INTERNATIONAL MONETARY FUND

IMF Country Report No. 19/207

ALBANIA

July 2019

SECOND POST-PROGRAM MONITORING DISCUSSIONS—PRESS RELEASE AND STAFF REPORT

Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. In the context of the 2019 second Post-Program Monitoring discussions with Albania, the following documents have been released and are included in this package:

- A **Press Release**
- The **Staff Report** prepared by a staff team of the IMF for the Executive Board's consideration on a lapse-of-time basis, following discussions that ended on July 1, 2019, with the officials of Albania on economic developments, risks and policies. Based on information available at the time of these discussions, the staff report was completed on June 13, 2019.

The IMF's transparency policy allows for the deletion of market-sensitive information and premature disclosure of the authorities' policy intentions in published staff reports and other documents.

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July 3, 2019

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IMF Executive Board Concludes 2019 Second Post-Program Monitoring for Albania

On July 1, 2019, the Executive Board of the International Monetary Fund (IMF) concluded the Second Post-Program Monitoring review for Albania and considered and endorsed the Staff Appraisal on a lapse-of-time basis.[1] Albania's capacity to repay the Fund is adequate reflecting a strong record of repaying the Fund, relative macroeconomic stability, and progress in reforms.

Albania's medium-term economic outlook is broadly favorable. In 2019, growth is expected to slow down to 3.5 percent, due to the base effect of the 2018 peak in power generation and the economic slowdown in Albania's main partner countries. Over the medium-term, GDP growth is projected to converge to its 4 percent potential rate, as activity is expected to be driven by a pickup in EU growth, increasing labor market participation, a gradual strengthening of exports including tourism, and the investments needed to close Albania's large infrastructure gap. Inflation is expected to converge slowly towards its 3 percent target by 2021, as the output gap narrows and imported inflation from the euro area recovers. The current account deficit is projected to narrow further over the medium term, supported by strong export growth and planned fiscal consolidation. The level of FX reserves remains comfortable.

Despite the favorable environment and positive short-term outlook, risks and vulnerabilities remain. Albania is exposed to the increasing risks to growth in the EU, notably in its main trading partners. On the domestic front, the vulnerabilities are primarily in the public sector, arising from high public debt, increasing contingent liabilities, and weaknesses in public institutions and economic governance in general. Domestic growth vulnerabilities include demographic prospects and heavy dependence of growth on weather conditions.

Executive Board Assessment

Following strong growth last year, the baseline projections foresee an ongoing economic expansion. Furthermore, inflation remains well under control, and the current account is expected to improve further. However, more ambitious improvements in governance and anti-corruption efforts, skills formation and other aspects of the business environment will be

[1] The Executive Board takes decisions under its lapse-of-time procedure when the Board agrees that a proposal can be considered without convening formal discussions.

needed to raise potential growth, and take advantage of the country's favorable location and low labor costs.

As a small open economy, with limited economic diversification, Albania remains considerably exposed to external and domestic risks. The country is especially vulnerable to drought, population aging combined with the ongoing emigration of skilled workers, and spillovers from lower growth in key trading partners. Furthermore, as a result of still high public debt, relatively large financing needs, and rising contingent liabilities, severe adverse shocks to growth or a deterioration in regional financial conditions could quickly undermine Albania's public balance sheet and impair its access to affordable financing.

At the same time, Albania's flexible exchange rate and ample reserves offer important tools for absorbing shocks. Furthermore, the recent fiscal consolidation and the lengthening of the maturity of public debt have also been helpful. As a result, risks to Albania's capacity to repay appear contained. Nonetheless, more is needed to limit risks related to the public finances.

It is critical to implement further fiscal adjustment, combined with improvements in the quality of budgetary policies. Accelerating the reduction in public debt over the medium term, will create space to absorb and offset adverse shocks through countercyclical fiscal policies. Given the need to improve Albania's infrastructure and human development, fiscal consolidation should be underpinned by improvements in tax policy and tax administration that lead to higher revenues. Such reforms should be supported by a careful analysis of the revenue system and a medium-term strategy to enlarge the tax base and level the playing field for businesses.

The authorities' ambition to address the buildup of fiscal arrears is most welcome. These arrears have undercut the business climate as well as trust in the government. Going forward, all validated new VAT refund requests should be honored without delay, and the existing arrears should be cleared as soon as feasible—even if, in the short term, this may raise the deficit (measured on a cash basis).

It will be important to put in place a more consistent framework for public investment management, and to limit the risks from PPPs and other contingent liabilities. The Ministry of Finance and Economy should exploit its new role as gatekeeper for new PPP projects to help ensure both value for money and the containment of risks. Furthermore, the proposed establishment of the AIC should be revisited, to make sure that--if such institution is created--it will act on a strictly commercial basis and without direct government interference or reliance on future budget support.

The energy sector needs to be put on a sound footing without delay. Given sector's endemic financial weakness and accumulating arrears, financial restructuring should be undertaken without delay, combined with continued actions to liberalize the sector and unbundle its key players.

Debt management should reconcile the search for lower financing costs and longer maturities, with the need to support the development of a robust and liquid domestic debt market. The latter would help mobilize domestic savings and reduce currency and rollover risks. In this context, it will be important to resume the issuance of short-term T-bills.

Continued strong supervision will be important to ensure that the expected increase in bank lending does not weaken financial stability. The banking sector has experienced a large-scale consolidation, combined with a shift in ownership away from EU banks. Against this background, the BOA's recent measures for further alignment with EU standards and the increased frequency of on-site inspections should be helpful, particularly to contain risks from large exposures and related-party lending. Further actions will be needed to address weaknesses in the AML/CFT framework.

Albania: Selected Economic Indicators, 2015–2020

	2015	2016	2017	2018	2019	2020
					Proj.	
Real sector						
Real GDP	2.2	3.3	3.8	4.1	3.5	4.0
Domestic demand contribution	0.6	3.2	3.6	5.0	4.0	4.3
Consumption	0.6	2.0	2.1	2.1	2.5	2.7
Investment (Incl. inventories and stat. disc)	0.0	1.1	1.5	2.9	1.5	1.6
External demand contribution	1.6	0.2	0.2	-1.0	-0.5	-0.3
Consumer Price Index (eop)	2.0	2.2	1.8	1.8	2.2	2.6
Consumer Price Index (avg.)	1.9	1.3	2.0	2.0	2.0	2.4
GDP deflator	0.6	-0.6	1.5	0.7	2.0	2.4
Saving-investment balance						
Foreign savings	8.6	7.6	7.5	6.8	6.6	6.4
National savings	15.8	16.8	17.0	17.3	17.6	17.8
Public	0.7	1.2	2.4	2.7	1.5	1.9
Private	15.1	15.6	14.7	14.6	16.1	15.8
Investment (incl. Inventories and stat. disc.)	24.4	24.4	24.5	24.2	24.2	24.2
Public	5.3	5.1	5.5	5.6	5.5	5.7
Private	19.2	19.3	19.0	18.6	18.6	18.5
Fiscal sector						
Total Revenues and grants	26.3	27.4	27.7	27.6	27.2	27.4
Tax revenue	23.7	24.9	25.7	25.8	25.0	25.2
Total Expenditure	30.9	29.6	29.7	29.3	29.7	27.3
Primary	28.2	27.2	27.7	27.0	27.7	27.3
Interest	2.7	2.5	2.1	2.2	2.0	2.1
Overall balance 2/	-4.6	-2.3	-2.0	-1.6	-2.5	-2.0
Primary balance	-1.9	0.2	0.1	0.6	-0.5	0.0
Financing	4.6	2.3	2.0	1.6	2.5	2.0
of which: *Domestic*	-1.3	0.9	-0.8	-1.3	1.2	0.2
of which: *Foreign*	5.0	1.3	1.9	2.9	1.3	1.8
General Government Debt 1/	73.7	73.3	71.9	69.9	66.3	64.5
Domestic	39.5	39.1	39.0	37.6	34.2	32.8
External	34.2	34.3	32.9	32.4	32.0	31.7
Monetary indicators						
Broad money growth	1.8	3.9	0.3	-0.2	6.4	6.5
Private credit growth	-2.8	0.4	-0.8	-0.9	5.0	5.7
Velocity (nominal GDP/broad money)	1.2	1.2	1.2	1.3	1.3	1.3
External sector						
Trade balance (goods and services)	-17.3	-16.9	-15.1	-14.0	-13.6	-12.8
Current account balance	-8.6	-7.6	-7.5	-6.8	-6.6	-6.4
Gross international reserves (billions of Euros)	2.9	2.9	3.0	3.4	3.7	3.9
(In months of imports of goods and services)	7.0	6.5	6.2	6.6	6.8	6.8
(Relative to external debt service)	2.6	3.6	3.5	3.1	3.8	3.1
(In percent of broad money)	32.5	31.5	31.4	33.2	34.0	33.8
Memorandum items						
Output Gap (percent)	-1.8	-1.4	-0.7	-0.7	-0.5	-0.2

Sources: Albanian authorities; and IMF staff estimates and projections.
1/ The stock of general government debt includes arrears from central and local government.
2/ The fiscal balance includes guarantees for new loans to the energy sector.

INTERNATIONAL MONETARY FUND

ALBANIA

SECOND POST-PROGRAM MONITORING DISCUSSIONS

June 13, 2019

KEY ISSUES

Growth was strong in 2018, backed by high electricity production. Inflation remains subdued, notwithstanding very accommodative monetary conditions. The fiscal stance in 2018 was somewhat tighter than expected, supporting a further decline in public debt. The medium-term economic outlook is broadly favorable, with growth projected to converge to 4 percent and a further narrowing of the current account deficit.

However, significant risks remain. Growth is vulnerable to a continued or sharper economic slowdown in the main trading partners. The main vulnerabilities remain in the fiscal sector, as public debt is still high, and contingent liabilities are increasing. Albania's relatively large financing needs also pose risks that could materialize, in particular, in case of tightening external financing conditions.

Mitigating these risks and supporting sustainable high growth requires:

- Policies to improve the business climate, including through better governance, infrastructure, and skills formation.
- A further improvement in the fiscal position by strengthening the revenue base. This would help create room for absorbing or offsetting adverse shocks.
- Actions to limit the risks from PPP-related contingent liabilities and to ensure more consistent public investment management.
- Continued strong financial sector supervision to ensure that the expected increase in bank lending does not weaken financial stability.

Albania's capacity to repay the Fund is adequate. Fund credit outstanding stood at 2.8 percent of GDP or 10.4 percent of gross international reserves in 2018. Albania's strong record of repaying the Fund and relative macroeconomic stability also suggest that repayment risks are contained.

Approved By **Jörg Decressin (EUR) and Nathan Porter (SPR)**	Discussions took place in Tirana during April 25–May 7, 2019. The staff team comprised Mr. Martijn (head), Ms. Khachatryan and Mr. Lafarguette (EUR), Ms. Nersesyan (FAD), and Ms. Spahia (local economist). Messrs. Fanizza and Di Lorenzo (OED) attended some of the meetings. Mr. Kopyrski and Mr. Stewart (EUR) assisted in the preparation of the staff report. The staff team met with Minister of Finance and Economy Denaj, Bank of Albania Governor Sejko, representatives of the Ministry of Energy and Infrastructure and the Ministry of Justice, Parliamentarians, other senior officials, donors and representatives from banks and the private sector.

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CONTEXT

1. Two years after the end of the last IMF-supported program, and notwithstanding robust economic growth, Albania faces pressing policy challenges. The country remains vulnerable to climatic conditions, adverse demographic developments, and external spillovers. Alongside successful further fiscal consolidation, structural reforms have slowed since the completion of the program. Reforms should focus on reducing vulnerabilities of economic growth and the public finances, and on improving governance and productivity in order to attain higher living standards for all parts of society. Successful implementation of these reforms would also reduce the appeal of emigration and help pave the way towards further EU integration.

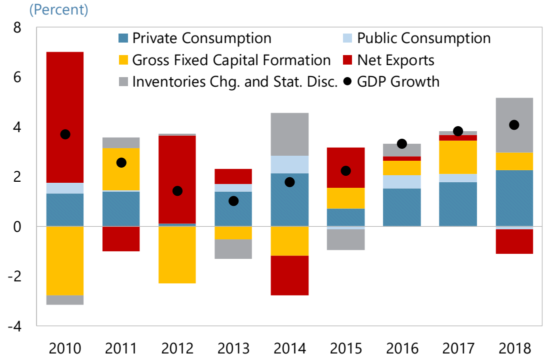
2. Politics have entered a period of heightened uncertainty since February 2019 when members of the opposition parties started renouncing their seats in Parliament. Furthermore, after the President decided on June 10 to cancel the local elections scheduled for end-June, the government responded that these elections would move forward as planned, and this issue remains to be resolved. At end May, the European Commission recommended that the EU Council decides to open accession discussion with Albania, pointing, in particular, to progress in reforming the justice system.

RECENT DEVELOPMENTS AND OUTLOOK

3. Growth was strong in 2018, backed by historically high electricity production. Real GDP grew by 4.1 percent in 2018--the highest rate since the global financial crisis. Although growth was broad-based, the largest contribution—0.9 percentage point—came from record-high hydropower production due to ample rainfall. On the demand-side, growth was primarily driven by consumption. The current account deficit narrowed to 6.8 percent of GDP, as import-intensive large energy projects were winding down, electricity production surged, and services exports, including tourism, grew strongly.

Real GDP Growth: Expenditures Constributions

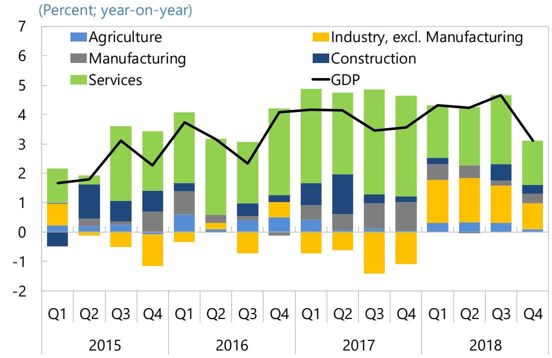
(Percent)



Sources: INSTAT; and IMF staff estimates.

Real GDP Contributions

(Percent; year-on-year)



Sources: INSTAT; and IMF staff calculations.

4. While monetary conditions are very accommodative, inflation remains subdued. Despite strong growth, the output gap remains negative, and headline inflation continues to be subdued at 1.4 percent in April 2019, well below the BOA's 3 percent target. Core inflation remained below 1 percent over the last six months. The BOA has maintained a very accommodative monetary policy stance; since the latest rate cut in June-2018, the policy rate has been at a historic-low 1 percent. The central bank ceased its FX interventions in the fall of 2018, after buying foreign currency in the spot market starting in June 2018. These interventions aimed to address disorderly market conditions and mitigate deflationary pressures stemming from the sharp appreciation of the Albanian lek during the first quarter of 2018.

5. The fiscal stance in 2018 was somewhat tighter than expected as lower tax revenue (especially VAT and excises) was more than offset by lower spending (mostly on capital, social insurance and wages). As a result, the fiscal deficit declined by 0.4 percentage points of GDP relative to the outcome in 2017, to 1.6 percent of GDP.[1] Helped also by the exchange rate appreciation, public debt declined to 69.9 percent of GDP (including arrears) from 71.9 percent the year before. As of end-2018, domestic government arrears stood at 1.8 percent of GDP.

6. The economic outlook is broadly favorable. In 2019, growth is expected to slow down to 3.5 percent, due to the base effect of the 2018 peak in power generation and the economic slowdown in Albania's main partner countries. Over the medium-term, however, GDP growth is projected to converge to its 4 percent potential rate, as activity is expected to be driven by a pickup in EU growth, increasing labor market participation, a gradual strengthening of exports including tourism, and the investments needed to close Albania's large infrastructure gap. On the monetary side, as inflation remains well below the BOA target, the monetary policy stance should continue to be accommodative over the medium term, and normalization should be data-driven. Inflation is expected to converge slowly towards its 3 percent target by 2021, as the output gap narrows and imported inflation from the euro area recovers. The current account deficit is projected to narrow further over the medium term, supported by strong export growth and planned fiscal consolidation.

Authorities' Views

7. The authorities noted the potential for higher growth. The Ministry of Finance expected GDP growth to exceed 4 percent in 2019, due to a surge in construction and a record-high touristic season. They pointed to the ongoing investments in infrastructure, the benefits from past FDI in energy, strong consumer confidence, and favorable labor market dynamics. The Bank of Albania (BOA) expected inflation to reach the 3 percent target in 2020, one year earlier than in the staff's baseline projection. The BOA is monitoring inflation developments closely and noted it was prepared to take measures as needed to attain its inflation objectives as soon as feasible.

CAPACITY TO REPAY THE FUND

8. Albania's capacity to repay is adequate under the baseline. Fund credit outstanding stood at 2.8 percent of GDP or 10.4 percent of gross international reserves in 2018. By contrast, FX reserves were 26 percent of GDP or 6½ months of imports. Fund credit-outstanding

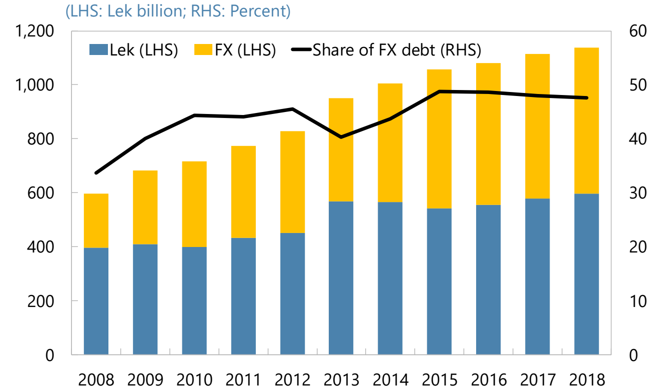
[1] Including the on-lending of government-guaranteed loans to the energy sector as part of government spending.

amounted to 209.4 percent of quota at end-2018 and is expected to remain above 200 percent of quota--the threshold for PPM--until November-2019. Debt service to the Fund is expected to peak in 2022 at around 0.4 percent of GDP and 1.5 percent of reserves, well within Albania's capacity to repay. Albania's strong record of repaying the Fund, and relative macroeconomic stability also suggest that repayment risks are contained.

9. The main vulnerabilities remain in the fiscal sector, as public debt remains high. Under the baseline scenario public debt will decline gradually, but alternative scenarios point to significant risks (DSA, Annex III)**.** Absent policy changes**,** debt is envisaged to decline to 56.8 percent of GDP by 2024. Under individual stress test scenarios, the debt path is especially sensitive to GDP growth and interest rate shocks. Among all stress test scenarios, Albania shows the highest vulnerability to a combined macro-fiscal shock, which would bring debt close to 72 percent of GDP as of 2020. Moreover, all scenarios exclude contingent liabilities arising from increasing PPP-financed investment and from energy sector losses (see below). Furthermore, domestic debt is highly concentrated--around 60 percent of it is held by the domestic banking system, held by a few large banks.[2]

10. Although gross public financing needs have declined from 37 percent in 2014 to about 19 percent of GDP in 2019, both public and external financing needs remain fairly large. Gross public financing needs are projected to remain above the 15 percent threshold (in the DSA) through the entire projection period. While the main sources of borrowing have been concessional, mainly from bilateral and multilateral donors, the authorities have shown an increasing appetite for external commercial borrowing, which is expected to increase as a share of total borrowing. Against this background, the main vulnerabilities will arise from: rollover risk, concentration risk due to the lack of diverse long-term institutional investors, and exchange rate risk. These risks could materialize, in particular, in case of tightening external financing conditions (see Annex I).

Currency Composition of Public Debt
(LHS: Lek billion; RHS: Percent)



Sources: Ministry of Finance.

11. Near-term risks to the necessary availability of foreign exchange are curbed by important mitigating factors. Albania's robust reserve coverage, at 189 percent of the ARA metric at end-2018 (and more than nine times Fund credit outstanding), and its flexible exchange rate remain important shock absorbers.[3] Access to donor-funded concessional and longer-term

[2] However, the average weighted maturity of domestic public debt has increased from less than a year in 2011, to 2.2 years at end 2018, with this debt being almost fully denominated in domestic currency.

