

BANK OF ALBANIA

PRESS STATEMENT

EXTERNAL SECTOR DEVELOPMENTS OF THE ALBANIAN ECONOMY FOR THE FIRST QUARTER OF 2007

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The overall balance of payments for the first quarter of 2007 resulted in a surplus of EUR 14.5 million. Capital inflows financed about 92 per cent of current deficit and led to the increase of the monetary authority reserve.

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.
- Progress in exports' performance.
- Increase of Albania's financial liabilities to the rest of the world, mainly expressed in the growth of foreign direct investments and borrowing.
- Increase of the monetary authority foreign reserve.

I. CURRENT ACCOUNT

The first quarter of 2007 was characterized by an intensive activity in the external sector, expressed in the considerable increase of current revenues and expenditure. The volume of current transactions has grown by about 12 per cent, compared with the first quarter of the previous year, amounting to EUR 1.8 billion.

More than 94 per cent of current expenditure was used for the purchase of goods and services. About 35 per cent of current revenues were in the form of transfers, while services and the exports of goods provided 34 per cent and 23 per cent of Albania's foreign currency revenues, respectively.

Current deficit for this quarter was estimated to total EUR 183 million, increasing by about 39 per cent compared with the same period the previous year.

The high trade deficit, which characterized the developments in the external sector of economy over this quarter, neutralized the positive effect of the deficit reduction in the services' account and of the positive flows' growth of net factorial income, remaining the main cause for the current deficit deepening over this period.

I. 1. FOREIGN TRADE

The high flow of foreign exchanges continues to characterize the first quarter of 2007. The total trade volume amounted to about EUR 811 million, being 23 per cent higher than the same period the previous year.

In relative terms, both exports and imports recorded high growth rates, growing by 26 per cent and 22 per cent, respectively. Although exports have grown under more rapid rates than imports, their low base did not manage to reduce trade deficit, which remains a permanent feature of Albania's foreign trade.

Trade deficit for this period is estimated at EUR 448 million or 21 per cent higher than the first quarter of 2006.

The ratio of imports' coverage by exports remains in low levels (about 29 per cent), providing evidence for a significant orientation of foreign trade towards imports.

Exports had a booming season, as a result of the improvement in the situation of textiles and footwear industry, as well as of minerals exports. As of end quarter, exports' revenues amounted to EUR 182 million, increasing by EUR 38 million, in absolute terms.

The structure of exports, in terms of diversification, continues to be low, without any significant changes over this quarter. Exports of textiles and footwear continue to share 53 per cent of the total, growing by 22 per cent and 8 per cent, respectively. The export of mineral products displayed a substantial upward trend by doubling their volumes. The export of chrome, which shared 40 per cent of exported minerals, mostly to China, provided a considerable contribution to this growth.

As far as imports are concerned, the data show positive developments and further growth of main imported products. Our country spent about EUR 630 million for the purchase of goods, or EUR 114 million more than the previous year.

The high demand for energy, along with the unfavourable energy situation in the country maintained the imports of energy in high levels, which consequently, had a significant influence on the increase of imports expenditure for this period. While, unlike the dynamics of the last years, fuels and lubricants decreased over this quarter (40 per cent), compared with the first quarter of 2006. This performance was somehow a response to their high prices.

The positive developments in the imports of machinery and equipment are promising, providing evidence for the growth of investments in the country. This commodity group shares 21 per cent of total imports.

Our exports were mostly oriented towards the regional countries over this quarter. This group increased its share to about 10 per cent of total exports. The exports to Kosovo, which quadruplicated over this quarter compared with the previous year, provided the main contribution to this growth. Almost half of our exports with the region had Kosovo as their destination, while the rest were mostly oriented towards the markets of Serbia, Montenegro and Macedonia.

The advantages of the free trade in goods, deriving from the entry into effect of the Stabilization and Association Agreement with the EU on 1 December 2006, seem to have pushed the Albanian exporters, since there have been considerable upward exporting trends with almost all the participant countries. Despite this fact, there is a non-proportional distribution of these exports, with a high concentration of exports to the neighbouring countries, Italy and Greece (about 82 per cent of total exports).

