

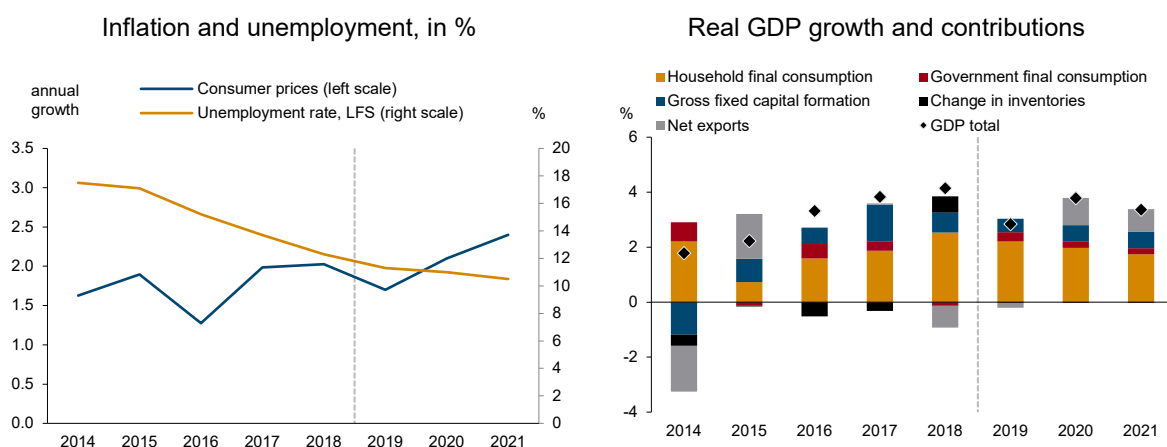


ALBANIA: Growth will remain below potential

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Growth has been held back by uneven energy supply. Although it will pick up in the next two years, it will remain below its potential. Private and government consumption will continue to support growth, the former underpinned by positive labour market trends, while investment will remain subdued. Outward migration of the young and highly skilled remains a drag on growth potential. Further delays to the start of EU accession negotiations create the risk of backsliding on reforms.

Figure 5.1 / Albania: Main macroeconomic indicators



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

The European Council last met on October 17-18th, 2019, to take a decision - among others - about starting membership talks with Albania and North Macedonia. The German parliament voted in support of opening the accession talks with Albania under the conditionality that reforms in the judicial system, the building of institutions – e.g. the Special Anti-corruption Prosecution office (SPAK) - and reforming of electoral law should be implemented by the date negotiations start. The position of France and the Netherlands is a standoff and for the most part, France is pressing into the direction that EU enlargement criteria should be reformed ahead of any other country joining in. Certainly, the opening of accession talks is vital for Albania. The country would benefit by moving forward a number of reforms already launched with the support of the EU as well as by getting access to EU transfers. However, a protracted EU enlargement process - in the foreseeable future - might create downside risks for the ongoing reforms.

Growth lost vigour and will remain moderate over growing downside risks. For the first half of 2019, y-o-y, the economy grew by 2.4% thanks to the positive contribution of sectors such as trade, real estate activity and agriculture. Otherwise industry, electricity production and water supply, as well as recreation services, were a drag on growth. In particular, the performance of industry has been in sharp contrast to the previous year, mostly because of the drought which affected electricity production in hydro power stations. Over the last decade the exposure of the economy to extensive drought periods and frequent floods has soared. Droughts have hampered electricity production (the bulk of it coming from hydropower stations) and strengthened the dependence on electricity imports. In the future, these shocks might continue to affect GDP growth, given the importance of this sector for the economy.

Private and government consumption will continue to support growth. Private and government consumption increased more than GDP for the first half of 2019, y-o-y. Domestic aggregate demand will continue to be supportive to growth. Signals from the labour market are positive. The pool of employees enlarged by 3.4 % - more than 42,000 new entries have been recorded for Q2.2019, y-o-y. Half of these jobs went to the young age group 15-29, mainly women and those with a tertiary level of education. The unemployment rate sank by 1.1 pp y-o-y, down to 11.5% for Q2/2019. Real gross monthly wages rose above 3% for Q2/2019, y-o-y, and remittances have been on a continuous rise. For some sectors - information and communication as well as trade - nominal wages soared by 11% for Q2/2019, y-o-y. A hike of 8.3% was applied to the minimum wage starting from January 2019. Certainly, rising nominal wages have been driven by tightening labour markets, as outward migration continues to be high (165,000 Albanians, or 6 % of the current population, emigrated over the last decade).

