



REPUBLIC OF ALBANIA

ECONOMIC AND FISCAL PROGRAM

2007 - 2010

November 2007

CONTENTS

INTRODUCTION	4
1. LATEST ECONOMIC DEVELOPMENT AND MACROECONOMIC FRAMEWORK	6
1.1. Latest economic development	6
1. 2. Medium Term Macroeconomic Scenario	12
1.2.1. Real Sector	12
1.2.2. Inflation	18
1.2.3. Monetary policy and exchange rate	19
1.2.4. External Sector	20
2. PUBLIC FINANCES	22
2.1. Total Balance of Government and Debt	22
2.1.1. Strategy of Policies and medium term objectives	22
2.1.2. Present Balance and Medium Term Perspective	27
2.1.3. Levels of Debt Development	30
2.2. Quality of Public Finances	36
2.3. Institutional Characteristics in the Public Finances	39
3. STRUCTURAL REFORM OBJECTIVES	45
3.1. Sector of Enterprises	45
3.1.1. Development of Enterprises of Private Sector	45
3.1.2. Policies Launched for the Development of Private Sector	46
3.1.3. Regulatory Reform for Improving the Business Climate	50
3.1.4. Progress of Privatisations in Strategic Sectors	54
3.1.5 Competition Policy	56
3.1.6. Policies in the Sector of Public Procurement	57
3.2. Financial Sector	60
3.3. Labour Market	61
3.4. Administrative Reform	83
3.5. Additional field of reform	91
ANNEX 1: TABLES CONTAINED IN THE ECONOMIC AND FISCAL PROGRAM AND SUBSEQUENT UPDATING	94
Table: Macroeconomic perspectives	94
Table 1b: Developments of prices	95
Table 1c: Development in labour market	95
Table 1d: Sector balances	96
Table 2: General budget developments	97
Table 3: Budget expenses according to functions	98
Table 4: General government debt developments	99
Table 5: Deviation from preceding program	100

Table 6: Basic assumption on external economic environment on which PEF 2007 framework is based	101
ANNEX 2	103
MATRIX OF POLICY COMMITMENTS	103
ANNEX 3	104
ASSUMPTIONS ON THE EXTERNAL ECONOMIC ENVIRONMENT BASED ON SPRING 2007 FORECASTS.....	104

TABLES

Table 1: Increase in % of sales	7
Table 2: Contribution of aggregate expenses in real increase rate	15
Table 3: Contribution of sectors in the real growth rate	17
Table 4: Budget revenues, 2006-2010.....	26
Table 5: Budget deficit and its financing for years 2006 – 2010 \f D \f.....	27
Table 6: Expenses of Local Government 2006 – 2010	28
Table 7: Characteristics of debt.....	30
Table 9: Indicators of the debt service.....	32
Table 12: Funds foreseen for the employment policies	74
Table 13: Indicators of developments in labour market	75
Table 14: Number of contributors and expenses for social insurance.....	81

INTRODUCTION

Since 2006, the potential candidate countries for acceding the European Union, among which also Albania, submit, in the framework of the deepened economic cooperation program with European Union, a medium-term Economic and Fiscal Program. This program is one of the most important documents including the working out of the economic, fiscal policies and structural reforms in medium term perspective, and prepares the institutional and analytical capacities for the participation in the economic and monetary surveillance procedures of European Union.

Even this year, in the letter dated 27 June 2007 of European Commission, the community party has required the continuation of the process instituted with the drafting of the medium term Economic and Fiscal Program (PFE), considering this experience as a platform for dialogue. Thus, Albania participates for the second time in the deepened Economic Cooperation Program with European Union and, in the framework of this cooperation, Albania should submit to the European Commission this medium term Program every year.

The Economic and Fiscal Program (PFE) 2007 is a document drafted by the Albanian Government, reflecting a description of the economic and financial situation in Albania and efficiency of economic and fiscal reform launched during 2007. This document reflects clear information on the economic policies and medium term priorities of the country in the framework of the structural reforms which are foreseen to be implemented during 2008 – 2010, which aim at further strengthening the macroeconomic consolidation and ensuring a high economic growth, as well as setting up a regulatory framework and sector policies in accordance with the European standards.

The Economic program forwarded in this document for the period 2007 – 2010 has been based on the Program of Government 2006 – 2009, on the Medium Term Budget Program 2008 – 2010, on the Sector Strategy for Public Finances (SSEP) 2007 – 2013. At the same time the economic and fiscal program for the three year period shall be in full compliance with the National Strategy for Development and Integration (SKZHI). The medium term economic and fiscal policy is in full compliance even with the policies of the program supported by the three year agreement PRGJ/EFF financed by IMF.

The document PFE 2007 – 2010 lays out the main priorities of the Albanian economy. *In the first chapter*, there is described the current situation of the economic development of the real, monetary, fiscal and foreign sector. *In the second chapter*, there is described the medium term sector of the economy divided into three parts, dealing with the forecasts with regard to the real sector, connected to the level of inflation, connected to the monetary sector and exchange rate and that of the foreign sector. *In the third chapter*, there is described in detail the medium term framework of the public finances. This chapter starts with a short description of the relations existing among the different levels of governance and their development in the upcoming years. This chapter pays specific attention to the description of the income and budget expenses for the medium term period as well as a treatment of the public debt strategy. The chapter ends with the sources of financing of the deficit and fiscal risks which might be encountered by the economy in the medium term period. At the same time, this chapter deals with the most

important structural reforms which shall be undertaken by the Government of Albania in the field of entrepreneurship, competition, reforms or absorption of the foreign investments, privatisation of strategic sectors, financial sector, labour market and administrative reforms.

The implementation of the economic reforms and structural reforms provided for in PFE 2007 shall ensure an economic growth and faster and safer economic and social development; it will support the absorption of the foreign investment; it shall boost the competing capabilities of our economy, thus ensuring a higher standard towards a faster and more European convergence.

1. LATEST ECONOMIC DEVELOPMENT AND MACROECONOMIC FRAMEWORK

1.1. Latest economic development

Developments in the Albanian economy indicate that it is developing within the framework determined in the program of the medium term development of the country. Despite the difficult energy situation, where the Albanian economy was in 2007, generally it has, even during this year, gone through satisfactory developments towards the confirmation of the programmed speed rates of the economic growth, of further consolidation of the macroeconomic stability and continuation of the structural reforms in the economy. There is expected the same positive progress even during the remaining part of the year.

During 2007, the economic growth has been oriented mainly through the domestic demand, where the latter has been supported by a fast economic growth of crediting the economy as well as by the continuous significant amount of remittances. Other factors in the economic growth have been also the growth of exports and Direct Foreign Investments (IHD) compared to a year ago. At the same time, the continuous improvement of infrastructure, mainly the road infrastructure, the continuous renovation of the technology in different industries, development of human capacities have brought about that the total efficiency of the economy be increased and always be an important factor in the economic growth. Thus, despite the difficulties in the energy sector and an unsatisfactory agricultural production, mainly in the third semester due to the long droughts, the general economic development makes us be more confident for an economic growth at least at the level foreseen earlier of 6%, accompanied by an average annual inflation, round 3 percent.

According to the Sales Index¹, the economic activity during the first six-month period of 2007 has registered a nominal growth of 20.7% as opposed the same period of last year (Table 1).

For the first six month periods of 2005 and 2006 this statistics was respectively 18.27% and 12.53%. The main contribution in the annual increase of sales of 20.7% during the first six month period is held by the branches “Trade, hotels and restaurants”, with 7.3 points percentage, “Manufacturing industry” with 4.6 points percentage, “Electrical power, water and gas”, with 2.1 points percentage and “Transport & telecommunication”, “Construction” and “Other services” with approximately 2 points percentage each. (Table 1).

The branches which in themselves have gone through the biggest increase of the first half of 2007 compared to 2006 are “Excavation industry” increased by 43.3%, “Other services” with 32%, “Electrical power, water, gas” with 31.4%, “Processing industry” with 27.2%, “Transport and telecommunication” with 19.7%, “Trade, hotels and restaurants” with 16.4% and “Construction” with 13.8%.

In the high increase of sales which has been registered by the excavation industry during this year a considerable contribution was made by the export of this industry. Out of 43.3% increase in total sales of this industry, the increase of sales for export contributes by round 22.7 points percentage (in themselves the sales for export have increased by 150%), while the other part 20.6 points percentage is attributed to the increase of the sales within the country, thus the domestic demand. This is confirmed even if we refer to the Statistics of

¹ Source: Institute of Statistics

Table 1: Increase in % of sales (first 6-month period of the year V / first 6-month period of the year V-1)

Code NACE	Activity	6M-04	6M-05	6M-06	6M-07
		6M-03	6M-04	6M-05	6M-06
C	Mining Industry	-12.4	21.1	22.0	43.3
D	Manufacturing Industry	8.1	12.7	14.9	27.2
E	Electrical Power, Water, Gas	-12.6	15.0	2.6	31.4
F	Construction	18.3	29.1	5.0	13.8
G+H	Trade, Hotels and Restaurants	2.8	19.9	16.0	16.4
I	Transport and Telecommunication	10.4	10.2	1.5	19.7
J - Q	Others	4.0	19.0	31.0	32.0
C - Q	Total	4.7	18.3	12.5	20.7
Contribution in growth (in points percentage)					
Code NACE	Activity	6M-04	6M-05	6M-06	6M-07
C	Mining Industry	-0.3	0.4	0.4	0.9
D	Manufacturing Industry	1.4	2.2	2.5	4.6
E	Electrical Power, Water, Gas	-1.1	1.1	0.2	2.1
F	Construction	2.1	3.8	0.7	1.8
G+H	Trade, Hotels and Restaurants	1.2	8.5	7.0	7.3
I	Transport and Telecommunication	1.2	1.2	0.2	2.0
J - Q	Others	0.2	1.0	1.6	1.9
C - Q	Total	4.7	18.3	12.5	20.7

Source: INSTAT

the Foreign Trade, where the export of Minerals, Burning Resources for the period January – September 2007 has increased by round 184% compared to the same period of the one year ago. It is worthwhile to mention that the working conditions in this industry (mainly in mines) have improved, mainly as a consequence of controls and measures taken by the authorities, which is expected to increase productivity in this industry, but at the same time contribute to reducing the unemployment, mainly at the layer of low qualification unemployed persons.

The growth in the manufacturing industry has been mainly led by the demand of the domestic market, where out of 27.2% increase of total sales in this industry, 22.2 points percentage come from the increase of the domestic sales and the main contribution is made by the food industry, manufacturing of the mineral and non-metallic articles and the metallurgy of processing of metals. There has been growth in itself also in the industries of clothing and textiles, leather and shoes, chemical and Cautchouc industry, but since each of them consists only a small part of the total sales of the processing industry, their contribution is modest.

The entire increase of 31.4% of the sales of the electrical power, water and gas, is attributed to the domestic demand. However, other than the other economic activities, the increase reached in the sales of this branch shall not be translated equally to economic growth, as the case could be in the other branches. Certainly, the reason for this is the decrease of domestic production and

drastic increase of import of the electrical power of 189% (in value). Thus, if for the other branches of the economy we would suggest a more or less constant relationship from year to year of the output and intermediate consumption, for the electrical power the intermediary consumption in this year has increased much more than the output, thus turning out in a reduction of the gross added value of the branch².

Actually the indicators of the electrical power sector for the period January – August 2007 speak of a lower level of offer of electrical power, compared to the same period of the last year. The reduction of offer by 9.3% came as a result of the reduction of domestic production, while the growth of imported quantity did not manage to meet the demand for energy, which was materialised in the re-occurrence and escalation of the restrictions of supplies with electrical power in the third semester of this year. However, the normal development of the reproduction process has not been hindered considerably by the restrictions of the energy. This being a consequence of the advantages done to the business in the supplies with electrical power. Despite the reduction of the total offer of electrical power, the energy supplied to the business in the first 7-month period has increased by 19.6 compared to the same period of one year ago. Thus, the required quantities of production generally have been supplied without any significant increase of costs per unit, and this goes for the industry and for a part of services. Positive development in the balance of the electrical power was the reduction of losses in total and losses to resources, mainly due to the increased level of cash collection. Despite the measures taken by the economic agents and by KESH to face the problems caused due to the electrical power cuts, this sector remains one of the major problems and consists the most potential risk for the further development of the economic activity in general.

The construction, although it marked an increase of 13.8% in the first half of 2007 compared to that of one year ago, there should be stated that the same statistics in 2005 turned out 29%. This slowdown of the growth rates of this sector has come mainly as a consequence of suspension of the construction permits by the authorities, as well as non-implementation of the public investments to the planned extent during the first half of the year. In the other part of the year, with the implementation of the planned public investments and with the normalisation of granting of construction permits, there is expected that this sector recuperate its traditional growth rates. Despite the slow down of growth rates in construction, during this period, the general real/physical investments in economy continue to have satisfactory growth rates led by the investments in technology. This is confirmed if we refer to the Statistics of the Foreign Trade³, where import of machineries and equipment in the first half of 2007 has increased by 22.6%, compared to the same period of the previous year. The same statistics was one year only 1.7%.

The growths of 16.4% and 19.8% in “Trade, hotels and restaurants” and “Transport and telecommunication” are mainly attributed to the increasing demand for these services from the local residents, but also a considerable part shall be attributed also the foreign residents, where it is worthwhile mentioning the boom in tourism during this season. The big increase in the trade activity is indicated also by the retail trade volume which has increased by round 5% in this period.

In the other services, the highest growth was that of the activity of “Immovable properties and renting”, “Financial Intermediation” and private and public education. For the public education,

² Here we refer only to the electrical power, not to water and gas, which have experienced growth

³ Source: INSTAT

we refer not only to the operational expenses of the government, where the expenses for the education for the first half of the year have increased by round 11%, but also to the evident increase of the number of students. Since our economy is an economy which needs a qualified labour force, the increase in education not only contributes to the economic increase of this year, but it also consists a very important “investment” for the future growth of economy.

As a consequence of the lengthy draught of this year and as a consequence of the real shortages in watering, the agricultural sector did not during 2007 have the expected growth. Generally, the agricultural production has registered a reduction compared to one year ago, thus having an impact also on the increase of the prices of agricultural products for this year.

In the second semester of the current year, the unemployment rates were reduced compared to the same period of the previous year, where out of 13.9% it was reduced to 13.5%, thus following its falling tendency. While the unemployment rates in the state sector has fallen mainly due to the privatisation and taking of measures for a more efficient functioning of the enterprises and of the public administration; the private sector was characterised by the increase of the number of registered entities and number of employees in the existing ones. The structure of unemployment continues to be dominated by age groups above 45 years, and individuals of low education (round 54% of the total of the unemployed job seekers). According to the gender criterion, the layout of the unemployed job seekers is almost equal between the males and females, although the unemployment rate is higher in the category of females compared to the males (only during 4 months of 2007 it was 18%, while at males round 12%). Unemployment in Albania has been characterised even by the fall of the number of long term unemployed.

Another feature of the labour market developments during the first half of this year was the reduction of the number of unemployed job seekers benefiting economic allowance and unemployment allowance, reflecting in this way: (i) increase of discipline of implementation and functioning of these schemas (ii) providing for new space for employment for this category (iii) emigration and internal movement of population, etc. Thus the number of unemployed benefiting unemployment allowance at the end of second semester 2007 was round 12.7% and 12.4% lower than respectively to the fourth and second semester of 2006. The average salary and minimal salary in the state sector have increased in annual terms at the end of the second semester 2007, respectively by 15.4% and 18.6%, reaching the levels 31 850 and 14 000 lek, remaining unchanged from the level of the end of the previous year. Although the unemployment allowance has remained unchanged since the second semester 2006 (at the level 5 240 lek), the average economic allowance for a family in annual terms has increased by 1.5% (reaching 4 320 lek).

The increasing tendency of inflation during the third semester of 2007 is increased to have been impacted by the added intensity of the action of factors of demand and offer, originating within and outside the domestic economy. The consumption in the private sector, supported partly by the increase of credit granting in this sector, has been the main engine which has incited the relatively fast growth rates of the increase of the aggregate demand in economy. The public sector has had also a positive impact with regard to the demand, but at lower levels that those which have been programmed.

However, the main impact in the inflation of the months August and September, the rates of which were above the target interval 2-4% of the Bank of Albania, with respectively 4.2% and 4.4%, has stemmed mainly from the reduction of offer in the domestic agricultural products. In the inflation of these two recent months and mainly in September, the biggest contribution was

made by the increase of the food prices. Out of 4.4%, which was the inflation in September, round 4 points percentage is contributed by the increase of the price of foods. This is attributed to the increase in itself of the annual price of the foods of 9.5%, as well as the considerable specific weight of 42.6% which this group makes up in the consumption basket. Almost the entire increase of annual price of foods has stemmed from the annual increase of the price of fruits, vegetables, bread and products based on corns, and dairy products.

Traditionally, during the period August - October, in the market of agricultural and dairy products there prevails the domestic production, which competes in prices that of the import, and the quantity of the latter in this period is inconsiderable. Thus, every year in this period, the prices of agricultural and dairy products fall considerably. This year, owing to the lengthy draughts and the real impossibility for watering, the domestic agricultural production experienced a considerable fall, reducing the offer on the one hand and making the costs per unit of the agricultural and dairy products increase, thus, leading to a considerable increase of the prices, compared to one year ago, and consequently contributing strongly to the inflation growth. While with regard to the increase of bread price and of the products based on corns, the main cause is evaluated to be the drastic increase of the price of corns in international markets, taking into account that most of the corns used for the production of bread and other products comes from import. At the same time the increase of oil price, electrical power shortage and its replacement by other alternative more expensive resources of energy in a considerable part of the businesses (mainly with the businesses of services) have had also an impact on the inflation related pressures over the year.

The satisfactory development of the demand has been supported by higher levels of imports and exports of goods, which during January – August 2007 have respectively marked the annual growth rates of 23 percent and 28 percent. The trade deficit, deepened by 4 points percentage in terms of GDP, seems to have reflected the increase of consumption and that of investments, where the foreign ones have ensured an important support for the economic activity.

The increase of the aggregate demand has been reflected in the steady extension of the monetary offer, which during the third semester of 2007 preserved the growth rates of the two previous semesters (+17 percent). In this tendency, decisive have been the high credit rates, which express directly the increase of the demand in economy. The relationship of credit for economy to the monetary value was at steady levels, round 34 percent, while the credit continued to extend at fact pace (+54 percent). Most of the growth reflected the high demand of businesses for funds.

Bank of Albania evaluates that during the period January - September of this year the offer in the Albanian economy has been considerably influenced by the fluctuation of the internal and external factors, which has determined also the tendencies in the general level of prices of consumption and production. The unfavourable climate conditions had an impact on the reduction of agricultural production offer. The continuation of the increasing tendency of the price of corns in international markets was evidently reflected in the increase of some basic products in the local market during the third semester. The increasing tendency of the raw material and oil prices paved the way for higher costs in the production of the industrial domestic production. The worsening of the energy situation in the country and in the region was on top of the unfavourable international tendencies, turning out into high annual price rates in consumption goods, specifically in the third semester of 2007.

Relying on the results of the macroeconomic analysis, as well as on the evaluation of the expectations for inflation in medium term period, the Supervisory Council of Bank of Albania has made two decisions, at time distance during the period January – October 2007. The monetary policy strained increasing the basic rate by 25 basispoints⁴. In this way Bank of Albania evaluates to have contributed and continues to contribute in softening the inflation related pressures in economy, analysing the expectations of the market agents and of the broad public towards the objective of inflation of 3 percent.

The total revenue of state budget for the period January – September reached in round 181.6 billion lek, out of 183.1 billion lek foreseen for this period, thus being realised in 99.19% or in a shortfall of 1.4 billion lek. Compared to the same period of one year ago, the revenues have increased by 19.3% billion lek.

The taxation revenues are round 164.1 billion lek, turning out to a shortfall of round 2.7 billion lek, although compared to the same period of last year, they turn out with round 15 billion lek more.

The revenues from customs and taxation reached round 127.6 billion lek, turning out with a shortfall of -323 billion lek, although compared to the same period of last year, these revenues were increased to 15.8 billion lek. While the annual collection of revenues from customs and taxation is round 71%. The positive development of collection of revenues reflects the extension of the taxable basis, being impacted by the total growth of the economic activity and by the increase of the performance of taxation administration.

The total expenses of the budget for this period have gone up to 171.3 billion lek compared to 192.0 billion lek foreseen for this period, being achieved round 89.2 percent or with a shortfall of 20.7 billion lek. Compared to the annual plan these expenses have been realised to round 55.3 percent, while compared to the same period of the previous year, the budget expenses turn out round 19.1 billion lek higher or round 12.5 percent more.

In the total of realisation of budget expenses for the 9 month period 2007, the current expenses make up round 87.8%, compared to the foreseen 82.9%, while the capital expenses make up round 12.2 percent compared to foreseen 16.9 percent. One year ago, the structure of total expenses of state budget realised as 9 month period was 90.2 percent the current expenses and round 9.8 percent the capital expenses.

The current expenses for the 9-month period 2007 went up to 150.4 billion lek or round 94.5 percent of the plan for this period, turning out with a shortfall of 8.8 billion lek. Compared to the annual plan, these expenses have been realised at the extent of 63.8 percent while compared to the same period of the last year these expenses turn out to be 13.1 billion lek more or 9.5 percent more.

The expenses for interests representing round 12.2 percent of the total of current expenses realised during this 9 month period turned out with an economisation of 1.8 billion lek, this being an economisation for round 1.5 billion lek in the internal interests and for 316 million lek in external interests. As opposed to the period plan, the interests have been realised at the extent of 91.1 percent.

⁴ Currently, the basic interest rate is 6 percent

The operational and maintenance expenses during the 9 month period of 2007 reached round 15.1 billion lek being round 818 million lek under the foreseen levels. At the same time, they turn out round 1.7 billion lek higher than one year ago or round 12.6 percent higher.

The expenses for subsidies have been realised almost at the foreseen levels or round 90 million lek less, being almost at the same levels of one year earlier, or round 41 million lek more.

According to the supplementary budget, round 3.75 billion lek have been provided by the state budget as a support for the energy.

The expenses for the local budget have reached round 12.5 billion lek out of 15.1 billion lek planned for this 9 month period of 2007, turning out with a shortfall of 2.6 billion lek or 17.4 percent less than the period plan. Compared to one year ago, these expenses turn out almost at the same levels or with only 107 million lek less or 0.9 percent less.

The unemployment allowance turns out with a shortfall of 6.6 percent or round 46 million lek less than the forecast being round 9 million lek or 1.4 percent less than one year earlier.

The economic assistance during the 9 month period 2007 was realised almost at the levels of forecast or round 71 million lek less or round 0.9 percent less than the plan, being at the same time round 987 million lek more than or round 15.1 percent higher than one year earlier.

With regard to the reserve fund of the Council of Ministers, up to later 9 month period 2007, there has been spent round 1.47 billion lek compared to the 1.8 billion lek which have been planned to be spent until later this year, or round 81.4 percent.

The capital expenses until later 9 month period 2007 have been realised at the level of 64.4 percent of the forecast of the period or round 29.9 percent of the annual plan turning out with a shortfall of 11.6 billion lek to the 9 month plan. Within these expenses, the investment with internal financing have been realised at the amount of 63.6 percent with a shortfall of 9.1 billion lek, while the investments with foreign financing have been realised at the extent of 66.8 percent of the forecast of the period or with a shortfall of 2.5 billion lek. Compared to the annual plan, these investments have been respectively realised 32.2 percent and 24.4 percent.

Later 9 month period 2007, the composition of the realised capital investments is 75.6 from the internal financing and round 24.4 percent from foreign financing.

1. 2. Medium Term Macroeconomic Scenario

1.2.1. Real Sector

The Albanian economy, same as a considerable part of the economies of the Central and South-Eastern Europe has in the 2 recent decades encountered a series of developments and natural structural reforms (excluding the internal negative blows) to a certain extent for the process of adjustment of the market mechanisms and guaranteeing the functioning of the free initiative. This process has, in the aspect of real developments of the Albanian economy, been reflected through the trends of the characterising indicators of the real sectors in the respective tables displayed in the section of charts at the end of this material. The projections of the main macroeconomic indicators for the period covered by this program have been realised making use of the resources and inputs: historic evaluations accomplished by the local institutions according to the respective field, SKZHI, Public Finances Sector Strategy 2007 – 2013, Medium Term Budget Program 2008

– 2010, suggestions and estimations of the report of a part of the indicators to GDP from IMF, as well as the forecasting models made use of by the Macroeconomic Department at MoF for the forecast of GDP and its constituent elements from the perspective per manufacturers and purchasers.

One of the main principles which has oriented the obtainment of the real indicators which is attributed to our economy for the period 2007 – 2010 is the preservation of consistency between this sector and the other sectors under the circumstances of a foreseeable external environment, same as it has been described in Annex 4. At the same time, we highlight that the potential external negative/positive blows of the form of: increase of fuel prices, deepening the deficit of the current account, increase of the price of the agricultural products, increase of the electrical power import, steady extension of Euro zone, reduction of the external inflation-related pressures, steady development of the national currency as against the foreign ones, positive developments in the international financial and goods markets etc, have been included in these projections to the extent which is technically permitted by the availability of data and functional logic of forecasting models we have used.

The public finances are expected to contribute in preserving and strengthening the macroeconomic stability reached during the recent years through the continuation of fiscal consolidation supported by: (i) improvement of administration of revenues and boosting efficiency of public expenses; (ii) increase of the level of allocation of budget resources with destination public investments in the most productive and strategic sectors; (iii) facilitation of the business environment through the establishment and implementation of fiscal real incentives; (iv) continuation of implementation of programs of economic assistance keeping almost the same level to GDP and improving the quality of targeting the aimed groups; (v) use of appropriate instruments for activating the local inputs of production (specifically in the sector of energy, water, agriculture and those of exports); (vi) reduction of the negative budget impact due to the expected improvement of the KESH performance; (vii) improvement of efficiency of the management of public debt being mainly led by the support of private investments and extension of the average time period of its maturity, etc. Consequently, at the extent that such a picture shall be made possible in the future, to the same extent there shall be increased even the reliability of macroeconomic projections “*ceteris paribus*”.

Under the circumstances of expectedness and circumstances mentioned above, we foresee that the economic growth even for the period 2007 – 2010 shall continue to be reliable at the level 6% reflecting: (i) increase of level of investments compared to GDP; (ii) improvement of the climate of business and other structural factors of growth to the effect of softening the negative tendency of total productivity of the factors of production encountered during the recent years; (iii) continuation of following the policy of differentiation of supply with electrical power in favour of businesses etc. As it is evaluated even in the different reports of IMF and World Bank, the displacement of the productive sources by the less productive sectors towards those with relatively high productivity has clearly explained the conduct of economic activity during the period 1993 – 2006. The low level of improvement of the education of the population, the not very high level of qualification of the work force, the presence of barriers for the entry and departure of businesses in the market are the main elements which have exercised pressure on weakening the impact of reallocation of the resources of economic growth. However, compared to the countries with high growth rates, our economy has marked one of the best performances (in terms of real growth).

The structural dynamics of the resources of growth until the present year and the economic policies which are aimed at being implemented through the different programs of the economic and social development at national level suggest that in the period 2007 – 2010 the sustainability of economic growth shall rely mainly on: continuation of following the efficient harmonisation between the fiscal policy and the monetary policy, in the service of the macroeconomic stability, accumulation of capital, increase of general efficiency of economy as a consequence of strategic investments in infrastructure, education and qualification of labour force, etc.

There is foreseen that the total investments in % of GDP (private and public) have to follow a growing tendency during the programmed period in the framework of EEP, expecting to mark 28.7% of the GDP in 2010, from 25.6%, 26.9% and 30.4% of GDP which are those foreseen to be respectively in years 2007, 2008 and 2009. During this period, this tendency of total investments shall be supported by the average contribution of the private investments and public ones, on an average of 9.49 and 3.71 points percentage, under the circumstances of respective standard deviations of 0.64 and 0.84.

