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How 'Berlin Process' will affect Albania's economic position?

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Introduction

The High Level Conference on the Western Balkans, held in August 2014 under the leadership of the German Chancellor, confirmed the unwavering political commitment on the European perspective for the Western Balkan countries (WB6).

The ‘Berlin Process’ is a new political initiative that aims to enhance regional cooperation by laying the foundations for sustainable economic growth of the Western Balkans. It will last till 2018 and it has a proper agenda - known as the “Berlin Agenda”. It uses existing financing programmes such as Western Balkans Investments Fund (WBIF), institutions and mechanisms such National Investment Committee (NIC), Sector Working Groups, Single Project Pipeline, etc. to identify, select and financially support regional initiatives and infrastructure projects that enhance connectivity. It is harmonised with respective EU policies through existing EU initiatives such as TEN-T, SEETO or PECL.

The impact of such a high-powered initiative in the Albanian economy will be felt in the short term through the infrastructure projects; in the medium and long term through improved economic governance, competitiveness, macro-economic conditions, and better relations with the neighbouring countries.

This analytical paper aims to outline the Berlin connectivity agenda and its relevance and impact on the economic growth of Albania. The methodology used by the authors will be based on the identification, and subsequent analysis and assessment of the political commitments and their respective legal base and consequences. We will sift through the official declarations and joint statements, public speeches, political statements, and press releases of the main EU and WB6 institutional actors and on their impact on the ground. The second component would focus on a formative evaluation process of the on-going connectivity projects in Albania.

The paper will be based on a qualitative analysis of the available information, completed with five semi-structured interviews with national and international stakeholders involved in the implementation of ‘Berlin Process’ related agenda in Albania such as Government, EU, IFIs and other involved actors.

Initially, the paper will start with the ‘Berlin Process’ institutions, approach and priorities as well as on the connectivity agenda with reference to the contribution of concrete projects to growth and prosperity in the country. Then, it will summarily assess Albania’s economic relations both at the regional and European level and identify the critical areas in need of reforms, the priority sectors and the obstacles to growth. Finally, conclusions will be drawn in order to take out the most from the ‘Berlin Process’. Special attention will be paid to the argument of a joint regional platform for economic governance and of the regional value chain.

1. The ‘Berlin Process’

1.1 Introducing the ‘Berlin Process’

On the 100th anniversary of the beginning of the First World War, on 28 August 2014, the German Chancellor Angela Merkel hosted in Berlin a High Level Conference on the Western Balkans. The Conference was attended by the Prime Ministers and Ministers of Foreign and Economic Affairs of WB6, along with representatives of EU Member States (Germany, Austria, France, Italy, Slovenia and Croatia), European Commission and International Financial Institutions (IFIs). This conference provided a joint forum of communication for Western Balkan leaders vis-à-vis each other as well as vis-à-vis six EU Member States and European Commission. This intergovernmental initiative was clearly aimed at the economic sphere by enhancing regional cooperation and laying down the foundations for sustainable economic growth of the WB6.

The Berlin Conference was followed by six follow-up meetings along with the WB6 Prime Ministers’ meeting in Brussels in April 2015. These meetings served as a joint platform where to discuss, select and agree upon regional projects of common interest. The selected projects were presented for funding at the Vienna Summit of 27 August 2015, which was already meant to serve as “an opportunity to evaluate the initial results” of the ‘Berlin Process’.¹ In this regard, the Final Vienna Declaration acknowledged the positive momentum that this process has created for regional cooperation in the Western Balkans, and set new milestones for the next Summit of Paris in summer 2016.²

Although, the ‘Berlin Process’ might seem rather orientated towards regional cooperation – which is quite important for the sustainable development of the Western Balkans – it is not a substitute of the European integration process. It has to be considered as a complementary and EU integration reinforcing instrument which affirms the resilient political support to the European accession perspective of the WB6 countries, despite the declaration of the European Commission President, Jean-Claude Juncker, that “no further enlargement will take place over the next five years”³.

Overall, at this stage the ‘Berlin Process’ has generated several political declarations and commitments. It is the turn of the WB6 governments to demonstrate their capacity to deliver on their political engagements. Although this initiative is intended to last till 2018, specific political commitments go beyond 2020. The infrastructure projects last even longer and the joint economic governance has not started as yet.

