

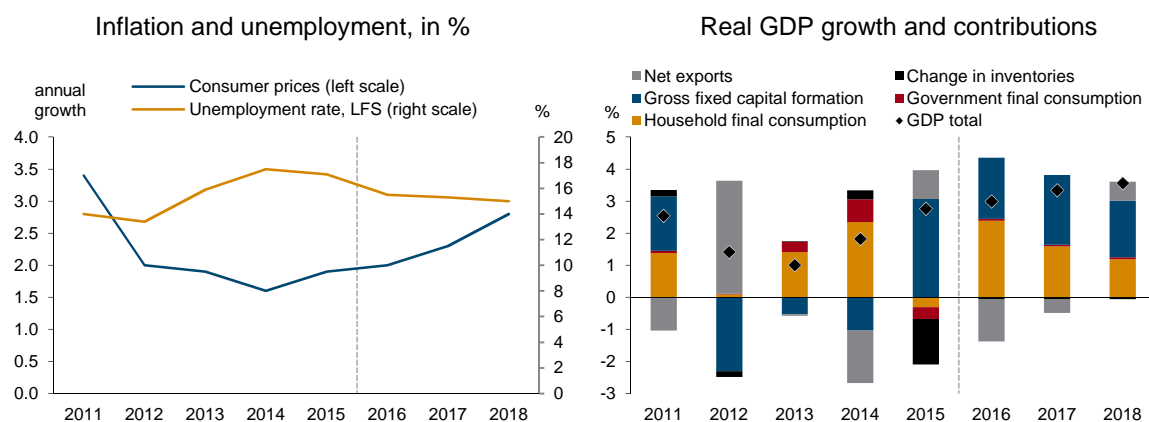


ALBANIA: China, the new old strategic partner?

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Buoyant household consumption and private investment have had a positive impact on the acceleration of GDP growth, whereas sluggish external demand for Albanian products partly attributable to shrinkage in oil and mineral exports has had the opposite effect. Fiscal consolidation has for the most part been backed by containment of expenditures and a rise in revenues. Based on expectations of vigorous domestic demand, we have revised our forecast upwards slightly to 3.0%, 3.3% and 3.6% for 2016, 2017 and 2018, respectively.

Figure 23 / Albania: Main macroeconomic indicators



Source: wiiw Annual Database incorporating national and Eurostat statistics, own calculation. Forecasts by wiiw.

The political turmoil during summer 2016 ended up with the judicial reform finally seeing green light from the parliament. The reform was unanimously voted by the governing and the opposition parties under the constant pressure put forth by the international partners. The reform aims to combat the high corruption in the judiciary system. Besides it is one of the key conditions for the opening of EU membership negotiations. In the medium and long run, the reform is expected to improve law enforcement and the business climate as well as to assure fairer competition. Currently, the political debate is centred on a law on 'integrated management of waste', the latter to be imported from the European Union. The law had been repealed in October 2013, but was relaunched in September this year by the current government; it has encountered a lot of resistance on the part of the civil society, environmentalists but also ordinary citizens. They are sceptical about the hazardousness of the waste

that will enter the country and the ability to properly control it, and are trying to get through a referendum on the issue.

In economic terms, for the first half of 2016, compared with the same period in 2015, a rise in overall domestic demand of 3% stimulated the economy to grow at a similar rate. With reference to the same period, exports continued to be oriented mainly towards services and less towards goods – in nominal terms the former increased by 13% while the latter dropped by 26%; low international oil prices continued to affect negatively the mining industry; gross fixed capital formation grew by 5% in real terms while foreign direct investments, despite a fall by 12% in euro terms, still poured in at a level which corresponds to 72% of the current account deficit.

Household consumption rose by 2.8% during the first half of 2016, year on year, partly due to low inflation, but also owing to the upsurge in employment by 0.9 pp, to 48.4%, and the fall in unemployment by 1.8 pp, to 15.5%, partly attributable also to the government campaign against informality. Even though emigrants transferred less remittances, -5% in the first half of 2016, year on year, still these stood at a remarkable 5% of GDP.

In fiscal terms, consolidation has characterised public finances until August 2016. For the first time since 2008 a budget surplus of 2.2% of GDP has been achieved for the first half of 2016, triggering a reduction in the public debt to GDP ratio from 72% to 70.8%. Until August, on a year-on-year basis, revenues increased by 7%: the collection improved especially in VAT, profit, and personal income and excise taxes. For the same time span, on a year-on-year basis, expenditures were cut by 4.8%. The shrinking occurred mainly on account of arrears and to a lower extent due to interest payments, wages and social benefits, whereas capital expenditures almost stagnated. According to the national accounts, final government consumption has been on the positive side but rather flat for the first half of 2016. The budget revision in July 2016 was characterised mainly by a reallocation of expenditures towards covering recently generated arrears (between January and April 2016 amounting to LEK 1,383 million). Moreover, the general elections to be held in mid-2017 hint at the possibility of government spending to slightly accelerate for the rest of the year.