Credit growth revived and monetary policy will continue to stay loose. Overall, credit to private non-financial corporations increased by 3.4% until August 2019, y-o-y and the Central Bank kept the key interest rate at 1%. Demand for credit regained momentum thanks to small and medium size enterprises – mainly operating in industry, but also in tourism – whose demand for loans grew respectively by 15% and 11% until August 2019, y-o-y. Credit to households also rose by 5% over the same period. Non-performing loans continued their downward trajectory falling by 2 pp. y-o-y down to 11.2% in July 2019. Importantly, 60% of loans are in foreign currency - predominantly in EUR - hinting that the euroisation of the economy persists in being high, despite the Central Bank announcing a number of measures aiming at de-euroisation.

Fiscal consolidation might be at risk. General government budget performance has been below expectations; capital expenditures have been in decline while overall expenditures have been rising and exceeded budget revenues in January – August 2019. As such, fiscal consolidation might stall as long as the general government budget deficit rises.

Net exports contribution to growth has been positive thanks to an upsurge in services exports which contrasted with falling goods exports. The tourism sector continued being buoyant and exports of services expanded close to 10% for the first half of 2019, y-o-y. On the contrary, goods exports weakened by 9% over the same period. Further appreciation of domestic currency has negatively affected exports of goods – e.g. LEK appreciated against EUR by 2.2% for January – September 2019, adding to 8.2% appreciation in 2018. Until August 2019, y-o-y, goods exports fell for all groups – both in nominal and real terms – except for agriculture and chemical products. Exports of goods falling into the group of minerals, fuels and electricity suffered the most, while imports in this category hiked owing to protracted drought periods.

Foreign direct investments kept the upward trend, although overall investments will remain subdued. FDI inflows for the first half of 2019 soared by 10%, y-o-y. Close to 37% of FDI inflow was thanks to the Trans-Adriatic Pipeline (TAP) and the Norwegian Statkraft investment on Devoll Hydropowers. Since these projects are approaching the final construction phase - in 2019 - their contribution to FDI inflows will be significantly reduced. Meanwhile, over the same period, FDI inflow to the extraction industry rose by 67% meaning that 19% of FDI inflow was absorbed by this sector. Countries such as Italy and Austria more than doubled their FDI inflows to Albania for the first half of 2019 y-o-y and contributed by 10% each. Positive signalling comes also from Shell Upstream operating in Albania. After the clamorous announcement last May 2019 about the discovery of onshore extensive oil reserves, the company is progressing with further appraisal drillings. Bankers' petroleum - owned by Chinese Geo-Jade Petroleum Corporation – owing to favourable heavy oil commodity markets - announced a rise in production of 18% and plans to invest up to \$255 million by the end of 2019.

High potential for renewable resources to fix unstable energy supply, but the progress is slow. Solar power plants could be a niche sector for Albania because of its high exposure to sunny days. Still, such projects are progressing slowly. In November 2018 the first bid for solar power plant building was awarded to India Power Corporation Ltd Consortium - a conglomerate owned by Kanoria Foundation, a trust entity with headquarters in Kolkata, India. The construction phase is 18 months; still information about its progress is scarce. TAP is approaching the end of its construction phase. By 2020 it will start to deliver gas from Azerbaijan to the EU. Therefore, Albania, and other Western Balkan (WB) countries – e.g. Montenegro, Croatia, Bosnia and Herzegovina – have made joint efforts to get access to TAP through Ionian Adriatic Pipeline (IAP). The latter will be integrated to TAP along the pipeline crossing Albania and will enable the delivery of gas from Azerbaijan to WB. Widening of energy sources will certainly reduce the dependence on hydro energy production and electricity imports, especially for Albania.

In a nutshell, along the forecasting period, growth is expected to be moderate and below potential, owing also to an unsteady energy supply. The main drivers of growth will continue to be consumption, tourism and, to a lesser extent, investment in infrastructure projects. Our forecasts will be revised downwards for 2019 – to close to 2.8%. By 2020 growth will accelerate to 3.7%.

