

BANK OF ALBANIA

EXTERNAL SECTOR
PERFORMANCE
OF THE ECONOMY
FOR THE FIRST
NINE-MONTH PERIOD
OF 2007

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For the first nine-month period of 2007 the external sector of the economy is presented with a deepened negative balance sheet in the current account, caused by a high trade deficit.

Capital inflows have been sufficient for compensating the current deficit, enabling an overall positive balance sheet at Eur 172.7 million.

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

- Intensive activity in the external sector, reflected in the increase of income and current expenditures.
- Considerable growth in merchandise exports and imports.
- Deepening of the current and trade deficit.
- Increased foreign capital inflows in the form of foreign direct investments.
- Increased financial liabilities to non-residents, created in the form of increased deposits of non-residents with the banking system.
- Increased foreign reserve stock of the monetary authority.

I. CURRENT ACCOUNT

Current transactions carried out during the first nine-month period of 2007 are estimated at Eur 6.2 billion or 21 percent higher than in the previous year. Trade exchanges in goods and services guide the volume of current transactions of Albania with the world. More than 94 percent of current expenditures over this period have been used for purchasing goods and services, while about 32 percent of current incomes have entered in the form of transfers. Exports in goods and services ensured respectively 21 percent and 39 percent of current income.

High trade deficit characterizing the developments of the external sector of the Albanian economy has neutralized the positive effect of the significant reduction of the deficit position in services account and the growth of surplus of net factorial revenues, remaining the main cause of the current deficit deepening even for this period.

The current deficit for this nine-month period is estimated at about Eur 579 million, with a nominal growth of about Eur 188 million (or 48 percent), against the same period of 2006.

I. 1. EXTERNAL TRADE

Merchandise trade constitutes the main component of our current exchanges with the rest of the world. During this nine-month period they represented 43 percent of them, recording an overall trade volume of Eur 2.7 billion.

Expenditures for merchandise import recorded approximately Eur 2.1 billion or Eur 423 million more than in 2006. Merchandise export revenues are estimated to about Eur 589 million, with a nominal growth of about Eur 125 million.

The underlined orientation of the Albanian economy to imports continues to characterize this period as well, resulting to further trade deficit deepening. During this period Albania recorded the highest trade deficit in years by Eur 1.5 billion or 25 percent higher than in the previous year.

The trade deficit has constituted a permanent feature of external trade performance, dictating high levels of current account deficit. The high demand for imports for meeting the needs of the growing economy and simultaneously of the population for consumer goods has obviously highlighted the expanded basis of imports in years. This dynamics, however, has not been followed by a strengthening of the large import basis, making the trade gap deepen and constitute the main factor for the high current deficits.

Imports growth observed during the first nine-month period of 2007 is a co-consequence of some external factors – unusual oil price rise and price rise of some goods in international markets – and of some internal factors – worsened energy situation in the country, which has led to high imports of electricity. During this year they increased by about 25 percent, from 17 percent increase noticed in the same previous year period.

However, trade deficit might have been even worse without the progress observed in exports of this year. The exports grew by about 27 percent, from 16 percent growth over the same previous year period.

Notwithstanding the deteriorated situation in the country's power supply, even during this year exports grew highly, with the key industries of Albanian exports rendering the main contribution (again almost half of exports (48 percent) remains significantly concentrated to textiles and footwear.

In the meantime, high international market prices have significantly stimulated internal exports (during 2007 the crude oil and chromium mineral exports have increased obviously), contributing to high growth rates of merchandise export revenues even for 2007.

I. 2. OTHER CURRENT ACCOUNT ITEMS PERFORMANCE

Services trade during this nine-month period has been inclined towards extending trade exchanges with the world and narrowing the deficit position, reflecting the same tendencies observed during the recent years.

Trade exchanges in services are estimated to about Eur 2.2 billion, with an annual growth of 18 percent compared to the previous year. The net position of this category is estimated at Eur -11 million, with an obvious improvement compared to the previous year (Eur -63 million). During this year revenues from export of services increased faster than expenditures for import of services, respectively by 21 and 14 percent compared to the previous year.

During this year the services deficit position improvement is due to the positive balance sheet of the category "other services" and to the surplus expansion in "travelling" item.

The services benefited and offered in "Travelling" item continue to render the main contribution to services sector for Albania, respectively by 70 percent of revenues and 64 percent of expenditures for this nine-month period. Tourism in Albania currently represents the activity with the highest foreign currency inflows for the Albanian economy. According to Bank of Albania's estimates, export in tourism during the first nine-month period of 2007 has generated about Eur 754 million receipts, a value of about 28 percent higher than the value of merchandise exports.

The growth of annual tourism revenues is estimated to about 23 percent. This growth has been influenced mainly by increased number of foreign citizens and emigrants that have visited the country, while the coefficient of daily spending has fluctuated around the previous year levels, whereas that of staying days has slightly decreased.

