

Compared with the previous year, the quantity of counterfeited banknotes and coins discovered in circulation decreased by 13.4% during 2016. Overall, compared with the number of banknotes and coins in circulation, they remain insignificant. We observe that the counterfeited banknotes of the 1000 Lekë denomination constitute around 47% of the total counterfeited banknote and coins, followed by the 50 Lekë coin at 19% of the total as well as the denomination 500 Lekë and 2000 Lekë at 15% and 14 % of the total, respectively.

The monitoring of the phenomenon of counterfeit national banknotes shows that it continues to be dominated by the digital colour reproduction, combined with the application of additive methods for the imitation of the security features. Meanwhile, in terms of techniques of banknote falsification, we note that there is no tendency toward professional printing. Mostly, the tendency is to imitate first level - visual and tactile - security features, and less frequently those readable through authentication devices.

2.6 PAYMENT SYSTEM

To accomplish its legal responsibilities, the Bank of Albania promotes and supports the smooth functioning of the domestic payment systems in Albania. The Bank of Albania has taken steps to achieve this objective, by promoting developments, in its role as the systems' operator and overseer. These measures have consisted in the completion and improvement of the regulatory framework of the payment system, the promotion of the inter-institutional cooperation, the expansion of research work and the increase of transparency.

PAYMENT SYSTEM OVERSIGHT

The Bank of Albania fulfils its legal obligation on the normal functioning of the payment systems through three approaches: operator, overseer and promoter. In this framework, the Bank of Albania has continued to take concrete steps, by promoting developments in its role as both the operator and the overseer of these systems. More specifically, in addition to the completion of the regulatory framework on payment systems oversight, particular attention has been dedicated to the promotion of the inter-institutional collaboration, the expansion of the research activity, and the increase of transparency.

The payment instruments, as components of the payment systems, have also been in the focus of the payment system oversight. Thus, during 2016, in order to promote the efficiency of electronic money and in accordance with the EU directives, the regulatory framework "On electronic payment instruments" approved by decision of the Supervisory Council No. 11, on 09.11.2016, was revised.

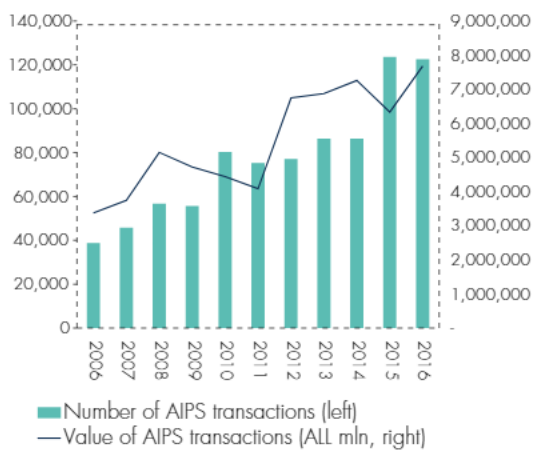


In view of fulfilling the strategic duties of the Bank of Albania in the framework of the European integration, throughout 2016, the Bank of Albania has started the work for the transposition in the Albanian legislation of the Directive 2015/2366 "On payment services in the internal market". For this purpose, the Bank of Albania started a cooperation project with the Bank of Italy, which will contribute to strengthening the rules related to internet payments as well as the implementation of the European practices and regulations on payment system supervision.

PERFORMANCE OF AIPS AND AECH SYSTEMS

Albanian Interbank Payment System for large-value payments (AIPS)

Chart 22 Transactions in AIPS by number and value



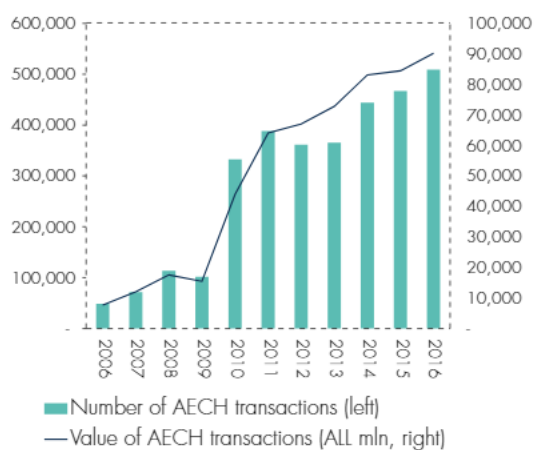
Source: Bank of Albania.

During 2016, the Bank of Albania and 16 commercial banks participated directly and the Ministry of Finance indirectly in the AIPS system. The volume of transactions processed during the year was 122,550 with a total value of ALL 7,676 billion. Compared with the previous year, the volume of processed transactions decreased by around 0.83%, while the value of the processed transaction increased by 21.29%.

The Intraday Loan Facility (ILF) has decreased in terms of both number and value (13.25% and 28.64%, respectively), reflecting the decrease of the exposure of the system to liquidity risk.

Albanian Electronic Clearing House for small-value payments (AECH)

Chart 23 AECH transactions, by number and value



Source: Bank of Albania.

