>
<td>289,006</td>
<td>331,426</td>
<td>375,843</td>
<td>432,960</td>
<td>489,693</td>
</tr>
<tr>
<td>Total equity</td>
<td>18254</td>
<td>18760</td>
<td>21620</td>
<td>21,985</td>
<td>25,949</td>
<td>26,993</td>
<td>39,883</td>
</tr>
<tr>
<td>The ratio of credit to GDP (in %)</td>
<td>5.3</td>
<td>4.8</td>
<td>6</td>
<td>7.3</td>
<td>8.9</td>
<td>15</td>
<td>&gt;18</td>
</tr>
<tr>
<td>The ratio of total deposits to GDP (in %)</td>
<td>43.9</td>
<td>47.1</td>
<td>45.8</td>
<td>48</td>
<td>48</td>
<td>52</td>
<td>&gt;56</td>
</tr>
</tbody>
</table>

Table 2 Banking system data in years

<table>
<thead>
<tr>
<th>Indicator in %</th>
<th>December -00</th>
<th>December -01</th>
<th>December -02</th>
<th>December -03</th>
<th>December -04</th>
<th>December -05</th>
<th>9M/06</th>
</tr>
</thead>
<tbody>
<tr>
<td>Capital adequacy</td>
<td>41.80</td>
<td>35.30</td>
<td>31.60</td>
<td>28.51</td>
<td>21.63</td>
<td>18.60</td>
<td>18.27</td>
</tr>
<tr>
<td>Non-performing loans minus provisions on equity</td>
<td>2.00</td>
<td>5.80</td>
<td>4.80</td>
<td>3.94</td>
<td>3.80</td>
<td>3.64</td>
<td>6.29</td>
</tr>
<tr>
<td>Non-performing loans to total loans</td>
<td>42.90</td>
<td>6.90</td>
<td>5.60</td>
<td>4.65</td>
<td>4.20</td>
<td>2.33</td>
<td>3.20</td>
</tr>
<tr>
<td>ROA</td>
<td>2.10</td>
<td>1.50</td>
<td>1.20</td>
<td>1.24</td>
<td>1.28</td>
<td>1.40</td>
<td>1.28</td>
</tr>
<tr>
<td>Interest income to gross income</td>
<td>67.70</td>
<td>83.70</td>
<td>87.00</td>
<td>89.63</td>
<td>80.32</td>
<td>83.97</td>
<td>95.58</td>
</tr>
<tr>
<td>Liquid assets to total assets</td>
<td>80.40</td>
<td>81.30</td>
<td>77.90</td>
<td>73.57</td>
<td>71.10</td>
<td>62.62</td>
<td>58.73</td>
</tr>
</tbody>
</table>

- Year 2005 recorded ALL 33 billion of the shareholders’ equity of the system, or about ALL 7 billion higher compared to 2004, and 19% of the capital adequacy indicator or about 3 percentage points lower than in the same previous year period, whereas for the nine-month period of 2006 these indicators are respectively: shareholders’ equity of the banking system reached ALL 39.8 billion, being increased by ALL 6.8 billion compared to year-end 2005, and the capital adequacy indicator was 18.3% or 0.3 percentage point lower than in the same previous year period.
• Another welcomed development of the banking system belongs to the customer service, which through electronic terminals, has been naturally associated with the increased number of electronic cards in circulation. Presently, banks provide debit and credit cards, in cooperation with the international companies of Visa and MasterCard, Diners Club. Nine banks provide the ATM service and the number of the latter ones at end of December 2005 was 205, while in August of this year it has reached to 266. In the meantime, the number of the points of sale has reached to 1073, of debit cards to about 70,176 and of credit cards to 4,245.

• Undoubtedly, the further expansion and strengthening of the banking system is an important aspect. The geographic extension of covering the territory with banking business, the increased competition, the introduction of many new products and the new recent developments constitute an additional argument for the vital role played by the banking system. The map of covering the country with banking business was further expanded, including new regions uncovered previously. Thirty new branches and agencies were opened during 2004, while in 2005 their number became 48, making the total number of branches at end of 2005 reach 127 and that of agencies reach 113.

• The positive developments in the banking sector and the increased number of subsidiaries and agencies have brought about a considerable increase in the number of employees. So, at year-end 2004, 3491 persons were employed at the Albanian banking system, from 2816 persons in the previous year. This constitutes a growth of 24% per year and expresses clearly the priority the banks are giving to the enhancement of human resources, as a necessary condition for growing the activity in the future.

• These developments indicate an improved perception, not only by banks but also by businesses and households for the investing environment in Albania, encouraged even by the sustainable macroeconomic environment. The annual increase of the number of employees that work at the banking industry by about 24%, versus 26% of the previous year is a logical outcome of the positive developments in the banking sector.

An important role in these developments has been played by the Bank of Albania, in terms of creating a favourable climate for the development of business and the economy. We may highlight here:

• The monetary policy followed in the recent years has always aimed at cutting the interest rates, with a slight change in 2006, intending to keep inflation rate under control. This has impacted on the establishment of a stable business climate, where the business plans and decisions are not jeopardised by the insecurity of inflationary erosion.

• Since some years the Bank of Albania has been committed to create an updated payment infrastructure, so that the banking system is open and closer to customer relations. Hence, after putting into operation the real time gross settlement system and the automated electronic
clearing house system, the establishment of a loans register is presently
aimed at. After the completion of the automated electronic clearing
house system, another possibility is created not only for the banking
system but also for the business of services of a periodic nature, so as
to enhance its economic efficiency.

- The Bank of Albania deems that a banking system helps the economic
growth if it is sound financially, since the developing economies, such
as our economy, are generally characterized by a fragile stability.
Therefore, the Bank of Albania has taken a number of measures,
aimed at enhancing its supervisory abilities, with the purpose to have
a strong, sound and efficient banking system.

Regardless of the positive developments, still much has to be done. The
degree of financial intermediation continues to be relatively low.

Some economy sectors, such as agriculture, continue to be slightly
credited or not credited at all. The banking credit contribution to productive
investments is still low, and moreover, given the high weight of lending to
support the trade activity, the conclusion drawn is that the majority of loans
go for financing the imports. Also, the degree of using the banking system is
not in the required parameters, and moreover, the degree of using cash is
still high.

During the current year, it has been worked for improving the existing
Law “On Banks in the Republic of Albania”. These improvements are
being driven by the need for adopting the European directives in this area,
and by the Basle principles for an effective supervision. Compared to the
existing law, the new draft is aimed at being more complete, more accurate
in some of its elements, including new concepts in compliance with the
European directive 83/349 and other important directives. Amendments
are envisaged in the way of licensing activities according to capital level,
in the consolidated supervision, etc. Many provisions are planned to be
introduced in the law, as concerns to risk management, which so far has
been covered by some regulations. The draft-law, for which international
financial institutions have also given their assistance, has been subject to a
large discussion with the banking industry and is currently submitted to the
Parliament for passing it.

In conclusion, I would say that:

As a result of reforms undertaken, the Albanian banking system, as the most
dynamic part of the financial system, has recorded a constant progress in the
recent years. This process is the fruit of clear visions and earnestness with
which the Albanian authorities have treated the banking sector reformation,
fruitful collaboration these authorities have had with international financial
institutions, such as the IMF, the WB, for drafting the medium-term strategies
and beyond, for the development of this sector as a vital sector of the market
economy and the numerous challenges it has been faced with throughout
these years.
Hence, the Albanian banking system is presented as safe, sound, under a constant reformation and consolidation process, passing into a qualitatively new stage, which will provide the business and bank customers with a modern banking service that aims at achieving the levels and standards of Western banks.

ENDNOTES

1 While the credit outstanding in ALL is increased by ALL 17.5 billion or 128 percent, the one in foreign currency is increased by ALL 40.1 billion, or 71 percent.
Ladies and Gentlemen,

It is a pleasure for me to welcome you in Tirana to this Round Table on Inflation Targeting. This meeting is a follow-up of the Open Forum that took place in December last year. Today and tomorrow we will discuss the work that the central bank has been doing since the Open Forum. Together, we hope to have deep discussions and to determine a list of topics that should go on our IT-agenda for the year 2007 and possibly for the year 2008.

I am very pleased to welcome our foreign guests. Some of you, we have met before here in Tirana at the Open Forum. Others join us today for the first time. You come with your experience from other European central banks (Croatia, Czech Republic, Frankfurt, Finland, Hungary, United Kingdom and Turkey) and from major international institutions (IMF, European Commission) and, last but not least, academia. Next to our foreign guests, I warmly welcome our guests from other institutions in Tirana.

From the Bank of Albania about 30 experts will actively participate during these two days. Some of them will be presenting our Discussion Papers and others will enter the discussions with our guests. The management of the Bank of Albania can exchange their ideas with you on the follow-up of all these ongoing projects, in the short to the medium term.

Our Governor, Mr. Ardian Fullani will join us later today or tomorrow.

Metaphorically, I would like to sketch these two days as follows. Today we will start swimming in a troubled ocean. Although troubled, you will be able to distinguish two schools of fishes. One school consists of the employees of the BoA. The other school consists of our guests. The fishes in the first school may swim, let us say “wildly”, but together. Their diversity will become more apparent during these days: the different fishes have different characteristics, and some will swim shallow and others will swim deep. Some may even reach the bottom of the ocean. Both schools will be swimming apart, but the discussions will make the two schools heading for the same direction. At the end of tomorrow you may not even see many differences between the schools anymore. And, hopefully, all fishes will be heading for the same direction towards clearer water.

On the contents, today will be a day where we concentrate on the Inflation Targeting path that the BoA is following, macro-econometric modeling and inflation forecasting and the communication strategy. The BoA can swim by
and large on its own. But, it is seeking for some confirmation on the direction, and the depth level.

Tomorrow, the relation with other institutions here in Albania comes into play. The BoA is seeking a way to get (1) the statistical framework for Albania in order, (2) to transform its Monetary Policy Report into an Inflation Report (3) to coordinate issues with the Ministry of Finance and (4) to identify the legal borders to Inflation Targeting.

Ladies and gentlemen, I wish you fruitful discussions during these two days.

As said before, we seek a confirmation that we are on the right track as we want to bring the Bank of Albania to high central banking standards. Like human nature everywhere, we like to receive nice words. Next to the confirmation, please give us your true views. But during this Round Table we will need your critical remarks for further improvements in the daily processes of the Bank of Albania.

Thank you for your attention.
ON THE FINDINGS OF THE ROSC MISSION ON THE STATISTICAL DATA DISSEMINATION MARCH - APRIL 2006*

ACRONYMS:

COICOP – Classification of Individual Consumption by Purpose
CPI – Consumer Price Index
DMFAS – Debt Management and Financial Analysis System. In use by the Ministry of Finance
DMFAS – Debt Management and Financial Analysis System. In use by the Ministry of Finance
DQAF – Data Quality Assessment Framework
FSAP – Financial Sector Assessment Program
GDDS – General Data Dissemination System
GDP – Gross Domestic Product
HBS – Households Budget Survey
IIP – International Investment Position
IMF – International Monetary Fund
ISWGNA – Intersecretariat Working Group on National Accounts
ITRS – International Transaction Reporting System
NACE Rev. 1 – Statistical Classification of Economic Activities in the European Communities, Revision 1
PPI – Producer Price Index
ROSC – Report on the Observance of Standards and Codes
SBS – Structural Business Survey
SDDS – Special Data Dissemination Standard
SNA 93 – System of National Accounts, 1993
WB – World Bank
ABSTRACT

This paper summarizes the findings of the ROSC Mission on the statistical data dissemination, which visited Albania over March – April 2006. The Mission made a positive assessment of the progress achieved in producing and disseminating the national statistics since 2000. The Mission’s findings and the recommendations left in order to improve the Albanian statistical framework constitute the core of the future developing plans of the three main national statistical agencies: INSTAT, the Bank of Albania and the Ministry of Finance.

INTRODUCTION

ROSC Mission on data dissemination visited Albania for the second time over March – April 2006. The assessment of the statistical processes development in Albania, the identification of problems and the taking of measures timely precedes one of the most important projects of national statistics: membership to the SDDS project. This paper summarizes the findings and recommendations of the Mission on the five main macroeconomic statistics categories: external sector statistics, national accounts, prices statistics, monetary statistics and fiscal statistics of the Government.

The first part of the paper provides some information on ROSC and its importance in the development of one’s country financial market, focusing on ROSC for the data dissemination. Moreover, it provides an explanation of the method of assessment (Data Quality Assessment Framework - DQAF) and of the criteria considered in the assessment. The second part of the paper gives the findings of the Mission on each of the data categories according to the DQAF framework. The third part provides the measures taken by the three statistical agencies in the country (INSTAT, Ministry of Finance and the Bank of Albania) in order to observe the Mission’s recommendations.

ROSC AND ITS IMPORTANCE

The role of the international standards in consolidating the financial structure is perceived by the international community as an ever-increasing need. In an environment where there are integrated capital markets, the financial crisis can be spread quickly and jeopardize the international financial stability. As a consequence, the establishment of a minimum of international standards is considered as a public “good”, from which both international and national systems would benefit. At an international level, these standards enhance transparency and enable the multilateral supervision of the national systems; they provide the opportunity of identifying the weaknesses that may potentially lead to an economic and financial destabilization, as well as enhance market efficiency. At a national level, the international standards provide a criterion for identifying problems and orienting the reforms. In order to reach these goals, the observance of standards must be assessed in the context of the general strategy of the country’s development and in
accordance to its terms. In this context, the IMF and the WB have, since 1999, been undertaking an initiative to evaluate the whole number of rules where given countries’ economic policies are implemented, comparing them with the best international practices. These rules and practices named codes and standards are being assessed as important for the development and stability of the financial and private sector and are summarized in some modules called ROSC - Report on the Observance of Standards and Codes -, under the responsibility of the IMF, the WB or in their common projects. The IMF is in charge of assessing the standards in data dissemination and transparency. The modules for the financial sector (transparency of monetary and fiscal policy, banking supervision, regulation of securities markets, payment system and deposit security) are undertaken under the joint responsibility of the WB and the IMF in the Financial Sector Assessment Program (FSAP). The WB is also in charge of three other fields covered by ROSC, corporate management, auditing and accounting and creditors’ rights.

Through the promotion of the adoption of the international standards, this initiative aims to achieve three intermediate goals: first, help countries to enforce their economic institutions; second, support the IMF and the WB to better assess the needs and risks of a country; and third, to inform the market members and enhance market efficiency.

The assessment of ROSC missions has been generally applied in developing financial market countries and in developed ones, while the participation of developing countries has been lower. Around 90 percent of developed countries and of developing financial markets countries have, at least, had one assessment from the ROSC missions. Empirical tests indicate that participating countries are mostly those countries that aim to be more transparent and to reinforce their institutions. Around 75 percent of the ROSC assessments have been released, while the developed countries mainly are the ones to publish this assessment.

