



Foreign Direct Investment Report

Albania 2010



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ALBANIA

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NOTE

The terms country/economy as used in this report also refer, as appropriate, to territories or areas. The major country groupings used in this *Report* follow the classification of the United Nations Statistical Office. These are:

Developed countries: the member countries of the OECD (other than Chile, Mexico, the Republic of Korea and Turkey), plus the new European Union member countries which are not OECD members (Bulgaria, Cyprus, Estonia, Latvia, Lithuania, Malta, Romania and Slovenia), plus Andorra, Israel, Liechtenstein, Monaco and San Marino.

Transition economies: South-East Europe and the Commonwealth of Independent States.

Developing economies: in general all economies not specified above. For statistical purposes, the data for China do not include those for Hong Kong Special Administrative Region (Hong Kong SAR), Macao Special Administrative Region (Macao SAR) and Taiwan Province of China.

The following symbols have been used in the tables:

- Two dots (..) indicate that data are not available or are not separately reported. Rows in tables have been omitted in those cases where no data are available for any of the elements in the row;
- A dash (–) indicates that the item is equal to zero or its value is negligible;
- A blank in a table indicates that the item is not applicable, unless otherwise indicated;
- A slash (/) between dates representing years, e.g., 1994/95, indicates a financial year;
- Use of an en dash (–) between dates representing years, e.g., 1994–1995, signifies the full period involved, including the beginning and end years;
- Reference to “dollars” (\$) means United States dollars, unless otherwise indicated;
- Annual rates of growth or change, unless otherwise stated, refer to annual compound rates;

Details and percentages in tables do not necessarily add to totals because of rounding.

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EXECUTIVE SUMMARY

- Foreign direct investment (FDI) flows to Albania have grown significantly in recent years, rising from €258 million in 2006 to €705 million in 2009. They have developed independently of global and regional trends during the financial and economic crisis, showing a continuous increase extending into 2009.
- The increase in FDI inflows to Albania may, however, be difficult to sustain in 2010, due to unfavorable international economic conditions and sluggish outward investment from some of the main home countries of transnational corporations (TNCs) investing in Albania.
- Albania is ranked in the 25th place among 141 countries according to UNCTAD's FDI performance index for 2009, representing a rapid improvement from the country's position of 80th place in 2006. The improved position is partly the result of rapid increase of FDI flows to the country, much of it in response to improved business environment and opportunities opened up by privatization of state-owned enterprises.
- FDI inflows amounted to one fifth or more of the value of gross domestic capital formation in Albania and financed nearly half of the country's current account deficit in 2008-2009.
- Manufacturing accounts for a relatively low share of FDI in Albania, with less than one fifth of the FDI stock in 2008. Services receive the dominant share; transport, communication and storage services accounted for 23% and financial services for one third of the FDI stock in 2008.
- Foreign affiliates play an important role in the Albanian economy in terms of investment activity, value added, production, and employment. INSTAT survey data for 2008 indicate that majority-foreign-owned enterprises accounted for 41% of total investment, 39% of total value added, 27% of total turnover, and 16% of total employment.
- The degree of foreign-affiliate participation in the Albanian economy is similar to that in the Central European countries such as the Czech Republic, Estonia and Slovakia which are among those with the highest indicators of such participation in Europe. High foreign participation indicates favorable conditions for FDI in several industries in the country, but is also a sign of weaknesses in the domestically-owned part of the economy, including an underdeveloped local SME sector.
- Foreign affiliates in Albania are distributed unevenly across the economy. Although they drive some industrialization in the country, their involvement in activities with higher technologies is limited.
- The labour productivity gap between foreign affiliates and domestic companies in the country is relatively small in the manufacturing industries, pointing to a relatively low technological level of foreign affiliates which may in part reflect constraints with respect to the availability of adequately skilled workers.

- The entry of foreign investors on a significant scale into the financial and telecommunication services has increased the scope and efficiency of those services.
- Albania has adopted a policy framework favorable for FDI since 1993, and has more recently introduced policies to support private sector development in general. Measures are also under way for further improvements in the business environment, including, among others, a reform of the agency in charge of investment promotion.
- In a survey of foreign affiliates conducted for this report, foreign investors give a positive overall assessment of the appropriateness of economic policies and various legislative measures such as those relating to taxation, employment, and the environment. Dissatisfaction is expressed, however, with government support programmes. The biggest problem identified is that more than half of the investors do not find people with the adequate skills. Investors also call for steps to improve the implementation of laws, tax collection, VAT reimbursement and a reduction of bureaucracy.

INTRODUCTION

Rapid economic development and heading towards EU accession are high on the agenda of the Albanian Government. The country's main policies have targeted the liberalization of the economic framework, improving conditions for doing business and for attracting foreign direct investment (FDI), as an important objective. Thanks to progress in economic transformation and a supportive external environment, economic growth was robust between 2000 and 2009. Albania achieved an average annual GDP growth of 6% in this period. Still, per capita GDP at purchasing power parity is only 25% of the EU-27 average, less than of Bulgaria - the lowest-income EU member state.¹ Thus the room for catching up is wide and the potential role of FDI in transferring capital and technology invaluable.

Albania is a small country with only 3.2 million inhabitants, but among the countries of South-East Europe² its economy is in the medium range in terms of GDP. Its nominal GDP in 2009 at the prevailing exchange rate was €9 billion, three times more than that of Montenegro and 50% more than of the former Yugoslav Republic of Macedonia, but only one quarter of Croatia's. Size matters, just like the level of development and geographic position when it comes to attracting FDI. Small countries usually fall short in attracting large multinationals and industries producing for export markets of a mass scale. While this limits the extent to which it can compete with larger, low-cost host countries in attracting export-oriented FDI from a range of sources, Albania, with its cheap and motivated workforce, has good potential to become a production and services hub for exports to Italy and Greece which are the main markets in the neighbourhood.

In 2009 the Albanian economy had a fairly robust growth of 3.3% despite the financial crisis and economic downturn in the rest of Europe and associated decline in Albanian exports and remittances. The impact of the international financial and economic crisis on Albania was mitigated by the limited importance of the export channel to transmit the crisis to the country, and by Albania's relatively modest reliance on the international financial markets. The monetary policy framework, careful banking supervision and the flexible exchange rate also had stabilizing effects. Foreign financial imbalances did not curtail growth because the financing of a huge and increasing current account deficit could to a large extent be achieved by growing FDI inflows from privatization. Due to the positive effects of privatization and FDI, the supply and quality of utility services also improved, providing a stimulus to economic activity.

The economic growth is expected to continue in 2010. The growth forecast for 2010 as a whole is in the range of 3.0% (EBRD, 2010a). Sluggish economic growth is expected to go hand in hand with a slow-down of FDI inflows. This corresponds to the trend observed in all other countries in the region³ and also reflects the limited investment activity of European TNCs (the most important investors in South-East European countries).

Under the given challenging circumstances it is all the more important that the Government of Albania has embarked on an economic policy path, including, among others, a strong emphasis on the training of workers, that is supportive of private sector development and international investment in the country. With respect to the latter, the aim is to attract more Greenfield FDI, and FDI in industries producing for exports, those improving the

¹ "GDP per inhabitant varied by one to six across the EU27 Member States" *Eurostat Newsrelease* 94/2009.

² South-East Europe includes Albania, Bosnia and Herzegovina, Croatia, Serbia, Montenegro and the former Yugoslav Republic of Macedonia.

³ Gábor Hunya (2010).

economic infrastructure and those contributing to an increase in the technology level in the country.

In the chapters that follow, this report first examines the experience of Albania with FDI, focusing on trends in FDI flows to the country, the importance of FDI flows for the country's balance of payments, main features and patterns of inward FDI and the relative importance of foreign affiliates activities in the Albanian economy. It goes on to consider the role and impact of FDI in services in the economy. Finally, it reviews the regulatory and business environment for FDI in the country and outlines policy options and measures that could contribute to the efforts of the Government to develop a more effective and targeted FDI policy.

CHAPTER I. FDI IN ALBANIA: TRENDS, MAIN FEATURES AND ROLE IN THE ECONOMY

A. FDI in Albania in the global context.

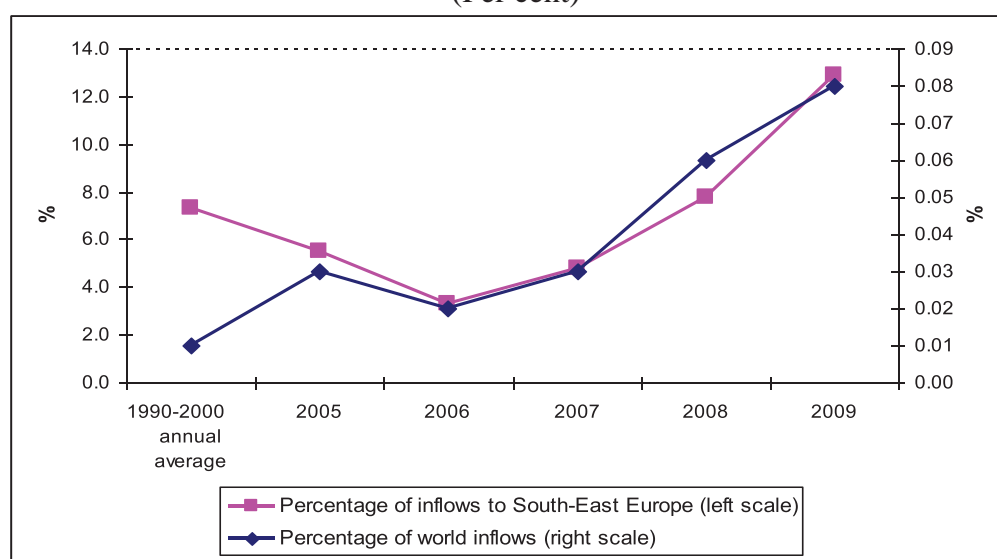
Global FDI inflows doubled in the 2005-2007 period (in nominal terms) but fell back to the 2005 level of €802 billion (\$1.1 trillion) in 2009 (table I.1). Inflows to South-East Europe followed the global trend, peaking in 2007. FDI flows to Albania during the period, however, developed mostly independently of the global and regional trends showing a continuous increase, extending beyond 2009 (table I.1). In dollar terms, however, FDI inflows to Albania declined slightly, due to the appreciation of dollar with respect to the euro and the Albanian Lek.

Table I.1. FDI inflows: world, South-East Europe and Albania (Millions of euro)					
Host economies	2005	2006	2007	2008	2009
World	782 673	1 164 682	1 534 682	1 208 931	802 041
South-East Europe	3 870	7 885	9 384	8 663	5 446
Albania	212	258	484	674	705

Source: UNCTAD, *WIR10*.

The share of FDI inflows to Albania in the world total remains marginal, at 0.1% in 2009, even though it grew to ten times its share in 2000 (figure I.1). The country's weight as a host to FDI in the South-East European region has, however, grown remarkably since 2006, especially since 2007, when inflows to the South-East Europe decreased while flows to Albania kept growing (table I.1, figure I.1).

Figure I.1. Shares of Albania in FDI inflows to South-East Europe and the world
(Per cent)



Source: UNCTAD, FDI/TNC database (www.unctad.org/fdistatistics).

Table 1.2. Albania's ranking according the Inward FDI Performance Index and the Inward FDI Potential Index, selected years

	1995	2000	2005	2006	2007	2008	2009
Inward FDI Performance Index	40	58	67	80	53	35	25
Inward FDI Potential Index	112	101	82	83	82	79	.. ^a

Source: UNCTAD, *WIR10*, annex tables.

^a The latest year for which data is available for some variables included in the Inward FDI Potential Index is 2008

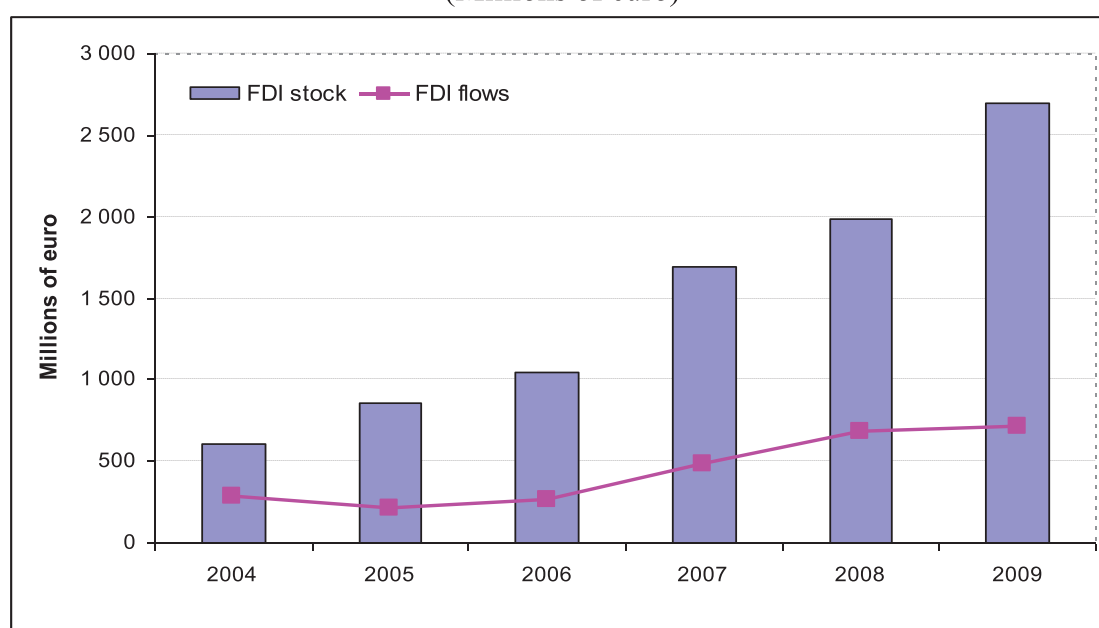
Albania ranks relatively high in the global ranking based on UNCTAD's Inward FDI Performance Index which measures the relative size of FDI inflows that the country receives in the light of its size of economy, calculated as a country's share in global FDI flows divided by its share in global GDP. The latest ranking by this indicator (for the year 2009) placed Albania in the 25th place among 141 countries (table 1.2). This represents a rapid improvement from the country's position of 80th place in 2006 (table 1.2). Five years ago Albania was ranked next to Poland, now it is next to Chile which has one of the most FDI-oriented economies in the world (UNCTAD, *WIR06* and *WIR10*). The improved position is partly the result of rapid increase of FDI flows to the country, much of it in response to improved business environment and opportunities opened up by privatization of state-owned enterprises.

The FDI Performance Index ranking achieved by Albania is better than the country's rank by the Inward FDI Potential Index, according to which Albania ranked 79th in 2008 (the most recent year for which data are available), far behind other European countries (ranking by the FDI Performance Index for the same year is 35). The Inward FDI Potential Index is based on 12 indicators including among others the level of development in general and of infrastructure in particular (UNCTAD, *WIR02*). The discrepancy between performance and potential denotes that despite poor infrastructure, energy shortfalls and modest research and development activity, there have been investment opportunities encouraging FDI flows to Albania after the country opened up in full to foreign investments. But the country has needed improvements in its FDI potential before more FDI, especially Greenfield investments in the various production sectors could be attracted. As pointed out in the policy section of this report, there has been rapid development lately in Albania exactly in those fields of infrastructure, such as energy supply and roads which had been identified as bottlenecks in international comparisons. Foreign companies have acquired concessions to develop these areas and are improving the conditions for further investments in other sectors.

B. FDI flows and their importance for Albania's investment and balance of payments

FDI inflows to Albania were relatively low and grew slowly before 2006. Since that year, they have shown a continuous increase in nominal euro terms.⁴ The most significant increases occurred in 2007 and 2008. In 2009, the increase was moderate but nevertheless made the country a unique case among European countries, most of which suffered serious setbacks in their inward FDI inflows in the wake of the financial crisis. As noted, although the nominal amount of FDI to Albania is of modest magnitude due to the small size and relative backwardness of the country, relative to the level of development it is rather significant.

Figure I.2. Inward FDI in Albania, 2004-2009
(Millions of euro)



Source: UNCTAD, FDI/TNC database (www.unctad.org/fdistatistics) based on data obtained from the Bank of Albania.

The size of inflows as a percentage of gross fixed capital formation (GFCF) provides a rough indicator of the size of FDI inflows relative to total investment in the economy (table I.3).⁵ This indicator increased from less than 10% in 2005 to over 19% in 2008 and nearly 23% in 2009. Among countries of the region, only Montenegro have attracted much more FDI relative to GFCF, both due to relatively higher amounts of FDI inflows and to lower amounts spent on fixed capital formation. In Albania, the ratio of GFCF to GDP was 41% in 2008, much higher than in other countries of the region. Having such a high investment rate is supportive to economic growth especially as much of the investments have gone into infrastructure facilitating business investments including FDI.

⁴ Flow data reported by the Bank of Albania (BoA) in the balance of payments are obtained from the banking system's monthly reports and direct reporting from a limited number of companies. Stock data come from company surveys conducted annually in the period 2006-2008. All data are reported in euro.

⁵ FDI does not necessarily constitute gross fixed capital formation as the compilation of the two data sets follow different methodology. Among other items, cross-border M&A investments are part of FDI but do not comprise new investments as long as they acquire existing shares.

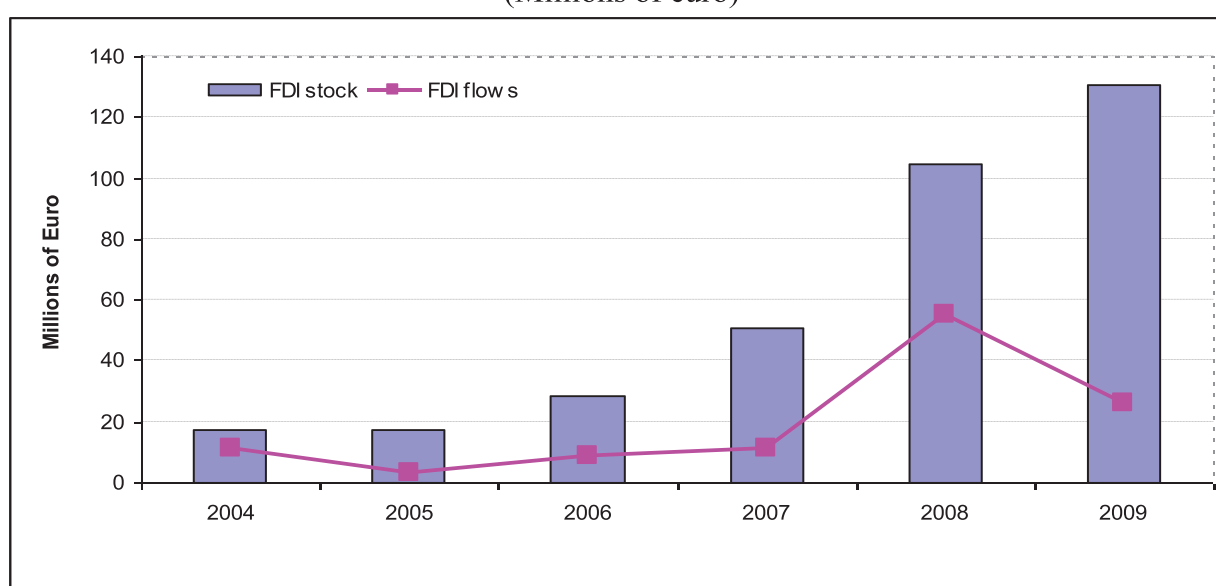
Table I.3. FDI inflows as a percentage of gross fixed capital formation, South-East European countries, 2004-2009

Region/country	2004	2005	2006	2007	2008	2009
South-East Europe	17	21	37	36	29	22
Albania	13	9	10	17	19	23
Bosnia and Herzegovina	27	20	25	46	22	14
Croatia	12	17	27	33	32	17
Montenegro	18	118	105	78	53	177
Serbia	21	33	71	37	26	22
The FYR of Macedonia	34	10	37	44	28	13

Source: UNCTAD, *WIR10*, annex tables.

