



INTERNATIONAL MONETARY FUND
RESIDENT MISSION IN ALBANIA

Tirana, November 14, 2007

Statement by IMF Staff Mission to Albania

An IMF mission led by Mr. Gerwin Bell visited Tirana October 31–November 14, 2007 for discussions on the fourth review under the IMF program and the fiscal, financial, and macroeconomic impact of the ongoing energy crisis. The mission met with Prime Minister Berisha, Minister Bode, other key ministers, Governor Fullani, other senior officials and representatives of civil society and the international community. On Wednesday November 14, 2007, at 9.00, a joint press conference together with Minister Bode and Governor Fullani will be held at the Ministry of Finance.

The Fund remains committed to support Albania’s sustainable growth. Looking ahead, a key challenge for the authorities will be to steer a clear course among the many competing priorities for the Albanian economy.

Economic growth has remained strong at 6 percent despite the energy crisis and regional drought but cost pressures have added to inflation and fiscal risks are on the horizon. Stronger-than-projected exports and manufacturing activity have offset the negative impact of the energy crisis and drought on growth. Also, the growth outlook remains positive but serious macroeconomic challenges will have to be tackled urgently and forcefully if the good progress of recent years is to be maintained. In particular, the severe deterioration in KESH’s financial position needs to be reversed and public capital expenditures will need to be contained to avoid inflationary pressures. With these prerequisites in place, the recent increase in inflation is likely to be temporary, mainly reflecting one-off effects of higher food prices and energy disruptions, and the Bank of Albania’s timely policy action and well-established credibility should help bring inflation back to the target range.

Immediate action is needed to stabilize the financial position of KESH, while privatization is critical to place the energy sector on a long-term sustainable footing. KESH’s large deficit reflects not only the drought but, more fundamentally, chronic problems with losses and collections, unsustainable import levels, and import prices well above domestic tariffs. While losses and collection rates are improving, except for collections from water companies, further efforts will be needed to address these core problems. Privatization is essential for next year, but will require close collaboration between the authorities, the World Bank, IFC and other key development partners so that all requirements—including the establishment of the necessary regulatory and market structures—are pursued in concert. Pending these actions, uninterrupted provision of electricity should become possible over the medium term.

The authorities are aiming at faster mobilization of foreign financing for large infrastructure projects in 2008, which could add to overheating pressures and fiscal risks. Therefore, it will be important to ensure that the budget deficit does not give rise to inflationary pressures. A deficit of some 5 percent of GDP (compared with a projected 4 percent in 2007) would allow for a temporary acceleration of spending on critical transport infrastructure while maintaining macroeconomic stability, safeguarding continued fiscal consolidation and providing sufficient financing for other medium-term public investment objectives. Looking ahead, we commend the authorities’ intention to consider additional fiscal rules in the 2009 budget to more sustainably anchor fiscal policies, in turn facilitating medium-term budget planning.



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Monetary policy, which has been well managed in an increasingly challenging environment, should remain the main policy response to short-term threats to price stability, but anchoring inflation expectations requires other actors to also play their roles. The drought, energy crisis and strong credit growth have all contributed to upward pressure on prices. Meanwhile, a fiscal surplus through most of 2007 has helped to offset these pressures, enabling the Bank of Albania to focus on combating the spill-over effects of cost-push inflationary pressures. Looking ahead, we remain convinced that inflation will return to the 3 ± 1 percent target range in 2008, supported by an appropriate fiscal and monetary stance, measures in the electricity sector, and further steps to strengthen banking supervision. We support the Bank of Albania's efforts to reinforce safeguards for financial stability, including establishing Memorandums of Understanding with the home country supervisors of the major banks, and measures to improve the ability of banks to execute collateral.

Progress continues in structural reforms. Steps to further broaden the tax base, together with other revenue-compensating measures, will allow the government to sustainably reduce the corporate income tax rate; this and the planned improvements in the taxpayer registry and social security administration, will help reduce informality and in turn allow the economy to reap the benefits of further financial market development in the future. In debt management, we welcome the significant lengthening of maturities of government domestic debt and support the efforts by the authorities to deepen the domestic money and bond markets. In the area of statistics, while there is progress to date, the outstanding agenda remains daunting. In this regard, two IMF technical assistance missions over the next six months will focus on the consumer price index and improving the national accounts statistics.

It is expected that the fourth review under the current combined Poverty Reduction and Growth Facility and Extended Fund Facility will be presented to the IMF's Executive Board in early 2008.

The mission would like to thank the authorities for their continued close cooperation and warm hospitality.

Gerwin Bell
Mission Chief

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Resident Representative