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## **Albania: Part of a Greek tragedy?**

Economic growth in 2009 turned out much stronger than expected. Data for the first three quarters exhibit real GDP growth of almost 5%. In fact, for the whole year 2009 we expect a growth rate of above 4% (the earlier forecast from July 2009 was a 1% decline). The main drivers of growth were strong government investment in the wake of the parliamentary elections and a boom in the telecommunications industry due to more competition in the mobile telephony sector. For 2010 we expect growth as low as 1% given that government expenditures will tend to decrease and household consumption will stagnate in a fragile global economic environment. In particular the unfolding economic crisis in Greece may pose a threat to economic growth in Albania in 2010 and thereafter.

In the closing months of 2009 economic activity in Albania was decelerating. Growth of credit to residents decreased from a peak of about 30% in early 2009 to 15% in mid-2009 and to some 5% at the end of the year as compared to the same months a year earlier. This is despite the National Bank having decreased its base rate and the president of the National Bank asking the heads of the commercial banks to maintain lending. Quarterly GDP growth rates were decelerating: from above 5% in the first two quarters to some 4% in the third quarter of 2009. The Economic Sentiment Indicator from the National Bank's Business and Consumer Survey, though improving slightly in the course of the year, was well below its long-term average throughout all three quarters of 2009.

By December 2009 the Albanian lek depreciated by some 11% as compared to the same month of the previous year. This, along with an increase in excise taxes, has *inter alia* caused price increases in the food and beverages sector. This will further dampen the consumption of households. In addition, heavy flooding has devastated the country's north-western plain lands. This will also have negative effects on agricultural production in 2010. On the positive side, due to the heavy rainfalls the Albanian hydro power production could operate at full capacity and export electricity.

Another gleam of hope arises from the fact that the lek depreciation may improve the conditions of the tiny Albanian export sector during 2010. While in 2009 exports fell by nearly 20%, 2010 may bring a reversal. Also the tourism sector might finally generate a stronger surplus. Figures for 2009 show a growth of some 17% in net tourism revenues. This is mainly attributable to the opening of the newly built highway from neighbouring Kosovo to the Albanian coast in June 2009.

In 2009 it was possible to finance a huge and increasing current account deficit with growing FDI revenues from privatization. It will be difficult to reach a similarly high level of FDI in 2010. Also

remittances sent home from Albanian migrants abroad tend to further decline. Thus continued consumption of imported goods and services will have to be financed increasingly by borrowings. In this respect the Albanian Ministry of Finance has opened a tender for a bond management company in a bid to emit EUR 300 million in euro-denominated bonds, after a first attempt failed in early 2009.

It is yet unclear whether and to what extent Albania will be affected by the economic crisis in neighbouring Greece. Heavily increasing budget deficits and public debt triggered a collapse in the Greek bond market. At present it is not known in what way the Greek government will raise money to refinance existing debt and keep paying public sector salaries and pensions. A pay freeze for civil servants, tax increases and a substantial cut in government expenditures seem to be inevitable. This will most probably lead to several years of poor economic activity for one of Albania's most important economic partners. Four possible transmission channels can be identified: trade, remittances, FDI and banking.

Greece is Albania's second most important export partner (after Italy) with a share of about 8% in total Albanian exports. Most likely a fall in Greek demand would cause a drop in Albanian exports, but not necessarily. It might well be that lower-priced goods from Albania substitute for higher-priced goods from other countries. There are about half a million holders of Albanian citizenship living in Greece, which makes the country one of the most preferred targets of Albanian work migration. Though the actual amounts of remittances sent to Albania are not precisely known, it can be expected that the share is large. Again, an economic downturn in Greece will most likely cause remittances to decrease, but this may not necessarily happen. Albanians in Greece are barely working in the public sector and might thus be affected only indirectly by the crisis. Latest data from 2004 suggest that Greece is by far the most important source country of FDI in Albania. A slowdown of Greek FDI inflows is very likely and will cause additional pressure on the economy. Finally, Greek banks have a strong position in the Albanian banking sector. Here the Greek mother banks may find it more profitable to lend money to the Greek state and hence less capital could flow to their branches in Albania – but again, not necessarily.

Thus, overall prospects for economic developments in Albania in 2010 are rather modest and certain downward risks seem to arise from the Greek economic crisis, although these effects are difficult to forecast. We expect Albania's economy to grow by merely 1% in 2010. Further currency depreciation in 2010 could support Albania's export sector in subsequent years in spite of potential slight re-appreciation. This, together with household consumption regaining strength and improving access to credit for the private sector, could raise economic growth to some 4% in 2011 and 5% in 2012.