The relatively high FDI inflows to Albania seen in 2007-2009 may not be sustainable in 2010 due to less favourable international conditions. FDI outflows from major countries investing in Albania, like Italy and Greece have declined in recent years. Further sluggish outward investment activities from the most active investing countries may lead to less FDI in Albania in the future. The relative success of Albania in attracting FDI in 2007-2009, if observed in the context of declining outward investments from the main home countries of FDI, suggest that many investors were attracted by special and largely one-time opportunities. As explained in a subsequent section, it was mainly the privatization of utility companies which attracted those investments. Such opportunities usually cause a peak in FDI in specific years and inflows usually subside in subsequent years if no new opportunities emerge.

FDI inflows have also been important for Albania's balance of payments. Outflows of FDI from Albania that is investments abroad by Albanian firms – almost all of them to neighbouring economies, especially Kosovo and the former Yugoslav Republic of Macedonia - are modest, only about 6% of the FDI inflows in 2007-2009 (figure I.3).

Figure I.3. Outward FDI from Albania, 2004-2009
(Millions of euro)

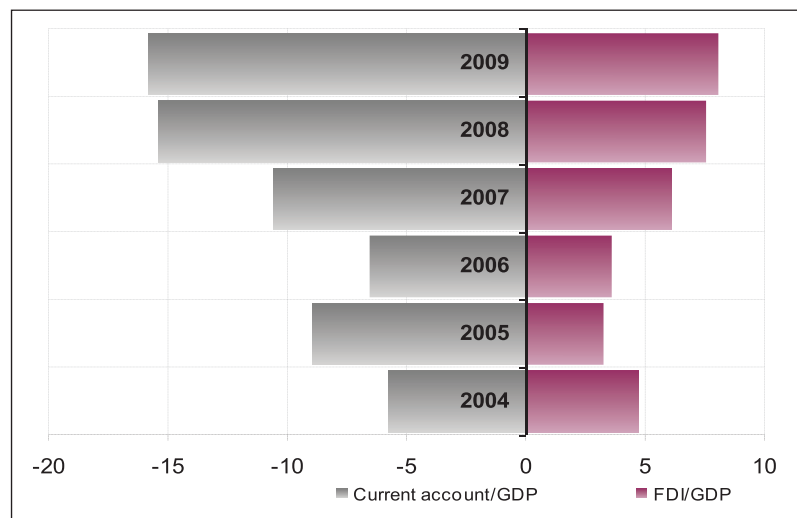
Source: UNCTAD, FDI/TNC database (www.unctad.org/fdistatistics) based on the Bank of Albania

The net balance of FDI inflows and outflows is thus positive. It has financed about half of the country's current account deficit in the years 2006-2009 (table I.4 and figure I.4), significantly more than in previous years. This is all the more important as the current account deficit grew three times between 2006 and 2008. Although the current account deficit shrank modestly in 2009, it still reached 15% of GDP (table I.4) which is one of the highest in Europe.

The current account deficit of Albania has been produced mainly by a foreign trade deficit (table I.4). Surging imports were a consequence of increasing private consumption and investments. Export capacities have remained very weak; the share of exports of goods in Albania's GDP, at around 10%, is one of the lowest in Europe. At the same time, the services balance has turned increasingly positive. On the whole, Albania exports by far more services than goods, a situation which is not a rarity with Mediterranean countries including Greece and Croatia, in which tourism has a higher share in GDP than manufacturing and the international competitiveness of the services sector is superior to that of the manufacturing sector. This situation is a result of historical developments and of natural conditions and cannot be directly linked to the effects of FDI, but it is in line with the distribution of FDI by economic activities in which, thus far, manufacturing has a relatively weak position and services a rather strong one. It also points, however, to the potential for FDI in manufacturing by foreign investors with competitive advantages in the sector.

Table I.4. External sector indicators, nominal and as a percentage of GDP (Millions of euro and per cent)					
Balance of Payment items	2005	2006	2007	2008	2009
Current account	- 589	- 471	- 831	- 1 370	- 1 327
<i>in % of GDP</i>	- 9	- 7	- 11	- 16	- 15
Exports of goods	530	631	786	917	751
<i>in % of GDP</i>	8	9	10	10	9
Balance on goods	- 1 477	- 1 659	- 2 104	- 2 431	- 2 304
<i>in % of GDP</i>	- 23	- 23	- 27	- 27	- 27
Exports of services	967	1 157	1 415	1 688	1 718
<i>in % of GDP</i>	15	16	18	19	20
Balance of services	- 140	- 32	13	69	121
<i>in % of GDP</i>	2.1	0.4	0.2	0.8	1.4
FDI inflows	213	259	481	675	698
<i>in % of GDP</i>	3	4	6	8	8
FDI outflows	- 2	- 8	- 11	- 63	- 34
Balance on FDI (inflows-outflows)	211	251	470	612	664
<i>in % of the current account deficit</i>	36	53	57	45	50

Source: Based on data obtained from the Bank of Albania for BoP data, INSTAT for GDP 2005-2008 and Ministry of Finance for 2009.

Figure I.4 Albania: Current account deficit and FDI relative to GDP, 2004-2009

Source: Based on data provided by the Bank of Albania

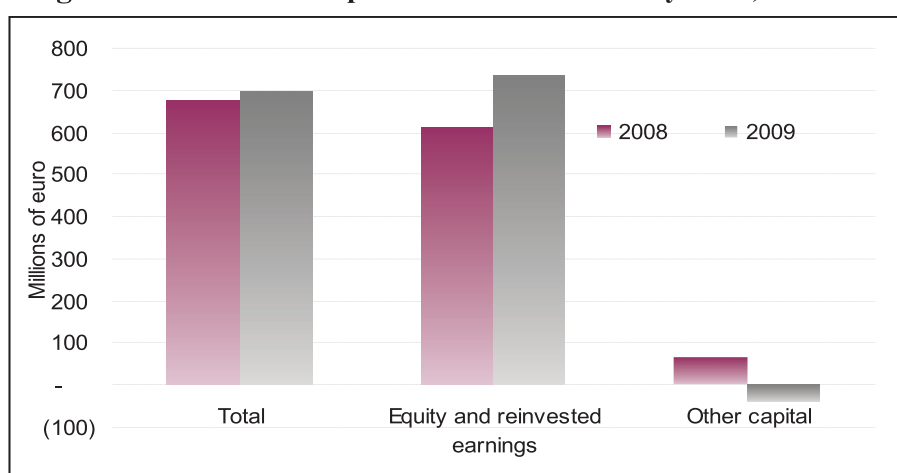
The type of FDI Albania has received so far, concentrated primarily in the production of services for the domestic market (section I.D.2 and chapter II) generating more imports than exports, which could contribute to a current account deficit in the absence of surpluses in other parts of that account. As FDI matures in a country, investors tend to earn more income which is recorded as an outflow on the current account and increases deficits. Other items like goods- and services-trade related surpluses have to counterbalance them. From a balance-of-payments perspective, it would be advantageous for Albania to attract more FDI which generates exports of goods and services in addition to that serving the domestic market.

C. Structural characteristics of FDI inflows

1. FDI by form

Most of the FDI inflows to Albania are in the form of equity capital, which accounts for some 70% of the total. Reinvested earnings constitute a smaller albeit rising share, while other capital (mostly intra-company loans) is almost negligible (figure I.5. and table I.5). This composition of FDI is a characteristic of countries at an early stage of receiving FDI; in more mature host countries the importance of other capital is usually larger. Given that most of the investment projects in Albania are new, a number of investors are bringing new equity into the country.

Figure I.5 Albania: composition of FDI inflows by form, 2008-2009



Source: Based on data provided by the Bank of Albania

Table I.5 Albania: Composition of annual and quarterly FDI inflows, 2008-2009 (Millions of Euro)										
FDI composition	Q1-08	Q2-08	Q3-08	Q4-08	2008	Q1-09	Q2-09	Q3-09	Q4-09	2009
FDI inflow	87	133	216	239	675	123	307	156	112	698
Equity capital	23	60	142	217	442	65	254	110	87	516
Reinvested earnings	52	77	47	- 5	171	51	42	57	72	222
Other capital	12	- 3	27	27	63	7	11	- 11	- 47	- 40

Source: UNCTAD FDI/TNC database (www.unctad.org/fdistatistics) based on the Bank of Albania

Reinvested earnings represent a growing component in the year-to-year increase of FDI in Albania. For 2009, they are estimated at €222 million, €50 million more than in 2008. The positive trend indicates the profitability of FDI in the country and the investors' decision to plough back profits into their enterprises in the country. The income of the foreign investors in Albania amounted to €186 million in 2008 which corresponds to 9% of the FDI stock (table I.6). This is a good rate of profit for the investors, the highest among the South-East European countries. Among countries of South-East Europe and the new EU member countries of Central and Eastern Europe, it is surpassed only by Hungary, the Czech Republic and Estonia, all of which have mature FDI projects which usually have higher income-generating capacities than new projects. Of the FDI-related income generated in Albania, 92% was reinvested in 2008. This is a very high share in international comparison and is another characteristic of the behaviour of investors in the early, build-up stage of investment projects.

Table I.6. Albania: Income payments on inward FDI, and reinvested earnings, 2008
(Millions of Euro and per cent)

Outflows (debit)	2008
Direct investment income	186
repatriated income on equity	9
reinvested earnings	171
income on debt	6
FDI stock (inward)	1,986
FDI related income payments as a percentage of FDI inward stock	9%
Reinvested earnings as a percentage of FDI income payments	92%

Source: Based on data provided by the Bank of Albania

Intra-company loans generally show large year-to-year fluctuations and not only in Albania. The inflow of loans to foreign affiliates in Albania was negative for the first time in 2009, to the extent of some €40 million. The reasons are not clear, but the experience is similar to that in several other countries in the region in the wake of the financial crisis. One explanation can be that foreign banks and other investors withdrew some loans that they had provided earlier. In some cases the better-off affiliates in the host country may have even extended credit to their parent companies which may have been more severely affected by the financial crisis. In 2008, foreign investment enterprises in the telecommunications sector were active in offering direct loans to their investors (for example Albanian Mobile Telecommunications provided loans to its parent company).

2. FDI by mode of entry and economic activity

Equity investments enter a country in the form of greenfield investments or cross border mergers and acquisitions (M&As). Based on data compiled by UNCTAD (box I.1) during 2003-2009, the largest number of greenfield projects (nine) were initiated in financial services (table I.7). Seven projects were initiated in each of the following industries: food, tobacco, beverages; coal, oil and natural gas, and building and construction materials. In category “business activity”, 44.5% of the projects were in extraction, industry and construction, with more than a quarter of them in the manufacturing industries. The rest (55.5%) were in services likes retails (including financial services), trade and business services. Among the investing companies the Albanian-American Fund for Enterprises from the United States is the top company with five announced investment projects. The second is the Italian food-store co-operative Conad. The top ten companies accounted for 35% of the investment projects.

Box I.1. Definitions and sources of the data on greenfield projects

Data on greenfield investment projects used in this study are based on the information compiled by UNCTAD based on data from fDi markets of the Financial Times Ltd. fDi Markets tracks all new investment projects and expansion of existing investments but without information on the equity participation by investors. While there is no minimum size for a project to be included, as a selection criteria for inclusion in this database an investment project has to create new direct jobs and capital investment. Information sources to collate and validate those projects include Financial Times newswires, nearly 9,000 media sources, project data received from over 1,000 industry organizations and investment agencies, and data purchased from market research and publication companies. The data are cross-referenced against multiple sources and over 90% of them are validated with company sources. As far the industry classification is concerned every FDI project tracked by fDi Markets is classified according to its cluster, sector, and business activity, based on a proprietary industry classification system. As the value of the projects is not available in most of the cases, the data compiled by UNCTAD and presented in its World Investment Reports so far relate only to the number of cases recorded.

Source: UNCTAD, *WIR10*

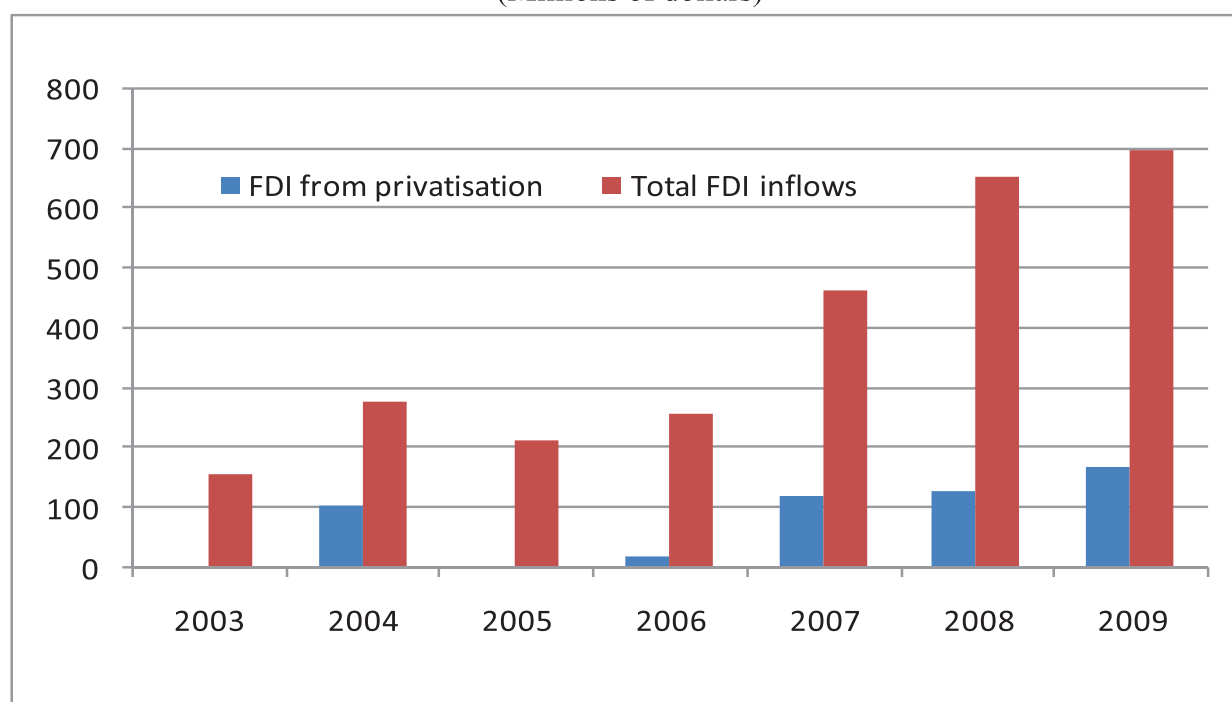
Table I.7. Greenfield FDI in Albania: main investing companies, 2003-2009
(Number of the announced projects)

Company	Home country	2003	2004	2005	2006	2007	2008	2009
Albanian-American Fund for Enterprises	United States	1	1	2	1			
Conad	Italy				3		1	
Kurum	Turkey	1		1			1	
Rompetrol	Romania / Netherlands			1	1			
Titan Cement	Greece				1		1	
La Petrolifera Italo-Rumena (PIR)	Italy			1		1		
ProCredit Holding	Germany			1	1			
Moncada Costruzioni (Moncada Energy Group)	Italy						2	
Fresh Property	United Kingdom						2	
Ber Oner	Turkey	1						
Other companies		6	6	7	4	7	9	7
Overall total		9	7	13	11	8	16	7

Source: UNCTAD FDI/TNC database (www.unctad.org/fdistatitics) based on fDi markets from Financial Times Ltd.

FDI entry through cross-border M&As in a transition economy like Albania usually occurs through privatization of state-owned enterprises. There has been a considerable inflow of FDI to Albania through the privatization process, involving both privatizations of small and medium-sized enterprises (SMEs) in a number of industries, and the privatization of large enterprises in strategic industries (such as banking, telecommunications and energy), that have attracted participation by transnational corporations (TNCs). It is mainly the privatization of the strategic-sector enterprises which has generated high FDI inflows in recent years. In 2004-2008, 24% of the total FDI came as a result of privatizations; in 2009 this share was as much as 26% (figure I.6).

Figure I.6. Albania: contribution of privatization to FDI inflows, 2003 -2009
(Millions of dollars)



Source: Based on data provided by the Bank of Albania for FDI inflows and Ministry of Economy, Trade and Energy and Ministry of Finance for FDI inflows from privatization.

For example, over the five years 2005-2009, all the main banks were privatized, with several of them being sold to banks from other countries. New development policies for other strategic industries such as mining and energy were put in practice in 2008, which allowed for the privatization of state-owned enterprises in those sectors, including through sales of shares to foreign firms. Some privatization deals in 2009 involving FDI are listed in box I.2.

Box I.2. Major privatization deals involving FDI in Albania in 2009

Major privatization deals involving FDI in Albania in 2009 included the following:

- The sale of 12.6% of shares in mobile telecommunication company AMC to the Greek telecommunications group COSMOTE, for €48.2 million;
- The sale of 76% of shares in the energy distributor (OSSh) to the Czech company CEZ for €102 million.
- Investments in the cement industry by Antea Cement (Italy), Colacem Albania (Italy), Cementos Aguila (Italy).
- The fourth mobile telephony license was sold to the Post-Telecommunication of Kosovo for €7.5 million.

Source: UNCTAD, based on data from Thomson Financial.

Beyond the direct inflows of FDI in the form of the sales revenue for the assets, privatization also brings follow-up investments in the form of capital increases of an acquired company.

The structure of FDI inflows to Albania by economic sectors underwent some important changes in the 2006-2008 period for which data are available. There was a rapid increase of investments in industry and construction (table I.8). Large fluctuations reflect important privatization deals. The privatization of the oil refinery complex ARMO for about €125 million was the main factor that led to the large increase of FDI in manufacturing in 2008 (table I.8).