During 2016, the Bank of Albania and 16 commercial banks participated directly and the Ministry of Finance indirectly in the AECH system. The volume of cleared payments during the year was 508,935 with a total value of around ALL 90 billion and an average value of around ALL 180,000. Compared with the previous year, the activity of the AECH system, increased in both volume and value of cleared payments, by 9.05% and 6.79%, respectively.

PAYMENT INSTRUMENTS

Banks' reporting on payment instruments show that around 11.9 million payment transactions were

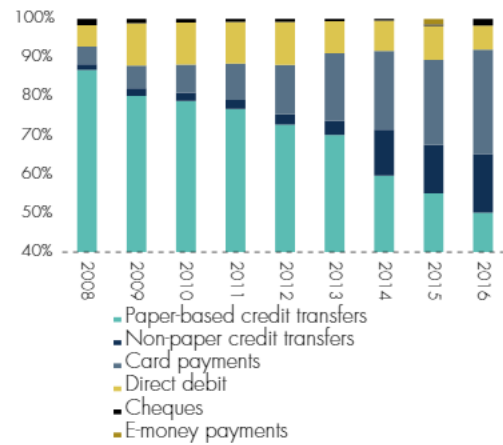


made, totalling ALL 4.512 billion, registering an increase by 8.54% in volume, and a decrease by 1.85% in value, during 2016.

From the total number of clients' payments, we observe for this period a high use of credit transfer (at 65.08%), of which, around 76.94% were payment instructed in paper form. However, it is worth highlighting that, in the last years, we have noted a contraction of paper credit transfers, meanwhile non-paper credit transfers (home banking) and card payments increased.

In terms of use of electronic payment instruments, it is worth highlighting the use of electronic money by both bank and non-bank financial institutions. The increase in the use of such instrument is considered to have a positive impact on the financial inclusion of the population in financial services.

Chart 24 Performance of payment instruments during years



Source: Bank of Albania.

Bank cards

As at the end of 2016, fourteen banks were licenced as card issuers in the Republic of Albania, 9 of which were also licenced as card accepters, up 1 bank compared with 2015. Also, during 2016, two electronic payment institutions exercised their activities in the market as well. During the year, the issuing of debit cards increased by 5.5% and the issuing of credit cards increased by 5.9%. On the other hand, the introduction of cards with electronic money functions has showed a rapid upward trend during the year.

From the use of bank cards in ATM and POS terminals, we see that the major share of processed transactions with cards has been cash withdrawals from ATMs, an indicator of a largely cash-based economy. However, during 2016, we observe a significant increase in the number and value of card payments in physical and virtual POSs, 28.9% and 21.2%, respectively, continuing the positive trend registered in the last years. In relative terms, payments carried out with prepaid cards reached up to 6.51% of the payments with debit and credit cards.

As at the end of 2016, the number of POS terminals increased by 6.31%, while the number of ATMs slightly decreased by 3.15% compared with the last year. Notwithstanding the positive upward trend in the number of POS terminals, their concentration continues to be high in the region of Tirana,³⁸ at

³⁸ Regions are divided according to the branches of the Bank of Albania.



81.76%, while terminals for the use of electronic money cards registered an upward trend of 13.9% compared with the end of 2015³⁹.

Home Banking

Recently, home banking has been increasingly expanding in the Albanian market. Thus, 14 of the 16 banks were offering different home banking products, as at the end of 2016. These products provide remote access to the bank account, via on-line, telephone or software that the bank makes available to its clients. From banks' reports, we observe a significant increase of 27.63%

of the volume of home banking payments and of 21.51% of the value of the transactions, compared with the previous year. The increase of home banking transaction also dictates to a large extent market's developments in this aspect.

The increasingly upward trend of home banking is closely connected to the presence of infrastructure and the expansion of possibilities to access internet through a smartphone.

Regarding cash transactions conducted by customers at banks' cash desks, during 2016, we observe a decrease of the number and an increase of the value compared with the previous year. This year has registered a slight decrease of cash desk transactions by 0.4% in numbers, and an increase by 10.27% in value, compared with the previous year.

Chart 25 Trend of online accessible accounts against total accounts and trend of online accessible accounts utilisation ratio*



Source: Bank of Albania.

*The utilisation ratio shows how much on average an account is used on-line to carry out transactions.

NATIONAL PAYMENT SYSTEM COMMITTEE

The National Payment System Committee (NPSC) continued its proceedings in this year, in light of fulfilling its operational strategy. Particular attention was paid to fulfilling the NPSC recommendations as well as to the cooperation and collaboration with the institutions participating in it.

In November 2016, the first standardisation process of the payment order format was successfully completed, which is based on SEPA's standards⁴⁰. Another project initiated by the Albanian Association of Banks that requires the collaboration of the Bank of Albania is that of the implementation of the Interbank Direct Debit. Its goal is to increase the use of this instrument by the

³⁹ Electronic money is a payment instrument, different from the remote payment instruments. E-money is an electronic store of monetary value and provides to the holder the possibility to make payments electronically. This instrument may be reloaded with monetary value whenever necessary, within the limits set out by the Bank of Albania. Electronic money may be stored on a card or a system (i.e. PAYPAL) and is not conditioned by the need to own a bank account.

