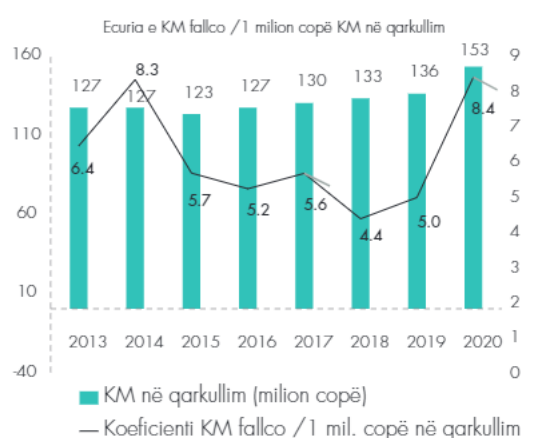


less than once a year. This coefficient is higher for 500 Lekë and 1000 Lekë banknotes (about 1.2 and about 0.78 respectively) and lower for 5000 Lekë banknote about 0.13, showing that the latter are returned more rarely to the cash desks of the Bank of Albania.

Bank of Albania aims to increase and strengthen technological and administrative capacities dedicated to protecting banknotes from counterfeiting

During 2020, despite the pandemic conditions, the Bank of Albania has carried out actions in view of safeguarding the currency from counterfeiting. These actions are preventative in nature, mainly focusing on testing and monitoring the processes of authenticating and sorting machines/equipment used by the professional staff. It is encouraged to identify and withdraw from circulation suspected banknotes and use authenticating and sorting machines/equipment successfully tested by the Bank of Albania. The public is recommended to verify the authenticity of the banknotes when accepting them based on the method "Feel, Look; and Tilt" published in the website of the Bank of Albania.

Chart 29. Counterfeited banknotes statistics



Source: Bank of Albania.

The quantity of counterfeited banknotes discovered in circulation has increased during 2020, meanwhile coins continue on the same trend compared with previous years. However, the coefficient of counterfeited banknotes per 1 million banknotes in circulation remains low.

By structure the 2000 Lekë and the 1000 Lekë denominations have the main share in the total counterfeit banknotes, followed by the 5000 Lekë and the 500 Lekë denominations. From the technical and/or technological aspect of counterfeiting Albanian banknotes, colour digital printings dominate, mainly ink-jet, accompanied by the use of additive artisanal and technological methods to imitate security elements.

2.7 PAYMENT SYSTEMS

Operation, oversight and reform of payment systems are some of the main functions of the Bank of Albania. Their implementation guarantees the security, sustainability and efficiency of the basic infrastructure of payments in lek. This is a crucial precondition for transmitting the monetary policy, safeguarding financial stability and the overall economic growth.

In fulfilment of these responsibilities, the Bank of Albania, beyond the stable operation of payment systems, has paid particular attention to the oversight and catalysing role in the fulfilment of the National Retail Payments Strategy.



2.7.1 PAYMENT SYSTEM OVERSIGHT

Throughout 2020, the Bank of Albania, in order to fulfil the oversight function of payment systems, finalised the overall evaluation of AIPS system according to the oversight principles of the European Central Bank. The evaluation process analyses and provides recommendations where necessary for all types of risks borne by the operation of the system, starting from the legal and governing risk, financial and operational risks, to including the transparency and objectivity of the system participation rules.

The evaluation of AIPS system was conducted with the support of the Central Bank of Italy in the framework of Twinning Project "Enhancing Bank of Albania's alignment with EU Acquis." The rules, procedures, and infrastructure of AIPS system is fully aligned with the standards of the Central European Bank and the provided recommendations are deemed to be easy to address. The positive results of this evaluation guarantee the stability of the core infrastructure of financial markets and are significant to the continued efforts on capital market developments.

The oversight of AECH system has also derived attention during the year, as an analysis was conducted on the fulfilment of recommendations given for the system evolution in 2018. The safety and efficiency guarantee of this system is quite important for the development and modernization of the small-value payments market, which is among the priorities of the Bank of Albania, in the framework of the National Retail Payments Strategy 2018-2023.

