Bank of Albania

Monetary Policy Department

Business and Consumer Survey results

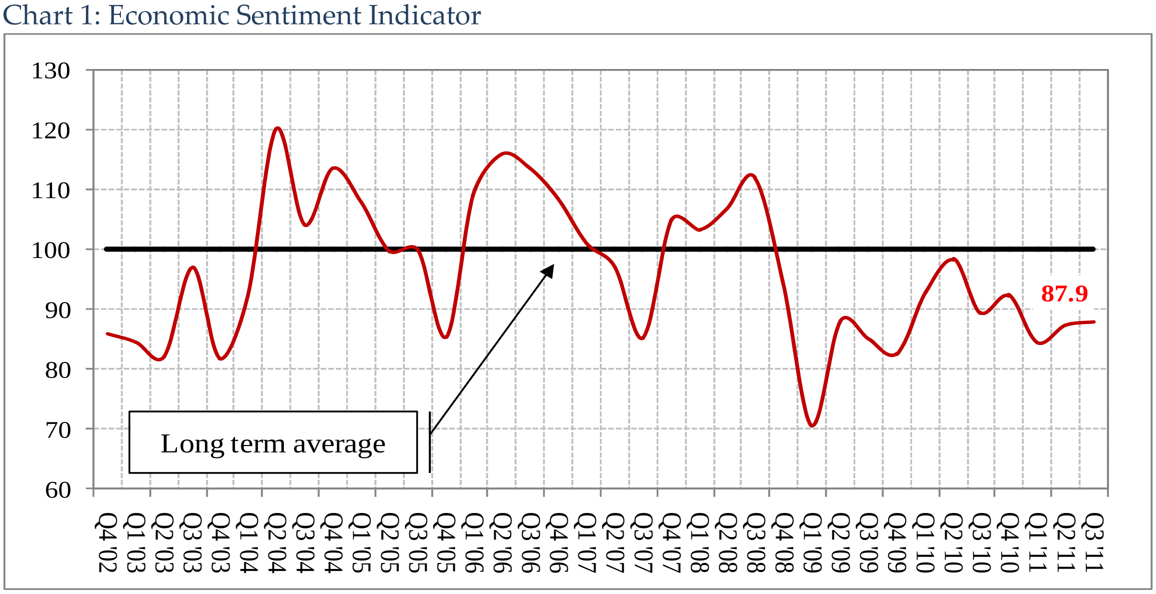
October 2011

Economic Sentiment Indicator[1]

Economic Sentiment Indicator (ESI) increased by 0.6 pp in the third quarter of 2011. The current ESI (87.9) stands 12.1 percentage points below the long-term average.

Improvement in ESI was driven by the positive developments in its components. The improvement of confidence in services, industry and construction affected positively ESI. The increase in consumer confidence provided the same impact.

Chart 1: Economic Sentiment Indicator



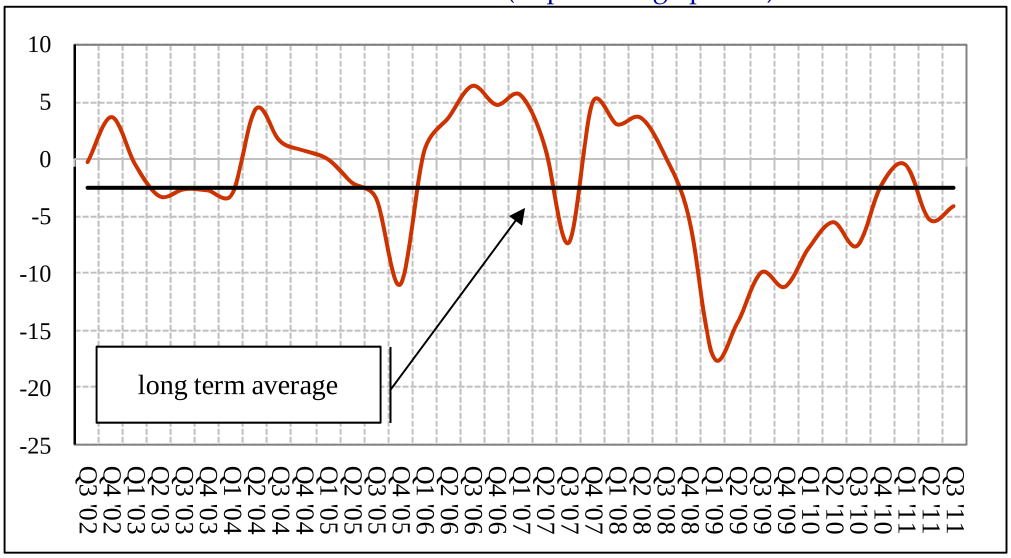
Source: Business Confidence Survey and Consumer Confidence Survey, Bank of Albania