[3] The External Sector Assessment presented in the January 2019 Staff Report for the 2018 Article IV Consultation remains valid.

external borrowing mitigates rollover risks. In addition, the successful allocation of Eurobonds and a buyback operation in 2018, helped improve the profile and maturity of public debt.

12. On balance, the impact of the potential realization of macro-fiscal risks on Albania's capacity to repay seems contained. As discussed below, the larger risks, which concern the prospects for economic development and the build-up of public sector contingent liabilities, are not immediate but pose concerns beyond the horizon of outstanding debt obligations. Growth shocks that could occur in the near term (including the impact of draught and political uncertainties), appear less likely to have a material impact on capacity to repay.

RISKS AND POLICY DISCUSSIONS

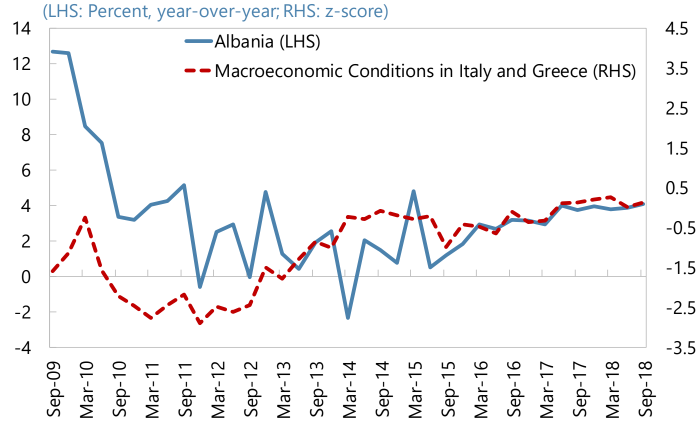
In line with the objective of post-program monitoring, the discussions focused on risks to growth, the public finances, and financial stability, and on policies to address key vulnerabilities

A. Risks to Growth

13. Albania's growth is vulnerable to shocks and faster income convergence hinges on ongoing structural reforms. The main contributors to growth on supply side have been electricity production, services and construction, which are prone to external and domestic risks. On the demand side, net exports have been the most volatile contributor to growth. In addition, increasing political uncertainties could have an adverse impact on domestic demand and investors' sentiment. Against the background of rising global uncertainties, a continued or sharper economic slowdown among Albania's main trading partners could hamper growth through reduced exports, remittance inflows and FDI.

Albania Growth and Regional Macroeconomic Conditions

(LHS: Percent, year-over-year; RHS: z-score)



Sources: Haver Analytics; and IMF Staff calculations.

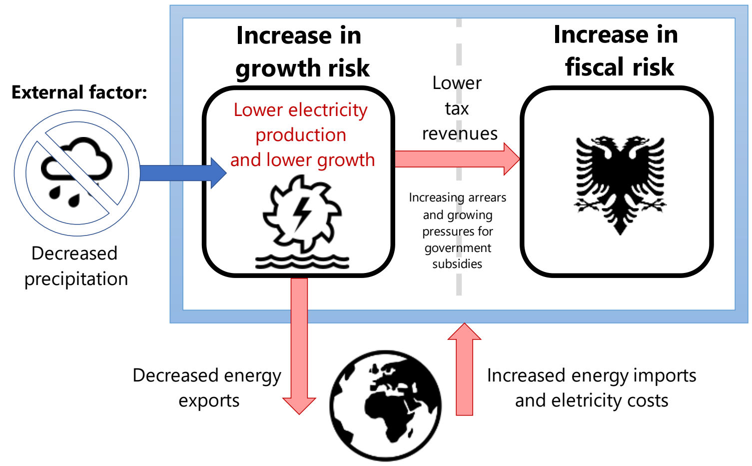
14. Domestic growth vulnerabilities include demographic prospects and heavy dependence of growth on climate conditions:

- **Albania's aging population and emigration pose risks to its productive capacity over the long run[4].** First, the labor force is projected to decrease substantially over the next three decades. The working age population has already started to decline, by 0.6 percent, over 2015-'19. Second, population aging could increase demands on healthcare and pension

[4] See EUR departmental paper 'Demographic Headwinds in Central and Eastern Europe' (Forthcoming Draft, 2019).

resources. During 2015-'19, the population above 65 years of age increased by 12 percent. While the existing (pay-as-you-go) public pension system offers very modest allowances and appears sustainable, spending pressures could rise in case of demands for higher replacement incomes. Third, aging of the labor force and brain-drain could cause average productivity to deteriorate.

- **Albania growth is highly dependent on weather conditions.** In the absence of sufficient precipitation, electricity production declines, affecting growth, the trade balance and the public finances. For example, a severe draught shock as occurred in 2017 could worsen the trade balance by about 0.6 percent of GDP[5] , with a similar potential impact on the public finances. While this shock could materialize in any year, its impact on Albania's capacity to repay the Fund seems manageable.



15. Staff emphasized the importance of policies to create an environment conducive to sustainable employment and growth. This requires improving the management and financial viability of energy sector, and measures to improve the quality of human capital. Moreover, sustained growth, including lifting exports and tourism growth, require taking full advantage of Albania's relatively low labor cost and proximity with the EU, which hinges on improvements in overall economic governance, transportation infrastructure, and the investment environment.

Authorities' views

16. The authorities broadly concurred with the staff view on risks to growth and agreed with the vulnerabilities shown in the risk assessment matrix (Annex I). They emphasized vulnerabilities to weather-related shocks and Albania's main Euro-Area trading partners, noting that these were long-standing and well understood. The authorities also mentioned their ongoing commitment to further structural reforms including to promote tourism, to enhance coordination within the energy sector, and to enhance road and airport infrastructure.

[5] Assuming a generation shortfall of 2000 Gwh and an import price of 40 Euros per Mwh.

B. Risks to the Public Finances

Strengthening the Fiscal Position

17. While the fiscal deficit declined to 1.6 percent in 2018, absent further measures, it is projected to widen to 2.5 percent of GDP in 2019 (including guarantees for new loans to the energy sector of 0.4 percent of GDP). This widening is driven in part by the planned repayment of government arrears which, by itself, is welcome. However, the deficit is also augmented by recent tax measures that erode the already narrow tax base. There are risks of further revenue shortfalls and expected losses in the energy sector due to lower hydropower production. Moreover, there are risks due to rising contingent liabilities, and a tightening of financial conditions in the euro area could raise the cost of financing.

Medium-term fiscal paths

(in percent of GDP)

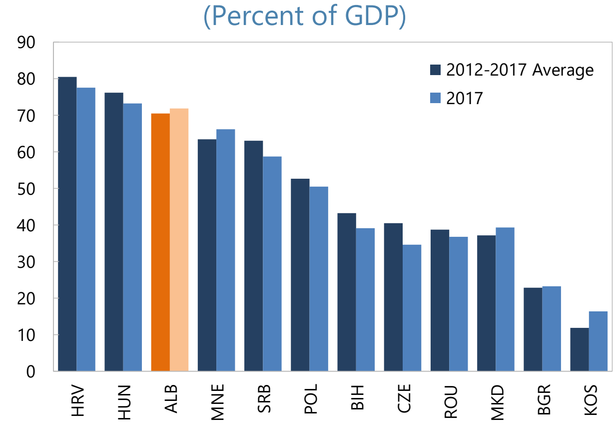
	2018	2019	2020	2021	2022
Overall balance					
IMF baseline	-1.6	-2.5	-2.0	-1.9	-1.8
IMF recommended path	-1.6	-1.8	-0.8	-0.5	-0.4
Authorities MTBF*		-1.9	-1.6	-1.2	-1.1
Primary balance					
IMF baseline	0.6	-0.5	0.0	0.2	0.2
IMF recommended path	0.6	0.2	1.2	1.5	1.5
Authorities MTBF*		0.5	0.9	1.5	
Structural primary balance					
IMF baseline	0.8	-0.3	0.1	0.2	0.2
IMF recommended path	0.8	1.0	1.4	1.5	1.5
Authorities MTBF*		0.2	1.0	1.5	
Public debt					
IMF baseline	69.9	66.3	64.6	61.6	59.7
IMF recommended path	69.9	65.6	62.7	58.5	55.3
Authorities MTBF*		65.5	63.7	59.9	

* MTBF as of November 2018. Based on the authorities' own definitions of debt and deficit (i.e., excluding some energy sector support from the deficit, and omitting arrears in the debt statistics).

18. Staff recommended using the favorable economic environment to improve the fiscal position by strengthening the revenue base. At the current level of public debt and the deficit, fiscal policy has little room for absorbing or offsetting adverse shocks. Specifically, a front-loaded fiscal adjustment to bring the primary surplus to 1.5 percent of GDP by 2021 should help build fiscal buffers, and ensure faster convergence of debt towards the 45 percent objective stipulated by the organic budget law. This adjustment should be achieved through higher revenues because Albania's large infrastructure and human development needs argue against expenditure cuts. Staff also reiterated its advice to bolster the fiscal rule, including by putting a cap on the annual fiscal deficits (with an escape clause to manage severe downturns) to underpin the medium-term debt objective.

CESEE: Public Debt

(Percent of GDP)



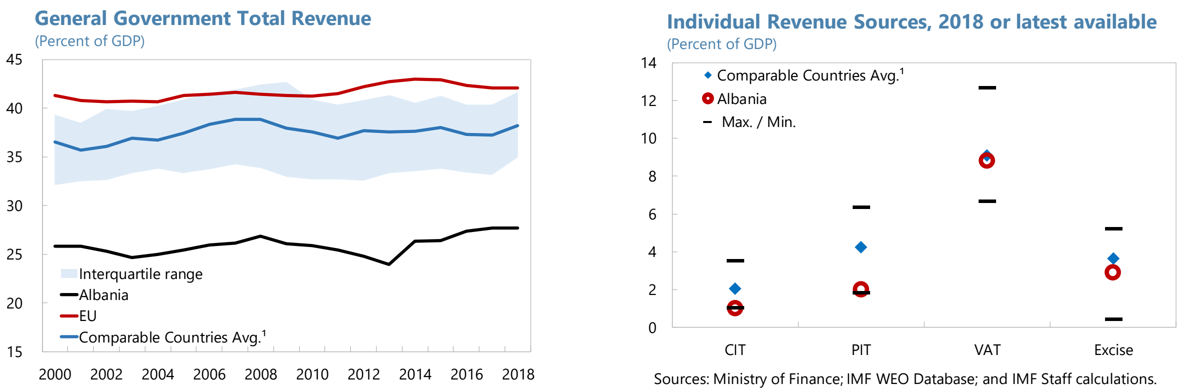
Source: IMF, WEO database.

19. While headline rates of the VAT, as well as corporate and personal income tax rates[6] are broadly in line with regional peers, revenue performance lags behind, in part due to recent tax base-narrowing measures, coupled with low compliance. Tax cuts and sector-

[6] The standard VAT rate is 20 percent, the standard CIT rate is 15 percent and the top personal income tax rate is 23 percent as of May 2019.

specific incentives introduced in 2018 and 2019 have further eroded the system's revenue generating capacity, as well as the tax system's efficiency and simplicity.[7] For example, the government has significantly expanded exemptions in the VAT, and introduced preferential treatment of additional sectors, including through reduced VAT and corporate tax rates. It also increased the turnover-based threshold for businesses in corporate taxation, from ALL 8 to ALL 14 million (see Box 1).

Figure 1. Government Revenues



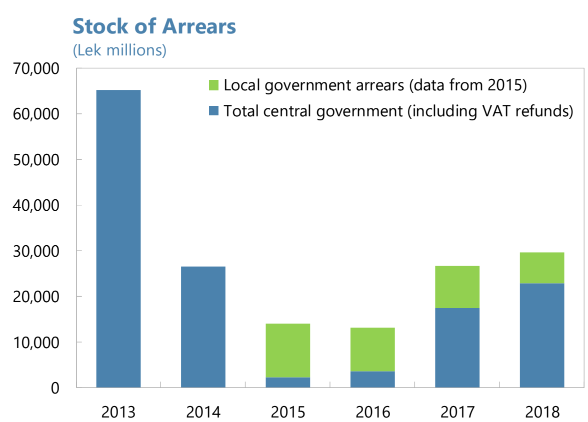
Sources: Ministry of Finance; IMF WEO Database; and IMF Staff calculations.

Sources: Ministry of Finance; IMF WEO Database; and IMF Staff calculations.
CIT = Corporate Income Tax; PIT = Personal Income Tax; VAT = Value Added Tax.

Unweighted average of select regional comparators, including BLR, BIH, BGR, HRV, CZE, EST, HUN, UVK, LVA, LTU, MKD, MDA, MNE, POL, ROU, RUS, SRB, SVK, SVN, TUR, UKR.

20. **Staff recommended strengthening the tax system by reversing measures that fragment and weaken the tax base and by levelling the playing field across businesses.** In this context, staff welcomed the authorities' intention to develop a medium-term revenue strategy (MTRS) covering both tax policy and administration. It would provide a medium-term anchor, helping to build consensus on revenue goals and on a comprehensive package of tax measures for achieving them.

21. **Urgent action is needed to curtail the persistent public sector arrears.** These arrears undermine the business climate and the communication strategy of the tax authorities aimed at improving voluntary compliance. Staff urged the authorities to ensure the full and timely payment of all validated new VAT refund requests from now on, disconnecting them from corresponding revenue flows. In this context, staff welcomed



Sources: Ministry of Finance; and IMF Staff calculations.

[7] See the January 2019 Staff Report for the 2018 Article IV Consultation.

the authorities' plans to repay the outstanding stock of VAT refund arrears as soon as feasible (and for the most part within 2019). It is also important to take swift measures to strengthen commitment controls for investment projects to put an end to government payment arrears, in particular by the road fund.

22. Staff recommended strengthening debt management. While the increased reliance on Eurobond issuances may seem beneficial in favorable times, building a robust and liquid domestic debt market should be a priority as it helps mobilize domestic savings and reduces currency and rollover risks. Staff advised resuming the issuance of short-term (three-months and six months) T-bills. This would be in line with the debt issuance strategy prepared in collaboration with the World Bank. These instruments are necessary for cost-efficient cashflow management by the treasury as well as commercial banks, for the development of secondary and hedging markets—which utilize the pricing at different segments of the yield curve—and for facilitating BOA liquidity management. More generally, it is critical to strengthen the MOFE's debt management capacity and to ensure good coordination with the BOA.

Authorities' Views

23. The authorities expected to meet their 1.9 percent of GDP deficit target for 2019, as they had identified sufficient buffers on the spending side to offset expected revenue shortfalls. They presented plans to prevent the creation of new VAT refund arrears while settling the existing arrears on an accelerated schedule (within their updated budget estimates). The authorities emphasized the importance of preparing a broad diagnosis of the revenue system and a medium-term roadmap for future reform. The authorities also noted that short-term Treasury bills had been crowded out by recent benchmark issuances at longer maturities, and agreed with the case for maintaining three-months instruments to support financial market development.

Containing Fiscal Risks

24. Albania faces significant infrastructure gaps compared to its regional peers, which are currently being addressed through the extensive use of PPPs. More than 200 PPP projects (31 percent of GDP) have been contracted, with about 15 percent of GDP in the pipeline. [8] However, PPPs are not well integrated into the overall public investment management framework, with a separate process--compared to traditionally procured projects--for assessing feasibility, affordability and risks. At the same time, the projected annual budget payments for (government-funded) PPPs are already approaching the legislated ceiling amounting to 5 percent of the previous year's fiscal revenues. Power generation projects account for about 23 percent of GDP and are covered by power purchase agreements that determine the purchase price, with little apparent residual fiscal risk. Most of the other projects relate to infrastructure

[8] Based on the 2019 budget documentation.

and are still in the planning or construction phase. The associated fiscal risks (including due to minimum revenue guarantees), would likely materialize over the medium or longer term.

Box 1. Assessing the VAT Effectiveness in Albania and Measures to Enhance it

The effectiveness of the VAT in raising revenue depends critically on its policy design and the success of its enforcement. In Albania, the significant number of deviations from an ideal VAT structure undermine its revenue potential as well as its efficiency and neutrality. We measure the relative revenue performance of the VAT by calculating the C-efficiency (Figure below). Albania's C-efficiency is one of the lowest in the comparator group of regional peers, pointing to vulnerabilities in the VAT system, including exemption and reduced rates, as well as weak enforcement.

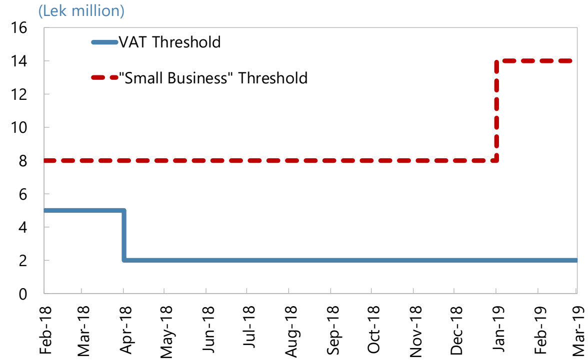
VAT, C-efficiency

Montenegro	0.80
Croatia	0.79
Bosnia and Herzegovina	0.76
Estonia	0.73
Belarus	0.71
Slovenia	0.65
Bulgaria	0.64
Serbia	0.61
Hungary	0.60
Czech Republic	0.59
Northern Macedonia	0.57
Albania	0.54
Slovak Republic	0.51

Source: IMF, FADTP C-Efficiency Database (internal).

Turnover-based Tax Thresholds

(Lek million)



Sources: Decision of the Council of Ministers no. 652, November 2017. Law No. 39/2018 dated 9 July 2018.

Even at relatively low levels, the C-efficiency indicator overestimates Albania's VAT effectiveness due to the outstanding stock of VAT refund arrears—at 1.2 percent of GDP at the end of 2018. The authorities plan to tackle the issue with two complementary streams. The first stream addresses the structural nature of the VAT refunds, reducing the further build-up of VAT refund arrears; it ensures a reduced flow of new refund claims through structural policy changes, including, for example, an introduction of a reverse-charge mechanism for the TAP project. The second stream institutes a gradual repayment schedule, based on consultations with the private sector, introducing a greater transparency and predictability into the refund payment process.

Expanding the VAT base and eliminating preferential reduced rates would considerably improve the revenue effectiveness of Albania's VAT. The recent lowering of the VAT registration threshold from ALL 5 to 2 million should be re-considered.

VAT C-Efficiency = VAT Revenue/(Total Final Consumption net of VAT Revenue * VAT Rate). A ratio closer to 1 is indicative of lesser deviation from the 'ideal' VAT system–a single VAT rate, uniformly applied on all consumption.

25. Staff urged the authorities to make use of proposed amendments to the PPP law to limit the risks from PPP-related contingent liabilities and to ensure more consistent public investment management. This is important to protect the public finances and to help ensure value for money. Staff welcomed the amendments that aim to improve risk management of PPPs. However, as the MOFE embarks on its new role as gatekeeper for PPPs, it will be essential to make sure it has the capacity to assess the risks and costs of these projects, particularly in the pre-feasibility stage. In this context, the Ministry should have access to all contractual information from line-ministries (including for existing projects). In addition, reversing the fragmentation of decision making in public investment management, including through upcoming regulations, would greatly enhance cost-effectiveness. Staff also continued urging the authorities to abolish the use of unsolicited proposals for all PPPs.

26. The authorities are considering the establishment of the Albania Investment Corporation (AIC)—a development institution that would exploit "idle" state assets using IFI as well as other sources of funding. The corporation's tasks would include the preparation and implementation of investment projects on state-owned property, and to fund or co-fund such projects.

27. Staff strongly advised the authorities to revisit the proposals for establishing the AIC, to avoid risks to the budget and to the integrity of the public investment management framework. As it stands, the draft law would allow the government to direct individual investment decisions, which could make the AIC an off-budget spending tool that risks eroding fiscal discipline and circumventing public investment management processes. Instead, the framework should ensure that the AIC will operate on a commercial basis and at arm's length of government. The law should affirm the independence of the AIC in operational decisions and in selecting individual investment projects. Staff also recommended limiting the government's financial contribution to the AIC more explicitly in the legislation and making the AIC subject to the Public Procurement Law.