In the framework of regulating payment services, the Bank of Albania increased the efforts for the approval of the Law No. 55/2020 "On Payment Services," by the Parliament of the Republic of Albania²⁰, and intensified the work on drafting the bylaws for its implementation. The Bank of Albania has collaborated with the World Bank for drafting the regulatory framework. There has been collaboration with the Bank of Italy regarding specific components, such as Deep Customer Authentication and cybernetic security.

Measures have been taken in relation to drafting the legal act for the transposition of the European Union Directive "On payment accounts". This Directive, besides further encouraging transparency and competition through creating standardized procedures for transferring/switching the customer's account from one bank to the other, is expected to bolster the financial inclusion of people by presenting an account with basic characteristics. This type of account does not have a minimum cost for persons who currently do not have any access to banks.

Prior measures have been taken for the conduction of a survey, which has been sent to banks in relation to the financial inclusion and banking products

²⁰ Law "On Payment Services" approved on 30.04.2020.



offered by them. The information presented from this survey may help the Bank of Albania to draft the legal framework on the transposition of the Directive regarding the determination of fees for instruments and services relevant to these "accounts with basic features." The results of the survey have identified the fields where more detailed investigation may continue as regards the connection between opening a "payment account with basic features" and its impact to the financial inclusion.

The Bank of Albania has also initiated a series of projects for building and improving the infrastructure of the payment system such as: building the system for settlements in euro, where, during the year, the terms of references were finalised and the procurement of the system development has started; instant payment development which is drafting the project completion report in collaboration with the World Bank a Project; direct debiting function, while working for drafting a regulatory framework.

2.7.2 THE REFORMATORY ROLE OF THE BANK OF ALBANIA IN PAYMENT SYSTEMS

The Bank of Albania has continued its work for the implementation of the National Retail Payment Strategy in Albania (2018-2023). In 2020, a set of measures have been undertaken for implementing a considerable degree of the action plan of this strategy.

BOX 5 APPLICATION OF THE ACTION PLAN OF THE NATIONAL RETAIL PAYMENTS STRATEGY UP TO 2020

In the framework of monitoring developments in relation to National Retail Payment Strategy (2018-2023), the 6th meeting of the National Payment System Committee (NPSC), on 17 December 2020, presented the measures provided for in the action plan, short-term priorities, as well as a review of some deadlines on measures which are in process. This analysis, besides the support to NPSC for monitoring the fulfilment of objectives, aims to encourage transparency and accountability of the Committee. It must be emphasized that the fulfilment of strategy is ever more important due to the interconnection it has to both the national and cross border plan. More concretely, a series of measures forecasted in the strategy support the fulfilment of objectives of the Cross-institutional Working Group on Development and Electronic Commerce in Albania, National Strategy for Diaspora and Emigration, and it is part of the 10th reform of the Economic Reform Programme 2021-2023.

In this framework the conducted analysis identified that, up to now, over 50% of the forecasted measures in the action plan strategy were realised. The following analyses the measures achieved primarily in 2020.

- ***The approval of the Law "On the Payment Services"(PSD2) which transposes the reviewed EU Directive 2015/2366***



This Law, through re-dimensioning the non-bank financial activities which currently offer payment services and transfers (but including those that will potentially enter the market) and allowing the opening of bank accounts by them (currently forbidden by the legal framework in force "On Banks in the Republic of Albania" which classifies every credit surplus as deposit) and issuing of electronic payment instruments, will impact the increase in population that has an account to carry out payments. More specifically, if citizens currently use the Albanian Post Office, Western Union, Money Gram to conduct and receive payments, but cannot have an account in these institutions, the Law No 55/2020 "On the Payment Services" enables and encourages the use of electronic payments through these accounts. By taking into consideration the fact that these institutions have a geographical presence even in rural areas, the impact on financial inclusion will be high. The Law also creates possibility of collaboration between banks and non-bank financial institutions, which helps a larger presence of banks across the territory. The prudential framework for consumer protection provided by this Law will have an impact on financial inclusion. Also the spaces created by the innovative services will allow the larger public to use electronic payments daily.

