



ALBANIA: Economic development under house arrest

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Albania's GDP growth rates are expected to hover around 1% in the years to come. Weak domestic demand, especially due to fiscal austerity measures, is the main reason for the sluggish development that is a far cry from pre-crisis economic dynamics. The signals emanating from the private sector are contradictory and do not make for a more optimistic outlook at present.

Annualised average consumer price inflation for the first eight months of 2014 is at a record low of 1.8%. This is the result of weak domestic demand and a disinflationary European environment. The Supervisory Board of the Bank of Albania decided in late September 2014 to keep its prime policy interest rate for the next quarters unchanged, at another record low of 2.50%. It was for the first time that the Board convened under the leadership of the acting governor Elisabeta Gjoni. She has replaced long-time governor Ardian Fullani after he was arrested in early September on charges of sloppy management in connection with a cash theft of more than five million euro at the Central Bank. The thief, an employee of the bank, was arrested in July and admitted he had been stealing banknotes for four years. The parliament has sacked Fullani as governor after a decade on the job. He is now under house arrest pending a trial.

Fullani was broadly believed to have conducted quite a pragmatic, growth supporting monetary policy during his mandate, earning him some confidence also on the international scene. However, over the last weeks his and the reputation of the Central Bank were tattered. All the more concerned has been the Supervisory Board of the Bank in the recent weeks to propagate the stability of the Albanian banking sector. Stress tests have shown that the banking sector is overall resilient to macroeconomic shocks. Also capitalisation indicators seem to be at adequate levels. However, the Board mentioned that the banks (which are mostly in foreign ownership) should 'cautiously monitor the possible scenarios for the future developments and their needs for additional capital'. Certainly the credit portfolio quality remains the main concern. The share of non-performing loans stabilised at about 24% in the first half of 2014, though.

Interestingly enough, new loans to the economy increased by some 18% in the first seven months of 2014 as compared to the same period a year earlier. Most of this growth, however, stems from strongly increasing overdraft credits in the business sector, while investment credits for machinery stagnated. Also new loans to households stagnated. This was mostly due to strongly falling credits in foreign currency, whereas especially credits for durable consumer goods in domestic currency experienced a marked increase. Hence the information content of the development on the credit market as an indicator for domestic demand is rather mixed.

Similarly inconsistent signals come from other indicators relevant for the forecasting of domestic demand. On the one hand, unemployment rates increased by several percentage points to levels of 17% to 18% in the first half of 2014 as compared to a year earlier. On the other hand, we find a 4% real annual increase in the first quarter of 2014 in the turnover of the wholesale, retail trade and repair of motor vehicles sector. This turnover figure is generally considered to be a good indicator regarding the economic expectations of consumers.

Moreover, the Economic Sentiment Indicator (ESI), which quantifies business and consumer confidence, increased in the second quarter of 2014, keeping on the positive developments of the previous two quarters. The ESI is now close to its long-term average. This development is particularly driven by the outstanding advance of the Industry Confidence Index (ICI), which has finally reached pre-crisis levels far above the long-term average. The improved ICI was positively affected by considerable improvements in the production figures and the financial situation of industrial firms. Indeed industrial production figures from the first quarter of 2014 show a real increase of about 15% year on year.

These figures are also confirmed by the customs statistics for the first seven months of 2014. Both, imports as well as exports increased by about 8% on the year. Interestingly, exports increased particularly into Italy, Greece and Turkey. Commodity-wise it is especially exports of textiles, wood but also chemicals that fared well. The largest export group of minerals, fuels and electricity experienced a decline of some 7% in the same period, mainly due to the halved hydro power production in the first half of 2014. This comes a bit as a surprise as precipitation figures appeared to be quite high this year. If autumn continues to be as rainy as the summer was we might expect a reversal in electricity export and import developments and hence a positive contribution of net exports to Albanian GDP.

It is also surprising that the currently published balance of payments figures appear to be quite different from the customs trade figures. In the current account data, goods exports in the first half of 2014 declined by 4% while goods imports increased by 7% on the year. However, this might be related to the adjustments made with the recent implementation of the revised IMF rules published in the sixth edition of the Balance of Payments and International Investment Position Manual. According to these data, services exports have apparently increased by as much as 21% whereas services imports only by 17%, during the same period as above.

Currently the government is rather a drag on aggregate demand. The announced fiscal austerity measures have been indeed realised. From January to July 2014 total revenues increased by 10% and total expenditures decreased by 4% on the year. The cut was especially strong in capital expenditures, which were slashed by as much as 54%. It can be assumed that these trends will continue throughout the whole year. It has to be hoped that private investment replaces public investment as business sentiment improves.

Due to the ambiguous signals from the economic indicators we keep our forecast for GDP growth unchanged as compared to our July 2014 forecast update. Hence we expect economic growth for 2014 at 1.3% and for 2015 at 1.5%. Given a continuous fiscal austerity policy and given that rainfall, which is crucially important for local electricity production, is a mean reverting process, we expect somewhat lower growth for 2016, at 0.9%. Overall these growth rates are only a far cry from pre-crisis growth rates. It will need a substantial boost in domestic demand to get out of the doldrums. A more courageous fiscal policy might be a way to go.