[1] Starting from the second quarter of 2011, two amendments have taken place in business confidence indicators: (i) the sample, based on which the Services Confidence Indicator (SCI), increased by 200 firms which operate in the sector, excluding trade; (ii) with regards to trade, ia new sample has been constructed and we are working to build up a specific confidence indicator. Currently, trade-related sector is excluded from ESI.

Industry

Industrial Confidence Indicator (ICI) improved slightly by 1.2 percentage points in the third quarter of 2011, after the deterioration in the previous quarter. ICI stands 1.7 percentage points below its long-term average during this quarter. The ICI improvement is mainly attributable to the less negative assessment of *industrial production* situation, whose balance rose by 7.6 percentage points. The growing of *inventories and the* deterioration of *employment situation* in industry provided a negative contribution to the aggregated indicator.

Chart 2: Industrial Confidence Indicator (in percentage points)



Source: Business Confidence Survey, Bank of Albania

<u>The following provides an analysis of selected indicators not included in the construction of ICI:</u>

Industry related businesses, report a decline in the total *economic performance* and in the *overall situation of their businesses*, during the third quarter of 2011. Although, the balances appear negative, they improved by 1.5 and 6.0 percentage points, respectively, compared to the previous quarter. All factors restricting industry-related businesses activity provided a lower effect compared to the second quarter of 2011. In particular, *energy supply problems, corruption, informal economy, public order and security* at home and the *internal political situation* decreased the negative impact on industry-related businesses activity. On the other side, the *legal framework and its implementation* have restricted the conduction of normal activity within this sector to a higher extent.

The *domestic demand* for industrial products continued to be negatively assessed during the third quarter of 2011, albeit lower compared with the previous quarter. On the other side, *foreign demand* was assessed as positive for the same period. Industrial-related businesses reported an increase in *product prices* in the third quarter of 2011. Respective balance stood at 10.9% from 9.4% in the quarter ahead. In line with the developments of demand and prices, industry-related businesses' *financial situation* continued to deteriorate in the third quarter of 2011, although at a lower level compared with the quarter ahead.

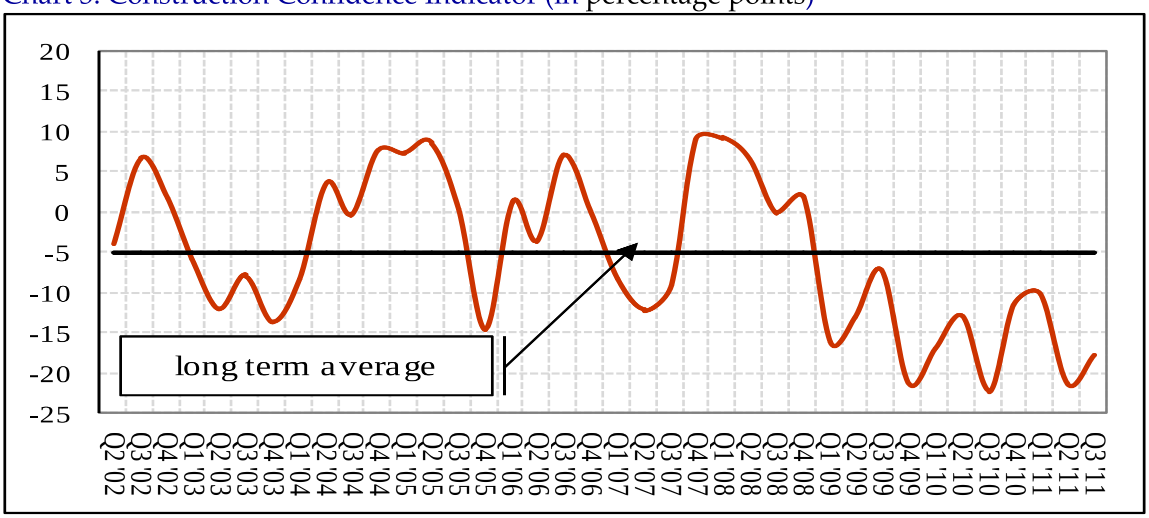
Capacity utilisation rate in industry has slightly dropped by 0.5 percentage points, pointing to 72.4% in the third quarter of year 2011. This rate is about 1.7 percentage points higher than its long-term average. About 70.9% of this sector-related business thinks that the current utilisation rate of production capacities is sufficient considering the current demand and expectations regarding orders for the next 12-month period. Accordingly to 9.7% of businesses, the current utilisation rate of production capacities is insufficient.