There have been several empirical studies, mainly of the Fund experts, in order to assess the ROSC efficiency. They all pose the hypothesis that the ROSC assessment, ROSC publication and the membership to the data standards projects (GDDS and SDDS) bring advantages in borrowing costs reduction, strengthening the country’s rating and increasing the market efficiency. Despite the limits that these studies have, due to the small volume of choices, to the short time series, etc., they generally show that the participation in these projects brings some advantages to the countries. Four of these studies point out that the identification of issues and the follow-up of the proposed reforms, in particular in banking supervision and in policies transparency, improve the market performance rating and indices.

Both the IMF and the WB have developed detailed methodologies for the assessment of standards, which are under a continuous process of review. For instance, the IMF uses DQAF in the data dissemination, which is essentially a methodology for assessing the statistical data that covers their entire production cycle and is straight related to their accessibility, assurance of data integrity
and their quality. These methodologies can be even used by the countries themselves in order to assess the observance of standards in certain areas. In general, the countries’ self-assessment using the ROSC methodologies among developing financial market countries has had a greater impact on policies transparency, financial infrastructure and on the rules and practices that assure the market integrity. Such an assessment has been made on the Bank of Albania statistics dissemination in 2005 by the Statistics Department and has enabled the improvement of some practices prior to the ROSC assessment.

Further in this paper, we will briefly explain the assessment methodology used by the ROSC for the data dissemination – DQAF. The second part of the paper summarises the assessment of the ROSC mission for the statistical data in Albania.

DQAF is a methodology for data quality assessment which joins the best international practices and methodologies including the “United Nations Fundamental Principles of Official Statistics” and SDDS and GDDS projects. Since 1997, this methodology has been constantly being reviewed, following the consultations with different countries statisticians, experts from international organizations, IMF experts and statistical data users outside the IMF. In order to develop the quality assessment methodology, it was first necessary to clarify the dimensions of the statistical data related to the quality. Even though the quality of statistical data often implies their accuracy, today there is a general consensus that the quality of data is a multidimensional concept. According to DQAF, there are five dimensions which define data quality: assurance of data integrity, adequate methodology, accuracy and reliability, data serviceability and data accessibility. For each of these five dimensions, DQAF is detailed in monitorable characteristics that can be used to assess quality. Moreover, DQAF specifies that there should be some prerequisites of quality – a supporting environment for the statistics, accordance of sources with the statistical programs requirements and the orientation to quality in statistics. DQAF includes a normative affirmation, which describes the international standards and the assessment is made comparing the latter with the country’s practices. DQAF assesses the practices according to a four-point rating scale:

- Practice observed,
- Practice largely observed,
- Practice largely not observed, and
- Practice not observed.

This system makes the assessment easily understandable even from a non-technical auditor, highlights the priorities for improvement more clearly, and it also enables the comparison of the practices among different countries.

The component dimensions and characteristics are summarized in table 1. Section 2 of the paper presents the assessments for each characteristic of the official statistics assessed by the ROSC mission. The first column of the table presents the five dimensions of data quality along with the prerequisites of quality (in the table, listed from 0 to 5). The second column of the table
presents the components of each dimension and the third one the criteria used to assess their observance. We will refer to the second column elements in section 2, which are grouped according to the respective dimensions.

### Table 1 DQAF dimensions and component elements

<table>
<thead>
<tr>
<th>Dimensions</th>
<th>Dimensions' elements</th>
<th>Indicators</th>
</tr>
</thead>
<tbody>
<tr>
<td>0. Prerequisites of quality</td>
<td>0.1. The legal and institutional environment is supportive of statistics</td>
<td>The responsibility for collecting, processing, and disseminating the statistics is clearly specified.</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Data sharing and coordination among data-producing agencies are adequate.</td>
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<td>Individual reporters’ data are to be kept confidential and used for statistical purposes only.</td>
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<td>Statistical reporting is supported through legal mandate or other measures to encourage response.</td>
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<td></td>
<td>0.2. The resources must be adequate to meet statistical programs’ needs.</td>
<td>Human resources must be at an adequate level, in order to carry out the duties in accordance to the statistical programs.</td>
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<td></td>
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<td>The level of technology must be adequate to carry out the duties in accordance to the statistical programs.</td>
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<td>Financing for the compilation of statistics must be adequate to carry out the duties in accordance to the statistical programs.</td>
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<td>There should be mechanisms to ensure the most efficient use of resources.</td>
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<td></td>
<td>0.3. Monitoring of the serviceability of statistical data</td>
<td>The statistical agency is entitled to comment on erroneous interpretation and misuse of statistics.</td>
</tr>
<tr>
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<td>0.4. Statistical information quality on the basis of the process.</td>
<td></td>
</tr>
<tr>
<td>1. Assurance of data integrity</td>
<td>1.1. Professionalism</td>
<td>Statistics are produced on an impartial basis.</td>
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<td></td>
<td>Choices of sources and statistical techniques should be based solely on statistical considerations.</td>
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<td>The statistical agency is entitled to comment on erroneous interpretation and misuse of statistics.</td>
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<td></td>
<td>1.2. Transparency of statistical processes</td>
<td>The terms and conditions under which statistics are collected, processed, and disseminated are available to the public.</td>
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<tr>
<td></td>
<td></td>
<td>Internal governmental access to statistics prior to their release is publicly identified.</td>
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<td></td>
<td></td>
<td>Products of statistical agencies/units are clearly identified as such.</td>
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<tr>
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<td></td>
<td>Advance notice is given of major changes in methodology, source data, and statistical techniques.</td>
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<tr>
<td></td>
<td>1.3. Ethical standards – policies and practices are guided by ethical standards</td>
<td>There are ethical standards in the statistical agency, whose observance is continuously monitored.</td>
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<tr>
<td></td>
<td></td>
<td>The ethical standards are well known to managers and staff of the statistical agency.</td>
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</tbody>
</table>
### 2. Methodology
- **2.1. Concepts and definitions**
  - For each data category, the IMF has a reference standard, such as the MSMF, 2000 for monetary and financial statistics, etc. The methodology elements are assessed by comparing the existing practices with the reference manuals.
- **2.2. Scope**
- **2.3. Classification/sectorization**
- **2.4. Basis for recording**

### 3. Accuracy and reliability
- **3.1. Source data**
  - Source data are chosen based on all-inclusive programs, which take into account country-specific conditions.
  - Source data enable the compilation of statistics to meet the methodological requests for scope, classification, sectorization and valuation of assets and liabilities.
  - The information required as an input for the statistics are reported timely, in order to allow the timely compilation of the statistical indices.
- **3.2. Assessment of source**
  - The data reported from the reporting units are continuously controlled and the results of this control serve to identify and solve the problems.
- **3.3. Statistical techniques**
- **3.4. Assessment of intermediate data and statistical outputs**
- **3.5. Data revision studies**

### 4. Serviceability
- **4.1. Periodicity and timeliness**
  - Periodicity (different for different types of data).
- **4.2. Integrity**
  - The delay in statistics release (different for different types of data).
- **4.3. Existence of a data revision policy and its publication**
  - Statistics are consistent within the dataset.
  - Statistics are consistent with the time series (with a minimum duration of five years).

### 5. Accessibility
- **5.1. Data accessibility**
  - Statistics are presented in a way that facilitates proper interpretation and meaningful comparisons.
  - Dissemination media and format are adequate (hard copy, webpage etc).
  - Statistics are released on a pre-announced schedule.
  - Statistics are made available to all users at the same time.
- **5.2. Metadata accessibility**
  - Documentation on concepts, scope, classifications, basis of recording, data sources, and statistical techniques is available, and differences from internationally accepted standards, guidelines, or good practices are annotated.
  - Levels of detail are adapted to the needs of the intended audience.
- **5.3. Assistance to users**
  - Contact points for each subject field are publicized, and there should be catalogues of publications, documents, and other services.
THE FINDINGS OF THE ROSC MISSION MARCH-APRIL 2006 ON THE ALBANIAN STATISTICS

The ROSC Mission on the data quality that visited Albania in 1999, published by the Fund in 2000, apart from the positive assessments, left a number of recommendations including the establishment of a national accounts system, the improvement of the legal framework and the coverage of economic activities, in particular of the real and external sector statistics, as well as the efficient use of the information sources. During March – April 2006, another ROSC Mission on the data quality visited Albania to reassess the progress achieved in these data categories: national accounts, consumer price index, producer price index, government fiscal statistics, monetary statistics and external sector statistics. The statistical agencies responsible for the dissemination of these types of data – the Institute of Statistics (INSTAT), the Ministry of Finance and the Bank of Albania, were also assessed for the prerequisites of quality and assurance of data integrity. Further in this paper, there is a summary of the Mission’s assessments for each of the data dimensions.

0. PREREQUISITES OF DATA QUALITY

0.1. The institutional responsibility for the compilation and dissemination of the data categories covered by ROSC is clearly specified in the legal framework and in the day-to-day work practices of INSTAT, Ministry of Finance and Bank of Albania.

- The new Law “On Official Statistics”, No. 9180, which stands at the basis of the functioning of the INSTAT, defines INSTAT as an independent governmental unit under the supervision of the Statistics Council, which before 2004 had only consulting functions. This Law clearly gives the INSTAT the responsibility for the collection, processing, and dissemination of official statistics. Moreover, the Law explicitly states the reporting confidentiality and the responsibilities of respondents to submit data to INSTAT.

- The Macroeconomic Department in the Ministry of Finance is specifically designated to compile government fiscal statistics and to produce monthly and quarterly bulletins on fiscal statistics. The Organic Budget Law No. 8379 of July 29, 1998 authorizes the Ministry of Finance to specify reporting requirements for budgetary institutions, budgetary and extra-budgetary funds, and local government.

- The Bank of Albania is, by tradition, responsible for compiling and disseminating monetary statistics, although the BoA Law does not specifically spell out this statistical mandate. The BoA is the only statistical agency carrying out this function and the Law gives to the Bank of Albania the right to formulate the reporting requirements for commercial banks, juridical and natural persons. However, the Law is not clear on the cases of misreporting. Reported data confidentiality is rigorously observed in practice by the work procedures, however, the Law states that these data may be disclosed to tax authorities. The Mission suggests that the existence of such a possibility in the Law may...
potentially decrease the reporting entities’ confidence on the usability of reports by the Bank of Albania. Moreover, the perception of such a possibility provided by Law reduces the confidence of the public in the official statistics.

The Mission assesses that the information sharing among agencies and the conditions, under which the entities report, need improvement. The information sharing is done through Memorandums of Understanding among the institutions, a part of which actually is in the process of drafting. Regarding the regulation of the flow of information, the Mission suggested the implementation of an electronic reporting system for banks and other financial institutions to enhance the efficiency of monetary and balance of payments statistics compilation processes and to allow a more efficient use of the resources. Another recommendation is the introduction of a database for keeping and compiling the statistical information for monetary, financial and balance of payments statistics.

0.2. The sources of the statistical agencies are insufficient to carry out the existing processes adequately and to realize the plans of these agencies related to their projects.

- The Mission assesses that INSTAT’s human resources, work conditions, information technology and financial resources are inadequate to fulfil this institution’s targets.
- At the Ministry of Finance, the human resources are inadequate to put the current and planned statistical programs into function, required to monitor the fiscal policy.
- At the Bank of Albania, human resources in the Balance of Payments are not adequate, while resources for monetary statistics are adequate for current responsibilities only. The Mission suggests that additional statistics staff resources are needed to compile other financial statistics, such as the funds flow account, the compilation of financial flows for monetary statistics and for other short- and mid-term plans of the division. In addition to the increase of the statistics staff, the Mission recommends more information technology support and integrated database development to further enhance the efficiency of statistical processes at the BoA.

0.3. Monitoring of the data relevance:

The three institutions monitor regularly users’ needs through seminars, surveys and periodical meetings among statistical agencies and international organizations. Particular users’ needs are another information source that serves to extend or modify the published statistical indices.

4.4. Statistical information quality

The three institutions show interest for the statistics quality. There are regular practices to monitor quality including self assessment (DQAF prepared by the Statistics Department of the Bank of Albania), monitoring of the working programs related to the statistics, as well as periodical meetings with the reporting subjects in order to clarify the reporting
requirements.

1. ASSURANCE OF DATA INTEGRITY

1.1. Professionalism

- At the INSTAT, professionalism and impartiality of official statistics are guaranteed by the Law “On official statistics”, which specifies that there should be no interferences from the government or any other institution. The Law also stipulates that the roles and tasks of the Statistics Council and of INSTAT’s General Director. The Statistics Council proposes the appointment of the General Director, who is approved by the Prime Minister and the Council of Ministers. INSTAT staff has the Civil Servant status and is appointed based on qualifications. INSTAT promotes staff participation in seminars and research activities which enhance professional capacity. The selection of data sources, statistical techniques and data dissemination practices are based only on statistical considerations. Governmental bodies have no right to preliminarily access the statistical data prior to their publication. INSTAT staff is obliged to respond to erroneous interpretation and misuse of statistics and organizes and encourages the correct use of statistics through seminars with the users and through explanations of the indices.

- The Organic Budget Law provides the independence of the Ministry of Finance staff in executing the accounting and statistics functions. This Law gives the MoF the independence to choose sources and reporting methods, which are released on its website. The MoF regularly monitors the coverage of its data in the media. The Spokesperson for the Minister comments on erroneous interpretations of official statistics when deemed necessary.

- The Law “On Bank of Albania” ensures the independence of the BoA. The BoA defines its own methodologies and procedures for compiling and disseminating monetary and balance of payments statistics, taking into account international standards. Recruitment and promotion of BoA staff are based on professional competence and training and professional development opportunities are provided. Choices of statistical methodology are based solely on statistical considerations. The BoA comments on public use of statistics and is active in developing a culture of statistics through a training program for the media.

1.2. Transparency

The terms and conditions under which statistics are compiled are available to the users by all the three institutions. The major changes in methodology are released in advance and are available to the public on the websites of each of the statistical agencies. All users have simultaneous rights to use all data categories.

1.3. Ethical standards

Staff behaviour in all the three statistical agencies is guided by the Law “On the Status of Civil Servants” (INSTAT and Ministry of Finance), the related Ethical Code of each agency. Staff is trained on the institution’s ethical standards and during periodical performance reviews, ethics observance is
2. METHODOLOGY

2.1. Concepts and definitions
The elements for assessing the statistical indices for each data category are assessed based on SNA 93, NACE Rev. 1, COICOP and the relative IMF’s manuals: MFMS 2000, GFSM 2001, and BPM5. For all the statistical categories except for Government Finance Statistics, the concepts and definitions used are evaluated to be in line with the best international practices. Regarding the fiscal statistics, the concepts and definitions follow GFS 1986 and it is not yet realized the transition to the new methodology.