Table I.8. FDI inflows by economic activities, 2006-2008 (Millions of euro)			
Economic activity	2006	2007	2008
Agriculture, hunting and fishing	2	2	- 54
Construction	8	61	147
Industry	69	56	369
Electricity and gas	-	4	2
Services sector	180	357	211
Telecommunications	62	196	- 61
Financial intermediation	30	136	167
Total	259	481	675

Source: Data provided by the Bank of Albania

High FDI in the financial sector in 2008 was the result of the purchase of certain shares of Banka Popullore and Union Bank by foreign investors. The contribution of FDI in financial intermediation to the total flows of FDI also remained high in 2008, with a share of 24% of the total. The manufacturing industry also gained more FDI in recent years with its share accounting more than half of FDI inflows in 2008. The main recipient industries are labour intensive, including the production of textiles and shoes which has attracted investors from Italy and Greece. In 2008, inflows to the construction sector reached €147 million mainly as the result of infrastructure investments.

D. Main features of FDI stock in Albania.

1. FDI stock by form

Inward FDI stock in Albania reached almost €2.7 billion in 2009, according to the Bank of Albania (BOA) survey of foreign investment enterprises (box I.4), while outward FDI stock amounted to a mere €131 million in 2009 (table I.9)). Among foreign affiliates in Albania that responded to the Bank of Albania survey, 78% of them are majority owned. As to the size of the companies, 28% are small and 22% are of medium size. 66% of the companies are concentrated in central Albania and the rest are distributed in the other prefectures of the country in almost equal percentages.

Box I.3. Collection of data on FDI and activities of TNCs in Albania

FDI flow and stock data for Albania are derived from the Bank of Albania's annual survey of companies with at least 10% foreign ownership. According to the statistical register for 2009 produced by Albania's Institute of Statistics (INSTAT), there were 1700 active foreign investment enterprises in the country. These companies were contacted by the Bank of Albania through various channels to collect FDI data. One third of the companies, mostly large ones, provided data regarding foreign investments. The results allowed Bank of Albania to update their FDI flow statistics and to provide FDI stock data by various structural characteristics. Parallel to the Bank of Albania survey, INSTAT carries out a structural business survey (SBS) covering all active companies in the country. From the results of this survey it derives the data for the majority foreign-owned enterprises to provide the statistics on the characteristics of foreign affiliates' examined further below (section E).

Source: Bank of Albania

FDI stock data are recorded by two forms: equity capital and reinvested earnings (combined), and other capital (mainly intra-company loans). The item "equity capital and reinvested earnings" represents the overwhelming part of the FDI stock in Albania – 97% at the end of 2009. The stock of direct investments abroad also consisted mainly of "equity capital and reinvested earnings".

Table I.9. Components of inward and outward FDI stock, Albania, 2003-2008 (Millions of euro)							
FDI components	2003	2004	2005	2006	2007	2008	2009 ^a
Inward FDI stock	357	612	846	1 054	1 688	1 986	2 692
Equity capital and reinvested earnings	352	603	806	982	1 622	1 858	2 603
Other capital	5	9	40	72	67	128	89
Outward FDI stock	..	8	8	31	51	105	131
Equity capital and reinvested earnings	..	8	8	31	51	103	127
Other capital	..	-	-	-	-	2	4

Source: UNCTAD, FDI/TNC database (www.unctad.org/fdistatistics) based on Bank of Albania.

^a Data for 2009 are estimated.

Albania has the lowest FDI stock relative to GDP among the countries of South-East Europe (table 1.10). This is due to the fact that FDI in Albania is a very recent phenomenon and much of stock has been accumulated over the past few years only. Albania has also had more rapid economic growth in recent years than its regional peers.

Table I. 10. Inward FDI stock as a percentage of GDP in Albania and other South-East European countries, 2004-2009

Country	2004	2005	2006	2007	2008	2009
Albania	11	12	15	23	21	29
Bosnia and Herzegovina	28	28	34	45	40	46
Croatia	31	33	56	77	46	58
Montenegro	11	29	51	69	72	110
Serbia	17	22	34	33	40	49
The former Yugoslav Republic of Macedonia	41	36	43	47	47	52

Source: UNCTAD, *WIR10*, annex tables.

The increase of FDI stock in the country in 2008 was a result of investment transactions, exchange rate changes and other adjustments (table I.11). While the transactions resulted in an increase in the stock value by €675 millions, the “other adjustments” item and the exchange rate changes decreased the stock by €305 and €73 million respectively. The increase of Albanian FDI stock abroad in 2008 was mainly the result of transactions during 2008 (€56 million).

Table. I.11. Composition of change in inward and outward FDI stock, 2007-2008
(Millions of euro)

FDI stock	Position at end of 2007	Transactions	Price changes	Exchange rate changes	Other Adjustments	Position at end of 2008
Direct investment in reporting economy	1688	675	1	-73	-305	1986
Equity capital and reinvested earnings	1622	612	1	-72	-305	1858
Other capital	67	63	..	-2	..	128
Direct investment abroad	51	56	..	-2	..	105
Equity capital and reinvested earnings	51	54	..	-1	..	103
Other capital	..	2	2

Source: Data provided by the Bank of Albania

^a The data for the composition of changes in FDI stock are not yet available for 2009.

2. Inward FDI stock in Albania by main economic activities

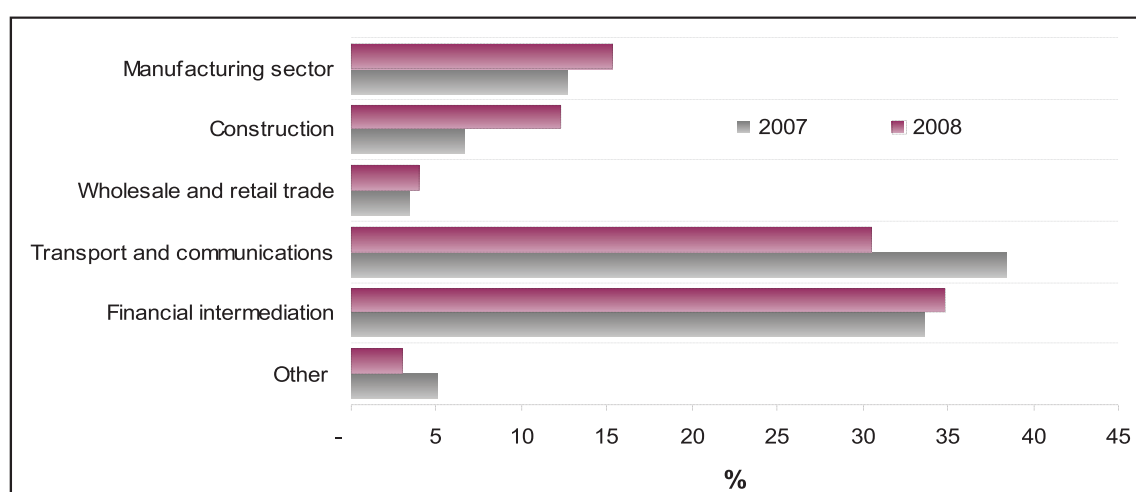
Only 16% of the FDI stock in Albania was in the manufacturing sector in 2008 (figure I.7 and table I.12), less than in other South-East European countries and much less than in most of the EU new member states. Most of this FDI is in the basic heavy industries (construction material, metals) while more sophisticated manufacturing is missing not only in the foreign but also the domestic enterprise sector. The construction sector with 15% of the inward FDI stock is almost as important as manufacturing. The building boom partially financed from remitted income gave rise to a residential construction boom in 2004-2008.

Services account for the overwhelming proportion of the FDI stock in Albania (figure I.6, section E). Among them, wholesale and retail trade activities still account for a low share of FDI, with only 7% of the total stock in 2008 as the major foreign supermarket chains have not been established in the country on a large scale yet. Transport, storage and communication accounted for 23% of the FDI stock in 2008, mainly due to FDI in fixed-line and mobile telephone services. But its share declined from that in 2007 due to some disinvestments. Financial intermediation has been the most important FDI target with one third of the stock in 2008. The almost full privatization of the banking industry to foreign banks and investors has

resulted in a large inflow of capital by which the banks have been restructured and credit activities expanded.

The hotels and restaurants industry has only 1% of the FDI stock, although the country has good natural potential for attracting tourism. Real estate renting and other business services are also underrepresented in the country's FDI stock compared to more developed countries but account for a higher share than in some other countries in the region. There is also very little investment in legal and consulting services, the presence of which would be necessary for investors. FDI in these services may expand as demand for them grows.

Figure I.7. Albania: Inward FDI stock by economic activity, 2007-2008



Source: Based on data provided by the Bank of Albania

Table I.12 Albania: Number of investment projects and inward FDI stock by economic activity, 2007-2008
(Number, millions of euro and per cent)

NACE category ^a	Sector/Industry	No of investment projects	2007		2008	
			FDI stock	%	FDI stock	%
	Primary	21	15	1	-29	-1
A	Agriculture, hunting and forestry	7	6	0	11	1
B	Fishing	3	0	0	-59	-3
C	Mining and quarrying	11	9	1	19	1
D	Manufacturing	225	224	13	321	16
	Services	316	1451	86	1696	85
E	Electricity, gas and water supply	6	1	0	3	0
F	Construction	49	136	8	306	15
G	Wholesale and retail trade, repair of motor vehicles	155	84	5	140	7
H	Hotels and restaurants	7	20	1	19	1
I	Transport, storage and communication	23	588	35	467	23
J	Financial intermediation	22	551	33	663	33
K	Real estate, renting and business activities	37	56	3	79	4
L	Public administration and defence; compulsory social security	0	0	0	0	0
M	Education	4	2	0	2	0
N	Health and social work	4	0	0	-1	0
O	Other community, social and personal service activities	9	13	1	18	1
Total		562	1,688	100	1,986	100

Source: Based on data provided by the Bank of Albania

^a General Industrial Classification of Economic Activities within the European Communities (Nomenclature Générale des Activités Économiques dans les Communautés Européennes).

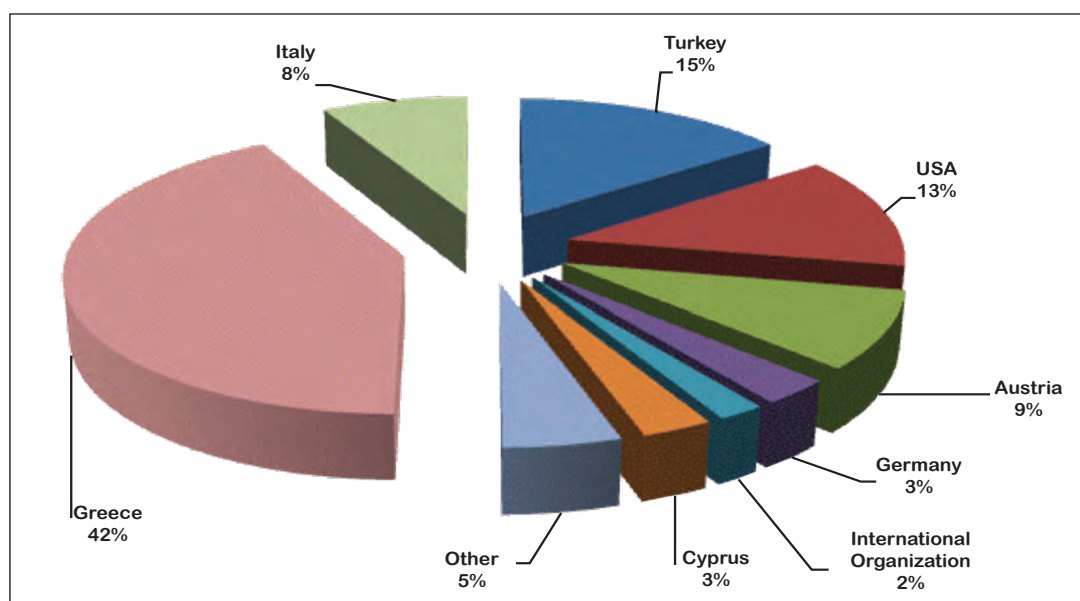
The increase in FDI stock in 2008 was accompanied by a change in its structure. The stock in construction rose to more than twice its size in the previous year, almost doubling its share in the total stock, and that in manufacturing expanded by 43%, leading to a small increase (3%) in its share. Transport, storage and communication suffered a 21% decline in FDI stock, while the stock in financial intermediation rose by 20% to maintain its share in total stock at almost the same level as in 2007 (table I.12).

3. FDI stock in Albania by investing country

As is usual with small countries, Albania receives an exceptionally large part of its FDI from a neighbouring country – in its case, Greece (table I.13 and figure I.8). FDI from Greece accounted for 41% of the FDI stock in 2008, six percentage point less than in the previous year. However, only 26% of the investors in Albania came from Greece, indicating a high concentration of Greek FDI and its focus on the capital-intensive activities. Greek investments in Albania are mainly in telecommunications (61%) and financial intermediation (22%). Also for FDI in the financial industry, Greece is also the most important home country.

Table I.13. FDI stock in Albania by region and home country, 2004-2008 (per cent)					
Home country/region	2004	2005	2006	2007	2008
Developed countries	87	85	88	85	81
European Union	78	78	79	72	66
Austria	6	5	9	9	9
Germany	2	3	3	2	3
Greece	56	55	53	47	41
Italy	13	12	11	11	8
North America	5	6	7	11	13
United States	5	4	4	11	12
Developing countries	10	12	10	14	18
Africa	1	0	0	0	0
South America and the Caribbean	-	-	-	-	-
Asia and Oceania	9	12	10	14	17
Lebanon	1	3	2	2	2
Turkey	4	6	6	11	14
Transition economies	3	3	2	1	1
Southeast Europe	3	3	2	1	1
International Organizations	3	0	0	1	2

Source: Data provided by the Bank of Albania

Figure I.8. Albania: geographical breakdown of inward FDI stock by source, 2008

Source: Data provided by the Bank of Albania

The second largest source-country for FDI in Albania, and the main gainer of share in 2007 and 2008 is Turkey with 14% of the stock in 2008, up by 3% compared with the previous year (table I.13). There were 40 Turkish investors, with FDI concentrated in non-financial activities.

The United States is third in importance as a home country, with 12% of the FDI stock in Albania in 2008, somewhat more than in the previous year (table I.13). The United States is seldom among the top sources of FDI in countries in the region. In 2004, the United States was only seventh among the source-countries for FDI in Albania, with just 2% of the inward FDI stock. No major United States investors are among the top 10 foreign companies investing in Albania except for a private equity fund, the Albanian-American Enterprise Fund which invested in several projects including the American Bank of Albania which merged with and became part of the Intesa San Paolo Bank from Italy in 2008.

Austria occupies the fourth place as a home country for FDI in Albania, with 9% of the inward FDI stock in 2008 (table I.13). Almost all of the Austrian investment is in the banking sector, mainly as a result of the purchase of the Savings Bank of Albania by Raiffeisen International to become the largest bank in Albania with 30% of the banking assets in the country.

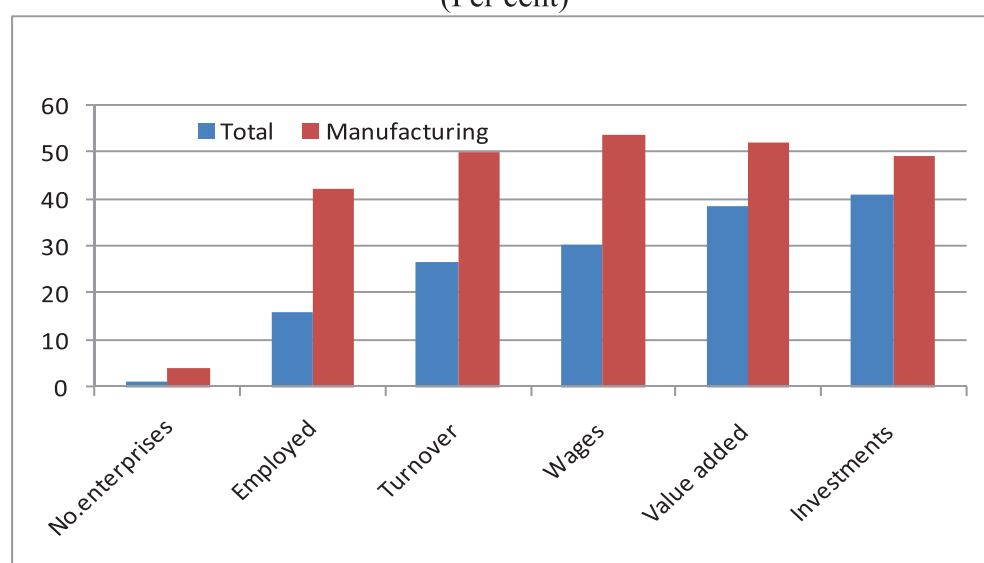
Next in importance as a home country is Italy, with 8% of Albania's inward FDI stock in 2008, a lower share than in the previous year when it still held 11% (table I.13). Investments originating from Italy focus mainly on manufacturing and construction. While they are also present in the services sector, mainly in financial intermediation, finance is still under-represented in Italian FDI in Albania, compared with FDI from other major investor-countries. Another peculiar feature of Italian investments is that it is distributed among a large number of companies: 42.5% of the 546 investors come from Italy. The decline of Italian investments in relative terms is even more striking if compared with 2004 when the country was still second in importance after Greece, with 30% of Albania's inward FDI stock.

The five countries mentioned above together account for 84% of the FDI stock and 80% of the foreign affiliates in Albania. Further peculiarities beyond the high representation of Greece and the second and third positions of Turkey and the United States in the FDI stock in Albania include the low representation of investors from Germany, which ranks normally among the first five in importance among the home countries for FDI in other countries of Central and Eastern European countries. The limited presence of German FDI in Albania could be due to the relative lack of investment opportunities in manufacturing.

E. Effects of FDI: the role of foreign affiliates in the Albanian economy

This section looks at some important features of enterprises with majority foreign ownership (foreign affiliates) with a view to understanding their contribution to the Albanian economy. The coverage of the data on FDI projects included, gathered by the Structural Business Survey (SBS) conducted by Albania's INSTAT, and closely resembles that of the Bank of Albania (BOA) survey based FDI statistics (box I.4). The main difference is in the minimum share of foreign ownership in enterprises covered, which is 10% in the BOA's FDI statistics and 50% in the INSTAT's foreign affiliate statistics (FATS) (in line with the Eurostat definition). Also, the source of enterprise data is partly different, but both the BOA survey and the INSTAT survey cover the main foreign investment enterprises. Data are grouped by economic activities according to NACE (*Nomenclature Générale des Activités Économiques dans les Communautés Européennes*) at the two-digit level. However, the coverage by economic activity is only partial, and excludes enterprises active in financial intermediation, education, health, and cultural activities. The SBS and FATS data refer to the year 2008 and a comparison can be made with the year 2007 for which similar data are available. The INSTAT surveys cover 512 foreign affiliates for 2008 and 405 for 2007. FATS data were weighted in the same way as other SBS data thus comparability is achieved which allows calculating the share of the foreign affiliates in the Albanian economy by various indicators covered by the SBS.