Expectations for the fourth quarter of year 2011 are optimistic. Industry-related businesses expect an improvement in the *business' overall situation*, an increase in both *domestic* and foreign *demand* and a fall of *inventories*. Furthermore, businesses expect growth in *production* and improvement in the *employment situation* during the fourth quarter of year 2011.

Construction

Construction Confidence Indicator (CCI) improved by 3.5 percentage points during the third quarter of 2011. Notwithstanding the slight improvement in the current quarter, CCI continues to be deeply negative. Developments in CCI were attributable to the lower negative assessment of *employment situation* and *demand* by the construction businesses. *Production* in construction continues to be negatively assessed and almost at the same level with the second quarter of year 2011. Current CCI level stands 12.8 percentage points below its long-term .

Chart 3: Construction Confidence Indicator (in percentage points)



Source: Business Confidence Survey, Bank of Albania

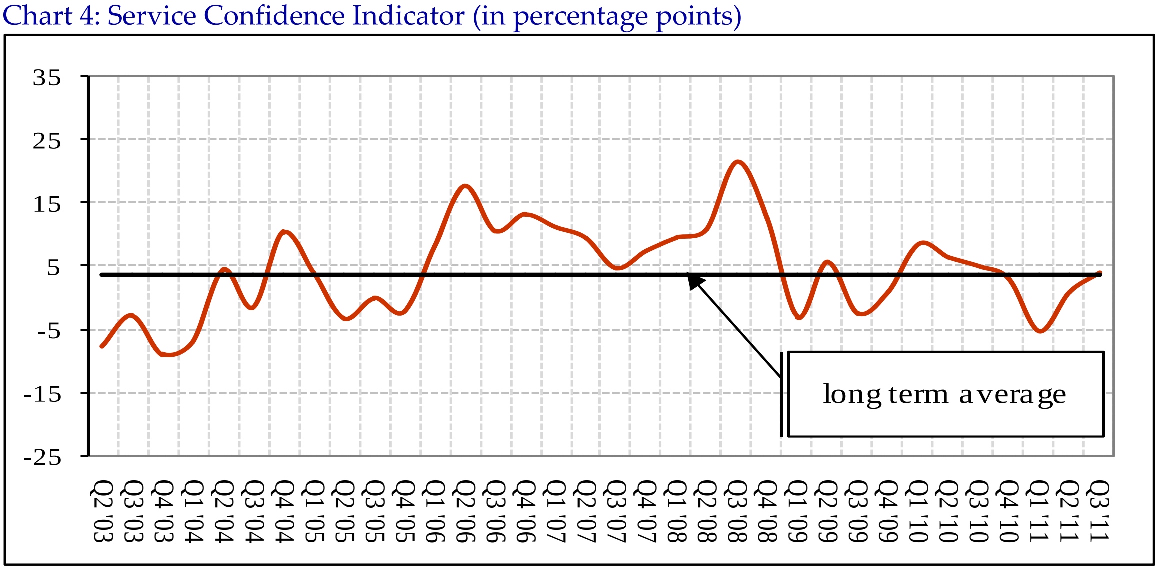
<u>The following provides an analysis of selected indicators not included in CCI construction:</u>

Construction-related businesses decreased their assessment concerning the *overall economic situation at home*, in the third quarter of year 2011, and continued to negatively assess *their business' overall situation*. The fall of optimism of businesses in this sector is due to the negative impact of problems related with the *legal framework* and their *implementation*, *corruption* and *the informal economy*. The problems related to *energy supply, relationships with* *banks and domestic political situation are* assessed to hamper the normal activity of the industry-related businesses at a lower degree compared to the previous quarter. .