At the same time, even the internal savings based on the increase of real revenues and improvement of the living standard, there are foreseen to reach more than 23% of GDP earlier 2010 out of 18.3% in 2007, following a falling tendency but slower compared to the total investments, as well as reflecting the increase of foreign non-debt making financing, such as the direct foreign investments and the official foreign transfers. From the quantity point of view, this fact is translated as an average contribution of private and public savings in the annual rate of increase of total savings, on average 11.9 and 2.9 points percentage.

Under the condition of projecting the real annual increase of 6% and annual average increase of inflation of 3%, the forecast of nominal GDP shall reach 1 293 000 million lek out of 982 000 million lek in 2007. Consequently, the deflator of GDP in a form of coefficient shall be reached to 1.40 in 2010, compared to 1.27, 1.31 and 1.24 respectively in 2007, 2008 and 2009. In addition to the above, there has been mentioned in the conduct of deflator of GDP that there has been reflected: steadiness of exchange rate of lek towards Euro and USD, keeping inflation within the target (3-1, 3+1) % established by the Bank of Albania for a medium term period. The harmonisation of the forecast of the increase of population on average with an annual increase rate of 0.4% and of the dynamics of forecast of nominal GDP explained above, is expected to be reflected in the increase of GDP per capita⁵ at a cumulative extent of 30% during the upcoming 4 year period (including also the present year) reaching 404 785 lek per capita or 4 126 USD per capita (Table 1a, ANNEX 1).

From the viewpoint of the purchasers/aggregate expenses, the main contribution in the realisation of the economic growth is expected to be caused by the total consumption, which is expected to be supported by (Table 2):

- (i) still low level of GDP per capita compared to the countries encountering the same growth rate
- (ii) increase of available revenues in the form of remittances, (only the private transfers for the period 2007 – 2010 are foreseen to be increased with a cumulative norm of 26.5% under the circumstances of the weight of remittances to the private transfers 98.7% during the 3-4 previous years)
- (iii) increase of productiveness of work due to the prioritisation of the public expenses in

⁵ In the material IMF WP/07/170 there is evaluated that the coefficient of correlation between the ratio Investments/GDP and growth of revenues per capita for the 27 transition countries is 0.36 for the period 1996-2006. At the same time the correlation between the revenues per capita from one hand and the terms of trade, remittances and EBRD reform index on the other is evaluated respectively 0.25, 0.26 and 0.65.

the sector of education and policies of inciting employment (iv) increase of the scale of intermediation in the financial system (v) continuation of implementation of programs of support of social support and reduction of poverty (payment of unemployment and economic assistance taken together are expected to have an average annual increase in nominal terms of 11.8% for the time period of 4 upcoming years) (vi) the policies of re-distribution of national revenues (vii) deepening of regulation of the markets to the effect of making possible the trading of the agricultural by the local farmers, etc.

Table 2: Contribution of aggregate expenses in real increase rate

	2004	2005	2006	2007	2008	2009	2010
<i>Internal Final Demand</i>	4.1	12.2	5.2	7.6	5.9	6.7	6.3
Total Consumption	-0.7	8.6	4.4	5.0	1.8	5.5	2.6
Private consumption	-1.9	7.9	4.4	4.6	1.6	4.8	1.8
Public consumption	1.1	0.7	0.0	0.4	0.3	0.7	0.8
Gross Formation of Tangible Capital	4.8	3.6	0.9	2.6	4.1	1.2	3.7
Private F.B.K.F	3.2	3.8	0.6	1.5	2.4	3.9	3.1
Public F.B.K.F	1.6	-0.2	0.3	1.1	1.7	-2.7	0.6
Trade Balance	1.6	-6.4	-0.2	-1.6	0.1	-0.7	-0.3
Export (goods and services)	5.7	3.9	0.8	1.7	1.6	2.1	2.0
Import (goods and services)	-4.1	-10.3	-1.0	-3.3	-1.5	-2.8	-2.3
Real Growth	5.7	5.8	5.0	6.0	6.0	6.0	6.0

The consuming nature of the economies of the countries in transition makes the private consumption to continue to be the main contributor not only in the total consumption, but also in the economic growth even for some years in the future depending from the increase of the essential standard of the increase of integration scale of our country into EU and other international structures. The more the convergence of the living standard is realised with the other countries of the region and Euro zone, the more it is expected to change the culture of spending the revenues by our society being increasingly led in decision making towards the purchase of long term consumption goods and more savings. Thus, the private consumption in the economic growth of the three upcoming years is expected to be round 1.6, 4.8 and 1.8 points percentage, out of 5.6 points percentage in the three last years (including the current year).

The fiscal directives which are connected to: increase of efficiency of public administration, unification of the salaries of employees of the same category, programming of the operating expenses and maintenance of the functioning of improvement of impact of existing infrastructure and additional investments in the future is expected to include the annual increase of public consumption by 7%, 10% and 13.4%, respectively in 2008, 2009 and 2010. This tendency in the public consumption in the form of its contribution in the formation of economic growth is translated to the figures of 0.39 points percentage in 2007 and 0.26, 0.69 and 0.81 points percentage in each of the following years.

In long term perspectives, along with the technological progress and structural reforms, a source of the steady increase is expected to be the accumulation of capital/physical investments, which is expected to be supported by: (ii) reduction of profit tax to the extent of 10% since January '07 (iii) improvement of the management of public investments through the continuation of a) giving priority to the big existing projects b) improvement of the contents and implementation of the law

of public procurement c) improving the quality of cash management, (iv) preserving the real positive interest rates of the market (v) increase of the level of intruding cash to the system, etc. As a consequence of potential impact of these measures, there is expected that the contribution of the 'Gross Fixed Capital Formation' in the relative real change of the economic activity register, during the period that this program is considering, an average of 2.89 points percentage following an increasing tendency.

The relatively high influence of investments in the future economic activity is explained through a not very good utilisation of the potential level of this resource by the countries in transition, during the last decade and by the high sensitiveness of the economic growth towards the change of the physical stock of capital. The biggest contribution of the total consumption in the economic increase compared to that which is provided by the formation of gross capital reflects the heavy weight of the consumption to the aggregate total demand rather than the difference between the respective annual increase rates.

The expectations for an annual growth rate of more exports than that of imports, the preservation of a considerable weight of machineries and equipment in the total of our imports, the continuation of the utilisation of comparative advantages with regard to the production of the textile products and shoes, improvement of total infrastructure in the country, subsidies (lately there has been approved the reimbursement of VAT for the agricultural and dairy products with domestic origin) and support of agricultural products, steady increase of the economies of Euro zone, increase of the level of tourism due to the favourable Mediterranean climate and exploitation of potential resources in this field is evaluated that they are going to be reflected in a positive real rate of trade balance, however, reduced from year to year, during 2008 – 2010⁶. From the perspective of contributions, we highlight that the contribution of the external demand in the economic growth is foreseen to be increased in the upcoming years in order to mark during this period in average terms the level of 3.8 points percentage as a support to the increase of competitiveness of the domestic economy.

For the generation of the projections of the added value according to the economic sectors, there has been used: (i) the method of designed production within the logic of the Input-Output model, which is being used for the forecast of GDP by the Macroeconomic Department, MF, and (ii) trend of forecasting the GDP and some exogenous variables according to the sectors by IMF. The Input-Output model relies on the assumption that the sub-branch structure of the intermediary product and the added value would not change in medium term period. The forecast of some indirect taxes and subsidies in real terms has been realised through combination of the use of index of annual difference of CPI, taking as base year 2000, and the latest respective forecasts of PBA following the reflection o the budget plan of 2008.

As a result of: (i) improvement of the regulation of market and incitement of competition (ii) increase of the taxable basis due to fiscal reformation (iii) increase of effectiveness of tax and customs administration as well as (iv) reduction of the financial support of state enterprises in the framework of the process of privatisation and improvement of their performances, there is expected an increase o GDP evaluated by the market prices at approximate levels to that of GDP, evaluated with the costs of factors/base prices.

The real growth of GDP in the context of the sector composition, there is foreseen to be supported during the period of this program by the sector of services, sector of construction and

⁶ With the exception of 2008, where it expected that the trade balance growth real rate be negative and concretely - 0.3 %.

that of transport (Table 3). In average terms, 2007 – 2010, the contribution of these sectors is expected to be respectively 1.95, 1.71 and 1.09 points percentage.

Table 3: Contribution of sectors in the real growth rate

	2004	2005	2006	2007	2008	2009	2010
Industry	1.08	0.21	0.64	0.34	0.35	0.28	0.28
Agriculture	1.51	0.22	0.73	0.75	1.06	0.98	1.05
Construction	1.12	1.73	1.58	1.62	1.71	1.75	1.77
Transport	0.53	0.33	0.73	0.99	1.08	1.14	1.14
Other services	1.46	3.32	1.37	2.34	1.83	1.81	1.80
Real growth	5.7	5.8	5.0	6.0	6.0	6.0	6.0

The influence of the sector of services and transport in the real activity is expected to embody: (i) improvement of the climate of business through: a) reformation of the process of registration of businesses and establishment of National Registration Centre b) improvement and implementation of the law of procurement and concessions c) institutional policy strengthening for the differentiated supply of electrical power (ii) boosting of investments in the energy sector, infrastructure in general and transport specifically (iii) boosting of efficiency of functioning of telecommunication and insurance market as a consequence of the privatisation done this year of the Alb-Telekom and INSIG in the future (iv) national policies of inciting the direct foreign investments (v) improvement of the infrastructure and marketing of tourism (vi) continuation of reliability of demand for housing as a consequence of internal migration and intensification of the activity of business in the country (vi) fall of prices of a part of inputs which are used by these sectors as a consequence of implementation of SAA.

The internal structural changes in our economy, high levels of the price of electrical power and unsteadiness of prices of oil at global level, the increase of the range of economic opening up in the upcoming years support our estimations about a relatively steady contribution (not increasing) of the sector of industry in the economic growth. Thus, the average contribution of this sector during the period 2007 – 2010 is foreseen to be 0.31 points percentage, reflecting a standard deviation of 0.04. The relative steadiness of the contribution of this sector shall reflect also: (i) improvement of the operational efficiency and privatisation of the domestic companies of production and processing of oil in the country (ii) preserving the weight of volume of processing and textile industry due to: a) the advantages of low cost of labour in the country b) reduction of the capital tax (i.e., profit taxation in 10% early next year) c) continuous compensations of the load which causes in the level of low salaries the unification of the taxation on the personal income⁷ in the form of the external threshold 10 000 lek for the low salaries and up to 30 000 lek and other measures in this framework.

The agricultural activity in our country continues to plan an important part in the respect of the relatively high weight of agriculture to the nominal GDP (on average 21-22% during the seven last years), level of self-employment (round 58%), support to the households, possible spaces of improvement of the relationship of covering the imports with agricultural and food exports from

⁷ Since July 2007, the tax on personal income has been unified at the level 10% from the previous system, which consisted of 5 tax scales

Albania etc. The presence of this picture even in the medium term creates a condition of arguments for undertaking and continuation of some measures in this sectors, such as: (i) introduction of the concept of the agricultural associations, cooperatives in the new law on agriculture (ii) reimbursement of the VAT for the agricultural and dairy products to the effect of inciting the exploitation of the local products by the sector of agricultural and food processing and there is reduced the discrimination to the agricultural products of import origin (iii) investment in the water reserves to the effect of strengthening the guarantee with water supply (iv) continuation of programs of grants for rural development. Other factors which are expected to support this sector are (i) increase of the productivity of the factors of production due to the considerable weight of import of machineries and equipment and intensification of the process of integration of the country into EU (ii) narrowing the range of informality etc. the potential coordination of measures and the above developments is expected to turn out into an average contribution of the sector of agriculture of 0.96 points percentage in the real growth of GDP (with standard deviation 0.14) during the period 2007-2010.

1.2.2. Inflation

The main objective of Bank of Albania in the short and medium term periods has been and will continue to be the achievement and preservation of price stability. In order to make this concrete, Bank of Albania shall consider as its objective keeping the inflation at the level of 3 percent with a possibility of fluctuation of ± 1 points percentage round this central value. As an objective for the inflation, there shall be considered the annual growth of the index of consumption prices, assessed and published by INSTAT. The preservation of the stability of the total level in economy expressed in this form shall remain the main objective of Bank of Albania and its monetary policy for the upcoming medium term period.

The determination of the objective in the form of an inflation rate of 3 (+/-1) percent is in compliance with the level of macroeconomic development of Albania as opposed to that of the more developed economies of the European Union (EU). This digital objective of the inflation rate, as opposed to the objective of 2 percent of the European Central Bank, facilitates the compliance of the macroeconomic indicators to those of EU. The tolerance interval of (+/-1) has been projected to allow the minimisation of the effects of the unforeseen disturbances of the offer in the macroeconomic balances. The quantity value of the inflation objective declared above reflects the reality of the Albanian economy, as an economy in development. These economies are characterised by wider fluctuations of relative prices to the effect of reaching the required balances of the market economy. The aim for lower levels of inflation could impose high costs for the economy of the country. On the other hand, the preservation of the objective of inflation at the same level with the six preceding years will contribute positively in the consolidation of expectations related to inflation round the objective declared by Bank of Albania.

During this year, the average rate of inflation turned out to be round 2.6 percent. In the recent months there have been seen inflationist pressures coming mainly from the quick increase of credit for the private sector, increase of administered prices, increase of prices as a consequence of missing energy, and increase of prices of raw materials in international markets. These factors have brought about that in the two last years the annual inflation turn out more than 4%. Expecting the strengthening of the inflationist pressures, the Bank of Albania has signalled the

restriction of monetary conditions. The expectations of the public presently turn out to be anchored close to the digital objective of the Bank of Albania.

Although presently there exist pressures for the increase of inflation, in average medium terms, there is expected that this indicator fluctuate at the objective level. The monetary policy to be followed in this period shall be to the function of controlling the inflation rate in average terms, round the level of 3 percent. Its implementation shall continue to rely on the use of indirect instruments (operations in the open market) for orienting the short term interest rates. During this period, there shall be aimed at reaching the efficiency of these instruments, their approximation to the European standards and development of financial markets.

The present agreement between the Albanian government and IMF contours a certain framework of intermediary objectives to the effect of strengthening the macroeconomic stability. This agreement extends its effects even during 2008. In the meantime, for more than 2 years, Bank of Albania has announced publicly its aim to adopt a new monetary regime, that of the Restricted Inflation. Presently, it is trying to set up the human and technical capacities for the full adoption of this regime in the future. Upon undertaking this step, it aims at improving the policy making process and successful anchoring of the inflation related expectations for the realisation of the final objective of Bank of Albania.

1.2.3. Monetary policy and exchange rate

Bank of Albania, as the institution responsible for the drafting, approval and implementation of monetary policy, has made the decisions of this nature to the effect of reaching its main objective – reaching and preservation of stability of prices.

Bank of Albania operates under the regime of the monetary policy which formally is defined as the regime of Monetary Restriction. This regime assumes that the control of inflation could be realised through the determination and reaching the intermediary monetary objectives, which transmit the effects of monetary developments to the inflation rate. The monetary policy of Bank of Albania relies on the drafting of a monetary program which serves as a scenario for the eventual development of the monetary indicators. The present regime of the monetary policy is in compliance with the three year agreements PRGF/EFF, signed with IMF in January 2006. This program has served as a framework for working out steady policies to the effect of reaching the macroeconomic stability. During the ongoing period, there shall be deepened the attempts for going towards the Restricted Inflation regime. In the meantime, presently Bank of Albania has expressed a well-received objective and it is going to keep the present regime for the short term period; the aim is that for the future (in medium term period), the regime of restricted inflation be applied in its full form.

The current operational framework of Bank of Albania has been adjusted in its most part to the operational framework of European Central Bank. However, a challenge of Bank of Albania remained the efficient implementation of this operational framework of instruments which is interrelated directly to the aims of the Bank of Albania, in order to develop financial markets. The development of these markets shall determine closely even the further necessary

improvements of the current operational framework of Bank of Albania, bringing about approximation to the international standards.

In the framework of meeting the strategic objectives in the three upcoming years, Bank of Albania is going to use a combination of indirect instruments of the monetary policy. The importance which shall be attributed to each instrument shall depend on the nature of challenges it is going to encounter.

The operations of the open market shall continue to be the main regulatory instrument of reserves of the banking system. The interest rate of repos shall remain the indirect main instrument for the implementation of the monetary policy. With the further development of markets, there is expected that the mechanism of transmission of the monetary policy become more efficient and the basic interest rate is expected to be a reference for determining the interest rates in the banking market and in the other markets. Thus, Bank of Albania shall aim at developing an environment where the long term interest rates be determined by the market itself.

The present regime of the monetary policy cohabitates with the regime of fluctuating exchange rate implemented by Bank of Albania. Bank of Albania shall continue to preserve the present regime of exchange of currencies, that of the free fluctuation of the local currency (lek), the value of which shall be determined by the market. Bank of Albania has not intervened for the rectification of deviations of the exchange rate of the basic economic factors since 1998⁸. In the meantime, the interventions aiming at avoiding the irregularities have been mainly done for reducing the seasonal effects, in the period July – August and December of each year. During the two last years, there have been carried out even interventions to the effect of increasing the net currency reserve, combining the period of purchase with the seasonal factors. Bank of Albania shall continue to preserve the right to intervene with the market to the effect of increasing its currency reserve and softening the short term fluctuations of the exchange rate, which are caused by the irregularities in the market. At the same time, Bank of Albania preserves its right to intervene with the market whenever there is no compliance of the exchange development to the main macroeconomic indicators. Such interventions do not aim at orienting the value of lek in the medium term or long term period.

1.2.4. External Sector

The external sector of Albanian economy appears in 2006 – 2007 with a worsened balance of the current account, caused mainly by the high trade deficit. The incoming influxes in capitals have been sufficient for the compensation of the current deficit, making possible a total positive balance at the level of 207 million Euro for 2006 and 173 million Euro for the nine month period of 2007. The Studies of Bank of Albania suggest that the current account is steady, consequently it does not require taking of emergent measures or policies in this respect. However, it is necessary that the development in the current deficit be kept under the supervision of authorities.

The developments of foreign trade have been characterised by continuous and increasing trade deficits, dictating the high levels of the deficit in the current account. The main factor for the

⁸ stabilisation of the financial situation after the crisis of pyramid schemes was not reflected in the exchange rate development

increase of the trade deficit remains the high demand for imports, mainly to fulfil the needs of the economy for final and intermediary consumption. The positive development of imports has not been accompanied with the increase of export rates, thus making possible that the trade gap be deepened more and consist the main factor for high rates of the current account deficit.

The growth of imports during 2006-2007 has been one of the consequences of some external factors, such as the extraordinary increase of the oil price, accompanied with the increase of the prices of certain goods in international markets, and internal factors where the worsened energy situation in the country, brought about high imports in electrical power.

The slowdown of exports, sent during 2005, has been considerably recuperated during 2006-2007. In the meantime, the high prices in international prices have stimulated the internal export (crude oil and chromium mineral) contributing in the increase of the revenues from the export of goods for 2007.

Considerable entries in the form of current transfers have assisted in softening the high trade deficit, bringing about the facilitation of the position of payments balance. The remittances of emigrants for 2006 are evaluated in 935 million Euro, or round 12.8% of GDP. For the first half of 2007, the remittances of emigrants (of 723 million euro) are evaluated to be 11% higher compared to one year ago.

On the other hand, the financing of the current account has been made possible by the incoming influences of foreign capital as well as direct foreign investments and loan-taking from abroad.

The indicator of the direct foreign investment for 2006 is evaluated in 3.6% of GDP (250.3 million Euro). The service of the foreign debt is evaluated at modest levels, reaching round 4.1 percent of the total of exports (for 2006) or below the level considered to be critical, of 25%.

The movements of capital during the first half of 2007 registered a net influx of 327 million Euro, as a consequence of the incoming capital transfers of 44 million Euro, as well as of positive balance of the financial account of 283 million Euro. This positive balance of the financial account has come mainly due to the incoming influxes in the form of direct investment (foreign direct investment are evaluated at the level 145.6 million Euro or 16% higher compared to one year ago), of the loan-taking from abroad (the liabilities from loan-taking have been increased by 62.8 million) as well as of the deposits of the foreign financial institutions in our banking system. The loan-taking from abroad is evaluated to be 29% lower compared to one year ago, consequently of the reduction of the loan-taking from abroad, be it from the state sector (17 percent) as well as from the private one (66 percent).

The surplus in the total balance has brought about in the increase of the currency reserves of the monetary authority with round 38 million Euro. The currency reserve, evaluated in 1.4 billion Euro, at the end of the period remains at acceptable levels, covering round 4.1 import months. Bank of Albania shall continue to keep a sufficient level of the currency reserves to cover at least 4 import months. The incoming of the currency in the form of direct foreign investments and the remittances from emigrants can have an impact on increasing pressures for the evaluation of the local currency, which has been evaluated round 3.03 as against the basket of currencies since the beginning of the year.

In the framework of the regulatory changes and adoption of legislation to the “*acquis communautaire*”, Bank of Albania is undertaking the necessary regulatory preparations for

liberalising the capital account in the medium term period, through the approval of the Standing Rules of the Liberalisation of the Capital Account.

2. PUBLIC FINANCES

In the essence of the program of government for the public finances and at the same time of the Sector Strategy of Public Finances for the period 2007 – 2013 is the total reformation of the public finances, through the implementation of the system of the integrated planning and harmonising of the annual budget to PBA, SKZHI and process of stabilisation and association. The reformation of the essential constituents of the public finances for the upcoming years shall aim at:

- Extension of the taxation basis and reduction of fiscal load;
- Improvement of the quality of service to the tax payers, offering of new services and products;
- Simplification of the taxes system;
- Simplification of the procedure of disclosure and payment of taxes;
- Reduction of the unnecessary contacts of tax-payers with the taxation administration (even this can be included at the quality of the service to the tax payer);
- Modernisation of the debt management, increase of the basis of investment; extension of period for the maturity of the internal debt;
- Increase of quality and effectiveness of public expenses and reformation of management and implementation of the public investment;
- Improvement of the public financial management (including the functioning of treasury, accounting and internal control, for the development of a sustainable and steady system for the implementation of the budget).

2.1. Total Balance of Government and Debt

2.1.1. Strategy of Policies and medium term objectives

In the strategy of public finances, there are determined two main pillars of taxation and customs policy and administration for years 2007-2010, which consist in: (i) extension of the taxable basis and compliance of tax policy with national priority, and: (ii) boosting of performance and reliability of the taxation and customs administration.

1. Extension of the taxable basis and compliance of tax policy with national priority.

The aim is that the taxation policy in Albania create and preserve the balancing between ensuring the necessary revenues in order to support the public expenses and establishment of an appropriate climate for business. The fiscal load should not distort the decisions for investing of the local and foreign private, local and foreign sector. This aim of the taxation policy shall be achieved through:

- Distribution of the load of taxes equally and less deforming. This shall include: changes in policies and administration, to reach a higher level of performance of taxation obligations and for increasing the formalisation of employment; improvement in

implementation of the existing policies, in a way that taxes be distributed more equally within the community.

- Development of a tax system which supports the drafting of fair and promoting fiscal policies for the economic development and that of business. The policies of taxes and their level shall be drafted in order to serve effectively to the economic and social strategy of the government.
- Progressive approximation of the taxation policy towards the European legislation.

II. Boosting of performance and reliability of the taxation and customs administration

In the represent situation, the administrations of revenues have shortcomings in setting priorities in their activities and the focus of their work relies on fulfilment of the revenues plan for short term periods. This way of administration injures the reaching of strategic objectives of both administrations, such as the encouragement of voluntary performance of tax obligations of the tax payers, fight against evasion, establishing an appropriate climate for the development of business, protection of markets from trafficking and smuggling.

These objectives become more difficult to be reached in the absence of clear information on the taxation and customs obligations of the tax payers and by the non-transparent and non-uniform of the existing rules by the employees of both administrations. The achievements in this sector are necessary not only for collecting more revenues and for the establishment of a better taxation system, and extension of basis, but also as an indispensable institutional reform in order to incite new investments. The strategy aims at the reformation of administration towards the modernization, in order to operate more efficiently, be flexible to change which are incited by the international and domestic environment, collect revenues based on self-disclosure, and voluntary performance of obligations.

Main elements of this component of strategy are:

- Identification of the main resources of fiscal evasion, lowering the gap between the collectable taxes, according to the taxation and customs legislation, and the taxes which are effectively collected. As we highlighted above, the administration of taxes has a major role in reducing the fiscal evasion and in extending the taxable basis trough the administration and implementation in the appropriate way of the taxation legislation and increase of the voluntary performance of obligations. The same important role has also the customs administration, for ensuring the collection of taxes it administers, through the control it exercises on the movement of goods and correct implementation of the tax legislation.
- Improvement of quality of services for tax-payers, and establishment of appropriate conditions for the development of business. The insurance of an effective service for the tax-payers plays an important role in improving the public image of both administrations, and establishment of a reputation of integrity and effectiveness. In the taxation administration this is going to include the simplification of procedures, improvement of compliance of laws and regulations, as well as making them available to the tax-payers in simple and accessible ways. In the customs administration, the attention shall be on the implementation of the modern methods of work, and establishment of a computerised environment for the performance of obligations.

- Protection of markets and society. The customs are becoming one of the most important institutions for the protection of markets and society, paving the way for the development of the international trade. The Stabilisation and Association Agreement with EU opened up new ways for the Albanian customs for reaching this objective, through the establishment of the legislative and political framework in this field: the policies of EU for fighting against terrorism, resolutions of the International Organization of Customs on the security and simplification of the chain of international trade etc.
- The improvement of performance in both administrations, strengthening of control on management and auditing for the improvement of capacities for strategic management, consistent implementation of procedures, correct and unified implementation of MTLs and reduction of corruption. The achievement of these objectives shall include an internal control system based on the evaluation of risk, independent investigation for non-implementation of procedures and violation of rules, complaint procedures, simplification and clarification of rules and procedures for the elimination of the possibility for discretionary decisions.
- Acceleration of the progress in the reform of the administrations for meeting the EU requirements.

Medium Term Fiscal Policy, 2008-2010:

Fiscal forecasts have been based on an analysis of the multi-annual developments of fiscal indicators, of their realisation so far, in the objectives for the reduction of fiscal evasion, as well as in the forecasts of economic growth. A positive effect on the revenues shall be from the continuous administrative improvements and strengthening of administrative capacities. These improvements shall reduce the fiscal evasion and shall strengthen the voluntary disclosure of the tax payers and the formalisation of economy. The fiscal medium term policy is based on:

- Keeping the VAT rate constant during the three upcoming years. Keeping the VAT constant for the three upcoming years has been based not only on the negative impacts which can have on the revenues of state budget, but also on the social life. Our country is characterised by a steady macroeconomic environment, where the inflation related pressures have turned out to be lower than the foreseen ones (under 3%) although the government has launched a policy towards increasing the salaries and the pensions. At the same time, there has been established that the tendency of price towards the reduction appears not elastic, thus, it is not likely that the reduction of VAT would turn out into reduction of prices. Such a phenomenon has not been seen even in the present situation, where the reduction of the customs fee due to the signing of SAA and implementation of WTO is evaluated round 2-2.5%. Another important aspect for non-reduction of VAT is the indicator of the trade balance. Our country has a high trade deficit and the reduction of VAT would have further impact on the increase of the trade deficit, through the favouring of imports and discouragement of exports.
- Reduction to half of the profit taxation (from 20% to 10%) until 2010, starting the application from 1 January 2008. This fiscal measure is foreseen to have a positive impact on the domestic economy, since there shall be increased the taxable basis, domestic business shall be encouraged to declare the real figures of accounting balances, and the

climate shall be more attractive for investments, specifically for the foreign direct and indirect investments.