Figure I.9. Share of foreign affiliates in the Albanian economy ^a by various indicators, 2008.
(Per cent)



Source: Based on INSTAT, Albania, structural business survey (SBS)

^a Excluding financial intermediation, education, health and cultural activities.

The **number of foreign affiliates** is marginal relative to the total number of enterprises; only 1.2% of the total number of active enterprises in Albania is majority foreign owned (figure I.9, table I.14). The foreign share is larger in manufacturing (4%), and very low in some services. However, in activities where the number of enterprises is small altogether, more than half of them are foreign affiliates: in extraction of petroleum, tobacco industry, electrical machinery and air transport. These are the activities with very high capital intensity where SMEs, usually domestically owned, are rare. In other activities like retail trade or hotels and restaurants local SMEs are numerous and dominate.

Table I.14. Share of foreign affiliates in the Albanian economy by industry, various indicators, 2008

(Per cent)

Industry	Number of enterprises	Number of persons employed	Turnover	Total wages	Value added	Total investments
5 Fishing	1.4	8	7.9	14.5	8	8
11 Extraction of petroleum	75	9.5	53.5	10.9	45.7	100
13 Mining of metal ores	2.3	17.8	36.5	29	41.7	87.7
14 Other mining and quarrying	2.1	12.2	10	23.6	15.6	0
15 Food	0.6	16.3	30.8	27.7	14.5	27.6
16 Tobacco	66.7	98	100	97.4	97.5	0
17 Textiles	3	31.5	25.7	50.9	31.6	44.8
18 Wearing apparel	16.6	60.8	55.1	62.4	59.4	62.4
19 Leather	41.5	59.3	62.1	60.5	57.4	49.2
20 Wood	1.4	8.9	9.5	13.3	7.2	59.7
21 Paper	20.5	28.7	12.3	26.9	13.8	0.1
22 Publishing	2.4	8	10.4	10.4	9.2	8.9
23 Petroleum products	7.3	13.1	18.7	14.7	19.6	52.7
25 Rubber&plastic	10.5	58.4	58.6	58.5	61.7	56.1
26 Non-metallic minerals	4	37.6	59.2	64.9	67.9	72.3
27 Basic metals	7.4	89	95	95	94.8	93.7
28 Fabricated metals	1	19.7	25.1	35	25	8.4
29 Machinery n.e.c.	21.6	5.1	19.2	14	17.7	5.6
31 Electrical machinery	57.5	89	79.4	88.8	87	84.2
33 Medical instruments	4.8	8.6	4.2	13.8	4.2	11.9
35 Other transport equip.	37.5	52.6	57.4	54.3	52.1	0.5
36 Manufacturing n.e.c.	2.6	27.3	33.5	41.5	40.2	9.4
37 Recycling	4	16	3.9	18.6	10.7	34.9
40 Electricity, gas	25.6	0.2	0.8	1.6	2.4	1.4
41 Water	1.7	3.3	6.3	4.5	1.8	6.9
45 Construction	2.1	16	34.2	43.2	41.3	41.3
50 Sale of motor vehicles	1.7	3.9	10.7	11.8	4.6	21.8
51 Wholesale trade	5.4	11	15	17.2	6.2	27.8
52 Retail trade	0.1	0.6	3.6	4.4	2.5	35.2
55 Hotels and restaurants	0.1	2.4	6.6	10.3	8.6	23.9
60 Land transport	0.1	0.9	3.7	2.8	8.8	11.5
61 Water transport	9.4	7	1.2	8.3	3.4	0.3
62 Air transport	50	75.4	14.3	32	..	0
63 Other transport	2.8	12.1	25.8	18.8	29.5	2.3
64 Post and telecom.	3.9	50.5	92.8	61.7	93.2	89.2
70 Real estate activities	12.4	11.4	27.3	16	32.4	12.8
71 Renting	10	24.1	4.4	37.1	..	0
74 Other business activities	2.1	6.2	29.2	21.4	15	17
90 Sewage disposal	5.3	3.9	9.7	3.5	..	1
93 Other services	0.1	0.8	1.4	3.7	1.5	29.8
All Industries^a	1.2	16	26.7	30.6	38.7	41.3
Manufacturing	4	42.3	50.2	54	52.2	49.2

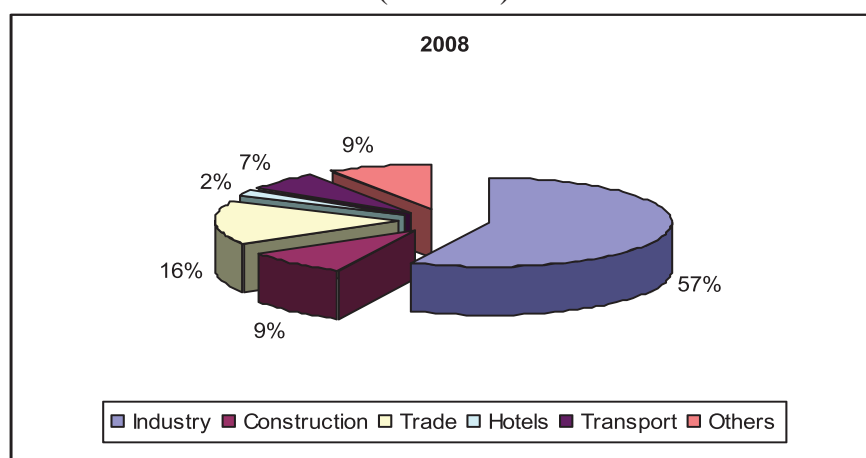
Source: Data provided INSTAT, structural business survey (SBS)

^a Excluding financial intermediation, education, health and cultural activities.

The share of foreign affiliates in the Albanian economy is much higher by all indicators other than the number of enterprises (table I.15, figure I.9). This indicates that the foreign affiliates are much larger in size; they have much more employees and turnover per enterprise than the domestically-owned companies.

The distribution of the foreign affiliates by economic sectors (figure I.10) differs from the structure of Albanian enterprises. The main distinguishing feature is the high share of companies in the manufacturing sector (57%) despite a relatively small share in total FDI stock (16%) (table I.12), as well as trade (16%).

Figure I.10. Distribution of foreign affiliates in Albania by economic activity^a, 2008.
(Per cent)



Source: Data provided INSTAT, structural business survey (SBS)

^a Excluding financial intermediation, education, health and cultural activities.

One of the most important indicators of the role of the non-financial foreign sector is its share in the **value added** in the non-financial economic sectors of the country. With almost 39% of the total, the foreign sector makes a very important contribution to value added. In manufacturing, foreign affiliates contribute the main part, 52%. Both shares increased compared with 2007. In other words, there is a re-industrialization process going on in Albania based on foreign investment. In fact, the whole manufacturing sector is still very weak and low-technology and factor-intensive activities dominate its structure.

Out of the 22 manufacturing activities, foreign affiliates have dominant position in producing the value added of eight industries (table I.14). These include labour-intensive industries such as the production of wearing apparel and leather goods and capital-intensive industries like the production of non-metallic minerals (including construction material) and basic metal products. These four industries are the most important manufacturing activities of the foreign investors, with 80% of the manufacturing value added by foreign affiliates.

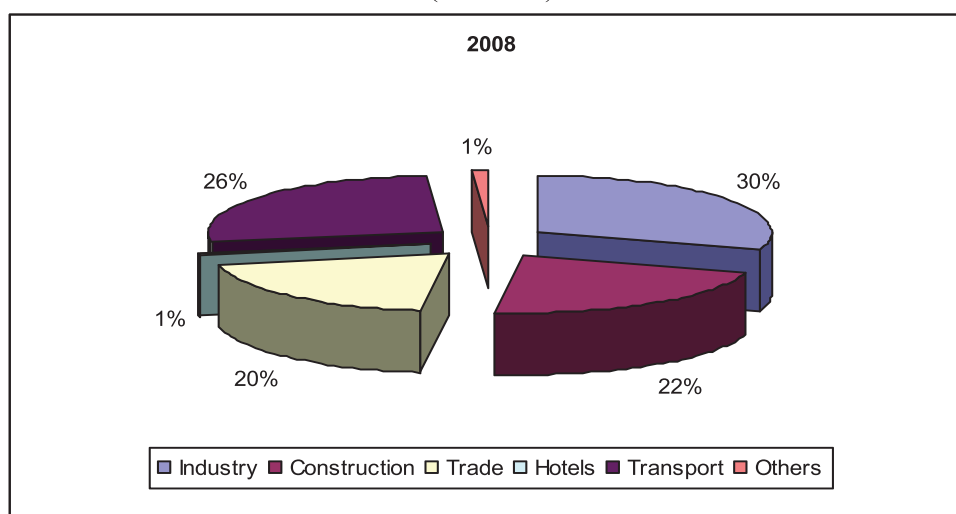
In the other industries, foreign affiliates dominate value added only in telecommunications. They also have a significant role with about 40% of value added in mining and construction. These are also the activities which have high shares in the FDI stock. As to the more sophisticated manufacturing industries, low foreign shares in value added and low share in FDI stock point to the same direction, a need to attract foreign investors. There are two such activities with important foreign presence already: the

production of electrical machinery and of transport equipment other than cars. In these industries foreign affiliates have a large share but in a rather small industry.

The **turnover** of foreign affiliates represents 27% of the total, but for the manufacturing industry, 50%. The main foreign-penetrated industries are the same as by value added. The turnover of foreign affiliates is generated by four main economic activities, industry (30%), transport and telecommunications (26%), construction (22%) and trade (20%) (figure I.11).

Compared with 2007 the turnover of foreign affiliates in 2008 was 50% higher in nominal prices (41% in real terms, deflated by the producer price index). The increase was above the average in construction and in manufacturing. In manufacturing the turnover of foreign affiliates hardly changed in textiles, clothing and leather but the production of non-metallic minerals boomed. While industrial development has been altogether remarkable, there has been no shift to export-oriented industries. The boom of the construction sector was the main growth engine effecting mining and quarrying of construction materials, production of non-metallic mineral products and also of wood and metals. Further growth stimuli were given by the communications privatization and foreign investments in the oil industry.

Figure I.11. Albania: turnover of foreign affiliates by economic activity^a, 2008.
(Per cent)



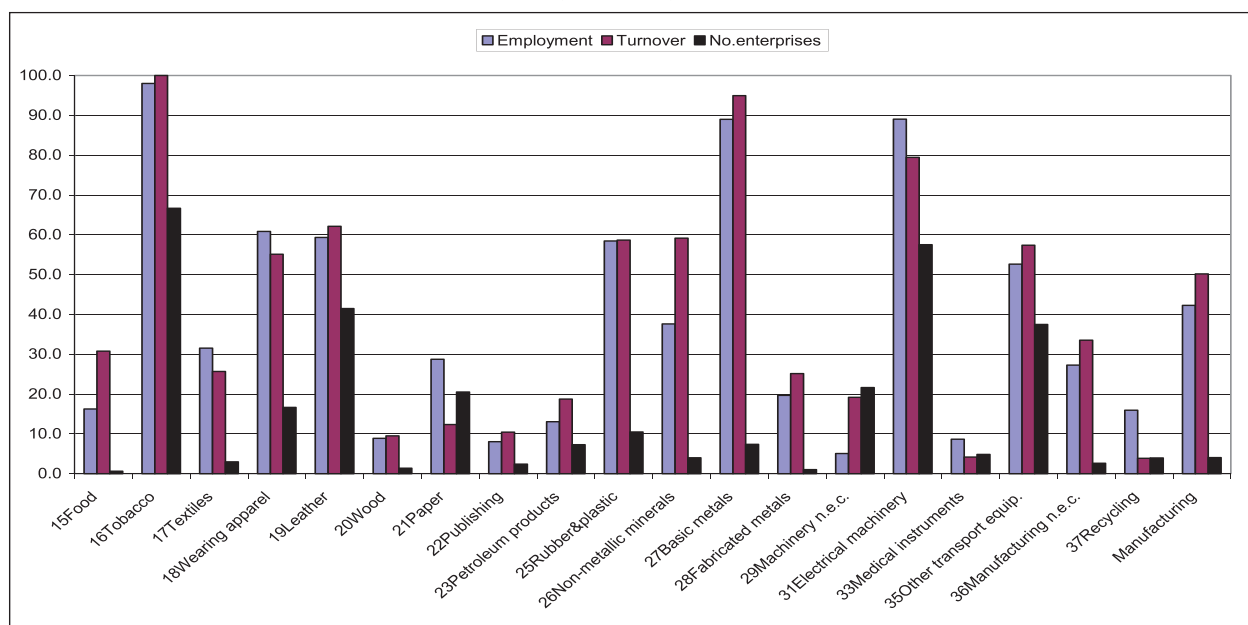
Source: Data provided INSTAT, structural business survey (SBS)

^a Excluding financial intermediation, education, health and cultural activities.

As to **employment**, the share of foreign affiliates is 16% for the economy as a whole, but much more, 42% for manufacturing. The employment share is relatively small compared with turnover or value added which is a sign of the higher labour productivity of the foreign sector as compared with the domestic sector. The productivity gap is much smaller in manufacturing than in other activities. Among individual industries, a comparison between the employment and the turnover shares indicates where the labour productivity of foreign affiliates is higher (higher share of turnover than of employment) than the average of the economy (figure I.12). In the light industries and the production of electrical machinery foreign affiliates have similar or even lower labour productivity compared to the average. In these activities both foreign and domestic companies rely on similar labour-intensive

technologies. The lead of the foreign sector in terms of labour productivity is more pronounced in capital-intensive industrial activities like non-metallic minerals, basic metals and general machinery.

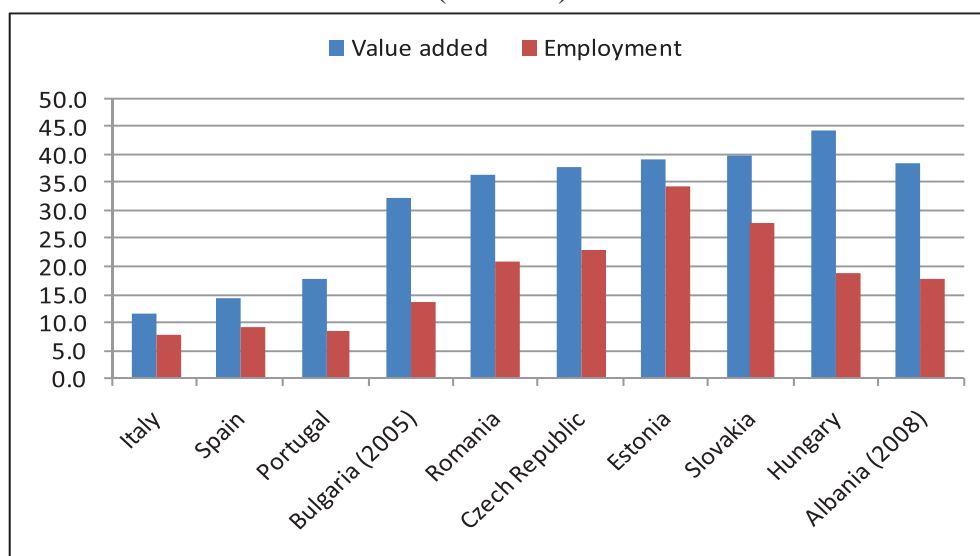
Figure I.12. Share of foreign affiliates in manufacturing in Albania by industry, selected indicators, 2008
(Per cent)



Source: Data provided INSTAT, structural business survey (SBS)

The **investment** activity of foreign affiliates amounts to 41% of total investments in the non-financial business sector (table I.14). Investment expenditures per unit of value added and turnover are higher in the foreign sector than the average of the Albanian economy. Increased investment due to the greater propensity of foreign firms to invest in more capital-intensive activities requiring larger investments is a clear advantage derived from FDI. Investment is especially high in the telecommunications sector following foreign takeovers; it is relatively small in manufacturing.

Figure I.13. Share of foreign affiliates in value added and employment, Albania and selected other European economies ^{a b}, 2006
(Per cent)



Source: EUROSTAT and INSTAT, structural business survey (SBS)

^a Excluding financial intermediation, education, health and cultural activities.

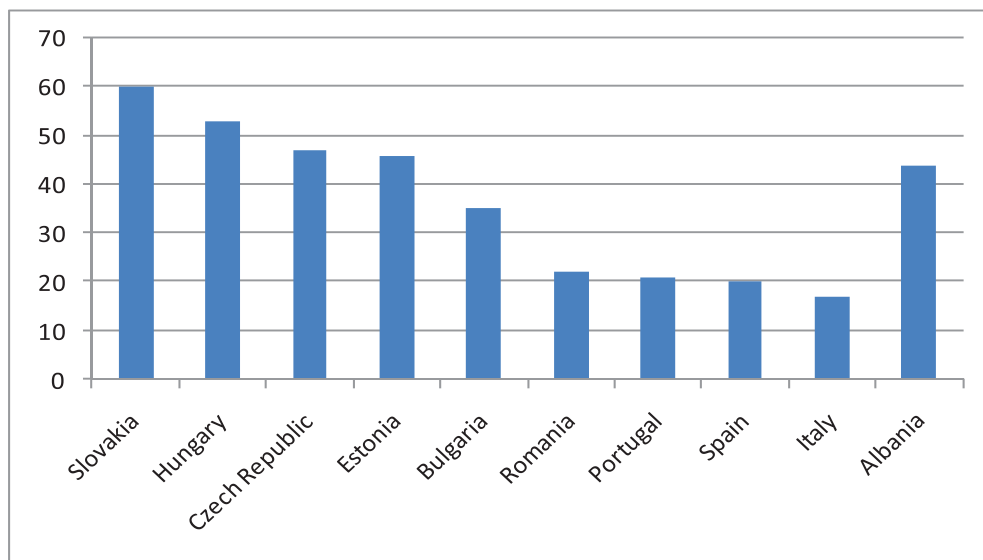
^b Data relate to 2008 for Albania and 2005 for Bulgaria

Albania is among the countries with the highest foreign penetration in Europe. International comparison is available from the Eurostat Standard Business Statistics for the indicators such as value added and employment in foreign affiliates in the year 2006.⁶ While the reference year is different, the share of foreign affiliates in the value added in Albania (2008) is the fourth highest, close to the countries with the highest shares, like the Czech Republic, Estonia and Slovakia. Only Hungary the leader in Europe is significantly ahead of Albania. In terms of employment in foreign affiliates, Albania is sixth, similar to Hungary and behind other countries like Estonia or Slovakia. In countries with a large gap between value added and employment, the foreign affiliates have much higher labour productivity than the rest of the economy. This is the case in Albania and in Hungary and can indicate weak spillovers from the foreign to the domestic sector. In countries where the two shares are close to each other (Estonia), the gap between labour productivities of foreign affiliates and domestic companies is similar to each other which may point to strong spillovers (Görg, H. and Greenaway, D., 2001)

The share of foreign affiliates is usually higher in industry than in other activities. Slovakia and Hungary have the highest foreign-affiliate shares in value added in Europe, with 60% and 53%. Albania ranks fifth with 44%.