The objectives achieved by the approval of the Law and the implementing bylaws fulfil the action plan measures as below:

1. Comprehensive regulation of agents and sub-agents for offering payment service and related services.
 2. Sustainable regulation of subcontracted services used by third parties in the entire payments sector, focusing specifically on using the technical service providers.
 3. Including regulation and supervision related to payment services in the legal framework.
 4. Creating a Consumer Protection Unit for payment services and more broadly.
 5. Creating a specific structure at the Payment Service Providers for addressing disagreements.
 6. Creating the banking concept that functions with an agent network.
 7. Encouraging competition and innovation in immigrants' remittances.
 8. Guaranteeing contracts that determine clear and applicable rights and obligations for service providers and users.
 9. Keeping an agent register used by banks and payment service providers. This register will be public and available to consumers.
- **Review the Regulation on the functioning of AIPS and AECH systems and the assessment of systems according to the supervisory principles of the Bank for International Settlements (BIS) and the European Central Bank (ECB), supported by the Bank of Italy.**

By reviewing the regulatory framework for the functioning of AIPS and AECH systems, where a series of findings and evaluations of the systems are reflected according to supervisory principles of BIS and ECB, a set of measures were fulfilled, as evidenced below:

1. Regulations and other rules on the entire infrastructure of the payment system in the Albania will guarantee direct and open access. Where necessary, legal reform will apply.
2. The operationalisation of the "indirect-participants" category of AECH.
3. Analysis of the ability to collateralise ex-ante / net debit positions caused



by participants of AECH. To also analyse the limits set for net debit positions of AECH participants.

4. Detailed assessment of AIPS and AECH based on CPMI-IOSCO of PFMI and the specific regulation of ECB: prepare a detailed self-assessment, conduct an external assessment. The payment systems operated by the private sector apply strict measures on risk management.
5. Assurance that payment service providers and payment service operators regularly review their cost and price structure (Home Banking).

- **Infrastructure developments**

1. Finalisation of the terms of reference for euro settlements and initiation of the procurement of system developments.
2. Draft of a regulatory framework on the functioning of Direct Debiting scheme.
3. In the framework of Instant Payment development an analysis/observation was carried out by banks in order to draft the report on project viability and the "ALBANIA: A Review of Implementation Options for Fast Payment System" report in collaboration with the World Bank.

In the framework of fulfilling its catalyst role, the Bank of Albania organised the VI²¹ meeting of the National Payment Systems Committee on December 2020. In this meeting, besides the presentations on fulfilling the National Retail Payment Strategy, as well as short-term priorities and the necessary measures for their realisation, a series of issues were addressed to support market developments. In relation to the creation of Open banking and Application Programming Interface (API) and the implementation of obligations of banks in compliance with the Law on Payment Systems, the experience of markets, which aim to maximise the effects against the reduction of investment needs, was presented. The membership of non-bank institutions in AECH system also derived attention. To address these topics, besides the members of the Committee, international institutions and companies were invited to attend the meeting, such as the World Bank, SWIFT, TIETO and CBI S.c.p.a.

2.7.3 THE OPERATOR ROLE OF THE BANK OF ALBANIA OF AIPS AND AECH SYSTEMS

The Bank of Albania has continued to play its crucial role in enhancing the normal functioning of payment systems, where the main infrastructure consists of AIPS²² and AECH²³ systems. This role has been important in promoting safety

²¹ https://www.bankofalbania.org/Pagesat/Komiteti_Kombetar_i_Sistemit_te_Pagesave/Mbledhja_e_Gjashte_Vjetore_e_Komitetit_Kombetar_te_Sistemit_te_Pagesave_17_dhjetor_2020.html

²² AIPS system is considered the core infrastructure for the settlement of payments in the national currency and of financial markets https://www.bankofalbania.org/Pagesat/Sistemi_nderbankar_i_pagesave_me_vlere_te_madhe_AIPS/

²³ AECH system which accommodates the clearing of interbank transactions by banks' clients (households and enterprises). https://www.bankofalbania.org/Pagesat/Sistemi_i_klerimit_te_pagesave_me_vlere_te_vogel_AECH/

