
COUNTRY REPORT

Albania

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The Economist Intelligence Unit

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Summary

January 2001

- Outlook for 2001-02** Following its victory in the local government elections in October, the Socialist Party of Albania (SPA) has a good chance of retaining power at the general election in mid-2001, and continuing Albania's progress towards internal stability after collapsing twice into anarchy in the 1990s. Real GDP growth of about 7-7.5% is likely in 2001-02, underpinned by domestic and foreign investment, some of it going into agriculture, which generates half of GDP. However, the recent electricity crisis suggests that economic growth may hit a ceiling, held back by poor infrastructure.
- The political scene** In the local elections in October 2000, 43% of the electorate voted for the SPA, which leads the government coalition but was standing on its own in most cases. Foreign observers said that there were irregularities, but not enough to mar the result; the main opposition Democratic Party (DP), however, withdrew from the second round. It then began a protest campaign of demonstrations, which have been marred by violence, raising the political temperature. The prime minister, Ilir Meta, has reshuffled his cabinet, demoting a rival, the former interior minister, Spartak Poci. Albania took a step towards the EU at the Zagreb summit in November, with preparations under way for a stabilisation and association agreement. Albania has viewed with caution developments in Yugoslavia since Slobodan Milosevic's departure from power. A realignment in Albania's relations with the Kosovo Albanians may follow a meeting between Mr Meta and Ibrahim Rugova, the Kosovo Albanian leader who in the past has been closer to the DP than the SPA.
- Economic policy** The IMF has renewed its positive appraisal of the government's handling of the economy. The fiscal deficit for 2001 will rise slightly to 9.1% of GDP. In the 2001 budget, public investment is to increase. The structure of taxation is changing, with cuts in the rate of profit tax. Monetary policy remains tight. Bids have been invited for a second mobile telephone network.
- The domestic economy** Real GDP growth has continued apace, although the official estimate of 7.8% growth for 2000 is likely to be overoptimistic: the EIU is estimating 7.5% growth because of the electricity shortage that has hit domestic production in the last two months of the year. Consumer prices have remained stable and unemployment has declined.
- Foreign trade and payments** Exports increased in the third quarter, but the trade deficit remains wide. The EU, the country's main trading partner, has opened up further to Albanian exports. Foreign investment has increased. The lek has remained firm.
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Political structure

Official name	Republic of Albania	
Legal system	A new constitution was adopted by referendum on November 22nd 1998 and came into effect on November 28th. It replaced the interim constitution that had been in place following the abandonment of the Marxist-inspired constitution in April 1991	
National legislature	Unicameral People's Assembly of 155 members: 115 directly elected and 40 elected by proportional representation. Under the new constitution, the number will be reduced to 140: 100 elected directly and 40 by proportional representation from party lists	
National elections	June-July 1997 (parliamentary), July 1997 (presidential); next parliamentary election due by June 2001	
Head of state	President, currently Rexhep Mejdani, elected by the People's Assembly, July 1997	
National government	Coalition, led by the Socialist Party of Albania, received parliamentary approval in June-July 1997; last cabinet reshuffle, November 2000	
Main political parties	<p>Government coalition, Alliance for the State (AS): Agrarian Party (AP), Democratic Alliance (DA), National Unity Party (NUP), Party of Democratic Unity and Prosperity, Social Democratic Party (SDP), Socialist Party of Albania (SPA), Union for Human Rights (UHR). Opposition coalitions: Union for Democracy (UD), comprising Albanian Liberal Union (ALU), Christian Democratic Party (CDP), Democratic Party (DP), Democratic Union (DU) and National Democratic Front (NDF); and Albanian Right Wing, including Conservative Party (CP), National Front Party (NFP) and Republican Party (RP). Unattached: Albanian National Community Party, Albanian Workers' Movement Party, New Socialist Party, Albanian Communist Party, Legality Movement (LM)</p>	
	Prime minister	Illir Meta (SPA)
	Deputy prime minister & minister for labour & social affairs	Makbule Ceco (SPA)
	Secretary of state to the prime minister	Ndre Legisi (SPA)
Key ministers	Agriculture & food	Lufter Xhuveli (AP)
	Culture, youth & sports	Esmeralda Uruci (independent)
	Defence	Ismail Lleshi (SPA)
	Economic co-operation & trade	Ermelinda Meksi (SPA)
	Education & science	Ethem Ruka (SPA)
	Finance	Anastas Angjeli (SPA)
	Foreign affairs	Paskal Milo (SDP)
	Health	Leonard Solis (UHR)
	Interior	Illir Gjoni (independent)
	Justice	Arben Imami (DA)
	Local government	Bashkim Fino (SPA)
	Public economy & privatisation	Mustafa Muci (SPA)
	Public works	Spartak Poci (SPA)
	Transport	Sokol Nako (independent)
Central bank governor	Shkelqim Cani	

Economic structure

Annual indicators

	1996	1997	1998	1999	2000 ^a
GDP at current prices (Lk bn)	281.0	341.7	460.6	506.2	529.5
Real GDP growth (%)	9.1	-7.0	8.0	7.3	7.5
Consumer price inflation (av; %)	12.7	32.9	20.9	0.4	-0.1
Population (mid-year; m)	3.3	3.3	3.4	3.4	3.4
Exports of goods fob (US\$ m)	243.7	158.6	208.0	275.0	300.0
Imports of goods fob (US\$ m)	922.0	693.6	811.7	938.0	1,019.5
Current-account balance (US\$ m)	-107.3	-272.2	-65.1	-156.0	-162.4
Reserves excl gold (US\$ m)	280.9	308.9	348.5	369.1	360.0
External debt (US\$ bn)	0.7	0.7	0.8	0.9	1.0
Exchange rate (av; Lk:US\$)	104.50	148.93	150.63	137.69	143.81

December 29th 2000 Lk142.75:US\$1; Lk134.02:€1

Origins of gross domestic product 1999	% of total	Components of gross domestic product 1999	% of total
Agriculture	53.3	Private consumption	96.9
Industry	25.0	Public consumption	9.6
Services	21.7	Gross fixed investment	16.0
Total	100.0	Exports of goods & services	10.0
		Imports of goods & services	-32.2
		Total	100.0

Principal exports 1999	% of total	Principal imports 1999	% of total
Textiles & footwear	60.4	Textiles & footwear	16.3
Mineral products	6.4	Vegetable products	11.5
Base metals	5.3	Machinery & electrical equipment	11.4
Foodstuffs, beverages & tobacco	4.6	Foodstuffs, beverages & tobacco	9.1
Vegetable products	4.5	Mineral products	8.6

Main destinations of exports 1999	% of total	Main origins of imports 1999	% of total
Italy	66.9	Italy	37.6
Greece	14.4	Greece	28.2
Germany	5.5	Germany	5.5
Austria	2.1	Turkey	5.5
Macedonia	1.5	Bulgaria	2.8

^a EIU estimates.

Quarterly indicators

	1998	1999				2000		
	4 Qtr	1 Qtr	2 Qtr	3 Qtr	4 Qtr	1 Qtr	2 Qtr	3 Qtr
Government finance (Lk m)								
Revenue	26,884	24,874	24,477	27,325	31,133	28,720	28,315	n/a
Expenditure	44,802	33,221	37,691	40,400	53,848	33,639	38,108	n/a
Balance	-17,918	-8,347	-13,214	-13,075	-22,715	-4,919	-9,793	n/a
Prices								
Consumer prices (Dec 1993=100)	219.5	223.5	220.0	213.0	216.5	220.0	218.9	212.3
% change, year on year	9.6	3.8	-0.1	-0.8	-1.4	-1.6	-0.5	-0.4
Financial indicators								
Exchange rate								
Lk:US\$ (av)	141.2	140.9	141.2	134.6	134.1	139.0	143.5	144.2
Lk:US\$ (end-period)	140.6	147.7	136.9	134.1	135.1	141.1	139.6	147.0
Bank rate (end-period; %)	23.4	21.7	21.5	18.7	18.0	15.9	13.8	11.6
M1 (end-period; Lk bn)	83.73	79.68	87.31	90.59	103.00	103.88	107.30	112.95
% change, year on year	-8.7	-6.1	7.9	10.1	23.0	30.4	22.9	24.7
M2 (end-period; Lk bn)	239.53	250.50	264.39	274.88	292.87	295.41	299.84	311.73
% change, year on year	20.6	23.3	24.5	22.0	22.3	17.9	13.4	13.4
Foreign trade ^a & payments (US\$ m)								
Exports fob	63.4	72.9	78.4	58.6	65.1	64.2	69.1 ^b	63.9 ^b
Imports fob	-240.6	-185.6	-250.2	-252.1	-250.1	-226.6	-259.8 ^b	-264.4 ^b
Trade balance	-177.2	-112.7	-171.8	-193.5	-185.0	-162.4	-190.7 ^b	-189.9 ^b
Services balance	-13.0	-5.7	87.0	18.9	6.1	14.2	n/a	n/a
Income balance	26.6	17.6	24.3	15.6	17.8	24.8	n/a	n/a
Transfers balance	178.0	114.7	94.2	66.8	50.3	101.0	n/a	n/a
Current-account balance	14.3	13.9	33.7	-92.2	-110.8	-50.8	-118.0	n/a
Reserves excl gold (end-period)	348.5	345.5	341.5	383.4	369.1	368.6	373.5	358.0

^a Balance-of-payments basis. ^b Customs based; imports cif.