- The revenues from the taxation on profit for the three upcoming years is based on the extension of the taxation basis (total profit of business) as a consequence of growth of economy and administrative and structural improvement (increase of GDP is oriented by the sectors paying profit tax), as well as strengthening of the exemption from profit tax. The realisation of the revenues from the profit tax for the period 2007 – 2010 consists even the risk of non-collection of the revenues from KESH, due to the worsened financial situation of the company. However, the financial situation of the corporation has good premises to be improved in the 3 upcoming years, regardless of the energy difficulties which can accompany the country even for some other years. In the macroeconomic forecasts there has not been taken into consideration this risk, since with reference to the historic tendency of lowering the profit tax, where the profit tax rate has fallen, the performance of the revenues from the profit tax has been increased considerably above the historic average.
- A light increase in the accise in strong goods. The revenues from accise rely on the increase of the level of accise of fuels, alcoholic drinks, wine and beer, from 1 July 2007, approximating their accises to the level of the accise of the regional countries, as well as an extension of the taxable basis, following the tendency of the recent years, as well as the growth rates of GDP. At the same time there has been foreseen the increase of revenues from accise in the other goods, which reflects the economic growth and extension of taxable basis.
- Application of the flat tax system on the personal income, eliminating the progressive taxation scale, and keeping an exclusive threshold level of 10 000 lek for salaries up to 30 000 lek. All the categories of the personal income shall be taxed at the unique level of 10%, starting from the second half of 2007. The application of the flat tax shall have a positive impact, specifically on the category of employees with high income, a category which after the application of this fiscal measure (part of private business), is deemed to be completely motivated to disclose the real revenues. At the same time, there shall be simplified even the procedures of disclosure and calculation of this taxation.
- The social insurance contribution rate has been foreseen to remain the same as the level applied in September 2006, as a consequence of the review of the existing schema.
- An increase in the level of the national taxes, considering an increase of the tax of import of used vehicles (environment tax), reduction of the tax of per-day-stay of foreign vehicles, consular and port tax (starting from 1 July 2007).
- There has been foreseen also an increase in the level of local taxes, respectively the property tax on the buildings, which are in ownership or use within the territories of the tourist villages (starting from 1 July 2007).
- Reduction of customs tax, as a consequence of lowering to zero the customs tax for vehicles (starting from 1 July 2007). The trend of revenues from the customs revenues is a falling trend, as a consequence of the reduction of the customs duties (WTO and SAA commitments).
- Forecast of the non-tax revenues is based on the transfer of profit from Bank o Albania, revenues from non-budget institutions, and other budget institutions. The revenue of the remaining period 2008 – 2010 shall again be subject to review, due to the process of privatisation of shares of the Government in the public enterprises.

- Forecast of the revenues from aid and grants is based in GDP 2007 – 2009 and in the agreement with IMF.
- At the same time, there are being done progressive and continuous improvements and approximations of the tax policy towards the European legislation. This shall lead to the increase of transparency, reduction of the administrative procedures and administrative improvement, and, consequently, in the extension of the taxable basis and of the taxation revenues.

Revenues of State Budget

The total of the budget revenues are foreseen to reach more than 27% of the GDP. The taxation revenues consist the bulk of the total revenues, round 94% and make up round 26% of the GDP in 2010. The fiscal policy of the government continues to remain an inciting policy of the offer and aims at further reducing the direct taxes, which make up a smaller percentage compared to the indirect ones (Table 4 and Table 2 in the Annex2).

Table 4: Budget revenues, 2006-2010.

No.	DENOMINATION	Fact 2006	Reviewed Budget 2007	Draft Budget 2008	Draft Budget 2009	Draft Budget 2010
	TOTAL OF REVENUES	25.50%	26.91%	26.37%	26.71%	27.36%
I.	Revenues from aid	0.89%	0.40%	0.44%	0.26%	0.19%
II.	Taxation revenues	22.84%	24.04%	24.39%	24.92%	25.68%
II.1	From taxation and Customs	17.24%	18.32%	18.19%	18.22%	18.73%
1	Taxation on Added Value	8.25%	8.94%	9.29%	9.19%	9.37%
2	Profit Tax	2.47%	2.33%	1.34%	1.50%	1.61%
3	Accises	2.56%	2.94%	3.58%	3.52%	3.59%
4	Taxation on Personal Income	0.95%	1.32%	1.51%	1.68%	1.88%
5	National Tax and others	1.45%	1.67%	1.60%	1.83%	1.85%
6	Customs Tax	1.56%	1.13%	0.87%	0.49%	0.43%
II.2	Revenues from Local Tax	1.24%	1.36%	1.45%	1.58%	1.68%
1	Local Tax	0.80%	0.85%	0.88%	0.93%	0.93%
2	Property Tax (buildings)	0.14%	0.23%	0.29%	0.37%	0.48%
3	Taxation on Small Business	0.29%	0.27%	0.28%	0.28%	0.28%
II.3	Independent Budget Revenue (contributions)	4.37%	4.36%	4.75%	5.13%	5.27%
1	Social Insurance	3.97%	3.90%	4.26%	4.60%	4.73%
2	Health Insurance	0.40%	0.46%	0.49%	0.52%	0.54%
III.	Non-tax Revenues	1.77%	2.47%	1.54%	1.53%	1.48%
1	Profit from Bank of Albania	0.58%	0.52%	0.51%	0.48%	0.45%
2	Revenues from Budget Institutions	0.92%	1.07%	0.93%	0.94%	0.93%
3	Dividend	0.00%	0.74%	0.01%	0.02%	0.03%
4	Others	0.27%	0.11%	0.09%	0.08%	0.08%

2.1.2. Present Balance and Medium Term Perspective

Financing the deficit

The government aims at preserving the fiscal stability. This requires that the budget deficit and public debt be kept within the limits which are in compliance with the sustainable growth of economy. In addition to the fiscal deficit 2008 (7.93% of the GDP), which comes as a consequence of the reasons mentioned above and for which there has been agreed even with IMF, there is a clear trend of reduction of the budget deficit 2006-2010.

Table 5 displays the deficit and its financing for the medium term budget program 2007 – 2010. The budget deficit is financed by the internal loan-taking and by the revenues from privatisation, as well as from the foreign development credit.

Foreign credits are foreseen to be reduced from 1.33% of the GDP in 2007 to 1.25% of the GDP in 2010, following the same trend as the public investments with foreign investment. The internal loan-taking is used as a balancing component for covering the part of deficit which has not been financed and it has been foreseen to be reduced from 2.41% of GDP in 2006 to 2.31% for 2010. During 2008 – 2010, the internal loan-taking is within the permitted limits for a careful macroeconomic management (for more information, refer to point 2.1.3).

Table 5: Budget deficit and its financing for years 2006 – 2010 (% of GDP)

	Fact 2006	Reviewed Budget 2007	Draft Budget 2008	Draft Budget 2009	Draft Budget 2010
DEFICIT	-3.26	-4.63	-7.93	-3.90	-3.63
FINANCING	3.26	4.63	7.93	3.90	3.63
I: Internal	2.63	3.30	2.73	2.43	2.38
Revenues from privatisation*	0.22	1.49	0.38	0.08	0.08
Net loan-taking	2.41	1.81	2.3	2.34	2.31
II: Foreign	0.64	1.33	5.20	1.47	1.25

*Revenues from privatisation for the strategic sectors have not been included.

Framework of public expenses for 2008 – 2010

The structure of expenses is based on the forecast of revenues and financing for the period 2008 – 2010, and it is in compliance with the structure agreed with IMF.

In the tables 6 there has been displayed the consolidated framework of the expenses for 2008 – 2010. The total of the public expenses is foreseen to reach round 31 percent of GDP in 2010. During this period the current expenses shall follow the same growing trend, this being a consequence of the increase of the expenses of maintenance, which shall support the increasing investments in the infrastructure (mainly roads). In the meantime, the capital expenses are foreseen to have a constant value making up round 6.35% of GDP for 2010 compared to 5.7% of

GD in 2006, with the exception of the year 2008 (which has been influenced by the foreign financing foreseen for the construction of the road Durres-Kukes-Morine). The expenses of the local government have been foreseen to be increased every year reaching 2.98% of the GDP for 2010. The fund of social insurance is foreseen to stay constant in round 7% of the GDP during the period 2008-2010.

Table 6: Expenses of Local Government 2006 – 2010 (% of GDP).

	2006	2007 (Supplement.)	2008 Proposed Budget	2009 Forecast	2010 Forecast
<i>TOTAL IF EXPENSES</i>	28.77	31.53	34.31	30.61	30.99
I. Current expenses	22.77	24.01	23.51	23.56	23.76
1) Expenses for personnel	6.30	6.44	6.32	6.09	6.21
2) Interests	2.78	2.87	3.10	3.09	2.98
Domestic	2.55	2.52	2.70	2.59	2.47
Foreign	0.23	0.35	0.40	0.50	0.50
3) Operating and Maintenance Expenses	2.53	2.53	2.59	2.73	2.89
4) Subsidies	0.43	0.27	0.21	0.24	0.22
5) Expenses for Social and Health Insurance	6.67	7.24	7.07	6.98	6.91
6) Expenses of Local Government	2.52	2.67	2.75	2.88	2.98
7) Transfers for Social Protection	1.53	1.44	1.44	1.51	1.52
8) Others	0.00	0.56	0.05	0.04	0.05
II. Capital expenses	5.68	7.14	9.81%	6.15	6.35
Internal Financing	3.94	5.00	3.61	3.86	4.37
Foreign Financing	1.74	2.13	6.20	2.28	1.98
Capital Transfers	0.32	0.00	0.00	0.00	0.00
III. Reserves and Contingency	0.00	0.39	0.99	0.91	0.87

* Expenses for personnel for the period 2008 – 2010 do not include the fund of contingency for the policy of salary increases.

A. Current expenses

1- Expenses of personnel

During this period the government shall continue to follow the same policy keeping the cost of expenses for personnel for the local government at the level 6.3% of the GDP. The expenses for personnel include the salaries and the social insurance for the employees of the central power. Consequently the real increase of salaries shall be above the inflation rate during 2008 – 2010, which is in compliance with the policy of the government for the improvement of the performance at work and for the absorption and keeping of personnel.

2- Interests

The internal interests are foreseen to be decreased from 2.53% of GDP in 2006 to 2.43% in 2010. The foreign interest shall increase slightly from 0.23% of GDP in 2006 to 0.5 % of GDP in 2010 (for more information see point 2.1.3.)

3- Operating and maintenance expenses

As it was highlighted earlier, the operating expenses and maintenance for the central power have been foreseen to increase to 2.89% of the GDP in 2010, which is in compliance with the policy of the government for the reduction of the operating and maintenance expenses connected to the administrative expenses and increase of that part which is connected to services, mainly for the maintenance of capital expenses.

4- Subsidies

The policy for the reduction of expenses for subsidies has been reflected in the relationship of the subsidy to the GDP which is foreseen to be reduced from 0.43% in 2006 to 0.22% in 2010. This is going to be accompanied even by continuous reforms in the priority sectors, such as drinkable water and railways.

5- Expenses for social and health insurance

The expenses for the social and health insurance, as it was highlighted above, shall stay constant during 2008 – 2010 in round 7% of GDP. The foreseen figures reflect the policy for increasing the revenues from social contributions, thus reducing the transfer from the central budget.

6- Expenses of local government

The expenses of local government shall reach the level of 2.98% of the GDP in 2010 compared to 2.5% in 2006, as a consequence of the continuous increase of the own revenues as a result of the process of decentralisation and boosting the administrative capacities.

7- Transfers for social protection

The transfers for the social protection include (i) payments for social assistance including economic allowance and payments for the disabled persons; and (ii) payments for the national service of employment covering the unemployment allowances. The policy of the government aims at the progressive reduction of subsidies for payments and programs of social insurance and re-allocation of the courses into the programs of the social protection. This is going to be accompanied with taking of measures for improving management, identifying and taking into account the programs of social protection, to the effect of improving the effectiveness of this

assistance. The transfers for the social protection in total are foreseen to reach 1.52% of GDP in 2010 compared to 1.44% of GDP in 2006.

B. Public investments

The public investments are financed by two sources: the foreign and internal ones. The new procedures of investments were introduced in 2007, to the effect of strengthening the connection of the policies of the government and allocation of the budget funds, as well as for the development of an Evaluation Cycle for the identification of the Public Procedures in the framework of the System of the Integrated Planning. With the implementation of these procedures, the government aims to point out the problems of information and management which have limited its powers for the use with effectiveness of the sources of the foreign financing available.

On the one hand, the foreign financing for the period 2007 – 2010 has been foreseen to be reduced every year reaching 1.98% of the GDP in 2010 (in addition to the fact mentioned above for the figures foreseen for the period 2008 – 2009 which are connected to the financing of the road Durres Kukes Morine) which reflects the increasing level of economic development of Albania. On the other hand the capital expenses with internal financing shall be increased every year reaching 4.37% of the GDP in 2010 which shall go mainly to the priority sectors, such as education, health and infrastructure.

2.1.3. Levels of Debt Development

The public debt in the Republic of Albania is represented by the debt of central government, since for the moment the local government does not yet have the right to emit securities for the public debt. The debt of the central government consists of the debt of financial instruments (bonds and obligations) as well as the contracted debt consisting of the different credits taken or guaranteed by the Albanian state for concession and trade interests.

The stock of public debt at the end of 2006 was 54.97% of GDP. Later 2007 it is foreseen that this stock reaches 53.61% of the GDP, divided into the debt with financial instruments for a total of 37.7% of the GDP, in the meantime the contracted debt is foreseen to be 15.91% of the GDP.

Policy of Debt Management for 2007

The management of the public debt in 2007 has been in compliance with the objectives set at the beginning of the year and with the debt strategy for the period 2007 2009. The situation of the debt and its services has been realised and it is foreseen as follows (Table 7):

Table 7: Characteristics of debt .

	2005	2006	2007
Stock of Internal Debt (million lek)	327,353	348,935	370,276
Stock of Foreign Debt (million lek)	140,729	145,649	156,250
<i>Stock of Debt in total (million lek)</i>	<i>468,083</i>	<i>494,584</i>	<i>526,526</i>
Stock of Internal Debt in Euro (million)	1,147.97	1,176.01	1,250.00

Exchange rate in lek/EUR	122.59	123.85	125
Stock of Internal Debt /GDP (%)	39.82	38.78	37.70
Stock of Foreign Debt /GDP (%)	17.12	16.20	15.91
<i>Stock of Debt in total / GDP (%)</i>	<i>56.94</i>	<i>54.97</i>	<i>53.61</i>

According to the forecast for the end of the year, the composition of the stock of public debt shall be:

- ▣ Debt with financial instruments: 70.3%;
- ▣ Contracted debt for the financing of projects: 29.7%.

During 2007, the financing of the deficit with internal net loan shall be realised entirely with the market instruments at the amount of 17 800 million lek, representing 1.81% of GDP. At the end of 2007, the stock of the financed debt with financial instruments shall be 370 276 million lek, or 37.69% of the GDP. The structure of this stock according to these instruments are foreseen to be as follows:

- ▣ Short term instruments (treasury bonds 3/m, 6/m and 12/m, re-evaluation of the currency reserve) 67.54%;
- ▣ Long term instruments (obligations 2, 3, 5, and 7 years) 32.46%.

The policy of issuing the securities has been oriented towards the long term instruments, the stock of which has increased by 59.16% compared to the stock of the year 2006, in the meantime that there has been reduced by 10.28% the stock of instruments with maturity time period up to one year.

This policy has been followed to the effect of reaching the objectives for the reduction of the re-financing risk and the risk of interest rates. Consequently, the indicator of the days in maturity has increased to 309 days at the end of September 2007 from 242 days, which it was later 2006. This indicator is higher than the forecast done in the previous strategy, which foresaw that the days in the maturity later 2007 would be 280 days. This indicator shall continue to increase later this year foreseeing even the emission of the 7 year obligations.

The increase of the average days in maturity of the debt portfolio had a direct impact on the indicator of the financial duration of the portfolio of securities of the Government. This indicator has been constant compared to the beginning of the year. Later 2007, the duration is foreseen to be at the value of 0.9756 and according to the forecasts at the end of 2008 it shall be 1.5624. At the same time the indicator of the weighted average yield of the debt portfolio has gone through increase compared to the end of 2006. This indicator has reached 7.677 % at the end of September compared to 6.871% which it was later 2006. It is believed that the weighted average yield later this year reach 7.858%. In this increase there has been taken into account the emission of the 7 year obligations in December 2007.

A deepened analysis of financing risk makes us understand that this risk has started to be reduced with the increase of the emission of the long term securities. Exactly in the stock of debt they have gone through an increase of their specific weight by round 8%, which has an impact on the

increase of the average maturity days and in the reduction of the risk of re-financing. With regard to the external debt, later 2007 the stock is foreseen to reach 156.250 million lek, divided into:

- External state debt 125 490 million lek;
- External guaranteed debt 28 580 million lek;
- Re-scheduled debt 2 180 million lek.

Regardless of the new needs for loan-taking, the relationship of the debt stock to the GDP is foreseen to be decreased later 2007, compared to 2006, from 54.97% to 53.61%. This result comes mainly from:

- Reduction of internal loan-taking needs due to the privatisation revenues;
- Nominal increase of GDP.

Tendency of interest rates for 2007.

Later 2007, the indicator of the public debt service appears as follows (Table 9):

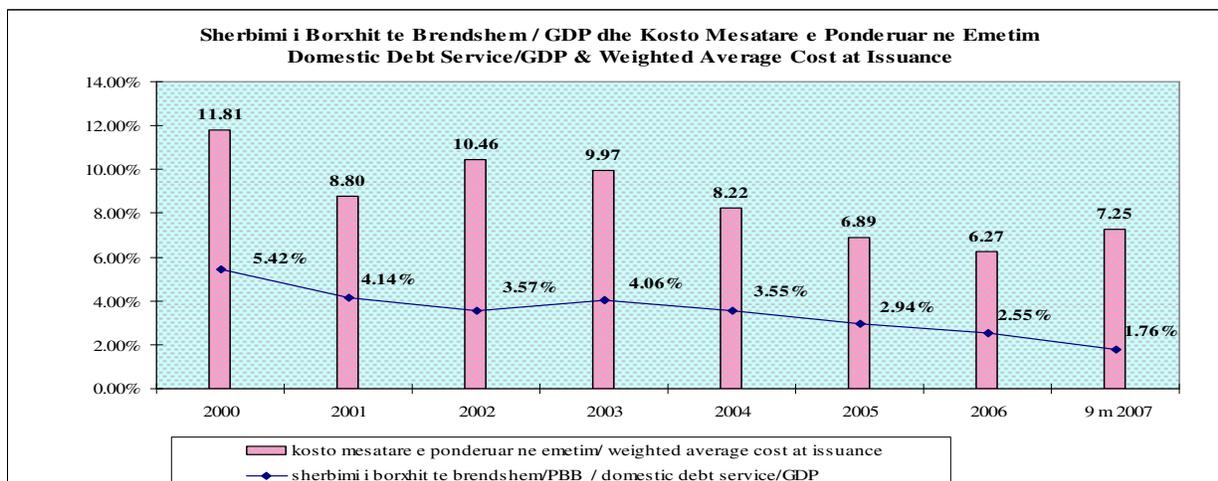
Table 9: Indicators of the debt service (million lek).

	2005	2006	2007
Debt Service in Total (1+2+3)	29,393	29,597	31,982
Debt Service (1+2) only interests	26,029	25,007	26,882
1. Service of Internal Debt	24,184	22,978	23,482
2. Service of External Debt	1,845	2,029	3,400
3. Principal Payment of External Debt	3,364	4,590	5,100
Debt Service (1+2+3)/GDP	3.58	3.29	3.26
Debt Service (1+2)/ GDP	3.17	2.78	2.74
Service of External Debt /GDP (2+3)	0.63	0.74	0.87
Service of Internal Debt / GDP (1/ GDP)	2.94	2.55	2.39

Even through starting from the second half of 2006 there has been interrupted the falling tendency of the interest rates of the securities of Government, which has been a characteristic since 2002, the policy of emissions has allowed to stabilise the indicator of expenses for interests of the internal debt in % of the GDP.

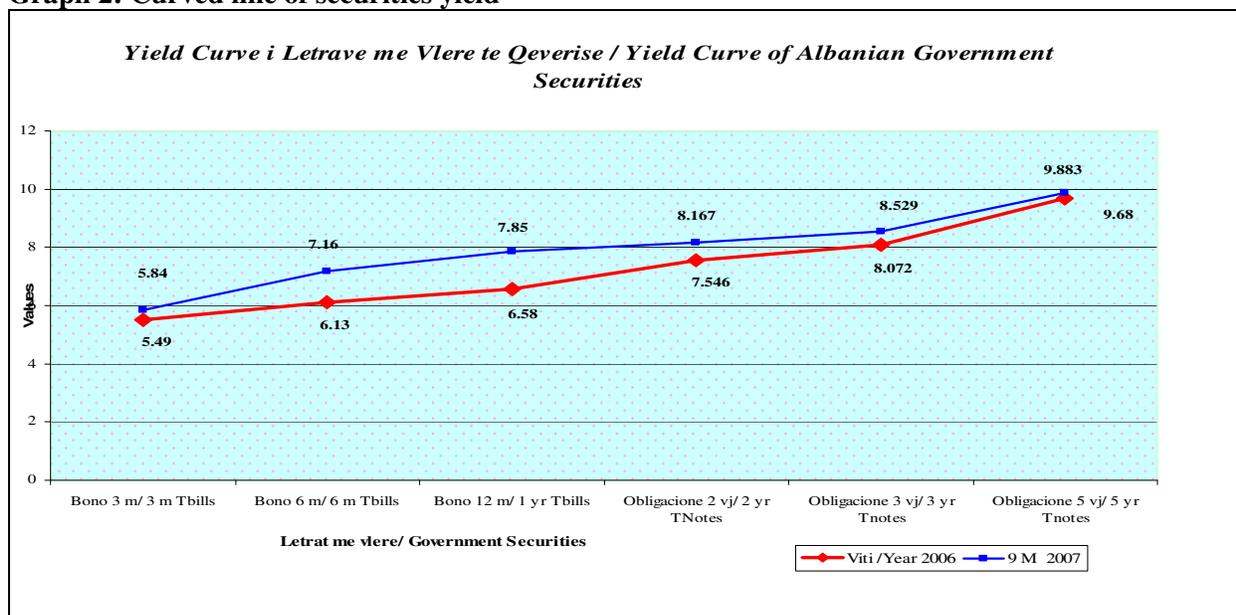
Concretely, out of 2.55% of the GDP in 2006, these expenses are foreseen to be reduced to 2.39% of the GDP later 2007. This reduction has been as a result of the reduction of the indicator of internal annual loan-taking, which compared to 25 billion which were foreseen was reduced to 17.8 billion , as a consequence of the privatisation of the state company “Albtelecom” as well as a consequence of the real annual growth of GDP by 6%. The increase of the interest rates has had an effect on the weighted average cost in the emission of the titles of state, which has been increased to 7.25% at the end of the first 9 month period of 2007, compared to the 6.25% of the end of 2006 (Graph 1). The impact of this increase shall be covered by the economy through the growth of real GDP by 6%.

Graph 3. Internal debt service.



The increase of the interest rates during 2007 was a consequence of different macroeconomic factors, the increase of the basic interest rate by the Bank of Albania, extension of the maturity of debt portfolio, situation of liquidity in the market. Taking into account the development of interests of securities of the government, we can say that compared to 2006, there is seen an upwards displacement of the curved line of the weighted average yield of the securities. Concretely, the on-year bonds have had the maximal increase with 127 basis points, while the 5 year obligations, the minimal increase by 20 basis points (Graph 2)

Graph 2: Curved line of securities yield



The service of the external debt appeals also increasing. An impact on this was exercised by the increase of disbursement as well as the repayment of the principle of the debt. The government has been committed in doing the priority investments at the right time, for this reason, within the limits of loan-taking from abroad the aim was the increase of the level of disbursement and the implementation in time of the projects.

Participants in the primary market

To the effect of improvement of the management of public debt, Ministry of Finances has implemented policies which aim at the development of the primary market of the securities of Government, through the extension of the basis of investors and increase of the kinds of instruments.

In the auctions of the treasury bonds there has been increased the participation of individuals, non-banking sector, as well as second level banks. The participation of the latter has been high even in the auctions of the obligations.

This has brought about a change in the structure of the internal debt structure, depending from the holders. Concretely we have had an increase of the percentage of the second level banks portfolio, non-banking sector and individuals.

With regard to the demand of the market with regard to the securities of the Government, we can say that during 2007 the indicator of the amount demanded on the offered amount for the treasury bonds and obligations has on average been higher than 1, which indicates that the demanded amount has been higher than the offered amount.

Reception of evaluation of “Credit Rating” in June this year from Moody’s Investors & Service, with B1 shall have an impact on the absorption of foreign investors. While the use of the Reuters system shall make more efficient the process of development of auctions of the securities.

A positive step is the signing in September 2007 of the new agreement with the Bank of Albania for meeting the long term obligations in the form of registration, through which there are determined the procedures for the participation in the auction of the natural and legal persons, local and foreign ones.

With the signing of this agreement, the Ministry of Finances aims at extending the basis of investors in the primary market of obligations, among the individuals, insurance companies and other financial institutions.

Assumptions of the Debt Strategy for 2008–2010

Fiscal Deficit: According to the forecasts of the Ministry of Finances, the budget deficit and the internal financing shall be at the levels of 2.35% in 2008 and 2.3% in 2009 and 2010.

Growth of GDP: Continuing with the speed of its growth, the GDP in real terms assumes its growth at the levels of 6% for the period 2008 – 2010.

Inflation: Forecasts for inflation are at the levels 3-4%.

Interest rates: Year 2007 has been characterised by a standard situation of the interest rates appearing at its beginnings with increasing tendencies due to the inflation which appeared in the

period August September. These factors have been taken into account in foreseeing the debt service for the years 2008 – 2010.

A) Main objective of the debt strategy continues to remain:

- Reduction of risk and decrease of the debt cost, seen in long term periods;
- Development of the market of securities, increase of number of instruments and improvement of its infrastructure.

With regard to the debt, there have been taken into account these assumptions, with regard to the risk of re-financing:

- Decrease of the internal debt ratio towards the GDP in the period 2008 – 2010 from 37.59% to 35.64 %. The portfolio with regard to the emitted debt for the re-evaluation of the currency reserve of Bank of Albania does not differ and it has been assumed to be constant after 2008.
- The net internal loan-taking is foreseen to be at the levels 2,35% up to 2,3 %of GDP in the years 2008 – 2010.
- Extension of the maturity period for the internal debt. The ratio long term debt / short term debt is deemed to be improved considerably and the long term debt shall make up 48% in 2008 and 67.9% in 2010.

Risk of interest rates has been seen connected to such aspects as follows:

- ✚ Increase of number of instruments and diversification of portfolio in the internal market;
- ✚ Changing the ratio internal debt / external debt to the favour of the external debt.

Operational risk

The adoption of the procedures of the Reuters system for the development of the auctions is considered to be one of the main factors during 2008 for the improvement of the organisation and their reporting having an impact on the increase of liquidity and decrease of the yield level.

Exchange rate risk

The additional amount of foreign investment and of the ratio of foreign debt to the GDP shall be considerable during 2008 and it is going to be moderated in the years 2009, 2010. Although the public debt to the GDP shall increase, again it is considered to be at constant levels due to the high level of the primary deficit and interest rate which remains lower than the GDP growth. In the forecasts of the basic scenario, there has been taken into account a devaluation of the money to Euro for the end of 2007 (Table 11).