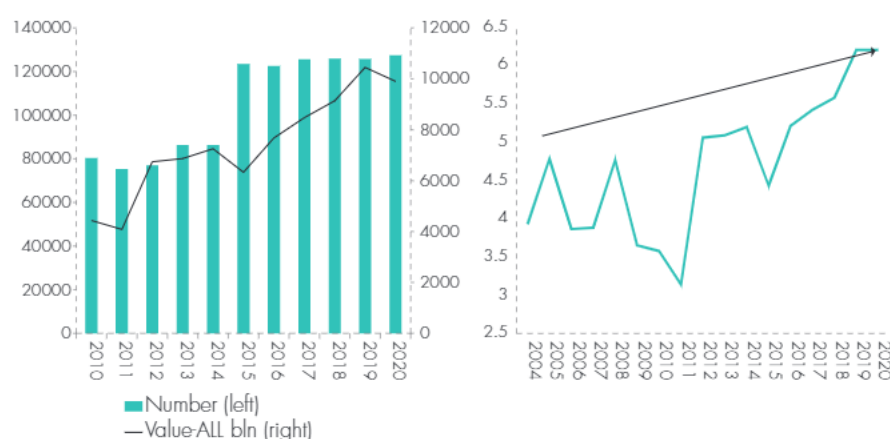


and efficiency, particularly in the first half of the year, taking into account the effect of "natural disasters" declared by the Albanian government. These two systems, administered and operated by the Bank of Albania, have continued to operate safely and efficiently. Both systems have offered maximum availability (99.66% for AIPS and 99.99% for AECH), and have always accommodated the needs of the market.

ALBANIAN INTERBANK PAYMENT SYSTEM FOR LARGE-VALUE PAYMENTS (AIPS)

A volume of 127,500 transactions was settled in AIPS, with a total liquidity circulating in the system of ALL 9,905 billion. Compared to the previous year, the volume and the value of settled transactions reflected an increase by 1.38% and a decrease by 5.24%, respectively. The value of transactions processed in AIPS in relation to the GDP is assessed at almost the same levels compared to 2019.

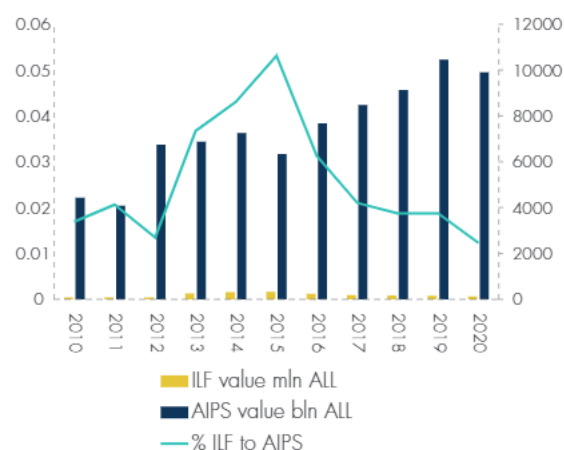
Chart 30. Number and value of transactions processed in AIPS (left) and the ratio of activities against GDP (right)



Source: Bank of Albania.

Referring to the use of this system by different transaction typologies, the item "Payments for Clients" (with main share of payments in terms of figures, 62.5%) continues to register increasing rates in both figures and value. On the other side, "Settlements in the AFISaR system" accounting for 25.6% of the total value of transactions processed in AIPS, registered a decrease of almost 3.4% in the number of transactions, and an increase in volume of 6.2% compared with the previous year.

Chart 31. Intraday Loan Facility (ILF) ratio to total value settled in AIPS



Source: Bank of Albania.



The Interday Loan Facility (ILF) registered a fall by 28.93% in terms of the number, and a rise by 26.1% in terms of value, driving to an increase of the average value per transaction. It must be noted that the decrease in the use of ILF through the years indicates a decline of the exposure of the system to liquidity risk.

ALBANIAN ELECTRONIC CLEARING HOUSE FOR RETAIL PAYMENTS (AECH)

The activity of the AECH reflected an increase, despite the situation created by the pandemic. In annual terms, the number and value of AECH payments have increased by 12.0% and 5.8%, respectively.

