

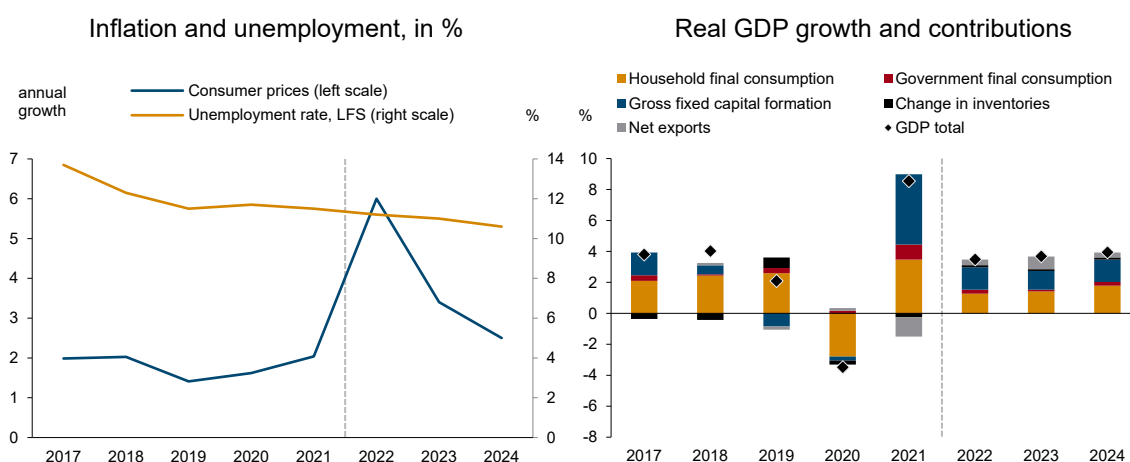


ALBANIA: Price hikes and energy supply issues will hamper growth

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Albania has a low volume of trade with Russia and Ukraine, but it will experience negative spill-overs from the war in Ukraine, on account of its strong trade relations with the EU. Monetary policy has shifted towards higher interest rates, and the government's fiscal stimulus measures will go some way to support consumption. Exports of minerals and fuel have gained momentum; however the country's current account balance will deteriorate. According to the baseline scenario, inflation this year will be 6% and growth 3.5%. In the medium term, inflation will fall to 3% and growth will rise to 3.9%.

Figure 4.1 / Albania: Main macroeconomic indicators



Source: wiiw Annual Database incorporating national and Eurostat statistics, own calculation. Forecasts by wiiw.

The economic recovery in 2021 – at 8.6% – exceeded our expectations; but the rebound will not last. Both government and household consumption grew – by 8% and 4%, respectively – while investment picked up by 21%. The drivers of the economy were the construction and financial sectors (both of which expanded by 21%) and manufacturing (which grew at 15%). External demand bounced back: exports of services reached their pre-pandemic level – thanks to tourism, which almost doubled compared to 2020 - while merchandise exports performed even better. Foreign direct investment surged by 10% between 2020 and 2021, and was worth over EUR 1bn (7% of GDP). However, the good times could not last. The energy crisis (announced by the government in October of last year) and the inflationary pressure (which was already starting to be felt in Q4 2021 and has been exacerbated by the war in Ukraine) will act as a drag on the economy in the short and medium term.

Inflationary pressure will intensify in 2022 and will have several implications. Last year ended with a rapid rise in commodity prices that continued over the first three months of 2022: inflation grew by 3.7% in January and by 3.9% in February, year on year. The prices of food products, especially those which are mainly imported, rose by 10% in February (year on year). Fuel and electricity prices increased by 3.4% in the first two months of the year, and in March, the steep rise in the cost of fuel sparked considerable frustration and led to mass protests. The government intervened by imposing price controls. Two boards have been created to monitor prices and set a price ceiling on fuel and several other goods in the 'consumer basket' (by limiting the profit margins of traders); the level allowed is altered daily or weekly. Accordingly, the country's heavy reliance on imports, the external supply shocks and pessimistic expectations for domestic electricity generation (which is quite volatile and very dependent on the weather) hint at an intensification of the inflationary pressure that this year is expected to hover at around 6%, before falling back to around 2.5% by 2024.

The volume of trade that Albania has with Russia and Ukraine is small, but the country is, to a certain degree, dependent on specific commodity goods. In 2021, imports from Russia and Ukraine did not exceed 2% and 1%, respectively; meanwhile exports to those countries are negligible. However, 41% of all cereals come from Russia. In the first two months of 2022, year-on-year grain imports dropped in both real terms (by 46%) and nominal terms (by 7%). The country is also reliant on imported animal and vegetable fats and oils – 30% comes from Ukraine and Russia. However, Albania is not the only country that relies for these commodities on imports from Ukraine and Russia: the supply shock is also affecting Albania's main trading partners. Thus, the shortages of these products will not be resolved overnight and the inflationary pressure will not be a passing phenomenon.

