

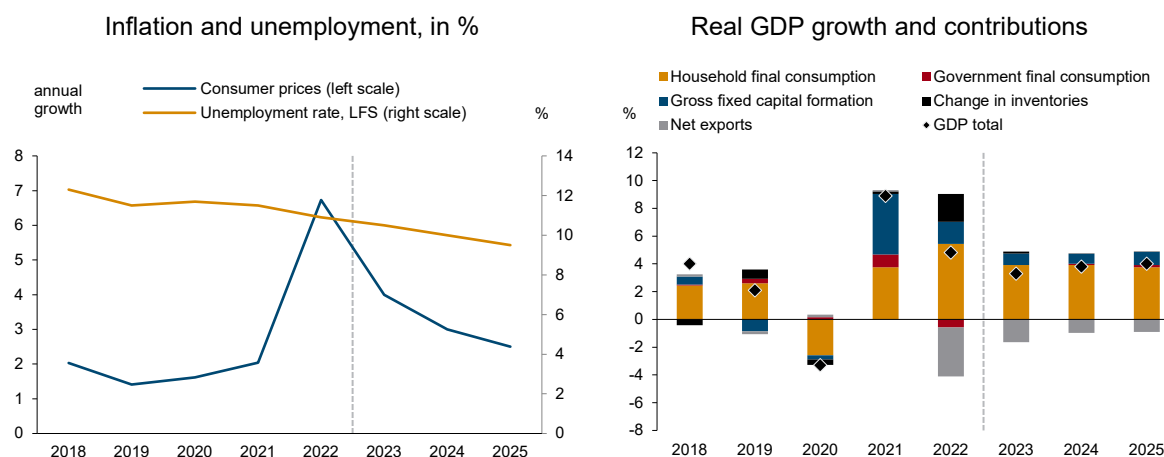


ALBANIA: Impressive resilience in the face of external shocks

RAVIK MIMA

The Albanian economy displayed remarkable resilience in 2022, with a growth rate of 4.8%, driven by a bumper tourist season, robust FDI inflows and strong household consumption on the back of rising real incomes. Inflation was the lowest in the whole CESEE region, averaging 6.7%, but is still high by the country's own standards. This year will be similar to 2022, with expected growth of 3.3% and inflation of 4%.

Figure 5.1 / Albania: Main macroeconomic indicators



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

Despite facing significant supply-chain disruptions and the impact of the ongoing conflict in Ukraine, the Albanian economy displayed impressive resilience throughout 2022. GDP grew by 4.8% for the year as a whole, with the trend continuing at a similar pace in Q4. This growth owes much to the success of the tourism sector, but also to a combination of robust domestic demand and prudent macroeconomic policies, which allowed the economy to stay afloat despite rising inflationary pressures.

Trade, tourism-related services and construction were the main sectors that drove economic growth last year. Strong consumer demand and an exceptional tourist season led to a 48.5% increase in income from tourist arrivals, compared to 2021. Tourist income totalled EUR 2.84bn – 36% more than in pre-pandemic times. In 2022, the sector made a significant contribution to the economy, directly accounting for 15.8% of GDP. The construction sector also put in a healthy performance, contributing 1 percentage point to overall GDP growth. On the other hand, agriculture and the energy sector faced severe challenges on account of unfavourable weather conditions.

Inflation averaged 6.7% in 2022, the lowest in the whole CESEE region. The invasion of Ukraine by Russia intensified the inflationary pressures in Albania, as food, energy and key minerals used as inputs by various industries became more expensive, due to higher global prices, disruption to supply chains and sanctions that targeted Russia. Food and transport prices were the primary drivers of inflation in 2022: these disproportionately affected the poorest citizens, because of the greater weight those items have in their consumption baskets. Despite the price rises, Albania's inflation remains significantly lower than that of its peers in the region or the EU average, thus mitigating macroeconomic, social and political pressures. This comparatively low inflation rate is attributable to several factors: the exchange rate against the euro has continued to strengthen; the domestically generated hydropower has provided some insulation against the energy crisis; the energy price rises were pegged back for regulated customers; and transport fuels and key foodstuffs were subject to temporarily controlled profit markups, with the local fruit and vegetable production base providing a good additional cushioning effect.

