



**REPUBLIC OF ALBANIA**  
**BANK OF ALBANIA**



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## **PRESS RELEASE**

### **EXTERNAL SECTOR DEVELOPMENTS OF THE ALBANIAN ECONOMY DURING 2004**

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The overall balance of payments for 2004 resulted in an outstanding of USD 288 million. Net capital flows marked a record level of USD 531 million and they fully made possible the financing of current deficit, leading as well to the growth of foreign exchange reserve.

The main highlights in the external sector of the Albanian economy can be summarized as following:

- The reduction of current deficit, compared to the last year, either in absolute value or as a percentage of Gross Domestic Product (GDP).
- Stable growth of exports, in spite of the worsening situation of competitiveness (exchange rate developments).
- Improvement in the ratio of coverage of imports from exports.
- Inflows as foreign direct investments doubled.
- Increase of financial liabilities to non-residents, mainly due to the growth of foreign direct investments inflows and of private borrowing.
- Increase of domestic claims to non-residents, mainly appeared in the form of deposits' growth of resident units abroad.
- Increase of foreign reserves stock of the monetary authority and of adequacy coefficient of foreign reserves for imports of goods and services.

In estimating the results of this analysis, there should be taken into account the fact that an important part of the growth in transactions volume reflects the annual

depreciation rate (calculated over the average monthly exchange rate) of the reporting currency – US dollar against Euro (7.7 percent) and of domestic currency, Lek (15.7 percent) recorded in 2004. A huge number of transactions between residents and non-residents are performed in Euro<sup>1</sup> and not in the reporting currency of the balance of payments.

## I. Current account

The favorable economic situation of the country is partly reflected also in the field of foreign transactions. Current transactions are estimated at about USD 6.2 billion or 24 percent higher than the previous year. Current deficit is estimated at about USD 404 million or 0.6 percent lower than 2003 (in absolute value the reduction of current deficit is estimated USD 2.5 million), equal to 5.3 of GDP from 7.1 percent in 2003. The improvement of current deficit position is due to the increase of transfers without remuneration and to the reduction of deficit in services, and to the fluctuations noted in US dollar exchange against both Euro and Lek. Meanwhile, trade deficit in goods deepened and net investment incomes reduced.

Despite the growth of transactions volume that characterized the developments in exchange of goods and services, throughout 2004, the indicator of Albania's economic openness showed a falling tendency<sup>2</sup>. Albania's economic openness for this year is estimated at 62 percent, from nearly 66 percent in 2003. Although Albania is considered as one of the most accelerated economies in the region during 2004, having an economic growth of 6 percent for the second year consecutively, the degree of economic openness still leaves much to be desired in comparison with other countries of the region.

### I. 1. Foreign trade

Trade transactions (imports plus exports) have represented during 2004 more than 45 percent of current services between Albania and the world. The general trade volume amounted to USD 2.8 billion, with an annual growth of USD 588 million or 25 percent compared to the previous year. The growth has been quicker for exports. Goods exports' income amounted to USD 603 million, being 35 percent (23 percent in Euro) higher than those of the previous year. Signs of the European economy (main trade partner of Albania) improvement, though being slow, as well as the efforts for structural reforms in the country, seem to give the first effects. In spite of competitiveness worsening (real exchange rate is estimated at 7.3 percent during this year compared to 4.5 percent of depreciation for the same period of 2003), goods export is characterized by a promising growth during the last two years. Exports contribution to GDP is estimated for this year at 7.9 percent, with an annual growth of 0.1 percentage points. The Albanian economy still remains an imports-oriented economy, which represented 78 percent of foreign trade volume. Goods

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<sup>1</sup> For instance, according to the General Customs Department estimates, around 57 percent of transactions for goods imports are performed in the European currency, Euro, 39 percent in US dollar and 4 percent in other currencies.

<sup>2</sup> Calculated as the ratio of trade volume in goods and services to GDP.

imports' expenses are estimated to be high, around USD 2.2 billion. The annual nominal growth of USD 411 million or 23 percent (12 percent in Euro) shows that even this year has followed the pronounced upward trend that characterized imports during 2000s. Growth of lending activity to the economy has helped in maintaining the purchasing power of Albanian citizens at relatively high levels.

The analysis of import structural dynamics highlights the continuous growth of capital goods imports, and that of raw material imports for the active processing industry in the country. Thus, annual imports growth, to a large extent (33 percent), is due to the high imports in machineries and equipments as well as in vehicles. The high demand of private sector for capital goods is a positive indicator for investments level, the renovation of technological base and of its productivity. The most advanced sectors in terms of technological base renovation are those of Information Technology and Communication and the construction industry.