Table 5.1 / Albania: Selected economic indicators

	2015	2016	2017	2018 ¹⁾	2018 January-June	2019	2019 Forecast	2020 Forecast	2021
Population, th pers., average	2,881	2,876	2,873	2,866	.	.	2,870	2,865	2,865
Gross domestic product, ALL bn, nom.	1,434	1,472	1,551	1,631	804	825	1,700	1,800	1,900
annual change in % (real)	2.2	3.3	3.8	4.1	4.3	2.3	2.8	3.8	3.4
GDP/capita (EUR at PPP)	8,800	8,600	9,100	9,500	.	.	.	.	.
Consumption of households, ALL bn, nom.	1,147	1,180	1,226	1,287	652	680	.	.	.
annual change in % (real)	0.9	2.0	2.3	3.2	3.2	2.7	2.8	2.5	2.2
Gross fixed capital form., ALL bn, nom.	350	359	381	394	173	175	.	.	.
annual change in % (real)	3.5	2.4	5.5	2.9	2.4	0.3	2.0	2.5	2.5
Gross industrial production									
annual change in % (real)	-2.1	-18.0	-0.6	18.5	25.4	-9.1	-2.0	3.0	4.0
Gross agricultural production ²⁾									
annual change in % (real)	2.6	3.3	4.0	5.0	.	.	.	.	.
Construction output total									
annual change in % (real)	19.4	5.1	19.6	5.6	0.8	0.9	.	.	.
Employed persons, LFS, th	1,087	1,157	1,195	1,231	1,227	1,257	1,275	1,280	1,290
annual change in %	4.8	6.5	3.3	3.0	4.1	2.4	3.6	0.4	0.8
Unemployed persons, LFS, th	224	208	190	173	174	168	160	160	150
Unemployment rate, LFS, in %	17.1	15.2	13.7	12.3	12.5	11.8	11.3	11.0	10.5
Reg. unemployment rate, in %, eop	12.9	8.8	7.2	5.4	6.9	6.0	.	.	.
Average monthly gross wages, ALL	47,900	47,522	48,967	50,589	49,769	52,088	53,800	56,600	59,100
annual change in % (real, gross)	3.2	-2.0	1.0	1.3	1.3	3.1	4.5	3.0	2.0
Consumer prices, % p.a.	1.9	1.3	2.0	2.0	2.1	1.5	1.7	2.1	2.4
Producer prices in industry, % p.a.	-2.1	-1.4	2.6	1.7	1.7	-0.3	-0.2	0.5	-0.2
General governm.budget, nat.def., % of GDP									
Revenues	26.4	27.6	27.7	27.6	27.0	27	27.6	28.0	28.0
Expenditures	30.5	29.5	29.7	29.2	26.8	27.8	29.5	29.5	29.5
Deficit (-) / surplus (+)	-4.1	-1.8	-2.0	-1.6	0.2	-0.4	-1.9	-1.5	-1.5
General gov.gross debt, nat.def., % of GDP	72.7	72.4	70.1	67.9	66.0	65.0	67.5	67.0	66.0
Stock of loans of non-fin.private sector, % p.a.	-2.6	0.2	0.7	-3.6	-2.4	3.6	.	.	.
Non-performing loans (NPL), in %, eop	18.2	18.3	13.2	11.1	13.3	11.2	.	.	.
Central bank policy rate, % p.a., eop ³⁾	1.75	1.25	1.25	1.00	1.0	1.0	1.0	1.0	1.3
Current account, EUR mn	-884	-812	-866	-861	-347	-517	-1,010	-970	-940
Current account, % of GDP	-8.6	-7.6	-7.5	-6.7	-5.6	-7.8	-7.3	-6.6	-6.1
Exports of goods, BOP, EUR mn	771	714	797	986	496	452	870	930	970
annual change in %	-17.2	-7.4	11.7	23.7	24.7	-9.0	-12.0	7.0	4.2
Imports of goods, BOP, EUR mn	3,070	3,317	3,621	3,857	1,795	1,928	3,990	4,110	4,170
annual change in %	-2.5	8.0	9.2	6.5	6.8	7.4	3.5	3.0	1.5
Exports of services, BOP, EUR mn	2,028	2,396	2,856	3,073	1,370	1,492	3,260	3,460	3,590
annual change in %	7.8	18.1	19.2	7.6	7.9	8.9	6.0	6.0	3.8
Imports of services, BOP, EUR mn	1,503	1,599	1,774	1,962	856	938	2,080	2,120	2,140
annual change in %	-3.5	6.4	11.0	10.6	9.0	9.6	6.0	2.0	1.0
FDI liabilities, EUR mn	890	943	900	1,020	486	535	700	.	.
FDI assets, EUR mn	72	6	-94	-3	-22	23	-50	.	.
Gross reserves of NB excl. gold, EUR mn	2,831	2,889	2,941	3,342	2,904	3,215	.	.	.
Gross external debt, EUR mn	7,634	7,882	7,949	8,353	8,113	8,339	8,300	8,200	8,700
Gross external debt, % of GDP	74.4	73.5	68.7	65.3	63.5	60.6	60.0	56.0	56.0
Average exchange rate ALL/EUR	139.74	137.36	134.15	127.59	129.96	123.88	123.5	122.5	122.5

1) Preliminary. - 2) Based on UN-FAO data, wiiw estimate from 2017. - 3) One-week repo rate.

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