



OVERALL ECONOMIC DEVELOPMENT AND OUTLOOK IN ALBANIA

1) Main macroeconomic developments

During 2009, despite a contraction of growth rate due to the negative impact of the global economic crisis, Albanian economy still performed extremely well and demonstrated that it is vital and optimistic. Real economic growth in 2009 was estimated at 3.3%, accompanied by an annual average inflation of 2.2%. It is worth noting that this positive growth trend of our economy along with well-preserved macroeconomic stability, is highly satisfactory if put to a comparative perspective with the regional countries and beyond. This economic growth was mainly driven by a satisfactory performance of the services sector and agriculture. The considerable volume of public investments accounted for around 9.9% of GDP in 2009, with 8.8% carried out by the central government, which represented the key fiscal policy instrument to minimize the negative impact of the global economic crises. Very positive developments are reported also in the energy sector which has overcome the two hard years due to unfavourable climate conditions.

Trade balance in 2009 saw a fall in exports growth by around 8.5% against the previous year, and imports also decreased by around 2%. Trade deficit expressed in ALL stood at the same level as the previous year, at 15.2 of GDP, including exchange rate impact. Although exports of goods suffered a significant setback, it should be noted that monthly decline reached its peak in April, while in the following months the declining rates narrowed progressively and eventually October, November and December marked a positive increase of 0.8, 4.7 and 41.8% respectively. Simultaneously, trade deficit in November and December decreased by 5.2 and 7.8% respectively.

Net FDI inflows expressed in EUR increased by around 3.1% against the previous year. Business facilitation through fiscal and administrative policies helped improve its performance. Continuous road infrastructure upgrading, technological progress in various sectors and human capacity building have enhanced the economic efficiency, with the latter increasingly becoming a promoter of economic growth. Positive developments in the local business community contributed to employment promotion and increased income available to households. Increased income sustained the high level of household consumption as well as aggregate domestic demand.

Inflationary pressure subsided during 2009, due to decreasing prices of raw material in the international level and the domestic demand in the face of global economic recession. Average inflation rate during 2009 was 2.2% and remained within the Bank of Albania's target range of 2-4%.

In the first months of 2009, the inflationary pressure decreased against the previous year. Annual average inflation in the first half of 2009 stood at 2.0%, due to decreased prices of imported goods, particularly food and fuels which make up the bulk of imports. Inflationary pressures from international markets grew gradually in the second half of 2009

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and consequently inflation increased. Inflation at year-end reached the highest peak of 3.5% for 2009.

In 2009, the Lek depreciated against the Euro by around 7.5% and against the US dollar by a considerable 12.8% from the previous year, mainly reflected by the strong position of the US dollar in international exchange markets. In 2009, average exchange rate stood at 132.06 Lek against Euro and 94.99 Lek against the US dollar.

Exports of goods during January-March 2010 amounted to 35,423 mln Lek, up by 60.2% against the same period last year. This period accounts for an increase in all categories of goods. Specifically, the category "Minerals, fuels and electricity" grew by 104.5%, "Leather and articles thereof" grew by 77.4% and the category "Machinery, equipment and spare parts" grew by 54.6%. Likewise, exports of "Chemical products and plastics" grew by 5.4%, "Textile and footwear" grew by 14.0%, while exports of "Wood and paper products" grew by 33%.

Import estimates indicate that imports of goods amounted to 100,284 mln Lek, or 5.9% more than the same period in 2009. Consequently, trade deficit for this period was 64,861 mln Lek, down by 10.7% against the same period last year.

Consumer Price Index reached 107.6% in April against December 2007 (December 07=100), marking a decrease of 0.4% from the previous month. Annual price fluctuation (inflation) was 3.5% in April (from 3.9% in March 2010). The Lek depreciated against both currencies by 4.2% against the US dollar and 6.1% against the Euro.

2) Economic outlook in Albania (in the mid-term period, 2010-2013)

Albania is one of the few countries having a strong and sustained economic growth of over 6% for a decade. It is experiencing a positive economic momentum and has proved to be vital and flexible economy. This is confirmed by the economic performance in the last three years. Despite energy supply shortages, the 2007 drought in agriculture and the financial and economic global crisis recently, economic growth continues to be at relatively high levels.