Chart 32. Number of AECH transactions in years (left) and the ratio of transactions processed in AECH to population over 15 years old (right). *



*It implies that 33.7% of the population over the age of 15 conducts an interbank transaction through the AECH system. This value marked a continuous increase which becomes relevant when taking into consideration the fact that in Albania around 40% of the population (Index 2014 assessment, World Bank) possesses a bank account for carrying out interbank payments.
Source: Bank of Albania.

The ratio of AECH transactions in relation to population has continued to increase, reflecting a greater usage of this system by the general public. The continuous increase of the use of AECH transactions, mainly payments for bank clients²⁴, indicates the efficiency of the measures taken by the Bank of Albania (in 2011 and also in 2020) on commissions applied by banks on the final user in order to expand the use of this system.

²⁴ The analysis of the payment distribution indicator according to the participants is evidence that customer payments initiated by banks continue to hold the main share of transactions processed in the AECH system, dominating the transactions initiated by other participants (Ministry of Finance and Economy, the Bank of Albania).



BOX 6 REVIEW OF THE REGULATORY FRAMEWORK OF AIPS AND AECH SYSTEMS AND MARKET IMPACT

In June 2020, the Bank of Albania approved the new regulations of AIPS and AECH systems. These reviews, among others, aim to address a series of market observations and further promote the measures foreseen in the National Retail Payment Strategy.

The main innovations of these reviews relate to the expansion of participations in the AECH system with non-bank financial institutions and the creation of well-defined requirements for cross-participating in both these systems, by aiming to address the risks carried on from these interconnections.

More specifically, the expansion of the participation of non-bank financial institutions, which offer payment services and electronic money, aims to encourage the interactivity among these institutions and banks. This enables these institutions to offer the most efficient services, which are provided mainly to the population category that does not have a banking approach. However, accommodating the participation of these institutions also creates added risks to the system, be it operational and financial, which was addressed through the clear determination of technical, operational and settlement conditions for the participants.

The review of the regulatory framework for the AIPS system aimed at creating the necessary conditions for the membership of private operators of licensed systems by the Bank of Albania. This enables various infrastructures to settle in the AIPS system including the ALREG operator, which functions as a Central Private Securities Depository and it is an important component to the functioning of the stock and capital markets.

The above-mentioned developments directly impact the increase in the activity of both systems as well as the risks carried on. In this framework, the regulatory reviews, besides the conditions determined to minimise risks, have consolidated the collaboration with a series of functions of the Bank of Albania, which relate to the stability and sustainability of these systems and the participants therein.

Lastly, the regulatory framework reviews addressed the need for a differentiation in commission between the system's payments initiated electronically and those in paper form. These reviews were based on the cost evaluation carried on by banks for their offer and reflected the objectives of the National Retail Payment Strategy on encouraging the use of electronic payments.

More specifically, the provisions of the regulatory framework provide the elimination of commissions for retail payments initiated electronically through home banking services for up to 20,000 Lekë and the differentiation of commission for the other payment part initiated through home banking for up to 50% of commissions applied for paper format payments. In this line, the Bank of Albania has determined the ceiling value for commissions applied by banks for payments processed in the AIPS and AECH systems, 1,500 and 500 Lekë respectively, since 2011. These ceilings will actually apply only for payments initiated in paper format.

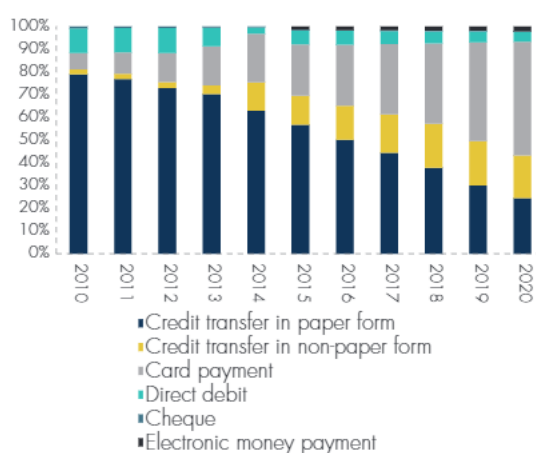
Encouraging the use of home banking services is necessary in the framework of promoting the innovation resulting from the implementation of the Law "On the payment services" and the Instant Payment project.