In terms of imports, the geographical structure is displayed the same over this quarter compared with the same period the previous year. The traditional partners, Italy and Greece, predominate the import countries. The implementation of the Interim Agreement provisions¹, instead of the Free Trade Agreements with the region, seems to have had a negative effect on the imports from Bulgaria and Romania. Meanwhile, imports with some of the EU member countries have decreased. On the other hand, worth underlining is the high demand for goods from Serbia and Montenegro. The imports with these two countries increased by five times, compared with the same period the previous year.

Inflows from China and Turkey continue to remain significant trade partner countries, considering the share they have in world trade. Over the last years, the growth of imports from these two countries has displayed stable growing rates. Over this quarter, they were 64 per cent (China) and 36 per cent (Turkey), respectively, higher than the first quarter of 2006.

I. 2. DEVELOPMENTS IN OTHER ITEMS OF CURRENT ACCOUNT

The volume of transactions in services recorded about EUR 579 million, decreasing slightly by 2 per cent, compared with the same period the previous year.

Trade in services ended in a negative balance of EUR 30 million, which is assessed to have improved by 14 per cent, compared with the first quarter of 2006.

The improvement in the net services account, which also observed in the beginning of the present year, is attributed to the considerable growth of revenues in "Other services". This performance brought about the shift of this item's net position, and partly offset the deficit in "travel".

The services provided by tourism share most of the weight in trade in services. The export and import of services in tourism over this quarter are assessed to have decreased compared with the first quarter of 2006, ending their net balance in a deficit of EUR 6 million.

According to the Bank of Albania estimations, the export of tourism brought EUR 170 million of income, which is 15 per cent lower than the previous year. Despite the slight increase of daily expenditure, the annual decrease

by 14 per cent of the number of non-residents, along with the decrease of the estimating coefficient of the duration of stay, was the main factor in the performance of this item's income over this quarter.

The Albanian residents spent in their travels abroad about EUR 177 million, or 62 per cent of total workers' remittances. The volume of travel expenditure for the first quarter of 2007 was assessed to be about 6 per cent less than the previous year, as a result of the decrease of the estimating coefficients of the duration of stay (27 per cent), despite the slight increase of daily expenditure and the number of travellers (9 per cent).

It is now known that the transportation and insurances services follow the trend of the trade activity in goods. The increase of imports caused the increase in the import of these items' services. As of end quarter, the import of goods' transportation and insurance services were assessed to be 17 and 37 per cent higher than the same period the previous year.

The item of "Other services" ended in a surplus of EUR 1 million, as opposed to the deficit of EUR 26 million of the first quarter the previous year. This services item is developing under rapid rates, in particular in terms of exports. The income deriving from the export of these services had an annual growth of 40 per cent. Within this item, the construction, communication and Government services recorded the most evident developments.

The positive balance of factorial income as of end period (EUR 57.7 million) is estimated to be 18.7 per cent higher than over the first quarter of 2006. The Albanian economy continued to benefit from the foreign currency resources. The foreign currency income derived from the labour of seasonal and border workers, from the accumulated interest from the investment of the banking system foreign reserve in non-resident financial institutions and the investment of financial assets in the form of portfolio investment. Income from labour shared about 48 per cent of the positive balance of income, while the net income in the form of interest from investment increased by 52 per cent. Over the first quarter of this year, Albania paid EUR 3.2 million to settle the interests on its external debt, which were assessed to have slightly decreased (EUR 1.5 million) compared with the same period the previous year.

Current transfers continued to be represented by worker's remittances. The latter amounted to about EUR 233 million and they were assessed to have financed 52 per cent of the trade deficit in goods. Compared with the same period the previous year, these transfers were 5 per cent higher. In addition to worker's remittances, there were other private and official transfers, which totalled EUR 39 and 11 million, respectively.

II. CAPITAL AND FINANCIAL ACCOUNT

Net capital flows for the first quarter of 2007 amounted to about EUR 169 million, financing about 92 per cent of the current deficit. Capital transfers

totalled about EUR 27 million. They were mainly characterized by investment grants, both in the public and private sector.