The rise in consumer prices will depress consumption. Nominal wages have been picking up in both the private and the public sector (by 10% and 6%, respectively), but given the level of inflation, in real terms, the effect is fairly small. In 2021, the employment rate recovered, but has not yet returned to its pre-pandemic levels. Consumer confidence has dropped off and is now below its historical levels: people are pessimistic about their personal finances and their ability to make major purchases, as well as about the economic situation in the country generally. The poverty rate is among the highest in the region: according to the World Bank, a third of all Albanians were living on less than USD 5.50 a day in 2021. The government has introduced a new Social Resilience support package worth EUR 80m to support those at greatest risk of poverty (especially pensioners). In April, the minimum monthly wage was increased from LEK 30,000 to LEK 32,000 (approximately EUR 260). The income tax threshold was also raised – by 33%, to LEK 40,000 (EUR 326) – and the tax payable on salaries of up to LEK 50,000 (EUR 408) has been cut from 13% to 6.5%. Remittances will continue to provide a buffer for consumption, but this year their impact is expected to be lower than during the pandemic. Real wages are falling sharply in the EU – by 3% in Italy and Germany (the countries where most migrants, and especially recent ones, reside). Higher consumer prices are eating away at the income and savings of migrants, meaning they have less money to remit.

The government has responded swiftly, with new fiscal stimuli, but fiscal consolidation will be postponed. The general government budget has been revised and the fiscal deficit is expected to exceed 4%, while public debt will hover at close to 75% of GDP. The new Social Resilience support package has required a further readjustment of spending plans – rise in general government expenditure as well as cuts on capital expenditure. This hints at lower public investment than was initially planned.

The central bank has responded to the inflationary pressure by raising its policy interest rates.

The exchange rate became volatile in March 2022, so that the central bank was forced to intervene. The euro was stabilised at a lower exchange rate than in 2021. The Albanian economy is quite closely linked to the euro, and exchange rate stability depends on external demand and the current account balance. In March 2022, the central bank changed its course of monetary stimulus and the interest rate was adjusted upwards, from 0.5% to 1%. The blow of higher energy prices and the expectation that there will be a further surge in consumer prices could prompt the central bank to increase interest rates again by the end of the year.

The trade deficit is expected to deteriorate further, though the signals are mixed.

Exports of goods and services picked up remarkably in 2021, and in the first two months of 2022 the export of goods rose in both real and nominal terms – by 9% and 49%, respectively, year on year. The greatest contribution was made by exports of minerals, fuel and electricity, output of the garment industry and chemical products. This was due to high prices on the international markets – especially of oil and other energy sources, but also of minerals. Imports rose by 5% in nominal terms and by 27% in real terms, with fuel imports accounting for the largest slice. There are no great expectations from tourism this year: while there have been many visitors from Ukraine and Russia over the past four years, but the war in Ukraine will disrupt travel from those countries. Ethnic tourism and tourism from the neighbouring countries helped the sector during the pandemic, and may also do so now. That said, ballooning prices will erode the real income and savings of this category of tourists as well: this year, they may opt to holiday in their own countries. Consequently, the tourism momentum may weaken.

The energy crisis could have been avoided, had appropriate policies been pursued over the last decade.

The consequences of the energy crisis – which was already announced by the government last October – will have a severe effect on the economy this year. Although Albania is a country rich in natural resources, there are several bottlenecks that prevent the economy from reaping the benefits of them. It is an oil-producing country, and certainly the huge surge in international market prices will be a boon for its exports. But for its own consumption, Albania relies exclusively on fuel imports – at much higher prices. According to Eurostat, the country's energy import dependency in 2020 was 35%. Its supply of electricity is very volatile, as it relies mainly on hydropower stations. The Trans Adriatic Pipeline (TAP) presents a missed opportunity: it delivers gas from Azerbaijan to Italy and crosses through several countries, including 215 km of Albania. However, Albania still does not have access to the gas flowing through the pipeline. Solar panel arrays account for no more than 1% of electricity produced – even though Albania boasts 300 days of sunshine a year. Several projects have tackled this sector, but progress has been very slow. In March 2022, in the face of the energy crisis, the government announced that households and small enterprises could install solar panels and produce electricity for their own consumption. The energy crisis could have been avoided if there had been greater diversification of energy resources.

COVID-19 seems to be the least of the country's concerns. The vaccination rate has reached 43%, restrictions have been greatly relaxed and there is no obligation even to wear a mask. The small number of daily infections (54 at the time of writing) and of COVID-related deaths (under 2 a day since February 2022) make for quite a relaxed attitude to the pandemic.