2.7.4 PAYMENT INSTRUMENTS

In 2020, the use of electronic payment instruments recorded an upward trend compared with the previous year. The reports of banks on payment instruments demonstrate that, up to year-end, there has been a continuous expansion of electronic payments such as bank cards and electronic money payments (pre-paid cards), as well as home banking.

Chart 33. Volume of payment instruments in years.



Source: Reports submitted by banks according to the "Methodology for reporting payment instruments"

The volume of payment instruments has increased by 18.5%, reaching a total level of around 22.06 million payments, while the total value of payments has slightly decreased by 2.9%.

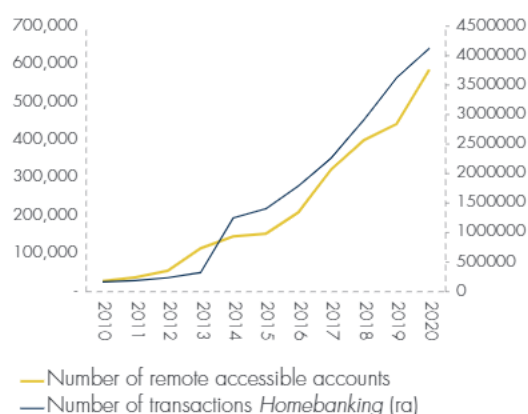
In terms of instruments used, the payment analysis indicates a continuous expansion of electronic payments. Card payments are the main payment instruments accounting for 50.1% of the volume, surpassing for the first time credit transfers in paper form. This increase is also due to movement restrictions during the pandemic.

E-money payments, a relatively new payment instrument, are being used exclusively by individuals, than businesses. Meanwhile, the same trend is noted in card payments, which continue to be used more

by individuals than businesses (with a usage ratio of 97.2% for individuals and 2.8% for businesses). On the other hand, businesses continue to reflect a more traditional use of banking (credit transfer in paper form, non-paper, cheques etc.) compared with individuals.

HOME BANKING

Chart 34. Volume of home banking transactions and account numbers offering these services



Source: Reports submitted by banks according to the "Methodology for reporting payment instruments"

The initiation of credit transfers in electronic form is realised through "home banking" services, which are provided by 11 of the 12 banks that operate in Albania. These services are both increasingly widespread in the Albanian market, and used to carry out payments, not only for basic information services for the account, but also for on-line payments.

In 2020, there was a significant increase in the volume of home banking payments, by 13.7%, and of the value of these transactions by 8.8%, compared to the previous year. Contributions to the upward trend of home banking were assessed to be the measures undertaken by the Bank of Albania and the policies



of banks, in the framework of promoting these alternative payment means. These measures were reflected in an increase in remote accessible accounts by 32.6% and an increase, against the total account, of 19.8%.

From the point of view of the use of internet accessible accounts, until the end of 2020, there were 7.03 transactions in non-cash payments per account, further approaching the level aimed by the National Strategy for Retail Payments (of 10 non-cash payments per capita by the end of 2022).

BANK CARDS

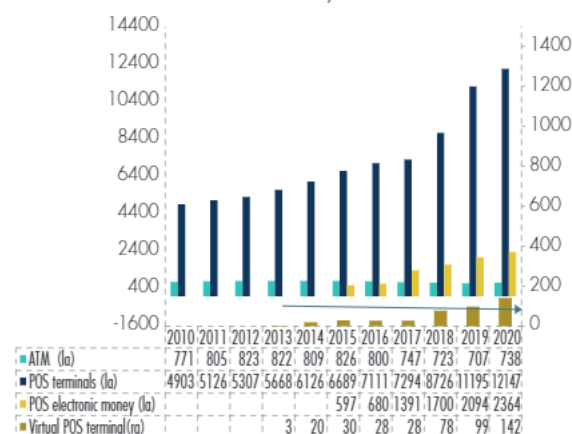
At the end of 2020, all the banks that operate in the Republic of Albania were licensed as card issuers, of which seven were licensed also as card accepters. The infrastructure provided by these banks has trended upward in terms of the number of POS terminals (increasing by 8.5% compared with 2019). Despite the positive trend of the increase of the number of POS terminals, reflected in the POS report per 1.000.000 citizens (4268 in 2020), their concentration continues to remain high in the region of Tirana²⁵, at 88.5%