2.2. Scope
The Mission assessed that the scope is in line with the international standards on production price index, fiscal, monetary and balance of payments statistics.

Regarding the national accounts, INSTAT does not produce all the accounts needed to meet the minimum requirement of the Intersecretariat Working Group on National Accounts7. Actually, the national accounts include only the annual value added and GDP at current and constant prices by 25 major activity groups and the annual expenditure components of GDP at current and constant prices.

Regarding the consumer price index, the scope was assessed to be broadly in line with the standards. However, the existing HBS (Household Budget Survey) covers only urban households, accounting for 45 percent of all households. The new HBS, currently in preparation by INSTAT will cover rural households as well.

2.3. Classification/sectorization
The Mission assesses that classification and sectorization practices used are consistent with internationally accepted standards (respective manuals for every data category).

2.4. Basis for recording
The basis for statistics recording are assessed to be broadly consistent with the standards, however the Mission remarks that there are some discrepancies in the consumer price index, national accounts, monetary and balance of payments statistics.

- In the national accounts, this discrepancy is mainly related to the treatment of the non-deductible VAT in the intermediate consumption and to the government accounts recorded on a cash basis6.
- In the consumer price index, the deviation from the standard is related to the non-inclusion of resold goods prices and their respective shares.
- In the monetary statistics, the deviation relates to the accounting of the savings and credit associations’ accounts on cash basis (while
required on accrual basis) and the treatment of long term securities held by the banks. In the current reporting requirements these instruments are reported at their purchase price in accordance with the banking accounting manual, while for monetary statistics purposes their recording is required at the market value.

- In the balance of payments statistics, the discrepancy relates to the recording of public debt interests on accrual basis.

### 3. ACCURACY AND RELIABILITY

This dimension is related to the source data and to their periodical assessment. Among all the other dimensions, the Mission assesses the lack of sources as the most problematic issue for the Albanian statistics compared to the other dimensions.

#### 3.1. Source data

The Mission assesses the source data for the monetary statistics as completely in line with the standards, the source data for CPI, PPI and fiscal statistics as largely in line with the standards, and the source data for the balance of payments statistics as largely not in line with the standards.

- Regarding the national accounts, the source data have some limitations, among which can be listed improper design of the questionnaires (SBS), partial coverage of the Albanian territory (HBS), the low frequency of the surveys, the exclusion of the informal economy and the delays in reporting.
- On CPI, the Mission assesses that the methodology used by the HBS is in line with the best international practices, but the non respondents to the questionnaire are not replaced. This causes a reducing deviation of the CPI, due to the fact that generally the entities that avoid reporting are those with the higher income.
- On PPI, source data do not provide the information reported on time. Prices are collected for each month but only once every quarter, causing delays in PPI dissemination for the first months of the quarter. Moreover, the weights used derive from the 1998 SBS and the enterprises that have ceased business are not replaced.
- The problem in source data for the fiscal statistics is in the availability of data on certain external donor financed (grants) projects that do not pass through the Bank of Albania and the commercial banks.
- According to the balance of payments statistics, the source data, even if in due time, are based on infrequent and/or incomplete surveys, including those on freight, insurance, and smuggling adjustments for imports; travellers’ expenditures domestically and abroad; workers’ remittances; direct and portfolio investment; and trade credit. Grants from abroad to regional and local governments are underreported.

#### 3.2. Assessment of source data

The assessment of source data is related to surveys routinely assessed,
sample error, coverage, misreporting, etc., and the use of this information to further guide the statistical processes. The Mission evaluates the national accounts, fiscal and balance of payments statistics as fully consistent with the standards, while the CPI, PPI and monetary statistics as largely in line. Actually, the identified problems are:

- Regarding CPI, the prices collected, even if checked for the very different values from the others, but the information obtained from the surveyor is not checked.
- Regarding the PPI, the remarks are the same with CPI.
- Concerning the monetary statistics, there are checking processes on the source data, such as the reporting control based on the “Manual of Control Procedures”, however they are time-consuming and cause delays in the whole statistics production process, since they are mostly manual.

3.3. Statistical techniques

In compiling the statistical indices, statistical techniques should adapt to data sources. Moreover, the statistical processes such as the data adjustments and transformations and the statistical analysis should be based on suitable techniques. In relation with this element, the Mission assesses the fiscal statistics as the only consistent with the standard, while assesses CPI, PPI, balance of payments and monetary statistics as largely in line with the standards. The statistical techniques used in the national accounts are evaluated as largely not consistent with the standards. More precisely, the identified problems are:

- In the national accounts, the estimates of the value added from the non-observed activities, especially for construction activity, is limited due to the very limited labour input data in production. Estimates of expenditure components rely also on weak assumptions and the results are not crosschecked against other data sources.
- Regarding CPI, the current weights derive from 2000 and considering the major changes in the real household consumption, the weights used are far from reality.
- The same issue is worthy even for PPI, where the weights derive from 1998. The Mission recommends changing the weights for 2005 and introducing a regular program for rebasing the index at least every six years.
- For the monetary statistics, the Mission recommends to change the practice of delayed reporting. In the previous practice, if there were delays in reporting by a commercial bank, the statistical indices were not compiled until the arrival of this report. The Mission recommends the dissemination of the elementary indices that are calculated using the existing reports and those of the previous period of the entity that has not reported. The elementary indices are identified as such in the publications of the Bank of Albania.
- For the balance of payments statistics, the current compilation system is based on distinct Excel spreadsheets and is prone to error. Remittances are calculated as part of the unidentified transactions in the balance of payments. The Mission recommends also that the split
of “total remittances” between remittances from seasonal work and remittances from workers residing in another economy should be re-estimated.

3.4. Assessment of intermediate data and statistical outputs

This element implies the evaluation of intermediate results, considering additional information, apart from those used in the compilation process and the study of possible discrepancies. As a result, it is needed a statistical analysis of the intermediate results and of the output in order to see if there are any discrepancies in findings and findings from statistical analysis of the other indices. The Mission evaluates this process consistent with the standards for CPI, fiscal and monetary statistics, while national accounts, PPI and balance of payments statistics are evaluated to be largely in line with the standards.

- Regarding the national accounts, the adjustments to remove discrepancies are not sufficiently detailed (used at a high level of aggregation). This is a result of the too limited resources they rely on, as well as of inefficient use of the existing resources.
- Regarding PPI, the Mission recommends to validate the PPI results with CPI and all the other available price indices.

3.5. Data revision studies

According to the best international practices, revised data should be accompanied by analysis on the effects due to changes in methodology that take place on the data, in order to aid users in understanding the functions in time. These studies should be carried out routinely with the statistical work. The Mission evaluates that this practice is fully followed in the CPI, PPI, fiscal, monetary and balance of payments statistics. Concerning the national accounts, revision studies are done on an ad hoc basis and not according to a definite program. As this data category is the most sensitive regarding revisions made even within a relatively long period of time, the existing practice is estimated as largely in line with the standards.

4. SERVICEABILITY

In order for the statistical data to be serviceable for the users, they should minimally fulfill these criteria: being available at the right time and periodicity, being consistent on time or within the series and among each-other and follow a predetermined review policy.

4.1. Periodicity and timeliness

As Albania is part of the GDDS project, the Mission evaluated the practices related to the delay from the reference date and the periodicity related to this standard. As shown in Table 2, the practices for national accounts and PPI are not consistent with the standards. Since Albania aims to adhere to SDDS by the end of 2007, in the table are shown even the requirements of this standard. The current practices do not meet the SDDS requirements on national accounts, PPI and monetary statistics.
Table 2: Timeliness and periodicity practices compared to the SDDS and GDDS standards

<table>
<thead>
<tr>
<th>Data Category</th>
<th>Practice</th>
<th>GDDS Standard</th>
<th>SDDS Standard</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Periodicity</td>
<td>Timeliness</td>
<td>Periodicity</td>
</tr>
<tr>
<td>National accounts</td>
<td>Annual</td>
<td>11 months</td>
<td>Annual</td>
</tr>
<tr>
<td>CPI</td>
<td>Monthly</td>
<td>8 days</td>
<td>Monthly</td>
</tr>
<tr>
<td>PPI</td>
<td>Monthly</td>
<td>4 months</td>
<td>Monthly</td>
</tr>
<tr>
<td>Government Finance Statistics</td>
<td>Monthly</td>
<td>1 month</td>
<td>Annual</td>
</tr>
<tr>
<td>Monetary Statistics</td>
<td>Monthly</td>
<td>6 weeks</td>
<td>Monthly</td>
</tr>
<tr>
<td>Balance of payment statistics</td>
<td>1 Quarter</td>
<td>10 weeks</td>
<td>Annual</td>
</tr>
</tbody>
</table>

4.2. Consistency
This element is related to the procedures that check statistical data for consistency within a dataset (with other statistical indices), as well as consistency as a time series. The Mission evaluated as consistent with standards all the other data categories except for national accounts that are evaluated as largely in line with the standards. This is due to the fact that the estimation of GDP with the expenditure approach is not independent from the production approach and consistency is ensured through balancing items on the expenditure side. The Mission recommends independently estimating the components of GDP with the expenditure approach, and checking the indices consistency.

4.3. Data revision policy
According to the standards, data revisions should follow a predetermined released calendar, in order for the users to know if the data are final or not and also to know when they can have the final data. Revision studies and analysis should be publicized together with the data. Except for national accounts and fiscal statistics, the current practices are consistent with the standards.
- Regarding the national accounts, not all the publications indicate clearly the data status (preliminary, revised, or final).
- Regarding the fiscal statistics, the revisions are indicated only at the data publication moment and not before.

5. Accessibility
The accessibility is related to the facility of the users to understand and use the data. The elements evaluated by DQAF related to this dimension are data accessibility, metadata accessibility (information on data), and assistance to users from the statistical agency.

5.1. Data accessibility
Data accessibility means data dissemination in a format and in a manner that is easy to use (such as through tables, charts, etc.). Moreover, it implies statistical indices dissemination according to a calendar released in advance by the agency. The Mission evaluated the practices followed by all data categories, except for national accounts, in line with the standards. For this data category, the Mission remarks that statistical indices dissemination does not follow the predetermined calendar published by INSTAT.
5.2. Metadata accessibility

The standards recommend the release of the concepts, scope, basis for recording, source data and deviation from the international standards. The levels of detail of the metadata should match the needs of the targeted audience, so there should be different media to disseminate this information. The Mission evaluates the national accounts, fiscal, monetary and balance of payments statistics as in line with the standards, while recommends the release of CPI and PPI statistical methodologies.

5.3. Assistance to users

The assistance to users according to the standards implies providing contact points for each data category in order to answer specific questions or requests of the users. Moreover, this element implies the existence of catalogs of publications on the indices, documents related and statistical services offered. The Mission assesses all data categories, except for national accounts, as consistent with the standards. This is due to the fact that the INSTAT website is not always updated with the latest information on the indices, even if this information is available on other formats (hard copy).

MEASURES ADOPTED BY THE STATISTICAL AGENCIES TO IMPLEMENT THE MISSION’S RECOMMENDATIONS

In response to the recommendations left by the Mission, all the three statistical agencies have taken measures to improve those practices that deviate from the standards. Together with the ROSC assessment has been published the response by the Albanian authorities to the ROSC assessment, which delineates the institutions’ plans and manner to improve their practices and measures already taken.

THE RESPONSE TO THE GENERAL ROSC RECOMMENDATIONS

- Hire new staff and increase the information technology support in the statistical agencies, in order to fulfil the current or planned statistical programs.

The structure of the Statistics Department at the Bank of Albania will be reviewed by the first quarter of 2007. Apart from the commitments in providing information for internal purposes of Bank of Albania, in its position as a distributor of statistical data, the staff increase in the Statistics Department, will enable the compilation of flows data (financial sector), IIP and External Debt statistics.

- Maintain a professional staff in the statistical agencies and upgrading the status of INSTAT staff in the hierarchy of the government civil service and upgrading office facilities in all the data-producing agencies. Continue emphasizing staff training and development.
The statistical agencies are continuing their work in order to enhance the competence level of the statistics staff. Therefore, the development of human resources in INSTAT has recently benefited from a raise in salaries of its staff. At the Bank of Albania’s commitment to meet the monetary policy needs for real and fiscal sector data, in the view of launching Inflation Targeting, the staff working in the Statistics Department, has been trained to comprehend and assess the statistical information produced by the other institutions.

- Increase financial resources for improving source data. Attach priority to improving source data to adequately capture the non observed economy and remittances, which are particularly important in the Albanian economy.

INSTAT and Bank of Albania are working on estimating the informal economy in Albania. A better understanding of the structure and type of the transactions will enable a better estimation of remittances.

- Sign Memorandums of Understanding between data producing agencies and define the modalities of data sharing (e.g., data details, timetable, responsibility on these data, etc.)

INSTAT and Bank of Albania are in the process of drafting a Memorandum of Understanding, which is in the final stage of completion. Moreover, with the establishment of a centralized database at the Bank of Albania, that shall contain a great number of statistical data, from the major data producing institutions, the Statistics Department at Bank of Albania is working to define the required modalities that will be included in the memorandums of understanding with these institutions.

- Implement an electronic (online) reporting system for banks and other financial institutions to enhance the efficiency of monetary and balance of payments statistics compilation processes. Introduce an automatic compilation system for monetary and balance of payments statistics.

The implementation of this recommendation is included in the BoA strategy plan as a medium-term plan, to be accomplished by 2007.

RESPONSE TO SECTORAL RECOMMENDATIONS

NATIONAL ACCOUNTS

- Expand and improve surveys, such as, labour force survey and country-wide HBS.
  By the beginning of 2007, INSTAT will conduct a labour force survey, while the preparations for HBS, that will be presented by 2007 have already started. Improving labour data should be a matter of priority in the context of using these data so as to ensure the reliability of the national accounts estimates.
• Expand the scope of annual national accounts to include the income account, the capital account, and the rest of the world accounts as intended in INSTST strategic plan.
In the framework of the EU funded Twinning project is created a strategic plan to define the possibilities to include these accounts in the INSTAT produced statistics. INSTAT is currently developing a methodology to estimate the generation of income account starting from the estimate of wages and salaries.

• Rationalize statistical techniques to maximize the use of existing source data, used for the expenditure approach. The introduction of a single balancing item combining household final consumption, changes in inventories, and the statistical discrepancies for years when household final consumption cannot be separately estimated.

INSTAT is working to improve the methodology of calculation of GDP from expenditures side.