Sources: Bank of Albania, *Monthly Statistical Report*; Institute of Statistics, *Indeksi i Cimeve te Konsumit Viti: Situation of Foreign Trade*; IMF, *International Financial Statistics*.

Outlook for 2001-02

Political outlook

Domestic politics Following the victory of the ruling Socialist Party of Albania (SPA) in the local government elections in October 2000, at which it gained 43% of the total vote, the party has a good chance of retaining power at the general election in mid-2001. Whereas before the elections the opposition Democratic Party (DP) held 80% of the towns and communes, it now holds only 24%. The SPA's achievement was all the greater because the party campaigned on its own, without support from its partners in the government coalition.

The political scene in Albania has been highly volatile since the collapse of communism. The SPA lost power at the 1992 elections after mob violence, but regained it in 1997, again after violent protests against the DP government led by the then president, Sali Berisha. The EIU believes, however, that Albania is making progress towards a more normal parliamentary style of politics, with elections that are seen to be properly conducted and leading to a fair result and orderly transfers of power.

A greater danger is whether the SPA has the internal cohesion necessary to repeat its electoral success in 2001. Fatos Nano, who led the party to victory in June 1997 but was later forced out of leading the government, only regaining the party chairmanship in October 1999, is increasingly acting as if he were prime minister again. He heads a faction in the cabinet in opposition to the prime minister, Ilir Meta, who has his own following. A reshuffle in October 2000 demoted the one senior minister, Spartak Poci, who is in neither camp, but who remains a close friend of a third former prime minister, Pandeli Majko. Mr Majko's chances of re-entering government are slim, but Mr Poci's considerable political stature—gained in combating crime and strengthening internal security—could be the focus for a realignment if Mr Nano and Mr Meta became open enemies. A factor in Mr Poci's demotion was Mr Meta's fear of him as a rival for the premiership. However, although these tensions undoubtedly exist within the SPA, it appears that they have not damaged its effectiveness; factionalism is part of Albanian political life, and the removal of Mr Majko from the premiership was achieved without weakening the government.

Opposition disarray The SPA may be assisted to victory in the parliamentary election by disarray among the opposition. The DP leader, Mr Berisha, has been weakened by the defeat of his party, his fruitless boycott of the second round of voting in the local elections and the appearance of a credible alternative leader in the person of Genc Pollo, who heads a DP "reform movement". The reformers have gained ground by showing restraint in not setting their candidates deliberately against those of Mr Berisha at the polls, and then taking the opportunity to blame him for the party's electoral failure. Their argument that he cannot provide a constructive opposition to the government has been vindicated by his campaign of rallies since the October elections, which have achieved little but disorder.

The DP remains a substantial force (it gained few local government seats but still achieved 34% of the vote). At the moment Mr Berisha seems to be still firmly in control of his party, making it unlikely that Mr Pollo will achieve his removal as party leader. However, in the longer term another defeat at the polls in 2001 would probably precipitate Mr Berisha's departure and a recovery in the SPA's electoral prospects. In the past Mr Berisha's policy has been to use street protests to put pressure on the government to call early elections; now that an election is approaching, the call is to replace the administration with a caretaker "government of national unity" to supervise the election. Such a policy only makes sense if it ends in electoral victory; if Mr Berisha's strategy produces yet another defeat, it is likely that pressure will build within the party to choose a different leader with a more contemporary political style.

International relations Because of its support for Kosovo's eventual independence, Albania will be less affected than other neighbouring states by the political changes in Yugoslavia (Serbia-Montenegro) following Slobodan Milosevic's departure from power. In its suspicions that Yugoslavia has not really changed its intentions, however, it may find allies in Croatia and Montenegro. Stability in the Balkans will depend on how Montenegro's relations with Serbia are handled. Outright secession would encourage the ethnic Albanians in Kosovo to press for their own formal detachment from Yugoslavia, opening up the possibility of disorder in Macedonia, which has a sizeable Albanian minority of its own. There is therefore a risk of tension re-emerging in the Balkans, with the Albanians closely involved. The probable eventual political eclipse of Mr Berisha, however, would free Mr Meta to pursue collaboration with Ibrahim Rugova, the moderate winner of the local elections in Kosovo, and to support a peaceful, negotiated solution to the aspirations of ethnic Albanians in Kosovo.

Mr Meta must rebuild relations with Greece, which could obstruct Albania's policy of joining NATO and the EU, after the damage caused when the SPA combined in the local elections with most other parties to defeat a Greek minority party in southern Albania. If, as the SPA hopes, Albania is to start negotiations with the EU on a stabilisation and association agreement before the general election, Greece as an EU member must be well disposed. A new US president will presumably bring a change in the US ambassador, removing a strong supporter of the present government. However, US foreign policy towards Albania is unlikely to change.

Economic policy outlook

Policy trends Speaking at the IMF-World Bank annual meeting in Prague in October 2000, the Albanian finance minister, Anastas Angjeli, listed policy priorities as achieving sustained macroeconomic stability and structural reform in order to reduce poverty, improve living standards and narrow the development gap with other countries in the region. However, Albania's still weak institutional capacity will make this difficult to achieve, and it will continue to depend on international support and guidance.

Strong growth in 2000, forecast to continue in 2001, together with low single-digit inflation have made Albania one of the best performers among the beneficiaries of the IMF's poverty reduction and growth facility (PRGF) arrangements. The current facility ends in June 2001, but a strategy for a PRGF-2 to follow on for three years has been formulated in association with IMF, World Bank, EU and UN advisers. It is therefore likely to be in place before the general election.

The government's main concerns are to develop agriculture and improve infrastructure, including the road network and (following an energy crisis in late 2000) the electricity supply. Building up tourism is a longer-term objective. The government is spending to boost employment, but the main emphasis is on encouraging private enterprise, both domestic and foreign. The financial sector is being restructured to improve intermediation between savers and businesses. Legislation on free-trade zones is intended to attract foreign businesses, for which the general environment is improving in two respects: personal safety throughout the country is better ensured by improvements in law and order; and the heavy investment in road building allows easier circulation of freight.

Fiscal policy The government aims to reduce the budget deficit from an estimated 11.3% of GDP in 1999 to 9.1% in 2001. On preliminary returns, government expenditure, allowing for a supplementary Lk4bn (US\$27.8m) authorised in September, is on target for a 9% deficit in 2000. The domestically financed deficit, at 5% of GDP, is likely to be slightly higher than the 4.5% recorded in 1999. The tax base has expanded, owing to greatly improved tax collection. The government aims to monitor both budget revenue and spending, in particular (under IMF urging) the collection of customs duties. The rate of profit tax has been cut from 30% to 25% from January 2001 to encourage business, and the highest customs rate has been reduced from 18% to 15%, with the rate on imports of machinery cut from 5% to 2%.

Privatisation policy The government plans to sell in 2001 the fixed-line telephone provider, Albtelecom, the petrol distributor, Servcom, a number of hydroelectric generating stations, and two large hotels in Tirana and Durres. The sale of the Savings Bank is projected for late 2001, but it may be held up by its poor profitability. The electricity utility, Korporata Elektroenergjitike Shqiptare (KESH), is also to be privatised, but this will almost certainly be delayed because of its poor performance. However, the stability of the lek, continued strong GDP growth and very low inflation should make privatisation more attractive to foreign investors.

Economic forecast

International assumptions Global growth peaked in mid-2000 and real world GDP growth is forecast to decelerate in 2001-02 to around 4%—still a respectable rate of growth. The greatest single threat remains that of a US recession, the risk of which has increased since November 2000 from a one-in-six to a one-in-four chance. A hard landing in the US would restrict the EU to only sluggish growth, with a

knock-on effect on eastern Europe. However, we expect real GDP growth in the EU to moderate only slightly, from 3.3% in 2000, the fastest rate since 1990, to 3% in 2001 and 2.6% in 2002.

Economic activity in the EU has been boosted by the weakness of the euro, which has enhanced EU competitiveness abroad. However, the euro is expected to appreciate in real terms in 2001. Domestic demand in the EU will moderate but there will still be a market for imports from eastern Europe, including Albania, which trades almost entirely with the EU, mainly Italy and Greece, most of its exports being finishing work for foreign contractors, exploiting low local labour costs. We expect oil prices to fall in 2001 as supply exceeds demand. This will moderate the inflationary pressure from the high prices of imported oil that have been recorded in 2000.