28. Containing fiscal risks also requires improving the performance of the energy sector, which is financially weak and struggling with endemic arrears (Box 2). The dependence of the sector on rainfall exacerbates its financial vulnerability and creates risks for the government budget (including this year). Staff encouraged the authorities to implement the restructuring plan for the sector prepared with World Bank advice to put the sector on a sustainable financial footing.

Box 2. Albania's Power Sector: Challenges and Solutions

Albania benefits from low electricity costs owing to its's reliance on hydropower. The sector consists of three major SOEs—for generation (KESH), transmission (OST), and distribution (OSHEE)—and more than one-hundred small private and concession-type hydropower plants (HPPs). KESH generates about two-thirds of the total electricity production from three hydro-powerplants on the Drin cascade. The country's only thermal power plant is currently non-operational. The reliance on hydropower creates significant weather-related vulnerabilities, with escalating (and expensive) import needs in years of drought. The Trans-Adriatic Pipeline (TAP), which will deliver Central Asian gas through Greece and Albania to Europe, is expected to increase demand for gas-fired energy and manufacturing investments in Albania. Its construction is expected to finish in 2019.

Persistent governance problems have left the sector with sizeable intra-company and intra-sector arrears. Underlying problems include a lack of accountability and transparency, and distortions in intra-company pricing mechanisms throughout the sector. Consequently, the sector has relied on repeated public support.

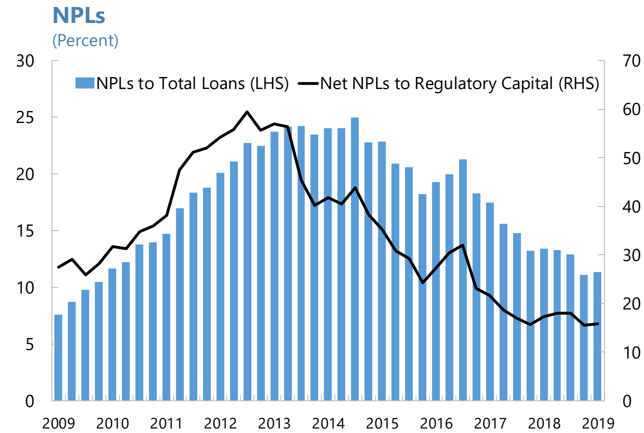
Going forward the authorities are determined to implement a financial recovery plan for the sector, supported by the World Bank. The plan aims at: (i) Improving the governance of the power companies, cleaning their balance sheets, and establishing rules for clearing intra-company and intra-sector arrears, (ii) establishing targets and controls for loss reduction, (iii) establishing clear borrowing rules, including for bank overdrafts, (iv) improving transparency and accountability concerning investment plans, and (v) the unbundling of OSHEE and finalizing the sector's liberalization.

Authorities' Views

29. **The authorities noted that they were preparing for the new role of the MOFE as gatekeeper for PPPs, and were upgrading their risk management.** Supported by TA from the World Bank and the Fund, they were putting in place the necessary organization and systems, including regulations. They were also considering the incorporation of feedback received from IFIs on the planned AIC. The authorities indicated that the financial recovery plan for the power sector had recently been adopted.

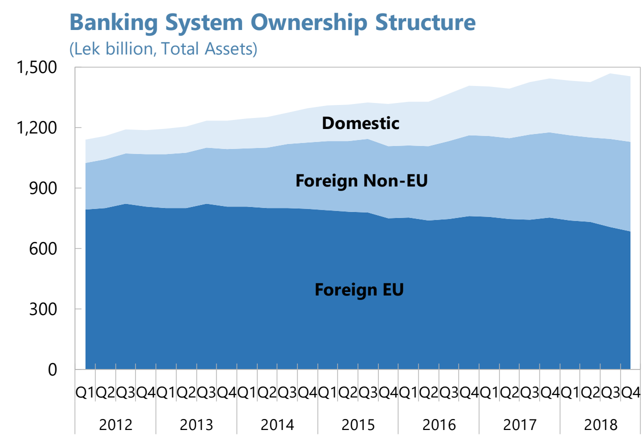
C. Risks from the Financial Sector

30. Overall, the banking sector in Albania is very liquid, and average regulatory capital stands at 18%, well above the minimum regulatory requirements (12% for most banks). However, bank balance sheets require further strengthening; while the NPL ratio in the banking sector has declined sharply between 2015 and mid-2018, progress has halted, and the NPL ratio still stands around 11%. **Fiscal and balance of payments risks** arising from the financial sector to Albania's capacity to repay appear small given its current financial position, the predominance of foreign ownership of the systemically important banks, and the absence of public ownership in the financial system.



Sources: Bank of Albania; and IMF staff estimates.

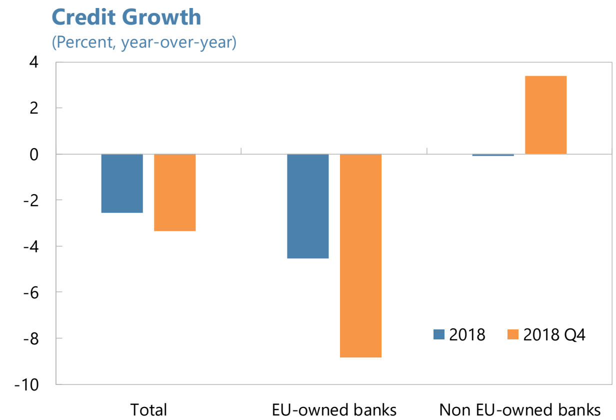
31. The banking sector is finalizing a significant consolidation, from 16 banks in 2016 to 13 at present. Within this process, bank ownership has shifted from long-established EU banks to new players-–some without banking experience, raising concerns about the quality of bank governance and risk management capacity. To cope with these risks, the BOA has adopted a more intensive inspection and supervision framework, both on-site and off-site, for banks with new shareholders. These measures are part of a broader effort by the central bank to further align the regulatory framework with international standards (Annex II).



Sources: Bank of Albania; and IMF Staff calculations.

32. Structural weaknesses in credit provision affect the credit channel, especially for SMEs, and hinder the transmission of monetary policy. Credit growth has been subdued in Albania over the last seven years but has recently shown some signs of recovery in specific market segments (local currency, loans to households).

33. To enhance financial sector resilience and intermediation, staff:



Sources: Bank of Albania; and IMF Staff calculations.

- Welcomed the substantial efforts made by the authorities to strengthen the supervisory and regulatory framework, in particular with regards to banks with new owners.

- Noted that other banks, including systemically important ones, were inspected on-site only once every two years, and advised the BOA to increase the frequency of inspections to once every year to enhance its ability to identify risks stemming from large exposures and related-party lending in a timely manner.

- Recommended unlocking credit growth further through an ultimate resolution to the stalemate with bailiffs on the new tariff structure, full implementation of the insolvency and resolution framework based on the legislation adopted [last year], and government measures to support further de-euroization. Staff also recommended action to reduce NPLs further.

- Emphasized the importance of ensuring strong and independent supervision of the emerging nonbank financial system by the Albanian Financial Supervisory Authority (AFSA), which is progressively preparing the necessary regulatory framework.

- Urged the authorities to continue reforms to address weaknesses in the AML/CFT framework including to support anti-corruption efforts, by implementing the action plan to address the deficiencies identified in the 2018 Moneyval evaluation report without delay.

Authorities' Views

34. The authorities broadly concurred with the staff views and announced plans to increase the frequency of on-site inspections for domestically large and systemically important banks to an annual cycle. The authorities remained confident that bank risks were adequately monitored and under-control, and that domestic banks were coping well with the new financial regulations and standards. They had prepared plans for enhancing financial education, that were expected to support further de-euroization. To help reduce NPLs, they were preparing a new framework to facilitate out-of-court restructuring of distressed loans. The authorities also explained that the AML/CFT action plan was being implemented broadly in line with the schedule.

STAFF APPRAISAL

35. Following strong growth last year, the baseline projections foresee an ongoing economic expansion. Furthermore, inflation remains well under control, and the current account is expected to improve further. However, more ambitious improvements in governance and anti-corruption efforts, skills formation and other aspects of the business environment will be needed to raise potential growth, and take advantage of the country's favorable location and low labor costs.

36. As a small open economy, with limited economic diversification, Albania remains considerably exposed to external and domestic risks. The country is especially vulnerable to drought, population aging combined with the ongoing emigration of skilled workers, and spillovers from lower growth in key trading partners. Furthermore, as a result of still high public debt, relatively large financing needs, and rising contingent liabilities, severe adverse shocks to growth or a deterioration in regional financial conditions could quickly undermine Albania's public balance sheet and impair its access to affordable financing.

37. At the same time, Albania's flexible exchange rate and ample reserves offer important tools for absorbing shocks. Furthermore, the recent fiscal consolidation and the lengthening of the maturity of public debt have also been helpful. As a result, risks to Albania's capacity to repay appear contained. Nonetheless, more is needed to limit risks related to the public finances.

38. It is critical to implement further fiscal adjustment, combined with improvements in the quality of budgetary policies. Accelerating the reduction in public debt over the medium term, will create space to absorb and offset adverse shocks through countercyclical fiscal policies. Given the need to improve Albania's infrastructure and human development, fiscal consolidation should be underpinned by improvements in tax policy and tax administration that lead to higher revenues. Such reforms should be supported by a careful analysis of the revenue system and a medium-term strategy to enlarge the tax base and level the playing field for businesses.

39. The authorities' ambition to address the buildup of fiscal arrears is most welcome. These arrears have undercut the business climate as well as trust in the government. Going forward, all validated new VAT refund requests should be honored without delay, and the existing arrears should be cleared as soon as feasible—even if, in the short term, this may raise the deficit (measured on a cash basis).

40. It will be important to put in place a more consistent framework for public investment management, and to limit the risks from PPPs and other contingent liabilities. The Ministry of Finance and Economy should exploit its new role as gatekeeper for new PPP projects to help ensure both value for money and the containment of risks. Furthermore, the proposed establishment of the AIC should be revisited, to make sure that--if such institution is created--it will act on a strictly commercial basis and without direct government interference or reliance on future budget support.

41. The energy sector needs to be put on a sound footing without delay. Given sector's endemic financial weakness and accumulating arrears, financial restructuring should be undertaken without delay, combined with continued actions to liberalize the sector and unbundle its key players.

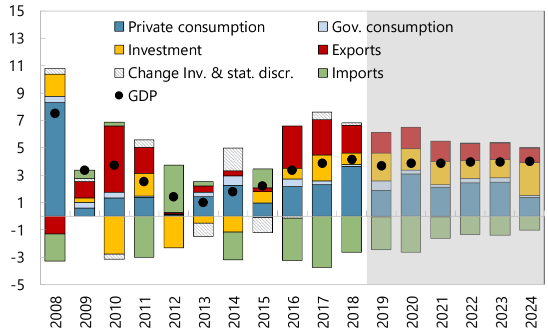
42. Debt management should reconcile the search for lower financing costs and longer maturities, with the need to support the development of a robust and liquid domestic debt market. The latter would help mobilize domestic savings and reduce currency and rollover risks. In this context, it will be important to resume the issuance of short-term T-bills.

43. Continued strong supervision will be important to ensure that the expected increase in bank lending does not weaken financial stability. The banking sector has experienced a large-scale consolidation, combined with a shift in ownership away from EU banks. Against this background, the BOA's recent measures for further alignment with EU standards and the increased frequency of on-site inspections should be helpful, particularly to contain risks from large exposures and related-party lending. Further actions will be needed to address weaknesses in the AML/CFT framework

Figure 2. Albania: Real Sector Developments

Domestic demand has been the main driver of the strong GDP growth in recent years.

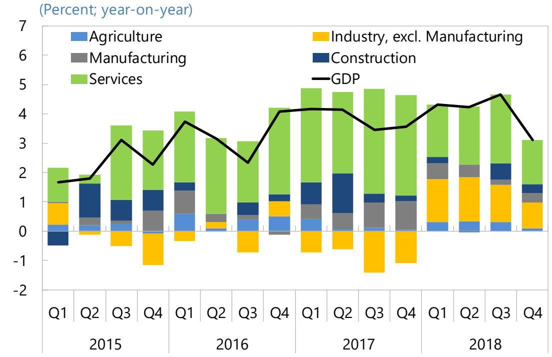
Real GDP Growth: Expenditures contributions
(Percent)



Sources: IMF Staff estimates.

On the supply side, the impact of higher electricity production (part of industry) in 2018 stands out.

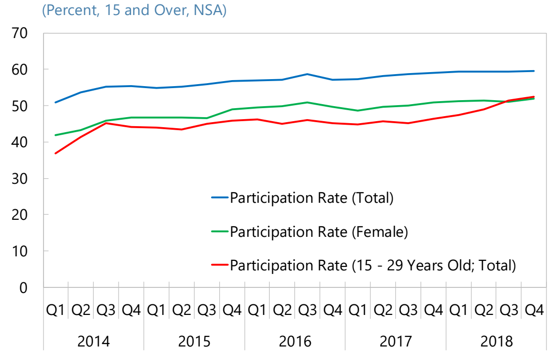
Real GDP Contributions
(Percent; year-on-year)



Sources: INSTAT; and IMF staff calculations.

Participation rates have been edging up

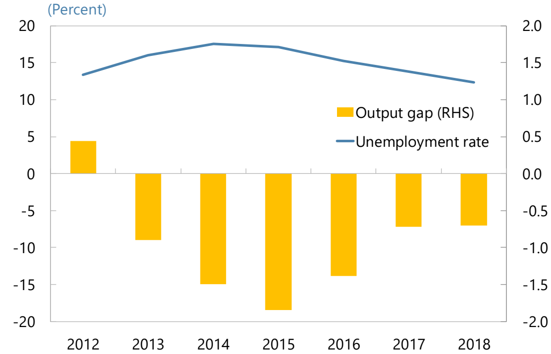
Participation Rates
(Percent, 15 and Over, NSA)



Sources: Haver Analytics; and IMF Staff calculations.

And the unemployment rate has been declining since 2014, but remains high; above 10% of the active population

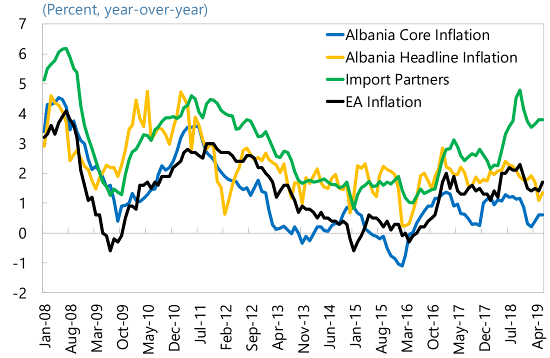
Unemployment Rate and Output Gap
(Percent)



Sources: Haver Analytics; and IMF staff calculations.

Consumer prices have been subdued since 2011, despite higher import partner inflation

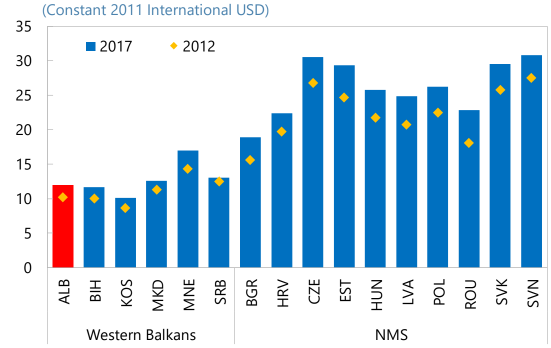
Consumer Price Index
(Percent, year-over-year)



Sources: Haver Analytics; IMF, Direction of Trade database; and INSTAT.

Albania is one of the poorest countries in Europe and has not been catching up over the last decade

GNI per Capita, PPP Adjusted
(Constant 2011 International USD)

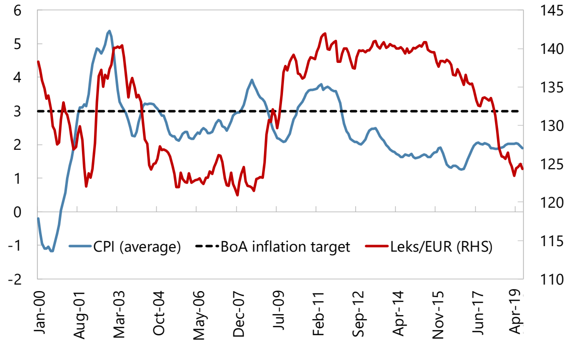


Source: World Bank, World Development Indicators.
Data not available for Lithuania.

Figure 3. Albania: Monetary Sector Developments

Inflation has been below target for more than 8 years…

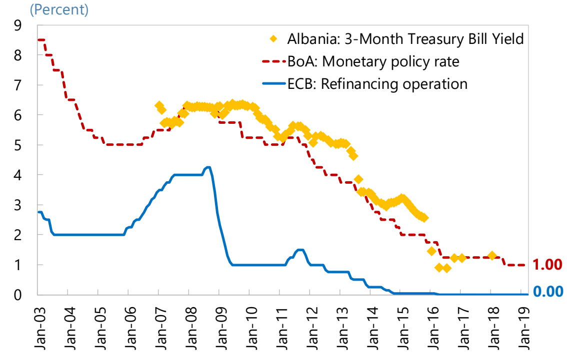
Average Inflation and Exchange Rate
(Percent)



Sources: Haver Analytics; INSTAT; and IMF staff calculations.

…despite a historically accommodative monetary stance.

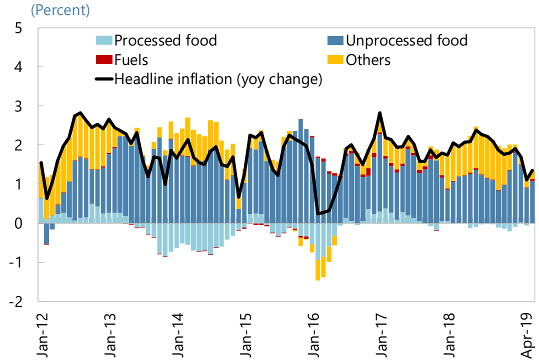
Monetary Policy Rates
(Percent)



Sources: Haver Analytics; and IMF staff estimates.

Headline inflation is driven by unprocessed food, the largest non-core component.

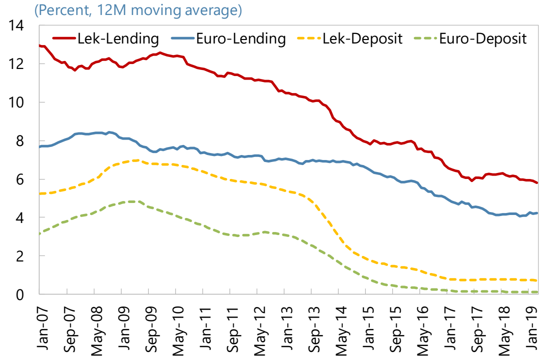
Headline Inflation
(Percent)



Sources: INSTAT; and IMF staff estimates.

Lending rates have declined less than deposit remuneration, widening banking spreads.

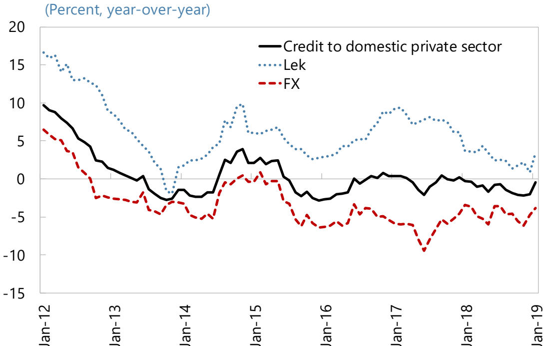
Lending and Deposit Interest Rates, 12-Month
(Percent, 12M moving average)



Sources: Haver Analytics; and IMF staff calculations.

However, despite low funding costs and liquid financial system, credit to the private sector has been contracting.