In monetary terms, the monetary easing of central bank has been preserved also in 2016 with a policy rate maintained at a low level of 1.25%. Until August, the level of overall loans stagnated, year on year. Still, total new loans to businesses slowed down by 2.1%. Such a tendency among businesses can be partly explained by tighter credit standards applied to businesses. It is also reflected in the deterioration of confidence indicators for the industry and trade sectors. In contrast, new loans to households moved up by 11.5% in the first eight months of 2016 as compared to the same period a year earlier. The consumer confidence indicator also improved. In terms of currency, new loans in domestic currency grew, both for businesses and households. In contrast, new loans in foreign currency fell, lowering the exposure to exchange rate risks. Non-performing loans have started to move up again, to a level of 21% of total loans in the first half of 2016. The further increase in NPLs is also attributable to the bankruptcy of Kurum Albania early this year: one of the biggest steel producing companies in Albania belonging to the Kurum Holding Group, based in Turkey. Already in 2015 a new strategy and a new bankruptcy law, aiming to better deal with NPLs, were drafted under the technical assistance of the IMF. However, a further deterioration of NPLs is not excluded if the law and the strategy do not become effective.

As concerns external demand, exports continue to be driven mainly by the textile and garments industry, with a share of 45% and an increase of 21% year on year in January to August 2016. In contrast, in the same period exports of minerals, fuels and electricity declined by 13% in real terms and by 39% in nominal terms. Despite the sharp decline in nominal terms, the increase in real terms by 2% experienced during July-August 2016 indicates some recovery of the sector. The recent changes reflect the moderate rise in international oil prices which started in the second quarter of 2016. In contrast, imports increased by 8%. In particular, the 18% rise in import of machinery and equipment points to a further recovery in private investments.

A further stabilisation of international oil prices might reverse the decline in exports of minerals, fuels and electricity. Bankers Petroleum, the main oil producer, has entered into an agreement with the Albanian government to sell up to 65% of its crude oil in the domestic market. At the same time the Chinese government has approved an arrangement between the Canadian Bankers Petroleum and the Chinese Geo-Jade Petroleum Corporation about the acquisition of the former by the latter. The acquisition by the Chinese company 'China Everbright International Limited' of the Tirana International Airport in early October 2016 points to an increasing influence of China in strategic sectors of the Albanian economy. (These developments are reminiscent of the close alliance Albania and China had between the late 1950s and the late 1970s.) Foreign direct investments, despite the setback in the first half of the year, are expected to regain importance for the Albanian economy especially through two key infrastructure projects: the TAP (Trans Adriatic Pipeline) and the Devoll Hydropower station project which are moving forward.

All in all, the recent GDP growth acceleration has been fuelled by buoyant household consumption and private investments, but dragged down by sluggish external demand partly attributable to oil and mineral exports shrinking in nominal and real terms. The magnitude of external imbalances will continue to depend largely on the oil price; some optimistic signals in this respect have started to become evident with the recent dynamics. Fiscal consolidation is ongoing and is backed by a rise in revenues but also a slight restraint on expenditures. Based on expectations of stronger domestic demand (household consumption and private investment), our forecasts are that the economy will grow by 3.0%, 3.3% and 3.6% in 2016, 2017 and 2018, respectively.