International assumptions summary

	1999	2000	2001	2002
GDP growth (%)				
US	4.2	5.1	3.2	2.6
OECD	3.0	4.1	3.0	2.7
EU	2.4	3.3	3.0	2.6
Exchange rates (av)				
US\$ effective (1995=100)	116.4	120.9	120.1	113.2
US\$:€	1.07	0.92	0.95	1.05
Financial indicators				
US\$ 3-month commercial paper rate	5.18	6.32	6.25	5.25
€ 3-month interbank rate	2.97	4.50	5.00	4.70
Commodity prices				
Oil (Brent; US\$/b)	17.9	28.8	23.4	19.1
Food, feedstuffs & beverages (% change in US\$ terms)	-18.6	-6.0	10.6	14.1
Industrial raw materials (% change in US\$ terms)	-4.2	14.2	4.2	9.6

Economic growth

With the present Albanian administration likely to continue in office after mid-2001, IMF and World Bank assistance expected with a PRGF-2, and infrastructure investment continuing because of the EU Stability Pact for South-eastern Europe, real GDP growth of about 7-7.5% is likely in 2001-02. Domestic and rising foreign investment will underpin that growth. Agriculture, which generates half of GDP, is likely to be strongly featured in the PGRF-2, as policy concentrates on modifying income differentials between rural and urban areas.

To the extent that new investment into (now wholly privatised) agriculture with security of tenure is capital intensive and encourages land consolidation, redundant rural labour may reverse the recent fall in unemployment from its present high level. Social protest from that source would have to be included in the political equation if non-farm employment is not substantially increased. Foreign and domestic private-sector capital is essential to such diversification of the production profile. There remains the possibility that the opposition DP, having failed to displace the government at the election in mid-2001, may foment protests that could disrupt the smooth path of economic growth, but Albania's gradual progress towards a more orderly society renders that scenario less and less likely.

Investment in assets that will generate goods and services is slowly picking up, but much of the productive capacity inherited from communist industrialisation is obsolete or wrecked. The continuing recession in the extractive branch is holding back the whole sector, but metallurgy is reviving. Services are expected to expand in 2001-02 by about 12-15%, spearheaded by privatisation in the telecoms and financial services branches. However, the recent electricity crisis suggests that Albania's economic growth may hit a ceiling because of the constraints of its poor infrastructure.

Forecast summary

(% real change year on year unless otherwise indicated)

	1999 ^a	2000 ^b	2001 ^c	2002 ^c
Real GDP	7.3	7.5	7.5	7.0
Agricultural output	5.0	5.2	4.5	3.0
Consumer price inflation (av; %)	0.4	-0.1	2.6	2.0
Exports of goods (US\$ m; fob)	275	300	350	440
Imports of goods (US\$ m; fob)	938	1,020	1,140	1,250
Current-account balance (US\$ m)	-156	-162	-169	-109
% of GDP	-4.2	-4.3	-4.2	-2.6
Exchange rate (av; Lk:US\$)	137.69	143.81	150.00	155.00

^a Actual. ^b EIU estimates. ^c EIU forecasts.

Inflation Domestic expansion is unlikely to be accompanied by significant inflation. Average consumer price inflation is estimated at -0.1% in 2000, but is forecast to accelerate, nearing 3% in 2001, before falling back to 2% in 2002.

Albania is a highly import-dependent economy, and therefore the exchange rate is of crucial importance to the rate of inflation. Monetary policy remains tight and the rate of saving is likely to rise, both as inflationary expectations remain stable and the banking network develops to serve as an intermediary between households and small business and the corporate sector. The Bank of Albania (BoA, the central bank) has lifted its controls on interest rates set by state-owned banks. An IMF report has shown that the effect of the pyramid schemes of 1996-97 was less serious than perceived; the regulatory measures subsequently imposed have enhanced confidence in the financial system.

Exchange rates With low domestic inflation and external reserves levels close to those of a year ago, the lek is forecast to depreciate slowly in nominal terms against the US dollar to average around Lk150:US\$1 in 2001 and Lk155:US\$1 in 2002.

The lek maintained its value in 2000. By mid-December it had depreciated against the US dollar by 7% since the beginning of the year, and had appreciated against the euro by 6%. The expectation for end-2001 is for the rate to fall in nominal terms in line with domestic inflation, to Lk152:US\$1.

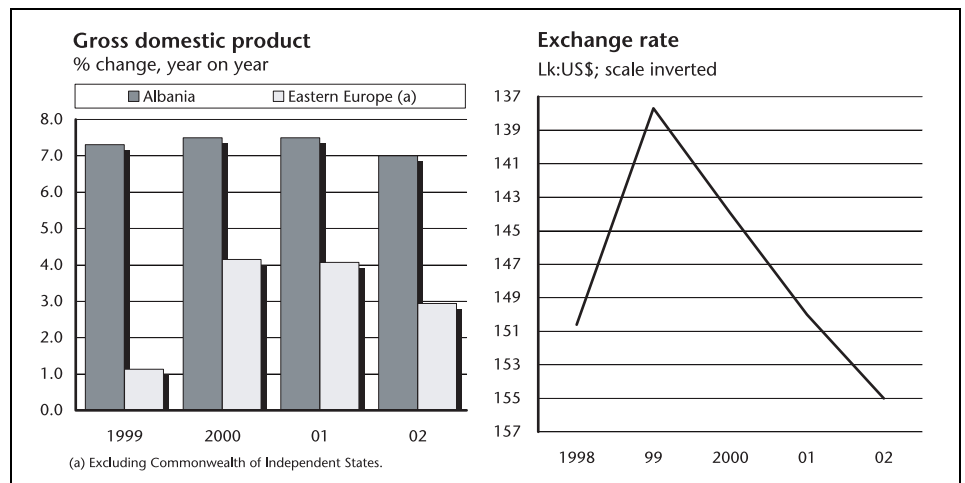
External sector Exports are expected to increase in 2001-02, as an improving internal situation encourages foreign companies to locate production in Albania, attracted by cheap, well-educated labour, and as agricultural exports increase. Rising tourism revenue should help a continuing strong inflow of remittances home by

emigrant workers to narrow the current-account deficit from 4.2% of GDP in 1999 to 2.6% by 2002.

The EU's decision in September to lift customs dues for 95% of Albanian imports (from 80%; the decision also applies to Bosnia and Hercegovina, Croatia, Kosovo and Macedonia) should help trade with the EU. Albanian farmers may expect to increase sales of early season vegetables in countries further north. Steady economic growth in the EU assures a continued flow of emigrants' remittances, most of which are generated by workers in the EU. Trading links will be improved by better access through Serbia.

Imports will also increase, but at a slower rate than exports, as industry slowly revives and gradually reduces import dependency, and as rising farm production cuts food imports and boosts exports. A revival in industrial production is heralded by machinery imports, which should increase Albania's export capacity.

On returns for the first three quarters of 2000, exports covered only 26.3% of imports, and the balance-of-payments gap has to be filled mainly by a continued flow of emigrants' remittances and by external financing. Foreign direct investment (FDI) of US\$92m in 2000 was nearly back to the inflow registered in 1996 (US\$97m) and is officially forecast to increase substantially in 2001. Official funding and private-sector investment will flow in to maintain reserves and the stability of the lek.



The political scene

Electorate backs Socialists in local elections

The local elections were the first test at the ballot box of the government that gained power in June 1997: they delivered an electoral majority to the Socialist Party of Albania (SPA), the senior coalition partner, sufficient to suggest that, barring major changes, the parliamentary election that is due by June 2001 will return the SPA to power. The elections were held on October 1st and there were run-offs on October 15th; further voting was required in some localities on October 29th and November 12th. At stake was control of 65 towns (mayor

and councillors) and 309 communes (chairmen and councillors); the capital, Tirana, had recently been divided into 11 microdistricts. Mayors and chairmen were elected directly and councillors by party under a system of proportional representation. The turnout was 62%. According to the final results released on November 7th, the SPA won 255 towns and communes; its main rival, the Democratic Party (DP), won only 90.

Local elections, Oct 2000

	Votes cast	% of votes	Mayors	Councillors
Socialist Party of Albania (SPA) ^a	579,806	43.04	255	2,573
Democratic Party (DP) ^a	452,052	33.56	90	1,962
Social Democratic Party (SDP)	95,736	7.11	9 ^a	517
Democratic Alliance (DA)	42,137	3.13	1	238
Republican Party (RP)	36,591	2.72	3	188
Christian Democratic Party (CDP)	31,447	2.34	0	116
Union for Human Rights (UHR)	30,757	2.28	8 ^a	179
United Right Wing	28,227	2.10	0	117
Agrarian Party (AP)	20,798	1.54	7	99
Albanian Communist Party (ACP)	11,508	0.85	0	49
Total incl others	1,347,322	100.00	378 ^b	6,086

^a Where the SPA and DP were standing jointly with candidates from minor parties, the votes and seats gained are included in the major party's total. This also applies to mayoral seats won by the SDP and UHR. ^b Not including undecided contests as at November 7th.