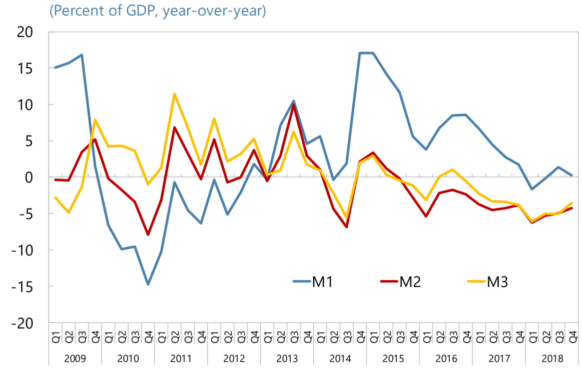
Credit to Domestic Private Sector
(Percent, year-over-year)



Source: Bank of Albania.

Therefore, monetary aggregates in Albania have also been contracting.

Money Supply
(Percent of GDP, year-over-year)



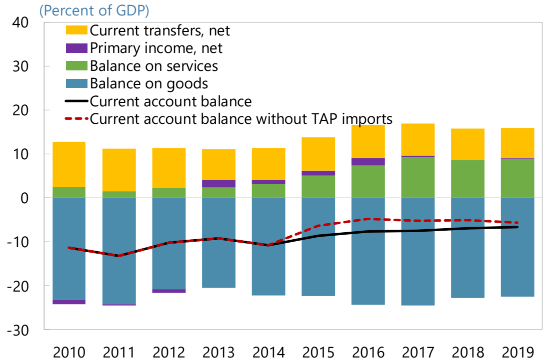
Sources: Haver Analytics; and IMF staff calculations.

Figure 4. Albania: External Sector Developments

The current account deficit has narrowed due to strong growth of energy and services exports…

Current Account Balance

(Percent of GDP)

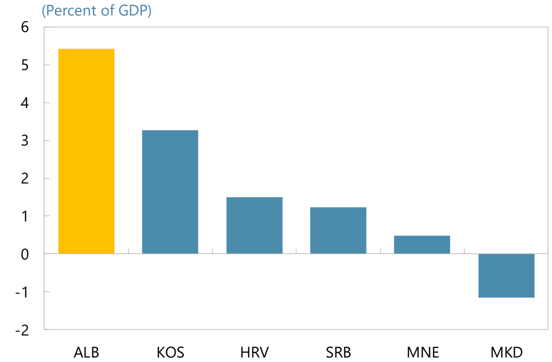


Sources: Bank of Albania; and IMF Staff calculations.

…with the marked improvement in the services balance driven primarily by tourism exports.

Change in Services Balance Relative to GDP, 2014-2018

(Percent of GDP)

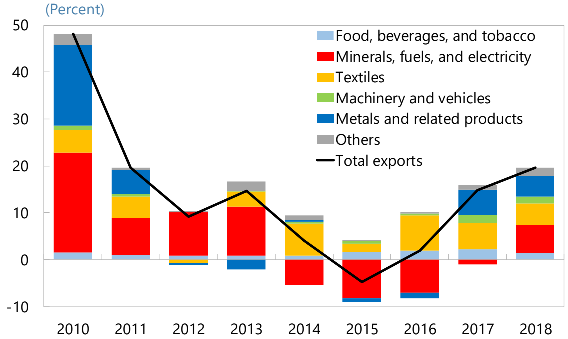


Sources: Bank of Albania; and IMF staff calculations.

Growth of goods exports has picked up largely due to energy exports, especially of electricity…

Contribution to Export Goods Growth

(Percent)

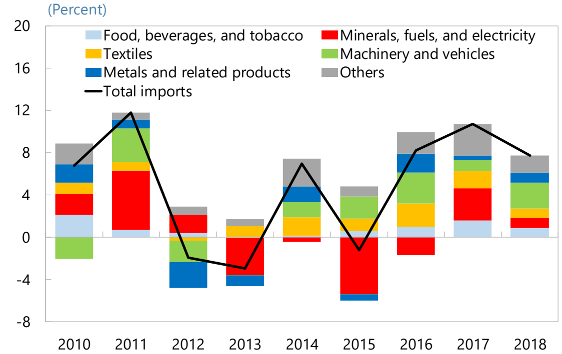


Sources: Haver Analytics; and IMF staff calculations.

…while import growth has slowed as import-intensive energy projects have started to wind down.

Contribution to Import Goods Growth

(Percent)

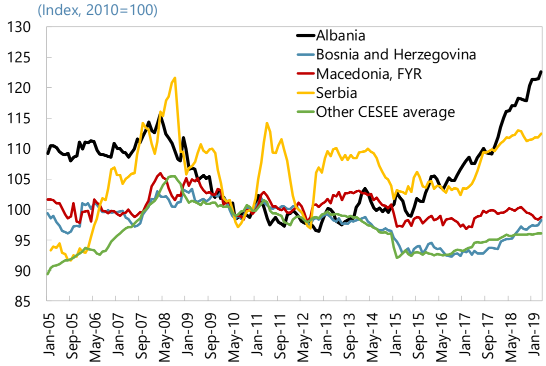


Sources: Haver Analytics; and IMF staff calculations.

Albania's real effective exchange rate has appreciated significantly more than peers…

CESEE: Real Effective Exchange Rate

(Index, 2010=100)

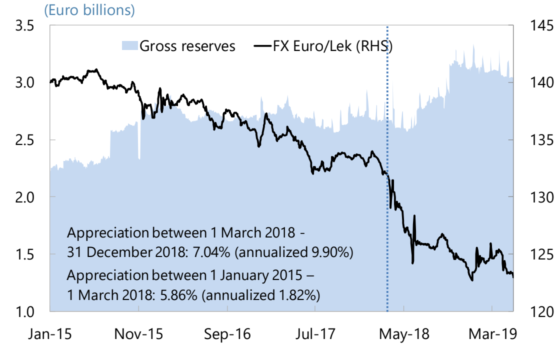


Sources: IMF, INS database; and IMF Staff calculations.

…and the country has accumulated substantial FX reserves.

Reserves and Foreign Exchange Rate

(Euro billions)

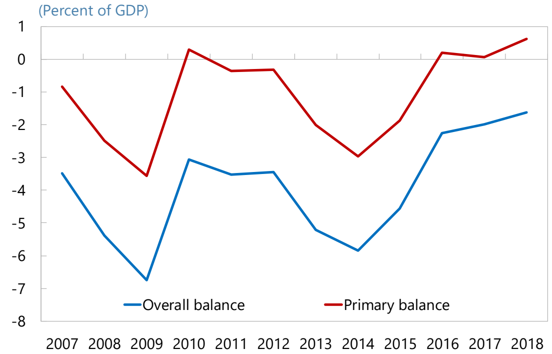


Sources: Bank of Albania; and Haver Analytics.
Rates annualized using 365 days/year.

Figure 5. Albania: Fiscal Sector Developments

Fiscal balances have improved recently…

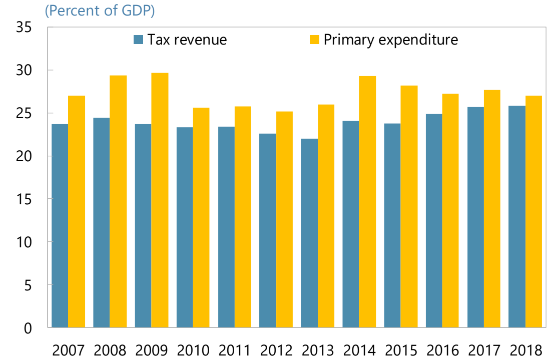
Overall Fiscal and Primary Balance
(Percent of GDP)



Sources: INSTAT; Ministry of Finance and Economy; and IMF staff calculations.

…driven by under-execution of expenditures, while tax revenues are stagnating

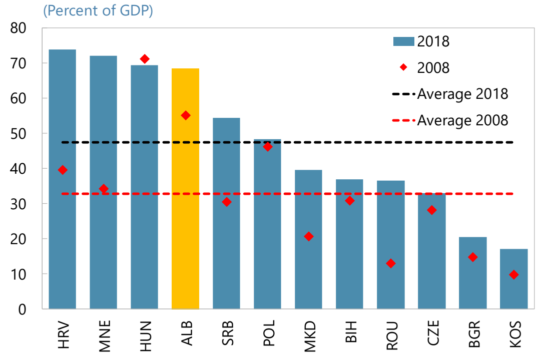
Tax Revenue and Primary Expenditure
(Percent of GDP)



Sources: INSTAT; Ministry of Finance and Economy; and IMF staff calculations.

Public debt has declined from its peak but remains high.

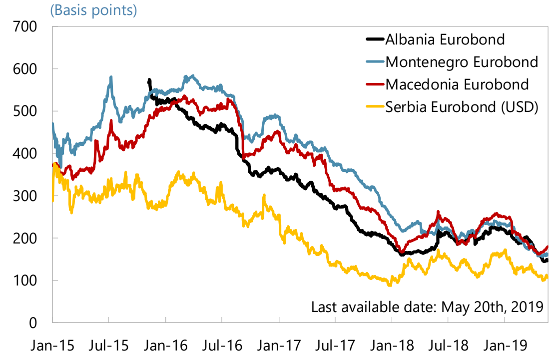
CESEE: Public Debt
(Percent of GDP)



Source: IMF, WEO database.

Sovereign spreads have been declining, in line with regional peers.

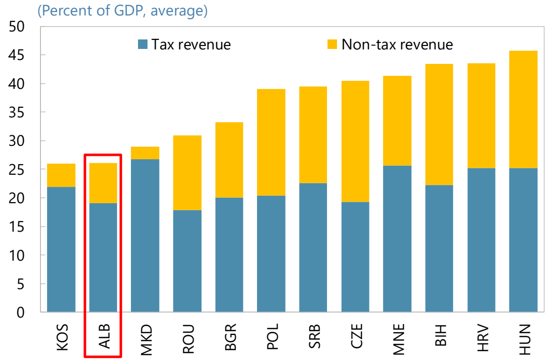
Selected Western Balkans: Sovereign Spreads
(Basis points)



Sources: Bloomberg Finance L.P.

Higher revenues could support fiscal consolidation…

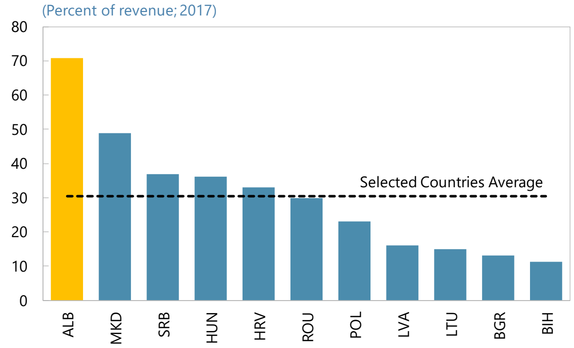
CESEE: Total Revenue, 2009-2018
(Percent of GDP, average)



Sources: IMF, WEO database; Haver Analytics; and IMF Staff calculations.

…and improve debt affordability given the high level of gross financing needs.

Gross Financing Needs, 2017
(Percent of revenue; 2017)

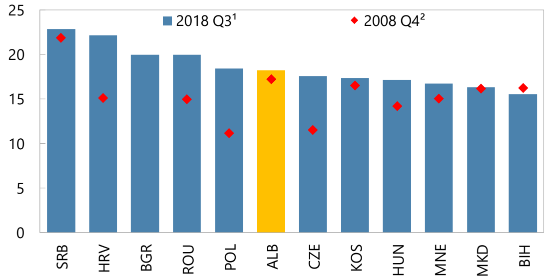


Sources: IMF; Vulnerability Exercise database; IMF, WEO databse; and IMF staff calculations.

Figure 6. Albania: Banking Sector Developments

Albanian bank capital has recovered and is now back to its pre-crisis level.

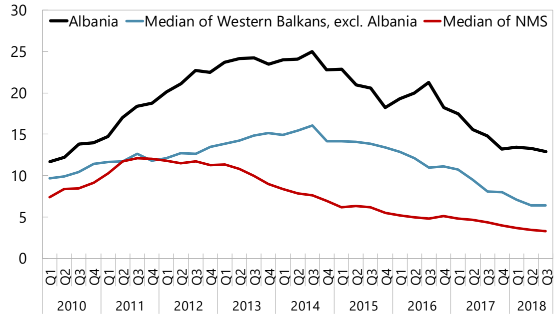
Regulatory Capital to Risk Weighted Assets
(Percent)



Sources: National authorities; IMF Financial Soundness Indicators; and IMF staff estimates.
1/ Except for Montenegro (2017 Q3).
2/ Except for Hungary, and Romania (2010 Q1).

Notwithstanding the recent and significant decline of NPLs, Albania's NPL ratio remains high.

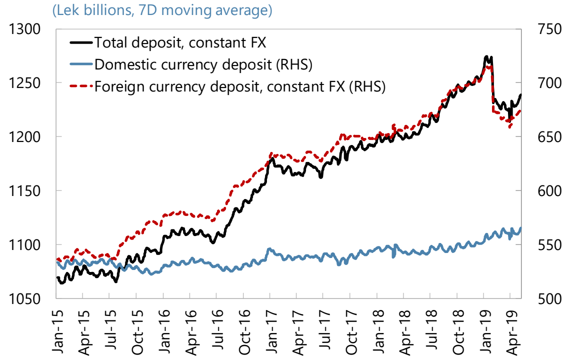
Non-Performing Loans
(Percent of total loans)



Sources: National authorities; IMF Financial Soundness Indicators; and IMF staff estimates.

While money creation in domestic currency has halted in Albania, deposits in FX have increased…

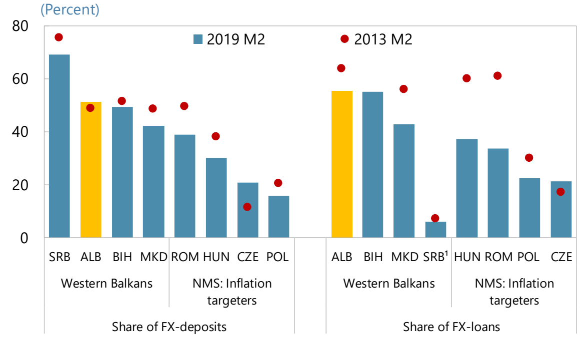
Albania: Deposit by Currency
(Lek billions, 7D moving average)



Sources: Bank of Albania; and IMF staff calculations.

…and Albania is one of the most euroized economies in the region

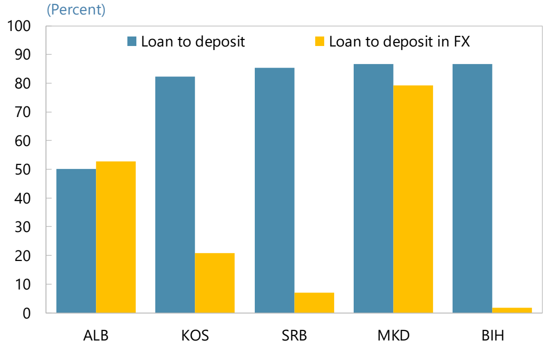
Euroization
(Percent)



Source: IMF, IFS database; and IMF Staff calculations.
1/ Doesn't include FX-indexed loans.

Financial intermediation is low in Albania, and the loan to deposit ratio is the lowest in the region…

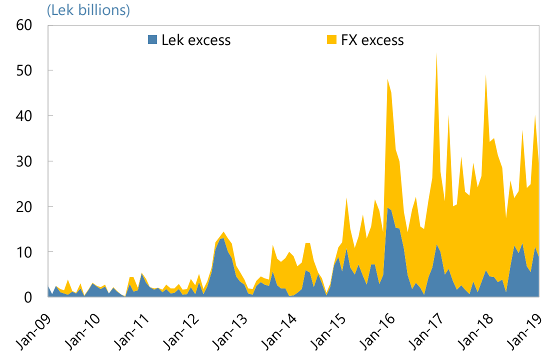
Loan to Deposits Ratio, 2018
(Percent)



Sources: IFS, MFS database; and IMF staff calculations.

…as banks are hoarding more cash at the central bank.

Commercial Banks: Reserves at the Central Bank
(Lek billions)

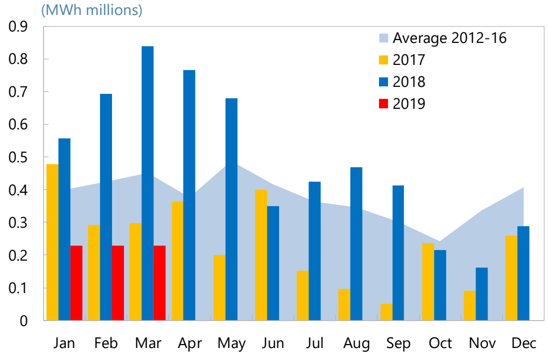


Source: Bank of Albania.

Figure 7. Albania: Electricity Sector—Selected Indicators

After a strong year of electricity generation, the lack of rainfall took toll on electricity generation

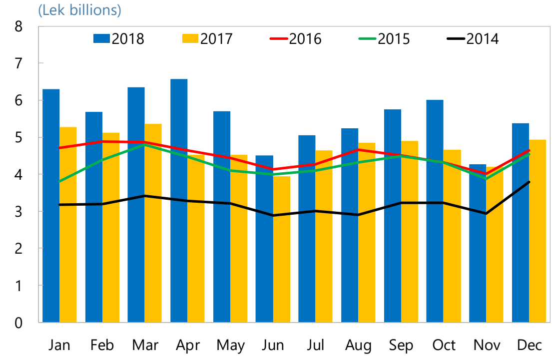
Net Electricity Generation by KESH
(MWh millions)



Sources: KESH; and IMF Staff calculations.

The collection of bills continued to improve....

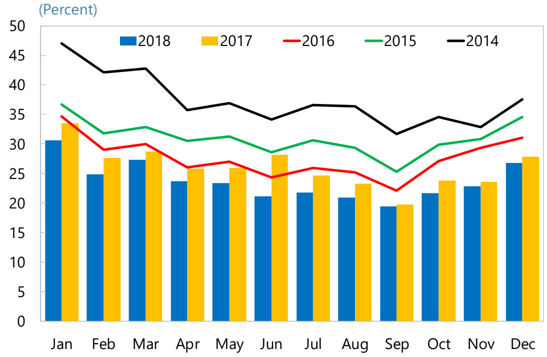
Current Bill Collections by OSHEE
(Lek billions)



Source: OSHEE.

While distribution losses declined from highs in 2014-2016, they continue to remain high

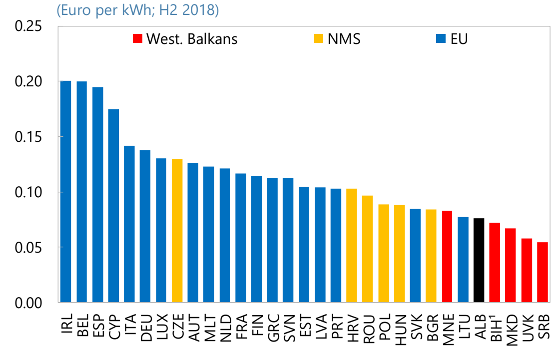
Electricity Distribution Losses
(Percent)



Sources: OSHEE; and IMF staff calculations.

Owing to reliance on low-cost hydropower and despite the sector's persistent financial problems, tariffs for household are among the lowest in the region....

Electricity Prices for Household Consumers
(Euro per kWh; H2 2018)



Source: Eurostat.
1/ H1 2018 data.