1.2 The importance of economic dimension

The thematic areas of the ‘Berlin Agenda’ can be represented in a three-pillar structure format: diplomatic, economic and soft pillar. Additionally, there are two mutually reinforcing transversal issues concerning the firm European perspective of all WB6 along with the strengthening of the rule of law and

¹ Final Declaration by the Chair of the Conference on the Western Balkans, Berlin, 28 August 2014, point 2.

² Final Declaration by the Chair of the Vienna Western Balkans Summit, Vienna, 27 August 2015.

³ Jean-Claude Juncker, “*A new start for Europe: My agenda for jobs, growth, fairness and democratic change*”, Political guidelines for the next European Commission, Opening Statement in the European Parliament Plenary Session, Strasbourg, 15 July 2014, p. 12, available at: http://ec.europa.eu/priorities/docs/pg_en.pdf

good governance in their path towards EU membership. The actuality issues of ‘foreign fighters’ and ‘migration flows’ were introduced as a specific ‘section’ in the Vienna Final Declaration.

Firstly, the *diplomatic pillar* deals with the resolution of outstanding bilateral and internal disputes of the WB6 countries, in the interest of good neighbourly relations and improved regional stability. In this regard, during the Vienna Summit the Ministers of the Foreign Affairs of the WB6 countries signed a joint declaration where they commit to a resolution of all bilateral questions and exclusion to block the progress of neighbours on their respective EU path.⁴

Secondly, the *economic pillar* prioritizes joint economic governance - which constitutes the heart of the new approach of the European Commission – and connectivity⁵. Currently, none of the WB6 countries is yet considered to be a functioning market economy.⁶ The prolonged economic crisis illustrated by a high unemployment rate – particularly among the young generation – and other structural obstacles to growth, has highlighted the necessity of the WB6 countries to find alternative ways of dealing with slow growth and global competition. Regional cooperation is yet an untapped source of growth.

The mechanisms promoted by the ‘Berlin Process’ emphasize the need of the WB6 countries for open markets and increased foreign direct investments (FDI), reduction of current account deficits, strengthening of legal certainty, as well as enabling a positive investment climate. Moreover, at the Vienna Summit the WB6 leaders agreed on bringing to an end the on-going negotiations in CEFTA on the Trade Facilitation Agreement before mid-2016 and further foster the development of regional value chains. They underline the importance of including the social partners in the economic reform processes.

In this spirit and under the technical support of the European Commission, the WB6 countries agreed to prepare every year credible National Economic Reform Programmes (NERPs),⁷ including both a *macroeconomic and fiscal programme* along with a *structural reforms and competitiveness programme*.⁸ In January 2015, the WB6 countries submitted to the European Commission the first NERPs, which included clear timelines and detailed budgetary implications.

Thirdly, the *‘soft sector’ pillar* comprises the thematic areas falling under the social affairs, people to people relations as well as cooperation with the civil society. For the first time, the Berlin Conference included the civil society in the list of strategic partners of regional cooperation. It also reserved a place for the enhancement of academic and vocational training to tackle youth unemployment. The Vienna Summit provided for the civil society and for the whole ‘soft sector’ pillar the opportunity to expand in terms of role and opportunities. It is to be expected that the Paris Summit will continue on this track.

Regarding the people-to-people relations, the WB6 countries progressed further with the plans for establishing the Regional Youth Cooperation Office of the Western Balkans and for the expansion of the

⁴ Vienna Western Balkans Summit 2015, Addendum, Annex 3, Regional Cooperation and the Solution of Bilateral Disputes, 27 August 2015.

⁵Connectivity will be analyzed in the next section.

⁶ European Commission, Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions, *EU Enlargement Strategy*, COM(2015) 611 final, Brussels, 10.11.2015, p. 8.

⁷ Joint Statement, ‘*Western Balkan 6 Ministerial – Economic Governance and Connectivity*’, Belgrade, 23 October 2014, point 5.

⁸ European Commission, Communication from the Commission to the European Parliament and the Council, *Enlargement Strategy and Main Challenges 2013-2014*, COM(2013) 700 final, Brussels, 16.0.2013, p. 4.

dual vocational education (so as to tackle the growing global competition and raise the skilled labour forces). Underlining the importance of the human dimension, under the auspices of the German Chancellor, the first annual Joint Science Conference of the Western Balkans was held in 2015, with the purpose of reducing the brain drain phenomenon and strengthening the science-politics-society dialogue for decision-making.