• Use of more data sources to cross-check the accuracy of intermediate data.
Basing on the Mission’s recommendations, INSTAT will review the methodology that estimates household consumption for 2003-2004, on LSMS basis. In the same time, there are possibilities for a better use of the business structural survey to revaluate the construction sector activity.

• Apply the revision policy consistently. Identify status of disseminated GDP (e.g., preliminary, revised, and final) in all releases.
The recommendation is implemented already.

• Update the advance release calendar.
The recommendation is implemented already.

• Improve the timeliness of the data for the national accounts releases through a better use of the INSTAT website.
The recommendation is implemented already.

CONSUMER AND PRODUCER PRICE INDICES

• Update the weights.
Update of CPI weights will be enabled by the HBS conduction. The current version of PPI uses a fix base index and INSTAT is working to replace this approach with the chain index one. This type of index enables the use of different weights, if felt necessary.
The revision of product list was done using the Business Structural Survey of 2004. Moreover, INSTAT is preparing a new questionnaire for PPI data compilation. Creation of authentic data entry, in collaboration with IT staff, is in process.
• Publish the PPI every month.
The publishing of PPI every month requests the collection of the data on monthly basis. So far, because of usage of enumerators, INSTAT collects the data on the enterprises on monthly basis. The recommendation will take place on medium term.

• Check on the prices reported by the enumerators.
With the renovation of CPI and PPI the new data entry system will have an automatic check of price reported.

• Replacement of the non-respondents to the HBS with similar households (CPI) and replacement of the enterprises that go out of business.
In the methodology of the HBS it is not foreseen the replacement of the non-respondents with the similar household. In the new PPI index the replacement of enterprises will be once a year, in December.

• Validate the PPI results against all other available price indices.
INSTAT is working to find comparison methods between PPI and export – import prices, CPI etc.

• Update the methodology used and publish it in both languages (English and Albanian).
The drafting of the relative methodologies is in process.

GOVERNMENT FINANCE STATISTICS

• Accelerate work aimed at adopting the GFSM 2001 methodology for monthly and quarterly reporting.
The Albanian Ministry of Finance Treasury System (AMoFTS) is on the phase of testing and training, until the end of 2006. MoF plans to go-live with the system on the beginning of 2007. This system is going to ensure the passage from a cash basis reporting to an accrual basis one as required by the standards.

• Construct a national chart of accounts for the government sub sectors aligned with GFSM 2001 classifications.

Ministry of Finance will implement and publish a detailed (7 digits) chart of accounts for the general government, in 2007.

MONETARY STATISTICS

• Strengthen the BoA law to provide full legal assurances that individual reporters’ data may be used only for statistical purposes.
The BoA’s Legal Department is drafting a new law on the Bank of Albania. Thus, it has been planned that the amended Law will pass to the Parliament by end 2009. This Law will also strengthen the legal
support for the dissemination of monetary and financial statistics by including an explicit role for the Bank of Albania to disseminate these statistics. It will also ensure confidentiality of individual data and use of these for statistical purposes only.

• Implement an electronic (online) reporting system for commercial banks and other financial institutions to enhance efficiency of monetary statistics compilation.
  The implementation of this recommendation has been included in the BoA’s strategy plan as a medium-term plan. This duty is expected to be fulfilled by the end of 2007.

• Increase of the Information Technology Department staff, involved in the statistical processes to (1) design the SARS database for a better performance including the automatic generation of monetary data and (2) implement an electronic (online) reporting system for commercial banks. More human resources are needed in the SD to expand monetary statistics to cover other financial corporations and to compile flow data for the financial sector, as recommended by the Fund’s methodology (MFSM-2000).
  The structure of the Department of Statistics will be reviewed until the first quarter of 2007, and will be expanded to include among other things, the compilation of flows data on the financial sector. The Sector of Financial Statistics is currently working on a draft structure.

  The compilation of flows data together with the stock would require additional information from bank’s reporting in order to separately identify the transactions from the changes in value due to changes in the market value of the securities holdings of the banks portfolios. The SD is currently considering the possibility of taking this information from the commercial banks.

• Revalue long-term securities for investment held by the commercial banks and use estimated fair value.

  The SD will consider obtaining this information by the commercial banks, while the information required for this change is already available from the Accounting and Payments Department.

• Adopt accrual accounting for SLAs so as to apply fully the MFSM guidelines.
  For the moment the SD considers that the SLA’s accrual assets and liabilities are not enough materially significant such as to justify an increase in the reporting burden. The total assets of such institutions represent only 0.4 percent of the total assets of Other Depository Corporations.

• Implement measures to minimize errors in commercial banks’ reporting and speed up processes that check and correct reports.
The time lag for reporting by banks has been already shortened, on October of the current year, from 20 days to 15 days, from the end of the referred month. It will be further shortened to 10 days starting from March 2007. This measure allows more time for the reports to be checked for errors, before they are used for the compilation process.

- When delayed reporting by commercial banks occurs, carry forward the balance sheet for the previous month of the late reporting bank and make users aware of this technique. The data should be denoted as provisional.

The recommendation is implemented already.

BALANCE OF PAYMENTS STATISTICS

- Conduct more frequent surveys: on quarterly basis for remittances, redo the foreign trade survey in order to revalue freight, smuggle and trade credit coefficients.

Particularly because remittances are a predominant item in the Albanian balance of payments, in 2007 several surveys in quarterly basis will be conducted to the households who receive money from their family abroad.

Later, it will be analyzed whether new coefficients need to be applied on freight and smuggled goods, that it will be conducted on the big importing companies.

- Strengthen the Bank of Albania law to provide sanctions for the entities that do not fulfil the legal obligation of reporting to the Bank of Albania for statistical purposes, include the right of the Bank to inspect the financial accounts of firms, and to prohibit the provision of these reports to tax authorities.

The legal status of the Bank regarding to the statistics and the right to reporting will be reviewed on medium term.

- Obtain the public debt service schedule from the MoF and record interest on an accrual basis.

The DMFAS system actually used by MoF for monitoring of external debt (suspended debt) does not calculate the accrued interest. With the implementation of the new version of this system it will be provided the necessary information for this change.

- Obtain quarterly reporting in direct investment equity, debt, and reinvested earnings; in portfolio equity and debt; and in trade credit.

The annual survey of Bank of Albania in cooperation with INSTAT is not supported by the legal requirement of Bank of Albania to have direct reporting from the firms. This recommendation will be applied in line with the improvement of the Bank of Albania legal framework.
• Estimate purchases of land and construction financed by unidentified foreign exchange inflows.
Bank of Albania is actually conducting a survey on construction companies and real estate agencies to find what portion of the constructions is being financed by unreported transactions between residents and non-residents. This is the very first survey of this kind in Albania. The results will be analyzed in order to understand the structure and the type of transactions necessary to develop estimation methods of the BoP statistics.

• Improve the coordination with INSTAT with respect to survey design, execution, and follow-up to non-response.
Bank of Albania’s Statistics Department and INSTAT, are both working to further improve the quality of the surveys starting with the designation of the questionnaire and the improvement of the response rate.

• IT support to set up an automated compilation system that would preclude the need for manual data entry, could include electronic reporting by banks, and possibly ITRS.
The implementation of this recommendation is included in the Bank of Albania strategy plan as a medium-term plan.

SUMMARY

The ROSC Mission on data dissemination finds considerable improvements in the national statistical framework since 2000. These achievements are mainly due to the implementation of the new Fund’s methodologies, to the improvements of the legal basis that supports statistics, to the increase of the staff involved in statistics compilation and dissemination, etc. From the assessment, it results that in the major part of the quality dimensions and component elements, the national practices are consistent with internationally accepted standards, as presented in table 3. The Mission recommends the enhancement of the support that implies support with financial resources, qualified staff, information technology and improvement of the working facilities. Among all the data categories, the most problematic ones are the national accounts statistics, whose quality is doubtful because of the insufficiency of sources, inappropriate techniques, etc. Their improvement through the measures given in section 3 of this paper is one of the main challenges for Albania’s membership in the SDDS project by the end of 2007. In addition to these improvements, this standard requires the compilation of some other categories, such as quarterly national accounts, data on wages and salaries, industrial production index, IIP, Albania’s external debt (including all its sectors and instruments), module of international reserve and foreign currency liquidity, etc. Monetary and fiscal statistics are presented much better than the other categories. In the meantime, the improvements in the national accounts structure are the most significant ones expected in the improvement of the statistical standards.
### Table 3 Data Quality Assessment Framework—Summary Results

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<td>Dimensions/Elements</td>
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<td>3.5 Revision studies</td>
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<td>4. Serviceability</td>
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<td>5. Accessibility</td>
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<tr>
<td>5.1 Data accessibility</td>
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<td>5.3 Assistance to users</td>
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</tr>
</tbody>
</table>

**Key to symbols:** O = Practice Observed; LO = Practice Largely Observed; LNO = Practice Largely Not Observed; NO = Practice Not Observed; NA = Not Applicable
REFERENCES


ENDNOTES

* This paper was prepared by Hilda Shijaku, Head of Financial Statistics Division and Kliti Ceca, Director of Statistics Department. Special thanks to Evis Ruçi, Head of Balance of Payments Division, for her collaboration.

1 Data Quality Assessment Framework.

2 Published in the Economic Bulletin, volume 8, number 1, June 2005.

3 The report has been already published on IMF website, at the following link: http://www.imf.org/external/pubs/cat/longres.cfm?sk=20059.0

4 Among the long-term projects are included the membership to the SDDS project, the provision of information needed by the decision-makers in terms of an inflation targeting regime and practices converging to the European standards.

5 ISWGNA recommends these accounts as minimum: annual value added and GDP at current and constant prices by activity; annual expenditures of GDP at current and constant prices; annual value added components at current prices by activity; sequence of accounts for the total economy up to financial accounts with an annual frequency; and rest of the world accounts.

6 The transaction is recognized when the cash accounts are affected.
INTRODUCTION

Economic development in the transition countries has been considerable over the past years. Positive performance, frequently higher than that of the developed countries, has helped in narrowing the gap of the economic development between transition and developed countries. Albania, like the other transition countries, has had significant economic growth in these last years. Maintenance of the macroeconomic stability is reflected in low inflation rate, in increased confidence of the public in the domestic currency and the banking system. Macroeconomic stability on the other hand, reflects a good coordination of the fiscal and monetary policies and the progress in structural reforms. But the economic development, like in many other countries could face risks caused by domestic and foreign factors. To better manage risky situations, structural reforms take a specific important role that could serve as a construction in building a healthy and robust economy. This paper analyzes the Albanian position as opposed to more developed countries in the region, which have made the greatest progress in the context of reforms. It also raises some key challenges the country faces to maintain and enhance economic development.

I. AN OVERVIEW OF THE TRANSITION COUNTRIES

The transition countries have displayed considerable economic growth rates over these last years. Economic growth in these countries has been mainly driven by a high domestic demand, which has been spurred by credit and wage growth. On the other side, strong domestic demand and high energy prices are exerting inflationary pressures throughout the region. Moreover, domestic savings are insufficient to cover investments, resulting in large current account deficits especially in countries that are not rich in natural resources. Foreign direct investments are projected to reduce slightly from the levels recorded in 2004-2005. In 2006, several countries’ currencies have come under pressure in the foreign exchange market. This reflects a more critical valuation by foreign investors on the vulnerabilities of the economies of this region. Furthermore, central banks in the United States, Euro area and Japan lately raised their interest rates, making investments in these countries become more attractive.

Central banks in transition countries have been trying to deal with the problems arising from the rapid development of the financial sector combined with a rising inflation rate. Many central banks have decided to raise the
interest rates, to introduce stricter regulations on the minimum reserves or to take other measures against inflation. Against this background, fiscal policy has generally been too loose to stem domestic demand effectively. The case of more restrictive fiscal policies is becoming more necessary in view of long term implications of aging population that will cause significant pressures on the fiscal budget in the future.

Economies of transition countries are gradually catching up with European economies and other matured markets. Thus, the economic growth of 5.7 per cent in 2005 and around 6.2 per cent in 2006 is several percentage points higher than that of the Euro area. Anyhow, further economic development faces risks coming from global imbalances and from the increase of the interest rates in the OECD countries, which influence on diminishing the interest in investing in these countries.

Over the medium term, transition countries are projected to continue to have considerable growth rates, although slightly slower for 2007. These developments are expected to reflect progress in structural reforms and increasing integration with the world economy. Performance in Central-Eastern Europe and the Baltic states is closely related to the performance in the Euro area, while South-Eastern Europe and Commonwealth of Independent States and Mongolia countries still face substantial hurdles in reforms.

Transition countries according to the European Bank for Reconstruction and Development are grouped in:

1. Central-Eastern Europe and the Baltic States. Countries of this region had the best start for transition. Many of these countries had welcomed the concept of private property, market based prices and had strong popular support for rapid economic and political changes that would accelerate integration into the European and transatlantic institutions. During the first 10 years of transition much was achieved in these countries. This was partly prompted by the need to harmonize their legislation with that of European Union countries before becoming member states. Over the last years, these countries have concentrated on completing the reforms that will allow them to compete effectively in the European and global market. Despite the successful accomplishment of the initial phase reforms, some of the second phase reforms in areas, such as governance and enterprise restructuring, competition policy and infrastructure have dropped behind. These reforms are often difficult to design and require more time to be implemented. Among these countries, Estonia is assessed to have made the greatest progress.

2. South-Eastern Europe. Many countries of this region started the transition process with some basic elements of a market economy. Over the last years, there has been a remarkable revival of the market forces all over the region. A very important factor was the relative stability after the turmoil of 1999. Institutions such as the Stability Pact for South-Eastern Europe have assisted in creating a climate of cooperation in all the countries of the region. The prospective of this region is the continuity of the reform progress. The countries

Bank of Albania
of this region are divided into two main groups, SEE3 including Bulgaria, Rumania and Croatia and SEE5, including the other countries, such as Albania, Bosnia Herzegovina, Macedonia, Montenegro and Serbia. Bulgaria and Romania have had the most rapid progress, in the context of joining the EU. The success of Bulgaria and Romania in achieving the objective of EU membership in January 2007 is a factor of motivation for the other countries of the region. Therefore, the Association and Stabilization Process in the EU plays an important role in encouraging main reforms in areas, such as trade policies and food and safety standards. Consequently, countries of this region have begun to narrow the differences with the countries of Central-Eastern Europe and Baltic states and have come before CIS countries in terms of progress.

