

## **Gent Sejko: Albania's economic and financial developments in 2023**

Address by Mr Gent Sejko, Governor of the Bank of Albania, to the Assembly of the Republic of Albania presenting the Annual Report of the Bank of Albania for 2023, Tirana, 18 July 2024.

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Honourable Speaker,

Honourable Members of Parliament,

Allow me at the beginning of the regular presentation of the Bank of Albania Annual Report for 2023, to re-affirm the high consideration that the Bank of Albania and personally have regarding accountability and the dialogue with parliament.

Traditionally, this presentation aims to present to the Assembly a complete and faithful overview of our opinion on economic and financial developments over the past year, the measures taken by the Bank of Albania in fulfilling its legal mission and duties, and to provide an assessment of their impact.

Dear Members of Parliament,

In 2023, Albanian economy has consolidated the positive development trends, both in terms of growth and improving the country's main economic and financial balances.

Despite a difficult and challenging external environment, the volume of economic activity in Albania continued to grow, generating higher income for Albanian businesses and households. According to INSTAT data, the volume of economic activity in Albania grew by 3.5% over the past year. In parallel, employment and average wage in private sector rose by 2.2% and 13%, respectively, while unemployment rate fell to the new historical minimum of 10.7%. The expansion in family consumption, private investments and in the export of tourism services underpinned the economic growth, while fiscal policy maintained the consolidation trend. From the macroeconomic perspective, economic growth reflected the sound financial balance sheets of private sector, the gradual improvement in businesses and households' confidence, the expansion in bank credit, inflation coming down, and the rapid growth in the income from tourism.

The surge in the demand for goods and services did not harm the downward trend of inflation. In contrary, over 2023, this indicator fell gradually to 4% as at end of 2023, from 7.4% at the beginning of year. The decline in inflation in international markets, the strengthening of the exchange rate, and the normalisation of the monetary policy stance affected this performance. The decline in inflation and its progressive approach towards the target helped preserving the value of households' income and savings, supported the smooth functioning of financial markets and backed the strengthening of macroeconomic stability in Albania.

In parallel, the domestic and external balances of our economy improved in 2023. In particular as following:

- First, the improvement in the external position of Albania, reflected in a rapid fall of the current account deficit. This deficit dropped to 0.9% of GDP over 2023, recording a historical minimum of the post-transition period. Also, external debt dropped below the level 50% of GDP, while the level of foreign exchange reserves of the Bank of Albania grew, in turn improving our ability to respond to both domestic and external shocks. The increase by EUR 1.7 billion in the Albanian exports over the past year, coupled with the immediate growth in foreign direct investments - which reached a new historical record of EUR 1.1 billion – led to these improvements.
- Second, the improved fiscal position of Albania, being reflected in the reduced budgeted deficit and public debt, at 1.4% and 58.9% of GDP, respectively, the minimum levels for more than a decade. The decreased public debt increases fiscal spaces for reaction against potential shocks in the future, as well as decreases risk premia and financing costs for all economic operators.
- Third, the sustainability of the banking sector, being reflected in the improved indicators of capitalization, profitability, as well as of the loan portfolio quality. The non-performing loans ratio stood at 4.8%. These positive trends enable the banking sector to supply - efficiently and continuously - the Albanian economy with financial funds as well as with payment and saving instruments.

The Albanian economy, in a longer-term perspective, has displayed an admirable degree of resilience and flexibility in face of the huge challenges experienced in recent years. Among others, this fact was reflected in the improved risk ranking of the country's public debt by foreign rating agencies, now at BB-, according to Standard & Poors, as well as in the increased interest of international operators to invest in Albania, both in real economy and financial market.

Honourable Members of Parliament,

The positive development momentum of the country is attributable - first - to the resilience, flexibility and dynamism of the private sector. In addition, this positive developing momentum, reflects our prudential monetary policy, our supervisory, regulatory and macro-prudential measures, as well as the continuous work we have carried out for the advancement and modernization of payment systems. In more concrete terms, the prudential normalisation of the monetary policy stance, first enabled to keep inflation under control and further its continuous reduction, at minimum costs on the economic activity and financial stability of Albania. Also, our rigorous micro and macro-prudential measures strengthened the stability of the banking system, while the continuous alignment of our regulations with the European Union standards led to a considerable regulatory convergence, by reducing financial risk premia in Albania. Last, the ongoing advancement regarding the infrastructure and regulatory basis of payment systems has driven up financial inclusion and has helped efficiency and formalisation of private sector edging up.