Notwithstanding the positive developments that characterized goods export during this year, its structure continues to have a low degree of diversification. There is still no evidence of marketing strategies of the Albanian businesses towards foreign markets. Hence, goods export performance for this year is considerably determined by the changes in the processing industry of the country (ordered merchandise). Exports of this category performed about 75 percent of the annual income in exports of goods. Nevertheless, the growth of domestic exports with mainly regional markets is a promising one, stimulated by the free trade agreements in the region. Of an annual growth of around USD 48 million, the latter have increased the representative level in total exports to 25 percent, from 23 percent in the previous year.

In absolute value, imports growth is on an annual basis followed by a modest growth of exports. However, during the last two years exports growth has been more promising. The degree of coverage of imports from exports for this period reached 28 percent, from 25 percent in 2003.

Trade deficit of 2003 amounted to about USD 1.6 billion or 19 percent higher than the one of the previous year. Trade deficit position against GDP is estimated to have improved, to 21 percent, from 23.4 percent in the previous year. Imports came down to 2.3 percentage points against GDP, from 28.9 percent of GDP in the previous year. The reduction of domestic needs for electric energy, stimulated by the favorable weather conditions as well as the improvement of distribution network and the good administration of electric energy, followed by a prudential fiscal policy, might be the factors that were behind the improvement of net trade position in GDP.

## **I. 2. Developments of the other items of current account**

Net services export for 2004 was estimated at – 24 million USD, being rather lower than the one of -82.7 million USD, recorded at the end of 2003.

Services export continues to be dominated by the tourism activity. According to the estimations of the Bank of Albania, tourism has generated about USD 673 million as income in services or nearly 11 percent more than the goods export. In addition to

the impact of fluctuations in the exchange rate of the reporting currency - American dollar against Euro, in which Albania benefits mostly the exports income from the services provided for tourism<sup>3</sup>, the annual growth of tourism income is also affected by the volatility shown in the estimated indicators (increased number of foreigners and emigrants as well as a moderate increase of daily expenses).

Meanwhile, Albanians have expended in their travels abroad about USD 560 million or 58 percent of total remittances. Tourism income, compared to the previous year, increased more than the expenses of the same service category. At the end of the year, the positive balance of this category is estimated at USD 112 million, from 33 being in 2003.

Transport and insurance services follow the developments of the trade activity of goods. The growth of import volume brought about the growth of services import of these categories. Simultaneously, the ever-greater participation of the resident transportation companies that supply services in foreign trade has considerably increased the income of these categories. However, deficits of transport and insurance services, by the end of the year, are estimated to have increased compared to the previous year, at 21 and 9 percent, respectively.

“Other services” category has recorded a deficit of USD 11 million, remaining to almost the same deficit level as the previous year. The current deficit is mainly due to the increase of the deficit of Government expenses and of the deficit in cultural activities and business categories. Meanwhile, income being generated from telecommunication services increased significantly, a category that is closed in a positive balance sheet of USD 574 million, from 27 being recorded during the previous year.

Positive balance of income, by the end of year, is estimated at about USD 168 million. This surplus is attributed to the income deriving from seasonal and frontier workers. Net revenues of this category are estimated to be 12 percent higher than the previous year, being affected as well by the rising demand for labor force in the neighboring country, Greece, during the organization of the 2004 Olympic Games. The other part of income provided from investments, marked a decline, thus surplus of “income” category slightly reduced (1.3 percent) relative to the previous year.

Current transfers, like the previous years, have been shaped as a result of emigrants' remittances. The latter represent the main source for the financing of deficit in trade of goods and services, and during 2004 they are estimated at USD 972 million, being 25 percent higher than those of the previous year. However, considering the currencies in which these transfers are performed, we can say that even in this item the exchange rate effect is significant.

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<sup>3</sup> According to the estimations of the Balance of Payments Sector, 80 percent of foreign currency inflows are in Euro (including citizens coming from the European Union countries, from Kosovo and Monte Negro).

Emigrants' remittances (of USD 972 million) are followed by government transfers, mainly as technical assistance (of USD 46 million), which are estimated to decrease (at 9 percent).