The labour market has also shown considerable improvement. Employment and labour force participation recovered quickly after the pandemic-induced disruptions. The annual growth in employment accelerated to 5.4% in Q4 2022, while unemployment reached a record low of 10.8%, mainly because of the greater participation of women. At the end of 2022, the average salary in the Albanian economy stood at approximately EUR 580 a month, with a 10.8% nominal rise and a 4.1% real growth rate when adjusted for inflation. The Albanian government's decision to increase the minimum wage in April 2023 is expected to further support the labour market, stimulating household consumption and, in turn, overall economic activity.

The country enjoyed double-digit growth in both foreign direct investment (FDI) and remittances in 2022. FDI inflows reached an impressive EUR 1.37bn – a 37% increase over the previous year – and accounted for 7.6% of GDP. The Netherlands, Italy and Germany were the top three countries of origin of the FDI. The Netherlands was the biggest investor, providing EUR 218m and taking advantage of Albania's favourable tax environment and legal system, which make it an attractive destination for foreign companies to register. Reinvested profits accounted for 53% of total FDI in 2022 – up by around a half over the previous year. Mining and quarrying, real estate, and the energy, gas and water supply sectors attracted the most investment. The real estate sector has witnessed substantial growth in recent years, with foreign investments reaching a total value of EUR 291m during 2022 – a significant increase of 52% year on year. Purchases by foreign nationals are becoming a significant factor in the Albanian property market. Thanks to the country's geographical position, its climate, the favourable taxation system and its low prices, more and more foreign citizens are deciding to invest in properties in Albania, especially in the coastal areas. At the same time, net remittances in 2022 increased by 10% nominally, to EUR 834m, but declined as a share of GDP, to 4.5% of GDP.

Thanks to the strong capital inflows and the bumper tourist season, the national currency appreciated strongly in 2022. The nominal exchange rate at the end of 2022 stood at around 114 Albanian lek to the euro (compared to around 121 lek to the euro at the end of 2021). The appreciating pressures are continuing in 2023 as well. They are also partly driven by monetary tightening – the central bank raised its policy rate from 0.5% in February 2022 to 3% in March 2023. Still, this tightening is mild by regional standards – and milder than that undertaken by the European Central Bank, which hiked its rate by 350 basis points over the same period. The more moderate tightening can be explained by the lower inflation in Albania.

Despite the interest-rate hikes, the banking system in Albania is in a strong position. The capital adequacy ratio exceeds regulatory requirements, and the sector has a high level of liquidity and profitability. The provision of credit to both enterprises and households has experienced a positive trend, indicating the banking sector's commitment to supporting economic growth. Private-sector credit in Albania continued to grow strongly in 2022, with outstanding credit to the economy increasing by 7.1%. Total deposits in the banking system also increased by 5%.

Albania's fiscal position improved in 2022, with controlled spending and healthy revenue flows as a result of high inflation. The government provided direct support to households and firms amounting to about 0.8% of GDP. The reduction in public debt from 73.2% in 2021 to 67% of GDP at the end of 2022 confirms a sustained downward trajectory since the immediate aftermath of the pandemic crisis, this time also helped by the elevated inflation. On the other hand, government borrowing costs increased following the Bank of Albania's interest-rate hikes.

Looking ahead to the rest of 2023, the Albanian economy is expected to maintain its positive trajectory, with a projected growth rate of 3.3%. This will be supported by sustained expansion in household consumption, private and public investment, and exports of goods and services. Favourable financial conditions, healthy private-sector balance sheets, and continued improvements in business and household confidence are also expected to drive growth. On the other hand, the withdrawal of policy support linked to reconstruction in the aftermath of the 2019 earthquake will push growth down a bit.

Despite inflation being the lowest in the region, it remains a concern in the country. Inflation has become both more persistent and more broad based, with core inflation running slightly higher than the headline consumer price inflation since August 2022. Inflationary pressures remain high even at the start of 2023, owing to robust demand for goods and services, rapid wage and production cost increases and rising inflation expectations. Inflation in January and February stood at 7.2% and 7.1% on an annual basis, respectively, exceeding initial projections. It declined to 5.3% in March, which is still above historical levels for the country. For 2023, inflation should gradually subside to the 4% level, reaching the central bank target of 3% in 2024.