Source: Organisation for Security and Co-operation in Europe (OSCE), Office for Democratic Institutions and Human Rights, *Republic of Albania, Local Government Elections, Final Report* (December 11th 2000).

The day after the first round the Central Electoral Commission appraised the elections as “free, democratic and transparent”. The deputy minister of public order, Col Bujar Himci, cited only three incidents, including a demonstration and shooting in Lac, which escalated into the killing of a DP activist. The prime minister, Ilir Meta, said that the elections were “not only the fairest, most democratic and most transparent the country has ever had, but also the calmest”.

Other parties allege irregularities

However, the DP leader, Sali Berisha, condemned the voting in Tirana as “an electoral farce that was totally manipulated”, an allegation that he soon extended to Elbasan, Durrës, Fier and Korça. All the parties in the DP-led coalition grouping, the Union for Democracy, two of the parties in the Albanian Right Wing (ARW) grouping and the Legality Movement (LM) sided with the DP in alleging voting irregularities. More seriously, they were joined by two parties in the government coalition, Alliance for the State—the Democratic Alliance (DA) and the Union for Human Rights (UHR), which represents Albania's minorities. There must be an element of party politics in these criticisms; Albanian elections have usually ended in allegations of fraud. International observers, led by the Organisation for Security and Co-operation in Europe (OSCE) and the Council of Europe, declared that “some irregularities had been noted but none seemed significant enough to have any impact on the results”.

DP withdraws from second round	<p>A second round of elections was held on October 15th for areas where none of the mayoral candidates had secured 50% of the vote. After initially expressing readiness for his party's candidates to participate in the run-offs, Mr Berisha said that evidence of numerous irregularities in the first round had compelled him to call for non-participation. This evinced protests from DP candidates whose first-round vote had given them a high chance of success. Dispensations to stand were given in Shkoder, Vaj i Dejes and Korca, but these only covered 5% of the DP candidates who could have stood. The DP's reform wing of dissident members rejected the boycott.</p> <p>The OSCE found the conduct of the second round less satisfactory than the first, although it stopped short of condemning the results. It particularly regretted the "nationalistic rhetoric" that marred voting at Himare, a Greek-speaking district, where an SPA candidate with the support of all ethnic Albanian parties defeated the UHR, although it is in coalition with the SPA at the national level. Some Greek MPs encouraged an Albanian nationalist reaction by coming to Albania and openly backing the UHR candidate, causing tension in Albania's relations with its neighbour.</p>
Violence mars the DP's protest campaign	<p>Addressing a mass rally in Tirana on October 27th, Mr Berisha declared "we shall never accept the humiliation we experienced at the hands of the ruling clique on October 1st". Banners at the rally carried the slogans "We do not want dictatorship", and, in a reference to the communist dictator, Enver Hoxha, "Meta has restored the era of the damned man." The DP embarked on a campaign of demonstrations calling for a caretaker government until the parliamentary election in mid-2001, which have raised the political temperature and led to violent incidents.</p> <p>At an enlarged DP National Council on November 18th Mr Berisha obtained the support of eight other parties both within and outside the Union for Democracy to submit a report on election irregularities and to "paralyse state institutions" by protest rallies, for which a co-ordinating central staff was established. In the course of the rallies an SPA deputy's car was burnt in front of the parliament building, petrol bombs were thrown at the prime minister's office and public buildings were stoned. On November 28th, Albania's National Day, two people died after DP demonstrators in Bajram Curri attacked the police station and courthouse in Tropoje district (Mr Berisha's home territory). The following day Mr Berisha was briefly detained in Tirana by the police, as a warning that events were getting out of control. Since then 30 demonstrators have been convicted for the violence in Tirana.</p>
EU and US differ on seriousness of the situation	<p>The political scene is still violent. After Edi Rama was elected for the SPA as mayor of Tirana, shots were fired at his house (the DP dissociated itself from the incident), and in mid-December a roadside bomb was detonated in Fushe-Kruja half an hour before the prime minister was due to pass by on his way to the local cement factory. In early December the EU expressed concern at "the increasing use of violence in pursuit of political aims" and implied that it could set back Albanians' desire for a closer relationship. However, the US ambassador in Tirana, Joseph Limprecht, put his weight behind the Meta</p>

government a few days later. In a speech to judges, the envoy criticised those who used violence to gain political advantage, adding, however, that the confrontation would not plunge the country into anarchy because of the progress made since the disorder of 1997-98.

DP reformers put pressure on Mr Berisha

Genc Pollo, once the closest collaborator of Mr Berisha and now leading the DP reform movement, said that Mr Berisha's rallies were an attempt to deflect criticism for losing the elections. The reformers have been touring DP regional branches to gain support. They received a boost when the Austrian foreign minister, Benita Ferrero-Waldner, visiting Albania as OSCE chairman, met Mr Pollo and two other reform deputies, Leonard Demi and Ferdinand Xhaferri. Mr Pollo was invited to a US-sponsored conference in Athens on the position of the Albanians in the Balkans, which was attended by Javier Solana, the EU's foreign policy chief, and Bernard Kouchner, the head of the UN interim administration in Kosovo (UNMIK).

Meanwhile, there are indications of a realignment on the right that could eventually supplant Mr Berisha. The smallest of the three parliamentary alliances, the ARW, has suggested collaboration with Mr Pollo's reform movement. Analysing the results of the local elections, a leading ARW politician, Petrit Kalikula, described Mr Berisha's followers as incapable of change, whereas the DP reformers could offer a more constructive opposition to the SPA in partnership with the ARW.

Mr Meta demotes a rival

After the success of the SPA in the local elections, Mr Meta took steps in November to reinforce his own position, carrying out his third cabinet reshuffle since taking office in October 1999 and the sixth since the government came to power in 1997 (July 2000, pages 14-15). Transferring the interior minister, Spartak Poci, to the junior public works portfolio, the prime minister weakened a potential rival. However, Mr Meta is still forced to share authority with the SPA chairman, Fatos Nano, who has made himself available to foreign visitors and international emissaries. Relations between the two SPA leaders have been tense since Mr Meta replaced Pandeli Majko as prime minister—a post that Mr Nano would have preferred for himself. Mr Meta, who is 32, represents a modernising, technocratic approach, whereas Mr Nano (48) has links with the party's traditional supporters.

Mr Poci had performed better than any previous interior minister in combating the criminal gangs fostered by corruption under Mr Berisha's presidency and the 1997 insurgency and looting of army arsenals. Public opinion must be considered ahead of the parliamentary election, and therefore a niche was found for him, as a structural engineer, as minister of public works. Ilir Zela was dismissed after only four months with that portfolio. Since a strong hand was needed at the Ministry of the Interior, the defence minister, Ilir Gjoni, took Mr Poci's place, being replaced in turn by a newcomer, Ismail Lleshi. Mr Gjoni had also only taken over the Ministry of Defence in July and, as an independent, has no party allies in the government. He does not lack experience—he was his minister's *chef de cabinet*—but he and Mr Lleshi together form an untried team, responsible for the security of a state that is among Europe's worst for political fragility and poverty (as measured by GDP per head).

Because of the election of Mr Rama as mayor of Tirana, a new culture minister was required. Mr Meta doubled the number of women in his cabinet by appointing Esmeralda Uruci, who had been narrowly defeated as an independent with SPA support in the Shkoder mayoral election. She is 39 and was dean of the economics faculty at Shkoder university.

The government coalition holds together

Neither the election campaign (which sometimes pitted government parties against each other) nor the reshuffle has affected the four posts held by coalition partners, three of which have not been changed since Mr Nano's first cabinet of 1997—Lufter Xhuvëli of the Agrarian Party (AP) at the agriculture ministry, Paskal Milo of the Social Democratic Party (SDP) at the foreign ministry and Leonard Solis of the preponderantly Greek-minority UHR at the health ministry. Arben Imami came from the Democratic Alliance (DA) to the Ministry of Justice only in July, having been a minister of state in the Majko government. The DA criticised the local elections; its chairman, Neritan Ceka—dismissed as interior minister in April 1998—has implied that the DA will contest the parliamentary election independently, but expects to join the SPA in a new coalition government. The DA, SDP and UHR accepted Mr Meta's invitation to a roundtable discussion in early December.

However, the chairman of the UHR, Vasil Melo, declined to allocate blame for the two deaths in Bajram Curri on November 28th, and was immediately denounced by Mr Meta, who saw his attitude as incompatible with coalition membership. Although the UHR deputy chairman, secretary-general and members of the party presidency supported the government against Mr Melo, the clash, following UHR complaints over SPA gains at its expense in Vlore and Himare, leaves the UHR's loyalty to the coalition uncertain.