In the meantime, Albanians have spent in their travelling abroad about Eur 700 million. The volume of travelling expenditures for 2007 is estimated at about 20 percent higher than in the previous year, due to the increased number of traveller. The coefficient of the staying time and of the average daily expenditures has slightly decreased.

The positive balance of factorial revenues at end of the period (Eur 169 million) is estimated to about 21 percent higher compared to the previous year. The growth of this year is due to interests accumulated from banking system foreign reserve investment in non-resident financial institutions, income, preferred from our direct investments abroad and financial assets investments in the form of portfolio investments. Net interest incomes from investment have increased by 45 percent. Incomes from work represented about 52 percent of the positive balance sheet of revenues. In the meantime, during 2007 Albania has paid Eur 13.1 million to pay off the interests on its external debt, which have decreased against the level accrued for the first nine-month period of 2006 (about 19 percent).

Current transfers, as in the preceding years, are dominated by inflows in the form of remittances. The latter ones represent the main source of financing the trade deficit (to 47 percent) and for the first nine-month period of 2007 they are estimated to Eur 711 million or Eur 18 million more than in the same previous year period.

The monetary inflows from emigrants have been associated with state transfers, whose net flow for this year is estimated at about Eur 11 million higher than in 2006.

II. CAPITAL AND FINANCIAL ACCOUNT

Net capital inflows during this nine-month period recorded about Eur 598 million, enabling the current deficit financing (at 103 percent) as well as increased foreign reserves. Inflow capital transfers of Eur 65 million and the positive balance of the financial account by about Eur 534 million stay behind this positive figure.

The financial account of this period is defined by a considerable growth of the financial liabilities of Albania with the world (by about Eur 633 million), as well as by increase of our foreign assets (by about Eur 99 million). Compared to the first nine-month period of the previous year, the financial liability flow is estimated to about 84 percent higher than in the previous year, while the increase of financial claims of Albania on the rest of the world is estimated to 40 percent lower.

The growth of financial liabilities to the world is mainly due to capital inflows in the form of direct investments (Eur 370 million) and accumulation of banking system foreign currency assets, while the flow of foreign borrowing is estimated at about 30 percent lower than in the same period of 2006.

Foreign direct investment flow reached the value of Eur 370 million against Eur 201 million over the previous year. These capital inflows have become a dominant factor in the growth of financial liabilities and in the development of capital and financial transactions of the country. In this year they are presented as foreign capital derived mainly from the privatization process (Albtelecom privatization).

The phenomenon of the considerable growth of deposits of non-residents with the banking system observed at end of the last year, has continued also during this nine-month period, increasing the financial liabilities of the country by about Eur 134 million. This has derived from the emigrants' deposit placements with our banking system, a reflection of their increased interest to invest in the Albanian economy.

In the meantime, the borrowing seems to have slowed down its growth rates. Extensions of long-term loans and soft-term ones from abroad, recorded a flow of Eur 88 million, which is estimated at about 30 percent lower compared to the borrowing flow of the previous year. The increase of private sector's liabilities through borrowing has been only Eur 10 million, from Eur 27 million over the same period of 2006.

External debt service has reduced our liabilities by about Eur 54 million. This level represents only 3.2 percent of our exports during this nine-month period

and indicates a solvency within the accepted levels.

On the other hand, the financial claims of Albania on the rest of the world have increased by Eur 99 million. The assets growth has been mainly determined by increased assets owned by the banking system in the form of deposits abroad, while the portfolio investments of resident units abroad have maintained almost the same level.

Foreign currency inflows in the form of financial capitals were reflected in the growth of Monetary Authority Reserves, by about Eur 173 million. At end of September 2007 the foreign reserve recorded the level of Eur 1.5 billion, being sufficient to cover about 4.2 months of import of goods and services.

Table 1 Balance of payments (in millions of EUR)

	9M 2006	9M 2007
Current account	-391.6	-579.1
Merchandise export	463.3	588.6
Merchandise import	-1663.2	-2085.8
Trade balance	-1199.8	-1497.3
Services: Credit	896.7	1085.2
Services: Debit	-959.9	-1096.5
Income: Credit	166.9	212.6
Income: Debit	-26.7	-43.3
Private unrequired transfers	697.2	714.7
Official unrequired transfers	34.3	45.3
Capital account	108.7	64.6
Financial account	179.2	533.8
Direct investment	197.7	361.6
Portfolio investment	23.3	-0.7
Other capitals*	-47.6	167.4
Net errors and omissions	224.9	153.5
Overall balance	121.1	172.7
Reserve assets	-121.1	-172.7
Use of IMF credit and loans	5.8	5.5
Total change in reserves	91.2	146.7
Of which: exchange rate change	-29.9	-25.9

* not included Use of IMF credit and loans

Source: Bank of Albania