Overall, we expect the economy to lose vigour. Even on the twin assumptions that the war-related shocks do not extend beyond this year and that inflation does not exceed 6% this year, the economy will grow by no more than 3.5%. In the medium term, we expect international commodity prices to cool off, which will help Albania a bit. In the medium term, inflation will fall to 3%, while growth will rise to 3.9%.

Table 4.1 / Albania: Selected economic indicators

	2018	2019	2020	2021 ¹⁾	2022	2023	2024
					Forecast		
Population, th pers., average	2,866	2,854	2,838	2,829	2,810	2,800	2,800
Gross domestic product, ALL bn, nom.	1,637	1,692	1,644	1,890	2,100	2,300	2,500
annual change in % (real)	4.0	2.1	-3.5	8.5	3.5	3.7	3.9
GDP/capita (EUR at PPP)	9,150	9,520	9,110	10,160	.	.	.
Consumption of households, ALL bn, nom.	1,282	1,340	1,313	1,409	.	.	.
annual change in % (real)	3.1	3.3	-3.5	4.4	1.7	1.9	2.4
Gross fixed capital form., ALL bn, nom.	391	378	374	456	.	.	.
annual change in % (real)	2.3	-3.6	-1.1	19.9	6.0	5.0	6.0
Gross industrial production							
annual change in % (real)	18.7	-1.1	-6.3	26.6	5.0	8.0	8.0
Gross agricultural production ²⁾							
annual change in % (real)	1.8	-2.9	3.0	2.0	.	.	.
Construction output total							
annual change in % (real)	5.6	-2.5	9.5	18.0	.	.	.
Employed persons, LFS, th, average	1,231	1,266	1,243	1,249	1,267	1,275	1,280
annual change in %	3.0	2.8	-1.8	0.4	1.5	0.6	0.4
Unemployed persons, LFS, th, average	173	165	165	163	160	160	150
Unemployment rate, LFS, in %, average	12.3	11.5	11.7	11.5	11.2	11.0	10.6
Reg. unemployment rate, in %, eop	5.4	5.8	7.4	6.0	.	.	.
Average monthly gross wages, ALL	50,589	52,380	53,662	57,182	64,300	69,800	75,100
annual change in % (real, gross)	1.3	2.1	0.8	4.4	6.0	5.0	5.0
Consumer prices, % p.a.	2.0	1.4	1.6	2.0	6.0	3.4	2.5
Producer prices in industry, % p.a.	1.7	-0.8	-3.3	2.7	4.5	3.0	1.7
General governm. budget, nat. def., % of GDP							
Revenues	27.5	27.2	25.9	27.0	27.0	27.5	28.0
Expenditures	29.1	29.1	32.6	31.5	31.6	30.5	30.0
Deficit (-) / surplus (+)	-1.6	-1.9	-6.7	-4.5	-4.6	-3.0	-2.0
General gov. gross debt, nat. def., % of GDP	67.7	65.8	74.5	73.2	75.0	74.0	73.0
Stock of loans of non-fin. private sector, % p.a.	-3.6	6.6	6.9	9.6	.	.	.
Non-performing loans (NPL), in %, eop	11.1	8.4	8.1	5.7	.	.	.
Central bank policy rate, % p.a., eop ³⁾	1.00	1.00	0.50	0.50	1.0	1.2	1.2
Current account, EUR m	-866	-1,089	-1,153	-1,186	-1,390	-1,360	-1,350
Current account, % of GDP	-6.8	-7.9	-8.7	-7.7	-8.1	-7.3	-6.7
Exports of goods, BOP, EUR m	986	907	794	1,265	1,450	1,520	1,580
annual change in %	23.7	-8.1	-12.5	59.4	15.0	5.0	4.0
Imports of goods, BOP, EUR m	3,857	4,050	3,776	5,094	5,650	5,820	6,030
annual change in %	6.5	5.0	-6.8	34.9	11.0	3.0	3.6
Exports of services, BOP, EUR m	3,073	3,405	2,226	3,466	3,810	4,080	4,370
annual change in %	7.6	10.8	-34.6	55.7	10.0	7.0	7.0
Imports of services, BOP, EUR m	1,962	2,141	1,174	1,690	1,890	1,970	2,070
annual change in %	10.6	9.1	-45.1	43.9	12.0	4.0	5.0
FDI liabilities, EUR m	1,020	1,072	937	1,032	.	.	.
FDI assets, EUR m	-3	36	43	42	.	.	.
Gross reserves of CB excl. gold, EUR m	3,342	3,240	3,806	4,831	.	.	.
Gross external debt, EUR m	8,353	8,246	8,548	9,740	10,400	10,800	11,300
Gross external debt, % of GDP	65.1	60.0	64.3	63.1	61.0	58.0	56.0
Average exchange rate ALL/EUR	127.59	123.01	123.77	122.46	123.1	124.0	124.0

1) Preliminary and wiiw estimates. - 2) Based on UN-FAO data, wiiw estimate from 2020. - 3) One-week repo rate.

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