Notwithstanding the negative assessment of production, construction-related businesses reported that *capacity utilisation rate in construction* stands at 66.9% in the third quarter of 2011, only 0.2 percentage points below its long-term average. This rate is about 0.7 percentage points higher compared with the quarter ahead. Over the third quarter of 2011, about 64.3% of firms stated that the current capacity utilisation rate is sufficient, considering the demand level and order contracts for the next 12-month period. Meanwhile, about 18.5% of this sector – related businesses report that this level is insufficient. Businesses assess that the *demand insufficiency* and the *financial limitations* are the main factors influencing thil level of capacity utilasation. In the third quarter of 2011, sector-related businesses reported an increase of *production prices* and a *rise of inventories.* The financial situation in this quarter has been negatively assessed to a lower degree compared to the previous quarter.
Expectations regarding various aspects of business, such as output, demand and employment, remain positive in the fourth quarter of year 2011. Construction–related businesses expect positive developments in their activity during the fourth quarter of year 2011.

Services
Services Confidence Indicator (SCI) rose by 3.0 percentage points in the third quarter of year 2011. The SCI recovery during this quarter is attributable to the developments in its three composing balances.

Chart 4: Service Confidence Indicator (in percentage points)



Source: Business Confidence Survey, Bank of Albania

The assessment about the *financial situation* provided the main contribution to the improvement of this indicator. This balance stands at 10.0%, 7.3 percentage points higher than the previous quarter. The positive assessment of businesses regarding *employment situation*, contributed positively to the climbing up of confidence indicator, even if it was slightly lower compared to the previous quarter (0.1 percentage points),. The businesses' *overall situation* balance improved by 1.8 percentage points in the third quarter, albeit remaining negative. Currently, SCI stands at 0.3 percentage points higher than its long-term average, for the first time since the third quarter of year 2010.

The following provides an analysis of selected indicators not included in the construction of SCI:

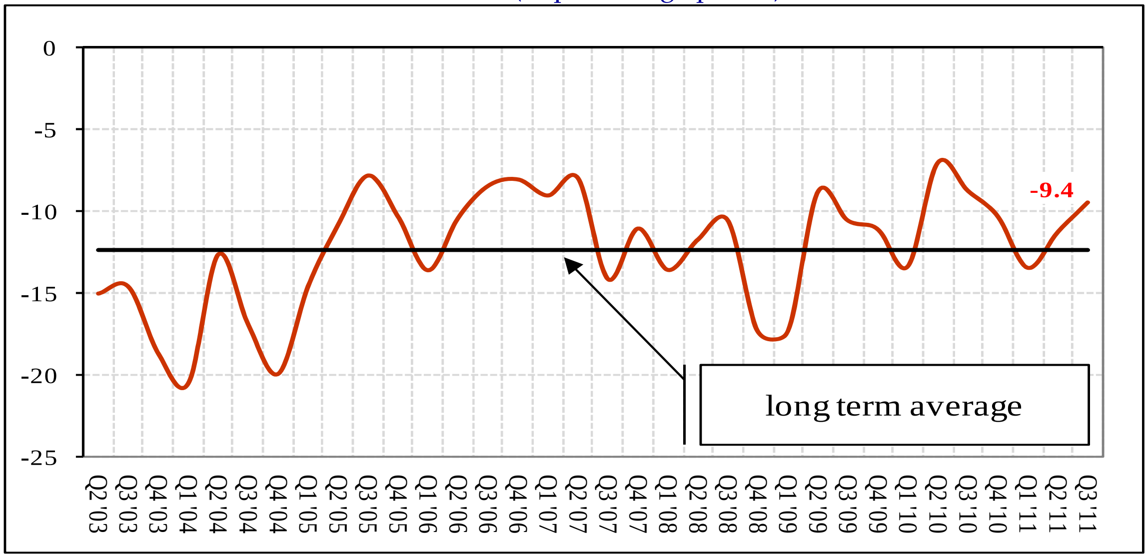
Service-related businesses assess as negative the *overall economic situation at home* in the third quarter of 2011. The respective balance fell by 3.7 percentage points compared with the quarter ahead. The l*egal and institutional framework* is considered as the main factor hampering the normal activity in services. Other factors, such are the *political climate at home, corruption and informal economy* had a lower impact on the restriction of normal activity of services compared to the previous quarter.