The new local councils start work

The massive transfer of power locally from the DP (which had controlled 80% of local authorities before the elections) allows the SPA little time before the general election in which to ingratiate itself with the electorate. The SPA secretary-general, Gramoz Ruci, quickly convened mayors and commune chairmen in the important Tirana and Durres districts to emphasise the need for patently efficient management. In Tirana Mr Rama has launched an ambitious plan to make the municipal staff "neither socialist nor democrat, but devoted and professional civil servants" within 100 days, and "to restore civic pride among Tirana's 600,000 inhabitants", by cleaning the imposing Italian-period public buildings, and tidying and paving side streets within 300 days.

The new police minister takes over a troubled brief

The new interior minister lost no time in appointing a new general-director of police. Col Bilbil Mema promised improved performance and the introduction of new technology. The north of the country remains a danger zone. In October 41 staff including eight police officers in Tropoje were dismissed for misconduct. On November 1st locals stoned and machine-gunned a rapid reaction force patrol between Bajram Curri and Shoshat when one of the cars broke down, killing a police major. A suspected accomplice of the assassins of Azem Hajdari, the SPA deputy murdered in September 1998, has been arrested: Sali Lushaj had been recruited into Mr Berisha's personal protection unit, the Republican Guard, during the 1997 insurgency and is alleged to have been at

least an eyewitness to the murder. The ministry reported an 8% fall in crime for January-September 2000 compared with the same period of 1996, which is taken as a suitable yardstick because of the collapse in law and order in 1997.

The Zagreb summit is a step towards the EU

The EU's western Balkans summit on November 24th in Zagreb was unexpectedly attended by the new president of the Federal Republic of Yugoslavia, Vojislav Kostunica, whose displacement of Slobodan Milosevic has transformed the prospects for the region. The Albanian delegation took it on itself to be the voice of ethnic Albanians in Kosovo and Macedonia after the Kosovo delegation had been limited to the UNMIK head, Mr Kouchner, and his officials. At the meeting the EU formally committed itself to helping Albania, Bosnia and Hercegovina (BiH), Croatia, Macedonia and Yugoslavia become potential candidates for EU membership. The process requires a stabilisation and association agreement (SAA). For Albania, a high-level steering group has been set up with the EU, which will report before mid-2001 on preparedness for negotiating an SAA. The SPA hopes that negotiations will begin before the parliamentary election.

Under the new Community Assistance for Reconstruction, Democratisation and Stabilisation (CARDS) the five states will benefit from €4.65bn (US\$4.2bn) assistance during the period to 2006, but more funds could be made available if recipients can demonstrate the capacity to use them. Of this, €839m will be on offer to the five states in 2001. An EU mission visited Tirana in December to get concrete proposals for spending on the public infrastructure, judicial reform and institutional consolidation.

The Stability Pact is deepened

A condition of progress towards EU membership is that the south-east European states engage in closer co-operation. The foreign ministers of Albania, Bulgaria, Croatia, BiH, Greece, Macedonia and Turkey, joined for the first time by Yugoslavia, gathered in Istanbul in October for the third regional conference of the Stability Pact for South-eastern Europe (October 2000, page 18), together with the pact co-ordinator, Bodo Hombach, and representatives of the World Bank, European Bank for Reconstruction and Development, European Investment Bank, and UN Development Programme. The Albanian minister for economic co-operation and trade, Ermelinda Meksi, told them that road projects under initial "Quick Start" funding were being satisfactorily implemented, but that Albania needed substantial funding for restructuring its electricity industry (see The domestic economy).

Albania views Yugoslav developments with caution

The Albanian government welcomed the change of government in Yugoslavia in October. Although this has greatly eased tensions, Albania says that it prefers to wait and see if Yugoslavia has really embraced "democratic reform". In November Yugoslavia was readmitted to a regional co-operation forum, the Central European Initiative (it had been excluded in 1992). Mr Milo discussed with his Yugoslav counterpart, Goran Svilanovic, the complete opening of their common frontier, although full formal ambassadorial relations are taking time to be re-established. Mr Kostunica has made clear his view that independence for Kosovo (which Albania supports) or dismantling Macedonia (which has a sizeable Albanian minority) would be dangerous for regional stability.

SPA relations with
Mr Rugova may improve

In December Mr Meta paid the first visit to Kosovo by an Albanian prime minister for 50 years. He met Hashim Thaci, the leader of the Democratic Party of Kosovo, an offshoot of the former Kosovo Liberation Army (KLA), which was supported by the government in Tirana during its guerrilla war with the Yugoslav authorities. Mr Meta also met the head of the Democratic League of Kosovo (LDK), Ibrahim Rugova, who won the October 24th local elections in Kosovo and is Mr Thaci's bitter rival. Mr Rugova has in the past aligned himself with Mr Berisha and the DP, and he may now pay a return visit to Tirana. The SPA and the LDK may be establishing more friendly relations on the understanding that both seem now well established as the parties in power in their respective countries.

Relations with Greece
are rocky

If Albania is to start negotiations with the EU on an SAA before the general election, the government needs the support of its two EU neighbours, Greece and Italy. Both resent the inflow of illegal immigrants (October 2000, page 17), but Greece has the additional irritant of the Albanian treatment of the Greek-speaking, Orthodox Christian minority. By uniting against the UHR in the Himare election, ethnic Albanian parties laid themselves open to charges of repressing a minority. Mr Meta has counterattacked by condemning the UHR and the Greek minority's own party, Omonia, for nationalism.

Southern Epirus is another bilateral problem (1st quarter 2000, page 17). Part of Greece since 1913, it had a substantial Albanian-speaking population, known as Chams, until they were expelled in 1945, allegedly for collaboration with the invading Italians in 1940. An open letter to Mr Solana by the Chameria Association published on November 15th requested that compensation for their abandoned real estate be put on the agenda of the EU's Zagreb summit.

Mr Nano, Mr Meta and Mr Milo attended a conference in Athens on the Albanian question in early December. Mr Nano somewhat eclipsed the others by making the Albanian keynote speech and paying calls on leading Greek politicians and the company Hellenic Petroleum, which has substantial operations in Albania. Mr Meta assured the Greek prime minister, Costas Simitis, that Greek minority problems would be solved. However, the Albanian government probably made a more substantial move towards improving its relations with Greece when it dropped its attempts to force a group of Greek companies (including Hellenic Petroleum) to move out of the fuel depot at Durres port, to clear the way for expanding the port's facilities.

Relations with Italy
are good

Italy's government, as the prime minister, Giuliano Amato, said to Mr Meta in October, appreciates co-operation in reducing illegal trafficking, and testified to increasing normalisation by reopening, after a 60-year closure, the Italian consulate in Shkoder and by rescheduling Albania's debt (see Foreign trade and payments). The Italian ambassador has promised support for Elbasan, where the unemployment and lack of investment is among the worst in Albania.

Economic policy

The IMF renews its positive appraisal

An IMF team came to Tirana in October 2000 to discuss with the Albanian authorities macroeconomic prospects and the preparation of the budget for 2001, notably the proposed fiscal changes. In November it was joined by missions from the World Bank, EU, UN and Organisation for Security and Co-operation in Europe (OSCE) in a two-day conference with Albanian ministers and representatives of non-governmental organisations to evolve a strategy for a new three-year poverty reduction and growth facility (PRGF) covering the period June 2001 to June 2004. The coincidence of the start of a new, much needed PRGF with the parliamentary election means that all negotiations on it and the completion of the current PRGF will be conducted by the present government (assuming that the election takes place no earlier than May or June 2001).

The IMF mission in October went out of its way to commend the government's performance. Riccardo Faini, the IMF executive director for the region, told the prime minister, Ilir Meta: "Of all the countries where similar co-operation programmes with the IMF are being implemented, Albania takes first place for the realisation of the indices as they are envisaged." In the current programme the Albanian authorities agreed to a detailed set of indices and benchmarks to be reached at specified dates (October 2000, page 19). The Albanian president, Rexhep Mejdani, told Mr Faini that he thought that priority should be given in the forthcoming programme to the rural economy and poverty reduction in the depressed north of the country. Mr Meta returned to this topic at the PRGF-2 strategy conference, emphasising that differentials should be reduced between urban and rural areas, and between regions of the country. One in three Albanian households lives on an average of US\$64 a month. However, the IMF criticised Albania for allowing the electricity utility, Korporata Elektroenergjitive Shqiptare (KESH), to operate inefficiently, requiring high imports of electricity to make up the shortfall (see The domestic economy).

The assessment that Albania has entered a period of macroeconomic stability and consistently high GDP growth is confirmed by preliminary data for 2000 (see The domestic economy). The 2001 budget assumes that real GDP will grow by 7.3% to Lk588.4bn (current prices; US\$3.9bn). A significant aspect of macroeconomic stability is that average annual consumer price inflation for 2000 is estimated at about zero, and is forecast within the range of 2-4% in 2001.