3- Commonwealth of Independent States and Mongolia (CIS). The countries of this region started the transition process with the most unfavourable conditions among the transition countries, including here the geographic isolation from the Central European countries, lack of experience in market economy and democratic institutions and the long time under the communist regime. Anyhow, they made significant progress during 1995-2000. Meanwhile, progress in reforms decreased significantly after 2000, in particular in oil and gas producing countries. Since 1992, non-energy producing countries have outpaced the energy producing countries in the two phase reforms. There is a strong link between the rise in oil prices and the slowdown in reforms in the energy producing CIS countries. The majority or reforms in these countries took place during 1992-1997, when oil prices fluctuated between 5 and 20 US $ per barrel. From 1999, when oil prices started to rise quickly, reforms have slowed down and in some years have gone into reverse in a few countries. Furthermore, the investment climate has become worse in energy producing countries in CIS as oil prices have increased. Similarly, the majority of corruption indices suggest that this phenomenon is a more disturbing problem in energy producing countries than in non energy producing one in this region. In this region, Russia, Ukraine and Kazakhstan have made the greatest advances.

II. THE POSITION OF ALBANIAN BETWEEN MORE DEVELOPED TRANSITION COUNTRIES

In the table below, is given a comparative development of some of the countries of the three transition regions that have made the greatest progress in reforms and Albania. This information is based on the evaluations of EBRD about progress in reforms for these countries. EBRD follows the development in reforms in transition countries throughout 9 indicators of transition. These cover four main elements of a market economy:

- Markets and trade reform is measured by the liberalization of prices, the liberalization of traded and access to foreign exchange and the effectiveness of the competition policy.
- Enterprise reform includes indicators for small-scale and large-
scale privatizations and a measure of governance and enterprise restructuring.

- Financial institutions reform is measured by the development of the banking sector, including the quality of financial regulations and the creation and development of securities markets and non-bank financial institutions.
- Infrastructure reform is measured by the progress in five sectors, electricity, railways, roads, telecommunication and water and water waste.

The chosen indicators cover issues like: commercialisation, reform in tariffs, quality of the regulator framework and involvement of the private sector. The scale of measurement of the indicators ranges from 1 to 4+, where 1 stands for little or no change from a centrally planned economy and 4+ stands for standards of an industrialized market economy.

Table 1 Progress in reforms

<table>
<thead>
<tr>
<th>Countries</th>
<th>Enterprises</th>
<th>Markets and trade</th>
<th>Financial institutions</th>
<th>Infrastructure</th>
</tr>
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<tbody>
<tr>
<td></td>
<td>Large scale privatisation</td>
<td>Small scale privatisation</td>
<td>Governance and enterprise restructuring</td>
<td>Price liberalisation</td>
</tr>
<tr>
<td>Albania</td>
<td>3</td>
<td>4</td>
<td>2+</td>
<td>4+</td>
</tr>
<tr>
<td>Estonia</td>
<td>4</td>
<td>4+</td>
<td>4-</td>
<td>4+</td>
</tr>
<tr>
<td>Hungary</td>
<td>4</td>
<td>4+</td>
<td>4-</td>
<td>4+</td>
</tr>
<tr>
<td>Bulgaria</td>
<td>4</td>
<td>4</td>
<td>3-</td>
<td>4+</td>
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<tr>
<td>Romania</td>
<td>4-</td>
<td>4</td>
<td>3-</td>
<td>4+</td>
</tr>
<tr>
<td>Russia</td>
<td>3</td>
<td>4</td>
<td>2+</td>
<td>4-</td>
</tr>
<tr>
<td>Ukraine</td>
<td>3</td>
<td>4</td>
<td>2</td>
<td>4-</td>
</tr>
</tbody>
</table>

Source: EBRD

From the comparison of the evaluations presented in the above table, it seems that Albania is positioned after the more developed transition countries of Central and South-eastern Europe countries and almost in the same level with the most developed CIS countries.

To better understand the Albanian position between these transition countries, we need to take into account the conditions of the country when the transition process started. Albania started transition with a lack of experience in the market economy, democratic institutions and coming from a hard communist system. As such, the transition process of the country started from significant worse conditions in comparison with the Central-eastern and South-eastern European countries and in more similar conditions with CIS countries. Economic performance, as a result of the measures taken by fiscal and monetary policy and structural reforms during these years, has been successful and is reflected in strong economic growth, low inflation rate and stable exchange rate. On the other side, the maintenance of the good macroeconomic performance over these last years, faces risks like instability from high credit growth and the continuing reliance on remittances from abroad to cover the trade deficit.
From the analyses of the stage of the economic development of Albania, it results that a lot is to be done. Among the most important challenges that Albania faces to induce and maintain the macroeconomic performance and to approximate standards with the most developed transition countries of our region like Romania, Bulgaria and Croatia and later on with the Central eastern European countries are:

- Taking systematic and effective decisions against corruption and organised crime. Taking measures to increase the efficiency and impartiality of the public administration and the juridical system are needed to improve the business confidence in the public sector.

- Improvement of the transport infrastructure, road network and the progress in restructuring and privatisation of the electricity system are needed to promote more reliable services, enhance standards and robust economic growth. Improvement of the energy supply system is one of the most immediate problems in the country. Reliability of energy supply is noticeably under the international standards and electricity blackouts are a continuous problem in the country, especially in dry periods. Improvement in the investment in the electricity sector is endangered by the low tariff collection rates.

- Improvement in the quality of the domestic production through increase in investments and labour training would increase the competitiveness of the exports. These measurements would help to lower trade deficit and to reduce the dependency created from remittances of the Albanians working abroad.

Concluding, we can say that Albania like many other transition countries has a lot to do to reach the best macroeconomic parameters. But, despite the so-far developments, the further development of the country seems to be a derivate of the willingness for further progress in structural reforms.
ENDNOTES

* This paper was prepared by Ms. Elvana Troqe, Specialist of Monetary Issues Office, Monetary Policy Department.

1 Transition countries are usually called the countries that have moved or are moving from a system of state planning to a system of market economy with private ownership of assets and market supporting institutions.

2 Include: Czech Republic, Estonia, Hungary, Latvia, Lithuania, Poland, Slovak Republic, and Slovenia.

3 Include: Bulgaria, Croatia, Romania, Albania, Bosnia Herzegovina, Republic of Macedonia, Montenegro, and Serbia.

4 Include: Russia, Armenia, Azerbaijan, Belarus, Georgia, Moldova, Ukraine, Kazakhstan, Kyrgyz Republic, Mongolia, Tajikistan, Turkmenistan, and Uzbekistan.

5 Also by EBRD.
SURVEY OF DEPOSIT AND CREDIT ACTIVITY DURING JULY - DECEMBER 2006*

SUMMARY

After processing the opinions of the commercial bank specialists about the development in the deposits and credit activity during the second half of 2006, it resulted that:

DEPOSITS ACTIVITY

- Commercial banks’ specialists consider that deposit activity performance has improved during the second half of 2006, in comparison with the first half of the year;

- The majority of commercial banks have fulfilled almost 100 per cent of their quantitative targets about deposits, sometimes exceeded, for both lek and foreign currency deposits;

- Positive performance of deposits has been affected by increases in interest rates, for both lek and foreign currency deposits, high credibility toward the bank and the provision of services of a higher quality;

- In the majority of the cases, commercial banks have developed strategies to maintain and increase the deposit clientele. As frequently met, elements in commercial banks strategies are: “introduction of new products and marketing them”, “competitive interest rates”, “qualitative and fast service”, “preferential treatment of existing clients” etc.,

- Actual levels of lek interest rates are considered as normal;

- Based on the specialists opinions, in the future is expected:
  - A better performance of deposit activity, especially for foreign currency deposits;
  - a growing tendency of the interest rates in lek and in foreign currency;

CREDIT ACTIVITY

- Credit activity in the banking system has shown a good performance in the second half of 2006 compared to the first one. The average level of the fulfillment of the quantitative targets for credit in lek is higher than for credit in foreign currency.
• Credit risk has been estimated to be higher than in the first half of the year. Electricity crises have been mentioned as an important factor which threatens the future of the economic and financial statement of the business, affecting credit payments.

• Banks have shown higher preference for lending to small business and to individuals. Under higher competitive pressures in the market, banks have been oriented toward new segments of the credit market, facilitating the procedures and policies for credit approval for these groups. Credit policies and procedures have remained unchanged for the large business clientele.

• The demand for credit is estimated to be higher than in the first half of the year for all bank clients. Evidently the small business and individuals have had higher demand for credit.

• According to the opinions of the bankers, in the first half of 2007, is expected:
  • The same level of credit risk;
  • Further increases in credit level. Credit activity is expected to accelerate in forms of mortgages, consumer credit and credit for business.
  • The same preference toward economic sectors, trade sector being the preferred one.
  • An acceleration of credit in lek more than in foreign currency.

INFLATION EXPECTATIONS

• The majority of the commercial bank specialists expect an increase in the rate of inflation during the first half of 2007. The main reasons behind this expectation are: lack of political stability, local elections which are expected to be followed by higher government expenditures and actual electricity crises.

• Expectations for unchanged levels of inflation and those for a lower inflation rate are mainly based on the confidence in the Bank of Albania policy for maintaining price stability.

ANALYSIS OF THE SURVEYED DATA FOR THE SECOND HALF OF 2006

During January 2007, Bank of Albania conducted the survey on deposit and credit activity for the second half of 2006. The purpose of this survey is to collect the commercial bank specialists’ opinions about the latest developments in the deposit and credit activities. In this survey there are included the opinions of about 86 deposits specialists and 93 credit specialists.
I. DEPOSIT ACTIVITY

About 82 percent of commercial banks’ representatives regard the deposit activity of the second half of 2006 as better than that of the preceding six-month period. The remaining part does not see a difference between these periods. Around 70 percent of depositing specialists claim their quantitative targets about deposits have been completed at 50-100 percent levels. About 27 percent of the banks exceeded their targets. A satisfactory situation is observed in foreign currency deposits, where 72 percent claimed fulfillment of targets at 50-100 percent levels while 25 percent surpassed their targets.

In overall, the positive performance of depositing activity during the second half of the year has been affected by: interest rate increases, both in lek and foreign currency, a high level of credibility toward banks and a high quality of the services provided to the public. In the mean time, some of the reasons for poor performance in deposits are mentioned: high competition, other options for public to invest their savings, such as real estate (foreign currency mostly) etc.

Indeed, the banking service has shown positive developments during 2006. It enlarged to 17 banks from 16 in the previous year and a lot of existing banks expanded their branches, creating more options for the public to invest their savings. Commercial banks seem more cautious toward their clients, and especially their competitors. During 2006, banks have been pretty active and somehow aggressive, in order to attract more deposits. About 94 percent of the surveyed specialists claimed that their banks have been following a strategy for preserving and increasing the number of their clients. Elements such as: “introduction of new products and marketing them”, “competitive interest rates”, “qualitative and fast service”, “preferential treatment to existing clients” etc., have been part of these strategies. Commercial banks’ specialists have named a lot of new products and offers focused toward different market segments, such as products for clients under 18 years old, promotional offers during periods of emigrants’ arrival, internet banking service to businesses, etc. When asked about the proportion of internet banking in their depositing activity, a lot of specialists said that internet banking is in its initials but with a good perspective for the future.

Opinions about the positive performance of depositing activity during the second half of the year
are well supported by real data on commercial bank deposits during this period. Contrary to previous part of the year, growth rates of both lek and foreign currency deposits have been increasing. Foreign currency deposits have continued to show high rates of growth. The ratio of foreign currency deposits to total deposits increased to 38.3 percent or by 1.7 percentage point higher than in June. Interest rates in lek and foreign currency have shown an increasing trend during the second part of the year. These rates have reflected changes of policy rates of Bank of Albania, ECB and Federal Reserve, during this period.

Specialists seem optimistic regarding the development of the deposit activity during the first half of 2007. Furthermore, this optimism remains higher for foreign currency deposits. About 77 percent of the specialists foresee an increase in lek deposits during the first half of 2007 whereas, 20 percent do not expect changes. Regarding foreign currency deposits, about 82 percent of the specialists expect increases of them and 16 per cent do not expect changes. As main factors that will influence mostly the future tendency of deposits in their respective banks, specialists rank: the quality of the service, market interest rates developments and offering good conditions (relatively high interest rates, low commissions). Confidence index on expectations, in both deposits in lek and in foreign currency, shows an enforcement of the growth tendency.

About 83 percent of the specialists have assessed as normal the level of interest rates of lek deposits. About 13 percent of the specialists assessed actual levels as high whereas 4 percent of them described them as low. About 52 per cent of the specialists that have described the level of actual interest rates as normal forecast increase on lek interest rates in the first half of 2007. The other part, 36 percent, does not expect changes in lek interest rates.

Specialists’ expectations for interest rates in foreign currency are divided between alternatives for increase (about 47 per cent) and remaining the same (about 45 per cent). Confidence index on expectations in interest rates indicates an increasing tendency for interest rates in lek and in foreign currency. Specialists rank central bank policy
via repo auctions as the most important factor in determining future tendencies of lek interest rates. Than are ranked development in inflation rate and in the yields of the treasury bills.

Approximately, 86 percent of the specialists affirm that:

- The depositing decision (in lek or foreign currency) is mostly affected by interest rates;
- Monetary policy of the Bank of Albania and interest rates defined in repo auctions, affect lek deposits interest rates and aftermath the change in preferences for deposits in lek or in foreign currency.
- Bank of Albania’s interventions in the banking sector market are effective.

II. LENDING ACTIVITY

The survey on commercial banks in January 2007, shows that credit activity in the second half of 2006, has performed better than in the first one. The average level of the quantitative targets about credit in lek is 83 percent, being 4 percentages point above the June survey. The opinions show an increase in the number of banks which fulfilled or exceeded their credit targets. This survey shows a decrease in the number of banks or their branches, achieving less than 50 percent of their quantitative target in lek credit.

Foreign currency lending has shown positive improvement in quantitative targets. In average, banks have fulfilled 70 per cent of their targets. According to commercial banks specialists, the fulfillment of targets for lending in lek is substantially higher compared with the foreign currency lending. Still the number of branches or agencies that do not disburse foreign currency lending continues to be significant.

Credit risk is estimated to be higher than six months ago. The statistical distribution of opinions demonstrate significant asymmetric deviation on the left in the upper side (see chart 7). This shows a considerable increase of opinions for higher credit risk. The acceleration of the lending activity and, in particular, the involvement of banking system in lending more to small business and individuals has made them more aware of the higher credit risk they take. Besides the acceleration of lending activity, major part of the specialist judge the electricity crises as a threat to the future of economic and financial business activity, and as such to poor performance
of repayments. In the same way the distortion in the political area and lack of register for credit are also regarded as important factors in influencing the growth of credit risk. Some specialists have also mentioned that aggressive policies of the banks, in order to maintain and extend their market size, may bring to unexplored disbursement of loans.