Table 11. Basic Scenario

Denomination	2006	Proj. 2007	Proj. 2008	Proj. 2009	Proj. 2010	
Domestic Debt Stock (million lek)	348,935	370,276	404,056	431,118	460,859	Domestic Debt Stock
External Debt Stock (million lek)	145,649	156,250	199,640	206,640	216,480	External Debt Stock
External Debt Stock (million	1,176.01	1,250.00	1,610.00	1,680.00	1,760.00	External

Euro)						Debt Stock in Euro
Exchange rates EUR/ Lek	123.85	125.00	124.00	123.00	123.00	Exchange rates
Domestic Debt Stock/GDP (%)	38.78	37.70	37.59	36.64	35.64	Domestic Debt Stock/GDP
External Debt Stock/GDP (%)	16.19	15.91	18.57	17.56	16.74	External Debt Stock/GDP
Total Debt Stock	494,584	526,526	603,696	637,758	677,339	Total Debt Stock
Total Debt Stock/GDP (%)	54.97	53.61	56.16	54.20	52.38	Total Debt Stock/GDP

B) Operational objectives for realisation of the debt strategy

Debt composition

2007 Internal debt 70% (including the re-evaluation of the currency 3%)
External debt 30%

Forecast 2008 Internal debt 66.9%
External debt 33.1%

Refinancing of the internal debt

2007 Short term debt 67%
Long term debt 33%

Forecast 2008 Short term debt 48%
Long term debt 52%

Objective 2010 Short term debt 33%
Long term debt 67%

Number of average maturity days

Later 2007, the average number of days immaturity is foreseen 347 days including the portfolio of Bank of Albania. For 2008, our objective is that this indicator will reach 629 days with a tolerance of + 10 days. While the duration of the total of portfolio for the end of 2007 is foreseen 0.97 and 1.56 for 2008.

2.2. Quality of Public Finances

Deepening the institutionalisation of the Medium Term Budget Program

With regard to the expenses, the Albanian government has forwarded since 2001 the medium term budget program, which aims at strengthening the connections of the policies of the government and the allocation of the budget funds, and to reach the real value of money. All the line ministries were involved in the medium term budget program since 2006 and in a near future it is aimed at including all the other budget institutions. The medium term budget program aims at the gradual displacement from the budgeting based on input bases to the budgeting based on the programs and performance. During 2007, there were implemented new procedures of the projects of public investments in the framework of the medium term budget program, aiming at improving the identification of the projects and their evaluation.

Strengthening and institutionalisation of the fiscal intergovernmental relations

In the framework of decentralisation and strengthening the financial autonomy of the local government, there has been realised the transfer of the small business tax payers from the central taxation authorities to the administration of the taxation structures of the local government. This measure has had an impact on the facilities for the tax-payers of the rural zones, who now contact the administration of communes where they carry out their activity for the problems of the payment of taxes.

The process of local budgeting has so far been *ad hoc*. The mechanism of determination of the conditioned and unconditioned transfers is still unforeseeable and not completely transparent, being often the result of discussions and negotiations (bureaucratic and political) between the units of the local government and the respective line ministries. For this, there shall be further improved the horizontal equalisation to reflect better the demographic and economic dynamics of the different regions of the country, as well as their inequalities. In the field of conditioned grants the process of competing allocations for the investments, which has started in 2006 shall be extended. A new regulatory/legislative framework for the budget process of the local government shall be developed and shall be part of the new Organic Law of Budget. The new legal framework shall institutionalise the respective roles of the Ministry of finances and the local government, as well as the process of consultation of consultation among them, with regard to the management and monitoring of the local finances, wording of fiscal policies and the reforms proposed with regard to the decentralisation, in the framework of Medium Term Budget Program.

The improvement and clarification of the legislative framework for the process of implementation of the local budget. The main fields of the intervention of Ministry of Finances shall be: (i) procedures of treasury, mainly those connected to the big differences turning out between the foreseen amount of the conditioned grant by the units of local government and the effective amount; (ii) issue at right time and clarity of instructions and details by the Ministry of Finances with regard to the process of budget; (iii) regulations for the implementation of the budget with regard to the existence of a unique account of the treasury for all the revenues of the local government and consequently, with the possibility to have transfer and use of these resources in time of liquidity crisis; (iv) system of financial reporting and accounting and difficulties connected to the “follow up” of the expenses of local budgets and their use in accordance with the approved budget.

Improvement of the legislative framework of local taxes, taking into account the possibility of review of the basic taxation scales for the taxes on the property and small business, and the

possibility of adopting a provision which allows the local governments to modify the level of taxes based on inflation.

Implementation of a sustainable fiscal framework for the local loan-taking. The local governments do not yet take loans, but serious attempts are being made for drafting a law on the local loan-taking. For the approval and implementation of the local loan taking, the government shall ensure a framework of policies which set out clear rules on: (i) coordination of policies for the national and local loan (in a way that the central government keep under its control the nature and extension of the financial obligations of the local governments); (ii) ensuring a careful local loan-taking (with regard to the management of risks in the framework of public finances); (iii) system of local guarantees for loan-taking; (iv) restriction in volume of the public local loan, closely connected to the management of the public finances and the total public debt; (v) mechanisms of monitoring and control; (vi) solution of the cases of financial difficulties of the local government stemming from the loan-taking in order to avoid that central power be responsible for these financial obligations (Ministry of Finances).

Objectives of Investments of Public Sector

As it has been highlighted above, the continuation of the budget financing of the priority sectors such as education, health, infrastructure and defence by the Government and for the period 2008 2010 leads naturally to the allocation to these sectors of the budget resources destined for investments. With reference to the data of the Medium Term budget Program 2008 2010, in the following there are provided the main directions of funds of investments for these sectors:

Education

The capital expenses in this sector consisting on average round 9.7% of the total capital expenses foreseen for the period 2008 – 2010 shall mainly concentrate in the financing pre-university education for:

- Construction of new schools;
- Reconstruction of the existing schools;
- Provision with complete labs;
- Provisions of schools with internet services.

It is worth mentioning here that the allocated part for the construction and reconstruction of schools of pre-university education is provided in the form of competing grant for the units of local governance, which compete and are selected based on the projects forwarded and the criteria set out by the central government.

Health

The investments in this priority sector for the period 2008 – 2010, which make up on average round 5.9% of the total investment of the period 2008 – 2010 shall mainly concentrate on:

- Construction and re-construction of hospital facilities;
- Construction and re-construction of the primary service facilities;
- Purchase of medical equipment and apparatuses.

Infrastructure

Initially it is worth mentioning the fact that the capital expenses for this sector make up the biggest amount of total capital expenses, with round 62.7 percent for the period 2008 – 2010. In this sector, as the main directions of investments for this period, there can be mentioned:

- Road Durres-Kukes-Morine has been seen with priority for the development of the northern artery;
- Corridor North – South;
- Corridor East – West;
- Investments for extending and improvement of the networks of water pipelines and sewage systems;
- Investments in the port infrastructure;
- Investments in the housing field.

Defence

There needs to be highlighted the fact that with the figures of the draft budget 2008 it has become possible to reach the NATO standard of 2% of GDP of the budget expenses allocated for this sector, this being a tendency to be kept constant during 2008 – 2010. Referring to the capital expenses, it is seen that for this sector there have been allocated round 7.5% of the total expenses for investments mainly focusing in the improvement of the existing military infrastructure to the effect of reaching the standards of the NATO member countries.

2.3. Institutional Characteristics in the Public Finances

Amendments to the Organic Law of State Budget

During November 2007, ministry of Finances shall finalise the draft of the new organic law of the budget and shall forward it to the Council of Ministers for approval within this month. The main characteristics of this draft are:

- Institutionalisation of the Medium Term budget Program for the units of the central and local government, as well as the units of the special funds, in order to make a direct connection between the policies of the Government and the allocation of the budget funds;
- The design of a new chain of responsibilities specifying a clear list of responsibilities for all the actors involved in the process of the management of public finances;
- Restructuring of the fiscal relations between the local and central government;
- Implementation of the statistical standards and those of the public accounting in line with the international standards such as GFS and SNA 93;
- Implementation of the sanctions for failure to implement the procedures as they have been set out in this law.

Measures taken for improving the collection of revenues

In the upcoming months and years until 2010, there have been foreseen some important elements for the improvement of the system of the tax administration, to the effect of extending the taxable basis and compliance of the taxation policies with the national priorities. Among the most important successes reached so far, there can be highlighted:

a) Improvement of the functions of the service of tax-payers

The service of tax-payers has been considered as one of the most important components of the tax administration. The realisation of this objective has been aimed through:

- Increase of number of employees in the functions and service of tax-payers;
- Improvement of the quality of service;
- Providing accommodating facilities for these functions;
- Intensification of an aggressive media campaign for the clarification of the legislation;
- Inciting of voluntary performance of obligations by the tax payers;
- Considerable improvement of the website of Tax General Department which has to respond better to the needs of the tax payers. There is being completed a specific project with USAID.

In October this year, the Tax General Department there has been set up the Department of the Service of the Tax-payers which offers services to the big tax-payers and for the tax-payers of the zone of Tirana. This group of tax-payers do 75% of the total revenues at country level. The facilities in the service of this group of tax-payers are modern and with contemporary procedures.

b) Offering the service of the disclosure and payment of tax payment through the internet

Presently there has been completed the project for offering the service of disclosure and payment through the internet of the tax obligations. In the first phase, this project shall be implemented for the big tax payers, who shall have the possibility to withdraw their taxation declarations of VAT of the Insurance Contributions and Tax on Profit through the internet. At the same time, the attempts are focused on offering the service of the payment of taxes through this system. After testing this project with the big tax-payers, this service shall be extended also to the other categories of the tax-payers. This shall consist a considerable achievement of the performance of the taxation administration, with evident effects in the improvement of communication and contacts of these tax payers with this administration.

c) Transformation of the office of big tax-payers into a full service office

Out of 1100 tax-payers in total which are being administered by the Big Taxpayers Unit, 50% of them have their seat in Tirana and are totally administered by the Big Tax-payers Unit (they declare, pay and are controlled by this Branch).

The other part of the tax-payers hand over the statements and pay the obligations with the respective branches where they have the seat, while the functions of the taxation control are carried out by the Unit of Big Tax-payers. In two or three last years there has been realised the transfer of 5 biggest tax payers from the tax-payer branches in districts to the Big Tax-payers Unit (cement factories in Elbasan and Kruje, steel plant in Elbasan and some strong construction companies). Attempts are focused for the other potential tax payers be transferred to the

administration of this Unit later, depending from meeting the parameters set out (turnover they have). Within October, there was realised the opening of the Department of Service of Tax-payers in Taxation General Department, which offers quality services to the tax payers registered at the Unit of Big Tax payers, as well as to the other tax payers having a seat in the town of Tirana. This department has been provided with the necessary logistics; there have been provided the necessary conditions for receiving the tax payers, and there are implemented contemporary procedures for processing the requests and their resolution.

d) Strengthening the complaining system to guarantee the protection of tax payer at two levels: one appeal instance which has been set up within the taxation administration, and another, independent from the executive, which shall be set up in the form of a taxation court, as the last instance of the administrative review.

Strengthening the taxation policies shall in the upcoming years rely on three main fields:

A) Extension of the taxable basis and its distribution evenly and less distorting

In the present situation of fiscal evasion in Albania, the extension of the taxation basis has more to do with the administration of taxes, rather than with legislative changes. However, the taxation policies shall contribute to the increase of incompatibility of tax payers to their obligations to the state and in the improvement of the culture of taxes in Albania. The key policies shall be:

Adoption of a flat fiscal system, with lower tax rates. This shall be translated into the uniform taxation of the personal income (starting from a certain threshold) with a single scale of 10% and taxation of the business profit with the same rate. The fiscal reform undertaken in July 2007 (mentioned above) has turned out into a fiscal system with the lowest load among the countries mentioned above.

Management of fiscal compliance. The policies shall focus on the identification and reduction of the main resources of the fiscal evasion and narrowing the gap between the taxes collected based on the existing legislation and the taxes which effectively are collected. Studies and analysis from different sources, have identified as a field specifically affected by evasion the Profit on Personal Income and the contributions of Social Insurance. Another considerable source of evasion is failure to report to the effect of registration with VAT. Some of the legal changes which shall be implemented are:

- Determination of the integral declaration of income. The declaration of personal income considers as a key factor for preventing the taxation evasion on the personal income. This is because, under the present circumstances of failure to report and payment of salaries in *cash*, the controls and inspections for keeping the tax at source have not been effective in collecting additional revenues compared to their cost. Determining the integral declaration of the personal income shall have an impact also in collecting some taxes which presently are paid in insignificant amounts to the state budget, such as the taxation on income from rent and contributions of the social insurance. The decision for this policy to be long term is connected to the difficulties and serious restriction of the tax administration to manage appropriately the requirements of the integral declaration.

- Simplification and reduction of tax rates. The imposition of the flat tax and reduction of the social and health insurance contributions (which remain the highest in the region) shall reduce the taxation load on the employment and it is going to simplify the taxation schema. This policy aims at increasing the number of declared employees. At the same time, the reduction of taxation load for the businesses is expected to reduce the stimuli for failure to report of the turnover level to the effect of being categorised as small business. The reduction of VAT shall be considered in the long term period.

Changes in the taxation legislation and the respective instructions. The Albanian tax laws (specifically on the taxation procedures and profit tax) contain contradictory provisions, articles which are overlapped and gaps which have to be clarified. This situation provides the possibility to the taxation employees to exercise their discretion in the interpretation of the laws, paving the way to corruption and decreasing/discouraging the voluntary payments of the obligations. For this reason, there has started and will continue the review of all the rules and procedures for the harmonisation of the Albanian taxation legislation. In this framework, very important is the review and amendment of the law on the taxation procedures and the review and amendment of the procedures of collecting the profit tax.

In the framework of *transfer of the collection of the tax on the small business to the local administration*, there shall be provided a solution through cooperation to the problems which might arise from the administrative overlapping between the central and local tax administration in the course of performing their tasks, specifically those connected to the registration of businesses and the controls for failure to report the effective turnover.

B) Development of a tax system supporting the formulation of the fair fiscal and inciting policies for the economic and business development

Performance of the obligations stemming from the trade policy of Albania. The commitments in the framework of WTO and MTLs shall be reflected in the fiscal packages every year. These are:

- Signing the Unique Free Trade Agreement, CEFTA, Amended and Extended, which shall create the regional zone of free trade between Albania, Bulgaria, Croatia, Macedonia, Moldavia, Rumania and Union Serbia and Montenegro, as well as UNIMK, Kosovo.
- Negotiation and signing within 5 years from entry into force of Free Trade Agreement with EU of the Free Trade Agreement with Turkey.
- Abiding by the reviewed schedule, not making any further derogation, in the framework of commitments undertaken in WTO.

Establishment of the appropriate climate of investments:

- Evaluation of the impact of elimination of fee and non-fee barriers in the improvement of the business climate;
- Imposing the flat tax. Along with the advantages mentioned above with regard to the extension of the taxable basis, this policy is expected to increase the competitiveness of the Albanian Economy through the improvement of the business climate. Although there has not been proven a direct connection between imposing a flat tax and the macroeconomic development of a country, the analysis done on the economies of a number of countries, where this tax has been imposed, have shown a positive tendency of the growth of economy after imposing this tax (see case of Slovakia).

- Rationalisation of the number and kind of taxes to reduce the load on businesses. Considering the entire range of taxes which the businesses pay, the effective rate of profit tax exceeds that which is foreseen by the law (50% compared to 20% respectively).

C) Approximation of policies on taxes to the European legislation

The policy shall focus on the approximation of the legislation on the indirect and direct taxes, and gradual reduction and elimination of the trade barriers with EU countries.

Strengthening of Performance and Reliability of Taxation Administrations

The main policies shall consist in the concentration of the attempts on the main resources of the fiscal resources and the reduction of the gap between the collectable tax according to the taxation legislation and those effectively collected.

Strengthening of management of compliance with taxes. The compliance with the taxes shall be translated onto the voluntary payment of the obligations to the state by individuals and businesses. The Taxation General Department shall displace the focus of its work from the objective fulfilling the plan of revenues towards the management of compliance with the taxes. This change of working objectives shall require close monitoring of the level of compliance of the tax payers with their fiscal obligations with regard to the registration, declaration, payment, failure to report and other ways of fiscal evasion. The attention shall be focused on:

- Improvements in the collection of the taxation on the personnel income and social contributions. In the short and medium term period, the policies shall focus on the simplification of procedures for the disclosure and keeping at source of personal income tax and social contributions, intensification of controls on the obligations of disclosure and payments, and joint auditing for both taxes, in a way as to make use of the scale economies and increase revenues as a consequence of the combination of both functions. In the long term period, there shall be determined the integral disclosure of revenues, accompanied by a program for the improvement of the compliance of individuals with the law, based on the effective controls on the disclosure and payment, in effective auditing processes and efficient administration of the outstanding payments.
- Improvement of the VAT administration: strengthening the controls on the implementation and payment of VAT, and resolving the problems of non-reporting. A key element of implementation of this tax is the reimbursement, which has important effects on the compliance and its payment by the tax payers. For this, the strategic plans of TGD and the management of performance shall have as objective the full implementation of the obligations of the non-reimbursed VAT and the identification and implementation of the work methods for ensuring the reimbursement of this tax in time.
- Simplification of the registration procedures and payment of taxes. With regard to the registration of businesses, the establishment of the system one stop shop, shall eliminate the segment of registration with the tax administration, reducing considerably the registration time. With regard to the simplification of the procedures for the payment of taxes, in the long term there shall be considered the possibility of payment through internet, relying on the monitoring of developments with regard to the use of internet by business and balancing the cost and the benefits.

- Improvement of registration and collection of taxes, to prevent the violations of the tax legislation.

Protection of markets and society

This is about one of the missions of the customs administration. The policies followed by the latter for reaching this strategic objective shall be:

- *Implementation of measures for preserving security of international trade* and for the prevention of the terrorist acts and organised crime;
- *Improvement of the computerised system of the method of controls*, based on the management of risk, exchange of information on-line with the international specialist structures;
- *Customs shall play the role of a coordinating institution*, responsible for the control of goods which go through the external borders of Albania, in the framework of Integrated System of Protection of Borders of Republic of Albania. The control of goods movement shall be realised with modern methodology used in the EU countries for the examination of goods and transporting vehicles;
- For the performance of its protective function, the Customs shall *be provided with control means and modern apparatuses for inspection* and the staff shall be trained for the efficient use of them.

Boosting of performances, strengthening of control on management and internal auditing on the tax administration

The policies in this field aim at improvement of the situation connected to the inappropriate of the procedures, absence of the management based on the risk, absence of effectiveness of auditing, absence of training of employees etc.

Improvement of capacities for strategic management. This shall ensure that TGD evaluate and react to the developments and internal and external changes, identify the biggest risks which might appear with regard to the revenues, to decide measuring ways of the performances of employees and manage the activities based on the priorities set out in the strategic plans. This is going to avoid the use of practices of implementation of measures which are not based on strategic analysis and objectives.

Boosting of new knowledge of personnel on the procedures, so that the employees understand adequately and implement strictly their tasks on day basis, in accordance to the functional and manual structures of the procedures.

Improvement of procedures and system of auditing of taxpayers. There shall be established an auditing system selecting on the basis of risk, supported by a software for the evaluation of risk, which shall ensure the selection of tax payers based on the objective criteria. The schema of auditing shall pass from one all-inclusive schema, as it presently is, into a closer one, or focused on specific cases. There shall be prohibited the procedure practice of obligatory auditing. There shall be held trainings supporting the establishment of the modern techniques of auditing.

Review of the efficiency/effectiveness of the use of the resources in tax administration. Some of the intervention fields are:

- Review of the role of tax police. Human resources shall be displaced from the less successful activities to the collection of revenues, towards the high productiveness activities (such as the auditing, implementation of the law etc) which assist in the increase of voluntary payment of obligations;
- Establishment of big regional branches (14-15), which shall include the present small branches of taxes (presently 37 in all Albania); transformation of the present regional branches to offices of tax service;
- Orientation of the sources towards the big tax payers, improvement of the structures of the branches of big tax payers, taking of measures for strengthening the control on the performance of obligations.

Strengthening of the work of the Anti-Corruption unit, set up within the tax administration, for combating the corruption, fraud and theft; review of the Code of Ethics, set up of the services of the professional and moral standards.

Strengthening of the internal auditing procedures, through the conduct of investigation on the irregularities at work, implementation of the complaining procedures. At the same time the simplification and clarification of procedures and rules shall prevent the discretionary decisions of the employees in the course of accomplishing their tasks.

Strengthening of the management of human resources. Setting out transparent terms for the recruitment, promotion and dismissal of employees, in accordance with the basic rules of the public service and the law on tax procedures; gradual involvement of the tax employees in the public service; intensification of training, specifically in the field of auditing, and reaching the full observation of the legislation and regulations which have to do with the procedures and issues of human resources.

*The completion of computerisation of taxation administration, inclusion into the SIT (Tax computerised System) of all the kinds of taxes, communication *on line* with the taxation regional branches/ Setting up of the Taxation Computerised System shall be financed by European Union.*

3. STRUCTURAL REFORM OBJECTIVES

3.1. Sector of Enterprises

3.1.1. Development of Enterprises of Private Sector

The development of the private sector is considered one of the main contributors to economic growth, employment and reduction of poverty. During 2006 there has been ensured an economic growth of 5% towards the GDP. The private sector contributed in more than 80% in GDP and round 70% in employment.

The private sector has gone through an increase during 2005 – 2006. With reference to INSTAT data, the number of active entities until the end of 2006 reaches 77 814, out of which 974 are companies with foreign capital. The active enterprises for 2006 turn out round 20% higher compared to 2005. With reference to the structure of enterprises, small and medium sized enterprises, SMEs, (according to the definition of EU) with up to 250 employees consist 99.9% of all the active enterprises.

During 2006, there has been found out a quick increase of the new enterprises, set up recently, and respectively with 14 372 new entities out of which 108 businesses are with entirely foreign or joint capital. Birth coefficient for 2006 is 18% with an increase to that of 2005 which was 15%.

With regard to the geographical distribution of businesses in Albania, round 51% of the active enterprises have focused on the prefectures of Tirana and Durres, where there have been employed 57% of the employees in the private sector. The distribution of SMEs according to the sector of economy are trade with 49%, services (with 26%), industry (with 10%) and transport (with 9%). In the sectors of trade and services where 75% of the businesses are operating, there have been employed 45.2% of the employees of the private sector.

The figure of entrepreneurship ensured from the sector of trade and services consists round 63.8% of the total figure of entrepreneurship, while the figure of entrepreneurship ensured by the sector of production and construction consists 36.2% of the total figure of entrepreneurship.

The influx of IHD for 2006 are calculated in 258.6 million Euro, which consist round 4% of the GDP. The IHD stock until later 2006 is calculated with round 1.8 billion Euro. IHD per capital for 2006 are round 83 Euro per capita. Round 72.5% of the enterprises with foreign capital are focused in the prefectures of Tirane and Durres, round 7% in Korce, round 4.4% in Shkoder, 4.4% in Fier, 4% in Vlora.

The structure of exports for 2006 turns out at the extent of 29.9% from the internal production and 70.1% from the production with ordered material (active processing). The exports from the enterprises of industry (non-food) consist 92.1% of the total exports or 725.3 Mln/\$, with an increase to 2005 by 19%. These exports have been dominated in more than 60% by fason.

The exports from the food industry enterprises and agricultural products consist 7.9% of the total of exports or 62.8 million USD (a steady weight in these years) with an increase of 16.2% to 2005 and they are considered for the most part by the internal production.

3.1.2. Policies Launched for the Development of Private Sector

Among the important measures which have been launched by the Albanian government for the implementation of economic reforms, have at their foundations the reforms for the development of the private sector, specifically for SMEs. During 2005-2006, the Government has undertaken inciting policies for the development of the free entrepreneurship, consisting in some of the main directions:

Facilitation of the procedures to enter into business

The regulatory reform which has been undertaken by the Albanian government since October 2005 aims at the facilitation of the practices and procedures of entering into the business market making the regulatory environment more transparent, foreseeable, simplified and equal for all the local and foreign businesses.

In the framework of the regulatory reform, during 2006, there has been shortened the legal time period for the registration of business with the court from 30 days to 8 days (*law no 9536, dated 15.5.2006 on some changes to the law no 7667, dated 28.1.1993 "On trade registration and formalities which have to be observed by the commercial companies"*) as well as in September 2007, there was made possible the start of functioning of the National Registration Centre, which functions as a one-stop-shop.

Reduction of Informality in Economy (unmonitored economy)

During 2006, there has been reorganised the inter-ministerial group for the reduction of the informal economy upon the order of Premier no 145, dated 27.6.2006. It has reviewed the action plan “On reduction of informal economy for the period 2006 – 2009” approved by CMD no 430, dated 28.6.2006. The measures foreseen there aim at avoiding the fiscal evasion in the field of taxes and social insurances, as well as reduction of the CASH in economy.

The outcome of the monitoring the action plan for the reduction of informal economy during 2005 is that out of 25 programmed measures, there have been realised 20 measures, and the other parts are under process for 2007.

Facilitating policy in the fiscal field

During 2005 – 2007, there have been taken a series of measures in the field of taxes for the facilitation of the fiscal load for businesses summarised as follows:

- Reduction of the profit tax from 20 to 10%;
- Reduction of the simplified tax on the profit for the small business from 3% to 1.5%;
- Reduction of the fiscal load for the tax pertaining to social insurance for the employer by 9 points percentage (from 29% to 20%);
- There has been reduced the price of electrical power by 30-40% to the effect of reducing the cost and making the Albanian goods competitive;
- There have been repealed or halved a considerable number of taxes and fees, in the spirit of ‘Albania 1 Euro’;
- Clarification and transparency of the provisions for complaints;
- Clarification of provisions pertaining to the reimbursement of VAT, shortening of time periods for asking for the reimbursement, facilitation of the reimbursement procedures for the exporting companies; imposing the obligation for paying the interests by the taxation administration in case of delay beyond the time period set out by law for the return of reimbursement amount, etc

Improvement of financing of SMEs

Although the levels of financing the private companies have increased, it is still considered insufficient to incite fast development of the sector. In order to improve the climate of financing, specifically that of SMEs, there have been taken in the recent years a series of measures connected mainly to the introduction of the schemas of guaranteeing the credits of SMEs.

Approval of Fund for guaranteeing the export credits

The Council of Ministers approved upon CMD no 489, dated 25.07.2007 “On the fund for guaranteeing the export credits” the establishment of a limit fund, within which there shall be granted guarantees for the export credits starting from 2007. This fund is a part of the guarantees granted by the state and the maximal limit is 200 million lek and it shall continue to be used for a time period of 6 months.

The increase of funds for micro-credits

The non-banking financial institutions with the support of the donors are contributing for meeting the needs for small credits not only in the urban zones but also in rural zones. To this effect, there has been signed the agreement between the Albanian government and KfW (ratified by the parliament at the end of 2006) for a fund of micro credits for the small business in a value of 2.6 million Euro and there is expected its disbursement. During February 2007, the Spanish Agency for International Cooperation has signed an agreement with 3 institutions of the micro credit for financing with a fund of 13 million Euro.

- *Making functional the law on leasing No.9396, dated 12.05.2005*

The introduction of the leasing services could be considered as a financial alternative for SMEs, having an impact on the development of business and boosting of employment. During 2006, there has started the leasing activity, but so far there have entered into the market only 4 leasing companies so far.

- *Drafting of the law on factoring* is another supporting measure which shall facilitate the crediting of the accounts for the supplying companies of goods and services. Parliament has approved the law no 9630, dated 30.10.2006 “On factoring”.