Demand in services sector continued to be negatively assessed during the third quarter of year 2011 as well. Its balance stood at -1.6%, slightly lower compared with the previous quarter. Services-related businesses assess that *prices* in this sector have been increasing. Respective balance increased to 5.1% from 2.9% in the previous quarter. *Capacity utilisation rate*, over the third quarter of year 2011, stood at 78.5%. This rate is about 3.9 percentage points higher than in the previous quarter and about 3.5 percentage points higher than the long-term average.
Services sector businesses are optimistic concerning the *firm's economic activity*, during the fourth quarter of year 2011. Expectations regarding the *overall economic situation* and the *demand* remain positive, albeit lower than in the previous quarter.

Consumer Confidence

Consumer Confidence Indicator (CCI) climbed up in the third quarter of 2011 for the second consecutive quarter. After the increase by 2.2 percentage points in the second quarter, CCI rose by 1.8 percentage points in the third quarter. The improvement of consumer confidence during this quarter is mainly attributable to the improvement of the balance of *purchases of major items.* Although negative, this balances, in the current quarter, improved by 10.4 percentage points. The balance concerning *current financial situation* of families, maintained the same level as in the quarter ahead. The drop of expectations' balance about the *financial situation of families* in the next quarter provided an opposite impact. Its balance stood at 6.3%, descending by 1.5 percentage points compared to the previous quarter. The lower and negative assessment of the overall economic situation for the fourth quarter of 2011, negatively contributetd to the increase of CCI.

Chart 5: Consumer Confidence Indicator (in percentage points)



Source: Consumer Confidence Survey, bank of Albania

<u>The following provides an analysis of selected indicators, not included in the construction of CCI:</u>

The consumers' assessment of the *families' financial situation* and the *overall economic situation at home,* in the third quarter of 2011, was less negative compared to the previous quarter. The respective balances stood at -1.2 and -7.4%, improving by 4.9 and 6.0 percentage points. The *average living cost* remained unchanged compared to the previous quarter. *Prices* are expected to rise in the next quarter and to somewhat increase during the next 12- month period. Consumers expect *unemployment rate* to turn down during the second half of year.

Consumer's expect the inflation rate to be 2.22% within the next 12 months. This value is 0.2 percentage points higher than the one otf the previous quarter.

Table 1: Indicators of Confidence by sectors *

	Values since Q2-2002			**2010**				**2011**			**Current situation**	
	Min.	**Ave.**	**Max.**	**Q1**	**Q2**	**Q3**	**Q4**	**Q1**	**Q2**	**Q3**	**Conjectural****	**Structural*****
Industry	-18.0	-2.5	6.1	-7.8	-5.6	-7.7	-2.4	-0.6	-5.4	-4.2	↑	-
Construction	-21.8	-5.2	9.4	-17.0	-12.8	-22.2	-11.6	-10.2	-21.2	-17.7	↑	--
Services	-9.5	3.7	21.3	8.4	6.5	4.9	3.0	-5.1	1.0	3.9	↑	+
Consumer	-20.5	-12.3	-7.0	-13.4	-7.0	-8.7	-10.3	-13.4	-11.3	-9.4	↑	+

Source: Consumer Confidence Survey, Bank of Albania.

**) Excluding the Consumer Confidence Indicator, the balances are seasonally adjusted.*

***) The situation compared with the previous quarter.*

****) The situation for each indicator is regarded as very satisfactory (+ +) when the index is more than 1 standard deviation higher than the average; the situation is considered as satisfactory (+)when the index is less than 1 standard deviation higher than the average; the situation is considered as unsatisfactory (-)when the index is less than 1standrad deviation lower than the average; and the situation is considered as highly unsatisfactory when the index is more than 1 standard deviation lower than the average. .*