⁶ EUROSTAT, Foreign controlled enterprises in the EU, Statistics in Focus, 30/2008.

Figure I.14. Share of foreign affiliates in value added in industry, selected countries, 2006
(Per cent)



Source: EUROSTAT and INSTAT, structural business survey (SBS)

In conclusion,

- Foreign affiliates have high significance in the Albanian economy in terms of value added, production, employment and investment activity.
- The degree of foreign participation in the economy is similar to that in the Central European countries which have the highest indicators of FDI participation in Europe.
- High foreign participation in certain sectors is also a sign of weaknesses in the domestically- owned part of the economy, including an underdeveloped local SME sector.
- Foreign affiliates in Albania have an uneven distribution across the economy. Although they drive some reindustrialization in the country, their involvement in activities with higher technologies is limited.
- The labour productivity gap between foreign affiliates and domestic companies in the country is relatively small in the manufacturing industries pointing to a relatively similar level of technology used by foreign affiliates.

CHAPTER II. THE ROLE AND IMPACT OF FDI IN SERVICES IN ALBANIA

Over the past two decades, Albania has been transformed from an agricultural economy into one dominated by services. The share of agriculture fell from above 50% in 1992 to 23% in 2002 and came further down slowly to 18% in 2008 (table II.1). At the same time, the share of industry decreased to about 10% in 2008, while that of construction increased to 14%. The rest of the GDP, some 58% is accounted for by services (table II.1). The increase in services output is partly explained by the growth in GDP and the accompanying shift of demand to services that has occurred partly due to the opening up of the Albanian economy and the increase in imports of agricultural and manufactured goods which led in particular to a decline of industrial production. Non-tradable services can only be delivered by being produced where the customers are located and their production needs to grow to match demand.

The shift of production away from agriculture to services is not entirely matched by a similar structural shift in employment. Agriculture is still the most widespread occupation accounting for the largest share of employment while services account for only 38% of the employment. The discrepancy between production and employment shares is partly due to overestimation of employment in agriculture where all population above 16 years is considered employed, but also denotes that low labour productivity in the agrarian sector is accompanied by relatively high productivity in the rest of economy, dominated by services. A driving force of output growth and productivity increase in the non-agrarian sectors has been FDI.

Table II.1. Gross value added by economic activities, 1992 and 2001-2008.
(Per cent)

Economic activity	1992	2001	2002	2003	2004	2005	2006	2007	2008
Industry	17	13	7	9	10	11	11	9	10
Agriculture	54	34	23	24	22	21	20	19	18
Construction	8	10	12	12	14	14	14	15	14
Transport	3	10	7	5	5	5	5	5	5
Services	18	33	51	50	49	49	50	52	53

Source: Data provided by INSTAT

Services FDI may positively impact the services sector in a host country by providing capital and transferring knowledge, managerial expertise and skills that increase services productivity and output in the country. On top of this, new services may be introduced by FDI. More competitive service firms offering higher quality and lower cost services benefit the Albanian end-users as well as the industries that use the services as intermediate inputs, thus contributing to the competitiveness of the overall economy. Technology transfer also takes place if employees who acquire skills when employed in foreign enterprises disseminate those skills when they leave the foreign companies and move to Albanian firms.

FDI in services accounted for three quarters of Albania's FDI stock in 2008. There are two major services, telecommunications and financial intermediation which are of particular importance as hosts to FDI, accounting for 23% and 33% respectively of the total FDI stock in the country (figure I.7, table I.12). The FDI-led development of these services is examined in greater detail below. As noted in the first chapter, other services like wholesale and retail trade have not yet attracted foreign investors on a large scale. The European supermarket chains that dominate the retail sector in the new member states of the EU are not yet

represented to any significant extent in the Albanian economy. Besides a wholesale store by the METRO GROUP (Germany), the Italian cooperative food store Conad is the most important foreign firm operating in wholesale and retail trade services in Albania with several smaller shops in Tirana. Real estate activities by foreign affiliates are also marginal, accounting for only 0.7% of the FDI. More noteworthy is the development of “other business activities” including consulting, IT and call centre services, with 3.3% of the FDI stock in 2008. Business process and information technology services have undergone some growth since 2007 and may have good prospects, also in comparison with other countries in the region. Proximity to Italy and good Italian language skills in a growing section of the Albanian population enable the country to attract Italian firms to set up IT and call service centres. Pioneers in this respect include Italy’s Answer Group and Teleperformance. More training of the labour force as well as better fixed-line telephone services have been identified as factors of key importance for further growth of business services.

A. FDI in telecommunication services

Telecommunications are among the most dynamic service activities in Albania. They have developed mainly via privatization and subsequent investments of foreign investors and to some extent through domestic investments.

- The first mobile operator in Albania was launched in May 1996 by Albanian Mobile Communication (AMC), a state-owned company at that time. In 2000, 85% of the shares of AMC were privatized for the amount of €85.6 million through their sale to the Cosmote Telenor Consortium (Greece). The remaining 15% state shares were privatized in March 2009 for €48.2 million. At the time of privatization AMC counted 15,000 users, while in 2008 it counted around 1,400,000, consequently covering 47.1% of the mobile industry, employing around 500 persons.
- Vodafone Albania was the second cellular operator to be licensed in Albania in June, 2001. The GSM network of Vodafone covers 90.9% of the territory of Albania, and 99.6% of Albanians in rural and urban areas. Eagle Mobile, the newest mobile operator in Albania, entered the market on October 2008, employing 250 people in the company, while another 150 people are employed in subcontracting companies. Also it has contributed in a larger number of mobile subscribers in 2009. In 2009, the fourth mobile operator received its license to enter the Albanian market. The license was sold for €7.5 million to a joint venture between Albanian companies and Kosovo Post & Telecommunication.
- The fixed telephone operator, Albtelekom sh.a, privatized 76% of its shares for an amount of €120 million through their sale to Calik Enerji Telekomünikasyon (Turkey) along with its partner Turk Telekom. The number of fixed telephone users at the end of 2008 was around 324,000, i.e. 9% higher than in 2007.

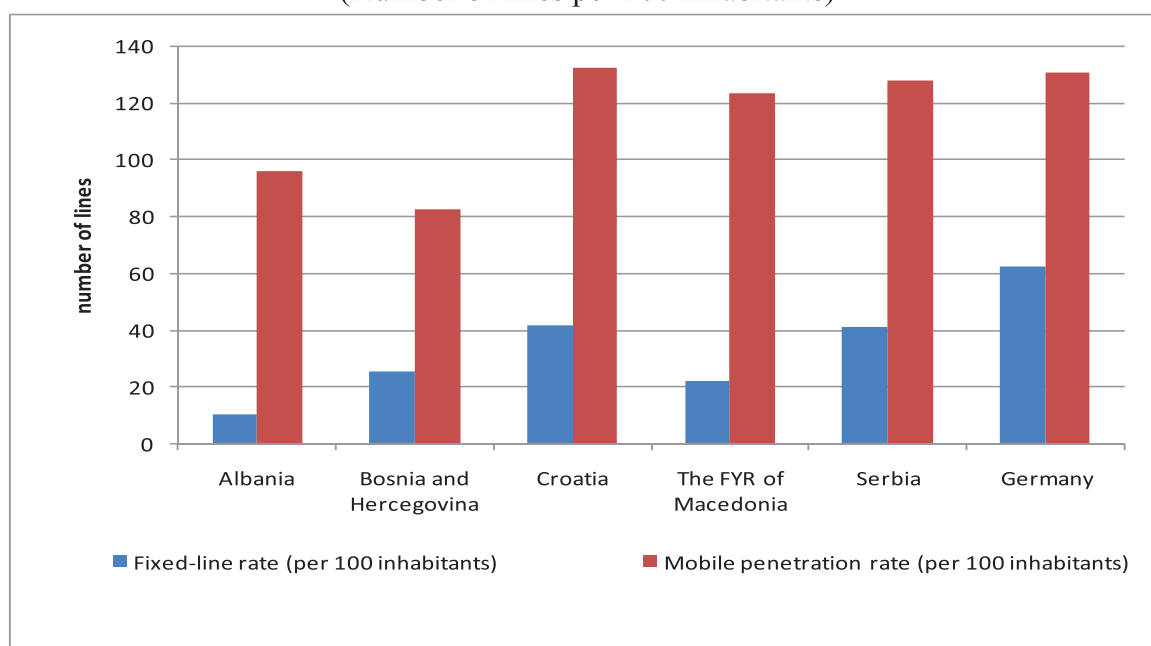
Tabela II.2. Number of user connections of mobile phones and of fixed-lines phones in Albania 2003-2009

	2003	2004	2005	2006	2007	2008	2009
Fixed-line	243 858	256 266	273 056	289 637	296 146	323 964	363000
Mobile	1 099 611	1 259 195	1 530 244	1 909 885	2 323 436	2 964 473	4 163 624

Source: Data provided by the Authority of Electronic and Postal Communication (AKEP), Tirana, Albania

Between 2005 and 2009, the numbers of fix line telephone connections in Albania rose by 30% to 360,000 subscribers. While those for mobile phone more than tripled to over 4.16 million subscribers (table II.2). This level of mobile phone penetration is similar to developed countries such as Germany.

Figure II.1. Fixed-line and mobile telephone penetration rates, selected countries
(Number of lines per 100 inhabitants)



Source: OECD, "South East Europe - Investment Reform Index 2010: Monitoring Policies and Institutions for Direct Investment", 2010.

According to the latest assessment of the Investment Reform Index (April 2010) of OECD, the spread of fix line telephony in Albania remains the lowest in South-East Europe, while mobile telephony has increased rapidly. This is a typical of telecommunications development in countries where the population at large has its first access to telephone services in the mobile phone age. That the low use of fix line telephone is not a matter of supply but of demand, is confirmed by the short time necessary to obtain a new connection—about 7 days in Albania compared with 18 days in Bosnia and Herzegovina and 6 days in the former Yugoslav Republic of Macedonia and Montenegro (OECD, 2010). However, the quality of services provided by the fix line telecommunication infrastructure as measured by the interruptions and the deficiencies per 100 main lines is among the lowest in the region (OECD, 2010).

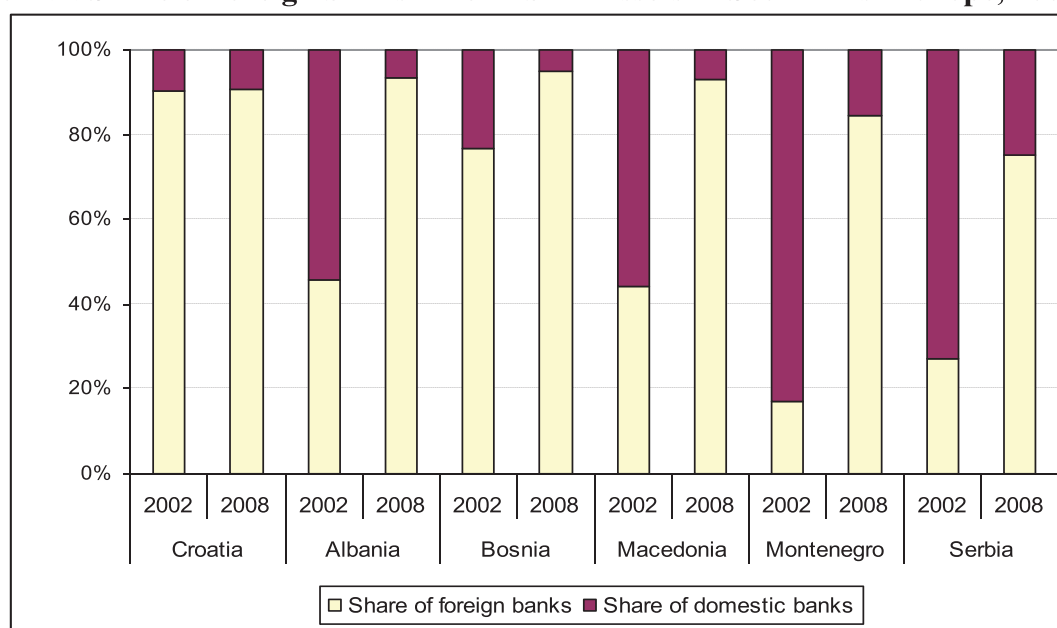
The density of internet connections in Albania is the lowest in the region 2.52 per 100 inhabitants, although there is an increasing trend. The low level of fix line connections has limited access to internet, but in the future internet access may also spread through mobile internet providers. For the time being, the growth and spread of call centres and IT services are also hindered by the lack of sufficient fixed-line telephone connections.

B. FDI in banking services

Market reforms speeded up in Albania since the late 1990s, as in other South-East European countries. All countries in the region restructured their banking system by privatizing state-owned banks, mostly to large foreign banks. The transfer of banking knowledge and funds through such FDI stabilized their financial systems. In 2008, finance was the largest recipient of FDI, accounting for 32% of the region's inward FDI stock (UNCTAD, *WIR10*, p.52). At the same time, the share of banking assets owned by foreign entities had risen to 90% both in Albania and in most other countries of the region (figure II.2). This represents a higher exposure to foreign banks than in the new EU member states (EBRD, 2010b).

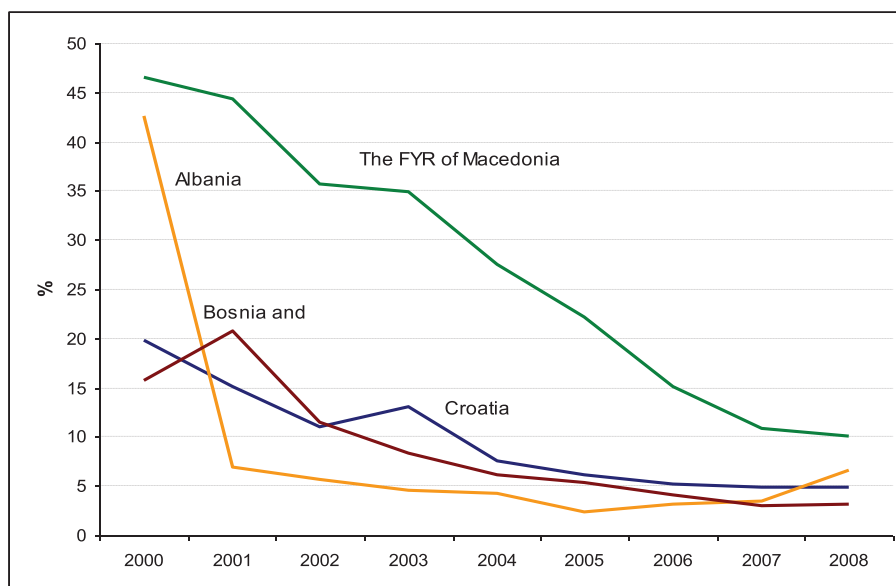
The largest banking investors in the region, including in Albania, are from Austria, France, Greece and Italy. In 2009, Greek banks are estimated to control roughly between 15% and 30% of the market in some countries of the region. Overall, foreign banks appear to have had a positive influence on the efficiency and stability of the banking system in the region. They have strengthened risk management and corporate governance through a more efficient allocation of capital and increased competition, and have introduced more sophisticated financial services. As a result the banking industry has expanded rapidly supporting economic growth and non-performing loans have declined in Albania as well as other countries in the region at least until 2008 (figure II.3).

Figure II.2. Share of foreign banks in total bank assets in South-East Europe, 2002, 2008



Source: UNCTAD, *WIR10*.

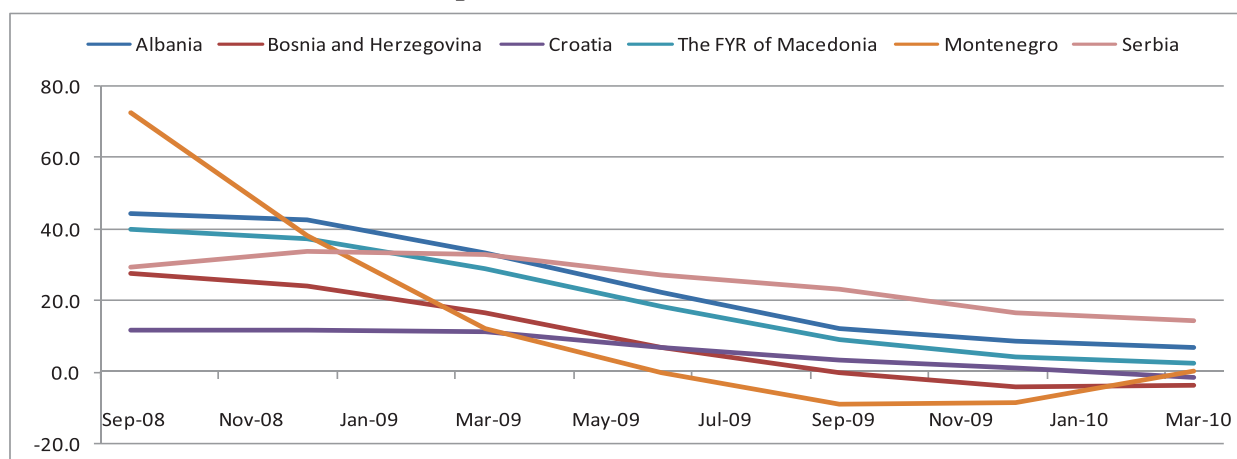
Figure II.3. Non-performing loans in selected South-East European countries, 2000–2008



Source: UNCTAD, *WIR10*.

More recently, the effects of the international financial crisis through banking have raised concerns in Albania and other countries of South-East Europe. In Albania, however, the banking sector is in good shape not only due to its privatization and the involvement of foreign banks but also to monetary policy which provided timely support via two cuts in the central bank's interest rate and liquidity injections via the exchange rate in 2009. Prudent supervision and regulation helped ensure that banks entered the crisis in good shape and could rely on substantial solvency and liquidity buffers. These were further boosted by foreign parent-bank support (IMF, 2009). Bank lending has slowed down or contracted throughout South-East Europe and also in adjacent new EU member countries. Albania has been one of the countries where loans provided to the private sector continued to grow, although at a declining rate (figure II.4).

Figure II.4. Bank loans to the non-financial private sector, percentage change over the preceding year, Albania and other countries of South-East Europe, September 2008–March 2010.