Table 1. Albania: Basic Indicators and Macroeconomic Framework, 2015–24

	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024
					Proj.					
Real sector										
Real GDP	2.2	3.3	3.8	4.1	3.5	4.0	4.0	4.0	4.0	4.0
Domestic demand contribution	0.6	3.2	3.6	5.0	4.0	4.3	3.9	4.0	3.9	4.0
Consumption	0.6	2.0	2.1	2.1	2.5	2.7	2.3	2.4	2.3	2.4
Investment (Incl. inventories and stat. disc)	0.0	1.1	1.5	2.9	1.5	1.6	1.6	1.6	1.6	1.6
External demand contribution	1.6	0.2	0.2	-1.0	-0.5	-0.3	0.1	0.0	0.1	0.0
Consumer Price Index (eop)	2.0	2.2	1.8	1.8	2.2	2.6	3.0	3.0	3.0	3.0
Consumer Price Index (avg.)	1.9	1.3	2.0	2.0	2.0	2.4	2.8	3.0	3.0	3.0
GDP deflator	0.6	-0.6	1.5	0.7	2.0	2.4	2.7	3.0	3.0	3.0
Saving-investment balance										
Foreign savings	8.6	7.6	7.5	6.8	6.6	6.4	6.2	6.0	6.1	5.9
National savings	15.8	16.8	17.0	17.3	17.6	17.8	18.0	18.2	18.1	18.4
Public	0.7	1.2	2.4	2.7	1.5	1.9	2.2	2.3	2.4	2.5
Private	15.1	15.6	14.7	14.6	16.1	15.8	15.8	15.9	15.8	15.9
Investment (incl. Inventories and stat. disc.)	24.4	24.4	24.5	24.2	24.2	24.2	24.2	24.2	24.2	24.3
Public	5.3	5.1	5.5	5.6	5.5	5.7	5.8	5.8	5.8	5.8
Private	19.2	19.3	19.0	18.6	18.6	18.5	18.4	18.5	18.5	18.5
Fiscal sector										
Total revenue and grants	26.3	27.4	27.7	27.6	27.2	27.4	27.4	27.2	27.0	26.9
Tax revenue	23.7	24.9	25.7	25.8	25.0	25.2	25.2	25.0	24.8	24.7
Total expenditure	30.9	29.6	29.7	29.3	29.7	29.4	29.3	29.0	28.7	28.5
Primary	28.2	27.2	27.7	27.0	27.7	27.3	27.2	27.0	26.6	26.4
Interest	2.7	2.5	2.1	2.2	2.0	2.1	2.1	2.0	2.1	2.0
Overall balance 2/	-4.6	-2.3	-2.0	-1.6	-2.5	-2.0	-1.9	-1.8	-1.7	-1.6
Primary balance	-1.9	0.2	0.1	0.6	-0.5	0.0	0.2	0.2	0.4	0.4
Financing	4.6	2.3	2.0	1.6	2.5	2.0	1.9	1.8	1.7	1.6
Of which: Domestic	-1.3	0.9	-0.8	-1.3	1.2	0.2	1.8	-1.0	1.9	1.3
Of which: Foreign	5.0	1.3	1.9	2.9	1.3	1.8	0.1	2.8	-0.2	0.3
General Government Debt 1/	73.7	73.3	71.9	69.9	66.3	64.5	61.6	59.7	57.1	56.8
Domestic	39.5	39.1	39.0	37.6	34.2	32.8	31.9	29.3	28.9	29.3
External	34.2	34.3	32.9	32.4	32.0	31.7	29.7	30.4	28.2	27.5
Monetary indicators										
Broad money growth	1.8	3.9	0.3	-0.2	6.4	6.5	6.8	7.1	7.1	7.1
Private credit growth	-2.8	0.4	-0.8	-0.9	5.0	5.7	6.1	6.8	6.9	7.1
Velocity (nominal GDP/ broad money)	1.2	1.2	1.2	1.3	1.3	1.3	1.3	1.3	1.3	1.3
External sector										
Trade balance (goods and services)	-17.3	-16.9	-15.1	-14.0	-13.6	-12.8	-12.2	-11.9	-11.5	-11.1
Current account balance	-8.6	-7.6	-7.5	-6.8	-6.6	-6.4	-6.2	-6.0	-6.1	-5.9
Gross international reserves (billions of Euros)	2.9	2.9	3.0	3.4	3.7	3.9	4.2	4.4	4.5	4.6
(In months of imports of goods and services)	7.0	6.5	6.2	6.6	6.8	6.8	6.8	6.7	6.3	6.0
(Relative to external debt service)	2.6	3.6	3.5	3.1	3.8	3.1	3.8	3.9	3.8	4.1
(In percent of broad money)	32.5	31.5	31.4	33.2	34.0	33.8	33.3	32.6	31.0	29.4
Memorandum items										
Output gap (percent)	-1.8	-1.4	-0.7	-0.7	-0.5	-0.2	0.0	0.0	0.0	0.0

Sources: Albanian authorities; and IMF staff estimates and projections.

1/ The stock of general government debt includes arrears from central and local government.

2/ The fiscal balance includes guarantees for new loans to the energy sector.

Table 2a. Albania: General Government Operations, 2015–24

(Percent of GDP)

	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024
							Proj.			
Total revenue and grants	26.3	27.4	27.7	27.6	27.2	27.4	27.4	27.2	27.0	26.9
Tax revenue	23.7	24.9	25.7	25.8	25.0	25.2	25.2	25.0	24.8	24.7
VAT	8.7	8.7	9.0	8.8	8.4	8.6	8.8	8.8	8.8	8.8
Profit tax	1.7	1.9	2.0	2.1	2.0	2.0	2.0	2.0	2.0	2.0
Excise tax	2.7	2.8	2.9	2.8	2.7	2.7	2.6	2.5	2.4	2.3
Customs duties	0.4	0.4	0.4	0.4	0.4	0.4	0.4	0.4	0.4	0.4
Personal income tax	2.1	2.1	2.1	2.2	2.4	2.2	2.2	2.2	2.2	2.2
Other taxes	2.3	2.4	2.5	2.4	2.1	2.0	2.0	1.9	1.8	1.8
Local government revenue 1/	0.8	1.0	1.2	1.3	1.3	1.5	1.5	1.5	1.5	1.5
Social insurance contributions	5.0	5.4	5.6	5.7	5.8	5.7	5.7	5.6	5.6	5.6
Non-tax revenue	1.8	1.5	1.3	1.4	1.3	1.3	1.3	1.3	1.3	1.3
Grants	0.8	1.0	0.7	0.5	0.8	0.8	0.9	0.9	0.9	0.9
Total expenditure	30.9	29.6	29.7	29.3	29.7	29.4	29.3	29.0	28.7	28.5
Current expenditure	24.8	25.2	24.7	24.4	24.7	24.3	24.1	23.8	23.5	23.3
Personnel cost 2/	5.1	4.6	4.7	4.5	4.7	4.5	4.4	4.2	4.2	4.0
Interest	2.7	2.5	2.1	2.2	2.0	2.1	2.1	2.0	2.1	2.0
Of which: domestic	1.9	1.7	1.4	1.4	1.4	1.4	1.4	1.3	1.3	1.4
Operations & maintenance	3.0	3.0	2.8	2.8	2.7	2.7	2.7	2.7	2.7	2.7
Energy guarantees 3/	0.3	0.0	0.0	0.0	0.4	0.1	0.1	0.1	0.0	0.0
Sector suport (e.g., KESH, OSHEE)	0.3	0.0	0.0	0.0	0.4	0.1	0.1	0.1	0.0	0.0
Nonenergy guarantees	0.0	0.1	0.0	0.0	0.1	0.0	0.0	0.0	0.0	0.0
Other	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1
Social insurance outlays	9.8	10.4	10.5	10.3	10.5	10.5	10.4	10.4	10.2	10.2
Local government expenditure 2/ 4/	2.4	2.8	3.0	3.1	2.9	3.1	3.0	3.0	3.0	3.0
Social protection transfers	1.4	1.7	1.5	1.4	1.4	1.3	1.3	1.3	1.3	1.3
Capital expenditure 4/	4.4	4.0	4.4	4.8	4.8	4.9	5.0	5.0	5.0	5.0
Domestically financed	2.6	2.6	3.0	3.2	2.5	2.3	2.3	2.5	2.7	2.8
Foreign financed	1.7	1.4	1.4	1.6	2.4	2.6	2.6	2.5	2.3	2.2
Lending minus repayment	0.5	0.5	0.6	0.0	0.0	-0.1	-0.1	0.0	0.0	0.0
Reserve and contingency funds				0.0	0.2	0.2	0.3	0.2	0.2	0.2
Overall balance 5/	-4.6	-2.3	-2.0	-1.6	-2.5	-2.0	-1.9	-1.8	-1.7	-1.6
Financing	4.6	2.3	2.0	1.6	2.5	2.0	1.9	1.8	1.7	1.6
Domestic	-1.3	0.9	-0.8	-1.3	1.2	0.2	1.8	-1.0	1.9	1.3
Privatization receipts	0.1	0.2	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Net borrowing	-0.9	0.7	0.5	1.1	0.2	0.9	1.4	-0.4	1.5	1.4
Gross borrowing	31.1	25.3	21.8	18.3	14.2	15.8	16.3	14.8	14.5	14.0
Amortization	31.9	24.6	21.3	17.2	14.0	14.9	14.9	15.2	13.0	12.5
Change in general gov. deposits	0.5	-0.3	-0.3	-2.1	1.7	-0.6	0.4	-0.6	0.3	-0.1
Other	-0.9	0.3	-0.9	-0.3	-0.7	0.0	0.0	0.0	0.0	0.0
Foreign	5.0	1.3	1.9	2.9	1.3	1.8	0.1	2.8	-0.2	0.3
Gross borrowing	9.5	2.8	3.5	6.1	3.3	5.5	2.1	4.8	1.7	1.6
Amortization	4.3	1.5	1.7	3.2	2.0	3.6	2.0	2.0	1.9	1.3
Memorandum Items:										
Primary balance	-1.9	0.2	0.1	0.6	-0.5	0.0	0.2	0.2	0.4	0.4
Structural primary balance	-0.6	0.4	0.2	0.8	-0.3	0.1	0.2	0.2	0.4	0.4
General government debt 6/	73.7	73.3	71.9	69.9	66.3	64.5	61.6	59.7	57.1	56.8
Direct general government external debt	32.4	32.7	31.6	30.6	29.4	29.4	27.7	28.7	26.7	26.3
Government guaranteed external debt	1.8	1.6	1.3	1.8	2.7	2.3	2.0	1.7	1.5	1.2
Nominal GDP (billions of leks)	1434	1472	1551	1626	1718	1830	1955	2095	2244	2403

Sources: Albanian authorities; and IMF staff estimates and projections.

1/ Includes the property tax, the simplified profit tax for small businesses, and other local taxes.

2/ There is a structural break in 2016, reflecting the transfer of central government employees to local governments, as part of fiscal decentralization.

3/ Starting in 2017, guarantees are recorded on a net basis, including amortization.

4/ There is a structural break in 2017, reflecting the transfer of the Regional Development Fund to the Ministry of Urban Development.

5/ The fiscal balance includes guarantees for new loans to the energy sector.

6/ The stock of general government debt includes arrears from central and local government.

Table 2b. Albania: General Government Operations, 2015–24

(Billions of leks)

	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024
							Proj.			
Total revenue and grants	377.5	403.1	430.4	449.4	467.6	500.6	535.6	569.7	605.5	646.0
Tax revenue	340.6	366.0	398.6	419.3	430.1	460.7	492.9	523.9	556.5	593.6
VAT	124.8	128.1	139.5	143.5	143.6	157.8	172.6	184.8	197.8	211.6
Profit tax	24.2	28.5	31.6	34.5	33.6	36.1	38.9	42.0	45.5	49.1
Excise tax	39.0	41.9	45.1	45.0	46.8	48.8	50.9	52.7	53.8	55.0
Customs duties	5.8	6.1	6.5	6.2	6.6	7.1	7.5	8.1	8.6	9.3
Personal income tax	29.7	31.4	32.1	36.5	40.9	40.9	43.7	46.8	50.1	53.6
Other taxes	33.7	35.8	38.5	38.6	36.2	37.3	38.5	39.7	41.2	42.7
Local government revenue 1/	11.7	15.0	18.4	21.9	23.0	27.9	29.8	31.9	34.2	36.7
Social insurance contributions	71.7	79.2	86.8	93.2	99.4	104.8	111.0	117.9	125.3	135.6
Non-tax revenue	25.7	22.5	20.7	22.0	22.9	24.4	26.1	27.9	29.9	32.0
Grants	11.2	14.6	11.1	8.1	14.6	15.6	16.6	17.8	19.1	20.4
Total expenditure	443.0	436.5	461.2	475.9	510.1	538.1	573.3	607.4	643.9	684.4
Current expenditure	355.9	370.6	382.6	397.1	424.3	445.5	471.8	498.9	528.1	560.6
Personnel cost 2/	72.5	67.5	72.6	73.6	80.3	82.4	85.3	89.0	93.2	96.0
Interest	38.6	36.3	31.9	36.5	34.8	38.0	41.6	41.8	46.4	48.9
Operations & maintenance	42.4	44.3	43.4	45.3	46.7	50.2	52.5	56.1	60.2	64.4
Energy guarantees 3/	4.6	0.0	0.1	0.0	6.4	0.9	1.3	1.3	0.7	0.7
Nonenergy guarantees	0.5	2.0	0.2	0.0	0.9	0.5	0.5	0.5	0.5	0.5
Other	1.7	1.7	2.3	1.9	1.5	1.5	1.5	1.6	1.7	1.8
Social insurance outlays	141.2	152.6	162.1	168.3	179.8	191.5	204.1	217.8	228.5	244.6
Local government expenditure 2/ 4/	34.1	41.7	46.5	49.6	49.9	56.0	59.4	63.6	68.2	73.0
Social protection transfers	20.2	24.5	23.4	22.0	24.0	24.5	25.6	27.2	28.8	30.5
Capital expenditure 4/	62.6	58.2	68.8	78.8	82.9	89.6	97.4	104.3	111.7	119.7
Domestically financed	37.7	37.9	46.6	52.2	42.1	41.4	45.6	52.2	60.2	67.3
Foreign financed	24.9	20.4	22.3	26.2	40.8	48.2	51.8	52.1	51.6	52.3
Lending minus repayment	7.3	7.4	9.2	0.0	0.0	-1.0	-1.0	-1.0	-1.0	-1.0
Reserve and contingency funds				0.0	2.9	4.0	5.1	5.1	5.1	5.1
Overall balance 5/	-65.5	-33.3	-30.8	-26.5	-42.6	-37.4	-37.7	-37.7	-38.4	-38.4
Financing	65.5	33.3	30.9	26.5	42.6	37.4	37.7	37.7	38.4	38.4
Domestic	-18.0	13.9	-12.1	-20.5	20.6	3.9	35.7	-21.3	42.5	32.2
Privatization receipts	0.9	2.8	0.4	0.1	0.0	0.0	0.0	0.0	0.0	0.0
Net borrowing	-12.6	10.6	7.3	18.0	4.2	15.6	27.6	-9.2	34.8	34.6
Gross borrowing	445.5	372.1	338.4	298.1	244.6	288.9	318.1	309.3	326.4	335.4
Amortization	458.2	361.5	331.1	280.1	240.4	273.4	290.5	318.5	291.7	300.7
Change in general gov. deposits	6.9	-4.3	-5.2	-33.6	28.8	-11.7	8.1	-12.1	7.8	-2.4
Other	-13.1	4.8	-14.6	-5.1	-12.5	0.0	0.0	0.0	0.0	0.0
Foreign	71.0	19.5	29.4	47.0	22.0	33.6	1.9	59.0	-4.1	6.1
Gross borrowing	135.7	41.9	55.0	98.8	55.9	100.0	41.0	101.0	38.4	38.0
Amortization	61.7	22.0	25.8	51.7	33.9	66.4	39.0	42.0	42.5	31.9
Memorandum Items:										
Primary balance	-26.9	2.9	1.1	10.0	-7.8	0.5	3.9	4.1	7.9	10.6
Structural primary balance	-8.3	6.4	2.3	13.2	-5.4	1.5	4.0	4.1	7.9	8.5
General government debt 6/	1057.3	1079.7	1114.8	1137.0	1138.4	1180.2	1204.1	1250.0	1281.9	1365.8
Direct general government external debt	465.3	481.4	490.5	496.8	504.6	538.3	541.3	600.3	600.0	632.5
Government guaranteed external debt	25.6	23.2	19.8	29.5	45.5	41.8	38.8	36.0	33.5	29.4

Sources: Albanian authorities; and IMF staff estimates and projections.

1/ Includes the property tax, the simplified profit tax for small businesses, and other local taxes.

2/ There is a structural break in 2016, reflecting the transfer of central government employees to local governments, as part of fiscal decentralization.

3/ Starting in 2017, guarantees are recorded on a net basis, including amortization.

4/ There is a structural break in 2017, reflecting the transfer of the Regional Development Fund to the Ministry of Urban Development.

5/ The fiscal balance includes guarantees for new loans to the energy sector.

6/ The stock of general government debt includes arrears from central and local government.

Table 3a. Albania: Balance of Payments, 2015–24
(Percent of GDP)

	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024
							Proj.			
Current account	-8.6	-7.6	-7.5	-6.8	-6.6	-6.4	-6.2	-6.0	-6.1	-5.9
Balance of goods and services	-17.3	-16.9	-15.1	-14.0	-13.6	-12.8	-12.2	-11.9	-11.5	-11.1
Goods, net	-22.4	-24.3	-24.4	-22.6	-22.5	-21.7	-21.3	-21.1	-20.9	-20.7
Exports	7.5	6.6	6.9	7.8	7.1	7.3	7.2	7.1	7.0	7.0
Imports	29.9	30.9	31.3	30.4	29.7	29.0	28.5	28.2	27.9	27.7
Services, net	5.1	7.4	9.4	8.7	9.0	8.9	9.1	9.2	9.3	9.6
Exports	19.8	22.3	24.7	24.1	24.4	24.1	24.1	24.2	24.2	24.3
Imports	14.6	14.9	15.3	15.4	15.4	15.2	15.1	14.9	14.8	14.7
Income balance	1.2	1.6	0.2	0.0	0.1	-0.1	-0.2	-0.2	-0.3	-0.3
Current transfers	7.5	7.7	7.3	7.2	6.8	6.5	6.2	6.0	5.7	5.5
Capital and financial account	12.2	5.5	9.8	9.9	9.0	8.5	8.1	7.9	7.2	6.6
Capital transfers	1.2	0.6	1.1	0.8	0.7	0.7	0.6	0.6	0.6	0.5
Direct investment, net	8.0	8.7	8.6	8.2	7.2	6.6	6.8	7.0	7.1	7.5
Private borrowing, net	0.7	0.8	0.9	1.0	1.1	1.2	1.2	1.3	1.4	1.4
Government medium- and long-term loans, net	4.4	0.0	1.7	2.3	0.6	2.3	0.6	3.3	0.3	0.4
Project loans	1.7	1.3	1.8	1.4	1.7	1.9	1.9	1.7	1.5	1.4
Amortization (including Eurobond bullet payment)	-4.2	-1.3	-1.5	-3.0	-1.5	-3.1	-1.4	-1.4	-1.4	-1.1
Government Guaranteed Borrowing, net	-0.2	-0.1	-0.3	0.7	0.9	-0.2	-0.2	-0.1	-0.1	-0.1
Other flows	-1.9	-4.7	-2.2	-3.1	-1.6	-2.0	-1.0	-4.1	-2.0	-3.0
Errors and omissions 1/	1.4	1.2	-1.6	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1
Net balance	5.0	-0.9	0.7	2.9	2.2	2.0	1.8	1.7	0.9	0.6
Available financing	-5.0	0.9	-0.7	-2.9	-2.2	-2.0	-1.8	-1.7	-0.9	-0.6
Change in net reserves (increase = -) 2/	-5.9	-0.4	-1.3	-2.9	-2.1	-1.8	-1.5	-1.4	-0.6	-0.6
Other financing	0.9	1.3	0.6	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Memorandum items:										
Exports of Goods and Services	27.3	29.0	31.6	31.8	31.5	31.3	31.4	31.3	31.2	31.3
Imports of Goods and Services	44.5	45.8	46.7	45.8	45.0	44.2	43.6	43.2	42.7	42.4
Total external debt stock 3/	63.2	64.1	59.8	56.4	55.1	53.6	50.5	50.2	46.9	43.8

Sources: Ministry of Finance; Bank of Albania; donors; and IMF staff estimates and projections.