Table 6 / Albania: Selected economic indicators

	2012	2013	2014	2015 ¹⁾	2015 January-June	2016	2016 Forecast	2017 Forecast	2018
Population, th pers., average	2,900	2,897	2,894	2,889	.	.	2,886	2,880	2,870
Gross domestic product, ALL bn, nom.	1,333	1,350	1,394	1,436	699	721	1,500	1,600	1,700
annual change in % (real)	1.4	1.0	1.8	2.8	2.7	3.1	3.0	3.3	3.6
GDP/capita (EUR at exchange rate)	3,300	3,300	3,400	3,600	.	.	3,800	4,000	4,300
GDP/capita (EUR at PPP)	7,800	7,700	8,300	8,600	.	.	.	.	.
Consumption of households, ALL bn, nom.	1,032	1,074	1,130	1,141	576.6	596.0	.	.	.
annual change in % (real)	0.1	1.8	3.0	-0.4	-2.0	2.8	3.0	2.0	1.5
Gross fixed capital form., ALL bn, nom.	353	352	343	391	166.3	176.6	.	.	.
annual change in % (real)	-7.9	-2.0	-4.0	12.5	15.4	5.2	7.0	8.0	6.5
Gross industrial production									
annual change in % (real)	15.7	28.3	1.6	-5.0	-2.2	-12.7	-7.0	1.0	2.0
Gross agricultural production ²⁾									
annual change in % (real)	5.7	-3.4	2.0	2.9	.	.	.	.	.
Construction output total									
annual change in % (real)	-11.4	-13.0	5.0	19.3	20.1	1.7	.	.	.
Employed persons, LFS, th	1,140	1,024	1,037	1,087	1,075	1,139	1,150	1,170	1,180
annual change in %	-1.8	-10.2	1.3	4.8	7.0	6.0	5.8	1.7	0.9
Unemployed persons, LFS, th	176	194	220	224	219	217	210	210	210
Unemployment rate, LFS, in %	13.4	15.9	17.5	17.1	17.0	16.0	15.5	15.3	15.0
Reg. unemployment rate, in %, end of period	12.8	13.5	13.0	12.9	13.8	10.7	.	.	.
Average monthly gross wages, ALL	37,534	36,332	36,997	38,077	.	.	39,200	41,700	42,000
annual change in % (real, gross)	0.9	-5.0	0.2	1.0	.	.	1.0	4.0	2.0
Consumer prices, % p.a.	2.0	1.9	1.6	1.9	1.9	0.7	2.0	2.3	2.8
Producer prices in industry, % p.a.	1.1	-0.4	-0.5	-2.1	-1.5	-3.0	-3.0	-1.0	1.0
General government budget, nat.def., % of GDP									
Revenues	24.8	24.2	26.3	26.5	26.1	27.5	28.0	28.5	28.5
Expenditures	28.2	29.2	31.5	30.5	28.0	25.3	27.5	28.5	29.0
Deficit (-) / surplus (+)	-3.4	-5.0	-5.2	-4.0	-1.9	2.2	0.5	0.0	-0.5
Public debt, nat.def., % of GDP	62.1	65.6	70.1	72.7	70.8	71.3	69.0	65.0	62.0
Central bank policy rate, % p.a., end of period ³⁾	4.00	3.00	2.25	1.75	2.00	1.25	1.25	1.50	1.75
Current account, EUR mn ⁴⁾	-978	-1,049	-1,287	-1,105	-394	-578	-1,300	-1,200	-1,150
Current account, % of GDP ⁴⁾	-10.2	-10.9	-12.9	-10.8	-7.9	-10.7	-11.9	-10.3	-9.3
Exports of goods, BOP, EUR mn ⁴⁾	1,526	1,051	932	771	423	320	620	610	630
annual change in %	8.5	-31.1	-11.3	-17.2	-12.1	-24.3	-20.0	-2.0	3.0
Imports of goods, BOP, EUR mn ⁴⁾	3,525	3,030	3,147	3,070	1,400	1,576	3,350	3,550	3,690
annual change in %	-3.4	-14.0	3.9	-2.5	-3.8	12.6	9.0	6.0	4.0
Exports of services, BOP, EUR mn ⁴⁾	1,673	1,715	1,881	2,028	877	1,006	2,270	2,430	2,620
annual change in %	-4.2	2.5	9.7	7.8	8.4	14.7	12.0	7.0	8.0
Imports of services, BOP, EUR mn ⁴⁾	1,460	1,489	1,558	1,503	633	708	1,640	1,720	1,820
annual change in %	-9.5	2.0	4.6	-3.5	-11.5	11.8	9.0	5.0	6.0
FDI liabilities (inflow), EUR mn ⁴⁾	666	945	869	890	473	418	790	.	.
FDI assets (outflow), EUR mn ⁴⁾	18	22	58	72	23	35	45	.	.
Gross reserves of NB excl. gold, EUR mn	1,909	1,971	2,142	2,831	2,335	2,767	.	.	.
Gross external debt, EUR mn ⁴⁾	5,513	6,368	6,927	7,686	7,230	7,881	7,900	8,300	8,600
Gross external debt, % of GDP ⁴⁾	57.5	66.2	69.5	74.8	70.4	72.0	72.0	71.0	70.0
Average exchange rate ALL/EUR	139.04	140.26	139.97	139.74	140.43	138.28	137	137	138
Purchasing power parity ALL/EUR	58.64	60.67	58.25	57.97	.	.	.	.	.

1) Preliminary. - 2) Based on UN-FAO data, from 2014 wiiw estimate. - 3) One-week repo rate. - 4) From 2013 based on BOP 6th edition, 5th edition before.

Source: wiiw Databases incorporating national statistics and IMF. Forecasts by wiiw.