The fiscal deficit will rise

In September parliament approved additional government expenditure of Lk4bn: about one-quarter was authorised for public works, mainly improvement of the water supply; more than half was for school rehabilitation and construction, in combination with funds for this purpose given by the Soros Foundation programme; and the rest to subsidise repair and capital works for the electricity industry (in the absence of a World Bank loan; see The domestic economy). Varying official estimates have been given for the 2000 budget outturn, but on one set it would seem that expenditure, allowing for the supplementary Lk4bn, was on target, and that the revenue budget was slightly overfulfilled. The increment in the fiscal deficit (estimated at 9% of GDP) was therefore attributable almost entirely to the supplemental expenditure authorised in September.

The 2001 budget is passed in December

The 2001 budget as passed in parliament on December 19th shows a slight rise in the deficit to Lk54bn (9.1% of GDP), of which Lk27.3bn (4.6% of GDP) would be domestically financed and Lk26.7bn (4.5%) financed externally, compared with 5% of GDP financed domestically for the 2000 budget and 4% externally. Few details are available so far, but budget spending priorities have been reported as infrastructure, education, health and social protection. Infrastructure spending is aimed to encourage the private sector and tourism. Changes in the tax system are intended to favour business. Revenue from taxes and customs is planned to increase by 13% and expenditure by 11%, not including debt-servicing costs, which are projected to fall considerably. Longer-term projections within the new practice of three-year budgeting (July 2000, page 21) have not yet been made public.

Budgets
(Lk m)

	1998	1999	2000		2001
	Actual	Actual	Budget	Estimate	Budget
Revenue	93,515	89,431	122,559	123,600	134,987
Expenditure	141,393	148,818	171,733	175,800	189,022
Balance	-47,878	-59,387	-49,174	-52,200	-54,035

Sources: Ministry of Finance; ATA news agency; EIU calculations.

Public investment is to increase

Part of the rise in outlay in 2001 will be for capital investment. That financed by the budget is planned to increase from Lk15.2bn in 2000 to Lk16.5bn in 2001 (draft budget figures). Most of this increment is attributable to an under-fulfilment of budgeted state investment in 2000, which will now be made up. The budget has provisions favouring private-sector investment, and it is certain that the rise in overall economic activity and the expectations of low inflation, low interest rates and a stable exchange rate will put private investment considerably higher in 2001. This is consistent with the estimates in the draft budget for total foreign investment (direct investment, portfolio and savings), which is forecast at Lk31.5bn in 2001, compared with an estimated Lk20bn in 2000.

The structure of taxation is changing

Tax revenue is projected to rise in 2000 by 28% compared with 1999, largely owing to improved collection. The 2001 budget brings the tax share of GDP up from a modest 16% in 2000 to 22%, closer to the norm for successful transition economies. Within that increase, the mix of taxes is altering. The principal source of tax revenue, value-added tax (VAT)—currently 20%—is buoyant, owing to the introduction of new VAT invoices, which have already greatly reduced tax evasion. The improvement is shown in January-October VAT receipts, which rose from Lk3.9m in 1998 and Lk4.8m in 1999 to Lk6.4m in 2000—24% in excess of the Lk5.2m budgeted for the first ten months of the year. Consideration is being given to differential VAT rates, with lower rates for basic foodstuffs, writing materials and publications. On December 15th parliament approved legislation to reduce from January 1st customs tariffs (from 18% to 15%), the rate of profit tax (from 30% to 25%) and to speed up the reimbursement of VAT for exporters.

The reduction in the rate of profit tax from 30% to 25% from January 1st 2001 was praised by the IMF representative in Tirana, Volker Treichel, at the PRGF-2 strategy conference as likely to stimulate business activity: the incentive for tax avoidance will be reduced and investment encouraged, by leaving more profit to be ploughed back and increasing the net revenue flow from capital. Although in 2000 receipts from the small business tax did not meet the target, the continued rise in the number of small businesses (to 30,000 in 2001, compared with 22,300 at end-1998 and 25,000 in 2000) and new regulations on a form of simplified accounting should bring increased revenue in 2001. In all, 42,000 businesses are registered for tax and a special office was opened in late 2000 to service the 200 largest firms in the interest of prompter payment.

As a consequence of Albania's membership of the World Trade Organisation (WTO), the maximum rate of customs duty is being cut from January 1st 2001 from 18% to 15% (from 5% to 2% for raw materials and machinery and equipment). On the basis of dutiable imports for 2000, the reduction would cost Lk720m, but the budget sets receipts in 2001 13% above that expected for 2000. The difference is partly attributable to an expected growth in trade, especially in materials and equipment charged at very low rates, and to lower avoidance as rates are reduced and corruption is combated.

Monetary policy remains tight

Government policy remains rigorously against monetising the fiscal deficit and in favour of an active borrowing policy. In order to widen the range of lenders, sales of Treasury bills will from the first auction of 2001 be held not only in Tirana but also in Bank of Albania (BoA, the central bank) offices in district capitals. To familiarise provincial lenders with the procedure, the BoA ran a seminar in Gjirokaster in October for the five southern districts of the country. The wealthier south is the better launch-pad than the poorer and still unstable north.

Despite its absorption by government borrowing, money supply on preliminary 2000 data rose by more than targeted: at end-September M3 had already increased by Lk18.85bn, compared with a targeted increment for the full year of Lk16.47bn. The overshooting is largely attributable to increases outside the banking system. Against the overshoot target of a 10% increase in 2000, the BoA has set a goal of an 11.2% increase for that year. As announced in May 2000 (July 2000, page 21), the BoA has lifted its controls on short-term interest rates.

Bids have been invited for a second mobile network

Four companies have been short-listed for a second mobile telephone network, and the winner will be selected by end-January 2001. They are Fintur Holdings (a Finno-Turkish consortium of Sonera and Turkcell); Mobilkom (Austria); Rumeli Telekom Albania (a consortium in which Turkey's Telsim Mobil has a 30% stake); and a consortium of Vodafone with Greece's Panafon. They must submit bids by January 8th and the licence will be given to the highest bidder by end-January.

Small privatisation locally is stalled

Privatisation of smaller enterprises continues, although the new local authorities run by the Socialist Party of Albania (SPA) are pressing for some enterprises owned by the central government to be transferred to local government control. In 2000 in three northern districts (Kukes, Tropoje and Has) 21 objects have been privatised, 28 are in the process of privatisation and 148 have stood unsold for many years.

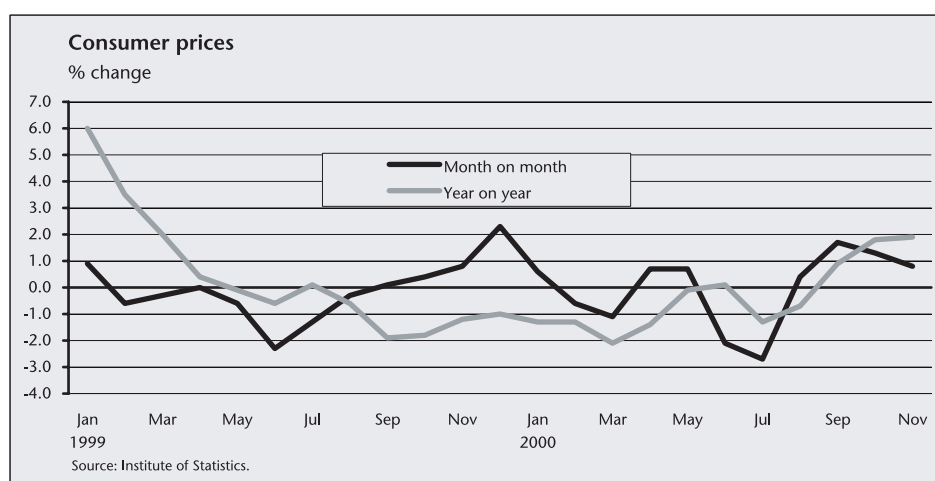
The domestic economy

Economic trends

Growth continues apace Annual real GDP growth, currently between 7% and 8%, is expected to continue to 2002. However, Albania is the second poorest country in Europe, measured by GDP per head, after Moldova, which slipped below it in 1995, and needs as rapid growth as possible. Much of the capacity built under communist industrialisation is now unusable, while some economic activity escapes statistical notice (and hence taxation). Tax reductions and anti-corruption drives are intended to bring these into the open.

Viewed by sector, GDP growth is being driven by high services growth (13%) as the economy restructures, and by agriculture. Farming provides more than half of Albania's output, and is expected to record substantial growth of 4.5% in 2000, not having been harmed by the drought that has hit economies further north in the Balkans. Industrial growth of 7.5% is on a smaller base, and the estimate may in any case prove optimistic, because the year will probably end badly for manufacturing, which is being held back by electricity shortages (and the EIU prefers an estimate for 2000 of 7.5% real GDP growth to the authorities' 7.8% estimate). Construction continues to boom, owing to the upgrading of infrastructure, often foreign-funded under the Stability Pact for South-eastern Europe. Official data do not break GDP down by expenditure, but it may be presumed that private consumption is a major growth factor, fuelled by above-inflation salary increases for public-sector workers in July (July 2000, page 20). Retail trade increased by about 50% in the third quarter of 2000 compared with the year-earlier period, with sales of non-food articles increasing by 221%. Gross fixed investment is also rising, with US\$166m loaned by the banks to public and private enterprises in the first nine months of 2000, US\$156m of it to the private sector. Nearly 30% of the credit has gone to construction companies, 23% to trading firms and 17% to the processing industry.