1/ Includes unidentified flows of private transfers, which are projected to decline gradually over the medium term with the decline in remittances as a share of GDP.
2/ Net of valuation effect. In projections, valuation effects are assumed to be zero.
3/ Public and private external debt, including arrears. Debt stock converted into Lek at the e-o-p exchange rate. Data revised to reflect the stock of intercompany liabilities and higher private external debt as captured under BPM6.

Table 3b. Albania: Balance of Payments, 2015–24
(Millions of Euros, unless otherwise indicated)

	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024
					Proj.					
Current account	-882	-812	-867	-873	-906	-956	-988	-1,038	-1,129	-1,179
Balance of goods and services	-1,772	-1,807	-1,744	-1,780	-1,865	-1,909	-1,954	-2,037	-2,131	-2,216
Goods, net	-2,297	-2,603	-2,825	-2,884	-3,098	-3,229	-3,401	-3,621	-3,860	-4,118
Exports	771	712	796	991	979	1,082	1,156	1,225	1,302	1,399
Imports	3,068	3,315	3,621	3,875	4,077	4,311	4,557	4,847	5,162	5,517
Services, net	525	797	1,082	1,104	1,233	1,320	1,447	1,585	1,729	1,902
Exports	2,028	2,396	2,856	3,066	3,348	3,577	3,853	4,152	4,470	4,829
Imports	1,503	1,599	1,774	1,962	2,115	2,256	2,406	2,568	2,741	2,927
Income balance	122	174	29	-5	20	-14	-30	-27	-55	-53
Current transfers	768	821	848	913	939	967	996	1,026	1,058	1,090
Capital and financial account	1,254	587	1,130	1,263	1,234	1,272	1,301	1,357	1,326	1,319
Capital transfers	126	66	122	102	102	102	102	102	102	102
Direct investment, net	818	936	994	1,049	987	981	1,086	1,196	1,316	1,485
Private borrowing, net	73	87	105	129	153	177	199	225	252	283
Government medium- and long-term loans, net	453	3	193	289	78	337	95	568	52	74
Project loans	171	138	203	174	230	278	302	298	286	285
Budget support loans	9	9	161	0	59	22	17	15	15	15
Commerical borrowing	700	0	0	498	0	500	0	500	0	0
Amortization (including Eurobond bullet payment)	-426	-144	-172	-383	-211	-464	-224	-245	-250	-226
Government Guaranteed Borrowing, net	-19	-7	-30	95	128	-29	-24	-22	-19	-18
Other flows	-197	-499	-253	-401	-214	-297	-157	-712	-376	-607
Errors and omissions 1/	142	129	-186	-18	-20	-21	-23	-24	-26	-28
Net balance	514	-97	77	372	308	295	290	295	171	111
Available financing	-514	97	-77	-372	-308	-295	-290	-295	-171	-111
Change in net reserves (increase = -) 2/	-610	-48	-147	-367	-290	-261	-235	-233	-109	-111
Other financing	96	145	70	-5	-17	-34	-55	-61	-62	0
IMF (budget support)	96	145	70	0	0	0	0	0	0	0
IMF repurchase	0	0	0	-5	-17	-34	-55	-61	-62	0
Memorandum items:										
Volume of Exports of Goods and Services (percent change)	5.3	10.4	10.1	3.4	2.6	5.1	5.3	4.9	4.6	5.2
Volume of Imports of Goods and Services (percent change)	0.0	8.5	5.9	6.0	4.4	4.9	4.9	5.2	5.1	5.3
Debt service										
(Percent of exports of goods and services) 3/	14.3	4.1	3.8	9.6	5.1	11.1	6.1	6.1	6.1	4.2
(Percent of central government revenues) 3/	15.6	4.7	4.9	12.0	6.5	14.1	7.7	7.7	7.8	0.0
Terms of trade (percent change)	-16.9	-6.0	8.3	6.0	1.0	-2.5	-2.0	-1.7	-1.2	-1.1
Reserves (percent of the Fund's ARA Metric)	178	173	178	189	180	190	186	196	188	175
Gross international reserves	2,880	2,945	2,996	3,399	3,699	3,949	4,174	4,399	4,499	4,599
(months of imports of goods and services)	7.0	6.5	6.2	6.6	6.8	6.8	6.8	6.7	6.3	6.0
Nominal GDP	10,264	10,720	11,564	12,746	13,748	14,872	15,969	17,179	18,492	19,906

Sources: Ministry of Finance; Bank of Albania; donors; and IMF staff estimates and projections.

1/ Includes unidentified flows of private transfers, which are projected to decline gradually over the medium term with the decline in remittances as a share of GDP.
2/ Net of valuation effect. In projections, valuation effects are assumed to be zero.
3/ Public and publicly guaranteed debt only.

Table 4. Albania: External Financing Requirement and Sources, 2015–24
(Millions of Euros)

	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024
							Proj.			
Total financing requirement	1,815	970	1,088	1,555	1,365	1,654	1,439	1,513	1,484	1,448
Current account (incl. official transfers)	756	746	745	771	804	853	886	935	1,027	1,077
Amortization	450	176	195	417	271	540	319	344	348	261
Of which: IMF	0	0	0	5	17	34	55	61	62	0
Change in gross reserves (increase = +) 1/	610	48	147	367	290	261	235	233	109	111
Total financing sources	1,815	970	1,088	1,555	1,365	1,654	1,439	1,513	1,484	1,448
Foreign direct investment, net	818	936	994	1,049	987	981	1,086	1,196	1,316	1,485
Official medium- and long-term project loans	171	138	203	174	230	278	302	298	286	285
Multilateral	68	57	151	111	69	120	116	118	116	114
Bilateral	103	81	53	63	161	158	186	180	170	171
Official guaranteed loans	3	16	2	118	157	15	18	18	18	18
Official budget support loans	105	153	258	0	59	22	17	15	15	15
Of which: IMF	96	145	70	0	0	0	0	0	0	0
Commercial borrowing (Eurobond and PBG)	700	0	0	498	0	500	0	500	0	0
Other	18	-273	-368	-285	-67	-143	16	-514	-151	-355
Portfolio investment, net	8	-17	-16	-1	-8	-5	-6	-6	-6	-6
Commercial bank flows, net	-77	-330	-24	-197	-198	-217	-171	-198	-196	-195
Errors and omissions	142	129	-186	-18	-20	-21	-23	-24	-26	-28
Other	-56	-56	-142	-68	159	100	216	-286	77	-125
Remaining financing needs	0	0	0	0	0	0	0	0	0	0

Sources: Ministry of Finance; Bank of Albania; donors; and IMF staff estimates and projections.

1/ Net of valuation effect. In projections, valuation effects are assumed to be zero.

Table 5. Albania: Monetary Survey, 2015–24

(Billions of Leks, unless otherwise indicated; end-period)

	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024
					Proj.					
Net foreign assets	615	697	700	724	786	838	884	931	962	992
Bank of Albania	363	390	391	412	450	477	503	528	538	547
Commercial banks	251	307	310	312	336	361	381	403	424	446
Net domestic assets	602	567	567	540	558	594	647	709	794	888
Ceiling on general government guarantees										
Claims on central government, net	332	357	351	341	347	370	412	398	450	502
Commercial banks	305	322	333	353	336	376	414	412	457	511
Bank of Albania	27	34	18	-12	11	-5	-2	-14	-6	-9
Claims on public enterprises	28	27	35	20	28	24	26	25	25	25
Claims on the private sector	509	511	507	502	527	557	591	631	675	723
In leks	212	231	239	247	259	274	291	310	332	356
In foreign currency	296	280	268	255	268	283	301	321	343	368
Other items, net	-267	-328	-326	-323	-343	-357	-382	-346	-356	-362
Broad money	1,216	1,263	1,267	1,264	1,344	1,432	1,530	1,640	1,756	1,881
Currency outside banks	231	249	265	275	293	312	333	357	382	410
Deposits	986	1,014	1,002	989	1,052	1,120	1,197	1,283	1,374	1,471
Domestic currency	493	488	474	456	485	517	567	635	700	749
Foreign currency	493	527	528	533	566	604	630	647	674	722
Memorandum items:										
Broad money growth (% change)	1.8	3.9	0.3	-0.2	6.4	6.5	6.8	7.1	7.1	7.1
Reserve money growth (% change)	15.3	7.9	2.6	-0.4	1.1	5.3	6.4	6.4	6.6	6.5
Private sector credit growth (% change)	-2.8	0.4	-0.8	-0.9	5.0	5.7	6.1	6.8	6.9	7.1
Broad money (as percent of GDP)	84.8	85.8	81.7	77.7	78.3	78.3	78.3	78.3	78.3	78.3
Private sector credit (as percent of GDP)	35.5	34.7	32.7	30.9	30.7	30.4	30.2	30.1	30.1	30.1
Velocity (nominal GDP/broad money)	1.2	1.2	1.2	1.3	1.3	1.3	1.3	1.3	1.3	1.3
Money multiplier (absolute values)	3.2	3.0	3.0	3.0	3.1	3.2	3.2	3.2	3.2	3.2
Currency (as share of broad money)	19.0	19.7	20.9	21.8	21.8	21.8	21.8	21.8	21.8	21.8
Foreign currency deposits/total deposits	50.0	51.9	52.7	53.9	53.9	53.9	52.7	50.5	49.1	49.1
Gross reserves (millions of euros)	2,880	2,945	2,996	3,399	3,699	3,949	4,174	4,399	4,499	4,599

Sources: Bank of Albania; and IMF staff estimates.

Table 6. Albania: Summary of Accounts of the Central Bank, 2015–24

(Billions of Leks, unless otherwise indicated; end-period)

	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024
							Proj.			
Net foreign assets	363	390	391	412	450	477	503	528	538	547
Assets	405	419	418	436	474	501	527	552	561	570
Liabilities	42	29	27	24	24	24	24	24	24	23
Net domestic assets	21	25	35	11	-22	-27	-23	-18	6	33
Ceiling on general government guarantees										
Domestic credit	41	66	60	22	-4	-8	-5	1	25	51
Assets	53	53	53	56	51	46	41	41	41	41
Net claims on central government	27	34	18	-12	11	-5	-2	-14	-6	-9
Liabilities	26	19	34	68	39	51	43	55	47	49
Other credit	15	32	42	34	-15	-3	-3	15	31	60
Private sector	2	2	2	2	2	2	2	2	2	2
Commercial banks	13	30	40	32	-17	-5	-5	13	29	58
Other items, net (assets = +)	-21	-41	-25	-11	-18	-18	-18	-18	-18	-18
Reserve money	384	414	425	423	428	451	480	511	544	579
Currency in circulation	231	249	265	275	293	312	333	357	382	410
Bank reserves	152	162	156	148	135	139	147	153	162	170
Other nonbank deposits	2	3	4	0	0	0	0	0	0	0

Sources: Bank of Albania; and IMF staff estimates.

Table 7. Albania: IMF Core Indicators of Financial Soundness, 2012–19

		Dec-12	Dec-13	Dec-14	Dec-15	Dec-16	Dec-17	Mar-18	Jun-18	Sep-18	Dec-18	Mar-19
I	Capital-based											
(i)	Regulatory capital as a percent of risk-weighted assets	16.2	18.0	16.8	15.7	15.7	16.6	16.9	17.9	18.2	18.3	17.9
(ii)	Regulatory Tier 1 capital as a percent of risk-weighted assets	14.6	14.9	13.8	13.5	13.8	15.1	15.6	16.6	16.9	17.0	16.6
(iii)	Capital as a percent of total assets											
	Regulatory Tier 1 capital as a percent of total assets	7.9	7.7	7.4	8.3	8.7	9.0	9.2	9.4	9.2	9.2	8.9
	Regulatory capital as a percent of total assets	8.8	9.3	9.0	9.7	10.0	9.9	10.1	10.1	9.9	9.8	9.6
	Shareholders' equity as a percent of total assets	8.6	8.4	8.6	9.5	9.7	10.2	10.2	10.5	10.2	10.1	10.2
(iv)	Nonperforming loans net of provisions as a percent of capital											
	As a percent of regulatory Tier 1 capital	61.8	48.5	46.7	28.4	26.3	17.3	18.7	19.4	19.3	16.6	18.6
	As a percent of regulatory capital	55.6	40.2	38.3	24.3	23.1	15.7	17.2	18.0	18.0	15.5	17.2
	As a percent of shareholders' equity	56.9	44.8	40.2	24.8	23.6	15.3	16.9	17.3	17.5	15.0	16.3
(v)	Return on equity (ROE) (annual basis)	3.8	6.4	10.5	13.2	7.2	15.7	13.2	15.0	12.9	13.0	13.6
(vi)	Net open position in foreign exchange as a percent of capital											
	As a percent of regulatory Tier 1 capital	4.1	4.9	10.4	9.0	8.0	7.3	6.9	8.2	6.0	8.4	5.9
	As a percent of regulatory capital	3.7	4.1	8.5	7.7	7.0	6.7	6.4	7.6	5.6	7.8	5.5
	As a percent of shareholders' equity	3.8	4.5	8.9	7.8	7.2	6.5	6.3	7.3	5.4	7.5	5.2
II	Asset-based											
(vii)	Liquid assets as a percent of total assets (Liquid-asset ratio)	29.4	27.6	31.9	32.3	31.3	30.2	31.9	32.2	33.5	34.2	34.9
(viii)	Liquid assets as a percent of short-term liabilities	34.9	34.7	40.4	41.4	40.6	40.8	43.1	43.2	45.9	46.2	47.0
(ix)	Return on assets (ROA) (net income to average total assets, annual)	0.3	0.5	0.9	1.2	0.7	1.5	1.3	1.5	1.3	1.3	1.4
(x)	Nonperforming loans (gross) as a percent of total loans	22.5	23.5	22.8	18.2	18.3	13.2	13.4	13.3	12.9	11.1	11.4
III	Income and expense-based											
(xii)	Interest margin to gross income	101.1	87.9	102.2	98.0	81.6	95.6	110.7	102.8	101.3	100.8	76.7
(xiii)	Noninterest expenses to gross income	65.9	58.3	61.8	57.0	50.4	71.9	81.1	77.3	77.1	77.6	55.8
IV	Memorandum items											
	Other (noncore) indicators:											
	Customer deposits as a percent of total (non-interbank) loans	171.6	180.8	180.2	187.8	192.8	194.0	193.2	196.8	200.2	203.2	204.7
	Foreign currency-denominated loans to total loans	64.5	63.0	62.4	60.8	58.6	56.4	55.9	56.5	56.5	56.1	54.1
	Foreign currency-denominated liabilities as a percent of total liabilities	52.6	52.8	52.4	53.5	54.6	60.4	60.3	59.3	59.4	59.1	57.6
	Other indicators:											
	Risk weighted assets as a percent of total assets	54.2	52.1	53.6	62.0	63.4	59.7	59.4	56.4	54.4	53.9	53.7
	Total loans as a percent of total assets	48.6	45.9	46.0	44.5	42.7	41.6	41.7	40.8	39.9	40.0	39.5
	Total loans as a percent of shareholders' equity	567.4	548.8	536.3	466.8	438.6	408.9	407.2	388.7	393.2	393.8	387.8

Sources: Bank of Albania; and IMF staff estimates.

Table 8. Albania: Indicators of Capacity to Repay the Fund, 2016–24 1/ 2/

(Under Obligated Repurchase Schedules)

(in Millions of SDRs)

	2016	2017	2018	2019	2020	2021	2022	2023	2024
Fund repurchases and charges									
In millions of SDRs	5.4	6.8	5.7	17.8	34.0	49.5	53.3	52.2	49.2
In millions of euro	6.9	8.1	7.0	22.0	42.0	61.5	66.6	65.8	62.5
In percent of gross international reserves	0.2	0.3	0.2	0.6	1.1	1.5	1.5	1.5	1.4
In percent of exports of goods and services	0.2	0.2	0.2	0.5	0.9	1.2	1.2	1.1	1.0
In percent of GDP	0.1	0.1	0.1	0.2	0.3	0.4	0.4	0.4	0.3
In percent of external public debt	0.2	0.2	0.2	0.5	0.9	1.3	1.3	1.3	1.2
In percent of quota	3.9	4.9	4.1	12.8	24.4	35.6	38.3	37.5	35.1
Fund credit outstanding (end of period)									
In millions of SDRs	241.5	296.8	291.7	277.3	249.6	205.1	155.9	106.7	61.4
In millions of euro	308.6	354.8	355.0	342.4	308.7	254.7	194.9	134.3	77.9
In percent of gross international reserves	10.5	11.8	10.4	9.3	7.8	6.1	4.4	3.0	1.7
In percent of exports of goods and services	9.9	9.7	8.8	7.9	6.6	5.1	3.6	2.3	1.3
In percent of GDP	2.9	3.1	2.8	2.5	2.1	1.6	1.1	0.7	0.4
In percent of external public debt	8.3	9.2	8.4	7.7	6.5	5.4	3.7	2.6	1.5
In percent of quota	173.4	213.0	209.4	199.1	179.2	147.3	111.9	76.6	43.7
Memorandum items:									
Gross international reserves	2305	2506	2793	2996	3193	3362	3519	3547	3566
Exports of goods and services	2432	3054	3334	3504	3766	4034	4302	4584	4903
GDP	8389	9672	10474	11135	12023	12862	13742	14685	15672
External public debt	2925	3215	3478	3599	3816	3817	4180	4127	4050
Quota	139.3	139.3	139.3	139.3	139.3	139.3	139.3	139.3	140.3

Source: Fund staff estimates.

1/ Projections are based on current interest rates for the PRGF and the EFF.

2/ End-year value.

Annex I. Risk Assessment Matrix[1]

Source of Risk	Relative Likelihood	Impact if Realized	Policy Advice
International Macroeconomic Environment			
Weaker than expected growth in main trading partners	High	High Growing global uncertainties and further weakening of growth across Europe (particularly in the main export destinations and sources of remittances) might spill over to Albania resulting in lower demand for exports and a decline in remittances.	Continue to diversify export markets, accelerate fiscal consolidation to build buffers, resolve structural bottlenecks to credit growth. If a significant external shock were to materialize, allow automatic stabilizers to operate, while strengthening the debt anchor.
International Financial Conditions			
Sharp tightening of financial conditions in the region	Medium	Medium An increase in the risk premium could raise interest rates for Albania and reduce international investor appetite for Albanian securities. Ample external reserves mitigate this risk.	Persist with fiscal consolidation and further lengthen the maturity of public debt. Optimize the foreign debt portfolio based on risk-return tradeoff analysis.
Domestic risks			
Financial disintermediation	Medium	Medium An abrupt and disorderly exit of a large foreign bank could stress the domestic banking system and create pressures on the market for domestic public debt. However, the new bank resolution adopted by the BoA should mitigate this risk.	Continue sharing information with parent banks and their regulators, strengthen contingency plans, and closely monitor capital and liquidity positions. Conduct strict fit and proper assessment of new entrants, especially those with limited banking experience. Continue to align bank regulations with European standards.
Poorly designed PPPs & increased contingent liabilities	High	Medium Engaging in poorly designed PPP contracts for infrastructure investment could impede the efficiency of public investment, and create large contingent liabilities, the realization of which could undermine fiscal and debt sustainability.	Strengthen governance and transparency in PPP implementation. Upgrade the capacity of the Ministry of Finance to undertake financial analysis of new PPP contracts.
Adverse weather conditions	Medium	Medium Drought conditions could affect electricity generation. Power shortages could damage growth. Electricity imports could pose quasi-fiscal risks for the budget.	Reinvigorate the implementation of the electricity sector reform. Finalize financial restructuring plans to restore the financial viability of public electricity companies. Prepare a backup power supply plan.
Rollover of public debt	Low	Medium Concerns about debt sustainability may make banks reluctant to roll over government debt, a significant part of which is short-term.	Diversify the debt holders base. Improve market communication and coordination with the central bank. Continue fiscal adjustment and debt reduction.
Domestic political instability	Low	High Volatile domestic politics and social tensions could hinder the implementation of the structural reforms and fiscal consolidation agenda. Reforms, including those to strengthen the rule of law are key for medium-term growth and prospects for EU accession talks.	Ensure that reforms are grounded in careful policy analysis and a consultative preparation process.