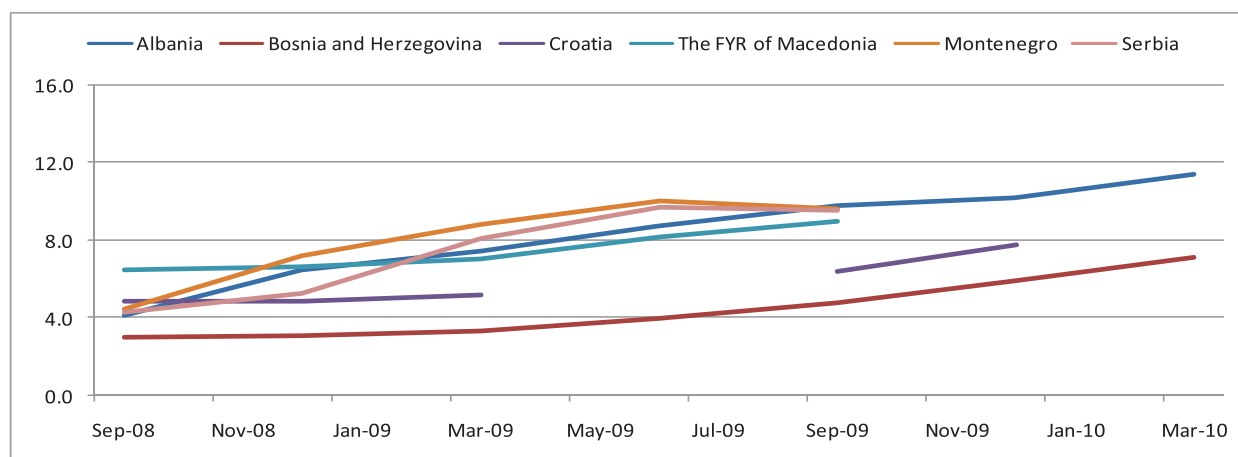
Source: The Vienna Institute for International Economic Studies (WIIW) FDI database relying on national statistics.

Since the outset of the crisis, credit conditions have become tighter and the private sector has had difficulty meeting its obligations. The share of non-performing loans increased again in all countries of the region for which data are available (figure II.5). Albania has the second highest share, close to 12% which indicates that bankruptcy is looming in an important part of the private sector. Banks have stocked up reserves and seem not to be in danger.

The Italian and Austrian banks active in Albania have weathered the crisis. However, the home banks of the Greek affiliates are facing difficult times due to the economic crisis in Greece and rely on government and EU support. This may save them but their activities will contract due to a shrinking and more risky domestic market. The future of the Greek banking affiliates in Albania depends to a large extent on their ability to finance their activities from locally-collected deposits as they cannot rely on their parents' support. Greek parent banks may find it more profitable to lend money to the Greek State and hence less capital could flow to their branches in Albania. A contraction of their activity in Albania would not, however, present a problem for the financial sector in Albania, as there are an ample number of other banks to take over the business.

The commercial banks currently operating in Albania are the outcome of privatization and of some Greenfield entries. During 2008, ownership of the capital in the banking system underwent important structural changes, which brought increasing domination by foreign banks and other financial institutions. The sale of the stocks of Credins Bank, owned by an Albanian private shareholder, to two foreign investors has increased the weight of foreign capital in that bank from 5% in 2007 to 33.3% in 2009. Two shareholders at ProCredit Bank, Fefad Foundation (domestic capital) and IFC (equity from the World Bank Group) have sold their shares to the Procredit Holding (Germany). During 2007, the European Bank for Reconstruction and Development (EBRD) became shareholder in Union Bank with 12.5% participation. This event marked the entry of foreign capital into the last bank in the country that was fully owned by domestic investors.

Figure II.5. Percentage share of non-performing loans in total loans, Albania and other countries in South-East Europe, September 2008-March 2010.



Source: The Vienna Institute for International Economic Studies (WIIW) FDI database relying on national statistics.

Also, in 2007 the number of banks in Albania fell from 17 to 16 (table II.3). This was due to the merger of Intesa San Paolo Bank, created as a joint venture of the banks Sanpaolo IMI and Intesa Bank, with the American Bank of Albania (table II.4 provides a complete list of banks in the country by ownership as of 2008). Employment in banks and the number of branches of banks have, however, continued to increase (table II.3).

During 2008, statutory capital of banks in Albania held by foreign investors increased by ALL 12.5 billion (33%), while Albanian capital fell by ALL 266 million (5.6%). By the end of December 2008, foreign capital in Albanian banking is estimated to have increased to ALL 50.3 billion or 91.8% of the total (from 88.8% in end-2007), while domestic capital is estimated to have fallen to ALL 4.5 billion or 8.2% of the total (Bank of Albania, 2009).

Table II.3. Main indicators of the size of the banking system in Albania, 2003-2008						
Indicators	2003	2004	2005	2006	2007	2008
Number of banks	15	16	17	17	16	16
Number of employees	2 236	2 816	3 479	4 189	5 155	6 493
Number of branches/agencies	161	188	250	294	399	511

Source: Data provided by the Bank of Albania

The indicators of banking-sector stability have improved. New and more up-to-date banking services have been introduced. However, the overall positive features by international banking standards do not satisfy all the needs of the Albanian economy yet. SMEs still have limited access to bank financing and there is need for improved credit guarantee schemes.

Foreign-owned banks have channelled, to some extent, the negative impact of the international financial crisis to Albania. Although credit to the private sector continued to grow even in the first quarter of 2010, the rate of expansion declined while the share of bad loans in total loans started to expand. However, these features are not due to foreign ownership per se but apply generally to banks in most European countries.

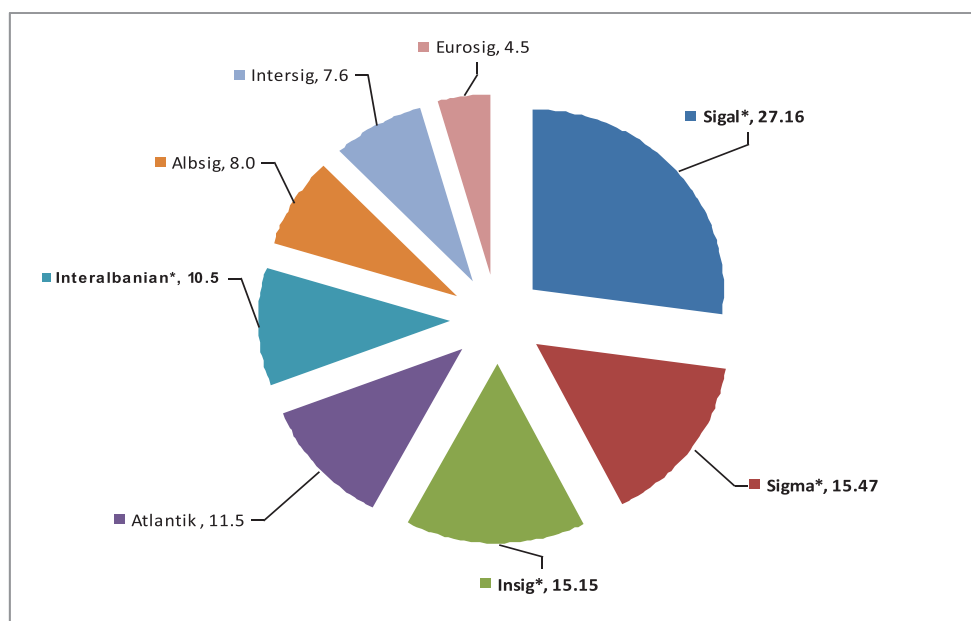
Table II.4. Banks in Albania by ownership, 2008				
Bank	Shareholder's name	Shareholder's %	Ownership	Shareholders' Country of origin
Raiffeisen Bank	Raiffeisen International Bank – Holding AG	100	Foreign Private	Austria
Banka Kombetare Tregtare (BKT)	Calik Sekei Konsorsiyum Yatirin A. S	60	Foreign Private	Turkey
	EBRD	20		International Institution
	IFC	20		International Institution
United Bank of Albania	Ministry of Finance, Albania	40	Government	Albania
	Shamil Bank of Bahrain	20		Saudi Arabia
	IDB Jeddah	15		International Institution
	Malaysian Co Business Fokus	6.3	Foreign Private	Malaysia
	Dallah Albaraka Holding	10	Foreign Private	Saudi Arabia
	7 Individuals	8.7	Foreign Private	
Banka Tirana	Pireus Bank	90.7	Foreign Private	Greece
	Dafnila S.A.	1.3	Foreign Private	
	5 Individuals	8	Foreign Private	
Branch of National Bank of Greece	National bank of Greece	100	Foreign Private	Greece
Alpha Bank	Alpha Bank of Greece	100	Foreign Private	Greece
Italian Bank of Development	Veneto Banca Holding S.c.p.A.	100	Foreign Private	Italy
ProCredit	Pro Credit Holding	80	Foreign Private	Germany
	Commerzbank AG	20	Foreign Private	
Banka Nderkombetare Tregtare	ICB Holding AG	100	Foreign Private	Switzerland (Malaysia)
Emporiki Bank	Emporiki Bank of Greece	100	Foreign Private	Greece
Credit Bank of Albania	3 individuals	100	Foreign Private	Kuwait
Credins	10 Individuals	68.5	Domestic Private	Albania – Spain
	Bushati Sh.p.k.	4.7	Domestic Private	
	EMIGRES	4.2	Foreign Private	
	BFSE Holding BV	22.2	Foreign Private	Netherlands
	SECO (SIFEM)	3.2	Private – Public	Switzerland
Banka Popullore	Societe Generale	75	Foreign Private	France
	9 Individuals	25	Foreign Private	Albania
Union Bank	Financial Union of Tirana	83.13	Foreign Private	Albania
	EBRD	12.5		International Institution
	2 Individuals	4.37	Domestic Private	Albania
First Investment Bank	First Investment Bank, Bulgaria	99.998	Foreign Private	Bulgaria
	Vitosha Ventures AD	0.0001	Foreign Private	Bulgaria
	First Finance Brokerage House LTD	0.0001	Foreign Private	Bulgaria
Intesa San Paolo	Intesa San Paolo S.p.a	78.5	Foreign Private	Italy
	Albanian-American Fund of Enterprises	12.2	Foreign Private	USA
	EBRD	7.8		International Institution
	Italian Society for Foreign Enterprises	1.5	Foreign Private	Italy

Source: Data provided by the Bank of Albania

C. FDI in insurance services.

During the year 2008, ten insurance companies, including both foreign and domestic, were operating in Albania. Seven of them were non-life insurance companies, two were life insurance companies and one provided both non-life and life insurance. The companies providing non-life insurance, ranked by market share, included Sigal, Sigma, Insurance Institute (Insig), Atlantik, Interlbanian, Albsig, Intersig and Eurosia (figure II.6). Sigal led the market with approximately 27.2% of non-life insurance premiums.

Figure II.6. Albania: distribution share of the non-life insurance market by provider, 2008

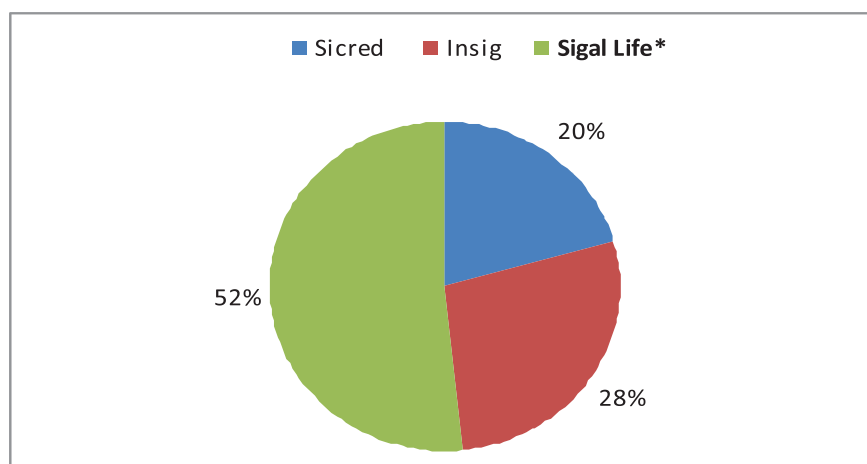


Source: Data provided by the Ministry of Economy, Trade and Economy

* Companies in Bold are owned by foreign affiliates with more than 10%

Life insurance services were provided by the companies Sigal Life, Insig and Sicred (figure II.7). Sigal – Life led the market with 40% of the premiums.

Figure II.7. Albania: Distribution share of life insurance market by provider, 2008



Source: Data provided by the Ministry of Economy, Trade and Economy

* Companies in Bold are owned by foreign affiliates with more than 10%

Foreign insurance companies have established operations in Albania since 2007. During the year 2008, foreign companies increased their participation further. In January 2008, the participation of UNIQA International Beteiligungs-Verwaltungs GmbH (Austria) in Sigal Holding (owner of the companies Sigal and Sigal-Life) with 45.6% ownership was approved. In October 2008, the participation of the company TBIH Financial Services Group N.V. Amsterdam (with 60% ownership by the Vienna Insurance Group) in the insurance company Sigma increased from 75% to 87%.

On the other hand, insurance companies operating in the Albanian market have also increased their presence outside the territory of the Republic of Albania. Insig, Sigal, UNIQA GROUP Austria and Sigma have expanded in Kosovo and the former Yugoslav Republic of Macedonia, and Albsig has established a branch in the former Yugoslav Republic of Macedonia. Sigma increased its investment in its Kosovo branch through issuance of new shares in branch in 2008.

D. Conclusion

The entry of foreign investors into financial and telecom services, the two largest recipient service industries, occurred mainly via privatization. There was significant additional capital invested in the privatized firms after the takeovers. While the Albanian economy has benefited from FDI in these services, there is considerable room for further improvements in its role in development (e.g. access to finance by SME) and for mitigating potential risks associated with FDI (e.g. contingency risks in financial markets). In order to attract more FDI into these and other services as well as other sectors, and to benefit more from it, at the same time minimizing costs and risks, the Government needs to put in place a more comprehensive and effective policy with respect to FDI.

CHAPTER III. REGULATORY FRAMEWORK AND BUSINESS ENVIRONMENT FOR FDI IN ALBANIA

Legal framework and institutional arrangements for FDI in Albania

A. The changing environment for business

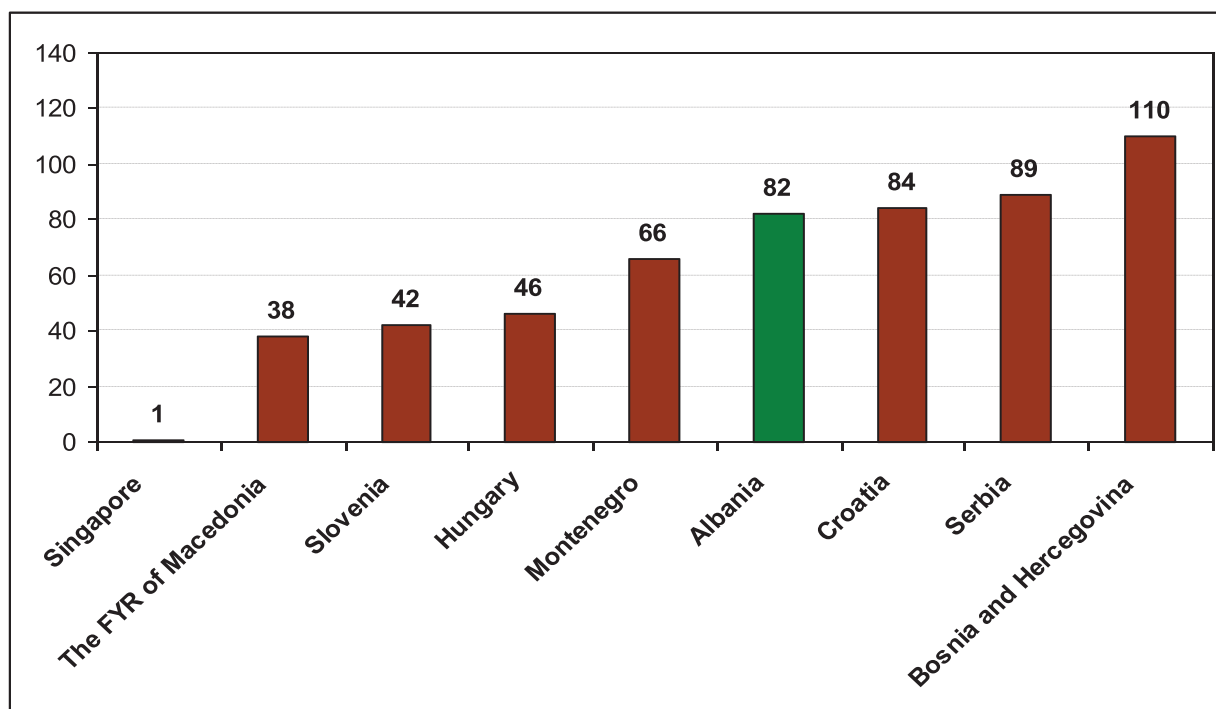
With the start of the reform processes towards a market economy in the 1990s, Albania embarked upon a transformation of the political, economic, legal and institutional framework of the economy. Since the late 1990s the Government has implemented a series of structural reforms including land reform, reform of the financial market, price liberalization and privatization. Over this time, almost all SME were privatized and there has been significant progress in the privatization of strategic industries such as telecommunications and banking. The banking sector has gradually increased the number of financial services it provides and credit extended to businesses. The country is now characterized by an open economy, with a liberal trade and investment regime.

Despite a high increase in recent years, FDI inflows in Albania are still relatively low compared with those to neighbouring countries. Attracting higher levels of FDI is still a challenge for the country. The reform process continues and aims at improving further the business and investment environment through the reduction of various legal and administrative barriers to doing business in Albania.

1. International comparative assessments

- In the European Commission's 2010 Progress Report, it has been noted, inter alia, that Albania as regards the economic criteria, has achieved a certain degree of macroeconomic stability and has made significant efforts in aligning its legislation with the EU acquis, particularly in some areas of the internal market, trade related provisions, customs and taxation. However, the country faces major challenges in implementing and enforcing legislation and to become a functioning market economy, Albania needs to further strengthen governance, improve the performance of the labour market, ensure the recognition of property rights and strengthen the rule of law. In order to enable it to cope over the medium term with competitive pressure and market forces within the Union, Albania needs to strengthen its physical infrastructure and human capital and pursue further structural reforms.
- As mentioned in chapter I, Albania ranks relatively high in the global ranking based on UNCTAD's Inward FDI Performance Index. The latest ranking by this indicator (for the year 2009) placed Albania in the 25th place among 141 countries, representing a rapid improvement from the country's position of 80th place in 2006. On the other hand, the country ranks low on investment potential, indicating that poor infrastructure, energy shortfalls and modest research and development activity can hinder FDI in the future.
- In the Doing Business 2011 report of the World Bank, Albania is ranked 82nd out of 181 economies in the ease of doing business (World Bank, 2011). It ranks in the middle of the group if compared to other Western Balkan countries (figure III.1).