Financial account ended in a positive balance of about EUR 142 million. This account's position for this quarter may be defined in the increase of Albania's financial liabilities to the rest of the world (about EUR 141 million). Compared with the first quarter the previous year, the net flow of financial liabilities is assessed to be 40 times higher. Meanwhile, our assets abroad dropped by EUR 1 million, compared with the increase by EUR 34 million over the same period the previous year.

The increase of financial liabilities is mainly attributed to the capital inflows in the form of foreign direct investments and to borrowing from abroad.

The flow of foreign direct investments recorded about EUR 88 million. It should be noted that the capital inflows in processing and production industry, as well as in communication, played the main role in these investments. 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, amounted to EUR 36 million, out of which 88 per cent were used for the Government and public sector. This increase has mainly financed investment and consumption, reflected in the growth of imports for consumption and in the companies' needs for capital and capital goods. Meanwhile, private borrowing seems to have slowed its growth rates down. Compared with 2006, the increase of this sector's liabilities is estimated to be as much as half of the previous year's inflow, and it shares only 12 per cent of the borrowing. The structure of external debt, created by borrowing, is dominated by the Euro and the Sdr, sharing 43 and 35 per cent, respectively.

External debt services in the form of principal and interest payments amounted to about EUR 6.5 million, which is equal to 4 per cent of the export of goods. This figure provides evidence for Albania's solvency within the accepted levels.

The international position of the Albanian economy, in terms of financial assets, was almost the same for the first quarter of 2007, slightly declining by EUR 1 million, but with structural changes. There has been a change in the ratio of investment assets. Portfolio investment assets and short-term foreign assets shifted to the investment of the banking system reserves in the international market in the form of deposits. Consequently, the dropping of portfolio investment and of short-term foreign assets investments by EUR 18.4 and 30 million, was offset by the increase of deposits by about EUR 46 million.

The foreign assets inflows in the form of financial capital were reflected in the increase of the monetary authority foreign reserve by about EUR 14.5 million. As of end quarter, the foreign reserve totalled EUR 1.375 billion, fully sufficient to cover nearly 4.4 months of imports of goods and services.

Table 1 Balance of Payments (in millions of EUR)

	Q-1 2006	Q-2 2006	Q-3 2006	Q-4 2006	Q-1 2007
Current account	-131.5	-153.2	-106.9	-143.1	-183.2
Merchandise: exports	144.4	165.7	153.2	167.3	181.9
Merchandise: imports	-515.2	-579.5	-568.5	-652.9	-629.5
Trade balance	-370.8	-413.8	-415.3	-485.6	-447.6
Services: credit	277.4	282.0	337.2	298.1	274.2
Services: debit	-312.7	-291.5	-355.8	-301.6	-303.9
Income: credit	55.9	53.2	57.7	96.1	65.8
Income: debit	-7.3	-12.2	-7.2	-27.6	-8.2
Private unrequired transfers	209.7	216.3	271.1	269.2	225.3
Official unrequired transfers	16.3	12.7	5.3	8.2	11.2
Capital account	41.1	39.5	28.1	34.7	26.9
Financial account	64.3	98.9	10.1	229.8	142.2
Direct investment	56.8	68.6	75.5	57.8	86.1
Portfolio investment	4.6	-3.1	21.7	3.9	18.5
Other capital*	3.0	33.4	-87.0	168.1	34.8
Net errors and omissions	38.7	44.2	141.9	-36.0	28.6
Overall balance	15.6	29.5	76.1	85.4	14.5
Reserve assets	-15.6	-29.5	-76.1	-85.4	-14.5
Use of Fund credit and loans	2.9	0.0	2.8	0.0	2.8
Total change in reserve assets	10.4	-6.5	-74.7	-67.9	13.3
of which: change due to exchange rate	-5.2	-23.0	-1.4	-17.5	-1.2

* Not included use of Fund credit and loans.

Source: Bank of Albania

NOTE

¹ On 12 June 2006, in Luxembourg, Albania signed the Stabilization and Association Agreement with the EU. Consequently, since December 2006, the Interim Agreement between the EU and Albania is in effect. This agreement replaced the Trade, Commercial and Economic Co-operation Agreement between the European Community and Albania. The Interim Agreement will remain in force until the ratification of the Stabilization and Association Agreement is completed by all the EU member countries.