⁴⁰ Single Euro Payments Area – initiative of the European Union for the integration of payment systems through the development of harmonized electronic payments schemes and systems.



clients of all the banks, regardless of the location of the utility companies' bank account thus contributing to reducing the use of cash in the economy.

In view of promoting innovation in banking services, the Albanian Association of Banks, in cooperation with the Bank of Albania and the NPSC, organized a conference on "Digital Banking". In this conference, international experiences were presented not only from the perspective of regulator and overseer of the market, but also from the perspective of the institutions that offer these services. Special attention was also paid to the initiatives of banks and other financial institutions in the Albanian market.

BOX 6 PROJECTS WITH THE WORLD BANK IN THE PAYMENT AREA

Throughout 2016, the Bank of Albania continued to cooperate with the World Bank in the framework of implementing a project on measuring payment instruments costs. This project is based on the methodology created by the World Bank and aims to identify and measure all costs carried by the different payment instruments, in order to create a strategy for the efficient reform and development of the payment market.

Preliminary results succinctly identify physical currency as the most expensive payment instrument and credit transfers in electronic form as the cheaper. The project will be completed within 2017.

Following this cooperation, two other projects started during 2016, which also aim at promoting payment services from the perspective of remittances as well as promoting financial inclusion of the public with in these services. The following is the summarized information on these two projects:

1) Financial inclusion

The purpose of this project is to assess and draft a strategy of financial inclusion from the point of view of payments, which fundamentally will aim to provide to individuals a broader access of the payment offer in the Albanian market. To achieve the goals abovementioned, experts of the World Bank and representatives of the Bank of Albania have analysed the Albanian context from the point of view of infrastructural and institutional developments, as well as the legal and regulatory framework related with the area.

2) Remittances

This project is divided in two activities. The first activity aims to carry out an assessment of remittances in the international market, based on a methodology of the Bank for International Settlements (BIS). The second activity, named Greenback, is an instrument, which, through financial education, is expected to help building a closer relationship between individuals that send remittances and financial institutions.

At the current stage, the two projects are in the process of finalisation of the market analysis report, the identification of gaps and need for improvement and the drafting of a programme/strategy to achieve the abovementioned goals.



LIST OF LICENCED ENTITIES ACTIVE IN THE PAYMENT AREA

Institution	Licence number and date	Area of activity
Paylink sh.a.	Nr. 1 dt. 04.10.2013	Operator national scheme card payments
Unioni financiar i Tiranës sh.a.	Nr. 1 dt. 08.12.1999	Payment and money transfer services
Posta Shqiptare sh.a.	Nr. 3 dt. 18.04.2001	Payment and money transfer services
Ak - Invest sh.a.	Nr. 7 dt. 03.12.2003	Payment and money transfer services
NOA sh.a.	Nr. 9 dt. 06.06.2007	Payment and money transfer services
MPay sh.p.k.	Nr. 22 dt. 31.05.2011	Payment and money transfer services
Vodafone MPesa sh.p.k.	Nr. 31 dt. 25.03.2015	E-money institution
EasyPay sh.p.k.	Nr. 35 dt. 16.11.2015	E-money institution
Kastrati sh.p.k.	Nr. 36 dt. 10.03.2016	Payment and money transfer services
Pay and Go sh.p.k.	Nr. 37 dt. 18.03.2016	Payment and money transfer services

2.7 FOREIGN-EXCHANGE RESERVE MANAGEMENT

The Bank of Albania is the national authority responsible for maintaining and managing the foreign exchange reserve of the Republic of Albania. It uses its best opportunities to achieve and maintain a certain level of foreign exchange reserve, which support Albania's financial stability, and is in accordance with the monetary policy.

The Supervisory Council is responsible for approving the objectives of the foreign exchange reserve management. The primary objectives of this process are liquidity and security, whereas ensuring returns from reserve funds management represents the third objective, as long as it does not infringe the objective for liquidity and security. The Investment Committee approves the names of entities where foreign reserves may be invested. These names include the governments of USA, Japan, Great Britain and those in the euro area, as well as government-related agencies or institutions that are generally rated at least AA- (for euro area governments the accepted minimum rate is BBB-).⁴¹ The names of entities allowed for investment also include multilateral institutions or other institutions rated at least AA-.

FOREIGN-EXCHANGE RESERVE PORTFOLIO

At the end of December 2016, the stock of foreign exchange reserve was around EUR 2.944 million. The composition of foreign exchange reserves by currency was: USD 22.2%; EUR 62.7%; GBP 2.8%; JPY 2.4%; AUD 1.4%; SDR 6.1%; gold 1.9%; CNY 0.5%.

At the end of 2016, foreign exchange reserve is invested in liquid assets, mainly with maturities of 0-3 years. The share of time debt instruments with maturity over 5 years does not exceed 2.5% of the reserve portfolio. The portfolio managed by the external manager (World Bank), is invested against a reference portfolio of 0-3 years, mainly in debt instruments issued by the government.

⁴¹ Entities/ instruments listed up to BBB- are included in "Investment" category (investment grade).