The majority of specialists expect the credit risk to remain unchanged in the first half of 2007. However the high positive value of the index for the future emphasizes the upper pressures in credit risk. These expectations are highly influenced from further acceleration of the lending activity and the lack of prompt solution of the energy crises. However the index of the future stands in a low level from the current one, showing a moderate postponement of the opinions in the low risk side.

The interviewers judged as high the quality of the loan portfolio, in the second half of 2006. Compared with the previous survey is evident the increase of opinions on the same quality of loan portfolio and also a decrease of opinions for higher quality of it.

The interviewers stress the presentation of nonrealistic balance sheet and the deficiency in business plan as main problems of business applying for a loan. These factors have shown an increase in importance comparing with the results in the previous survey. Also, banking specialists think that businesses suffer from lack of managerial skills to manage properly their activity. The fulfillment of the collateral criteria is judged to be a medium importance factor in the lending process.

In the second half of 2006, banks have not changed the credit procedures and policies for the large businesses. Commercial banks initiated their lending activity with the large businesses and as such the products for this group may have been consolidated during the last five years. Statistical distribution of the opinions shows that; with the decrease of the business size it increases the number of opinions for facilitating the procedure and policies of credit agreement. This result goes in line with the conclusions of the previous survey, which has demonstrated an attraction of the banking system toward the small business and individuals. In the second half of 2006 banks have been more policy oriented toward individuals. The majority of the opinions (66 per cent) show further easing of the procedures and policies for the individual’s credit. The official data demonstrate from more than a year, an acceleration of annual growth rate of credit to individuals. However the bank orientation toward retail banking may be seen as a response to stronger competitiveness in the credit market. Under the pressure of higher competition, banks are exploring new segments of the credit market, easing the criteria of credit agreement, especially for individuals. The attraction of individuals, as it has
been mentioned from the interviewers, will increase the possibility of deterioration of the loan portfolio quality, in the future.

According to credit specialists, the Bank of Albania policy has influenced the tightening of lending procedures. This is consistent with the recent announcement of Bank of Albania to increase the prudential measure in order to control the credit acceleration and the quality of loan portfolio. The deterioration of some of prudential indicators, such as capital adequacy ratio and the increase of nonperforming loan has also influenced the decisions of banks to tight procedures for credit agreement. The competitiveness from non-bank institutions is not considered to influence the policy orientation of commercial banks.

Demand for credit from all bank’s client is reported to be higher compared to the previous period. The distribution of the opinions shows a stronger demand from small business and individuals, affected by easing of procedures and policies for credit disbursement. Easing the conditions for credit approval is accompanied with higher demand of businesses to finance fix asset and liquidity shortage. In mean time, there are opinions that credit demand from large business is reduced.

The trade sector will continue to be the most attractive sector regarding credit disbursement in the future. Opinions of the current survey do not show any substantial change in the bank preference to credit distribution by the economy sectors. The service sector preference results higher than six months ago. This result is also supported from the banking system orientation to lend more to small and medium enterprises, which operate mainly in the service sector. Less favorite sectors will remain agriculture and transport. The official data confirm the results of this survey.

According to specialists’ opinions, credit will continue to accelerate in the near future. The lending activity will be channeled in mortgages and credit to fulfill business needs for funds. The index of credit in lek, eventually higher than the one of credit in foreign currency, transmits the signal that banks in the upcoming six months will aim at lending
more in lek. However, compared with the historical development of this index, the current figure is at the lowest value in the last 2 years, showing a restrained growth of lek credit. Meanwhile, lending in foreign currency is expected to remain at stable levels as the current one.

The further increase of lending activity is expected to be accompanied with interest rate increases. Such an increase of credit interest rate is a respond to higher risk of credit activity. The specialists are more confident about interest rate increases for credit in lek than in foreign currency. Credit interest rates in lek are going to reflect the policy of Bank of Albania. Credit interest rates in foreign currency will follow the developments on the international markets, which are expected mainly to remain in the same level.

INFLATION EXPECTATIONS

About 53 percent of the specialists expect an increase in the inflation rate for the first half of 2007. About 35 percent do not expect changes on inflation from actual levels. Factors that shaped the expectations of an increased inflation level on this survey are: lack of political stability, local elections accompanied by increases on government expenditures and the electricity crises. Whereas, expectations for unchanged inflation rate or a lower one are based mainly on the confidence that the Bank of Albania will take all the required measures to maintain price stability.

In the previous survey, the majority of specialists predicted inflation in the same levels with that of the first half of the year. Anyhow, this percentage had been decreasing in the past surveys and the percentage of the specialists predicting an increase in inflation is enhanced. According to the official data, the average annual inflation rate for the second half of the year 2006 was 2.7 per cent from 2 per cent in the first half of the year.
ENDNOTES

* Prepared by Ms: Eriona Suljoti, Head of Monetary Issues Office, Monetary Policy Department,
  Ms. Klodiana Istrefi, Chief Specialist of Monetary Issues Office, Monetary Policy Department,
  Ms. Elvana Troqe, Specialist of Monetary Issues Office, Monetary Policy Department.
  1 The level of response is about 97 percent.
  2 The confidence index is the difference of percentage between positive (increase) and negative (decrease) responses.
  3 The interviewers in lending activity have an average experience at work of about 4.3 years and they are mainly in management position.
On 30-31 October 2006, the Bank of Albania hosted the 6th International Conference titled “Regional financial markets and financial stability – a concept between national sovereignty and globalization”. The Conference was held at the Sheraton Hotel in Tirana. It addressed a broad range of issues related to financial stability against the backdrop of new financial trends in the region. It was organized in six panels, focusing on recent financial market developments, the role of commercial banks in financial stability, financial stability, surveillance and monetary policy issues, as well as financial institutions supervision. Regional co-operation, in terms of financial stability, was the key issue of the roundtable, which gathered the Governors of regional central banks in the sixth panel.

On 31 October 2006, during the proceedings of the 6th International Conference of the Bank of Albania, Mr. Ardian Fullani, the Governor of the Bank of Albania, announced the winners of the “Governor’s Award for the Best Diploma Theses”. A large number of Albanian students worldwide were part of this initiative. A scientific committee evaluated the diploma theses submitted by the Albanian students and three prizes were awarded to the following students:

- First prize to Ms. Gizelda Emini, a Finance graduate of the University of Tirana.
- Second prize to Mr. Arbër Boriçi, a Computer Science and Economics graduate of the University of New York, Tirana.
- Third prize to Ms. Lorena Gega, a Finance graduate of the University of Tirana.

This award will encourage prospective students to develop advanced studies related to monetary economics, financial stability and/or European integration issues, which are of a great interest for the Bank of Albania.

On 30 November – 1 December 2006, the Bank of Albania, in co-operation with the German Institute for Economic Research (IFO) and the German Association for Technical Co-operation in Tirana (GTZ), organized a two-day technical seminar on the development and implementation of business and consumer confidence indices. Participants in this seminar were also representatives from the Central Banking Authority of Kosovo, National Bank of the Republic of Macedonia, Central Bank of Montenegro and the National Bank of Serbia, as well as representatives of the Ministry of Finance,
Ministry of Economy and the INSTAT. Unlike the preceding seminar held in July of the same year, this activity treated the development of these indices from the regional viewpoint.

On 7-8 December 2006, the Bank of Albania organized the Round Table on Inflation Targeting 2. This activity was a confrontation of thoughts and opinions of both national and international experts regarding the future of monetary policy in Albania, with a special focus on the adoption of a fully fledged inflation targeting regime. This Round Table was a follow-up of the Open Forum, organized last year in December, which identified the preconditions to be met before the Bank of Albania can put a fully fledged inflation targeting regime into place.

On 11 December 2006, the parliament of the Republic of Albania approved the Decision No. 67 “On the appointment of two new members to the Supervisory Council of the Bank of Albania”. Based on this decision, Mr. Arjan Kadare and Mr. Halit Xhafa are the two new members of the Supervisory Council of the Bank of Albania.

On 18 December 2006, the Parliament of the Republic of Albania passed the Law No. 9662 “On banks in the Republic of Albania”, formulated by the Bank of Albania. The new banking law aims at harmonizing the Albanian banking legislation with the European Union Directives following the signing of the Stabilization and Association Agreement. The new law has considered all the suggestions provided by the International Monetary Fund and by the Albanian Association of Banks. The amendments made to the current law provide the expansion and improvement in some areas of banking activity, such as supervision, licensing of banks and foreign banks branches, the organization and management of domestic and foreign banks, as well as risk management. The passing of this law is expected to pave the way for the establishment of Credit Registry within the Bank of Albania, which aims to assist banks in minimizing credit risk.
LEGAL EVENTS OVER OCTOBER-DECEMBER 2006

INFORMATION SECURITY

On 25 October 2006, the Supervisory Council of the Bank of Albania approved the Decision No. 78 “On information security policy”. Information security policy aims to protect the Bank of Albania from deliberate or non-deliberate unauthorized access to the Bank’s information, which may infringe its activity and reputation.

MONETARY OPERATIONS

On 11 October 2006, the Supervisory Council of the Bank of Albania approved upon Decision No. 75 the Regulation “On the Bank of Albania intervention procedures in the domestic foreign currency market”. The new regulation aims to be in full compliance with the international standards and harmonized with the entire regulative basis of the banking system and the Bank of Albania.

On 13 December 2006, the Supervisory Council of the Bank of Albania approved upon Decision No. 93 the Regulation “On repurchase and reverse repurchase agreements”. This regulation details the rules and procedures of the Bank of Albania intervention in the money market through repurchase and reverse repurchase agreements. The intervention in the money market through these agreements aims to manage the banking system liquidity in the short-term in order to stabilize the market interest rates.

On 27 December 2006, the Supervisory Council of the Bank of Albania approved upon Decision No. 99 the Regulation “On the calculation of fixed interest rates in the money interbank market”. The purpose of this regulation is to define the way of calculating the fixed interest rates of deposits held with the interbank market, which are used by the Bank of Albania and the interested parties for reference, statistical, estimating and accounting purposes.

TRANSPARENCY AND CONFIDENTIALITY

On 11 October 2006, the Supervisory Council of the Bank of Albania approved upon Decision No. 74 an amendment to the Regulation “On the Bank of Albania transparency and confidentiality”. According to this amendment, the criteria and the way of using the information classified by the entities as “a banking secret”, which based on the law “On the Bank of
Albania” enjoy the right to control the accounts and records of the Bank of Albania are defined in the Instruction “On the rules of using and classifying the non-public information at the Bank of Albania” and they are in line with the International Audit Standards.

BANKING SUPERVISION

On 25 October 2006, the Supervisory Council of the Bank of Albania approved the Decision No. 79 “On the approval of the direct holding transfer at 71.79 per cent of the shareholder’s capital of Emporiki Bank Albania sh.a., to Credit Agricol sh.a., France.

On 25 October 2006, the Supervisory Council of the Bank of Albania approved upon Decision No. 80 some amendments to the Regulation “On the granting of licence to conduct banking activity in the Republic of Albania”. The purpose of this amendment is to regulate the cases when there is a change in the bank’s indirect shareholder of more than 10 per cent of its shareholder’s capital. Both in the case of the direct or indirect shareholder change, the bank is obliged to require a preliminary approval from the Bank of Albania. This decision also provides the requirements for the necessary documentation and the way of handling such a case by the Bank of Albania.

On 27 December 2006, the Supervisory Council of the Bank of Albania approved upon Decision No. 101 some amendments to the Regulation “On administering credit risk”, approved upon Decision No. 52, date 14 July 2004. The approved amendments aim to preserve the quality of credit portfolio under its relatively rapid growth rates.

ACCOUNTING AND PAYMENTS

On 15 November 2006, the Supervisory Council of the Bank of Albania approved upon Decision No. 82 the Regulation “On the inventory of material and monetary assets at the Bank of Albania”. The purpose of this regulation is to define the way of organization and conduct of the material and monetary assets at the Bank of Albania, as well as the compensation and adjustment of differences resulting from the inventory.

On 15 November 2006, the Supervisory Council of the Bank of Albania approved upon Decision No. 83 the Regulation “On the organization of cheque clearing in ALL at the Bank of Albania”. The purpose of this regulation is to define clearly and accurately the rules and procedures the commercial banks should pursue in the process of cheque clearing. The AECh system for small value payments required the regulative review of this area, which was previously provided by the regulation “On the organization of the clearing at the Bank of Albania”.

On 15 November 2006, the Supervisory Council of the Bank of Albania approved upon Decision No. 103 some amendments to the Regulation “On
special terms of the activity conducted by the Bank of Albania”, approved upon Decision No. 17, date 26 February 2003. According to this amendment, the Government holds with the Bank of Albania accounts in foreign currency related to various projects financed by international financial bodies, as well as foreign currency accounts for all the payments and liabilities deriving from the activity of the Albanian State.

**MONETARY POLICY**

On 30 November 2006, the Supervisory Council of the Bank of Albania approved the Decision No. 88 “On the increase of the interest rate of repurchase and reverse repurchase agreements from the Bank of Albania”. Following this increase, the interest rate of repurchase and reverse repurchase agreements increases from 5.25 per cent to 5.50 per cent.

**ISSUE**

On 13 December 2006, the Supervisory Council of the Bank of Albania approved the Decision No. 95 “Some configuration characteristics of the Albanian banknote of 2000 lekë face value, having a legal tender”. This decision defines the theme of this banknote, the respective printing year and its size and measures.

**ECONOMIC POLICY**

On 4 October 2006, the Council of Ministers approved in principle upon Decision No. 660 “The guarantee agreement, between the Council of Ministers of the Republic of Albania and the European Bank for Reconstruction and Development (EBRD), which relates to the loan agreement between the Albanian Electro-energy Corporation (KESH) and the European Bank for Reconstruction and Development (EBRD), under the framework of the South-Eastern Europe Energy Community program”. KESH will be extended a loan of EUR 16.000.000, according to the terms and conditions defined in this agreement.

On 16 October 2006, the Parliament of the Republic of Albania approved upon Law No. 9618 “The agreement between the Council of Ministers of the Republic of Albania and Haci Sakir Sabun and Gliserin Fabrikalari Turk Anonim Sirketi, Istanbul, Turkey, for the reschedule of debt”. The Government will pay USD 711 450 thousand to this company, upon the entry into force of this agreement.

On 16 October 2006, the Parliament of the Republic of Albania passed the Law No. 9621 “On the factual state budget of 2005”.

On 30 October 2006, the Parliament of the Republic of Albania passed the Law No. 9630 “On the factoring”. The scope of factoring contract are the
existing and/or future loans of client account, which have derived and/or will derive from the sale of goods and/or services from the supplier to the client.

On 30 October 2006, the Parliament of the Republic of Albania passed the Law No. 9632 “On local tax system”. This legal act details the rules on the way of exercising the rights and duties of local governing bodies for the establishment of local taxes, their collection and administration.