Establishment of the competitiveness fund

To the effect of supporting the SMEs and for boosting their competitive capability, upon the CMD no 112, dated 21.02.2007 “On establishment of the Albanian fund of competitiveness” the government has determined a fund of 25 million lek. There shall be financed the companies for a period of three years, with co-financing up to 1 million lek, but not more than 50% of the value of the project cost. The activities which shall benefit from this fund are connected to the improvement in the system of management, product certification, market studies, marketing of products, participation in the fairs and exhibitions etc. Albinvest is the agency which shall manage this fund. Until later September 2007, there have been approved the projects of 16 exporting companies.

Improvement of institutional framework

- *Setting up of Albinvest agency*

To the effect of implementing in a more efficient way the policies and programs of government in the field of development of businesses and investments, there has been set up the Albanian Agency of Business and Investments, by law no 9497, dated 20.03.2006.

Based on this law, there has been approved the statute of Albinvest, by CMD no 514, dated 26.07.2006. The Albanian Agency of Business and Investment Albinvest is responsible for the implementation of the policies of government in the field of promoting SMEs, of the support of exporters, promoting the direct foreign investments. This agency has a staff of round 31 persons and a budget for 2007 of 693 500 Euro (in which there is included also the fun for competitiveness of 203 thousand Euro) with a considerable increase from the budget of the three agencies taken together for 2006 which was 354 300 Euro.

Strengthening the dialogue government – business

- *Approval of law for the Consultative Council of Business*, no 9607, dated 11.09.2006, shall have an impact on the improvement of the dialogue government – business. There has started the functioning of the CCB. The CCB has in its composition 18 members, out of which are representatives of the business community. According to the standing rules of the functioning

of this council, there is operational the secretariat of CCB and there have been set up the commissions on *ad hoc* basis, according to the problems which concern business. During 2007, there have been held 4 meetings of CCB, where there have been discussed different draft-law specifically the fiscal ones.

- *Approval of the law for the Trade and industry Chambers*
There has been approved by the parliament the new law no 9640, dated 9.11.2006 “On industry and trade chambers”. This law consists in the improvement of the functioning and organisation of the trade and industry chambers. Thus the number of the chambers was reduced to 12 compared to 36 which existed earlier, being organised on region basis to the effect of their strengthening.

Drafting of medium term strategic program 2007-2009 for SMEs

To the effect of inciting the improvement of competitiveness of SMEs, there has been drafted the medium term strategic program 2007 – 2009. There have been programmed to be undertaken a series of measures for a medium term period, starting from the preparation of the legal framework, setting up of institutions, drafting the action plan and implementation activities.

During 2007, there was convened twice the forum of donors in the field of SMEs, where there was introduced and discussed the strategic program of SMEs, an on 17 October 2007, there was realised the signing of the memorandum for setting up the Forum of Donors for the implementation of the strategic program of SMEs for the period 2007 – 2009. This memorandum was signed by 11 donors, who operate in the field of SMEs as well as there has been hailed even by the other donors who are not signatories, but they are important part of implementation of the strategic program of SMEs. The memorandum institutionalises the forum of donors for SMEs to the effect of focusing and coordinating all the projects and new initiatives which shall be launched by donors and projects for fulfilling the strategic program of SMEs.

The total objective of this strategic program is the steady economic development of the sector of SMEs through the increase of the number of the new enterprises, as well as continuous improvement of the indicators of productiveness, competitiveness and of exports. Specific objectives which shall serve for reaching this general objective are:

- i) Promoting the entrepreneurship culture;
- ii) Development of increasing businesses with internationalisation capacities;
- iii) Improvement of financing of SMEs.

Drafting the law on electronic signature

Since January 2007, there has started the process of drafting the law on electronic signature in compliance with the EU standards.

- There has been set up a working group with representatives from METE, MJ, MPPTT and local and international experts for the preparation of a policy paper, as well as for the new draft law on the electronic signature. They shall prepare a study on the needs for the changes in the existing legal acts in accordance with the electronic signature.
- There have been organised a couple of round tables with representatives from the interested institutions and from the business community to be informed on the EU legislation on

electronic signature and for submitting the first draft, as well as the changes in it after the comments of the different stakeholders.

- Until later 2007, there has been programmed to be prepared the draft-law on the electronic signature, as well as the discussion of the draft law with all the interest groups and the business community.

On drafting the law on the commercial companies

The Albanian government has, in accordance with the obligations foreseen in the Stabilisation and Association Agreement been committed to approximate the legislation on the commercial companies with *acquis communautaire*. Law no 7638, dated 19.11.1992 “On commercial companies”, as amended, is a law partially approximated to the EU directives on commercial companies.

Since January 2007, there is being done the entire review of the law on commercial companies, in accordance with the latest changes in the EU on commercial companies. There has been prepared the new draft-law on the commercial companies which was presented and discussed in some round tables for the period September - October 2007, with representatives of the interested institutions, law firms, as well as by the business community, judges of commercial cases.

 *For boosting the private investments in general and absorption of the foreign investment*, there contributes also the approval and implementation of the new law no 9663, dated 18.12.2006 “**On concessions**” which was based on the practice and in conformity with the EU directives, offers a better chance for the construction of the infrastructure works, in tourism, energy, road infrastructure, services etc. This law is being appropriately implemented in the sector of energy.

For implementing this law, upon the approval of CMD no 27, dated 19.01.2007 “On approval of the rules of evaluation and granting of concessions” there is being made possible the boosting of transparency, efficiency and equality in entering into a contract by the public authorities and for determining the specific procedures for awarding the concessionary projects.

In specific conditions this law provides for the granting of concessionary incentives with minimal prices such as that 1 Euro for priority sectors and regions. The implementation of this project finds the main support in offering the state owned property (assets, natural resources, economic activities) with 1 Euro. The government has some alternatives for which this project can be implemented.

3.1.3. Regulatory Reform for Improving the Business Climate

The regulatory reform initiated by the Albanian Government aims at improving the climate where business is operating in Albania setting up in this way the basics for a sustainable economic and social development.

At the centre of this reform is the continuous consultation with the groups of interest to the effect of taking into account of their demands in the process of improvement of the existing legal framework and drafting a new regulatory framework, for eliminating the administrative barriers. The regulatory reform relies on the platform approved by the government and is oriented in four main directions:

- Development of the management system of the Regulatory Reform;
- Improvement of the existing legal framework eliminating the unnecessary obstacles;
- Guaranteeing the quality of the new regulatory legal and bylaw framework;
- Monitoring the evaluating the impact of Regulatory Reform.

The platform of the government for the Regulatory Reform relies on the principles of the regulatory quality and so far there have been implemented some of them, among which:

- Periodic consultation with business;
- Accountability of state administration and business;
- Steadiness of the new legislation through the establishment of the mechanism of evaluation of compliance of the new legislation to the principles of the Regulatory Reform.

One year after implementation of this reform, there has been managed to conclude a series of measures, by which there have been eliminated or reduced a good part of obstacles, which are encountered by business in the course of exercising its activity. In this sense, there has been done good progress in setting up the responsible structures for the implementation of the reform as well as in some of the main fields where this reform has extended.

Establishment of institutional framework for monitoring and implementation of the Regulatory Reform

There have been set up all the responsible structures for the monitoring and implementation of the reform, such as, Task Force led by the Premier, Group of Coordination of Reform led by the Minister of Economy, Trade and Energy, and the technical groups for the 7 main fields of the implementation of the reform (registration of business, licensing, customs, taxation, land & construction, inspection and administrative complaint).

Task Force is the main responsible structure for the implementation and monitoring the regulatory Reform and determines the priorities of Albanian government in the framework of Regulatory Reform. The Responsible structure for following the implementation of this reform is the Ministry of Economy, Trade and Energy, which leads the process of drafting the plans of measures and reports to the Task Force on the development and problems of the reform. This structure is also responsible for the evaluation of the impact of the reform and organisation of periodic meetings with the business community.

The institutional framework which has been set up has been hailed by all the initiatives where we are participating, and in many cases Albania has been a reference for the other countries which have undertaken such similar reforms.

Total reformation of business registration

According to “Doing Business 2006”, the registration of a business in Albania encountered a considerable number of administrative and judicial procedures. In order to be registered, there were needed at least 11 procedural acts, 39 days and 580 USD. Relying on this emergency situation, the government undertook the legal initiative to shorten the legal period of registration at court, from 30 days to 8 days, bringing an improvement in the reduction of the registration time, however, the registration time continued to be long. In the meantime, the registration

process continued to be fragmented, based mainly in the direct contact between the interested persons and state employees.

In order to resolve this situation, the Albanian government and the Government of United States of America signed on 3 April 2006 the Millennium Challenge Albania Threshold Agreement for Albania, which is assisting in three big projects, among which also that of the reformation of registration process.

In cooperation with the project mentioned above, ministry of Economy, Trade and Energy proposed the setting up of the National Registration Centre, having full decision-making autonomy, with regard to the process of the commercial registration, as an one stop shop for the registration of business. The National Registration Centre started its activity on 3 September 2007, in its main seat in Tirana. In the meantime, there has been foreseen for this centre to function with its counters in 29 municipalities of the country. The process of reformation of registration shall realised through this centre:

- Transformation of registration process from a mixed process (judicial and administrative) to a fully administrative process;
- Registration within a single day, in a single step, closer to the beneficiaries and fully electronic;
- Boosting transparency, impartiality, and simplicity in registration;
- Simultaneous registration for commercial, fiscal effect, social and health insurance, and labour, in a single step;
- Simplification of requirements and documentation needed for the registration of businesses;
- Lowering the registration cost, elimination of the contact with administrative employees and consequently reduction of corruption;
- Offering the service at national level, extending it to the structures of the local government;
- Full compliance of standards in the registration process to the European directives.

For this, there have been recruited and trained the personnel who are going to work in these counters, and there have been already opened the counters in the towns of Elbasan, Tirane and Shkodër. In the meantime, based on a calendar, set out carefully, is being worked for opening the other counters.

It is expected that later 2007, the centre could function in 8 biggest municipalities of the country and later 2008 there can be opened all the foreseen counters.

Review of the licensing system

Licensing is another problematic field due to the very complex documentation which is being required to be handed over by the entities for being provided with a licence and due to the very long time periods. For this, during 2006, there were reviewed 135 licenses. Permits and authorisations in the sectors: mines, hydrocarbons, public works, transport, agriculture and food,

fishing, environment, water administration, forest and pastures, health, customs, protection from fire.

The outcome of the review of the licensing system, there is proposed: (i) elimination as unnecessary of 24 kinds of licenses, (ii) reduction of requirements for licensing for the other part at the extent 30-40%. The reform in the licensing system applies for the first time the introduction of the new principles in this process, such as:

- Transfer from preliminary control to the subsequent and continuous control;
- Application of the principle of silent approval in case the responsible institutions do not respond in time and the application of sanctions for these institutions. This insures the implementation of the principle of accountability of administration.
- Support of the request for license on the self-declaration of the responsibilities by the applicant for guaranteeing the requirements of the law and the application of the strong sanctions in case of the false declarations. This insures the implementation of the principle of accountability of business.
- Application of Guillotine which implies the removal of all the superfluous requirements for licenses in a specific field and elimination of the license where it is not connected to the life, health, environment or if it is deemed that its added value is insignificant.

There needs to be highlighted that a very important role in the process of review of permits and licenses has been played even by the business community. In the periodic meetings held in this community for the presentation of the recommendation issued by the Licensing Group, there have been shared the opinions of representatives of this community connected to this process. The comments and recommendations of theirs connected to the licensing process have been taken into account in the review of requests and periods of specific permits and licenses.

In the meantime, there are under the evaluation process the licenses, permits, certificates and authorisations issued by the ministry of Tourism, Culture, Youth and sports and Ministry of Labour, Social Affairs, Equal Chances for which the Licensing Group is working for drafting the evaluation reports and necessary recommendations in cooperation with the experts of respective institutions.

In addition to the process of review, the reform in the system of licensing includes even the process of monitoring of implementing the recommendations issued by the Licensing Group on behalf of respective institutions, in accordance with the time periods set out in the permits and licenses matrix.

For this, upon the Order of Premier no 97, dated 22.06.2007 “On setting up the Monitoring Group for the evaluation of implementation of recommendations for improvement of the licensing system” there has been set up the monitoring group, which is working based on the basis of a methodology approved by Task force.

The Monitoring Group has started work in July 2007 and so far it has monitored the implementation of recommendations in five of the line ministries included in this process:

Ministry of Public Works, Transport and Telecommunications, Ministry of Education and Science, Ministry of Economy, Trade and energy, Ministry of Health and Ministry of Environment, Forests and Water Administration.

In the meantime, there has started the process of monitoring for Ministry of Agriculture, Food and Consumers' Protection. It is expected that until later 2007, the process of monitoring be completed for all the line ministries for which the Licensing Group has made the respective recommendations.

At the end of this process, there shall be drafted the respective process on the extent of implementation of recommendations by the respective institutions.

Action Plan of Regulatory Reform

The Regulatory Reform relies on the action plan of Albanian government approved in CMD no 157, dated 31.03.2006, after one year of implementation, this plan has been reviewed by institutions involved there and it has been approved by Task Force in June 2007.

At the end of the year, there shall be done the evaluation of achievements, realisations problems etc, and there shall be done all the necessary changes to adjust them to the initiatives and policies of Government for implementing its program.

3.1.4. Progress of Privatisations in Strategic Sectors

I. Restructuring of KESH sha and initiation of procedures for the privatisation of the sector of distribution of electrical power

For the company KESH sha there has been realised the process of division of the activity of transmission and distribution of electrical power, as a company in itself. In accordance with the CMD no 862, dated 20.12.2006, there has started the process of restructuring and privatisation of the company of distribution of the electrical power, with the consultancy of the company IFC, selected to assist the process. IFC has selected the sub-contractors for the legal, technical and financial consultations. It has completed the due diligence of the legal, financial, and technical consultants and there has been prepared the draft report for the process of due diligence. The draft report is being discussed with representatives of the IFC, Kalo Associates; Ernst and Young; USAID-it, ERE and KESH, with regard to the main problems of it and to coordinate further the follow up of problems which are raised in this draft report. In addition to the above, there is being worked even for the legal and regulatory framework of the energy market.

II. Restructuring and privatisation of the company "Armo" Sh.a

In accordance with the CMD no 29, dated 24.01.2007 "On restructuring for the effect of privatisation of the company "ARMO" there continue the procedures for the division from ARMO of the assets and financial accounts for the activity of retail trading, as well as the process of preparation for privatisation of the retail trading stations.

For the privatisation of the activities of the refinery and wholesale trading, there has been selected the consultation company to assist in the process the company Patton Boggs. The company has started the process of due diligence with the company ARMO and in cooperation with the respective structures of METE it is working for completing the DATA Room of the company. The privatisation procedures shall continue in accordance with the recommendations of the consulting company.

III. Restructuring and privatisation of Servcom sh.a & “Albpetrol” Sh.a

The process of restructuring the companies Servcome sh.a. & “Albpetrol” sha is being realised in accordance with a CMD no 784, dated 15.09.2006 “On restructuring the commercial companies with state capital “Albpetrol sh.a.” , “Servcom sh.a.” and “Transnafta shpk””.

IV. Continuation of the concession contract of Water utility and Sewage Elbasan (Elber shpk)

Based on the Agreement of Delegation of the management team of Elber shpk from BWI with METE there continues the implementation of the program of investments in accordance with the provisions in the concession contract. In cooperation with the Ministry of Interior, MPPTT and Department for the administration of Public Property, there is continuing the process of transferring the water utilities to the authorities of the local governance.

V. Privatisation of the state package at AMC company

With regard to the sale of the state package of AMC, there has started the preparation of the legal framework for the institution of the sales procedures. There has been approved the CMD no 410, dated 11.07.2007 “On transfer of the package of shares of AMC sha, which has remained after the transfer of the package to the strategic investors, to the former owners of the land and to the employees of this company”, which foresees also the selection of the consultant for implementing the transaction.

In this framework, there has been informed the private partner at AMC about the start of procedures for the privatisation of state package at AMC sha and there has been requested from him to take the respective decisions on this transfer.

In accordance with the decision of the Consultation and Transparency Committee for the privatisation of the sectors of special importance of the economy, there shall be set up a working group, with representatives of Ministry of Economy, Trade and Energy, Ministry of Finances and Ministry of Public Works, Transport and Telecommunication, which shall coordinate the work with the leading authorities of AMC company for all the steps which shall be undertaken in the process.

VI. Privatisation of the company Albtelecom Sh.a.

There has been concluded the r-negotiation of the contract with the company Calik Enerji Telekomunikasyon and on 20 June 2007 there was signed the contract for the sale/purchase of the shares with this company. The price of purchase was 120 million Euro.

3.1.5 Competition Policy

The Competition Authority has, in accordance with the law no 9121, dated 28.07.2003 “On protection of competition” and of the other legal obligations, approved a series of bylaw acts which assist the CA to reach the set out objectives. In this way, there has been approved the regulation “On organisation and functioning of the Competition Authority”, the regulation “On setting of expenses for following up the procedures at CA”, “On implementation of procedures of consolidation of enterprises”, (which is being amended in accordance with the regulation no 139/2004 “On control of concentrations between the enterprises”, and 802/2004 “In accordance of the Regulation of Council (EC) no 139/2004 “On control of concentrations between the enterprises”), regulation “On fines and exception from them”, etc.

At the same time attempts are focused for adjusting the regulations of European Commission and concretely of the Regulation 1/2003 “On implementation of the rules of competition according to the Articles 81 and 82 of the European Treaty” and of the regulation 773/2004 “On procedures set for use by the Commission of Articles 81 and 82 of the Treaty”.

In accordance with the legal obligations, there has been approved and published the National Policy of Competition. There has been translated and adjusted in cooperation with GTZ the Vocabulary of Terms of Competition of European Union (OECD). At the same time, there has been published the Annual Report of the Competition Authority for 2006 and attempts are focused for publishing a Bulletin of the Decisions of the Commission of Competition.

The Competition Authority has followed the respective procedures for the re-establishment of the free and effective competition in the market starting investigations in different sectors of the market to the effect of prohibiting the abuse with the dominant position, prohibition of illegal agreements and concentrations which could bring about consequences in the market. The Competition Authority is investigating in different economic sectors, such as the sector of mobile communication, sector of insurance, banking sector, sector of the bread and concrete production etc.

With the approval by the Parliament of Albania of the decision no 96, dated 30.04.2007 “On approval of the structure and organigramme of the Competition Authority” there have been announced the vacancies and there have been held the respective competitions for these positions in accordance with the law no 8549, dated 11.11.1999 “On Civil Servant Status” and there has been recruited a considerable part of the personnel.

Within the short term priorities of the Competition Authority, we mention the consolidation of the secondary legislation on competition, strengthening the institutional capacities, implementation of the law and cooperation with the regulatory entities, courts to the effect of implementing the law “On protection of competition”. At the same time it aims at organising training seminars in cooperation with OSCD, GTZ; organisation of awareness seminars on the competition law, cooperation of CA with public institutions (through the signing of memoranda of understanding) as well as European counterpart institutions (memorandum of cooperation with Macedonia etc).

Among the medium term and long term priorities, we mention the drafting and the publication of the commentary in the field of the competition, drafting and approval of new regulations, such as that of fines and exemption from them, strengthening the regional cooperation, strengthening the

institutional capacities (increasing budget and personnel of competition), consolidation to the legal framework etc.

3.1.6. Policies in the Sector of Public Procurement

In the context of the commitments which Albania has assumed in the field of public procurement (Approximation of the legislation in the field of public procurement to *acquis communautaire*; Elimination of discrimination and removal of barriers and obstacles; incitement of participation and boosting of competence; strengthening the capacities of PPA and all the Contracting Authorities – Article 70 and 74 of SAA), there was drafted the new law “On public procurement, in line with the EU Directives in this field. This is the first phase of approximation of local legislation on public procurement to the Directive 2004/18/EC, 89/665/EEC and Directive 2004/17/EC, 92/13/EEC as it has been foreseen in the National Plan of Approximation of domestic Legislation to that of EU and implementation of SAA.

The new law no 9643 “On public procurement” was approved in the Parliament of Republic of Albania on 20 November 2006 and entered into effect on 1 January 2007. In the context of the needs which stemmed in the course of implementation of this law, in September 2007, there was approved the law no 9800, dated 10.09.2007 “On some changes and addenda in the law 9643, dated 20.11.2006 “On public procurement”.

Based on and implementing the new law no 9643, dated 20.11.2006 “On public procurement”< the Council of Ministers approved, by decision no 1, dated 10.01.2007, “Rules of Public Procurement”.

2. *New legislation on Public procurement determines the rules to be implemented for the procurement of goods, works and services by the Contracting Authorities in Albania.*
3. *The law no 9643, dated 20.11.2006 “On public procurement” aims at:*
 - a. *Incite the efficiency and effectiveness in the procedures of public procurement, implemented by the Contracting Authorities;*
 - b. *Ensure the good use of public funds and decrease the procedural expenses;*
 - c. *Incite the participation of the economic operators in the procedures of public procurement;*
 - d. *Incite the competition through the economic operators;*
 - e. *Ensure an equal treatment and non-discriminatory treatment for all the economic operators, participating in the public procurement procedures;*
 - f. *Ensure integrity and transparency in the public procurement procedures;*
 - g. *Selection of winners in public contracts shall be done in line with the general following principles:*
 - i) *Non-discrimination and equal treatment of bidders or candidates;*
 - ii) *Transparency of procedures;*

- iii) *Equality of demands and obligations which are imposed on the bidders and candidates;*
- iv) *Right of bidders or candidates for judicial or administrative review in case of not accepting them.*

Further steps provided for in the gradual approximation until the full approximation of the legislation “On public procurement”

The full approximation is connected to the approval of the respective laws and to the changing of the general economic and social situation in Albania. The full approximation to the Directive shall be done step by step considering the development of the approximation to the *acquis communautaire* of the legislation in its entirety. Presently the component “Reform in Public Procurement”, of the Millennium Challenge Threshold Agreement for Albania, administered by USAID, is assisting the PPA in setting up the electronic procurement infrastructure.

Main changes brought about by the new legislation on public procurement

The main principle of the new public procurement is the Principle of Transparency. In this framework, different from the previous legislation, there has been foreseen the obligation of the Contracting Authorities to publish electronically in the website of PPA the entire tender documents and further on all the notifications connected to the development of a procurement procedure from the notification of contract to the moment of publication of entering into the contract. This measure is an important achievement being hailed by the business community and at the same time it has addressed a big problem in the country, that of absence of transparency in public procurement. The law no 9643, dated 20.1.2006 does not provide for the direct procurement procedure.

At the same time the new legislation on the public procurement has entered the concept of “offer abnormally low” and in the procurement rules there has been provided a reference formulae based on which there shall be done the calculation of the abnormally low offers.

In this law there are determined precisely the cases of disqualification of the entities in a procurement procedure, not leaving room for interpretations in the submitted documentation or possibility for abuse in their disqualification.

In the context of the efficiency and independence in considering the procedures of the law no 9643, dated 20.11.2006 there has been provided for the Institution of the Advocate of Procurement, who represents the rights and legitimate interests of the candidates, bidders, suppliers from the illegal and inappropriate actions or commissions of the Contracting Authority in the field of public procurement, through the monitoring and investigating the administrative procedures of public procurement and granting of respective recommendations upon their conclusion.

Institutional and administrative capacities

In the context of boosting the institutional and administrative capacities, the Public Procurement Agency has taken all the measures for the strengthening of administrative capacities within its personnel and for all the employees of public procurement in all the Contracting Authorities. Based on the law no 9643, dated 20.11.2007, PPA is the responsible authority for the organisation of the training in the field of public procurement.

To the effect of strengthening the administrative capacities of the PPA personnel and of the employees of procurement of all the Contracting Authorities, PPA in cooperation with the Millennium Challenge Threshold Agreement Program for Albania, administered by USAID, has organised and conducted informing seminars with regard to the new legislation of the public procurement. Initially these hearings were held with the entire personnel of PPA and beyond (until now); there have been held informing seminars with regard to the new public procurement legislation with procurement employees in central institutions and procurement employees in all the institutions of the local government. These seminars shall continue to be held with Contracting Authorities which have not yet been trained in the field of public procurement. The main aim of these seminars is the presentation of:

- New legislation of public procurement, harmonised with EU Directive;
- Its main principles;
- Procedures of public procurement;
- Review procedures and role of PPA and Procurement Advocate;
- Bulletin of Public Notifications and time periods;
- Improved internet website of Public Procurement Agency, characteristics and transparency ensured by it.

At the same time during the period February March 2007, PPA, with the assistance of Millennium Challenge Threshold Agreement Program for Albania, administered by USAID, organised four round tables with representatives of the private sector: representatives from the Association of Constructors, Albanian Chamber of Trade and Industry, American Chamber of Trade and Industry and Association of Women in Business.

Implementation including the measures for improvement of transparency and independent treatment of complaints

In the framework of implementing measures to ensure a good implementation of the law and boosting the institutional capacities of the Contracting Authorities in the field of public procurement, PPA, in cooperation with the Millennium Challenge Threshold Agreement Program for Albania, administered by USAID, have identified the needs for training at country level and based on the final report with regard to these needs, there shall be drafted the National Strategy of Training. Parallel to this, PPA and the project administered by USAID have set up the Training Unit which functions with the coordination and supervision of PPA and shall serve for the training of the employees of the public procurement at country level.

At the same time, in the framework of measures for the improvement of transparency, PPA has improvement considerably its internet website. There has been reflected more information there. Every interested person can find any time the Bulletin of Public Notifications in electronic form, which is published in real time, every Monday, the legislation of public procurement, Standard Tender Document, every notification or public clarification done by PPA, all the materials connected to the conducted trainings etc. This website shall continue to be improved and enriched with further information, as well as the publication of any information, even in English.

The setting up and functioning of the Advocate of Procurement shall widen the possibilities to address the legal violations to serve as a positive pressure on the PPA. At the same time, in the present legislation there has been foreseen the possibility of filing complaints by electronic means, being a facility for the parties.

3.2. Financial Sector

The second semester of 2007 has marked an increase of the banking activity, this being expressed in the extension of the network, boosting of total of assets (specifically the credit portfolio) and extension of the basis of deposits. The qualitative indicators which are connected to the revenues, portfolio of credits and situation of liquidity are at satisfactory levels. The general situation of the banking system is steady and capable to support with capital the intensive extension of the activity.

During this period, the credit portfolio has increased on average 46 percent in annual terms, while the long term credit has gained terrain towards the short term one. There continue to prevail the credits for small and medium businesses even for corporations, while the consumers credits are increasing fast.

During the second semester, there has continued the increase of the portfolio of credits with problems, but the increase has been lower compared to that of the first semester of the year. However, this increase can be considered acceptable in the circumstances of the fast increase of crediting, which has been reflected in the improvement of the ratio “credit with problems to the total of credits”. The outcome of the qualitative analysis of the crediting according to sectors is that the consumers credits have been of a better quality, although the corporations credits have shown improvements during the recent semesters.

The second semester of 2007 marked a lower level of Net Margin from Interests compared to one year ago, but a bit higher than the level of one semester earlier. The system has demonstrated capability to invest in assets which bring interests and in the increase of the funds for which interest is paid.

The level of the shareholder capital of the system has increased by 4 percent, while the regulatory capital has remained on the same levels. The fast increase of the crediting activity has reached the level of weighted assets with a risk of 6 percent. Consequently, the Sufficiency Report of Capital (RMK) has fallen from 17.5% (March 2007) to 16.4%, continuing the falling tendency.

After entering into force of the new regulation “On administration of the credit risk”, the banks reacted in different ways, slowing down the increase of credits or raising the level of regulatory capital. During the second semester of 2007, the number of banks which were impacted by this regulation (banks which exceeded the limits determined in the regulation and consequently have reported weighted assets of 150 percent) reached 7, compared to 9 banks in the first semester.