Table AL

## Albania: Selected Economic Indicators

	2004	2005	2006	2007	2008	2009 <sup>1)</sup>	2010	2011	2012
	Forecast								
Population, th pers., average	3127	3149	3135	3161	3177	3190	3210	3220	3240
Gross domestic product, ALL bn, nom.	750.8	814.8	882.2	971.2	1100.0	1180.0	1240	1350	1500
annual change in % (real)	5.7	5.7	5.4	6.0	8.0	4.2	1	4	5
GDP/capita (EUR at exchange rate)	1900	2100	2300	2500	2800	2800	.	.	.
GDP/capita (EUR at PPP - wiiw)	4600	5000	5500	5800	6500	6900	.	.	.
Consumption of households, ALL bn, nom.	584.7	634.5	680.3	775.1	860	910	.	.	.
annual change in % (real)	9.4	6.0	4.7	10.7	7.0	3	0	3	6
Gross fixed capital form., ALL bn, nom.	279.4	301.4	343.9	374.9	450	470	.	.	.
annual change in % (real)	2.7	4.9	13.0	5.8	12.0	6	1	8	10
Gross industrial production <sup>2)</sup>									
annual change in % (real)	14.1	11.7	12.1	-10.3	2.0	4.3	1	3	7
Gross agricultural production <sup>3)</sup>									
annual change in % (real)	6.3	0.9	3.1	2.6	1.0	3	1	3	3
Construction output total <sup>2)</sup>									
annual change in % (real)	7.9	6.3	10.5	10.1	7.0	7	0	3	5
Employed persons - LFS, th, June	.	.	.	1188.3	1103.0	1110	1050	1070	1120
annual change in %	.	.	.	.	-7.2	0.6	-5	2	5
Employment reg. total, th pers., end of period	931.2	932.1	935.1	965.5	974.1	970	910	930	980
annual change in %	0.5	0.1	0.3	3.3	0.9	-0.4	.	.	.
Unemployed persons - LFS, th, June	.	.	.	185.0	166.0	167.0	190	180	165
Unemployment rate - LFS, in %, June	.	.	.	13.5	13.1	13.1	15	14	13
Reg. unemployment rate, in %, end of period	14.4	14.1	13.8	13.2	12.7	12.8	14	13	12
Average gross monthly wages, ALL	19039	19993	21842	27350	29000	31900	.	.	.
annual change in % (real, gross)	-0.1	2.6	6.7	21.6	2.6	7.6	.	.	.
Consumer prices, % p.a.	2.9	2.4	2.4	2.9	3.4	2.2	2	3	3
Producer prices in industry, % p.a. <sup>4)</sup>	12.2	4.9	0.8	3.5	6.5	-2	-1	2	4
General governm. budget, nat. def., % GDP									
Revenues	24.6	25.1	26.0	25.9	26.5	25.5	23	25	26
Expenditures	29.6	28.5	29.3	29.4	32.0	32.5	29	28	29
Deficit (-) / surplus (+)	-5.1	-3.5	-3.3	-3.5	-5.5	-7	-6	-3	-3
Public debt, EU-def., in % of GDP <sup>5)</sup>	57.7	58.1	56.0	52.8	52.6	55	58	57	56
Base rate of NB, % p.a., end of period <sup>6)</sup>	5.3	5.0	5.5	6.3	6.3	5.3	5	6	6
Current account, EUR mn	-340.2	-589.1	-471.0	-831.0	-1318.8	-1660	-1780	-1800	-2100
Current account in % of GDP	-5.8	-9.0	-6.6	-10.6	-14.7	-18.6	-20.1	-18.0	-17.5
Exports of goods, BOP, EUR mn	485.6	530.2	630.6	786.3	917.5	760	810	890	970
annual growth rate in %	23.0	9.2	18.9	24.7	16.7	-17	7	10	9
Imports of goods, BOP, EUR mn	1762.3	2006.9	2289.6	2890.4	3348.9	3240	3400	3600	3900
annual growth rate in %	12.1	13.9	14.1	26.2	15.9	-3	5	6	8
Exports of services, BOP, EUR mn	807.6	967.3	1156.6	1415.1	1687.8	1800	1900	2100	2300
annual growth rate in %	27.6	19.8	19.6	22.3	19.3	7	6	11	10
Imports of services, BOP, EUR mn	848.1	1107.7	1188.0	1402.3	1618.4	1760	1800	1900	2100
annual growth rate in %	20.3	30.6	7.2	18.0	15.4	9	2	6	11
FDI inflow, EUR mn	278.4	212.6	258.6	481.1	653.1	750	600	500	700
FDI outflow, EUR mn	11.0	3.3	8.3	11.1	62.6	20	10	20	30
Gross reserves of NB excl. gold, EUR mn	982.7	1171.6	1329.2	1415.9	1626.1	1500	.	.	.
Gross external debt, EUR mn <sup>7)</sup>	1224.0	1373.5	1445.4	1445.7	2624.2	3000	.	.	.
Gross external debt in % of GDP	20.6	20.7	20.3	18.1	29.5	35	.	.	.
Average exchange rate ALL/EUR	127.7	124.2	123.1	123.6	122.8	132.1	140	135	125
Purchasing power parity ALL/EUR <sup>8)</sup>	51.9	52.1	51.2	52.7	52.9	53.7	.	.	.

1) Preliminary and wiiw estimates. - 2) Gross value-added. - 3) Gross value-added of agriculture, forestry and fishing. - 4) Until 2005 producer prices in manufacturing industry. - 5) Based on IMF data. - 6) One week repo rate. - 7) Until 2007 based on IMF data. - 8) Benchmark results 2005 from Eurostat and wiiw estimates.

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