Next, I will delineate in more concrete terms the main aspects of our work over the past year, by evidencing the undertaken measures and the achieved outcomes.

## **Monetary policy and price stability**

The monetary policy of the Bank of Albania has continued to be oriented towards the fulfilment of our legal objective: achieving and maintaining price stability. In this context, I would like to highlight that still high and above-target inflation rates dictated the continuation of a normalising monetary policy over 2023.

Nevertheless, we have tried to implement a more flexible monetary policy, aiming not to undermine the positive development trends of Albania and by taking care to harmonize it with the financial developments and the fiscal policy stance. In this context, allow me to focus on two important conclusions:

- First, the normalisation pace of monetary policy slowed down over the course of 2023. In this year, we have increased the policy rate only twice, with a cumulative effect of 0.5 percentage point.

This slowdown reflected the exchange rate strengthening and the consolidation stance of fiscal policy. In more concrete terms, rapid lek appreciation helped in mitigating imported inflationary pressures, while fiscal consolidation helped in curbing domestic inflationary pressures.

In particular, lek strengthening has been and continues to be one of the most prominent economic developments of this period by providing an entirely positive impact on the economy. It contributed to keep inflation under control, by enhancing the purchasing power of Albanian households, as well as enabling a more gradual normalisation of our monetary policy stance, by keeping financing costs to businesses low. Consequently, Albania has one of the highest economic growth rates, the lowest inflation rate and the slowest increase in financing costs, across regional countries.

- Second, the increase in policy rate engendered an overall hike in interest rates in the country, though the overall financing conditions in Albania still remain simulating.

In response to them coupled with the positive approach of banks, credit portfolio to private sector grew steadily and rapidly over 2023, presently standing at 14%. Growth in lending was characterised by certain positive features: i) new loans were broadly-based by sector; ii) it was concentrated in our national currency; iii) it showed an increasing orientation towards investment financing, and did not jeopardise the overall quality of credit portfolio. All the three features have continued and further strengthened during 2024.

Inflation and expectations on inflation, as a result of this reaction, stay already close to our 3% target, while forecasts for the future are positive.

## **Banking supervision and financial stability**

The increase in interest rates and higher uncertainties experienced over the past two years in Albania and worldwide, have created a challenging environment to banking activity and financial stability. Nevertheless, our banking system and financial stability in Albania appear solid. In particular, the Albanian banking sector closed 2023 with a

positive financial result, a high liquidity and capitalisation level, and a further improved credit quality. Our analyses show that systemic risks to banking sector remain contained.

In particular, two important achievements were recorded by the Albanian financial sector last year.

- First, the removal of Albania from FATF' list of jurisdictions under increased monitoring, regarding the development of infrastructure for anti-money laundering and counter-terrorism financing, known as "grey list", constitutes the pivotal point of the reforms undertaken by the Albanian institutions, including the Bank of Albania, to fulfil the necessary criteria. Albania taken off FATF grey list marks an important achievement for our country, the economy and the reputation of Albania, as it is a demonstration of trust by the international community on the Albania's dedication against money laundering and combating terrorist financing.
- Second, upon the delisting from the "grey list", the Bank of Albania has started the procedures to receive the equivalence status of our supervision and regulatory framework with the European Union standards. Our preliminary assessments suggest a level of convergence of approximately 90% with these standards. Therefore, we have submitted the official request to the European Banking Authority (EBA), and we are expecting to start our discussions on the equivalence assessment process for Albania. This equivalence assessment will enable the increase of lending to economy from the European commercial banks that conduct their activity in Albania.

The resilience, sustainability and flexibility of the financial system against the recent challenges reflect a supervision, which is both meticulous and efficient, as well as the structural reforms undertaken by the Bank of Albania. In particular, the continuous investment made over the years has strengthened the resilience of the banking sector against shocks and has enabled it to continue to meet the demands for funds of the economy.