[1] The RAM shows events that could materially alter the baseline scenario (the scenario most likely to materialize in staff's view). The relative likelihood of risks listed is staff's subjective assessment of the risks surrounding the baseline.

Annex II. Recent Developments of Financial Regulations in Albania

Both the central bank (BoA) and the non-bank supervisor, AFSA, have been upgrading Albania's regulatory landscape

Bank Capital Standards

- Implementation of Pillar 2 of Basel capital framework [upcoming, 2019 -2020].
- Basel III Leverage Ratio [Planned, 2020]

Note:

- Minimum capital adequacy ratio in Albania is set at 12% (vs. 8% in Basel standards), and can be higher for specific banks with known issues
- Since 2014, FX unhedged loans are subject to an additional risk weight of 50%, subject to total risk weight not exceeding 150%

Bank Liquidity Standards

- Basel III Liquidity Coverage Ratio [2019]
- Liquid Assets to Short-Term Liabilities Ratio (LAR), differentiated by currency: LAR is set at a minimum level of 15% for local and 20% for foreign currency, while it is at 20% for the aggregate position, in line with de-euroization package [2018]
- Basel III Net Stable Funding Ratio [Planned, 2020]
- Internal Liquidity Adequacy Assessment Process [Planned, 2020]

Other Bank Regulations and Guidelines

- Alignment of Albanian Large Exposures Regulations with the Basel Supervisory Framework for Measuring and Controlling Large Exposures [Upcoming, 2019-2020]
- Enhancements to regulation on licensing and transfer of significant ownership [Upcoming 2019-2020]
- Regulation/Guidelines on market risk management [Upcoming, 2019]
- Guidelines for banks on stress testing [Upcoming, 2019]
- Review of regulation on related-party lending [Planned, 2020]

Bank Supervision

- Increase in the frequency of on-site and off-site supervision for banks with recent change in shareholder structure; tighter reporting requirements [2019]
- Enhancements to off-site monitoring of banks' delinquent loans and recovery rates [Planned, 2020]

Macro-Prudential Frameworks

- Regulation on enhanced monitoring of systemic risks through a Systemic Risk Heat Map [2019]
- Countercyclical capital buffer framework [2019]
- Capital conservation buffer framework [2019]

- Framework for identification of domestic systemically important banks (D-SIBs) and higher loss absorbency requirement for them [2019]
- The required reserve rate for foreign currency deposits is 12.5%. For banks where foreign currency deposits account for more than 50% of total deposits, the required reserve ratio in foreign currency is 20%. For local currency deposits, the required reserve rate is 7.5% for maturity up to one year and 5% for maturity longer than one year. [2018]

Consumer Protection

- Right for the consumer to ask for currency conversion of his/her FX loan [2018]
- Banks must notify the consumer when exchange rate variation causes an increase of loan repayments by more than 20% [2018]

Regulatory Framework for Capital Market and Investment Funds

- New investment funds law, converging with EU regulations and clarifying the licensing, supervision, investors and consumer protection [upcoming 2019]
- New capital market law, aligning with EU regulations [upcoming, 2019]
- New liquidity regulation for investment funds: funds should keep a liquidity buffer of 10% of total assets or the 3-month cumulative redemption, whatever is higher. Half of the liquidity should be within assets with maturity less than a week and other half less than a month [2018]
- New regulation on related-party transactions: every kind of transactions should be done at arms' length principle [2018]
- Crisis management framework for investment funds [2018]

Annex III. Debt Sustainability Analysis

Public debt in Albania is expected to gradually decline over the medium term but remain high, posing significant risks. Under the baseline scenario, the public debt-to-GDP ratio is projected to reach 56.8 percent by 2024, from a 2017 level of 71.9 percent. Gross financing needs are expected to remain high. Rollover needs are gradually declining but remain sizable. The debt-to-GDP ratio is sensitive to real GDP growth, fiscal performance and borrowing costs.

A. Background

1. Albania's public debt has been on a declining path since 2015 but remains high. After a rapid increase of public debt between 2010–2013, the debt trajectory reversed in 2016. Supported by a sizable fiscal adjustment in last three years, and the sharp appreciation in 2018, total public debt declined from its peak of 73.7 percent of GDP in 2015, to 69.9 percent in 2018. Despite the decline, debt however remains high.

2. Debt Profile[1]. Domestic debt represents 53 percent of total public debt, of which 98 percent is denominated in domestic currency. The maturity of public debt has been gradually improving, with the authorities' effort to shift from short-term domestic financing to long-term external financing. Moreover, the average weighted maturity of domestic public debt has increased from less than 1 year in 2011 to 2.2 years as of December 2018.

B. Public DSA Results

Baseline Scenario

3. Macroeconomic assumptions. After the estimated increase in 2018, real growth is projected to moderate to 3.5 percent in 2019, and stabilize at 4 percent over the medium term, reflecting an expansion of investments, and a further strengthening of the export-oriented sectors, including industry and tourism. Inflation is projected to edge up gradually and reach the central bank target of 3 percent by 2021. Absent of new tax policy measures, fiscal consolidation is expected to widen with the overall deficit increasing to 2.5 percent of GDP in 2019, and gradually declining to 1.6 percent of GDP by 2024. The primary surplus will average 0.1 percent of GDP.

4. Debt level under the baseline. Under the baseline scenario, gross debt is projected to gradually decline over the medium-term, reaching 56.8 percent of GDP in 2024. Gross financing needs over the same period are projected to remain somewhat above the 15 percent threshold and average around 16.4 percent of GDP. The authorities have shown an increasing appetite for external commercial borrowing, which is expected to increase as a share of total borrowing.

5. Alternative scenario. Under the constant-primary-balance scenario (assuming the primary balance remains at the level of 2019), the debt ratio would reach 60.5 percent by 2024. The scenario

[1] Public debt refers to the general government and includes all public guarantees for energy and non-energy sector debt and stock of central and local government arrears. It does not include PPPs.

based on historical performance (assuming real GDP growth, the primary balance and real interest rates at the historical average of the past ten years) projects debt at 69.6 percent of GDP. This scenario highlights the risks to the baseline from slow growth, a sharp increase in interest rate, and a deterioration of the fiscal accounts.

6. Heat map and debt profile vulnerabilities. Risks related to the level of debt improved relative to previous DSA (January 2019), as the debt-to-GDP ratio remains around the 70 percent benchmark both under the baseline and shock scenarios. Gross financing needs breach the 15 percent threshold associated with past crises through all of the projection period. The debt profile shows moderate risks as the share of short-term debt declined (green in the heatmap), while the market perception reflected in the average sovereign spread in the last three months is just above the threshold. Despite the improvement in the maturity profile, ***rollover risks*** remain high, as 35 percent of total debt is short-term. Notwithstanding a notable decline from 2017, public gross financing needs are projected to remain above the early warning levels associated with past debt crises. ***Interest rate risk*** is expected to increase with the lengthening of maturity, but the impact on valuations is limited due to underdeveloped secondary market and banks' preference to hold government securities till maturity. ***Exchange rate risks*** will rise with the expansion of foreign currency debt (as a share of total debt), but Albania's comfortable level of international reserves should limit the negative impact (see paragraph 12).

7. Realism of projections. The baseline scenario remains realistic. Medium-term growth projections take into account Albania's relatively low per capita income by regional standards and its potential for convergence, continuous inflows of FDI throughout the period, and the expected launch of EU accession negotiations. The median forecast errors for real GDP growth (actual minus projection) in 2009–2017 are broadly within the inter-quartile range of the forecast errors of other countries, and do not suffer from large systemic bias. Forecast errors for the primary balance however suggest that staff projections have been too pessimistic, with a percentile rank of 85 percent. Inflation forecasts, on the other hand, have been too optimistic.

Stress Test

8. Stress test results. The debt ratio remains above 58.8 percent of GDP under all scenarios, and it is most sensitive to the interest rate and real GDP growth shocks. Under those stress scenarios debt reaches 60.7 and 59.5 percent of GDP in 2024, respectively. Sensitivity to exchange rate shocks is also notable, as under this scenario public debt reaches 58 percent of GDP. A combined shock incorporates the largest effect of individual shocks on all relevant variables (real GDP growth, inflation, primary balance, exchange rate and interest rate). Under this scenario the debt-to-GDP ratio will increase to 69.8 percent of GDP.

9. Stochastic simulations. The fan charts illustrate the possible evolution of the debt over the medium term and are based on both symmetric and asymmetric distributions of risks. Under an asymmetric distribution of risks, there is a high level of certainty that the debt stock will be in the range of 51 to 69.8 percent of GDP. However, if restrictions are imposed on the primary balance, debt could be above 61 percent of GDP by 2024 relative to the baseline scenario of 56.8 percent of GDP with a probability of 25 percent.

C. External Debt Sustainability

10. The external debt-to-GDP ratio remains high though its medium-term trajectory has improved modestly relative to the last DSA (January 2019). This is largely due to a more appreciated path for the exchange rate over the medium-term. Most external debt continues to be held by multilateral creditors and bilateral development agencies, though the share of commercial debt is expected to increase over the medium-term. Most foreign public debt is denominated in euros (inter-government loans and Eurobonds), followed by SDRs (IMF loans).

11. The external debt ratio peaked in 2017 and is expected to decline gradually over the medium-term as growth picks up and multilateral borrowing declines. External debt peaked at around 63 percent of GDP in 2017 but declined to 56.2 percent of GDP in 2018 due to exchange rate appreciation and the refinancing of a Eurobond (see below). Over the medium-term, the debt ratio is expected to decline gradually as growth accelerates and fiscal consolidation leads to reduced borrowing, reaching about 45 percent of GDP by 2024. Between 2018 and 2024, external private borrowing is expected to fall from about 25 to 18 percent of GDP. Although the accumulation of FDI-related debt liabilities will slow as investment in large energy projects (such as the Trans Adriatic Pipeline) tapers off, such liabilities will likely remain the largest component of the private external debt stock. The authorities issued a seven-year, €500 Eurobond at favorable rates in October 2018, and used €200 million to retire a portion of the €450 2015 Eurobond. The authorities are planning to issue a €500 Eurobond in 2020 to rollover the remaining maturity of the 2015 bond, and another €500 Eurobond in 2022. In line with the succession of new Eurobond issuances, commercial debt as a percentage of total PPG debt is expected to increase from 25 percent in 2019 to 36 percent in 2022, before declining thereafter as outstanding commercial debt is repaid.

12. Stress test results. Under a 30 percent exchange rate depreciation shock, external debt would peak at 82 percent of GDP in 2020 before declining to 67 percent by 2024. Depreciation shocks are likely to have added significance for debt dynamics in view of increased external commercial borrowing, although Albania's ample reserve buffers should help mitigate disorderly foreign exchange market conditions. Following a shock to the current account of half a standard deviation (around 2 percent of GDP), external debt would peak at 54 percent of GDP in 2020 and gradually decline to 52 percent by 2023.

Albania: Public Sector Debt Sustainability Analysis (DSA) - Baseline Scenario

(In percent of GDP unless otherwise indicated)

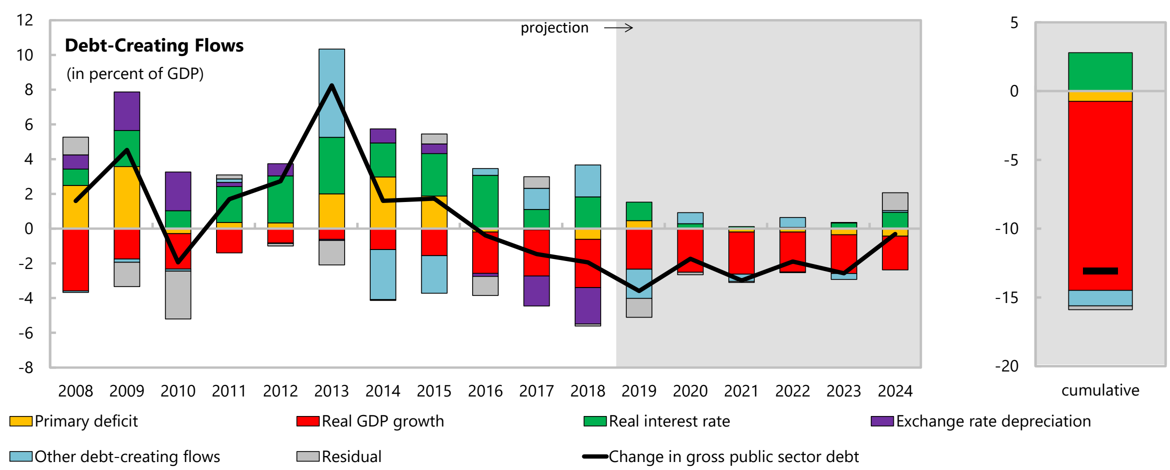
Debt, Economic and Market Indicators [1/]

	Actual			Projections					
	2008-2016 [2/]	2017	2018	2019	2020	2021	2022	2023	2024
Nominal gross public debt	64.8	71.9	69.9	66.3	64.6	61.6	59.7	57.1	56.8
Of which: guarantees	3.8	3.2	2.7	2.8	2.6	2.5	2.3	2.2	2.0
Public gross financing needs	36.8	25.0	22.0	19.2	16.5	15.5	16.1	15.1	15.8
Real GDP growth (in percent)	3.0	3.8	4.1	3.5	4.0	4.0	4.0	4.0	4.0
Inflation (GDP deflator, in percent)	1.8	1.5	0.7	2.0	2.4	2.8	3.0	3.0	3.0
Nominal GDP growth (in percent)	4.8	5.4	4.8	5.6	6.5	6.9	7.1	7.1	7.1
Effective interest rate (in percent) [4/]	5.4	3.1	3.4	3.5	2.8	2.9	3.0	3.5	3.9

As of Sep 24, 2018		
Sovereign Spreads		
Spread (bp) 3/		195
5Y CDS (bp)		n.a.
Ratings	Foreign	Local
Moody's	B1	B1
S&Ps [11/]	B+	B+
Fitch	n.a.	n.a.

Contribution to Changes in Public Debt

	Actual			Projections							
	2008-2016	2017	2018	2019	2020	2021	2022	2023	2024	cumulative	debt-stabilizing primary balance [10/]
Change in gross public sector debt	2.2	-1.5	-1.9	-3.6	-1.7	-3.0	-1.9	-2.6	-0.3	-13.1	
Identified debt-creating flows	2.8	-2.1	-1.8	-2.5	-1.6	-2.9	-1.9	-2.6	-1.3	-12.8	
Primary deficit [5/]	1.5	-0.1	-0.6	0.5	0.0	-0.2	-0.2	-0.4	-0.4	-0.7	-0.9
Primary revenue and grants [5/]	25.9	27.7	27.6	27.2	27.4	27.4	27.2	27.0	26.9	163.1	
Primary expenditure [5/]	27.3	27.7	27.0	27.7	27.3	27.2	27.0	26.6	26.5	162.3	
Automatic debt dynamics [6/]	1.3	-3.3	-3.0	-1.3	-2.2	-2.3	-2.2	-1.9	-1.0	-10.9	
Interest rate/growth differential [7/]	0.5	-1.6	-1.0	-1.3	-2.2	-2.3	-2.2	-1.9	-1.0	-10.9	
Of which: real interest rate	2.2	1.1	1.8	1.1	0.3	0.1	0.1	0.3	0.9	2.8	
Of which: real GDP growth	-1.7	-2.7	-2.8	-2.3	-2.5	-2.4	-2.3	-2.2	-1.9	-13.7	
Exchange rate depreciation [8/]	0.8	-1.7	-2.1	…	…	…	…	…	…	…	
Other identified debt-creating flows	0.0	1.2	1.8	-1.7	0.6	-0.4	0.6	-0.3	0.1	-1.1	
Accumulation of general govt. deposits	0.0	0.3	2.1	-1.7	0.6	-0.4	0.6	-0.3	0.1	-1.1	
Contingent liabilities	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Creation/clearance of end-2013 stock of arrears	0.1	0.9	-0.2	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Residual [9/]	-0.6	0.7	-0.1	-1.1	-0.1	-0.1	0.0	0.0	1.0	-0.3	



Source: IMF staff.

1/ Public sector is defined as general government and includes public guarantees, defined as domestic and external guarantees for the energy and nonenergy sector.

2/ Based on available data.

3/ Bond Spread over German Bonds, based on the 5-year eurobond issued in November 2015.

4/ Defined as interest payments divided by debt stock (excluding guarantees) at the end of previous year.

5/ The DSA includes unallocated measures in revenues and expenditures.

6/ Derived as $[(r - \pi(1+g) - g + ae(1+r)]/(1+g+\pi+g\pi))$ times previous period debt ratio, with r = interest rate; π = growth rate of GDP deflator; g = real GDP growth rate; a = share of foreign-currency denominated debt; and e = nominal exchange rate depreciation (measured by NEER).

7/ The real interest rate contribution is derived from the numerator in footnote 6 as $r - \pi(1+g)$ and the real growth contribution as -g.

8/ The exchange rate contribution is derived from the numerator in footnote 6 as $ae(1+r)$.

9/ Includes guarantees, asset changes, net privatization proceeds, and interest revenues (if any). It includes also exchange rate changes during the projection period. The large residual in 2019 is due to a combination of a large accumulation of deposits in BoA and large repayment of arrears

10/ Assumes that key variables (real GDP growth, real interest rate, and other identified debt-creating flows) remain at the level of the last projection year.

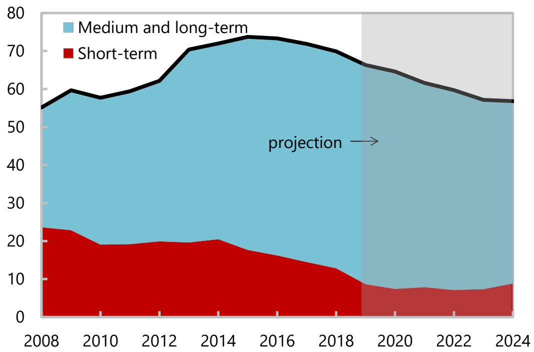
11/ Credit rating for short-term foreign and local currency sovereign debt is maintained at "B."

Albania: Public DSA – Composition of Public Debt and Alternative Scenarios

Composition of Public Debt

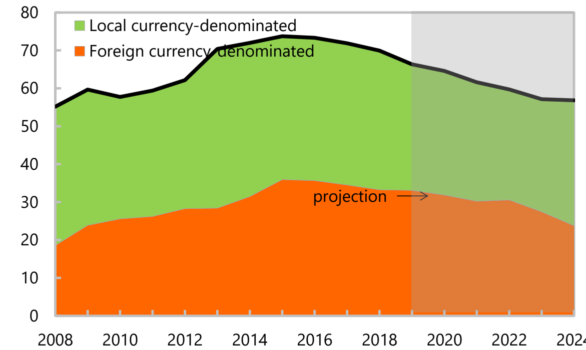
By Maturity

(in percent of GDP)



By Currency

(in percent of GDP)

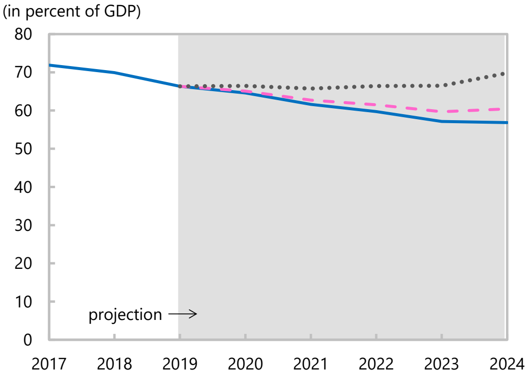


Alternative Scenarios

Baseline Historical Constant Primary Balance

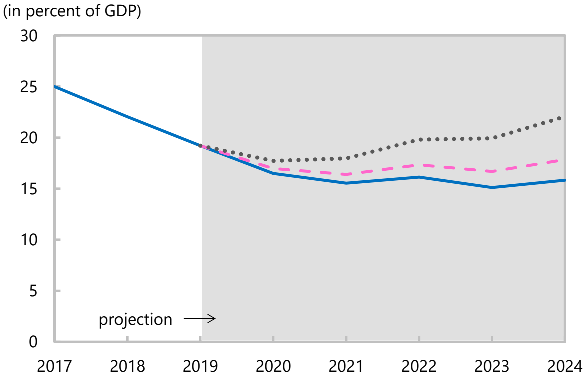
Gross Nominal Public Debt

(in percent of GDP)



Public Gross Financing Needs

(in percent of GDP)



Underlying Assumptions

(in percent)

Baseline Scenario	2019	2020	2021	2022	2023	2024
Real GDP growth	3.5	4.0	4.0	4.0	4.0	4.0
Inflation	2.0	2.4	2.8	3.0	3.0	3.0
Primary Balance	-0.5	0.0	0.2	0.2	0.4	0.4
Effective interest rate	3.5	2.8	2.9	3.0	3.5	3.9
Constant Primary Balance Scenario						
Real GDP growth	3.5	4.0	4.0	4.0	4.0	4.0
Inflation	2.0	2.4	2.8	3.0	3.0	3.0
Primary Balance	-0.5	-0.5	-0.5	-0.5	-0.5	-0.5
Effective interest rate	3.5	2.8	2.9	3.0	3.5	3.9

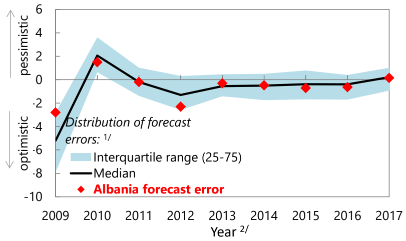
Historical Scenario	2019	2020	2021	2022	2023	2024
Real GDP growth	3.5	2.7	2.7	2.7	2.7	2.7
Inflation	2.0	2.4	2.8	3.0	3.0	3.0
Primary Balance	-0.5	-1.0	-1.0	-1.0	-1.0	-1.0
Effective interest rate	3.5	2.8	3.5	4.0	4.7	5.3

Source: IMF staff.