The ratio of credits to the total of assets has fluctuated between 19 and 79 percent for the individual banks. According to the historic data and the present tendencies, it is believed that in the future there shall be extended the crediting activity having an impact on the moderated

increased of the ratio of credits to the total of assets. Presently, this ratio for the Albanian banking system is at lower levels compared to the neighbouring countries.

Considering the ratio “credit with problems to the total of credits” there can be said that this indicator has had continuous fluctuations, but later August 2007, it has demonstrated a considerable improvement. Actually, it is about more of a quantitative improvement rather than qualitative improvement of the portfolio of credits, since the increase of the total of credits has been faster than that of credits with problems, offering a lower ratio of the latter to the total credits.

Since the portfolio of credits is relatively new, there will be needed time to judge on its quality as a consequence of the high increase of crediting. Generally, the banks have improved the structure of credits, getting adjusted to the increasing volume of credits.

The high rates of increasing of credits for the economy during the two last years and onwards have made possible that Bank of Albania take some coercive measures through the presentation of the new regulations in the supervisory aspect. The main aim remains the avoidance of further acceleration of credit expansion for the economy, a phenomenon which can lead to problems of quality, on one hand, and in increasing inflation related pressures on the other. In response to the fast increase of the credit in currency, Bank of Albania will require from the banking system a responsible treatment of the risk of exchange rate. To this effect, Bank of Albania shall present very soon a regulatory package. The proposed measures shall aim at avoiding this risk in two main directions: first, in strengthening the awareness of the bank and their clients about the risk of exchange rate, and second, in the increase of the provisions for the credits granted in foreign currency.

3.3. Labour Market

The state policies of employment shall continue to include, as measures for the incitement of employment (active policies) as well as insurance of support through income (passive policies).

a) Active policies in labour market

The active policies of labour market include:

- Employment services;
- Programs of creating new jobs;
- Programs of professional training.

The continuation of the work for the improvement of the system of services of employment and professional training which is aimed at being reached through: (i) establishment of a modern and unique of employment services in the entire country, (ii) establishment and development of the partnership relations with the other actors in the labour market, (iii) development of the information technology (IT) in the employment services as a key factor for the improvement of the quality of services, (iv) improvement of the contacts with the enterprises, (v) development of human resources, (vi) improvement of cooperation with the private services of employment, (vii)

establishment of a unique and qualitative system of AFP, capable to contribute in the continuous development of the professional capabilities and active civilian action of the young and grown up people, (viii) offering of professional qualifications, in compliance with the requirements of economic development of the country, in the framework of the regional and European integration.

At the same time, there shall continue to be developed programs from the employment offices, such as the program of incitement of employment, that of the unemployment allowance, and programs in the labour market (focusing on the vulnerable groups), program of professional training etc.

The main objective of the employment policies is the support of jobseekers in finding an appropriate job. The employment policies an important means for the improvement of situation of the labour market, however, they have a limited impact in decreasing the level of unemployment. This is as a result of some factors in the labour market which are connected to the fact that the policies in the labour market are expensive and require more people to implement them.

Despite the progress with regard to the transfer from the passive to the active policies, it is evident that the employment services have to be oriented towards the knowing and improving the labour market situation. Presently, round 47% of the total number of employees of the Employment Offices work and offer services for 145 000 unemployed jobseekers registered with the Employment Offices, while in the countries of EU this percentage is at the extent of 62-65%.

In this framework, the objective of SHKP for 2007 – 2010 is to continue improving the ratio of the services employees from 47% to 55%, compared to the auxiliary employees. The improvement of the level of Public Service of Employment in Albania shall continue to focus on:

- Improvement of relations with business, chambers of commerce and development of labour fairs;
- Extension of training of the personnel, focussing on the improvement of the capacities of the personnel to offer individual advise, competence and evaluation of needs, and follow up of the process for the persons registered in the SHKP. This is true for the vulnerable groups, social exclusion and exclusion from the labour market.
- Boosting the role of the social partners in all the labour levels of the National Service of Employment (drafting, implementation and monitoring of the policies and programs) etc.

Even for the period 2007 – 2010, there shall be held annual meetings at regional levels with the participation of the Employment Office, Representatives of Business, Chamber of Commerce, Local Authorities for introducing the situation of labour market and professional training at regional level. In the course of 2007, there was done the organisation of labour fairs in 6 pilot regions (Tirane, Durres, Vlore, Fier, Korce and Shkoder). During 2008, this experience shall be extended to 6 other regions. From 2009 and onwards, the conduct of employment fairs shall be done permanently.

In May 2007, in cooperation with the American Chamber of Trade, in the framework of the Labour Fair 2007, there was realised the organisation and participation in the conference “Reality

and tendencies of Labour Market in Albania”. In this conference, there was displayed in front of the business the draft of strategy of employment and professional training, legal framework where the Ministry of Labour, Social Affairs and Equal Chances is operating and the programs for the incitement of employment which are implemented by our employment offices. Here was also done the presentation of the new program of inciting the employment, that of professional practices for the unemployed jobseekers who have graduated from the higher education in the country and abroad.

The strategic objective for 2007 – 2010 in the field of services of employment shall continue to be the modernisation of services transforming SHKP continuously from one institution offering administrative services, to an institution offering services to two main clients: unemployed job seekers and business.

For reaching this objective, there has to continue the work: (i) for strengthening and developing institutionally the system of employment service; (ii) to set up a modern and unique system of employment services in all the country through the improvement and development of the working method and managerial capacities of the personnel, (iii) increase employment and decrease unemployment through the application of active policies of employment, (iv) set up and develop strong relations of partnership with other actors operating in the labour market specifically with social partners.

Under the objectives which have been launched continue to be implemented for the realisation of these main objectives which can be grouped as follows:

Setting up a modern and unique system of employment in all the country through the improvement and development of the working method.

- a) Unification of services of employment and improvement of the level of work of specialists in their work with clients, concentrating the work specifically in the local offices of employment, in order for them to raise the level of services offered by ZRPS.
- b) Review of capacities, geographic distribution and extension of employment services. The increase at employment offices of the number of specialists providing services to the clients and regulation of ratios between the employees of services and other services in favour of the former. (Objective is to go over from 47% to 55% with regard to specialists working directly with clients.)

The strategic objective with regard to this issue is the management with more efficiency the existing human resources, considering the possibility of opening the Services Agency in those Municipalities where the level of population and unemployment makes this indispensable.

- Further improvement of monitoring and evaluation of the work of employment services. This shall be realised in a more transparent way following the installation of the Vacancies Bank and the Register of Job Seekers.
- Qualitative of the short term study of the Labour market (done every year) where there is included a detailed picture of the situation of the labour market in all the components it includes, a forecast of its development, which shall contain the risk of unemployment,

tendencies of employment, needs for training. Based on them, there shall be foreseen the necessary measures for the further intervention with the labour market.

- Starting from 2004, implementing the CARDS 2002 project, there has been carried out the medium term study of the capabilities required in the labour market. Based on the methodology used by CARDS program this study shall be carried out by employment offices every two years.

Establishment and development of partnership relationship with other stakeholders in the labour market

- a) For intensifying the cooperation with business, being partners in their activity, the employers and the employment offices, have their respective rights and duties, which have to develop to the effect of improvement and eventual interventions with the labour market.
- b) Cooperation with Universities, INSTAT, with Social Partners, research institutions and different donors shall receive more attention for studies and applications in the field of labour market, boosting of capacities, development of human resources and professional training.

Development of Information Technology (IT) in the services of employment as a key factor for improving the service quality

To date the general infrastructure of IT in SHKP and in the Employment Office is entirely insufficient and does not have any central administration with regard to the IT equipment, which means that there are different conditions in different conditions. There is no separate budget for IT, and one of the short term objectives of this strategy is the establishment of an information system containing information on the labour market. The introduction of a Information Technology system for supporting the information on the labour market requires among others even the improvement of the quality of data collected from the investments with the employers, since very often these data or information are not always sufficient and reliable, etc.

In this context, for the development of an IT system, SHKP is implementing the project with the title: “Efficient Employment Services in Albania”. The expected result of the development of the IT system in SHKP shall be: Setting up of the Vacancies Bank, Bank of Unemployed Job Seekers, until later 2007 in the Central Offices of the National Employment Offices, in the Regional Pilot Office of Tirana and Korca. The main output of the implementation of this information system shall be:

- Better services for the unemployed job seekers, offering to them a wide range of offers employment at Republic scale (information system with internet access);
- Better services for employers, ensuring appropriate candidates for the other vacancies, i.e., compliance of demand and offer.

Strategic objective for SHKP for 2007 – 2010 is the continuation of the extension of the IT system in all the Employment Offices in the country. This shall continue to be implemented with the eventual support of the CARDS funds (2005 – 2006) of EU and with the funds made available by the Albanian Government.

Private employment services

The private employment services are provided by the Private Employment Agencies since 1999. These agencies provide: (i) services which make the evaluation of requests and applications for employment in the country and abroad; (ii) services connected to the search of a job; (iii) services on the employment of workers to be available to a third party, natural or legal person which sets out the tasks and controls their implementation.

Currently, there operate 11 private employment agencies. The multi-annual activity of the private agencies has focused on the employment of a limited number of persons, mainly abroad. The main aims for the improvement of the private employment agencies in the labour market continue to be:

- Boosting their cooperation with the public employment services;
- Control and selection at the moment of licensing and re-licensing, to the effect that those being provided with this license be able to perform their respective services.

In cooperation with the project ILO/emigrant, the private employment services have, during 2007, the forum of private employment forum. These agencies have adopted an ethical code for the coordination of activity and sharing of experience. In the forum, there are participating also the representatives of the public services for orientation, cooperation and sharing of experience with private employment agencies.

In October 2007, in cooperation with the project ILO/emigrant and with the participation of the private agencies of employment, there was organised a workshop with the topic “On preliminary information of migrant workers.”

Programs for inciting employment

The programs for inciting the employment shall be present in Albania even in 2008 and onwards. The main aim of these programs shall be: (i) creation of the new jobs and reduction of unemployment; (ii) professional training of the unemployed job seekers, specifically in those zones where there are missing the training capacities; (iii) assistance to the enterprise to extend its activity and make a better selection of the work force; (iv) direct inciting of employment of a part of the trained people; (v) minimising the illegal labour; (vi) involvement in these programs of the unemployed job seekers, beneficiaries of the support schemas with income to the effect of reducing the costs of these programs; (vii) inciting of the employment of young people and vulnerable groups, long term unemployed people, Roma community etc.

The implementation of the program of inciting the employment for 2006 – 2007, have yielded positive effects in the Albanian labour market and concretely:

- Increase of the number of the employed people reflecting directly the reduction of unemployed (in this program there have been employed in total 2221 unemployed job seekers being taken from the lists of job seekers).
- Involvement in these programs of the unemployed job seekers supported by income (unemployment allowance and economic assistance), reducing their costs. In the total of

the unemployed job seekers, 21% are beneficiaries of the economic support and unemployment allowance, reducing the respective fund by 10 million lek.

- Involvement of the unemployed job seekers of separate groups, such as females above 35 years old, unemployed above 50 years old, Roma , orphans, long term unemployed people, young people 16-25 years old, persons with social problems, persons coming out of the restructuring of the economy etc. In the total of the unemployed job seekers, 67% belong to this category.
- Under the circumstances of existence of limited training capacities or of their absence in certain zones of the country, the application of the program of training in service or that of the institutional training (according to CMD no 73 and 74) are the only possibilities to meet them. There are under the process of training through these programs (in clothing, shoe making, hotel, tourism, installation in houses, cosmetics with an average 9 month employment/unemployed job seekers) round 1139 unemployed job seekers. The application of training programs in service and the institutional training creates chances for a long term training and employment, since it ensures to the employers a profession and integrates them into the labour market.
- The application of programs by the Employment Offices strengthens the decision making role of Three Party Local Councils, strengthens the influence of Employment Offices, as well as in the development of employment relations with the employers. In these programs there have been involved 116 employers (40% are women employers, 20% of the enterprises are joint ventures).
- The implementation of the programs has had an impact on the boosting of inter-institutional cooperation and partnership among the interested entities (Employment Office – Labour Inspectorate, Taxation – Social Insurance), having a positive impact on the implementation of the programs.
- The evident increase of the female job seekers with the implementation of the projects according to the CMD no 632 “On female unemployed job seekers”. Presently, there turns out that there are being implemented 35 projects, with 1053 employed females, or 47% of all the employed, which are mainly females above 35 years, divorced, Roma , with social problems. In the general total of the employment in all the projects 92% are females.

New programs in labour market

The professional practices is a new program in the labour market, which started to be implemented this year as a pilot project in the Employment Office Tirana (Professional practices are being implemented in 34 state and private entities by 163 practitioners, who have graduated from the branches economics, law, social work, engineering, veterinary, with a funds of 7 million lek. The average duration of internship is 4.5 months), and evaluating the effectiveness, in the upcoming years it is going to be done by the other employment offices in all the country. This program is focused on the category of the young people who have just graduated from the university, in the country and abroad, and they are unemployed as a consequence of absence of experience at work. For this reason these young people shall be included in programs of professional internships in enterprises or institutions, being private or public. The young people benefit the appropriate experience to have further a long term employment.

The state/public institutions admit the newly graduated unemployed job seekers free of charge. While the latter receive a financial support to the level of unemployment allowance and the 6 month period shall be considered as insurance period for the effects of the aged and family retirement and invalidity pension.

Employment incitement program for the unemployed job seekers being in difficulty (shall be applied in 2008). The aim of this program is to employ the unemployed job seekers being in difficulty, who are long term unemployed, who benefit economic assistance, unemployment allowance, who enter for the first time into the labour market of the age 18-25 years old; above 45 years, not having a higher qualification than the secondary education or its equivalent, disabled persons, since in these groups is the highest percentage of unemployment.

Gender equality and equal chances

To the effect of improving the employment level, the ministry has undertaken a series of measures for the employment of females: thus, there has continued the implementation of the program for inciting the employment of females, where priority is provided to specific groups of females, such as victims of trafficking, disabled females, Roma females above 35 years old, mother girls, divorced females with social problems. The program of inciting the employment “For unemployed female job seekers” for the first time was applied in 2004. This program has continued even in the upcoming years and has as a priority the involvement there of females from the separate groups, registered with the employment offices as unemployed job seekers (explained with the programs of inciting the employment).

In reliance on the law no 8872, dated 29.03.2002 “On professional education and training in the Republic of Albania”, CMD no 616, dated 4.12.2002 “On determining the specific categories benefiting for the law no 8872, dated 29.03.2002 “On professional education and training in the Republic of Albania” Instruction of Minister no 2222, dated 31.10.2002 “On advising and orienting in the professional training” (point 6) instructs to pay special attention in professional training to the separate groups. Out of the separate groups there have been provided training with DREPP course of professions with a reduced fee, 1100 unemployed job seekers and free of charge 100 unemployed job seekers for 2007.

The national Employment Service continues its activity for increasing the possibilities and equal treatment between males and females in the field of the services of employment, professional training, as well as in the support through income in case of unemployment. The main aims of the gender integration shall continue to be:

- Active participation of women, representatives of NGOs and all targeted groups for the formulation of the policies, guaranteeing the responsibilities and the needs for the most discriminated social groups;
- Use of statistics and data according to the sex, making use of the detailed forms to contain the data based on the gender affiliation;
- Data have to be filled in and collected by all the implementing units of regions of the country, to the effect of enriching the data at national level;
- Gender budgeting has to be done based on the equal gender benefits. This has to be done after the reporting so far to draft policies, not only contributory but also equal beneficiary.

Employment of young people

Even in the upcoming years the employment of young people shall continue to be at the centre of attention of policies of Ministry of Labour, Social Affairs and Equal Chances. As we highlighted above, in addition to the program of professional internships, which has started to be implemented in 2007 with regard to the incitement of employment of young people, there is aimed at:

- Continuous implementation of programs for inciting employment where young people shall be a priority;
- Efficient implementation of the advising program on employment and profession, including here the mobile of advise at school, university and office of employment;
- For separate groups of young people, there shall be taken measures with regard to their professional training, with reduced fees or free of charge in the public centres of the professional training.

Employment and professional training of the Roma community

This part of population shall be under the focus of the Ministry to be dealt with since a considerable part of the unemployed and non-active persons of Roma community are still unemployed for a multi-annual period now, and among them the majority are not able to find a job.

The main reason for the high levels of long term unemployment of the Roma community remain those connected to: (i) absence of education, (ii) regional disadvantages, (iii) discrimination, (iv) low efficiency of active policies of employment of Roma community, because the majority of them have not been registered as unemployed.

The professional training free of charge or with reduced tariffs and their involvement in the programs of inciting the employment shall remain among the priorities of the ministry for increasing chances of employment of this community. At the same time, there shall continue the work which has started on: (i) identification of professional which can be learned by the Roma people, and (ii) opening of courses for professional training for the professional identified in the public and private centres of professional training.

The employment offices continue their work for the establishment of links with the unemployed of the Roma community, who are not registered with them and concretely this year, in the statistics coming from the employment offices, there have been identified the Roma unemployed people who are round 3300 registered at country scale.

Making the program of public works operational by the municipalities and communes to create new jobs for the unemployed Roma job seekers, not requiring qualifications. The implementation of the social existing programs for inciting the employment for Roma community.

At the same time, the use of facilitating policies for the companies employing members of the Roma community aims at: (i) possibility of financing companies where the employers and employees are

from Roma community; (ii) creation of fiscal facilities for those companies opening jobs for Roma, and (iii) support with materials, facilities, financial means and human resources for those businesses which have as destination the products of Roma tradition. With regard to the treatment of this community in professional training (this target group is free of charge in professional courses) in DREFPP, there has increased their participation adopting courses suitable for them.

b) Passive programs

Unemployment allowance

The program of unemployment payment is a part of the labour market policies and ensures the support with income for the unemployed during the time they are as such. The main objectives are: (i) compensation of unemployed with income, (ii) providing active support to the beneficiaries of the unemployment beneficiaries, in a way as to return to work.

The right to benefit belongs to all the persons who have been ensured in the social insurance and for them there has been contributed an unemployment insurance for not less than 12 months; they have been established by the Labour Offices that they are unemployed and accept to be qualified and re-qualified and they do not receive any other benefits from the Social Insurance law, with the exception of the partial pension of invalidity.

For 2006, the number of unemployed job seekers receiving the unemployment allowance was 11 200 from an unemployment fund of 925.6 million lek and the basic level of unemployment payment is 5240 lek per month, while the amount of unemployment allowance adding up on average the compensation for electrical power, fees for the dependant children, compensation for bread and food goes up to 7 500 lek per month. Starting from may 2006, the basic level of the unemployment payment as increased by the level of 20% and it had a financial effect until later 2006, by 90 million lek.

With reference to the analysis of the number of beneficiaries of unemployment payment for the current year 2007, we see that the number of beneficiaries of unemployment payments has been decreased compared to the same period of 2006, to 1890 beneficiaries less. The reduction of the number of beneficiaries has come about as a consequence of:

- Expiry of the processing period with unemployment payment;
- Their inclusion in the programs for inciting employment;
- Their employment through the mediation of the employment services.

In the course of the 8 month period of 2007, from the sector of the unemployment allowance there have been employed 730 persons, out of whom:

- 480 persons through the mediation of the employment service sector;
- 250 persons included in the programs of inciting the employment.

For 2007, there was not done the increase of the amount of unemployment allowance at the foreseen extent, as it is provided for in the ILO convention no 168 that the amount of unemployment allowance has to be 50% of the minimal salary at country level. In order to reach this, the unemployment allowance has to be increased gradually and parallel to the minimal

salary of the country. There has been foreseen by the Albanian Government that the minimal salary at country level be raised by 20% and the unemployment allowance be raised by 14.2% on 1 January 2008.

The outcome of the recent study of the labour market done by the SHKP, for the upcoming years, the tendency of unemployment shall not have any considerable increase, since only few are the economy branches which are going to be restructured or privatised.

Professional education and training

The transformations which brought about the birth of market economy have raised the need to the society for new qualification levels with regard to the technology and new services. In the professional and technical training schools presently study 28 178 students who make up 21% of the students following the secondary education. These students study in more than 45 branches, in more than 68 schools distributed all over Albania, mainly in the cities. In order to provide an opportunity for studying to the students in rural zones in the majority of these schools there are hostels, where there have been ensured good living and learning conditions for 28% of the students of professional education.

The increasing needs of the labour market for qualified people and for new professions in compliance with the new developments of economy have done indispensable the increase of number and quality of trainings. Concrete indicator is the care of the government, reconstruction and making functional the new public centres of professional training during this year, in the districts Gjirokaster, Fier and Elbasan.

The government supports the establishment of capacities for professional training, in quantity and quality, through the development of the public professional training system. There are operational 9 Regional Departments of Public Professional Training, (DREPP). DREPP no 1 and 4 in Tirana, DRFPP in Shkoder, DRFPP in Elbasan, DRFPP in Korce, DRFPP in Dures, DRFPP in Vlore, DRFPP in Fier and DRFPP in Gjirokaster, which offer courses of professional, mainly for categories of unemployed job seekers, as well as for the other persons of different ages and educational levels, who want to follow these courses and get a profession for different reasons, such as for e.g., they have abandoned schooling and it is indispensable for them to get a profession (have completed only the mandatory education), have left their job for restructuring reasons, they want to keep their job through the development of knowledge and capacities etc.

The foreign donors have provided and continue to provide a considerable contribution for supporting the system of professional training in our country. Presently, the professional training has been evaluated by the government as a priority and this has been materialised concretely in the aid that our country receives from EU in the context of CARDS program "Support for the reform in the field of AFP". In cooperation with the Ministry of Education and Science (MASH), there has been set up the national agency of AFP, which is being supported by a twinning project financed by CARDS 2004. The National Agency AFP is a very important institution in the field of AFP, having a considerable role for the reform launched in this field. There is close cooperation with MASH and twinning project supporting the agency for its strengthening and boosting the effectiveness of the National Council of Education and Professional Training with regard to the advising the policies and strategies in the field of AFP.

At the same time this cooperation with the Project “Support for the reform in the field of AFP – Second - phase II” financed by EU in the context of CARDS program continues even with the Ministry of Education and Science, and there is being drafted the Albanian Frame of Qualifications and the respective law for it.

In support of the project “AlbVET”, financed by the Swiss government, Ministry of Labour, Social Affairs and Equal Chances has set up the mobile centre for professional training for the east-northern zone, a zone with a high unemployment rate. Attempts are focused for this centre to start the activity aiming at offering the service of professional training with courses of demanded professions in the labour market, assisting the unemployed job seekers, to the effect of integrating them into the labour market. This centre shall start its activity early 2008 with the courses of plumbers, tailoring, electrical installations, repairing the domestic electrical appliances and hair dressing, which shall circulate every 6 months from one region to another, within this zone.

The ministry, using the funds from state budget, is continuing the good work in the direction of investments for extending the network of the public centres of professional training. Along with the centres of cities of Elbasan and Fier which are close to the completion, during 2007 has started the work for setting up the centres in Durres and Gjirokaster and in cooperation with the Project “Support to reform in the field of AFP – phase II” there shall be reconstructed the centre for professional training in the city of Korca.

Other important donors assisting the system of professional training for solving the problems in equipment, development of curricula, training of trainers, drafting of standards etc, is the Foundation PARSH, financed by the German government with the project “Learning during all life”.

The strengthening of the autonomy for DRFPP and specifically the support by investments and funds, there has been dealt with by our side as a measure for increasing cooperation with the Regional Employment Offices and their possibilities for opening new courses according to the demand of the labour market.

During 2006, there have been trained 6200 persons, out of which 1700 are unemployed job seekers in professional courses.

For the six month period of 2007, out of the activity of the 9 Regional Departments of the Public Professional Training, there turn out 4800 certified students, out of whom 1300 are unemployed job seekers, mainly in courses of professions such as tailoring, vehicle service, duralumin, plumber, domestic electrical equipment, furniture, solar panels, welder, electrician, construction etc.

In the centre of the professional training, there are organised short term courses (from 6-7 weeks up to 4 months in public centres, and 1 week up to 2 years in private centres). The professional training courses in the Regional Departments of Public Professional Training are frequented more by persons up to 24 years old (62.87%) and 56.17% of them have graduated from the secondary and professional education. Round 41.42% of the participants are unemployed, out of whom

17.89% of them are registered as unemployed (this figure differs from the kind of course and district).

The problems which are being experienced by the system of professional education and training (AFP) makes necessary the intensification of the reform in this sector. The final aim is harmonisation of policies of AFP among them and with the policies in the other fields, interested for the development of human, economic, social resources of labour market etc. This requires a rational use of the financial and human resources, always taking into account the reality and conditions of our country.

Training in the Private Professional Training Centres

In the field of professional training there exercise their activity even some private centres spread in the entire country. During 2006, by 156 private centres licensed by Minister of Labour, Social Affairs and Equal Chances, there have been trained 8600 persons. Even though not in similar proportions to the public information, in the private training there are evident the courses on foreign languages, computer, tailoring, hairdressing. Good progress has been made by the courses of tailoring and hairdressing and, compared with the same period of the previous year, there is an increase of the number of people for plumber, foreign language, electrician, cook, and sweets preparation.

For 2007, there have been trained by these centres, which so far are 125 licensed entities, round 5800 persons, 3700 of whom are unemployed. The specialities which are taught in these courses are computer, tailoring, hairdressing, plumber, electrician, secretary, kitchen etc.

Measures for the improvement of the situation in the informal market

Since its very beginnings in 1992, the Ministry of Labour has had one of its missions the drafting and making applicable the policies in the field of safety and health at work. Protection of the physical and mental integrity of employees is the priority which is expressed in the “policy of labour presently”. The implementing institution of this policy is the state inspectorate of labour, the mission of which in the future years is as follows:

The labour state inspectorate, as indispensable institution in the social policies of a state, has under focus the security and health at work, through the incitement of applicability of the labour legislation, physical, mental and social protection or employees.

This policy is in full compliance with the policy of the European Community for health and safety at work, aiming at improving continuously wellbeing at work, a new concept and priority for the service of labour inspection for the upcoming years in Albania. The promotion of a qualitative environment at work requires all the actors to assume full responsibilities, which means that each party should be subject to control and evaluation of the control. Historically, the labour inspection systems come as a result of the economic, political, social and cultural environment of a country, aiming at improving the labour environment.

Labour environment – regardless of the direct functions connected to the health and safety at work of employers, the labour inspection service ensures, through the control and advise, cooperation with different institutional mechanisms, prevention of risks which arise at the work

station, but also of the risks injuring the health of population and outer surrounding environment. This is connected to the motto “Only a healthy man shall be considered well integrated in the society”.

The phenomenon of the informal labour has its own negative sides, such as: disorientation of the labour market, encouragement of illegal labour, decrease of revenues in the state budget, reduction of revenues for social and health insurance, establishment of the layer of unprotected, etc. For minimising the illegal labour, there have been introduced new efficient methods making use of the experience of the other countries. The cooperation between the taxation and Labour State Inspectorate, control of money at banks and facilitation of the fees of medical services for the insured employees, etc, are the main methods for controlling the informality in the labour market and for increasing the number of insured persons.