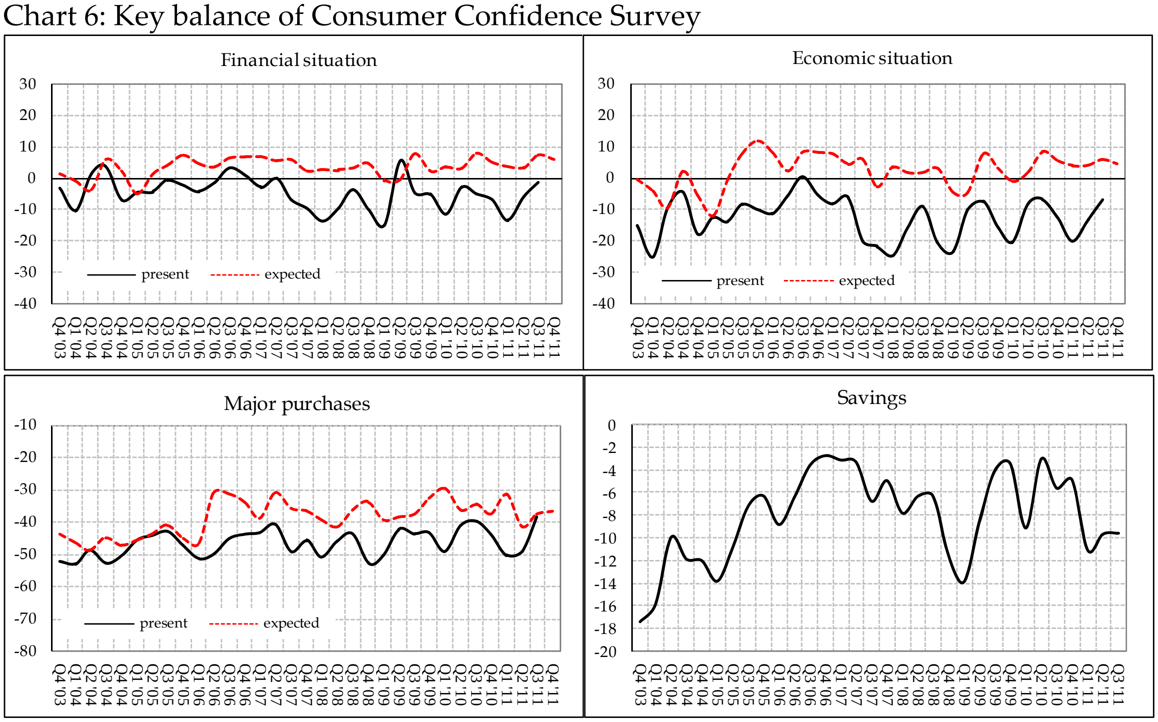
Table 2: Key balances of the sectors of the economy (in percentage points)*

	2010				2011			
	Q1	**Q2**	**Q3**	**Q4**	**Q1**	**Q2**	**Q3**	**Q4-expectations**
Demand								
Total	-3.2	-2.7	-5.8	-1.3	-4.4	-10.5	-8.1	18.7
Industry	-9.7	-5.3	-11.3	-2.6	0.7	-8.2	-6.2	19.8
Construction	-22.7	-13.8	-23.3	-11.2	-9.3	-28.0	-23.1	12.0
Services	7.9	3.3	4.1	3.7	-3.7	-3.0	-1.6	21.5
Business' overall situation								
Total	0.0	-0.8	-4.1	-3.2	-7.4	-9.3	-5.3	17.4
Industry	-12.2	-10.2	-9.8	-6.0	4.1	-8.7	-2.7	17.3
Construction	-16.2	-11.6	-22.8	-13.8	-7.7	-25.4	-17.9	10.2
Services	11.4	7.1	6.4	2.7	-10.7	-1.9	-0.1	20.8
Production								
Total	-13.7	-9.6	-15.2	-6.3	-0.4	-13.9	-10.1	15.4
Industry	-11.5	-7.0	-9.8	-1.0	7.4	-7.7	-0.1	15.8
Construction	-15.1	-11.2	-18.7	-9.8	-5.4	-17.9	-16.5	15.2
Consumers								
Financial situation	-11.4	-2.7	-4.8	-7.0	-13.4	-6.0	-1.2	6.0
Prices after 1 year, in %	2.2	2.1	2.2	2.2	2.3	2.0	2.2	…
Major purchases	-49.2	-41.1	-39.8	-43.9	-50.3	-49.0	-38.6	-36.7
Savings	-49.4	-42.8	-43.9	-44.2	-50.5	-46.0	-45.6	-41.0

Source: Consumer Confidence Survey, Bank of Albania.

