



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



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## **EXTERNAL SECTOR DEVELOPMENTS OF THE ALBANIAN ECONOMY DURING THE FIRST SEMI-ANNUAL OF 2005**

The overall balance of payments for the first semi-annual of 2005 resulted in a surplus of EUR 11 million. The capital inflows have been fully adequate to cover the level of the current deficit.

The main highlights in the external sector of the Albanian economy may be summarized as follows:

- Intensive activity in the external sector, expressed in the increase of income and current expenditures.
- Deepening of current and trade deficit.
- Reduction of inflows as foreign direct investments.
- Decrease of the level of private borrowings, compared to the previous year.
- Increase of domestic claims to non-residents, mainly expressed in the increase of portfolio investments with abroad.
- Simultaneous increase of foreign assets and liabilities and increase of the monetary authority foreign reserves.

## **I. Current account**

Current transactions during the first half of 2005 are estimated at about EUR 2.8 billion or 23 percent higher than the previous year. Trade exchanges in goods and services lead the volume of Albanian current transactions with the world. During this period, more than 93 percent of current expenditures have been used for the purchase of goods and services. About 41 percent of current income has entered in the form of current transfers, while the services and exports of goods provided respectively 33 percent and 20 percent of the income. Net factor income increased by about 26 percent, however, they could not reduce the high trade deficit (goods and services). As a result, at the end of the semi-annual, current account had a deficit of EUR 145 million, with an annual growth of 10 percent.

### **I. 1. Foreign trade.**

Even during the first half of 2005, it was noticed a growing trend of the Albanian trade activity in international markets. At a level of EUR 1.2 billion, the general trade volume was estimated to be 14 percent higher compared to the same period the previous year. Trade exchanges in goods during this period held about 41 percent of the current transactions volume. The Albanian economy and the domestic market remained import oriented, estimated to be 3.4 times higher than export. Domestic demand continued to push the import increase, while the exports positive performance has not been sufficient to narrow down the trade deficit. Import expenses were about EUR 905 million, EUR 114.5 million or 15 percent higher than in 2004. The income from the export of goods increased by 11 percent, reaching the value of EUR 265 million.

At the end of the semi-annual, trade deficit reached the value of EUR 640 million or 16 percent higher than that of the correspondent period in the previous year. The rising high deficit of foreign trade draws the attention towards policies that aim at replacing imports and inciting exports.

Intermediate goods continued to represent the overwhelming part in the structure of imports, having a share of 46 percent of the total. Their ongoing volume increase implies a positive performance of the domestic processing industry. Moreover, the performance of capital goods is estimated as promising, a positive indicator to the investments level, renovation of technological basis as well as productivity of the private sector. At the end of this semi-annual this item resulted with the highest growth pace compared to the other items (27 percent). We also notice that the consumer goods continued to maintain a considerable weight in total imports, about 32 percent; such a weight has easily decreased compared to the first semi-annual of 2004.

Re-exports (exports with orderer's material) were the main contribution to the rise of Albanian export; such exports remain predominant in the Albanian exports, by holding 67 percent of their overall volume. However, it is worth emphasizing the growing tendency of the domestic export, in particular during the second quarter, by remaining within the seasonal tendencies that characterize the performance of this export item. Export income for active manufacturing was estimated to be 5 percent higher than the income during the first semi-annual of the previous year.

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

Service trade, under rising paces even during this period, is becoming more and more a crucial integration element of Albania with other countries. Trade service transactions reached to EUR 925 million and were estimated to be 20 percent higher, compared to the first semi-annual of 2004. Service account closed with a negative balance of EUR 43 million, being higher than the negative balance of EUR 6 million, recorded at the end of the first semi-annual of 2004. This deficit has been mainly due to a negative balance in the "Other Services" item against a surplus noticed in this item the previous year, as well as a surplus narrowing of "Travel" item.

Movements in the services account were significantly influenced by the performance of services in "Tourism" (Travel), which contributed considerably to the inflows and outflows of this item, respectively 72 and 61 percent of the total for this semi-annual. Actually, the tourism activity continues to represent to the Albanian economy, one of the main sources of foreign income. According to Bank of Albania estimations, the export in tourism during the first semi-annual of 2005 generated about EUR 319 million income flows, which is about 21 percent higher than the value of export of goods. Income from tourism were estimated to be 17 percent higher than this period in the previous year, mainly influenced by the increasing flow of foreign citizens and emigrants visiting the country as well as a slight increase of evaluating coefficients of daily expenses. During the first semi-annual of 2005, the number of foreign citizens entering the country increased by 9 percent compared to the same period in the previous year.

An accelerated activity was noticed in services of tourism, which displayed increasing annual rates. Albanian residents spent in their travels abroad nearly EUR 298 million or 70 percent of the total workers' remittances. Increase of Albanian traveller's expenses abroad was higher than the income growth, causing the narrowing of the positive balance of this item from EUR 28 to 22 million in the first semi-annual of 2005.

"Other services" item resulted in a deficit of EUR 19 million, different from the surplus of EUR 11 million during the first semi-annual of 2004. The current year

deficit has been mainly due to the expenses increase in "Culture and business services" items.

Albanian economy benefits foreign income from the work of seasonal workers and investments of foreign reserves of the banking system in financial non-resident institutions, and at the same time it pays the external debt interest. Net transactions result on income remained positive even during this semi-annual and it was estimated at about EUR 66 million.

Work income compared to the first semi-annual in the previous year, rose to about EUR 9 million, by reaching the level of EUR 47 million. A growth was also recorded in the interest income from investing our foreign reserve in non-resident institutions, while interest income received from portfolio investments in resident institutions abroad, were lower than the previous year.