Figure III.1. Ease of doing business: global ranking of Albania and other countries by the World Bank



Source: World Bank, IFC, Doing Business 2011: Making a difference for entrepreneurs, a copublication of Palgrave MacMillan, IFC and the World Bank (Washington D.C.: Wold Bank), available at <http://www.doingbusiness.org/documents>

In terms of the ten main areas of the doing-business indicators, there is a large gap between Albania's performances by the different indicators. On "starting a business", Albania ranked 68th in 2009, moved to 46th in 2010 and 45th in 2011 in the global ranking. The average time in days for starting a business is five days as compared to the OECD average of 13 days. With respect to "getting credit" and "protecting investors" Albania ranks 15th out of 183 countries for both indicators in 2011 putting Albania among the top reformer countries. The "getting credit" indicator reflects the improved efficiency of the Albanian banking system after privatization and foreign investment. The areas included in the doing business indicators in which the country is among the worst performing in the world are "construction permits", "tax payment" and "closing a business". Property certification has to be improved and the issuing of all permits simplified. In 2010, Albania made it easier and less costly for companies to pay taxes by amending several laws, reducing social security contribution and introducing electronic filing and payment (World Bank, 2011).

- In the Global Competitiveness Report 2010-2011 of the World Economic Forum (WEF), Albania is ranked 88th out of 133 countries with a score of 3.94, improving its ranking over that in the previous year (WEF, 2010). The most advanced components of competitiveness index include
 - Institutions;
 - Goods market efficiency, due to the ease of starting a business; and
 - Labour market efficiency – flexibility of wage determination, hiring and firing practices, relationship between wages and productivity.

The most problematic factors hindering competitiveness in Albania according to this report are access to finance, corruption and tax regulations. The problem areas here are pretty much the same as those discussed above related to the doing business indicators.

- The OECD Investment Reform Index 2010 shows that progress has been made in reforming policies and institutions that influence the environment for investment in Albania (OECD, 2010). According to the indicators for the index, dimensions where policy reform is advanced are:

- Investment policy
- Trade policy

Dimensions where reforms have been slow are:

- Access to finance (incomplete credit register, cadastre, underdeveloped equity finance)
- Tax policy (efficiency of tax collection)
- Human capital (vocational and higher education)

According to the analysis of their ranking, Albania as well as other South-East European countries have made important progress, for example in further integrating into the multilateral trading system and improving legal frameworks affecting access to finance and the protection of physical property. But continued reforms are essential

- to address skills deficits by improving education and training systems;
- to speed the adoption of EU technical regulations and standards as well as sanitary and phytosanitary measures;
- to help companies obtain access to finance by improving the functioning of credit guarantee arrangements and the regulation of micro-finance. Governments could also explore measures to help develop a market for informal equity finance.

- While the World Bank Investing Across Border report mentioned Albania among the ten fastest countries in the region for start-up processes of foreign companies (World Bank, 2010), in 2010 Index of Economic Freedom of the Heritage Foundation, Albania is ranked 53rd out of 179 countries (Heritage Foundation, 2010).

2. FDI policy - the investment regime

In 1993, Albania adopted a legal framework that favoured FDI which was subsequently improved. The main characteristics of the current investment regime are:

- The Albanian economy is open to all investors. Prior authorization for investments is not required. As a rule, all sectors are open to foreign investment. The law guarantees equal and impartial treatment. Investment by both foreign and domestic investors is permitted on the same terms.
- No prior authorization is required for foreign investors to set up a company.
- The legal framework on FDI largely respects the principle of national treatment. Restrictions to national treatment appear for sectors covered by separate legislative frameworks, such as arms production, internal maritime transport, fishing, and notary and bailiff's services.
- The Law on Foreign Investments states that foreign investments may not be nationalized or expropriated, except in special cases defined by law and when in the public interest. In these cases procedures must take place without any discrimination and with compensation equal to the real market value.

- Investors in Albania are entitled to judicial protection of the rights related to their investment. The parties to the dispute may agree to submit disputes for consideration by an arbitration institution. In the event of a failure, foreign investors have the right to submit the dispute to an Albanian court or to the Arbitration Court in Tirana. In the event of a dispute regarding discrimination, transfer of assets, or indirect expropriation of foreign investment by the government, the investor may submit the dispute to the International Centre for Settlement of Investment Disputes (ICSID). Ratified international agreements have legal superiority over domestic legislation in Albania.
- Foreign-controlled enterprises registered in Albania as legal entities are allowed to own every type of land, so foreigners can buy land without any limitation through the companies that they establish legally in Albania. Problems remain with the cadastre system and ownership titles.
- Companies investing in Albania have the right to employ foreign citizens. Funds related to investments may be transferred outside the country in a convertible currency calculated with the exchange rate for current transactions on the day of the transfer. Transfer can be restricted for non-payment of taxes or not meeting obligations and by judicial decisions.
- Over the years, in Albania, there have been property issues because of multiple parties claiming ownership of the same land property. The Government has acknowledged this as impairment to FDI and therefore has been proactive in offering a solution. To this end, the Government has recently drafted a new law that protects and guarantees the investments of foreign investors.
- Albania has 37 bilateral agreements in force on reciprocal protection and promotion of investments. These are with Austria, Belgium and Luxembourg, Bosnia and Herzegovina, Bulgaria, China, Croatia, Czech Republic, Denmark, Egypt, Finland, France, Germany, Greece, Hungary, Israel, Italy, Kosovo-UNMIK, Kuwait, Republic of Korea, Lithuania, The former Yugoslav Republic of Macedonia, Malaysia, Moldova, Netherlands, Poland, Portugal, Romania, Russian Federation, Serbia, Slovenia, Spain, Sweden, Switzerland, Tunisia, Turkey, Ukraine, United Kingdom, and United States.

To ensure the highest competitiveness of the country and to make Albania the most attractive place for foreign investors, further administrative reforms, fiscal and judicial will be undertaken until 2013. While the overall environment and comprehensive policies already in place support these objectives, the Government will formulate and implement a programme with specific tools to support well-coordinated industrial and export development. Instruments to be used are:

- creation of specific infrastructure facilities such as the establishment of five industrial parks or business incubators;
- combination of industrial parks with fiscal facilities similar to the free zone;
- the use of subsidies from public funds for investments in innovative technology, supporting funding for SMEs, etc.; and
- creation and/or strengthening of consultative networks, or promotional information based on models already successful for increasing competitiveness and promoting foreign investments.

3. Recent reforms

As a foundation to its economic policy, the Albanian Government has introduced policies to support private sector development aiming at:

- improving the business climate and business infrastructure,
- reducing the informal economy,
- expediting the privatization process in strategic sectors such as telecommunications and insurance,
- extending and further developing the banking sector,
- developing the insurance market,
- increasing investment in oil and gas, and
- developing seaport and airport services.

In addition, investment in energy and infrastructure remains a priority for the Government. In cooperation with other donors, it will aim at raising additional funds in partnership with the private sector. Public-private partnership is considered to provide a real potential for generating savings in the economy and freeing budget funds in order to use them in priority sectors.

The Albanian Government has undertaken a comprehensive regulatory reform. The core of the measures consists in the reduction of administrative burden and cost of doing business. The steps taken during the years 2006–2011 are outlined below.

Reform of the business registration process

Since 2007 the registration of a business is made in one day at the National Registration Centre (NRC) for less than €1. Also, the number of steps for starting a new business was reduced from 10 to five. Within one day, in a single application, the new business can register online to satisfy the requirements relating to taxes, health insurance, and labour.

Issue of licences

The licensing procedures in different sectors of economy have been simplified. During 2007-2008 the reforms led to the elimination of the excessively large number of licences and permits, namely: of 170 existing licences required, 104 have been removed. Based on Law Nr.10081 of 23.02.2009 "On Licences, authorizations and permits in the Republic of Albania" the National Licensing Centre (NLC) started operations in June 2009 operating in Tirana with service centres in the cities of Korca, Shkodra and Vlora.

Licences are required in the following areas: national security, public order and civil protection, food and health, environment and basic environmental resources, mineral resources, hydrocarbons and energy, territory and construction, cultural heritage, transport, production, depositing, use and/or trading of products and/or substances or other equipment that pose a risk, education and science, notary services, bailiff's services, public finance. Activities requiring licences are divided into three groups (for groups I and II they are issued by the NLC itself within two to four days while for group III, licences are referred to the line ministries and the time allowed for the issuance of a license is 10-30 days).

Commercial code

Law No. 9901 "On Entrepreneurs and Commercial Companies," of 14 April 2008, which replaced the law of 1992, defines the type of legal status of companies. The new law brings Albanian legislation in line with EU's *acquis communautaire* and reflects the other

amendments made to Albanian legislation such as the Civil Code, the Law on the National Business Registration Centre, the Labour Code, and the Law on Titles and other important laws. The law envisions provisions for entrepreneurs with respect to the establishment of commercial companies, their representation, trust liabilities, shares of employees, the dismantling and liquidation of general and limited partnerships, limited liability companies, shareholding companies, and restructuring of companies.

Fiscal reform

The steps for fiscal reform undertaken during 2007–2008 and the expansionist fiscal policy pursued during the first half of 2009 made the tax system in Albania more facilitating and encouraging for business development. In parallel with this, the distribution of the tax burden has become more equal and less distorting. The main objective of tax policy is balancing the public budget, with the use of taxes as an instrument of economic policy to promote employment and investment in the economy. Tax policy reform has been based on the idea of lowering the tax rate and simultaneously extending the range of tax-payers. The main steps of the tax reform include:

- the gradual reduction of the rate for the profit tax from 25% in 2000 to 10% in 2010;
- the change in the system of personal income taxation, from progressive to proportional with the same tax rate as the those for corporate income (10%);
- significant reduction of the tax burden on income from work: currently the total measure of the tax-contribution on gross salary for social insurance and health is 27.9% of the gross monthly salary, down from 41.9% in 2000. However this measure left a considerable financing gap in the pension fund.

Trade policy

The integration of the Albanian economy into the regional markets in South-East Europe can compensate for its weakness in terms of the small size of its market by opening up the prospect of serving a market of about 50 million people. Integration is fostered by trade liberalization, supporting exports and encouraging FDI. The Government has taken action to harmonize the Albanian legislation with international trade rules and with the European Common Commercial Policy. Since becoming a WTO member in September 2000 Albania has implemented the full liberalization of its import-export regime for goods. Further trade policy steps will be achieved with the elimination of all non-tariff barriers to trade.

The Stabilization and Association Agreement (SAA) with EU signed on the 1 December 2006 contains an interim free trade agreement with the EU which came into force on 1st April 2009. This agreement, an important step on the way to EU membership, is expected to open new opportunities for the development of the country.

Since January 2004 Albania has completed and started to implement a full network of free trade agreements in the South-East European region with the former Yugoslav Republic of Macedonia, Kosovo, Serbia and Montenegro, Bulgaria, Romania, Bosnia and Herzegovina, Croatia and Moldova. That was followed by the liberalization process and the adoption of the unified agreement on free trade, Central European Free Trade Agreement (CEFTA) 2006, signed by all parties and fully operational since November 2007. This agreement is not a formal transformation of the network of the many free trade agreements into one agreement, but it reflects a higher level of trade opening and regional cooperation among the countries in the region. The liberalization policy has continued with the free trade agreement between

Albania and Turkey, and with the free trade agreement of Albania with European Free Trade Association (EFTA) states.

The tariffs applied by Albania on imports from outside the EU are very low. In 2008 Albania's average bound tariff was 6.6% while the average tariff applied was 2.3%. During 2008, an important reform was undertaken in customs procedures with the computerization of all customs points, considerably improving services to businesses, reducing time for completing documentation and controlling of traded goods.

Free zones and industrial parks

The Albanian Government has approved legal and sub-legal acts, namely Law No. 9789, dated 19 July 2007 "On the establishment and functioning of economic areas" and Council of Ministers Decision No. 860, dated 10 October 2007 "On the approval of regulations regarding the establishment and functioning of economic areas", with a view to providing the legal and institutional basis for the establishment of free economic zones and industrial parks for the establishment of activities by enterprises. As of 2010 the Government has approved nine economic areas. Eight of them have the status of industrial parks and one of them has the status of a free area. These are the industrial parks of: Spitalla (in development, state- and privately-owned); Vlora (in development); Koplik (manufacturing, agro-processing, trade, export-import); Shengjin (manufacturing, agro-processing, trade, export-import); the Industrial Park of Elbasan (in development, industrial, trade activities, services); the Industrial Park of Shkodra (in development, manufacturing, food, services, trade, import-export); the Industrial park of Lezha (manufacturing, agro processing, trade, export-import and services), the industrial park in Laknas (Tirana) and the free economic zone in Vlora. Investments of some \$60 million are foreseen to be allocated to activities in the industrial parks and 30,000 new jobs created.

Privatization

Privatization has been an important part of Albania's reform process, and has been an important tool to attract foreign investors (chapter I). The privatization strategy approved by Law No. 8306 dated 14 March 1998 has been aimed among others at the attraction of potential strategic investors, stimulation of the economy through the efficient use of human and natural resources and guaranteeing the stability of ownership. No limitations on the participation of foreign investors have been applied in the process of privatization. Foreign investors are allowed 100% ownership of privatized enterprises. Although it is facilitated by the law, the State has not maintained control on companies using the so-called "golden share".

Public Private Partnership (PPP)

The Government of Albania has prepared the full implementation of the legislative package under Law No. 9663, dated 18 December 2006 "On Concessions". Amendments should enable increased transparency, effectiveness and fairness when signing concessionary agreements for projects involving public private partnership (PPP). Concessions have been applied by the Albanian Government in different sectors like energy, mining, airport infrastructure and the management of water-supply and sewage systems in some cities of Albania.

One of the key infrastructural challenges facing Albania has been to develop a more efficient and reliable electricity power system. On the supply side, until 2005, there had been

just a few investments to develop and diversify Albania's infrastructure to generate energy. These were predominantly based on hydro-electric power which was dependent on precipitation. In addition, Albania's capacity to import electricity had been hampered by the physical limitations of the transmission system. The result was frequent power outages.

Concessionary projects in the energy sector aim at a production of almost twice the current electricity production and diversification of energy sources with the use of renewable energy. Concessionary contracts for the construction of hydropower signed by the Government in the 2007-2009 with foreign companies provide for about €1.3 billion of investments spread out across the next five years.

In recent years, a process of restructuring through privatization of the distribution company and the implementation of PPP projects has been implemented to increase the production of energy and facilitate investments in the transmission system. The signed concession contracts stipulate that 264 plants will be built with total installed capacity of about 1055 MW and average annual production of electricity of 4.5 billion kWh. There are also two projects implemented for the construction of interconnection lines, and one for a new overhead transmission line. The realization of these concessionary contracts and other projects underway will make it possible for Albania not only to meet domestic demand for stable energy but also to become an exporter of electricity. Another successful concession project is the fuel terminal, an investment of the Albanian-Italian Petrolifera in the value of €57 million, which was inaugurated in June 2009 in Vlora.

One of the most successful concessions is that for Tirana International Airport which is operated by a consortium of Hochtief Airport, Deutsche Investitions- und Entwicklungsgesellschaft mbH and Albanian-American Enterprise Fund in a Build-Own-Operate-Transfer (BOOT) contract for duration of 20 years. In 2009, the airport served 1.4 million passengers, 180% more than in 2005.

In the petroleum industry, the Government has hydrocarbon agreements in force for existing wells and exploration blocks with the companies Medoil (United Kingdom), Island Rockall, DWM Petroleum (Switzerland), Bankers Petroleum (Canada), Albania Stream Petroleum Ltd (Canada), and Sherwood. Recently it also pursued the preparation of two new such agreements with the company Iec Visoka, for the Visokë platform, and the company DWM Petroleum AG for blocks 2 and 3 of underground exploration.

Incentives to investors

Albanian legislation does not provide specific incentives for foreign investors. Foreign companies as well as domestic ones benefit in the same way from incentives offered in different laws. Incentives are regulated by Law No. 9374, dated 21 April 2005, on state assistance, and amended by Law No. 10183, dated 20 October 2009, on the implementation of important projects. The law on state assistance is valid for all production and service sectors and all measures undertaken by the national and local governments, as well as by other subjects acting on behalf of the state, and benefits all enterprises, except for those in agriculture and the fishing sector. Incentives provided include the following:

- Investors that build plants for the production of energy with an installed capacity of over 5 MW, through the use of liquid or hard burning means as well as investors who rehabilitate existing plants, may benefit from the exemption of the customs tax on imported machineries and equipment used for capital investments. Such investors may also be

reimbursed on the customs and excise tax they paid for the import of the fuel, used to produce energy (Law No. 8987, dated 24 February 2002 “On the creation of facilitating conditions, regarding the establishment of new plants for the production of energy”);

- Importers of machinery and equipment may benefit from postponement of VAT payment for up to one year if machinery and equipment are used entirely for the importer’s economic activity taxable by Law No. 9856, on some amendments to the law on the value added tax, dated 26 December 2007.

B. Upcoming measures for improving the business environment.

Albinvest reform

To adapt the activity of Albinvest to contemporary developments and the Government’s goals, a restructuring reform is under way in its structure that will also include a review of its functions. Albinvest up to now has been a promotion agency for the country’s image and attracting foreign and domestic investors. According to the OECD Investment Reform Index 2010, Albania will need to focus on improving services to investors in both the pre- and post-establishment phase. The report recommends the agency to function as a one-stop-shop for inward investors to ensure faster and efficient services to foreign investors but also to facilitate coordination among different government institutions. Recently a new law, No. 10303, dated 15 July 2010, approved by the Albanian parliament establishes AIDA (Albanian Investment Development Agency), which is designated as the national investment promotion agency (IPA) and will therefore be a key player in the attraction of FDI into the country. According to the law, the Government of Albania has assigned the following tasks to the agency:

- a) to facilitate and support direct investment in Albania, through the identification and promotion of investment opportunities, offering services and support to existing or potential investors;
- b) increase the competitiveness of small and medium-sized enterprises, enabling the renewal and improvement of products and services and the technology they use, offering mechanisms to increase their technical capacity and skills renovation;
- c) to promote and support exports of goods and services by providing support services and providing financial assistance to exporting companies, and export promotion.

The agency, in view of its operations, will conduct all activities and takes all necessary initiatives to support private sector development and improve the business climate and helping private companies at all stages of their economic activity, as well as intermediating with investors and state authorities. Special attention will be given to redressing shortcomings in monitoring and assessment of investment projects, managing relations with clients, and services provided after the establishment of foreign investors, among others.

Administrative court

A proposal to establish an administrative court is expected to be approved by parliament soon. The court is expected to speed up the administrative process. The aim is to

speed up procedures related to appeals by business and strengthen arrangements for the fulfilment of contracts.