## **II. Capital and financial account**

Capital movements, during 2004, recorded a net flow of about USD 531 million, totally making possible the financing of current deficit, and led to the growth of foreign reserve. Capital transfers marked USD 132 million or 25 million lower than the yearend of 2003, while the financial account is closed in a positive balance sheet of USD 399 million. This capital import, being performed for the major part through foreign investments and the extension of long-term and soft loans from abroad, gave rise to the growth of Albania's financial liabilities to the rest of the world, by about USD 588 million. This growth is estimated to be 70 percent higher than the one of the previous year.

Foreign direct investments, for year 2004, are estimated at USD 341 million. These capital inflows became a dominant factor on the increase of financial liabilities and on the developments of capital and financial transactions of the country. In 2004, they are mainly presented in the form of banking system privatization, with an inflow of 92 percent higher than the previous year.

Another important factor on the increase of financial liabilities has been the extension of long-term and soft loans from abroad. This includes also the use of loans and credits in the Fund estimated at USD 12 million. Foreign borrowing is used to a considerable extent (34 percent) from the private sector and is estimated 6 times higher than year 2003. Foreign debt services as payments of the principal, amounted to USD 48 million during the period.

Financial liabilities as non-residents' deposits in our banking system grew by about USD 3.4 million. Liabilities as trade loan grew by about USD 23 million, this being reflected in the growth of imports for this period.

Albania's financial claims to the rest of the world increased by USD 159 million or nearly 27 percent more than the previous year. Around 45 percent of this increase is performed during the third quarter, mainly due to deposits' growth of resident units abroad; this high inflow of deposits from inside outside is mainly due to both the conversion of "Raiffeisen" bank's capital and the shifting as investment – from portfolio investments to deposits. Thus, the rise of portfolio investments is estimated at about USD 3.6 million by the end of the year and that of deposits, at USD 90 million.

Net inflows of foreign currency assets as financial capital were reflected in the growth of foreign exchange reserve of the monetary authority, by about USD 348,6 million. The foreign reserve estimated at USD 1.374 by the end of 2004 remains at acceptable levels covering nearly 5.2 months of imports. Foreign reserves of the Bank of Albania are considerably affected by the impact of exchange rate. Foreign reserves, due to this impact, grew by about USD 54.8 million during 2004.

**Balance of Payments**  
in millions of USD

	1999	2000	2001	2002	2003	2004
<b>Current Account</b>	(132.9)	(163.1)	(217.9)	(420.8)	(406.7)	(404.2)
Merchandise: Exports, fob	275.1	255.4	304.6	330.2	447.2	603.3
Merchandise: Imports, fob	(937.9)	(1,076.4)	(1,331.6)	(1,485.4)	(1,783.5)	(2,194.9)
Trade Balance	(662.8)	(821.0)	(1,027.0)	(1,155.1)	(1,336.3)	(1,591.6)
Services: Credit	266.7	448.1	533.5	585.0	719.7	940.7
Services: Debit	(165.4)	(430.0)	(444.2)	(590.3)	(802.4)	(964.7)
Income: Credit	85.6	115.9	162.5	146.9	194.8	196.5
Income: Debit	(10.3)	(9.1)	(13.4)	(20.6)	(24.4)	(28.3)
Private Unrequired Transfers	188.4	438.6	542.6	575.0	781.7	977.8
Official Unrequired Transfers	165.0	94.4	28.1	38.2	60.3	65.4
<b>Capital Account</b>	67.5	78.2	117.8	121.2	157.0	132.3
<b>Financial Account</b>	36.8	182.5	97.0	201.6	190.9	386.9
Direct Investments	41.2	143.0	207.3	135.0	178.0	341.3
Portfolio Investments	-	(25.0)	(23.4)	(36.8)	(22.5)	(3.6)
Other Capital*	(4.4)	64.5	(86.9)	103.4	35.3	49.3
Net Errors and Omissions	131.3	15.0	136.1	121.3	147.4	161.3
<b>Overall Balance</b>	123.6	131.9	145.0	28.6	99.6	288.3
Reserve and Related Items						
Reserve Assets	(123.6)	(131.9)	(145.0)	(28.6)	(99.6)	(288.3)
Use of Fund Credit and Loans	20.9	19.3	12.0	5.3	11.1	11.9
Memorandum Items						
Total Change in Reserve Assets	(97.4)	(130.6)	(131.0)	(97.1)	(178.0)	(343.0)
of which: Change due to Exchange Rate	(26.2)	(1.3)	(14.0)	68.5	78.4	54.8

\* / Use of Fund Credits and Loans is not included.