Problems identified in the labour market and measures which are being undertaken

The Albanian labour market is characterised by some problems for which the Government is taking measures which shall have a direct impact on improving the situation of this market, which will have as a consequence the improvement of employment level. Among them, we can mention:

- The improvement of the climate of business in the framework of reduction of taxes specifically for the small business and the reduction of the amount of contributions for the social and health insurance (labour cost).
- Creation of new jobs in the private non-agricultural sector with more productiveness and higher salary consists an important element for the reduction of poverty and improvement of the living standard. Opening new jobs is a challenge at a time when the offer of labour force shall increase due to the demographic increase and the modernisation which shall transform the economic activity to activities requiring less labour force outside the agricultural sector.
- The Albanian labour market suffers still a high level of informal market. More over there is a little movement between the formal and informal sector. The insurance of more favourable stimuli for the formalisation of the jobs, more flexible contracting would assist specifically the more vulnerable employees. Drafting the action plan, approved by the government with the involvement of many actors in the labour market, is a step towards the implementation of the governmental policy towards the improvement of situation of the labour market.
- Persons with low educational level encounter considerable problems in the labour market. There is a concentration of persons with minimal or no education in the informal sector. The level of education is closely connected to the level of income. The extension of access to education and professional training is very important. In the future, with the urbanization of the economy and its departure from the agricultural sector, the development of human capital shall attain an even greater importance.
- Although migration has been considered as a very good source of income for the Albanian families and valuable instrument in the risk management, it incites the phenomenon of brain circulation. The brain circulation offers potential benefits for the future since the emigrants have benefited professional training and experience in the migration countries. Very positive in the direction of inciting the emigrants who return

and want to open new businesses in Albania, is the new initiative of the government for the exemption of these businesses from taxes for a certain duration.

- Women continue to have low employment rates and high levels of unemployment. Salaries for women are 35% lower than those of males, taking into account the age, education and other personal characteristics. While the level of unemployment in the Roma community is round 70% and the part of these who have been employed generally get low salaries and very often are employed in risky work stations in the informal sector. This has negative consequences and impacts the social wellbeing of these groups.
- There is missing the labour force survey which shall be carried out by INSTAT, a study which is foreseen to start to be applied in 2007. By means of this study INSTAT shall be able to provide official data on the unemployment rates, employment, professional training of work force, characteristics of unemployment etc. The indicators taken from this study can be such that they can be monitored by the European Commission and by the member countries. Such data would bring about the drafting of appropriate policies and the increase of efficiency of these policies.

In the framework of the program of government, there is aimed at creating the possibilities for the employment of each Albanian. The acceleration of the economic growth rates aims simultaneously even for this growth to create new jobs sufficient for reducing the unemployment to the level of European countries, to cover with employment possibilities the demographic increase of population and moreover even to start to have an impact on the return of a part of emigrants. The efficient use of the programs and instruments proven as successful to make possible the adjustments of the defects of labour market, such as, instruments of information, mediation, professional training, fiscal incentives etc. For the realisation of the above policies there have been foreseen in the medium term draft budget the funds necessary as follows (Table 12).

Table 12: Funds foreseen for the employment policies (million lek)

	2007	2008	2009	2010
State budget				
Labour market (total)	1.724	1.727	1.750	1.800
Incitement of employment	120	200	200	200
Professional training	174	185	196	208
Donors				
CARDS	81		375	
Swedish SIDA	150			
AlbVET	125	125	125	
IPA				
Others				

Table 13: Indicators of developments in labour market

Indicator	2007	2008	2009	2010
Unemployment	13.5%	13.1%	12.7%	12.4%
Employment	50.0%	50.8%	52.0%	53.0%
Number of mediation in employment by the employment services	10,000	10,500	11,000	11,500
Number of unemployed job seekers qualified in professional courses	4,500	5,000	5,500	6,000
Number of employees according to qualification	2,000	2,200	2,600	3,000
Number of unemployed job seekers employed/trained by the programs of employment incitement	200	2,000-2,500	2,000-2,500	2,000-2,500

Reform in the social insurance system

The Social Insurance Institute has been tasked with the administration of the social insurance system. Under these circumstances, in the following we are dealing with some issues connected to his activity, problematic and economic and financial indicators of the period 2008 – 2010.

The pensions are an important element and indispensable one of the social protection. Out of them, there presently benefit round 15% of the population, this being an indicator of a clear tendency towards the increase specifically after 2012, where there ends also the reform of the gradual increase of the age of retirement. There are presently included round 538 thousand beneficiaries of some categories.

The present system of pensions has been determined by law no 7703, dated 11.05.1993 “On social insurance in Republic of Albania”. This system is based on two pillars: in the obligatory one and supplementary one, which for the moment does not appear advanced yet, and covers only the high officials of the state and generally the militaries. There are the first steps of the activity of theirs, three funds of pensions, with contributions set out on voluntary basis.

The pillar of the obligatory insurance covers the employees, employers and the self-employed in the urban and rural, upon the condition that they have contributed for a certain period of time in the schema. The existing law of social insurance, sanctions these main principles:

- The social benefits or public pensions are covered by the Social Insurance Fund (FSSH) which is a financial structure, not depending from the state budget.
- Management of FSSH has been entrusted on the Social Insurance Institute (ISSH) which is an independent public institution, depending from and under the authority of Ministry of Finances.
- The social insurance fund is administered in five main branches, which are deceases, pregnancy-birth, pensions, disabled from accidents and professional deceases and unemployment.

- FSSH is financed from four main sources of income which are contributions, transfers from state budget, income from the investments of reserve fund and funds temporarily free and other revenues as follows:
 - Contributions are paid by the insured employees and their employers, by the self-employed and for some specific categories, even from the state budget. The contributions of the state are provided for the insurance of persons performing the mandatory military service, for those who are paid unemployment allowance as a result of abolition of the jobs, and for the categories receiving pre-timely pensions or temporary payments.
 - State transfers for FSSH are provided from the state budget for the indexing of pensions where these exceed the index of goods prices, for the financing of activities determined by CM (e.g., compensation of price increases), as well as for the subsidies determined by the parliament. In the form of state transfers come also the budget financing of compensation through income for persons receiving minimal pensions, as a measure for the reduction of poverty.
 - Revenues from the investments of the fund of ISSH. By law, there shall be established the separate reserve fund of social insurance with ISSH guaranteeing the payment of pensions for three months. This fund, as well as all the other monetary funds, temporarily free, shall be invested according to the financial plan of ISSH. At least 80% of this fund is invested in state contracts and immovable properties. The revenues from these investments consist a source of revenues for FSSH.
 - Revenues from other sources include revenues from penalties, arrears, commissions for the services that ISSH provides to the third parties and donations.
 - The law “On social insurance in Republic of Albania” allows the ISSH that for the collected contributions finance only two kinds of expenses:
 - Benefits which are provided according to the 5 different insurance schemas;
 - Administrative expenses which cover the operations costs and of the developments of ISSH, the maximum of which do not exceed 5% of the ISSH budget.

Present situation and problems found out

The present financial and administrative structure of the system of social insurance was reformed and became functional in 1993. Presently, in ISSH, there has been collected a multi-annual experience from the implementation of the reformed system of the social insurance. The consideration and evaluation of this experience in the context of political, economic and social developments, being problematic and difficult, which the country has experienced since 1993, allows to confirm that the new schema of social insurance, regardless of the shortcomings and difficulties it contains, has generally resolved the problems of the period, while it has found out a series of problems for solution

The development of the most important synthetic indicators of the social insurance schema appears as follows:

- The average annual number of contributions in the first years of the implementation of schema has been reduced; there started a raising tendency until 2006 marking again a

significant fall in 1997, which coincides the known crisis for that year. While subsequently, there is seen the tendency of gradual increase of the number of the contributors. Thus in 2005 this number reached 624 thousand as opposed 384 thousand, which it was in 1997, marking an increase of 79.3% and in 2006 due to the measures taken for the decrease of evasion as well as of the reform of August for the reduction by 9 points of the norm of contributions, this number reached 650 thousand persons and with clear increasing tendency. In the present situation, despite the marked improvements, there is evaluated that the participation of the population in the schema of social insurance, continues to be relatively low; more evident is this phenomenon in the rural zones. An impact on this negative phenomenon had specifically:

- Absence of information and control of the entities economically active, which has lowered the effectiveness of attempts to the effect of minimising the evasion in the schema of social insurance.
- Another factor of negative impact is the absence of the identification of movement of population, specifically of space movement. It is known that transition was accompanied with unforeseen dis-equilibrium in the demographic developments. They are connected to, on one side, with the violent chaotic development, happening in the natural movement and specifically in the space related one, with the emigration and the mechanic internal movements, in big and unforeseen measurements. The influx of emigration, although in smaller measurements, is judged to be present even in the future, as long as there will continue to exist the deep differences within the quality of life and level of development of Albania compared to the neighbouring countries. The implications of the mechanic movement on the demography and on the indicators of labour market are increased because emigration is not entirely permanent, but a part of it is temporary.
- The revenues from contributions in schema appear with considerable increase from year to year, excluding year 1997. In 2001, the revenues were 4.2 times more compared to 1994. It is to be marked that the increase rates of revenues are increasing in the recent years not only in the urban zone but also in the rural one, in the latter with higher increase rates. This is for the reason of the implementation of a series of favouring measures which were taken for stimulating the involvement in the insurance schema of the self-employed in rural zones. The biggest revenues in the und of social insurance belong to the last year, where although the amount of contribution was reduced in round 24%, the revenues compared to the previous year were increased by 6%.
- The number of beneficiaries, after a drastic increase in the first years of transition, starts to be normalised in the upcoming years with a gradual increase. Exception from this rule is 1995, where as a result of the early pensions, the increase of the beneficiaries compared to the predecessors is round 15 thousand people. In 2006, compared to 1994 this number for all the categories of pensions was 12.9% higher. The pressures from certain groups of employees for early pensions although has been decreasing, again they are present. They have an impact on the strained strengthening of the number of beneficiaries and in weakening the financial sustainability of the schema of social insurance. These elements are seen often where it is about the lowering of the retirement age or in the pressures of the certain groups for early retirements, such as the melting industry, military industry etc.
- The expenses of the social insurance schema have marked the same trend, as the number of pension, thus, a gradual and normal increase over years. In total the biggest increase of

the expenses is found out in 2006, where the transfers to the family budgets reached more than 56 billion lek, or 14.3% more than one year ago. While in 2005, the average revenues for one beneficiary were round 890 USD, in 2006 they reached round 1070 USD. Due to the compensation with the revenues of the minimal pensions, at the end of the year the minimal revenues from the aged pensions reached 10 000 lek. In the composition of the expenses, the main share is made up by the expenses for obligatory pensions, which in 2001 represented 82.5% of the social insurance fund. This indicator, in 1993 was 95.5%. In the composition of expenses after 1993, an important role have been made up by the special programs financed directly by the state. In the meantime, the part of administrative expenses has always been under 3% of the total budget of ISSH and in 2006 it was found out at the extent of 1.9% of total expenses.

Developments in 2006-2007

During 2006 – 2007, in accordance with the programmed objectives, the activity of ISSH has been concentrated on the following main directions:

- There were drafted the projects and implemented the decisions of Council of Ministers on the increase of pensions, starting from 01.07.2006 with 5% for the city, with 20% and 10% for the countryside in 2007.
- There was prepared and implemented the law and respective decision of Council of Ministers for the recalculation of pensions in the period 1994 – 2005 and this task was completed in November and the payments of the financial benefits for the beneficiaries was done in December 2006.
- In the framework of the strategy of increasing the benefits, there was drafted the legislation and implemented the decisions of Council of Ministers for the compensation with 500 lek and 760 lek and up to 680 lek per month, for the persons benefiting minimal pensions.
- For the strengthening of the financial sustainability of the social insurance system, the attempts are focused on the qualitative detailing of the budget and in following up operationally its implementations, in cooperation and sharing of information with the tax authorities for minimising the evasion of contributions, increase of number of persons to the effect of increasing the revenues and extending the participation of the population in the schemas of insurance, in realisation of the program of the revenues from the contributions from farmers and voluntary insurance, in implementing the measures for the transfer of the administration of debts from social insurance to the tax authority, in drafting contemporary methods in the field of auditing and monitoring of the use of funds, in realising and exceeding the revenues from the investment of funds, budgeting of payments and periodic supply, sufficient and limited to funds of the branches and affiliates of Albanian Post, for the periodic realisation of payments of pensions.
- To the effect of boosting the institutional capacities, the ISSH work has consisted in: Participation in drafting the draft law for the reduction of the amount of contributions for social insurance as a measure which would facilitate the cost of work for business and would make possible the extension of employment and unveiling of informality, in drafting a joint agreement with the Ministry of Interior for the exchange of information between the ISSH and Civil Registry Offices, in improving the legal framework of the social insurance system through the draft law of re-calculation of pensions, in monitoring,

updating and standardising the data basis for the pensions of the own as a main condition for carrying out qualitative activity in the fight against informality, further on to the work for collection of the archives and filing, archiving and informing documentation for every future beneficiary, but also in function of the prohibition and avoiding the possibility for manipulating with the data, in deepening and acceleration of implementation of the project for the distribution of the social insurance number, for the contributors and for the beneficiaries, as an important measure for the transparency of credits and benefits.

Among the main aims in the activity of the structures of social insurance during this year have been the intensification of efforts for boosting the quality of services in granting the benefits, in preserving the periodicity of implementation of the program of income from the contributions, strengthening and raising the level of cooperation with the other institutions mainly with the General Department of Taxation, General Department of Treasury, and Budget at the Ministry of Finances. As a result of this work, for the entire programming activity of ISSH in 2006, the planned income for the fund of social insurance are evidently exceeded, while the programmed expenses remain at the plan level.

Work is continuing intensively for the implementation of the project “Computerisation and filing of pensions” and that of “Digital archives of ISSH”, as well as the work for the elimination and avoiding the informality in the field of social insurance.

Some specific indicators

Since these data are highlighted at the end of each year, we are referring to the end of 2006, while we explain that with the implemented policies in 2007, all these indicators have improved.

- Replacement coefficient, which expresses the ratio between the size of the average pension with the average salary, turns out with worsening tendency in the town and in the village. In the town, in 1994 it was 60.2%, while in 2006 it turned out 43.4%. While in the village there is another tendency. Until 2000 there is a falling tendency up to 15.78% out of 27.34% which it was in 1994. Later, there is an increase of this ratio expecting in 2006 to be 26.9%. In this phenomenon, there has had an impact the high increase rates of the average pension in the village to the minimal salary of contributions.
- Covering coefficient, which expresses the ratio of the number of contributors to the work force, turns out with a slowdown, from 33.76% to 32.41% in the period 1994-1999. Later on, this indicator was increased reaching in 2006 the value of 58.4%. This indicator shows the decrease of the phenomenon of evasion of contributions in the schema of social insurance, which has been a concerning problem.
- Depending coefficient, which expresses the ratio of beneficiaries to the contributors in the social insurance schema, has worsened from year to year until 2002, starting with an improvement for 2003, due to the slow down of the increase rates of the number of the pensioners, but also of the increase of the number of contributors. Despite this, a negative impact is being exercised still simultaneously three factors:
 - Low number of employees; the percentage of the unemployed to the labour force remains very high;
 - High rates of illegal employment, which brings about the reduction of number of contributors;
 - Inclusion in the schema of some specific categories of pensions, such as the early ones, which still continue to the held in the obligatory schema.

General and specific objectives in the Medium Term Budget

At the foundation of the medium term programming of ISSH, there are set two general important objectives:

First, guaranteeing of a more comprehensive coverage of the population with the elements of the obligatory social insurance, kept at acceptable levels. This objective shall be achieved specifically through:

- Implementation of a social insurance system which responds to the phase of the economic and social development of the country;
- Improvement of management of the social insurance schema, specifically in collecting the contribution revenues and their equal distribution in the form of benefits, where and when the right arises.

Second, intensification of attempts for the further improvement of the financial sustainability of the social insurance schema, aiming at the gradual and fast increase of the contributions compared to the increase of the benefits and minimising the budget subsidies.

For meeting the above general objectives, ISSH has determined these specific objectives:

- Implementation of the projects started for the setting up of a computerised information system for the social insurance. Through this computerised system, there is aimed at:
 - Specifying the total number of resident persons;
 - Identification of persons economically active and the amount of their revenues;
 - Identification of private entities conducting economic activity and of contributors in these entities;
 - Identification of the total number of the beneficiaries, kinds and extent of beneficiaries which are granted from the social insurance system;
 - Determination, fast and precisely, of rights of persons and the obligations of this system to the insured persons at a certain moment and place;
 - Making possible the fast and precise exchange of information with the other interested local and national systems, as well as with the interested international institutions.
- Raising of the level of benefits of pensioners by 10% for the town and 15% for the village and avoidance of pressures for early pensions through:
 - Improvement of the method of indexing the pensions and inciting the setting up of the second and third pillar of the general system;
 - Continuation of the initiated process for narrowing the differences in pensions of the village with the town and harmonisation of this process with the amount of contribution and participation in the insurance schema;
 - Adjusting the compensation schemas being provided to the pensioners to soften the effects of liberalisation of prices or to meet the indispensable minimum of pensioners with the general system of benefiting from pensions.
- Wider involvement of the self-employed in the rural zones in the obligatory social insurance schema;
- Developing and boosting the institutional capacities of ISSH to guarantee a more efficient management and more efficient one of the social insurance schema and a correct and legal administration of the expenses.

- Improvement of the relationship contributor/beneficiary and salary/minimal pension with salary/maximal pension.

With regard to the revenues, the forecasts and problems are as follows:

- Responsibilities for the collection of data from social insurance contributions shall be divided between the DPT and ISSH.
- Programming and detailing the revenues 2008 – 2010 has relied on the ceiling of the revenues sent by the Ministry of Finances during the drafting of PBA (2008-2010);
- ISSH shall collect the revenues from contributions from:
 - Self-employed in agriculture;
 - Voluntary insurance.

For 2008, 2009, 2010, the number of contributors, revenues and expenses for the obligatory social insurance, specific compensating programs of the government and for the supplementary insurance, in the passive option without the cost of the policies for the raising of pensions, are displayed in Table 14.

Table 14: Number of contributors and expenses for social insurance

No.	Denomination	2008	2009	2010
<i>A</i>	<i>Number of contributors</i>	<i>276409</i>	<i>281287</i>	<i>293519</i>
1.	Self-employed in agriculture	265279	269489	281013
2.	Voluntary	11130	11798	12506
<i>B</i>	<i>Data (million lek)</i>	<i>3026</i>	<i>3806</i>	<i>5096</i>
1.	Self-employed in agriculture	2520	3228	4395
2.	Voluntary	506	578	701
<i>C</i>	<i>Expenses (million lek)</i>	<i>64913</i>	<i>66059</i>	<i>71306</i>

As it was described above, the programming of the number of contributors for the legal and natural entities shall be done by DPT, which has the responsibility for the collection of contributions.

With regard to the number of contributors in the village and their increase and to the revenues, the development relies on the improvement of the work for the collection of the contributions.

This shall be achieved through:

- Qualitative improvement of the work for informing the farmers with regard to the insurance schema;
- Cooperation with the local government and organisations carrying out activities in the village;
- Coordination of facilitating measures of the state for farmers, with meeting by them of the obligations for the payments connected to contributions;
- Improvement of the work with inspectors.

Objectives in the field of management and administration and Matrix of indicators of the medium term budget

Programming Fields

- Contemporary development of the schema of social insurance and combination of the financial sustainability in the framework of the multi-pillar system;
- Inciting and development of the private funds as the third pillar of the total system of the social insurance to the effect of division of responsibilities for a more efficient protection for third ages.
- Efficient methods in identifying the active population and economic relations between the employers and employees.
- Efficient methods in the collection of contributions and monitoring of debts;
- Drafting and implementation of specific programs for the collection of contributions from village;
- Implementation of advanced and computerised systems of the information administration;
- Application of the individual number and card of the social insurance;
- Administration with high efficiency and safety of the reserve fund.

Indicators subject to Monitoring

- Increase of social insurance fund;
- Increase of the indicator of income from the reserve fund investment;
- Improvement of the dependency ratio, replacement ratio and scale of coverage in the social insurance schema;
- Strengthening of new administrative structures, and specifically the extension and strengthening of institutional capacities;
- Making operational the central register and of a computerised system of archives and in general of the insurance period;
- Provision to the population with the social insurance numbers and cards;
- Gradual reduction of the state subsidies for the obligatory social insurance schema

Role of Government and Other Institutions

- Determining the form of the health and social insurance card, way of use of the insurance number and obliging the entities to make use of it;
- Obliging the entities to carry out all the financial transactions in the field of salaries, through banks;
- Obliging the entities to rigorously implement the provisions of the Labour Code with regard to the registration of employees, collective contracts, setting the personal salary of their employees, etc;
- Obliging the enforcement offices for the rigorous enforcement of the executive titles issued by the administration of the social insurance or judicial decisions;
- Orienting the tax police to ask for collection of the acts issued from the social insurance contributions and debts;
- Determining periodically the contribution facilities for the farmers against a program for the gradual increase of contributions they pay up to their equalisation to the contributions of other self employed persons;

- Approving regularly the index of prices, indexing of the pensions as well as narrowing the differences of certain pensions according to the different legislations.

Investments and Other Development Expenses

- Investments for making operational the full information system;
- Expenses for covering the cost of compensation or rights stemming from different statuses;
- Expenses to cover the cost of rights stemming from the supplementary insurance of militaries, employees carrying out constitutional functions and specific treatment of miners;
- Expenses for covering the annual additional cost of the increase of pensions where the indexing is done on the level of price index;
- Funds for covering the expenses where the income from the contributions are not sufficient;
- Funds for covering the level of the reserve fund of pensions where the revenues collected from fund investment are not sufficient.

Meeting the Needs for Funds for Specific Projects

- Ensuring the necessary donations for the implementation of the project Modernising the Social Insurance;
- Ensuring the necessary financial resources for the realisation of the network of social insurance.

3.4. Administrative Reform

Reform in public administration

The reform in the public administration includes:

- Functional – structural reform
- Deepening and extension of reform in the civil service:
 - Improvement of procedures of the legislation of civil service and extension of its field of activity;
 - Reform in the field of salaries (but this being extended, not only for civil service).

I. Functional – Structural Reform

Same as in 2006, the functional structural reform has continued even in 2007. Aiming at adjusting the structures and organigrammes of institutions of public administration continuously to the mission, functions, competences and activities which they have to carry out, concretely during 2007, the Albanian government has undertaken the following activities:

- Functional and structural review of the line ministries. This review has been done with the aim that the mission and objectives of each organisational unit within every ministry, be adjusted continuously with the intended strategies, to be achieved by the Albanian government. Thus during 2007, there have been implemented 15 changes of structures in the line ministries, which have reflected not only the change of employees of theirs, (in accordance with the respective decision of the Council of Ministers for the number of

budget employees for 2007) but also changes in the functions foreseen to be undertaken by them.

- The functional and structural review of the institutions under the authority of Council of Ministers/Premier, of line ministers. The aim has been standardisation of the way of organisation of structures and organigrammes of this category of institutions, trying and performing grouping of functions within each institution. From this perspective, during 2007, there have been approved the structures and organigrammes for 43 institutions, among which, 11 are new institutions, set up recently.
- Another important activity foreseen for 2007, is also the approval by the Council of Ministers of an instruction, which aims at making the responsible actors aware to consider the restructuring process not simply as an organisational issue, but as a need for setting up functional and steady structures, which respond to the missions and objectives of institution, aiming at eliminating the superfluous segments and in compliance with the management rules of the levels of the civil service.

This act shall be seen as a practical instruction, where there shall be provided:

- Basic principles which have to be taken into account by the managers of institutions which shall be restructured;
- Methodical instruments which have to be used for the accomplishment of a functional analysis of the institution;
- Standards which have to be used, for the improvement of the effectiveness and efficiency simultaneously.

The activity of the functional review is seen as a continuous concept, in an administration which is in continuous development and in this context, there is foreseen to continue with all the dependant institution during 2008 and onwards, until all the institutions, be organised in accordance with the generally accepted principles, for the institutions of the public administration. At the same time, for 2008, there are foreseen to be drafted a legal draft – act or by law act, which shall aim at determining the typology of institutions. This act shall serve as a basis for the setting up of institutions of public administration.

II.a. Deepening and extension of the reform in civil service

In reliance on the declared program of the Albanian government, the reform in the civil service implies not only the strict implementation of the procedures provided for in this legislation, but also the extension of the field of its activity, improvement of the procedures determined in the bylaw acts, boosting, strengthening and preservation of the capacities in the public administration in general, as well as making operational the National Register of Public Administration Civil Servants. It is exactly these directions where the work during 2007 has focused, which shall continue also during the upcoming years.

Concretely, the activities undertaken during 2007 and those foreseen for the upcoming years:

- Strengthening of the capacities in the public administration and absorption in this administration of the employees with post-university qualifications, scientific degrees and titles. For this, in July 2007 (in the framework of the approval of the draft decisions in the field of salaries), employees in the central administration institutions, was recognised the right of benefiting additional reward for their respective qualification, as long as this qualification is in line with the description of the job description.

- In the meantime, with regard to the treatment of the employees there has been approved for the period 2006-2007, the Strategic Plan of Public Administration Training Institute, where the priorities are:
 - Effective response to the needs for development in Civil Service;
 - Improvement of quality of service and products;
 - Improvement of structures, procedures and systems;
 - New perspective for financial management.

In the context of the above, the training for the employees of Public Administration, in accordance with their real needs aimed at:

- Improvement of managerial and functional capabilities, for high level, medium operating managers and for some specific positions in the public administration. For this group, an important part is made up by the training for the local government. In general, this training package, makes up round 82% of the trainings of the General Training Centre (QTP);
- Improvement of capabilities and knowledge, with regard to EU issues, for civil employees which belong to some specific positions, connected to the process of integration of EU. In total, this package makes up round 18% of the training of QTP;
- Trainings for the employees of Fiscal Administration, organised in three directions:
 - i. General trainings, where of priority are the trainings for the newly appointed employees in the tax and customs administration. This group is foreseen to make up round 28% of the scheduled trainings;
 - ii. Specific trainings, which are oriented towards the reception of specialised knowledge in the professional field and make up round 55% of the planned trainings;
 - iii. EU trainings in the fiscal field, aiming at providing knowledge on the impact of integration into EU, in the fiscal and customs field. This group is foreseen to make up round 17% of the total of trainings in 2007.

Specific objectives of the strategic plan of ITAP are:

- *Meeting the requirements for training of civil employees, set out in the Stabilisation and Association Agreement;*
 - *Responding to the needs for training within the Albanian civil service, specifically in the field of managerial skills;*
 - *Creation by ITAP of a method of agent for change;*
 - *Transformation of ITAP, in order to be an organisation oriented to the requirements, client and care for the client and promotion of the same attitude within the institutions and agencies of the civil service;*
 - *Reaching the status of excellence known by the clients and public, ensuring the preciseness of the aim and high quality of reaching the objectives;*
 - *Train the internal capabilities and capacities of ITAP and improvement of the capacity for the management of resources;*
 - *Setting up a system which will make possible the generation of respective influxes of income.*
- Drafting and proposal for approval to the Council of Ministers, of the Inter-Sector Strategy of Public Administration Reform, in the framework of the National Strategy for Development and Integration. For this, in August 2007, there has been approved the order

of Premier for setting up the inter-ministerial Working Group, which shall be responsible later even for monitoring and implementing the strategy. Drafting the strategy and approval by the Council of Ministers is foreseen to be concluded in June 2008.