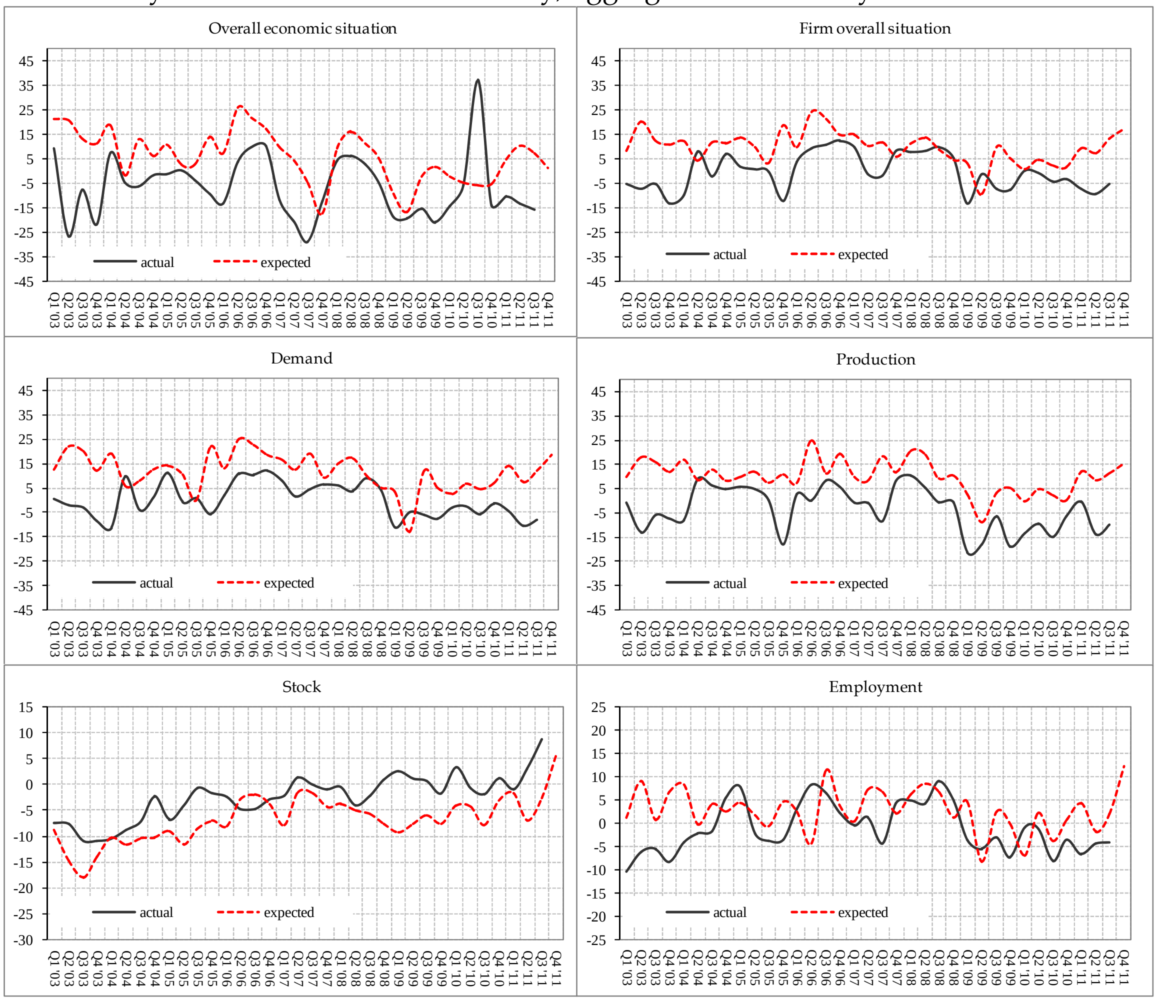
**) Excluding the Consumer Confidence Index, the balances of other indices are seasonally adjusted.*

Chart 6: Key balance of Consumer Confidence Survey



Source: Consumer Confidence Survey, Bank of Albania

Chart 7: Key balances of businesses survey, aggregated at economy level



Annex

Methodological explanatory notes

-**Balance** is the indicator more frequently employed in aggregating the qualitative data of surveys. It is estimated as a difference between the percentage of positive and negative responses. The balance is stated in percentage points.

-**Confidence Indicator** (CI) is produced for each of the surveyed sectors and is calculated as the simple average of seasonally adjusted balances of those indicators, which have the highest correlation with the reference series (the real data series of the economy).

-Economic Sentiment Indicator (ESI) is composed of 13 balances used for the construction of confidence indicators for the four economy sectors, weighted according to their activity. The ESI tracks by a single indicator the sentiment on the country's economic activity obtained from the two principal economic groups, businesses and consumers.