At the end of the first semi-annual, current transfers balance was estimated at about EUR 472 million or 28 percent higher than that of the first semi-annual in the previous year. Albanian workers' remittances remained the main contribution to the income of this item (about 76 percent). During this period these transfers reached to EUR 424 million, which is 24 percent higher than those of the same period in the previous year. These transfers represent the main source of trade deficit financing (in goods and services) with more than 50 percent. Worker's remittances (EUR 424 million) were also associated by state transfers, mainly in the form of technical assistance (EUR 18 million), which were estimated to be decreasing (28 percent).

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

Even during this semi-annual, net capital flows recorded EUR 201 million, fully enabling current deficit financing and contributing to the increase of foreign reserve. Behind this positive figure, there were inflow capital transfers of EUR 50 million and the financial account positive balance of about EUR 151 million. Compared to the first semi-annual of 2004, capital and financial account net position was estimated at around EUR 54 million lower. Let us remind that during the first half of 2004 high capital flows were recorded owing to privatisation.

Capital transfers during this period, grew by around EUR 1.5 million, while financial account positive balance was estimated to have decreased compared to the previous year (by about EUR 56 million). Financial account position during this quarter was defined as an increase of Albania's financial liabilities held with the world (by about EUR 177 million) and an increase of our assets held abroad (around EUR 26 million). However, compared to the first semi-annual in the previous year, financial liabilities net flow was estimated to be lower, about USD 78 and Albania's financial claims to the rest of the world were also set at a lower level (EUR 22 million).

The increase of financial liabilities to the world during this semi-annual was mainly due to capital inflows in the form of direct investments (EUR 96 million) and borrowings from abroad (by EUR 77 million). Foreign direct investments were estimated at EUR 79 million lower than the same period in the previous year where more than 60 percent of FDI's flow entered in the form of privatisation.

During this semi-annual, the granting of long-term loans and loan facilities from abroad, which remain another important factor in the growth of Albania's financial liabilities to the world, was EUR 26 million lower: state borrowing had a slight increase of about EUR 1.2 million, while unlike the previous year where it was noticed the private sector presence in long-term loans, during this semi-annual loan disburse of this sector was lower (less than about EUR 27 million).

External debt services in the form of principal and interest amounts were estimated at about EUR 25.5 million, equivalent to 10 percent of export of goods.

On the other hand, Albania's financial claims to the rest of the world grew by EUR 26 million. Assets growth was mainly determined by the increase in portfolio investments of resident units abroad, while banking system assets in the form of deposits abroad have been decreasing.

Financial assets stock in the form of portfolio investments, amounted to EUR 164 million with an increasing semi-annual flow of EUR 48.1 million. Regarding the structural composition by denomination, 47 percent of portfolio investments were in US currency, 52 percent in EUR and 2 percent in British pound. Foreign assets held with the banking system in the form of deposits abroad, decreased to about EUR 37 million. 56 percent of deposits held with the banking system was in US dollar and the other part in Euro (40 percent) and the British pound (3 percent). Cash foreign assets were estimated to have been decreasing. In the structural composition by denomination, cash foreign assets denominated in US dollar were 39 percent, EUR 53 percent and the British pound 8 percent.

Inflows of foreign currency assets as financial capital were reflected in the growth of foreign exchange reserve of the monetary authority, by about EUR 11 million. By the end of the period, the level of gross foreign exchange reserve was estimated at EUR 1.72 billion, a sufficient level to cover 4.6 months of goods and services import.

**Balance of Payments**

in millions of EUR

	Q1 2004	Q2 2004	Q3 2004	Q4 2004	Q1 2005	Q2 2005
Current Account	-36.9	-94.7	-25.5	-129.0	-44.8	-100.5
Export of Goods	109.1	129.9	121.6	125.0	121.5	143.3
Import of Goods	-363.5	-427.0	-453.7	-518.1	-398.0	-507.0
Trade Balance	-254.4	-297.1	-332.1	-393.1	-276.5	-363.7
Services: Credit	176.5	206.1	223.8	201.1	201.7	239.5
Services: Debit	-166.8	-221.9	-229.0	-230.4	-226.4	-257.6
Income: Credit	34.2	34.7	55.8	39.3	39.3	41.1
Income: Debit	-4.4	-7.0	-5.1	-6.8	-4.9	-9.6
Private Unrequired Transfers	166.2	176.6	244.5	242.3	210.3	243.3
Official Unrequired Transfers	11.7	13.8	16.7	18.5	11.8	6.5
Capital Account	27.2	21.3	29.1	28.5	35.5	14.6
Financial Account	18.3	183.7	-15.2	110.7	22.4	124.0
Direct Investments	28.0	138.1	58.7	42.6	43.3	50.3
Portfolio Investments	-1.1	3.3	98.2	-95.9	-42.9	-5.2
Other Capital*	-8.7	42.3	-172.2	164.0	21.9	78.9
Net Errors and Omissions	-1.5	-12.4	84.9	35.6	-8.0	-36.7
Overall Balance	11.8	97.9	78.1	45.9	9.7	1.4
Reserve and Related Items						
Reserve Assets	-11.8	-97.9	-78.1	-45.9	-9.7	-1.4
Use of Fund Credit and Loans	4.8	0.0	4.8	0.0	4.6	0.0
Memorandum Items						
Total Change in Reserves	-2.1	-94.5	-84.4	-95.2	15.7	35.3
of which: Change due to Exchange Rate	0.8	-3.4	6.3	49.3	-25.4	-36.7

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