A considerable increase was experienced by the virtual POS terminals, by means of which card payments could be done online for the purpose of electronic commerce. The banking system has offered such services since 2013, but the pace of use expansion by traders who want to conduct electronic trading, has been quite moderate. Meanwhile in 2020 the virtual POS terminals increased by 44. The development of this infrastructure is quite welcome in the framework of promoting the use of electronic payments. The implementation of the Law No 55/2020 "On Payment Services" will also have a positive impact in this regard.

At the end of 2020, the number of ATMs has increased at 738, compared with 707 terminals in 2019²⁶. Although ATMs are used mainly for cash withdrawal, in 2020 there was an expansion of ATM functions for carrying out deposits and transfers.

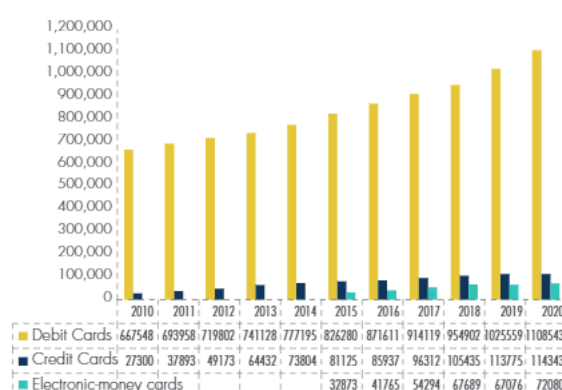
Positive developments were shown for ATMs, the use of which increased, to 12.9%, compared to the end

Chart 35. Performance of ATM and POS terminals across the years.



Source: Reports submitted by banks according to the "Methodology for reporting payment instruments"

Chart 36. Developments in debit and credit cards



Source: Reports submitted by banks according to the "Methodology for reporting payment instruments"

²⁵ Division of districts by branches of the Bank of Albania.

²⁶ At the same time, the number of banks fell from 14 at end-2018, to 12 at end-2019.



of 2019. Bolstering the use of electronic money instruments is estimated to have an impact on the financial inclusion of the population by enabling access to banking services from categories of the population that are not able access other services.

In 2020, the issue of debit cards increased by 5.6% and the issue of credit cards decreased by 4.3%. Also, the functioning of electronic-money cards in the market increased by 7.5% compared with the previous year.

Electronic money products, based on the legal and regulatory framework of the Bank of Albania, are also provided by non-bank financial institutions licensed as Electronic Money Institutions. Currently, in the Albanian market, three electronic money institutions are operating. In 2020, these institutions together have conducted a volume of around 3.8 million electronic money payments, with a value of ALL 10.8 billion.

The electronic money, although trending upwards, remains at low levels, but it creates a value added to that part of population that does not access bank accounts. The licensing of the Albanian Post is a very positive development in the electronic money market of non-banking financial institutions. This institution has expanded its presence in the territory of the Republic of Albania.

2.8 INTERNATIONAL RESERVE MANAGEMENT

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

The Regulation "On the policy and management of the international reserve", approved by the Supervisory Council, lays down the purposes of maintaining the international reserve. In compliance with the best international practices, the purpose of maintaining the international reserve is implementation and support of monetary policy and exchange rate policy, as well as safeguarding of financial stability. The primary objectives of international reserve management are liquidity and security. Ensuring returns from reserve funds management represents a third objective, as long as it does not infringe the objective for liquidity and security. The Supervisory Council also approves the qualitative principles and criteria for the development of international reserve management. In order to implement these criteria, the Investment Committee approves the quantitative indicators and follows the application of the investment policy through the periodical publications.

During 2020, several amendments were endorsed in the Regulation "On the policy and management of the international reserve". The main purpose of