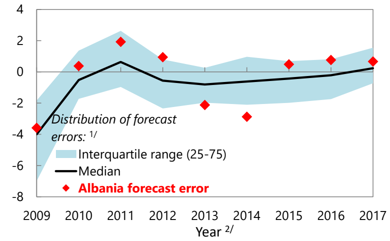
Albania: Public DSA – Realism of Baseline Assumptions

Forecast Track Record, versus all countries

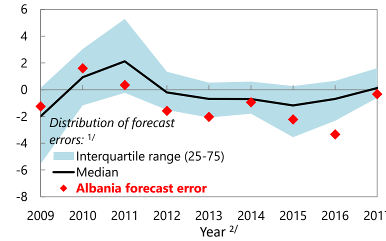
Real GDP Growth
(in percent, actual-projection)
Albania median forecast error, 2009-2017: **-0.48**
Has a percentile rank of: **44%**



Primary Balance
(in percent of GDP, actual-projection)
Albania median forecast error, 2009-2017: **0.48**
Has a percentile rank of: **85%**

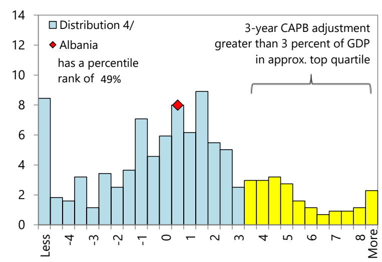


Inflation (Deflator)
(in percent, actual-projection)
Albania median forecast error, 2009-2017: **-1.25**
Has a percentile rank of: **20%**

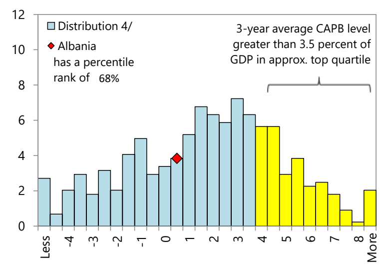


Assessing the Realism of Projected Fiscal Adjustment

3-Year Adjustment in Cyclically-Adjusted Primary Balance (CAPB) 5/
(Percent of GDP)

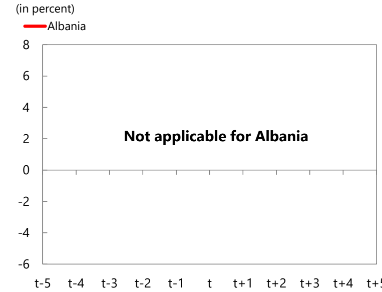


3-Year Average Level of Cyclically-Adjusted Primary Balance (CAPB)
(Percent of GDP)



Boom-Bust Analysis 3/

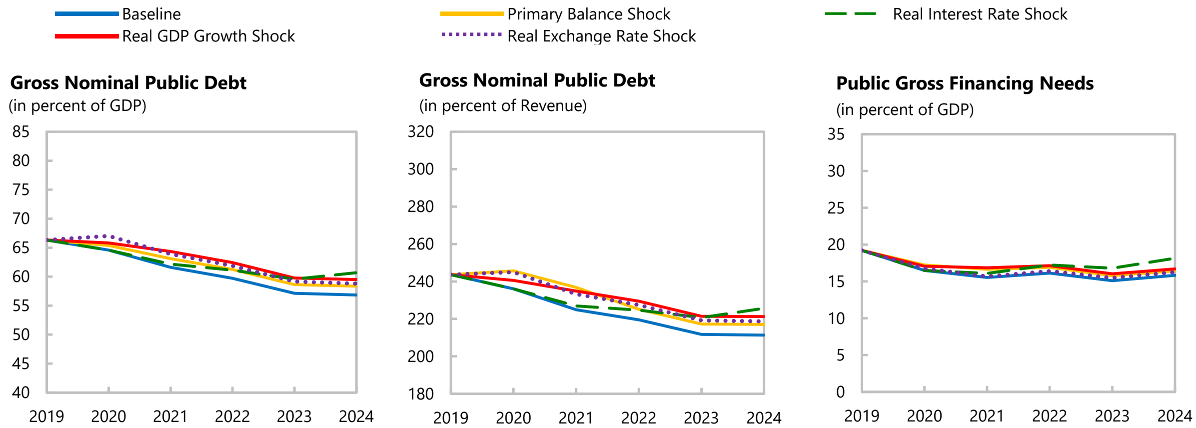
Real GDP growth
(in percent)



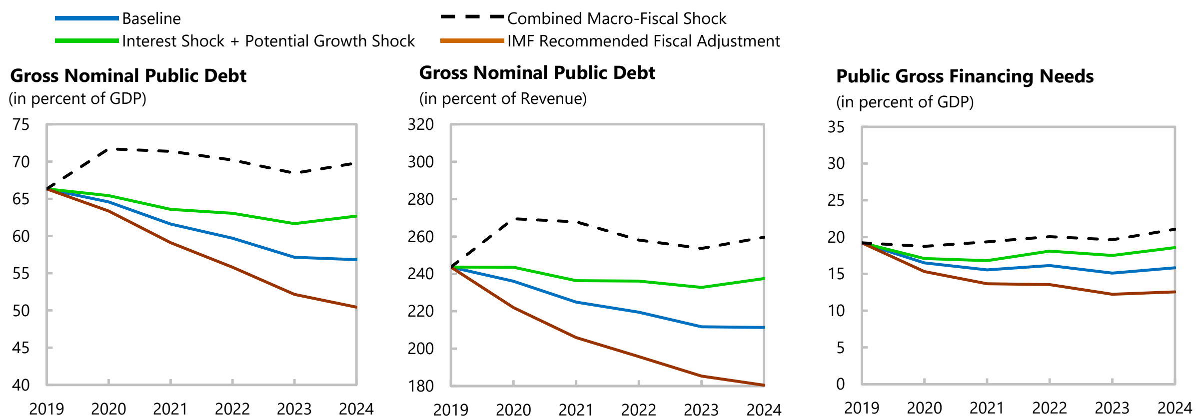
Source : IMF Staff.
1/ Plotted distribution includes all countries, percentile rank refers to all countries.
2/ Projections made in the spring WEO vintage of the preceding year.
3/ Not applicable for Albania, as it meets neither the positive output gap criterion nor the private credit growth criterion.
4/ Data cover annual obervations from 1990 to 2011 for advanced and emerging economies with debt greater than 60 percent of GDP. Percent of sample on vertical axis.
5/ The large 3-year improvement in Albania's CAPB is due to substantial arrear clearance in 2015-2017.

Albania: Public DSA – Stress Tests

Macro-Fiscal Stress Tests



Additional Stress Tests



Underlying Assumptions
(in percent)

Primary Balance Shock	2019	2020	2021	2022	2023	2024
Real GDP growth	3.5	4.0	4.0	4.0	4.0	4.0
Inflation	2.0	2.4	2.8	3.0	3.0	3.0
Primary balance	-0.5	-0.7	-0.6	0.2	0.4	0.4
Effective interest rate	3.5	2.8	3.0	3.1	3.5	3.9
Real Interest Rate Shock						
Real GDP growth	3.5	4.0	4.0	4.0	4.0	4.0
Inflation	2.0	2.4	2.8	3.0	3.0	3.0
Primary balance	-0.5	0.0	0.2	0.2	0.4	0.4
Effective interest rate	3.5	2.8	3.9	4.5	5.4	6.1
Combined Shock						
Real GDP growth	3.5	2.9	2.9	4.0	4.0	4.0
Inflation	2.0	2.1	2.5	3.0	3.0	3.0
Primary balance	-0.5	-1.1	-1.3	0.2	0.4	0.4
Effective interest rate	3.5	3.0	3.8	4.5	5.4	6.1

Real GDP Growth Shock	2019	2020	2021	2022	2023	2024
Real GDP growth	3.5	2.9	2.9	4.0	4.0	4.0
Inflation	2.0	2.1	2.5	3.0	3.0	3.0
Primary balance	-0.5	-0.3	-0.5	0.2	0.4	0.4
Effective interest rate	3.5	2.8	2.9	3.1	3.5	3.9
Real Exchange Rate Shock						
Real GDP growth	3.5	4.0	4.0	4.0	4.0	4.0
Inflation	2.0	6.3	2.8	3.0	3.0	3.0
Primary balance	-0.5	0.0	0.2	0.2	0.4	0.4
Effective interest rate	3.5	3.0	2.8	3.0	3.4	3.8
IMF Recommended Fiscal Adjustment						
Real GDP growth	3.5	4.0	4.0	4.0	4.0	4.0
Inflation	2.0	2.4	2.8	3.0	3.0	3.0
Primary balance	0.7	1.2	1.5	1.5	1.5	1.5
Effective interest rate	3.5	2.8	2.9	2.9	3.4	3.7

Source: IMF staff.

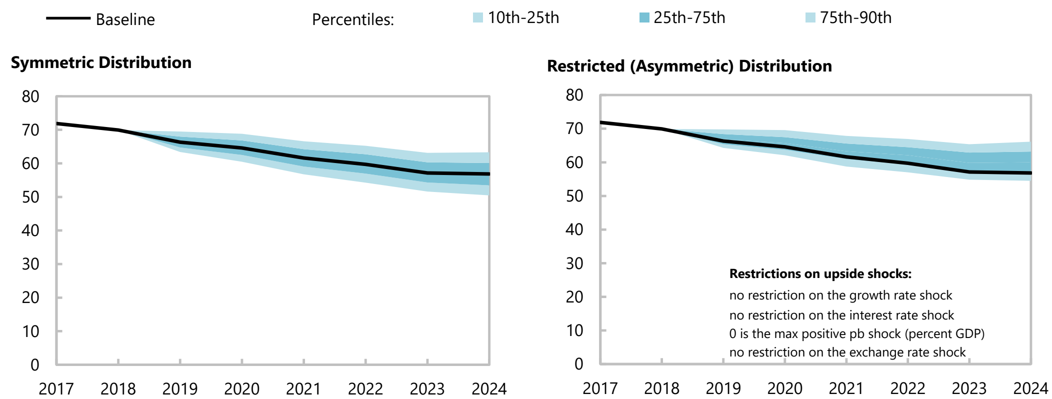
Albania: Public DSA Risk Assessment

Heat Map

Debt level 1/	Real GDP Growth Shock	Primary Balance Shock	Real Interest Rate Shock	Exchange Rate Shock	Contingent Liability shock
Gross financing needs 2/	Real GDP Growth Shock	Primary Balance Shock	Real Interest Rate Shock	Exchange Rate Shock	Contingent Liability Shock
Debt profile 3/	Market Perception	External Financing Requirements	Change in the Share of Short-Term Debt	Public Debt Held by Non-Residents	Foreign Currency Debt

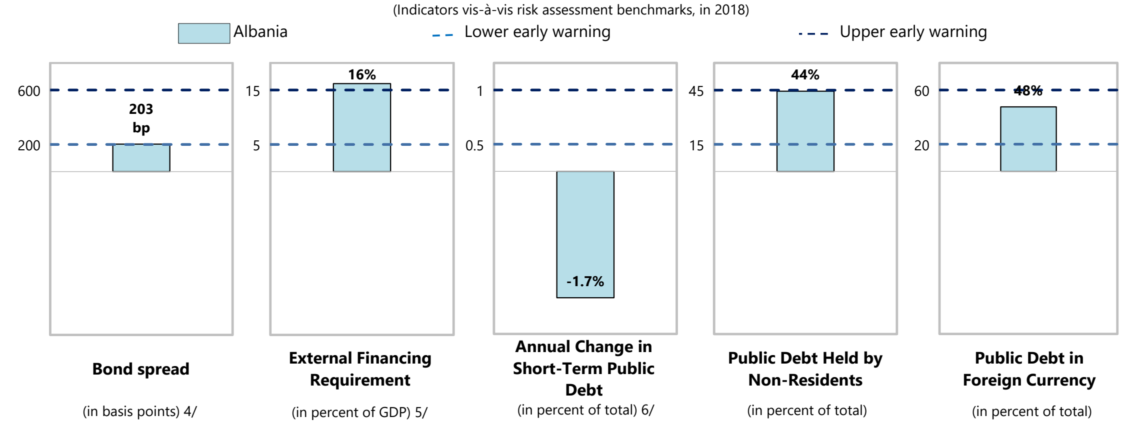
Evolution of Predictive Densities of Gross Nominal Public Debt

(in percent of GDP)



Debt Profile Vulnerabilities

(Indicators vis-à-vis risk assessment benchmarks, in 2018)



Source: IMF staff.

1/ The cell is highlighted in green if debt burden benchmark of 70% is not exceeded under the specific shock or baseline, yellow if exceeded under specific shock but not baseline, red if benchmark is exceeded under baseline, white if stress test is not relevant.

2/ The cell is highlighted in green if gross financing needs benchmark of 15% is not exceeded under the specific shock or baseline, yellow if exceeded under specific shock but not baseline, red if benchmark is exceeded under baseline, white if stress test is not relevant.

3/ The cell is highlighted in green if country value is less than the lower risk-assessment benchmark, red if country value exceeds the upper risk-assessment benchmark, yellow if country value is between the lower and upper risk-assessment benchmarks. If data are unavailable or indicator is not relevant, cell is white.
Lower and upper risk-assessment benchmarks are:

200 and 600 basis points for bond spreads; 5 and 15 percent of GDP for external financing requirement; 0.5 and 1 percent for change in the share of short-term debt; 15 and 45 percent for the public debt held by non-residents; and 20 and 60 percent for the share of foreign-currency denominated debt.

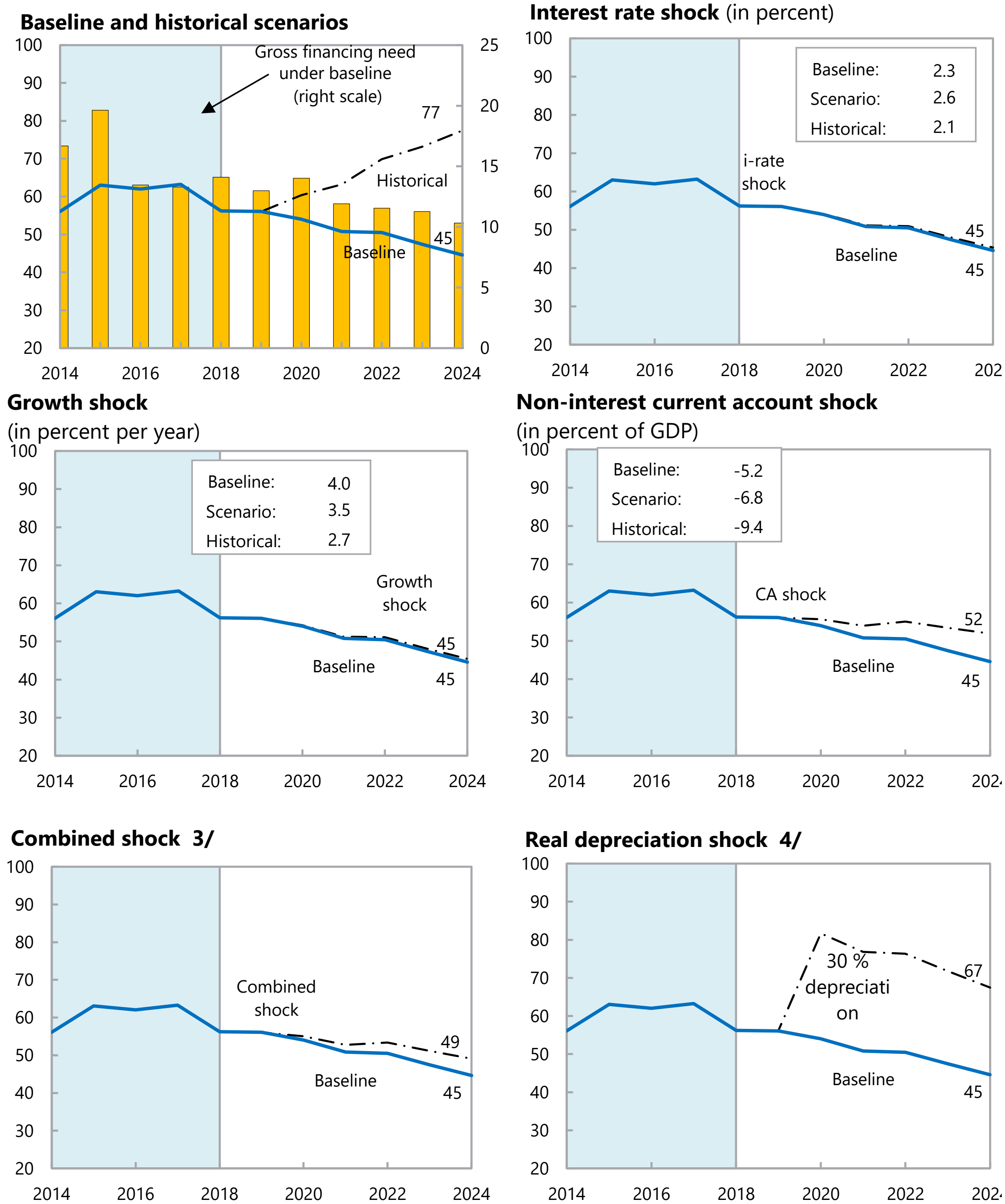
4/ Bond Spread over German Bonds, an average over the last 3 months, 20-Dec-18 through 20-Mar-19.

5/ External financing requirement is defined as the sum of current account deficit, amortization of medium and long-term total external debt, and short-term total external debt at the end of previous period.

6/ Following the Eurobond issuance in November, 2015, the government reduced issuance of short-term debt by both reducing rollovers and buying back bonds maturing in early 2016.

Albania: External Debt Sustainability: Bound Tests 1/ 2/

(External debt in percent of GDP)



Sources: International Monetary Fund, Country desk data, and staff estimates.
1/ Shaded areas represent actual data. Individual shocks are permanent one-half standard deviation shocks. Figures in the boxes represent average projections for the respective variables in the baseline and scenario bein presented. Ten-year historical average for the variable is also shown.
2/ For historical scenarios, the historical averages are calculated over the ten-year period, and the information i used to project debt dynamics five years ahead.
3/ Permanent 1/4 standard deviation shocks applied to real interest rate, growth rate, and current account balance.
4/ One-time real depreciation of 30 percent occurs in 2010.