Table 5.1 / Albania: Selected economic indicators

	2019	2020	2021	2022 ¹⁾	2023	2024 Forecast	2025
Population, th pers., average	2,854	2,838	2,812	2,760	2,745	2,730	2,715
Gross domestic product, ALL bn, nom.	1,692	1,647	1,856	2,134	2,400	2,600	2,800
annual change in % (real)	2.1	-3.3	8.9	4.8	3.3	3.8	4.0
GDP/capita (EUR at PPP)	9,510	9,210	10,300	11,230	.	.	.
Consumption of households, ALL bn, nom.	1,340	1,318	1,411	1,607	.	.	.
annual change in % (real)	3.3	-3.3	4.7	7.2	5.2	5.2	5.0
Gross fixed capital form., ALL bn, nom.	378	373	452	511	.	.	.
annual change in % (real)	-3.6	-1.4	19.2	6.5	3.5	3.0	4.0
Gross industrial production							
annual change in % (real)	-1.1	-6.3	26.2	2.8	3.5	4.0	4.5
Gross agricultural production ²⁾							
annual change in % (real)	-3.0	2.6	2.0	2.0	.	.	.
Construction output total							
annual change in % (real)	-2.5	9.5	18.0	12.5	.	.	.
Employed persons, LFS, th, average	1,266	1,243	1,249	1,298	1,325	1,350	1,375
annual change in %	2.8	-1.8	0.4	4.0	2.1	1.9	1.9
Unemployed persons, LFS, th, average	165	165	163	160	160	150	140
Unemployment rate, LFS, in %, average	11.5	11.7	11.5	10.9	10.5	10.0	9.5
Reg. unemployment rate, in %, eop ³⁾	5.8	7.4	7.3	7.0	.	.	.
Average monthly gross wages, ALL	52,380	53,662	57,191	61,884	66,300	70,300	74,200
annual change in % (real, gross)	2.1	0.8	4.4	1.4	3.0	3.0	3.0
Consumer prices, % p.a.	1.4	1.6	2.0	6.7	4.0	3.0	2.5
Producer prices in industry, % p.a.	-0.8	-3.3	2.7	19.9	5.0	3.5	3.0
General governm. budget, nat. def., % of GDP							
Revenues	27.2	25.9	27.5	26.8	27.5	28.0	28.5
Expenditures	29.1	32.6	32.1	30.5	30.0	30.5	31.0
Deficit (-) / surplus (+)	-1.9	-6.7	-4.6	-3.7	-2.5	-2.5	-2.5
General gov. gross debt, nat. def., % of GDP	65.8	74.3	74.5	64.6	67.0	68.0	69.0
Stock of loans of non-fin. private sector, % p.a.	6.6	6.9	9.6	7.0	.	.	.
Non-performing loans (NPL), in %, eop	8.4	8.1	5.7	5.0	.	.	.
Central bank policy rate, % p.a., eop ⁴⁾	1.00	0.50	0.50	2.75	3.50	3.00	2.50
Current account, EUR m	-1,089	-1,153	-1,166	-1,080	-1,260	-1,350	-1,480
Current account, % of GDP	-7.9	-8.7	-7.7	-6.0	-5.9	-5.8	-5.8
Exports of goods, BOP, EUR m	907	794	1,265	1,933	2,340	2,690	3,010
annual change in %	-8.1	-12.5	59.4	52.8	21.0	15.0	12.0
Imports of goods, BOP, EUR m	4,050	3,776	5,094	6,202	7,380	8,410	9,500
annual change in %	5.0	-6.8	34.9	21.7	19.0	14.0	13.0
Exports of services, BOP, EUR m	3,405	2,226	3,486	4,801	5,760	6,620	7,480
annual change in %	10.8	-34.6	56.6	37.7	20.0	15.0	13.0
Imports of services, BOP, EUR m	2,141	1,174	1,690	2,400	2,860	3,230	3,550
annual change in %	9.1	-45.1	43.9	42.0	19.0	13.0	10.0
FDI liabilities, EUR m	1,072	937	1,032	1,372	.	.	.
FDI assets, EUR m	36	43	42	166	.	.	.
Gross reserves of CB excl. gold, EUR m	3,240	3,806	4,831	4,786	.	.	.
Gross external debt, EUR m	8,246	8,549	9,755	9,799	12,100	13,500	15,000
Gross external debt, % of GDP	60.0	64.2	64.4	54.6	57.0	58.0	59.0
Average exchange rate ALL/EUR	123.01	123.77	122.46	118.98	113.0	112.0	110.0

1) Preliminary and wiiw estimates. - 2) Based on UN-FAO data, wiiw estimate from 2021. - 3) wiiw estimate from 2021. - 4) One-week repo rate.

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