- Improvement and strengthening of the procedure for job description. For this, there has been drafted the draft on the amendment to the Instruction no 1 of Council of Ministers, “On structure of listing the jobs in the civil service, respective methodology and generalising description of the role of the General Secretary in this service”. These changes, which have been prepared on the bases of the practical experience so far shall be connected to a good progress of the process and concretely:
 - A more evident role of DAP, not only as administrator, but also as assistant of the process, in support of the line ministries. This implies that, if irregularities are seen in the implementation of the procedure set in the instruction, DAP not only will take measures for rectifying this irregularity, but will also advise the respective institution about the appropriate way of accomplishment of the process, in order for the irregularity not to be repeated;
 - Improvement of some technical aspects which are connected to the generalising description of the job and typical denominations, according to the present structure of salaries, for these denominations;
 - A better division of the role of the group members for the evaluation of jobs, determining better the role of the Analyst of Jobs, not only as a secretary of the evaluation group (keeping the minutes, assistant of the evaluation group), but actually, what is more important, in the role of making precise and comprehensive information available for every position, as the position which is responsible for the drafting and implementation of the process of job description.
- Improvement and strengthening the procedure of evaluation of the individual annual results of civil servants. In order to assist the institutions for the strict implementation of the procedure of individual evaluation of the civil servants, there have been proposed some regulations in the present instruction of Council of Ministers. These changes reflect the regulation of some problems found out in the present practice, which are connected to a better progress of the process and concretely:
 - A more evident role of DAP, not only as administrator, but also as assistant of the process, in support of the line ministries.
 - A better layout of the hierarchy of positions according to the classical structure, dividing the roles better and the responsibilities of categories of directors, who shall be responsible for realising the process of annual evaluation;
 - Stronger focus on the drafting of the plan of personal development, in the event of the employees evaluated in the level 4, “generally sufficient”;
 - At the same time, since so far the measures for the reward, based on the levels of evaluation according to the present instruction, have not been possible to be applied from the financial side (for the level 1 – there were foreseen 3 monthly salaries, for level 2, there were foreseen 2 monthly salaries and for the level 3 there was foreseen 1 monthly salary), having an impact that the process of performance evaluation not to have any direct connection to the reward, which has a certain impact on the partiality of the process, there was raised the idea that in the project there had to be included a reflection of the levels foreseen in the respective Decision of Council of Ministers for the determination of the Special Fund. In this decision, there is determined that the civil

employees have to be rewarded with not more than 1 monthly salary, once a year (according to the calendar determined in the evaluation year), as well as the distribution has to be done in accordance with the procedure determined in the legislation of civil service.

- The review and evaluation of implementation of the legislation of civil service. This is another very important activity, foreseen by the Albanian government to be carried out in the period November 2007 – March 2008. Based on the conclusions of this activity, as well as relying on the strategy to be approved by the Council of Ministers (June 2008) for the Reform in the Public Administration, there shall be supported the planning of activities for the upcoming years. A possible option is the review of the legislation of civil service with its two main directions: extension of the field of effectiveness of legislation of civil service to some groups of institutions, as well as improvement of the procedures for the recruitment in the civil service and other means of the management of the human resources. However, the extension of the field of effectiveness of the law shall be in compliance with the implementation of the functional and structural review of the institutions in the ministerial system.
- The system of Management of Human Resources is one of the most important projects of Reform of Public Administration.
 - During the years 2005 and first half of 2006, attempts were focused on the setting up of the information system, which allowed the entry of the data of personnel of each institution, in an easy and efficient way. After the completion of the setting up of the program relying on the internet technology, there was done intensive work for testing different parts of the system and to see whether they coincided with the required functionality. The process of testing was followed with important changes, in the users interfaces and in the logical concepts of the system.
 - After passing successfully the first phase, there was passed over to the second phase of implementation, in that of the population of the system, with the basic data of employees. In this phase, there shall be included the institutions, which were responsible for entering the data. Initially, the process was piloted in the Premier's office and in the Ministry of Finances, and later there was extended to all the other ministries. This process was accompanied with the training of the employees, who would work with the system, a training done by the employees of the Public Administration Department.
 - Presently, the process of making fully functional the data base (which for technical reasons was suspended for almost one year) has resumed its work in July 2007 and there has been made possible the overcome of all the technical difficulties, such as re-configuration of the software and making it available to Gov-net.
 - Public Administration Department has made possible the entry of structures in the data base, as well as the respective salaries.
 - Simultaneously, upon the initiative of DAP and proposal of the Minister of Interior, there has been approved the Order no 139, dated 29.08.2007 of Premier, based on which there has started the entry of the personnel data electronically, from the Premier's Office, line ministries, into the Central Register of Personnel. This order has as expiry period for the entry of the data 16 November 2007.

- In the meantime, there is expected in the upcoming years that this experience be extended to the independent institutions and central institutions, regional or local, under the authority of Council of Ministers/Premier, or line ministries.

II.b. Reform in the salaries system

Closely connected to the reform in the civil service and public administration in general, during 2007 there was implemented the reform in the field of salaries. Concretely, this reform was carried out in this year, in the following directions:

- Considerable increase in a differentiated way of the level of salaries for the system of the pre-university system (average 22%);
- Considerable increase in a differentiated way of the level of salaries for the system of health (doctors and higher education employees, average 22%);
- Considerable increase in a differentiated way of the level of salaries for the nursing personnel in the system of health (average 26%);
- Increase of level of salaries for armed forces and different policies (average 10%);
- Increase of low salaries in a considerable and differentiated extent for the auxiliary employees (system of salaries in categories, average 14%);
- Increase of salaries level for the employees who are rewarded through the scheme of salaries in the civil service (average 7%);
- Approval of the increase for post-university qualifications, scientific degrees and titles, in accordance with the job description;
- Approval by Council of Ministers of the joint decision of salaries for independent institutions set up by separate laws.

For years 2008 – 2010, there is aimed at:

- Priority increase of the level of salaries for the employees of the pre-university education system;
- Priority increase of the level of salaries for the employees of health system;
- Restructuring of the salaries system for the teaching staff and scientific researchers, at universities and other schools, in accordance with the law and high education law;
- Restructuring of the salaries system for the scientific researching staff, at researching and scientific institutions;
- Restructuring of the salaries system for the auxiliary personnel (employees of the system with categories);
- Connection of the evaluation system and qualification of civil employees and other employees in the public administration to their salary, to the effect of making operational the schema of horizontal career of theirs;
- Indexing the salaries for the other part of the employees of the public administration.

Reform in the Judicial System

The government has considered as indispensable part of its activity the issues pertaining to the judiciary in general and judicial administration specifically. In the framework of the

implementation of the short term and long term policies, the government and Ministry of Justice of Albania aim at undertaking and implementing the important legal reforms aiming at the good functioning and improvement of the system of rendering justice, boosting quality of the process of adjudication, guaranteeing a due, equal and honest process.

In the context of these policies connected directly to the judicial system, for the period 2006 – 2008, there is aimed to reach:

- *Reorganisation of the courts of judicial districts and appeal courts, a reorganisation which is expected to be finalised by the decree of President of Republic.*

The decree 5350, dated 11.06.2007, “On establishment of the judicial circles, determination of territorial powers and the centre for carrying out their activity”, is an essential act, which has a direct impact on the effectiveness and efficiency in rendering justice.

This re-organisation is directly connected to the recommendations coming from a study of specialists of Ministry of Justice, where it is suggested that the powers of some small courts have to be transferred to some bigger courts, in order to make possible the extension of the judicial circle, including within the territorial power of the extended judicial circle court even the territorial competence of one or two small courts. Such a reorganisation would not affect the access of the public to the court, since the small courts will continue to exist as branches of the main court.

With regard to the above, the reorganisation of the courts of judicial circles would bring about an evident improvement in the management of the courts of judicial cases, as well as it would make possible the elimination of delegations of the judges from one court to another, gaining time and decreasing expenses. In this framework, there shall be reached a balancing of the work load in the courts among the judges and administrative staff.

Such a reorganisation will have also an impact on the improvement of professionalism of judges and quality of the adjudication as a result of their specialisation. A big court creates more possibilities for the specialisation of judges, which brings about a higher quality of trials, extension of the possibility for professional discussions among the judges and a more competitive situation, which could contribute to the extension of the quality and uniformity of the jurisprudence.

All these shall have an impact on the reliability of the judicial system, as well as on the boosting of efficiency of the judiciary in general, which is the main aim of this reorganisation. Such a thing would have a positive impact on the strengthening of the judiciary, fighting against such phenomena as corruption, and improving transparency of this power in rendering justice.

In order to combat corruption and improve transparency in the judiciary, upon the order of Minister of Justice, there has been completed the computerisation of the judicial cases management in all the courts of judicial circles. There has been completed the installation of the information system for civil cases, which shall extend also to the criminal cases.

- *Drafting of a strategy for the identification of the infrastructure needs of courts, as well as for the determination of the basic directions for the improvement of this infrastructure.*

Concerning the above, such an objective can be reached in close cooperation with the Office of Administration of Judicial Budget and the other authorities entrusted by law.

The drafting of such a strategy shall have a direct impact on reaching another long term objective, which will aim at the intervention, partially and fully, with the court houses of judicial circle and

appeal courts, to the effect of their renovation and providing for appropriate conditions for the work of the judges and administrative staff of courts.

Taking into account the novelties of the judicial reorganisation (at the courts of the judicial circles and appeal courts) the improvement of the infrastructure of judiciary is considered as a priority objective.

According to the Master Plan of the European Union, there have been made investments for the improvement of the existing infrastructure of the judicial circle courts, and there has been invested for constructing new buildings, such as, we can mention the starting of work for the construction of the building for the Serious Crimes Court in Tirana.

- *Improvement of the judicial administration status.*

Further to the deepening and improvement of the reforms in the judicial system, to the effect of improvement of the functioning and its efficiency in general, as well as to the boosting of efficiency of the judicial authorities in the fight against the serious phenomena of criminality and in order to respond to directly to the need for dealing successfully with these phenomena, a specific attention shall be focused on the improvement of the judicial administration status.

The judicial administration is a considerable part of the judicial system and plays an indispensable role in rendering justice.

Seen from this perspective, our attention has been focused on the improvement of not only structural, but also methodological of the judicial administration.

We take into account the idea of the review and further legal improvement of the status of the judicial administration, seen as a complex package which shall regulate not only the procedures of recruitment or employment of administration, but also of a more appropriate financial treatment and in line with the importance of this part of the judicial system.

In order to have a professional judicial administration with integrity and committed to work, it is indispensable to improve its status. Such a thing would have a positive impact in the strengthening of judiciary, fighting against such phenomena as corruption, and increasing transparency of this part in rendering justice.

Taking into account that these measures undertaken by the Albanian executive would be stimulating, we think that they would also influence the improvement of quality of the judicial administration, and it would provide for the basis for the recruitment of a more qualified staff and more positive in its ranks.

- *Training of judiciary.*

Another important objective which is worthwhile mentioning is the issue of the training of judges and judicial administration, an objective which is considered as a priority.

In this work, the Ministry of Justice shall cooperate with the School of Magistrates, a cooperation which has been very fruitful even in the past.

Parallel to the School of Magistrates, attempts shall be focused even on drafting a strategy for the identification of the needs which the judicial administration has for training and on the basis of the latter there have to be organised the respective trainings.

- *Carrying out the legal changes connected to the determination in a precise way the status of judges*

It is already known that it is necessary to have more precise definitions in some essential aspects which have a direct connection to the status of judge, such as that of the career of the judge, his protection, financial treatment etc.

Such an objective is aimed at being reached by carrying out the changes and respective improvements in the law “On organisation and functioning of judicial power in the Republic of Albania”.

In this framework, there have been well received the feedback, opinions and suggestions and different institutions in the field of judiciary, the recommendations of which shall be taken into account in the periodic changes and improvements which shall be done to the draft-law . The draft law has been sent for approval to the Parliament.

- *Launching of initiatives in cooperation with the High Council of Justice with regard to the improvement of legislation connected to the payment of the judicial service offered by the court, identifying clearly and fully the constituent elements and the final cost, guaranteeing the collection in their entirety the judicial expenses, as well as ensuring that that monetary amount be made available to improve the quality of the service for the future.*

This is an important objective (still under discussion) that the Ministry of Justice aims at achieving in cooperation with the High Council of Justice. In the upcoming years, there shall be forwarded a detailed schema of this project, which has under its focus the collection of the judicial expenses in their entirety, insuring that this be made available for improving the service quality in the future.

3.5. Additional field of reform

Approximation of legislation in the field of taxes

Approximation of the policies on taxes to the European legislation

The approximation of legislation on the direct and indirect taxes to the EU legislation, in accordance with the EU recommendations. In Annex 1 of the Plan of implementation of the Stabilisation and Association Agreement, point 3.11, lists the legal initiatives which have to be undertaken to approximate the Albanian tax legislation to the *Acquis*. Some of these legal changes include: harmonisation of the accises fees to those of EU (December 2010), extension of the integral system o disclosure and payment of taxation on the personal revenues (December 2008); application of the full integral system for the disclosure and payment of revenues (December 2010), as well as gradual reduction and elimination of the commercial tariff barriers with the EU countries.

Acceleration of the progress with regard to the reforms for meeting the EU requirements

The process shall be concentrated on:

- Improvement of taxation administration;
- Boosting the administrative capacities for the fight against the corruption and fiscal evasion;

- Adoption of Code of Conduct for Taxation of Business, its implementation with regard to every new fiscal measure;
- Completion of computerisation of taxation offices through the establishment of a centralised system for all the services which are connected to the taxation revenues, the implementation of electronic declarations and improvement in infrastructure;
- In crease of transparency and exchange of information with EU countries.

Legal changes and administrative reform in the banking system

The new law on banks in the Republic of Albania, approved in December in 2006, entered into effect on 1 June 2007. This law is based on the obligations stemming from the Stabilisation and Association Agreement (Directive 2000/12/EC) of European Parliament and European Council of 20 March 2000) and Bazen Principles, and determines the main principles for the establishment, licensing, organisation, management and liquidation of banks; financial and banking activity, as well as the supervision of this activity in Albania. The changes in the regulatory aspect stemming from the new law shall be approved and implemented within 2007.

On 18.07.2007, the Supervisory Council of Bank of Albania approved the regulation “On functioning of the Credits Register in republic of Albania”. This regulation establishes the necessary legal basis for the establishment and register of credits which is expected to become functional in December 2007.

Considering indispensable the need of market development, Bank of Albania has prepared and shall submit a legal and regulatory package to the effect of boosting the efficiency of the financial market according to the following points:

- Law on the repos. There has been drafted the draft-law, which makes possible without risk entering into repos between the second level banks. This law shall avoid the risk of credit in the loan-taking relations among the banks. It is going also to avoid the legal risk with which the banks are encountered through the use of repos.
- Drafting of the legal framework and making available the principle of title handover against payment. This regulatory framework is going to minimise the risk of making the payments, to serve the mediation of all the kinds of transactions including the securities, such as the collateral credit, repos and sale/purchase with full rights of the government securities. At the same time, work is being done for implementing in practice of the principle of principle handover against the payment.
- Decreasing the frequency of holding auctions of government securities. There has been agreed with the Ministry of Finances to more rarely distribute the auctions of the treasury bonds, as well as the increase of the value of emission in every auction.
- Extension and deepening of the financial market (extension of investors’ base). In cooperation with the Ministry of Finances and Financial Supervision Authority, there has been agreed to extend the investors’ base, who will have direct access to the auctions of the obligations of the Government. The new agreement for the emitting of obligations, signed by the Ministry of Finances and Bank of Albania, establishes the necessary regulatory framework to put an end to the monopoly that the banking system has possessed in the investment of the primary market of obligations, leaving room also the legal and natural persons, local or foreign.

- The primary rate. Being convinced that the efficiency of monetary policy is increased through the transparency, Bank of Albania aims at including in this norm the entirety of existing norms, which are being used by the second level banks.

Changes in the organisational structure of the Bank of Albania

Bank of Albania evaluates that the integration of the financial markets has increased the possibilities of business, but at the same time it has been accompanied with the increase of risks raising also risks of new natures. These developments brought about the need for the increase and strengthening the evaluating and analysing capacities with regard to these risks. Consequently, following the best worked practices and standards and to the effect of boosting the administrative capacities, Bank of Albania has assumed a direct role in the evaluation and preservation of the financial stability in the Albanian economy, setting up in 2007 the Department of Financial Stability.

Medium term main objectives of this department are:

- Boosting the internal capacities and infrastructure for the evaluation of the financial stability, setting up the Financial Stability Department and the Financial Stability Committee;
- Strengthening the procedures for the financial crisis management and introduction of instructions which will create flexible strategies and quick and effective decision-making in this field;
- Inciting a wide and active coordination through the institutions, proposing the setting up of inter-institutional forums which shall be important for the drafting of the procedures and the lists of actions.

The Department shall monitor carefully the developments in the other part of the financial sector, which is presently represented by the insurance companies and pension funds.

In the framework of the review of the organisational structure of Bank of Albania and restructuring of the Department of Payments and Accounting, in June 2007, there was set up the Department of Payments Systems as a separate organisational unit.

**ANNEX 1: TABLES CONTAINED IN THE ECONOMIC AND FISCAL PROGRAM
AND SUBSEQUENT UPDATING**

Table: Macroeconomic perspectives

Following indicators are in percentage (if not indicated differently)	ESA Code	2005	2006	2007	2008	2009	2010
		Level (mil. €)	Difference rate				
1. Real GDP and market prices	B1*g	5 656.8	5.0	6.0	6.0	6.0	6.0
2. GDP with market prices	B1*g	6 645.3	10.1	9.2	9.5	9.4	9.9
Real GDP components							
3. Private expenses for consumption	P3	3 474	5.19	4.32	1.36	5.21	2.43
4. Governmental expenses for consumption	P3	542.7	-1.27	7.58	3.91	6.91	10.07
5. Creation of the gross fixed capital	P51	1 536.1	14.80	15.46	17.48	2.94	11.98
6. Differences of inventories and net additions (% of GDP)	P52+P53	na	na	na	na	na	na
7. Exports of goods and services	P6	1 281.5	17.10	11.93	8.12	7.06	8.14
8. Import of goods and services	P7	2 665.7	10.34	11.83	4.01	4.96	5.03
Contribution of real growth of GDP							
9. Internal final demand		5 525.8	5.21	7.60	5.95	6.69	6.28
10. Difference of inventories and net additions (% of GDP)	P52+P53	na	na	na	na	na	na
11. Foreign balance sheet of goods and services	B11	-1 383.8	-0.21	-1.60	0.05	-0.69	-0.28

Table 1b: Developments of prices

Differences in percentage, annual averages	ESA Code	2006	2007	2008	2009	2010
1. Deflator of GDP		123	127	131	124	140
2. Deflator of private consumption		109.6	105.9	106.5	107.8	108.1
3. HICP		na	na	na	na	na
4. Difference in percentage of national İÇK		2.4	3.0	3.0	3.0	3.0
5. Deflator of public consumption (state)		111.4	118.0	125.9	125.2	129.0
6. Deflator of investments		132.0	127.7	141.8	131.3	132.4
7. Deflator of export prices (goods and services)		125.1	127.7	130.4	133.1	135.8
8. Deflator of import prices (goods and services)		131.6	125.6	129.2	127.9	128.2

Table 1c: Development in labour market

	ESA Code	2005	2006	2007	2008	2009	2010
		Level	Difference rate (in percentage)				
1. Employment, number of employed persons ⁹		932102	0.09	0.40	0.38	0.45	0.51
2. Employment or labour ¹⁰		na	na	na	na	na	na
3. Unemployment rate ¹¹		14.2	-4.2	-0.7	-3.0	-3.1	-2.4
4. Boosting of labour productivity, persons ¹²		8 475.6	6.8	5.6	5.6	5.5	5.5

⁹ Occupied population, ILO definition.

¹⁰ National accounts definition

¹¹ Registered unemployment.

5. Labour productivity or labour ¹³		na	na	na	na	na	na
6. Compensation of employees	D1	na	na	na	na	na	na

Table 1d: Sector balances

Percentages of GDP	ESA code	Year X-1	Year X	Year X +1	Year X +2	Year X +3
1. Net lending/borrowing vis-à-vis the rest of the world	B.9				optional	optional
of which:						
- Balance of goods and services		na	na	na	na	na
- Balance of primary incomes and transfers		na	na	na	na	na
- Capital account		na	na	na	na	na
2. Net lending/borrowing of the private sector	B.9/ EDP B.9	na	na	na	na	na
3. Net lending/borrowing of general government		na	na	na	na	na
4. Statistical discrepancy			optional	optional	optional	optional

¹² Real GDP per person employed (000 leks-ALL per employed person)

¹³ Real GDP per hour worked.

Table 2: General budget developments

In percentage of GDP	code ESA	2006	2007	2008	2009	2010
Net lending (B9) according to sub-sectors						
1. General governance	S13	na	na	na	na	na
2. Central power	S13 11	na	na	na	na	na
3. State government	S13 12	na	na	na	na	na
4. Local government	S13 13	na	na	na	na	na
5. Fund of social insurance	S13 14	na	na	na	na	na
General governance (S13)						
6. Total of revenues	ESA	25.50	26.91	26.37	26.71	27.36
7. Total of expenses	ESA	28.77	31.53	34.31	30.61	30.99
8. Budget balance	B9	-3.26	-4.63	-7.93	-3.90	-3.63
9. Interests	D41	2.78	2.87	3.10	3.09	2.98
10. Primary balance		-0.49	-1.76	-4,84	-0.81	-0.65
Revenues						
11. Taxes	D2+ D5	17.24	18.32	18.19	18.22	18.73
12. Social contributions	D61	4.37	4.36	4.75	5.13	5.27
13. Others		3.89	4.23	3.43	3.37	3.36
14. Total of revenues	ESA	25.50	26.91	26.37	26.71	27.36
Expenses						
15. Total consumption	P32	8.84	8.97	8.91	8.83	9.10
16. Direct social benefits	P31	1.53	1.44	1.44	1.51	1.52

17. Indirect social transfers	D62	2.30	2,88	2,32	1,85	1,64
18. Interests	D41	2.78	2.87	3.10	3.09	2.98
19. Subsidies	D3	0.43	0.27	0.21 %	0.24	0.22
20. Creation of gross immovable capital	P51	5.68	7.14	9.81	6.15	6.35
21. Others		7.21	7.97	8.53	8.96	9.17
22. Total of expenses	ESA	28.77	31.53	34.31	30.61	30.99

Table 3: Budget expenses according to functions

In percentage of GDP	Code COFOG	2007 (Supplementary)	2008 (Project)
1. General public expenses	1	2,0%	2,1%
2. Defence	2	1,2%	1,4%
3. Security and public order	3	1,7%	1,6%
4. Economic issues	4	5,0%	6,8%
5. Protection of environment	5	0,0%	0,0%
6. Housing and community commodities	6	1,1%	1,1%
7. Health	7	2,7%	2,8%
8. Recreation, culture and religious affairs	8	0,2%	0,2%
9. Education	9	3,2%	3,5%
10. Social protection	10	7,8%	7,8%
11. Others non-classified*		6,4%	6,8%
11. Total of expenses (art. 7 = 26 in Table 2)	TSh.	31,5%	34,3%

**includes interest payment, expenses of local governance, reserve fund and contingency*

Table 4: General government debt developments

Percentages of GDP	ESA code	Year 2006	Year 2007	Year 2008	Year 2009	Year 2010
1. Gross debt ¹⁴		54.97	53.61	56.16	54.20	52.38
2. Change in gross debt ratio		-1.97	-1.36	+2.55	-1.96	-1.82

¹⁴ As defined in Regulation 3605/93 (not an ESA concept).

Table 5: Deviation from preceding program

	2006	2007	2008	2009	2010
1. Growth of GDP (in percentage)					
Previous Update	5.0	6.0	6.0	6.0	6.0
Last Update	5.0	6.0	6.0	6.0	6.0
Differences	0	0	0	0	0
2. General government net lending (% of GDP)					
Previous update	na	na	na	na	na
Latest update	na	na	na	na	na
Difference	na	na	na	na	na
3. General government gross debt (% of GDP)					
Previous update	54.89	54.24	53.57	52.59	na
Latest update	54.97	53.61	56.16	54.20	52.38
Difference	0.08	-0.63	+2.59	+1.61	na

Table 6: Basic assumption on external economic environment on which PEF 2007 framework is based

INDICATOR (Annual rate of change)	ASSUMPTIONS FOR					COMMENTS
	Year X-1	Year X	Year X+1	Year X+2	Year X+3	
	<i>change*</i>	<i>change*</i>	<i>Change*</i>	<i>change*</i>		
Interest rates (in % p.a., annual averages)						
- Short-term interest rate ¹⁵ (annual average)						
- Long-term term interest rate ¹⁶ (annual average)						
Exchange rates (annual average “-“: depreciation)						
Exchange rate vis-à-vis €						
USD / €						
Nominal effective exchange rate						
Real effective exchange rate **						
PBB (ne terma reale)		5.4	5.2	4.8	5.1	
- World, excluding EU						
- EU 25						
World trade (in real terms)		9.2	6.6	6.7	7.2	
Country export markets						
Advanced economies (change in % - in annual terms)		8.2	5.4	5.3	5.5	

¹⁵ If necessary, purely technical assumption

¹⁶ If necessary, purely technical assumption

Developing countries and others (change in % - in annual terms)	11.0	9.2	9.0	9.8	9.8
World imports					
Advanced economies (change in % - in annual terms)	7.4	4.3	5.0	5.6	5.6
Developing countries and others (change in % - in annual terms)	14.9	12.5	11.3	11.0	11.0
International prices					
World trade prices (in €)					
Processed articles (manufactures)	2.9	0.3	1.0		
Oil	19.5	-0.8	7.6		
Primary products without fuel composition	27.4	4.4	-8.3		
Food	9.0	1.1	-2.2		
Liquids and drinks	5.4	-4.3	-5.1		
Raw material in agricultural sector	9.2	-3.8	-3.5		
Metals	55.3	9.7	-13.5		
Fuel prices (Brent – USD per barrel)					

*: change vis-à-vis assumptions made for last EFP
 **: please indicate type of calculation (number of currencies, type of price index for deflation)

ANNEX 2

MATRIX OF POLICY COMMITMENTS

Description of policy	Year X	Year X +1	Year X +2	Year X +3
<i>1. Policy measure</i>				
A. Implementation profile*				
B. Net direct budgetary impact (if any)				
B.1 Direct impact on budgetary revenue				
B.2 Direct impact on budgetary expenditure				
<i>2. Policy measure</i>				
A. Implementation profile*				
B. (...)				
(...)				
<i>Total net budgetary impact</i>				
Total impact on budgetary revenue				
Total impact on budgetary expenditure				

* indicate start and, if needed, end with an “X” mark

ANNEX 3

ASSUMPTIONS ON THE EXTERNAL ECONOMIC ENVIRONMENT BASED ON SPRING 2007 FORECASTS .

VARIABLES (annual average)	2006	2007	2008
Interest rates (in % p.a.)			
Euro zone: in short term periods (money market 3 -monthly).	2.2	2.9	3.4
Euro zone: in long term periods (10-year government bonds, Germany)	3.3	3.9	4.3
USA: short term (money market 3 -monthly).	3.6	5.0	4.2
USA: long term (10 year government bonds)	4.3	4.9	4.5
Exchange rates			
("“": under price)			
USD / € (level)	1.24	1.22	1.22
Effective norm of exchange rate of euro zone (% change in %)	-1.1	0.0	0.5
Effective norm of exchange rate of EU (% change in %)	-1.0	-0.6	0.4
Exchange rate of Euro: (Level)			
Czech koruna	29.8	28.5	28.3
Danish krone	7.45	7.46	7.46
Estonian kroon	15.7	15.7	15.7
Cyprus pound	0.58	0.58	0.59
Latvian lats	0.70	0.70	0.70
Lithuanian litas	3.45	3.45	3.45
Hungarian forint	248	263	267
Maltese lira	0.43	0.43	0.43
Polish zloty	4.02	3.91	3.93
Slovenian tolar	240	240	240
Slovak koruna	38.6	38.2	38.5
Swedish krona	9.28	9.35	9.34
UK pound sterling	0.68	0.69	0.70
GDP (in real terms, difference in %)			
World, excluding EU	5.4	5.2	4.9

(in terms of GDP)			
USA	3.5	3.2	2.7
Japan	2.7	2.8	2.4
EU-27	1.6	2.3	2.2
World trade			
(difference in %, goods)			
Export markets in EU, extra-EU (volumes)	9.0	9.8	8.1
Volume of world import, excl. EU	8.1	9.6	8.2
Prices of world import (in USD)	6.0	4.1	2.0
Prices of goods			
Fuel prices (Brent, USD/barrel)	54.1	68.9	71.0
Prices of goods non-fuel (in USD, difference in %)	8.3	16.8	0.7