In 2023, we have been working on the following:

- First, the Bank of Albania has improved its supervisory and regulatory framework, aimed at its approximation with the EU Acquis and Basel principles.
- Second, the approval of the Law "On payment accounts with basic features" by the Assembly of the Republic of Albania, which was drafted by the Bank of Albania with the assistance of the World Bank, and the regulation approved by the Bank of Albania "On the comparability of the fees related to payment accounts and payment account switching", enable the consumer to access the bank basic services, despite their employment status and financial situation.
- Third, the Bank of Albania drafted the document on the banking sector financial reporting, which is the first step for implementing the international standards on financial reporting and accounting.
- Fourth, we have compiled and adopted the Strategy on "Management and Supervision of Climate-Related Risks in the Financial Sector", in collaboration with the World Bank.
- Fifth, the Bank of Albania has continued monitoring the activity of banking sector, through on-site inspections and off-site analyses. Examinations has focused on

monitoring the completion of the regulatory requirements on capital, the assessment of governance systems and culture, the assessment of risk management regarding: capital and market risk; operational risks, information technology risks, liquidity risks, as well as the assessment of transparency with clients.

- Last, the Bank of Albania has continued the further enhancement of its resolution ability, alongside with its primary role in safeguarding the monetary and financial stability of Albania. In addition, the Bank of Albania carries out various activities which are crucial in bolstering the development and growth of the overall well-being of the society. Below, I will list briefly some of them.

The Bank of Albania assures the smooth operation of payment systems. In particular, the new payment system for the settlement of interbank customer payment orders in euro, within the territory of the Republic of Albania – AIPS EURO, since the start of its operation in January 2022, saved to the Albanian households and businesses EUR 50 million in the form of lower fees and commissions on payments. These savings amounted EUR 37 million only in 2023. The development of payment infrastructure has supported the expanded use of electronic payments and the increased financial inclusion of citizens. The use of electronic payments reached 21 payments per capita, recording an increase of 25.5% of payments via cards, payments via electronic money and of home banking payments.

In 2023, we started our work for participation in the Single Euro Payments Area (SEPA), an integral part of the Growth Plan for the Western Balkans, drafted by the European Commission. This process culminated in 2024, with the submission of the official application to European Authorities to be an integral part of this system. In parallel, we have taken important steps to develop new payment systems such as instant payments. This system enables electronic payments of small value, safely, at any point of the day and at an almost immediate time. For the development and implementation of such a system according to the model of TARGET Instant Payment Settlement (TIPS) in euro area, the Bank of Albania is actively supported by the Bank of Italy.

Also, the Bank of Albania has fulfilled the institutional obligations under the Stabilization and Association Agreement, the Progress Reports of the European Commission, joint EU-Albania sub-committees and the National Plan for European Integration. The Bank of Albania has provided its active contribution in bilateral meetings regarding the relevant chapters of the Acquis taking place between the Albanian delegation and the representatives of the European Commission. In this regard, we have chaired the drafting of chapters 4 and 17, related to the "Free movement of capital" and "Economic and monetary policy".

In parallel, we have: managed the foreign exchange reserve; worked to further develop and improve statistics; met the needs of the economy for cash; and worked to further improve the financial communication and education of public. In this regard, allow me to emphasise the approval in the past year of the Bank of Albania's Strategy on Financial Education and Inclusion. This strategy is the first document that promotes financial education in Albania.

**Honourable Members of Parliament,**

The activity of the Bank of Albania has been and will remain focused on three main pillars:

- Strengthening the monetary and financial stability of Albania, as a key precondition for the sustainable and long-term growth and for improving the well-being of society;
- Fulfilling all our institutional commitments, aimed at being a development promoter of the financial industry and a reliable institutional partner for the advancement of the structural reforms agenda; as well as
- Meeting all the recommendations addressed by the Albanian Parliament.

Allow me to conclude this presentation by assuring you that this philosophy will continue to guide our work throughout 2024.

**Thank you!**