The basic objectives of the coordinated monetary and fiscal policies aim to preserve macroeconomic stability, maintain inflation at the target range of around 3%, subdue deficit and reduce public debt by 54% by 2013 in line with the Maastricht criteria.

Alongside the technological progress and structural reforms, implementation of a series of efficient macroeconomic policies during this four-year period clearly driven by the "philosophy" of boosting economic growth through the promotion of aggregate supply, has given a significant impetus to the economy. Pursuing well-planned and well-coordinated macroeconomic policies and further advancement of economic and structural reforms - in parallel to the other natural processes that the economy is experiencing: such as technological progress, accumulation of capital and restructuring of economy towards a more efficient economy - shall ensure the continuation of this economic trend in the medium term at least. Average economic growth rate during 2010 – 2013 is forecasted to be at 6.4%.

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Economic growth will be sustained by the main sectors of economy. Hence, from the point of view of aggregate demand: (a) Final consumption in the upcoming medium-term period is forecast to grow in real terms by an average of 5.5% a year. This projected growth rate of the final consumption is in line with the traditional trend of this element of aggregate supply; (b) Investments (Gross Fixed Capital Formation) in the 4-year period ahead is forecast to grow in real terms by an average of 7%. A deviation from this estimate is projected to occur in 2010. Total investments in the economy in 2010 are forecast to grow in real terms by only 0.4%. This is mainly attributed to the slowdown of public investments planned for 2010 with around 30% compared to 2009. This slowdown was oriented by budget policies which - following the completion of some large infrastructure projects – shifted their focus on other priorities, and also by a prudent and sound fiscal policy aiming at preserving the macroeconomic stability. In the meantime, it is forecast a comeback to the high growth rates for private investments. The improved developments in private investments are explained by the introduction of financial facilitations, reduction of capital market uncertainty, and restoration of confidence among businesses and investors, reflecting also the gradual recovery of the world economy; (c) Net exports of goods and services deteriorated during 2000-2009 by an average of 13% each year, but a reduction of this falling rate is expected. In 2010, the net exports are forecast to be at the same level as in 2009, while for 2011 it is expected to improve by 1% against 2010. Main factors contributing to the improved trend in net exports are:

- recovery of the growth rates of exports of goods reflecting the departure from the economic crisis of many partner economies (expect for Greece that accounts for only 8% of total exports)
- growth of imports at a rather restrained rate then in three previous years, reflecting the reduced domestic demand driven by the large public investments in recent years and the strengthened competitiveness of several Albanian products against their imported substitutes
- high expectations in the tourism sector for the upcoming period nourished by infrastructure upgrade and quality of tourism products and reduced tourism costs.

Demand projections and its elements displayed above consistently correspond to the following supply projections and its main sectors:

- (i) Agricultural production in assumed normal conditions is projected to follow its traditional growth rate of 3.5-4.0% a year.
- (ii) Industrial production, including extracting and manufacturing industry, is forecast to grow by round 8.9 per cent in real terms in the medium term period.
- (iii) Construction is forecast to have an average growth of 6% a year in the medium term.
- (iv) Services are forecast to grow by 7.1% in the medium term period. The main contributors to this growth are expected to be trade, hotels and restaurants, transport and telecommunication services.

The above projections of aggregate demand and supply and in full consistency with the other macroeconomic sectors, GDP growth under this baseline scenario during the four upcoming years 2010-2013 is forecast to be at 5.5, 6.5, 7.1, and 6.7% respectively.

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Annual average inflation during 2010-2013 is expected to be at around 3%, in line with the objective and monetary policy of the Bank of Albania.

Trade deficit expressed in proportion to GDP for the period 2010-2013 is forecast to shrink gradually. It is forecast to decrease to 22.7% of GDP in 2013, from 26.1% in 2009.

Current account deficit is expected to be reduced to 8.9% of GDP in 2013, from 17.2% in 2009.