On 9 November 2006, the Parliament of the Republic of Albania passed the Law No. 9640 “On the chambers of trade and industry”. The purpose of this law is to define the rules on the organization, functioning and the activity of the Chambers of Trade and Industry and of the Union of Trade Chambers.

On 22 November 2006, the Council of Ministers approved the Decision No. 783 “On the establishment of accounting standards and rules”. These standards are mandatory for all entities defined in Article 2 of the amended Law No. 9228, date 29 April 2004 “On the accounting and financial statements”.

On 11 December 2006, the Parliament of the Republic of Albania approved upon Law No. 9653 “The financial agreement between the Council of Ministers of the Republic of Albania, represented by the Ministry of Finance, and Artigiancassa SPA, for the financing of rehabilitation project of Shkoder-Hani i Hotit road”. In accomplishing this project, the Italian Government extends to Albania through Artigiancassa a soft loan of about EUR 21 million for a 39-year period.

On 11 December 2006, the Parliament of the Republic of Albania approved upon Law No. 9654 “The financial agreement between the Council of Ministers of the Republic of Albania, represented by the Ministry of Finance, and Artigiancassa SPA, for the financing of the rehabilitation programme of Vlora Harbour”. In accomplishing this programme, the Italian Government extends to Albania through Artigiancassa a soft loan of about EUR 15 million for a 39-year period.
BANK OF ALBANIA MANAGEMENT
31 DECEMBER 2006

SUPERVISORY COUNCIL

<table>
<thead>
<tr>
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<tr>
<td>ARDIAN FULLANI</td>
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<tr>
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GOVERNOR

ARDIAN FULLANI

GOVERNOR’S OFFICE

GENC MAMANI

DEPUTY GOVERNORS

FATOS IBRAHIMI       First Deputy Governor

GENERAL INSPECTOR

TEUTA BALETA

DEPARTMENTS AND OTHER UNITS

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<td>RESEARCH DEPARTMENT</td>
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BRANCHES

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<td>LUSHINJA</td>
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* Up to November 15, 2006.
LIST OF ALL ENTITIES LICENSED BY THE BANK OF ALBANIA*

BANKS AND BRANCHES OF FOREIGN BANKS

1. ITALIAN - ALBANIAN BANK (JOINT-STOCK COMPANY)
License No. 1/1996, dated 17.07.1998
Certificate No. 1 “On Deposit Insurance”.
Director: Luigi MASTRAPASQUA
Address: Rruga “Barrikadave”, Nr. 70, Tirana, Albania
Tel.: 23 39 65, 23 56 97, 23 56 98, 22 62 62
Fax.: 23 30 34

2. RAFFEISEN BANK (JOINT-STOCK COMPANY)
License No. 2/1998, dated 11.01.1999
Certificate No. 2 “On Deposit Insurance”.
Director: Steven GRUNERUD
Address: Bulevardi “Bajram Curri”, European Trade Center, Tirana, Albania
Tel.: 22 66 99, 22 45 40, 22 26 69, 22 54 16
Fax.: 27 55 99, 22 35 87, 22 36 95, 22 40 51

3. UNITED BANK OF ALBANIA (JOINT-STOCK COMPANY)
License No. 3/1998, dated 11.01.1999
Certificate No. 3 “On Deposit Insurance”.
Director: Abdul Waheed ALAVI
Address: Bulevardi “Dëshmorët e Kombit”, Nr. 8, Tirana, Albania
Tel.: 22 84 60, 22 38 73, 22 74 08
Fax: 22 84 60, 22 83 87

4. ITALIAN BANK OF DEVELOPMENT (BANCA ITALIANA DI SVILUPPO) (FORMER DARDANIA BANK)
License No. 5/1998, dated 11.01.1999
Director: Libero CATALANO
Address: Bulevardi “Dëshmorët e Kombit”, Ndërtesa Kullat Binjake, Tirana
Tel.: 28 03 51 / 2 / 3 / 4 / 5.
Fax: 28 03 56.

5. NATIONAL COMMERCIAL BANK (JOINT-STOCK COMPANY)
License No. 6/1998, dated 11.01.1999
Certificate No. 5 “On Deposit Insurance”.
Director: Seyhan PENCAPLIGIL
Address: Bulevardi “Zhan D’Ark”, Tirana, Albania
Tel.: 25 09 55
Fax.: 25 09 56

* Up to December 31, 2006.
6. TIRANA BANK (JOINT-STOCK COMPANY)
License No. 07, dated 12.09.1996
Certificate No. 6 “On Deposit Insurance”.
Director: Dimitrios FRANGETIS
Address: Bulevardi “Zogu I”, Nr. 55/1, Tirana, Albania
Tel.: 23 34 41/42/43/44/45/46/47
Fax.: 23 34 17

7. NATIONAL BANK OF GREECE – TIRANA BRANCH (JOINT-STOCK COMPANY)
License 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: Spiro BRUMBULLI
Address: Rruga “Durrësit”, Godina Comfort, Tirana, Albania
Tel.: 23 36 23/24
Fax.: 23 36 13

8. INTERNATIONAL COMMERCIAL BANK (JOINT-STOCK COMPANY)
License 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.: 25 43 72 / 25 62 54
Tel/Fax: 25 43 68

9. ALPHA BANK – TIRANA BRANCH (JOINT-STOCK COMPANY)
License No.10, dated 07.01.1998
Certificate No. 9 “On Deposit Insurance”.
Director: Andreas GALATOULAS
Address: Bulevardi “Zogu I”, Nr.47, Tirana, Albania
Tel.: 23 33 59, 24 04 76/77/78
Tel/Fax: 23 21 02

10. AMERICAN BANK OF ALBANIA (JOINT-STOCK COMPANY)
License No.11, dated 10.08.1998
Certificate No. 10 “On Deposit Insurance”.
Director: Lorenzo RONCARI
Address: Rruga “Ismail Qemali”, Nr. 27, P.O. Box 8319, Tirana, Albania
Tel.: 27 60 00 / 24 87 53 / 4 / 5 / 6
Tel/Fax: 24 87 62

11. PROCREDIT BANK (JOINT-STOCK COMPANY)
License No. 12, dated 15.03.1999
Approved by the Supervisory Council Decision of the Bank of Albania No. 22, dated 03.03.1999.
Certificate No. 11 “On Deposit Insurance”.
Director: Frieder WOEHRMANN
Address: Rruga “Sami Frashëri”, Tirana e Re, P.O. Box. 2395, Tirana, Albania
Tel.: 23 04 99, 23 34 96
Tel/Fax: 27 12 76

12. FIRST INVESTMENT BANK - TIRANA BRANCH (JOINT-STOCK COMPANY)
License No. 13, dated 16.04.1999
Certificate No. 12 “On Deposit Insurance”.
Director: Martin Isvetkov BOGDANOV
Address: Bulevardi “Zogu I”, Nr. 64, Tirana, Albania
Tel.: 25 64 23, 3 564 24
Tel/Fax: 25 64 22

13. EMPORIKI BANK OF ALBANIA (JOINT-STOCK COMPANY)
License No. 14, dated 28.10.1999
Certificate No. 13 “On Deposit Insurance”.
Director: George CARACOSTAS
Address: Rruga “Kavajës”, Tirana Tower, Tirana, Albania
Tel.: 35 87 55/ 56/ 57/ 58/ 59/ 60
Tel/Fax: 35 87 52

14. CREDIT BANK OF ALBANIA (JOINT-STOCK COMPANY)
License No. 15, dated 28.08.2002
Certificate No. 14 “On Deposit Insurance”.
Director: Kamal Abdel MONEIM
Address: Rruga “Perlat Rexhepi”, Al-Kharafi Group Administration Building, Kati 1&2” Tirana, Albania
Tel.: 27 21 68, 27 21 62
Tel/Fax: 27 21 62

15. “CREDINS” BANK (JOINT-STOCK COMPANY)
License No. 16, dated 28.03.2003
Certificate No. 15 “On Deposit Insurance”.
Director: Artan SANTO
Address: Rruga “Ismail Qemali”, Nr. 21, Tirana, Albania
Tel.: 22 29 16, 23 40 96

16. POPULAR BANK (JOINT-STOCK COMPANY)
License No. 17, dated 16.02.2004
Certificate No. 16 “On Deposit Insurance”.
Director: Edvin LIBOHova
Address: Rruga “Donika Kastrioti”, Pall. 11/1, Kati I, Tirana, Albania
Tel.: 27 27 88 / 89 / 90 / 91
Fax: 27 27 81

17. UNION BANK (JOINT-STOCK COMPANY) TIRANA
License No. 18, dated 09.01.2006
Certificate No. 17 “On Deposit Insurance”.
Director: Gazmend KADRIU
Tel: 25 06 53
Fax: 25 06 54
NON-BANK INSTITUTIONS

1. TIRANA FINANCIAL UNION S.R.L (WESTERN UNION)
License No. 1, dated 08.12.1999, on conducting the following financial activities:
- offering payment services;
- mediating in the conduct of monetary transactions;
- acting as financial agent or advisor.
Director: Niko Leka, Edmond Leka
Address: Rruga “Reshit Çollaku”, Pallati Shalëvare, Sh 2, Nr. 18, Tirana, Albania
Tel.: 25 06 53
Fax: 25 06 54

2. DINERS CLUB ALBANIA S.R.L.
License No. 2, dated 09.10.2000, on conducting the following financial activity:
- mediating in the conduct of monetary transactions.
Director: Eni Koço
Address: Bulevardi “Zogu I”, VEVE Business Center, Tirana, Albania

3. ALBANIAN POST-OFFICE (JOINT STOCK COMPANY)
License No. 3, dated 18.04.2001, as a non-bank financial institution to conduct the following financial activities:
- offering payment services;
- acting as financial agent or advisor.
Director: Arqile Goreja
Address: Rruga “Reshit Çollaku”, Nr. 4, Tirana, Albania
Tel.: 22 23 15

4. CREDINS TIRANA (JOINT STOCK COMPANY)
License No. 04, dated 13.06.2001, as a non-bank financial institution to conduct the following financial activities:
- granting credit;
- offering payment services;
- mediating in the conduct of monetary transactions (foreign currency included);
- offering guarantees;
- acting as financial agent or advisor (excluding herein the services set forth in point 3/a and 3/b of Article 26 of the Law “On Banking Law in the Republic of Albania”.
Director: Migena Roshaj
Address: Rruga “Ismail Qemali” Nr. 21, Tirana, Albania
Tel.: 22 29 16, 23 40 96

5. MOUNTAINOUS AREA FINANCING FUND
License No. 5, dated 29. 03.2002, on conducting the following activity:
- granting credit.
Director: Bajram Korsita
Address: Rruga “Dervish Hima” Nr. 4, Tirana, Albania
Tel.: 25 90 80/1
Fax: 25 06 33

6. “AK-INVEST” (JOINT STOCK COMPANY)
License No.7, dated 31.12.2003, as a non-bank financial institution to conduct the following activities:
- offering payment services;
- mediating in the conduct of monetary transactions (foreign currency included);
- acting as financial agent or advisor.
Manager: Ilir Adili
Address: Rruga “Ded Gjon Luli”, Nr. 2/3, Tirana, Albania
Tel.: 24 01 47
FOREIGN EXCHANGE BUREAUS

1. “JOARD” FOREIGN EXCHANGE BUREAU S.R.L., TIRANA
License: No. 1, dated 01.10.1999
Address: Rruga “Ded Gjon Luli”, Nr.2, Tirana, Albania
Brokers: Josif Kote, Pajtim Kodra

2. “AMA” FOREIGN EXCHANGE BUREAU S.R.L., DURRËS
License: No. 2, dated 01.10.1999
Address: Rruga “Tregtare”, Lagja 3, Durrës, Albania
Brokers: Mirlinda Ceka, Ilir Hoxha

3. “ARIS” FOREIGN EXCHANGE BUREAU S.R.L., TIRANA
License: No. 3, dated 01.10.1999
Address: Rruga “Luigj Gurakuqi”, Tirana, Albania
Brokers: Ardian Goci, Ismet Noka

4. “UNIONI FINANCIAR” FOREIGN EXCHANGE BUREAU S.R.L., TIRANA
License: No. 4, dated 01.10.1999
Address: Rruga “Reshit Çollaku”, Pallati Shallvare, Shk. 2/18, Tirana, Albania
Manager: Niko Leka
Brokers: Arjan Lezha (Manager), Albert Sara, Dhimitër Papadhopolli, Genta Angjeli (Agalliu), Piro Teti, Flora Simixhi, Petrika Mano (Manager), Lindita Shala, Mirela Bakalli, Anila Demiri, Emili Bakalli (Nako), Astrit Sferdelli, Mirela Kaiku, Erisa Emiri

5. “AGLI” FOREIGN EXCHANGE BUREAU S.R.L., TIRANA
License: No. 5, dated 01.10.1999
Address: Agency No.1: Rruga “Islam Alla”, Nr.1, Tirana, Albania
Agency No.2: Rruga “Kavajës”, Tirana, Albania
Brokers: Kujtim Nina (Manager), Agim Cani, Selim Luli

6. “EXCHANGE” FOREIGN EXCHANGE BUREAU S.R.L., TIRANA
License: No. 08, dated 24.11.1999
Address: Agency No.1: Rruga “Durrësit”, Nr. 170, Tirana, Albania
Brokers: Ivan Pavlovski, Ervis Myftari

7. “UNISIX” FOREIGN EXCHANGE BUREAU S.R.L., KORÇA
License: No. 09, dated 26.11.1999
Address: Bulevardi “Republika”, Pallati 4, Korça, Albania
Brokers: Pandi Cunoti, Ernest Golka, Nikolin Bicka, Eli Bode

8. “EKSPRES J & E” FOREIGN EXCHANGE BUREAU S.R.L., DURRËS
License: No. 10, dated 26.11.1999
Address: Lagja 11, Rruga “Prokop Meksi”, Durrës, Albania
Brokers: Kostandin Ekonomi, Entela Ekonomi

License: No. 12, dated 25.02.2000
Address: Sheshi “Skënderbej”, Teatri i Kukullave, Tirana, Albania
Brokers: Edmond Ymeri, Ali Topalli, Ilir Janku

10. “SERXHIO” FOREIGN EXCHANGE BUREAU S.R.L., ELBASAN
License: No. 14, dated 07.04.2000
Address: Lagja “Luigj Gurakuqi”, Rruga “11 Nëntori”, Pallati 70, Nr.14, Elbasan, Albania
Brokers: Amarildo Canoku