Consumer prices remain stable Consumer prices are estimated to have remained stable in 2000, with deflation year on year every month between August 1999 and May 2000. This is attributable to tight fiscal and monetary policies, and low levels of employment and imported inflation, as prices have remained low in the EU, Albania's main trading partner. After low inflation of 0.1% in June 2000, deflation returned in July and August. However, inflation was recorded in September, with the index rising by 0.9% year on year, and although annual average inflation is estimated at around 0%, the year-end rate is expected to exceed 2%. An important contributor to the current trend in inflation is energy prices, whose rapid rise since April 2000 has been disguised by other components in the consumer basket; energy prices rose by 24.7% year on year in November. However, thanks to the efforts of the state-run AMRO refining company, petrol prices have stabilised at around Lk80/litre (54 US cents/l) for local brands, or Lk85/l for imported fuel.



Consumer price index, 2000

	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov
Index Dec 1993=100	221.7	220.3	217.9	219.4	220.9	216.3	210.5	211.4	215.0	217.7	219.5
% change											
Month on month	0.6	-0.6	-1.1	0.7	0.7	-2.1	-2.7	0.4	1.7	1.3	0.8
Year on year	-1.3	-1.3	-2.1	-1.4	-0.1	0.1	-1.3	-0.7	0.9	1.8	1.9

Source: Institute of Statistics (Instat).

Unemployment declines Thanks to the expansion of economic activity and to the creation of about 10,000 jobs under a special state programme, registered unemployment fell slightly from 239,847 at end-October 1999 to 219,179 at end-October 2000. A mere 20,833 of these receive unemployment benefit. During October 2000, 1,804 unemployed people found work. We estimate that the unemployment rate is currently around 16.5%, down from an average of 18.2% in 1999.

Unemployment, 2000

(end-period)

	Mar	Jun	Sep
Registered unemployed	241,075	228,214	219,170
Receiving unemployment benefit	21,038	21,850	21,895
Returning to work from register	1,098	1,526	927

Source: Instat.

At the end of the third quarter of 2000 there were 1,066,000 people in employment: 198,000 in the public sector, 761,000 in the rural private sector and 107,000 in the urban private sector. The long-term trend is for employment to fall, from a high point of 1,161,000 in 1994. Many Albanians have sought employment abroad, supporting their families (and the economy) by sending money home.

Manufacturing

Industry experiences an energy shortage

Towards the end of 2000 there was a severe energy shortage, which has affected manufacturing. Hydroelectric stations generate 98% of Albania's electricity production; two years of below-average rainfall have lowered reservoir levels. Water has been flowing into the Drin river (which powers 95% of generation) at its lowest rate for 30 years. However, the problem is not just a short-term one: Albania has not built any new generating capacity for 20 years and demand is soaring as the economy expands. In early December 2000 electricity generation ranged between 8m kwh/day and 10m kwh/d, compared with a wintertime demand of 16m-18m kwh/d. Supply was being rationed to an average of eight hours per day, and industrial users, notably mines, steelworks and cement makers, have had to interrupt production. The obsolete power grid can only accommodate about 5m-6m kwh/d of imported electricity from neighbouring countries. In mid-December it was reported that the water level in the Drin would allow hydroelectricity generation for only three more weeks, unless there was heavy rainfall.

The government has allocated Lk3bn (US\$20m) for energy imports in 2001 (from Croatia and Greece), but the World Bank and the European Bank for Reconstruction and Development (EBRD) have held back funding to the state electricity utility, Korporata Elektroenergjitike Shqiptare (KESh), until it improves its abysmal record in collecting payments for the power that it supplies (at present only 45% of the bills are collected) and reduces losses from unauthorised tapping. KESh presented a short-term action plan at a donors' meeting in Brussels in December hosted by the IMF and World Bank. The company intends to separate generation from distribution, privatise distribution and sack incompetent or corrupt staff. It is will probably take KESh a considerable time both to clamp down on non-payment for electricity, and build up a generating and distributing network that can satisfy Albania's current demand.

Industrial output index, 2000
(Dec 1993=100; public sector)

	Apr	Jun	Aug	Oct
Extracting industry	46.7	34.1	39.5	29.7
Energy extraction	57.0	46.3	46.7	43.0
Non-energy extraction	27.5	16.3	29.0	10.2
Manufacturing	80.5	58.9	96.3	75.1
Refining (oil, coke)	99.9	48.2	111.7	19.9
Non-metallic minerals	n/a	n/a	63.7	91.0
Metallurgy	79.2	83.3	77.8	193.6
Electricity	137.1	131.3	87.9	117.5
Total	94.2	82.6	78.7	81.3

Source: Institute of Statistics (Instat), *Monthly Briefly*.

Data for industrial output require caution

The Institute for Statistics (Instat) publishes regular data on public-sector industrial production in its *Monthly Briefly (Muaji Shkurtimisht)* publication. These suggest that manufacturing is closer to approaching its 1993 output levels than mining, although electricity generation has been performing better

than either. However, as the UN Economic Commission for Europe has pointed out in its latest *Economic Survey of Europe*, Albanian industrial output statistics are not mutually consistent, in particular Instat's monthly, quarterly and annual series.

Agriculture

The agricultural sector is being modernised

Private ownership with secure land titles (the provision of which has been a benchmark of the IMF's poverty reduction and growth facility, PRGF-1) has enhanced productivity. Privatisation, which began in 1991, was due to finish at the end of 2000. Long dependent on human and animal power, and on primitive farming techniques, the Albanian agricultural sector is gradually being modernised. In the first ten months of 2000, US\$45m was invested in agriculture and the agricultural processing industry by foreign and international agencies and the government. Eight olive oil processing plants were built in 2000, partly with the help of a Japanese grant and Italian technology, restoring facilities that were destroyed in the transition from communism.

Infrastructure

The sale of Albanian Mobile Communications (AMC), the cellular phone monopoly, to Telenor-Cosmote in May (July 2000, page 22) has increased AMC's attractiveness to subscribers, the number of which rose by 27% over the course of the third quarter of 2000, from 15,000 to 19,000.

Albanian Railways (HSH) has said that rising fuel prices have turned travellers on to the railways, with more daily passengers in November than in the summer high season. HSH also said that the rail terminal at the port of Durres had encouraged businesses to carry more freight by rail.

Transport statistics, 2000
(^{'000} tonnes unless otherwise indicated)

	Apr	Jun	Aug	Oct
Rail passengers (^{'000})	205	213	241	184
Rail freight	42	59	47	25
Goods landed at ports	214	360	227	225

Source: Institute of Statistics (Instat), *Monthly Briefly*.

Foreign companies building roads in Albania continue to attract criticism (July 2000, page 28; October 2000, page 26). The Socialist Party of Albania newspaper, *Zeri i Popullit*, reported in December that all the road building contractors were behind schedule. In particular, Granit (Macedonia) had finished only 17% of the Korca-Kapshtica road, with only one-third of the allotted time remaining, and the company building the road between Gjirokaster and Kakavija on the Greek border had built only two-fifths of the road, which was due for completion on December 23rd.

Foreign trade and payments

Exports increase in the third quarter

In the third quarter of 2000 exports (fob) increased by 25% in local-currency terms compared with the same period of 1999. In the preceding four quarters exports had decreased year on year; this was therefore the first improvement in export performance since the disruption caused by NATO's air war over Kosovo in the second quarter of 1999. However, imports also increased in July-September 2000 compared with the year-earlier period, by 13%, and the trade deficit (in lek) widened by 9%. As over the same three months the lek depreciated nominally by 7% against the US dollar year on year (and by 8% against the euro), while domestic deflation has continued at around -0.4%, Albanian exports have gained in competitiveness, and in US dollar terms the trade deficit has narrowed.

In the first nine months of 2000 exports increased by 1.8% compared with the same period of 1999 in local-currency terms, while imports decreased by 13.2%; the trade deficit fell by 17.5%, but it is still considerable at Lk79bn (US\$540m). Albania's foreign trade was distorted in 1999 by the need for extra imports to supply the refugees from the fighting in Kosovo. The deficit in the trade in goods is structural and will only slowly be reduced. Albania is forced to import many of the goods that it needs because of the inadequacies of its own production. The cement industry provides an example: under communism it satisfied local demand with 850,000 tonnes produced annually, until the industry collapsed in the early 1990s. Now that an Anglo-Lebanese company has taken over the Fushe-Kruja cement plant (July 2000, page 26), the local industry may be able to produce 45% of Albania's needs, reducing imports of cement for the booming construction industry.