Fostering entrepreneurship and innovation

In its strategic plans, the Government has devoted special attention to programmes for increasing the competitiveness of SMEs, based on an action plans regarding entrepreneurship and technology transfer and innovation. Currently the Government is taking steps to improve conditions for promoting entrepreneurship and fostering competitiveness of the economy. Reforms have improved the arrangements for the registration of enterprises through the National Business Registering Centre, the issuance of licenses through the National Centre of Licensing, and inspection reform, reducing the number of inspectorates. The reform of the tax system has led to a lower and more transparent taxation system.

The Business Innovation and Technology Strategy – which is in the approval process by the Council of Ministers – sets the framework for the creation of institutions and competitive industries and for the development of skills able to absorb and use imported technology and undertake authentic technological innovation. In addition, a Business Relay Innovation Centre (BRIC) will be established. The centre will assist local businesses to increase their managerial capacity, build advanced information systems and technological modelling, enhance performance and communication with internal and external markets, select the most appropriate technology, and ensure more efficient strategies, sustainability and productivity of their businesses.

Albania participates in the EU's Competitiveness and Innovation Programme (CIP). Within CIP there are three main sub-programmes which are focused on SMEs:

- Entrepreneurship and Innovation Programme (EIP);
- ICT policy support programme; and
- The intelligent energy-Europe programme (IEE).

All of the programmes are open to companies with no distinction between foreign and domestic ownership.

Privatization plans

The privatization of the remaining strategic assets of the State, mainly the assets of the oil company Albpetrol, Albania's minority stake in the fixed telephone operator Albtelecom, and Institute of Insurance (INSIG) are scheduled to take place in late 2010. In the meantime, the consolidation of the privatized companies also needs monitoring. The payment arrears of Albanian Refining & Marketing of Oil (ARMO) may threaten the privatization of Albpetrol and thus the conclusion of the strategic privatization programme (IMF, 2010).

International cooperation and assistance

Albania's efforts to strengthen the institutional arrangements and measures for promoting FDI are supplemented by cooperation and technical assistance from international organizations such as EC, UNDP, World Bank/FIAS, UNCTAD etc. One such successful initiative includes the "lead generation" exercises organized by Albinvest with support from the EC-UNDP Trade Liberalization and Promotion Project, which targeted potential investors and provided them with relevant information. Its role is illustrated by the following observation by Alberto D'Amica, General Manager of Teleperformance Albania, which opened an office in Tirana in November 2006 and which now provides 1,000 jobs per year:

“The decision to invest in Albania had already been taken at that time, since the company needed to delocalize urgently to meet corporate requirements but Albanian FDI targeting missions (organized with representatives of the Italian call centers in Rome and Tirana in June and September 2006 on the occasion of lead generation exercises in the services sector, organized with the support of the EC-UNDP Trade Liberalization and Promotion project, did a good job at presenting Albania’s opportunities in terms of taxes and overall country stability and played an important role in dissolving any remaining perplexity on the country”.

3. Specific investment sectors identified and promoted by the Government of Albania

A number of sectors and industries have been identified by the Government of Albania as areas for promoting foreign investment. They include:

Business services. Albania offers good opportunities for four types of export-oriented foreign investment in business services : customer support centres, data processing joint service centres, IT services and business regional headquarters. The best opportunities for attracting investment are in the first two activities (customer support centres and data processing) based on several competitive advantages, such as (i) qualified labour force with knowledge of foreign languages, (ii) labour costs at one fifth of the West European average, and (iii) availability of adequate office premises.

Agriculture and agro-business. Albania has considerable opportunities for developing its agriculture based on its favourable climate and inexpensive labour force in rural areas. Due to still traditional methods of fruit, vegetable growing and animal husbandry using little artificial feed additives, pesticides and chemicals, Albania is already known as a producer and exporter of organic products. Investment opportunities exist in several sub-sectors of the agro-food industry, the most promising segments being those that have exporting potential such as medicinal plants, vegetables, canned products such as olives or olive oil, fresh and processed fish, etc.

Mining. Albania has considerable mineral resources including chromium, copper, nickel and coal. Extraction industries are in private hands and, as a result, there are opportunities for Greenfield investments in the sector. New investment opportunities can also be offered by concession agreements.

Oil and gas. Hydrocarbons comprise 62% of the Albanian energy balance. Local and international companies operate in the sector, in activities ranging from exploration and production to sale and marketing of oil and gas products. The privatization process in the hydrocarbon sector is under way. It is expected to ensure greater efficiency in production, refining and sale.

Tourism. Albania has considerable natural tourist resources. The coastline is 450 km long and has some of the cleanest and most beautiful coastal areas in the Northern Mediterranean. Still foreign investment in tourism is very low. FDI in tourism is expected to assist to develop the industry and will encourage the development of infrastructure in touristic areas.

The activities listed above are also the strategic areas identified in the Regional Strategic Framework of the USAID and of the Western Balkans Sector Competitiveness Project initiated by the Investment Compact for South-East Europe (recommendations of June

2009). Both these initiatives as well as the Albanian Government exclude manufacturing industries as targets for FDI in Albania due to lack of tradition and experience in manufacturing in the country. However, some existing FDI projects reveal that there is scope for development in this sector, particularly for domestic-oriented products. However, human capital development is necessary in order for Albania to attract increased investment in any of these sectors.

C. Assessment of the institutional and legal environment in Albania: results of an FDI perception survey

The opinion/perception survey of foreign investors active in Albania regarding the policy framework has been undertaken in June-July 2010 by FIAA (Foreign Investor Association in Albania) and UNDP Albania, under One Un support to FDI Project (box III.1)

Box III.1. Characteristics of the survey on the FDI perception about the policy framework in Albania

The research team obtained 80 responses from a non-representative sample of foreign investment enterprises. The survey covered about 13% of the foreign affiliates in the country. There are some structural discrepancies between the sample and the population of foreign affiliates in the country. Compared with the database of INSTAT referred to earlier (chapter I), the survey under-represents the foreign-owned companies in manufacturing and over-represents those in services. However, the share of manufacturing in output is much lower than in terms of the number of enterprises thus the higher representation of these companies in the survey is justified by their importance in the Albanian economy. The regional distribution of the sample firms is very similar to that of foreign affiliates in the INSTAT database. There were at least 75 valid responses obtained for each question of the survey. The main characteristics of the respondent firms are the following:

- more than half of the responding firms were established before 2003, and the rest are of more recent origin;
- 59% of the responding companies were established as greenfield investments, 24% were established by privatization and the rest of them as brown-field investments;
- mainly 90% of all respondents are majority foreign-owned;
- with respect to foreign ownership, 15 companies (19%) are Greek, 13 (17%) are Italian and five (6%) are from Austria; the rest were established by parent companies from 21 different countries;
- as regards the main economic activities, 34% of the respondents are operating in manufacturing (half of them in textiles and clothing), 21% in mining, energy and construction, and the remaining 45% in other services;
- only one quarter of the companies have more than 250 employees; the rest are SMEs, especially medium-size companies (33%) with employment between 50 and 250 persons;
- most of the companies have been growing in recent years, 71% have more employees in 2009 than in 2007 and 76% have higher turnover;
- prospects for the future are optimistic, 61% of the companies expect an increase of employment in the next two years while only 13% expect a decrease (the rest plan to maintain the level of employment);
- there is a clear difference between exporting and non-exporting firms: 46% do not export at all, while 29% export more than half of their output;
- 62% of the companies are based in Tirana, the rest spread all over the country.

Source: FIAA/UNDP Albania survey on foreign investment enterprises.

The foreign investors surveyed give a positive overall assessment of the appropriateness of economic policies – 72% find them appropriate or very appropriate. Such a high level of overall satisfaction is not, however, in line with response rates to similar questions in individual areas of policy and with the modest World Bank doing-business indicators for the country. The explanation may be that there is a tendency that the more successful the company is, the more it responds to this types of survey.

The questionnaire tested the satisfaction of foreign affiliates with regard to nine legislative areas (figure III.2). A high proportion of respondents (70%) expressed satisfaction with the tax burden and the employment law. These factors comprise basic conditions for the success of the investors. A high proportion of investors also expressed satisfaction with the social security system and low related costs for employers. Dissatisfaction is often expressed with the *implementation of laws, tax collection, VAT reimbursement and bureaucracy in general*.

Nearly a third of respondents expressed dissatisfaction with the Government's support programmes, both the structure and access to the support programmes. It seems that the liberal environment alone does not satisfy the companies and they call for some real incentives.

Another set of questions asked companies about the main obstacles they face. The answers reveal that three quarters of the foreign investors can rely on adequate financing and find enough workforces for their activities. The biggest problem identified is that more than half of them do not find people with the adequate skills. This can be translated into a need for better education and vocational training. Labour offices are considered as almost useless by most of the foreign companies. They provide access to labour force in quantity, but not at all in quality.

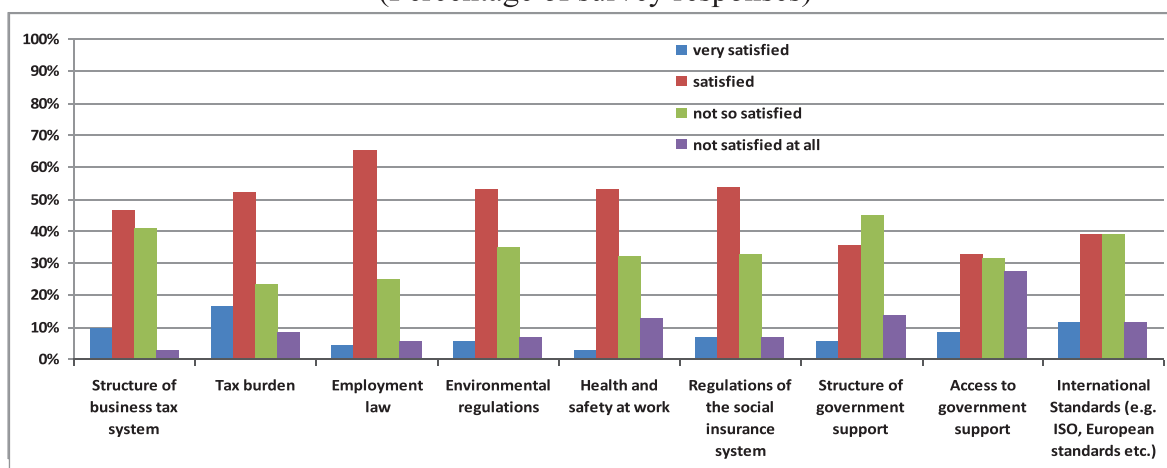
Another problem area identified is general economic uncertainty, which may be related both to regulatory conditions and market conditions. Market access was found more satisfactory than interaction with authorities. Cumbersome communication with authorities was also mentioned in the written comments.

The guarantee of access to real estate does not function properly in practice. Especially outside the capital city, it is difficult to register and obtain guarantee of property rights. A similar problem emerges with licences that are cumbersome for foreign firms to obtain, while some local competitors acquire fake licences.

The responses show that the activity of foreign investors is usually based on strategic development plans. Most of the enterprises are at least occasionally involved in R&D projects. Of those companies involved in R&D projects 48% do this in cooperation with other companies or organizations. More than one third of them cooperate with universities. These indicators provide some proof of technology transfer.

Trade and networking relations are characterized by a predominance of imported inputs and domestic sales of output. This is a suggestive proof of the local market orientation of the companies and rare export orientation mentioned above. But export orientation certainly differs for the individual economic activities.

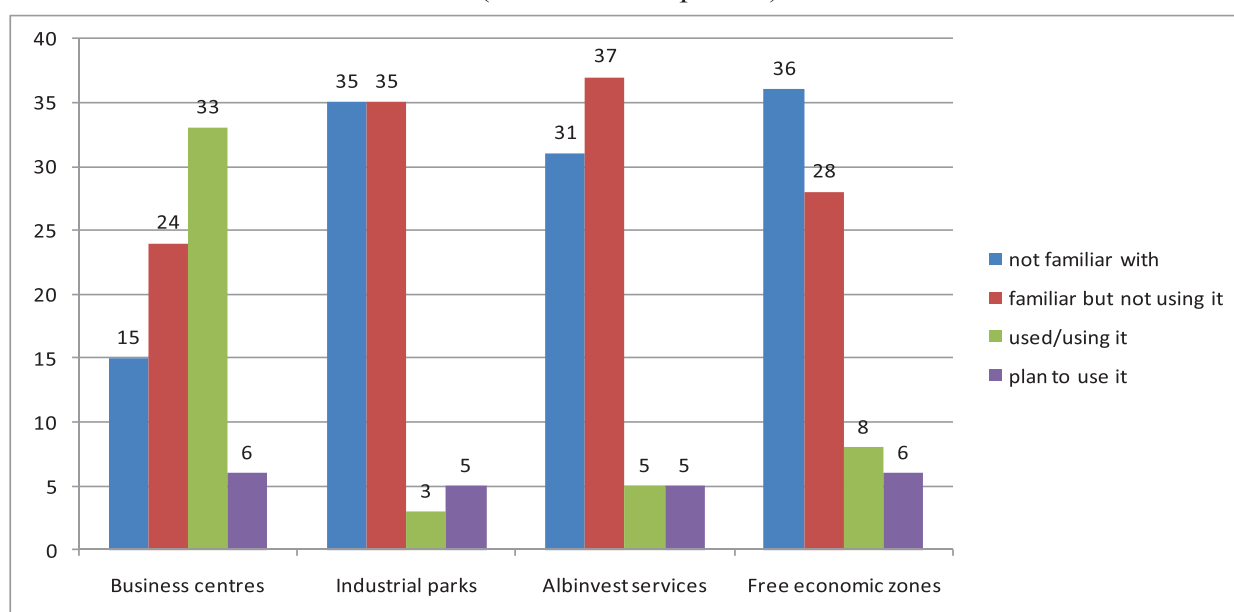
Figure III.2. Foreign affiliates' satisfaction with the legal framework for business in Albania
(Percentage of survey responses)



Source: FIAA/UNDP Albania survey on foreign investment enterprises.

Government support is expected in the form of support structures like business centres, industrial parks, Albinvest services, and free economic zones. Business centres are more familiar to the respondent companies than the other organizations, although respondents identify them with the chambers of commerce. According to the survey, 60-70% of investors are not familiar with other support structures, including the investment promotion agency Albinvest, and most of the firms do not use them (figure III.3).

Figure III.3. Foreign affiliates' familiarity with and use of business support structures
(Number of responses)



Source: FIAA/UNDP Albania survey on foreign investment enterprises.

In sum, the results of the survey give a favourable picture of the Government's activities in supporting the investment and business environment. However there are also important shortcomings mentioned and requests for improvements have been voiced. Such requests have to be treated with care. Companies usually have a mixed attitude towards government policies, especially taxation. On one hand, they are satisfied with low tax rates and the low level of fiscal burden or demand even less. On the other hand, they demand improved public services which need more government spending like better infrastructure, higher skilled workforce, government support, industrial parks, and R&D facilities. It is therefore the Government that can strike a balance between the revenue and the expenditure side of fiscal policy to ensure long-term economic growth.

D. POLICY CONCLUSIONS

Albania has attracted a remarkable amount of FDI inflows in recent years. In key sectors like mining, banking and telecoms, the Albanian economy is dominated by foreign investors. However, the stock of FDI relative to GDP is still lower than in other countries in the region. That suggests that there is room for increased FDI in the country. An improved institutional, administrative and technical framework for FDI, proper targeting and government support are necessary in order to keep the FDI inflow at the 2008-2009 level or higher in the coming years. Privatization has been an important channel to attract FDI into Albania. With privatization almost completed, attracting other types of investments will become a priority.

At the same time, it is important that the types of FDI Albania attracts are those with the potential to benefit the economy. The high share of FDI in certain industries of the country is partly a sign of weaknesses in the domestically-owned part of these industries. This can be a problem, as an underdeveloped local SME sector usually hinders employment and could be responsible for high imports. The labour productivity gap between foreign affiliates and domestic companies is relatively small in the manufacturing industries pointing to a relatively low technological level of foreign affiliates. In the telecommunications sector there are some bottlenecks in main-line telephony which may hinder the development of online services. As to the services of the banking system, which is now largely foreign-owned, risk premiums on the loans to SMEs are high and loan guarantee agencies are necessary to improve the access to financing.

Attracting FDI and increasing competitiveness of domestic companies are vital to sustainable economic development in Albania. FDI policy is part of the policies towards that end. In the past few years, as mentioned in chapter III, important action has been taken towards the improvement of the investment climate through institutional and regulatory reform, increased availability of finance for investment, development of infrastructure, improved conditions for free trade and regional integration.

Further reforms are necessary in the tax administration and customs administration, in land use and construction permits, in the administrative appeal system, the inspection system and e-government. Investors demand steps to improve the implementation of laws, tax collection, VAT reimbursement and a reduction of bureaucracy. Property certification has to be improved and the issuing of all permits simplified. In transparent procedures cause delays for investors and can be a hotbed for corruption.

Investors, including foreign investors, are satisfied with low tax rates and the low level of fiscal burden prevailing in Albania, but they also demand efficient public services which need more government spending. These include better infrastructure, higher skilled workforce, government support, industrial parks, and R&D facilities. The Government must strike a good balance between the two sides of fiscal policy in its attempts to attract and benefit from FDI. While tax rates are a factor in competing for investment flows, fiscal revenues need to be increased to finance public investments and services.

The Government has recognized the important role of infrastructure in promoting FDI and the development of the economy. Some roads and ports have been upgraded, often in public-private-partnership schemes. The concession law has opened the way for PPP projects also in the energy sector, among others, with the aim of increasing the production of electricity.

Deeper regional integration through full implementation of the CEFTA 2006 agreement is necessary to increase the Albanian market share in regional trade, service quality and FDI flows. This is important as in its absence foreign-investment enterprises in Albania find their access to markets inadequate. The local market is small, and the size of freely accessible international markets needs to expand. The cost of exporting from Albania is very high in international comparison.

A special focus needs to be given to improving the knowledge economy and information society within Albania through the introduction and application of information and communication technologies and solutions, and improving educational outcomes.

Specific policies to favour investments in less developed areas must be considered in order to reduce regional development disparities. The creation of industrial parks in specific areas may contribute to attracting new investments in these areas. Investors have expressed their desire to have the industrial parks ready for investment soon.

Investors hardly rely on Albinvest services. The Agency has to be put in a position to serve more investors more efficiently. The Government is working on upgrading the position of Albinvest into a business service provider and a one-stop-shop entry point for foreign investors. A concentration of Albinvest efforts on attracting FDI, in particular greenfield investments can bring future benefits for the country. For such efforts to succeed, it is necessary that not only the position of the investment agency but also its staff and funding be upgraded so as to put the agency in a position to search actively for investors and facilitate their entry. A further task for Albinvest should be to develop aftercare to transmit the needs and problems of established investors to the Government and encourage the reinvestment of profits. In addition, attracting FDI and improving the conditions for it should not be the task of only one government agency, but also of all ministries and of the regional and local administrations.

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