11. “ALBTUR” FOREIGN EXCHANGE BUREAU S.R.L., TIRANA
License: No. 15, dated 07.04.2000
Address: Bulevardi "Zogu I", Pallati 32, Shk.1, Tirana, Albania
Brokers: Albert Rahmani, Artur Rahmani

12. “R & M” FOREIGN EXCHANGE BUREAU S.R.L., TIRANA
License: No. 16, dated 22.05.2000
Address: Rruga “Punëtorët e Rilindjes”, Pallati 182, Tirana, Albania
Brokers: Edmond Stepa, Miranda Stepa

License: No. 18, dated 11.06.2000
Address: Lagja 4, Rruga “9 Maji”, Durrës, Albania
Broker: Shpëtim Hysa

License: No. 19, dated 24.11.2000
Address: Lagja “Popullore”, Shijak, Albania
Brokers: Nazmi Ademi, Farije Ademi

15. “MANUSHI” FOREIGN EXCHANGE BUREAU S.R.L., TIRANA
License: No. 22, dated 18.04.2001
Address: Bulevardi “Zogu I”, VEVE Business Center, Tirana, Albania
Brokers: Roland Manushi

16. “UNIONI SELVIA” FOREIGN EXCHANGE BUREAU S.R.L., TIRANA
License: No. 23, dated 21.05.2001
Address: Rruga “Sami Frashëri”, Pallati 11, Shk.4, Ap.29, Tirana, Albania
Brokers: Denis Merepeza (manager)

17. “KALENJA” FOREIGN EXCHANGE BUREAU S.R.L., TIRANA
License: No. 24, dated 29.06.2001
Address: Rruga “Kavajës” (next to Turkish Embassy), Tirana, Albania
Brokers: Haim Shametaj, Fatmir Shametaj

18. “TILBA” FOREIGN EXCHANGE BUREAU S.R.L., ELBASAN
License: No. 25, dated 30.09.2001
Address: Lagja “Luigj Gurakuqi”, Bulevardi “Qemal Stafa”, Njësia Nr.12, Elbasan, Albania
Brokers: Kristaq Bako, Vjolca Bako

License: No. 26, dated 31.10.2001
Brokers: Jani Anagnosti, Odise Anagnosti, Edlira Anagnosti
Agency No. 2 - Rruga “Kajo Karafili”, Nr. 11, Tirana, Albania
Broker: Fredi Cami

20. “KO-GO” FOREIGN EXCHANGE BUREAU S.R.L., TIRANA
License: No. 27, dated 12.11.2001
Brokers: Mihal Konomi, Përparim Goxhaj

License: No. 28, dated 22.11.2001
Address: Agency No. 1: Rruga “Abdył Frashëri”, Nr.3, Tirana, Albania
Brokers: Mirel Topçiu
Broker: Melis Çami

License: No. 29, dated 22.11.2001
Address: Agency No.1: Rruga “Muhamet Gjollesha”, Tirana, Albania
23. “EXCHANGECLOG” FOREIGN EXCHANGE BUREAU S.R.L., TIRANA
License: No. 31, dated 22.11.2001
Address: Rruga “Mine Peza”, Tirana, Albania
Brokers: Almida Sterio, Fatmir Tafaj, Eduard Andoni, Elida Hasamemi

License: No. 35, dated 12.12.2001
Address: Rruga “Kavajës”, Tirana, Albania
Brokers: Bashkim Shametaj, Luan Shametaj, Ilir Mesini

License: No. 36, dated 14.12.2001
Address: Lagja “Kongresi i Elbasanit”, Bulevardi “Qemal Stafa”, Pallati 9-katësh, Elbasan, Albania
Brokers: Arben Kovaçi, Besnik Lulja, Alfred Kapxhi

License: No. 42, dated 18.01.2002
Address: Rruga “Dibrës”, Nr.105/1, Tirana, Albania
Brokers: Kosta Papa, Arben Memko, Lorenc Konomi, Thoma Konomi, Aleko Plaku

27. “FORMAT” FOREIGN EXCHANGE BUREAU S.R.L., TIRANA
License: No. 43, dated 21.01.2002
Address: Rruga “Durrësit”, Pallati 85, Shk. 1, Ap. 1, Tirana, Albania
Brokers: Diana Lemi, Egon Sinani

License: No. 44, dated 05.02.2002
Address: Lagja “29 Nëntori”, Elbasan, Albania
Brokers: Fahri Sanco, Ismail Bejta

License: No. 46, dated 15.02.2002
Address: Rruga “Myslym Shyri”, Nr. 25, Tirana, Albania
Brokers: Belul Lleshi, Vladimir Avda, Mimoza Avda

30. “MARIO” FOREIGN EXCHANGE BUREAU S.R.L., SARANDA
License: No. 47, dated 14.03.2002
Address: Lagja 1, Saranda, Albania
Brokers: Vangel Gramozi, Blerim Dhima

31. “DROGU” FOREIGN EXCHANGE BUREAU S.R.L., TIRANA
License: No. 49, dated 23.04.2002
Address: Rruga “Vaso Pasha”, Kulla 1, Kati I, Tirana, Albania
Brokers: Shkelqim Drogu, Kostandin Koteci

32. “HYSEN-C” FOREIGN EXCHANGE BUREAU S.R.L., LAÇ
License: No. 50, dated 23.04.2002
Address: Lagja Nr. 3, Laç, Albania
Broker: Cen Hyseni

33. “UNIONI FIER” FOREIGN EXCHANGE BUREAU S.R.L., FIER
License: No. 51, dated 08.05.2002
Address: Lagja “15 Tetori”, Rruga “Kastriot Muça”, Fier, Albania
Brokers: Gjergj Dulaj (manager)
34. "TAXI EKSPRES" FOREIGN EXCHANGE BUREAU S.R.L., ELBASAN
License: No. 52, dated 20.05.2002
Address: Agency No.1: Rruga “Sami Frashëri”, nr. 11 (pranë shkollës “Edith Durhan”, Tirana, Albania
Agency No.2: Bulevardi “Bajram Curri”, Rruga “Lekë Dukagjini”, No.5, Tirana, Albania
Brokers: Arben Sharra, Sokol Kaleci

35. “GLEAR” FOREIGN EXCHANGE BUREAU S.R.L., SHIJAK
License: No. 55, dated 23.07.2002
Address: Lagja “Kodër”, Shijak, Durrës, Albania
Brokers: Argjend Calliku, Afërdita Calliku

36. “ALBA-POST” FOREIGN EXCHANGE BUREAU, TIRANA
License: No. 56, dated 28.08.2002
Address: Rruga “Reshit Çollaku”, Nr. 4, Tirana, Albania

37. “UNIONI BALLSH” FOREIGN EXCHANGE BUREAU S.R.L., BALLSH
License: No. 57, dated 11.09.2002
Address: Rruga “8 Nëntori”, Ballsh, Albania
Brokers: Luan Zenelaj, Lavdimir Zenelaj

38. “ESLULI” FOREIGN EXCHANGE BUREAU S.R.L, TIRANA
License: No. 58, dated 17.10.2002.
Address: Rruga “Reshit Çollaku”, Pallati “Shallvare”, Shk. 4/1, Tirana, Albania
Brokers: Maksim Çeku

License: No. 61, dated 02.06.2003
Address: Rruga “Myslym Shyri”, Pallati 60, Ap. 3, Tirana, Albania
Broker: Ylli Ndoci (manager)

40. “YLDON” FOREIGN EXCHANGE BUREAU S.R.L., TIRANA
License: No. 62, dated 03.06.2003
Address: Rruga “Qemal Stafa”, Pallati 382/2/2, Tirana, Albania
Broker: Ylli Ndoci (manager)

41. “BILLI” FOREIGN EXCHANGE BUREAU S.R.L., TIRANA
License: No. 63, dated 16.02.2004
Address: Sheshi “Wilson”, Tirana e Re, Tirana, Albania
Broker: Sybi Cenolli (manager)

42. “I.S.N.” FOREIGN EXCHANGE BUREAU S.R.L., TIRANA
License: No. 66, dated 06.05.2004
Address: Rruga “Kavajës”, Pallati 3, Kati I, Tirana, Albania
Brokers: Evzi Zemzadja (manager), Nexhmi Uka, Slandri Brojaj

43. “ARIABA” FOREIGN EXCHANGE BUREAU S.R.L., TIRANA
License: No. 67, dated 07.06.2004
Address: Rruga “Abdyl Frashëri”, Kati I, Shk. 5, Tirana, Albania
Brokers: Agim Xhemo (manager), Astrit Hado

44. “ALBACREDITS” FOREIGN EXCHANGE BUREAU S.R.L., TIRANA
License: No. 68, dated 13.07.2004
Address: Rruga “Ded Gjon Luli”, Nr. 5, Tirana, Albania
Brokers: Ermiq Skënderi (manager), Engjëll Skënderi, Burhan Kodra, Shqiponja Spahiu

45. “ALB-KREDIT” FOREIGN EXCHANGE BUREAU S.R.L., TIRANA
License: No.69, dated 19.07.2004
Address: Agency No.1: Rruga “Durrësit”, Nr. 2, Tirana, Albania
Brokers: Arben Cani (manager), Vasil Marto, Rudina Muskaj, Valbona
46. “OMEGA” FOREIGN EXCHANGE BUREAU S.R.L., TIRANA
Address: Rruga “Abdyl Frashëri”, Pallati 1, Shk.2, Ap.10, Tirana
Broker: Mihallaq Peko (manager)

47. “ELBA 2005” FOREIGN EXCHANGE BUREAU S.R.L., TIRANA
License: No.73, dated 28.04.2005
Address: Bulevardi “Bajram Curri”, Pallatet Agimi, Nr.16, Tirana
Brokers: Kujtim Elbasani (manager)

48. “JONADA – 05” FOREIGN EXCHANGE BUREAU S.R.L., TIRANA
License: No. 74, dated 27.06.2005
Address: Rruga “Kavajës”, Pallati 185, Shkalla 2, Ap. 9, Tirana, Albania
Brokers: Liliana Zyfi (manager), Pëllumb Zyfi

49. “BASHA – N.B.” FOREIGN EXCHANGE BUREAU S.R.L., ELBASAN
License: No. 75, dated 08.07.2005
Address: Lagja “Shënkoll”, rruga “Thoma Kaleshi”, Pallati 110, Shk.1, Kati I, Elbasan, Albania
Brokers: Nashifer Basha, Çlirim Basha, Sonila Alla

License: No.77, dated 09.09.2005
Address: Lagja “Besëlidhja”, Pallati 73, Lezhë, Albania
Brokers: Ilir Malaj

51. “EUROTOURS” FOREIGN EXCHANGE BUREAU S.R.L., TIRANA
License: No.78, dated 17.10.2005
Address: Rruga “Reshit Çollaku”, Nr. 2/18, Pallatet Shallvare, Tirana, Albania
Brokers: Albert Cara, Ilir Stafa.

52. “A.B.I.” FOREIGN EXCHANGE BUREAU S.R.L., TIRANA
License: No.79, dated 17.02.2006
Address: Bulevardi Zog I, Godina “Zëri i Popullit”, Tirana, Albania
Brokers: Ilir Doçi, Suela Dedaj

53. “REGENCY INTERNATIONAL CASINO TIRANA” FOREIGN EXCHANGE BUREAU S.R.L., TIRANA
License: No.80, dated 06.03.2006
Address: Rruga “Dëshmorët e 4 Shkurtit”, Parku Rinia, Tirana, Albania

54. “ARBËR F” FOREIGN EXCHANGE BUREAU S.R.L., TIRANA
License: No.81, dated 07.03.2006
Address: Rruga “Kavajës”, Pallati 3, Kati I (ish-Guden), Tirana, Albania
Brokers: Florina Jaho, Bukurosh Jaho

55. “EURO 2006” FOREIGN EXCHANGE BUREAU S.R.L., DURRËS
License: No.82, dated 12.04.2006
Address: Lagija nr.4, Rruga “Migjeni”, pranë Poliklinikës Qendrore, Durrës, Albania
Brokers: Hysni Baganaçi, Medi Dymishi

56. “VOSKOP” FOREIGN EXCHANGE BUREAU S.R.L., KORÇA
License: No.83, dated 13.04.2006  
Address: Lagjja nr.7, Blloku “8 Nëntor”, Korça, Albania  
Brokers: Anesti Leska, Rexhep Mankolli

57. “KRISTIAN 2002” FOREIGN EXCHANGE BUREAU S.R.L., LEZHA  
License: No.84, dated 31.05.2006  
Address: Lagjia “Besëlidhja”, përballë Degës së bankës “Raiffeisen”, Lezha, Albania  
Brokers: Sander Marashi

58. “PRE-LAND” FOREIGN EXCHANGE BUREAU S.R.L., LEZHA  
License: No.85, dated 31.05.2006  
Address: Lagja “Skënderbej”, ish-lokali “Gjahtari”, Lezha, Albania  
Brokers: Roland Kola

59. “SHQIPONJA VL” FOREIGN EXCHANGE BUREAU S.R.L., VLORA  
License: No.86, dated 16.06.2006  
Address: Pallati i Kulturës “Labëria”, përballë portit detar, Vlora, Albania  
Brokers: Vjetolca Musaraj

60. “BONVOYAGE” FOREIGN EXCHANGE BUREAU S.R.L., DURRËS  
License: No.87, dated 20.06.2006  
Address: Lagjja 11, Bulevardi kryesor “Durrahu”, Ap.243, Durrës, Albania  
Brokers: Petrit Shtara; Jusuf Milaqi
UNIONS OF SAVINGS AND CREDIT ASSOCIATIONS

1. “JEHONA” SAVINGS AND CREDIT ASSOCIATIONS UNION, TIRANA
License: No. 1, dated 27.06.2002
Address: Rruga “Kajo Karafili”, Nr. 26/1, Tirana, Albania
Head of the Executive Board: Vojsava Rama
This union consists of 41 savings & credit associations licensed also as special associations and technically assisted by the foundation “Movement for the savings & credit associations development”.

2. “ALBANIAN SAVINGS AND CREDIT UNION” SAVINGS AND CREDIT ASSOCIATIONS UNION, TIRANA
License: No. 2, dated 09.08.2002
Address: Rruga “Ismail Qemali”, Nr. 32, Tirana-Albania
Head of the Executive Board: Zana Konini
This union consists of 91 savings & credit associations, licensed also as special associations and technically assisted by “Mountain Area Financing Fund”.

REPRESENTATIVE OFFICES OF FOREIGN BANKS

THE REPRESENTATIVE OFFICE OF BANCA POPOLARE PUGLIESE IN ALBANIA
License: No. 01, dated 02.07.2003
Representative: Pasquale Guido Vergine
Address: Sheshi “Skënderbej”, Pallati i Kulturës, Kati III, Tirana, Albania
Tel.: 25 67 82