Trade in goods (Lk m)

	1999				2000		
	1 Qtr	2 Qtr	3 Qtr	4 Qtr	1 Qtr	2 Qtr	3 Qtr
Exports fob	9,259	10,964	7,354	8,793	8,918	9,949	9,205
Imports cif	-26,908	-62,669	-33,824	-34,023	-31,622	-37,410	-38,071
Balance	-17,649	-51,705	-26,470	-25,230	-22,702	-27,460	-28,866

Sources: IMF, *International Financial Statistics*; Institute of Statistics (Instat), *Situation of Foreign Trade*.

Processing for abroad is the main export earner

A major export category, textiles and footwear (contributing 61% of all exports), increased substantially, by 31% in July-September 2000 compared with the year-earlier period, when Albanian industry was still feeling the ill effects for the whole region of the Kosovo war. Albania's processing industry, in which cheap local labour is used to work on finishing off clothing and footwear for west European companies, continues to prop up its trading position (re-exports make up as much as two-thirds of total exports). A fast growing export category, construction materials, provided 9.1% of exports. Presumably many of these materials went over the Yugoslav border to supply the building boom in Kosovo; however, since Yugoslavia does not appear among Albania's leading ten trading partners in the statistics published by the

Institute of Statistics (Instat), this cannot be confirmed. The performance of agricultural exporters (14.4% of the total) was less impressive, growing by just 2% year on year. Of imports, 22% were food, beverages and tobacco; imports of this category rose by 21% year on year, largely in the form of processed food and drinks, foreign brands of which have penetrated the Albanian market, drawn in by growing consumer demand. Machinery made up another 20% of imports; these increased by 9% compared with July-September 1999, suggesting that the re-equipment of Albanian industry is continuing.

Trade by commodities, 3 Qtr 2000

(Lk m unless otherwise indicated)

	Exports	% change ^a	Imports	% change ^a
Textiles & footwear	5,647	31	5,228	28
Machinery & equipment	214	-9	7,541	9
Foodstuffs, beverages & tobacco	1,290	2	8,251	21
Mineral products	207	42	5,316	104
Chemicals	93	155	3,560	37
Building materials	811	265	4,728	46

^a Year on year.

Source: Instat, *Situation of Foreign Trade*.

EU remains main trading partner

In the third quarter of 2000 trade with EU countries made up 93% of Albania's exports and 75% of its imports; in the same quarter of 1999 the respective figures were 91% and 81%, suggesting that Albania's import structure has since diversified slightly away from the EU, particularly in its imports. Turkey and Bulgaria, among non-EU countries, have increased their share of imports into Albania, by 32% and 35% respectively. Nevertheless, exports to Italy (in local-currency terms) have increased by 71% since July-September 1999, representing the re-establishment of links with Italian companies using Albanian subcontractors to finish off textiles and footwear.

Main trading partners, 3 Qtr 2000

	Lk '000	% change ^a
Exports		
Italy	6,040,519	71
Greece	1,496,677	-23
Germany	710,113	43
Macedonia	124,266	-33
France	101,848	63
Imports		
Italy	13,530,479	25
Greece	10,711,542	25
Turkey	2,185,796	32
Germany	1,675,844	12
Bulgaria	1,175,063	35

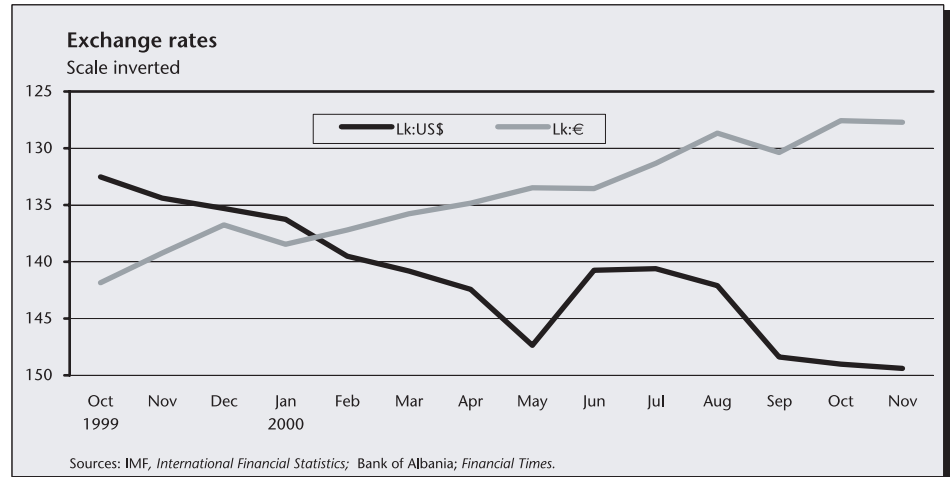
^a Year on year.

Source: Instat, *Situation of Foreign Trade*.

	<p>The possibilities of expanding trade between Albania and Slovenia were explored at a meeting of the chamber of commerce and industry in Maribor in early December. Slovenian companies are hoping to expand business links with Albania, hampered in the past by Albania's isolation and technological backwardness. Slovene exports to Albania, estimated at US\$4.4m in 2000, include medicines and paper products, while Albanian exports to Slovenia, worth about US\$1m, are mostly iron alloys, agricultural goods and steel fabrications. A free-trade agreement is being negotiated with Macedonia, which is an important destination for Albanian exports.</p>
<p>EU opens up to Albanian exports</p>	<p>In September the EU's General System of Preferences was altered for Albania and other western Balkan states, for industrial and agricultural exports: many industrial products may enter the EU duty free, and exports of the agriculture and fisheries sector will be eased. In 2001-02 the proportion of Albanian products entering the EU without paying duty rises to 95% from 80%. The reopening of economic links with Yugoslavia will not only increase regional trade with that country, but also facilitate transport for Albanian trade with central Europe.</p>
<p>Transfers should prop up the current account</p>	<p>Few, if any, data on the current account have appeared since the previous quarter (October 2000, page 27). Such evidence as there is suggests that unrequited transfers from emigrants and the Albanian diaspora have continued to pour in, and are expected to exceed a previous estimate for 2000 of US\$450m. The current account usually depends heavily on the current transfers balance, which in 1998 contributed US\$500m, going a long way to make up for the trade deficit of US\$600m.</p>
<p>Foreign investment greatly increases</p>	<p>Foreign investors were deterred by the insurgency and looting of 1997 and the riotous political rallies and lawlessness that persisted afterwards. Foreign direct investment (FDI) dropped from US\$97m in 1996 to an average of US\$46m in 1997-99. Vituperative rallies and occasional acts of violence persist but the stability of the economy has begun to attract foreign investors. By 2000 FDI had reached US\$92m and the finance minister, Anastas Angjeli, has said that he expects it to be 20% higher in 2001, at about US\$110m. The successful privatisations of the mobile phone company, Albanian Mobile Communications (AMC), and the National Commercial Bank have brought in restructuring capital, and the same consequences will follow the continuing programme of state disposals.</p>
<p>Some debt is reduced</p>	<p>Moves continue to reduce Albania's foreign debt, put by one recent estimate at about US\$725m (19% of GDP). In November an agreement was signed to reschedule US\$1.9m of bilateral debt incurred from Italy in 1992-96, in the context of the Paris Club agreement of July 1998. In December US\$9.3m in unpaid interest on US\$17.6m owed to Turkey was remitted. Albania's debt to China was discussed during the visit of the Chinese foreign minister, Tang Jiaxuan, in early December. The two sides have yet to agree how large the debt is, and whether it is still due from the communist period or only since the early 1990s, as diplomatic relations with China were broken off by the Hoxha regime in the 1970s. Mr Tang also confirmed China's interest in building a hydropower station at Bushat in northern Albania.</p>

The lek falls slightly against the US dollar

With low domestic inflation and external reserves nearly at the same levels as a year earlier, the lek has been able to avoid a large fall in value, being propped up by substantial inflows of foreign currency from transfers, foreign grants and (more recently) foreign investment. By December 15th 2000, at Lk146.10:US\$1, the lek had depreciated nominally against the buoyant US dollar by 7% since January (while appreciating against the troubled euro by 6%). At the year-end, however, the lek strengthened against the US dollar, to Lk142.75:US\$1 on December 29th, as migrant workers returning for the holidays drove up demand for the local currency, and as the euro appreciated against the US dollar. Foreign-exchange reserves are sufficient to inspire confidence, at about 3.8 months of import cover.



Exchange rates
(av)

	1999 Dec	2000 Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov
Lk:US\$	135.31	136.62	139.52	140.81	142.44	147.37	140.75	140.60	143.58	148.38	149.01	149.39
Lk:€	136.76	138.27	137.21	135.85	134.81	133.47	133.84	132.16	129.88	130.38	127.56	127.70

Sources: IMF, *International Financial Statistics*; Bank of Albania; *Financial Times*.