Table 1 / Albania: Selected Economic Indicators

	2010	2011	2012	2013 ¹⁾	2013 January-June	2014	2014 Forecast	2015 Forecast	2016
Population, th pers., average ²⁾	2,913	2,905	2,900	2,897	.	.	2,850	2,860	2,870
Gross domestic product, ALL bn, nom. ³⁾	1,240	1,301	1,335	1,369	684	686	1,400	1,440	1,470
annual change in % (real) ³⁾	3.7	2.5	1.6	0.5	2.9	0.5	1.3	1.5	0.9
GDP/capita (EUR at exchange rate)	3,100	3,200	3,300	3,400	.	.	.	.	.
GDP/capita (EUR at PPP)	7,100	7,400	7,500	7,600	.	.	.	.	.
Consumption of households, ALL bn, nom. ³⁾	961.9	1,011.8	1,034.6	1,055.0	.	.	.	.	.
annual change in % (real) ³⁾	1.7	1.8	0.7	0.5	.	.	2.0	0.5	0.5
Gross fixed capital form., ALL bn, nom. ³⁾	352.4	381.9	345.0	360.0	.	.	.	.	.
annual change in % (real) ³⁾	-8.5	5.9	-11.3	-5.0	.	.	1.0	1.5	2.0
Gross industrial production									
annual change in % (real)	37.5	27.1	12.9	23.2	32.2	4.4	5.0	6.0	4.0
Gross agricultural production									
annual change in % (real)	6.2	4.8	5.8	1.0	.	.	4.0	5.0	3.0
Construction output total									
annual change in % (real)	-13.3	-1.1	-11.4	-13.0	-13.2	-6.6	-1.0	1.0	1.0
Employed persons, LFS, th ⁴⁾	1,167	1,160	1,117	992	.	.	1,000	1,050	1,050
annual change in %	0.6	.	-3.7	-11.2	.	.	0.8	5.0	0.0
Employment reg. total, th pers., end of period ²⁾	896	948	962	927	934	910	950	950	950
annual change in %	-1.6	5.8	1.5	-3.7	-1.8	-2.6	2.5	0.0	0.0
Unemployed persons, LFS, th ⁴⁾	191	189	173	184	.	.	210	220	230
Unemployment rate, LFS, in % ⁴⁾	14.0	14.0	13.4	15.6	15.2	17.7	18.0	18.0	19.0
Reg. unemployment rate, in %, end of period ²⁾	13.8	13.1	12.8	13.4	13.6	13.5	14.0	14.0	14.5
Average monthly gross wages, ALL	34,767	36,482	37,305	40,860	.	.	.	.	.
annual change in % (real, gross)	-7.0	1.5	0.2	7.4	.	.	1.0	1.0	1.0
Consumer prices, % p.a.	3.6	3.4	2.0	1.9	2.4	1.8	1.0	1.0	1.0
Producer prices in industry, % p.a.	0.3	2.6	1.1	-0.5	.	.	0.0	0.0	0.0
General governm.budget, nat.def., % of GDP									
Revenues	26.2	25.4	24.7	23.9	22.9	25.5	26	26	26
Expenditures	29.3	28.9	28.2	28.8	30.0	28.8	27	27	28
Deficit (-) / surplus (+)	-3.1	-3.5	-3.4	-4.9	-3.5	-1.6	-1.0	-1.0	-2.0
Public debt, nat.def., % of GDP	57.7	59.4	62.0	70.0	.	.	69.4	68.5	69.1
Central bank policy rate, % p.a., end of period ⁵⁾	5.00	4.75	4.00	3.00	3.75	2.50	2.50	2.25	2.00
Current account, EUR mn ⁶⁾	-1,019	-1,225	-978	-1,035	-508	-618	-1,000	-950	-850
Current account, % of GDP	-11.3	-13.2	-10.2	-10.6	-10.4	-12.6	-10.0	-9.3	-8.3
Exports of goods, BOP, EUR mn ⁶⁾	1,172	1,406	1,526	1,756	500	479	1,150	1,200	1,250
annual change in %	56.1	20.0	8.5	15.1	.	-4.2	8.2	4.3	4.2
Imports of goods, BOP, EUR mn ⁶⁾	3,254	3,647	3,525	3,476	1,321	1,412	3,050	3,100	3,100
annual change in %	6.5	12.1	-3.4	-1.4	.	6.9	3.2	1.6	0.0
Exports of services, BOP, EUR mn ⁶⁾	1,751	1,747	1,673	1,656	971	1,170	2,700	2,750	2,800
annual change in %	-1.2	-0.2	-4.2	-1.0	.	20.5	14.9	1.9	1.8
Imports of services, BOP, EUR mn ⁶⁾	1,519	1,612	1,460	1,673	973	1,136	2,450	2,500	2,500
annual change in %	-4.9	6.2	-9.5	14.6	.	16.8	11.8	2.0	0.0
FDI inflow (liabilities), EUR mn ⁶⁾	793	630	666	953	410	380	900	800	700
FDI outflow (assets), EUR mn ⁶⁾	5	21	18	30	25	46	40	50	40
Gross reserves of NB excl. gold, EUR mn	1,851	1,851	1,909	1,971	1,962	1,964	.	.	.
Gross external debt, EUR mn ⁶⁾	4,100	4,958	5,513	6,177	5,854	6,372	.	.	.
Gross external debt, % of GDP	45.6	53.5	57.4	63.3	.	.	.	.	.
Average exchange rate ALL/EUR	137.79	140.33	139.04	140.26	140.19	140.21	140	141	143
Purchasing power parity ALL/EUR	59.94	60.33	61.18	62.30	.	.	.	.	.

1) Preliminary. - 2) According to census October 2011. - 3) According to ESA'10 (FISIM reallocated to industries etc). 2013 estimated by wiiw. Half-year data refer to gross value added. - 4) Until 2011 survey once a year, quarterly thereafter. From 2011 according to census October 2011. - 5) One-week repo rate. - 6) Half-year data and forecasts based on BOP 6th edition.

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