To conclude, even if the economic pillar seems to be one of three main components, the economic concerns are the underlining base for the Berlin process. This can also be observed from the amount of allocated budget for Berlin initiatives. However it is true that during the first year of its existence, the ‘Berlin Agenda’ has experienced a multiplication of the thematic areas – especially the ones falling under the third pillar, i.e. migration or fight against extremism and radicalization. The potential further inclusion of similar issues in the ‘Berlin Agenda’ raises concerns about the extent to which the continuous ‘swelling’ of this agenda might dilute the achievement of the initially posed objectives along with the risk of shifting key priorities.

1.3 The WB6 ‘Connectivity Agenda’ and its projects

Since its inception, the ‘Berlin Process’ focused on the concept of connectivity, as the new regional approach that would enhance regional cooperation among the WB6 countries, provide new prospects for sustainable economic growth and employment, and allow for positive spill over effects. The so-called ‘Connectivity Agenda’ consists of complex transport and energy infrastructure projects and investments, which aim to bond the Western Balkans countries to the core European transport network.

The connectivity agenda is strictly linked to economic governance and to the National Economic Reform Programmes prepared by the WB6 countries, and its implementation is deemed as a key factor for enhancing growth and employment. At the moment, the political ambitions are high and costly reflecting the complex infrastructure connectivity projects in transport and energy. Furthermore, these projects need highly specialized competencies and national coordination during the preparation phase until they reach the Single Project Pipeline. They have a long-term implementation period and thus call for very good sequencing of implementation, high cross-border relevance, besides the significant impact on other components of the socio-economic development strategies of the Western Balkans Six.

The process of identification and selection of the main connectivity projects took place during the follow up meetings. In April 2015, during the Western Balkans Six meeting in Brussels the respective Prime Ministers agreed on the Core Transport Network;⁹ whereas in June 2015 during the Riga Forum, it was decided on extending three Trans-European Transport Networks core corridors to the Western Balkans.¹⁰

Regarding the number of projects presented for co-financing from the six WB governments at the Vienna Summit 2015, it is:

- 11 road construction projects;
- 8 rail construction projects;

⁹ European Commission, *Western Balkans 6 Meeting in Brussels*, Brussels, Statement, Brussels, 21 April 2015, available at : http://europa.eu/rapid/press-release_STATEMENT-15-4826_en.htm

¹⁰ European Commission, Commission Staff Working Document, *Albania 2015 Report*, SWD(2015) 213 final, Brussels, 10.11.2015, p.22.

- 20 road and rail renovation projects;
- 6 power line projects; and,
- 5 strategic gas projects.¹¹

Although the WB6 countries presented an ambitious connectivity agenda, the number of mature projects in the pipeline ready for implementation, was reduced to 10: four energy and six transport projects. On the other hand, the prioritization of this limited number of investment projects provides for a concentration effort and higher implementation chances.¹² The total cost of the co-financing connectivity projects approved at the Vienna Summit amounted to 616.5 million EUR, of which 205.7 million EUR will be grants from the EU's Instrument for Pre-Accession Assistance (IPA II). The connectivity projects are funded by international donors according to the WBIF financing procedures. Grants are allocated mainly for technical assistance to prepare the infrastructure investments, while loans are used for infrastructure investments.¹³

Since 2009, WBIF – an EU-led facility instrument – provides finance and technical assistance for strategic investments in WB6. It is a structure operated and manned by consultants (contracted by EU or other donors) and works through pooling stakeholders' resources and expertise to finance projects, so as to strengthen coordination amongst donors and beneficiaries. It has supported WB6 administration in the preparation of mature infrastructure projects, which could be financed mainly through IFIs' loans and/or EU funds. Energy and transport have received biggest large-scale infrastructure investments, together with water and environment, municipal infrastructure and the social sector. The WBIF international donors are:

- European Commission;
- International Financial Institutions: Council of Europe Development Bank (CEB); European Bank for Reconstruction and Development (EBRD); European Investment Bank (EIB); World Bank Group (WB4); and KfW Development Bank; and,
- Bilateral Donors and Financial Institutions.

Referring to short term results, the WB6 countries agreed to fully implement, before the Paris Summit, the priority list of 'soft measures' - elaborated by SEETO and Energy Community - regarding the transport and energy sectors respectively. The implementation of these 'soft measures', is expected to open markets, eliminate trade barriers and generate a transparent regulatory environment.¹⁴ Whereas, the medium term results concern the implementation by 2020 of a series of priority projects identified along specific section of the core corridors.¹⁵

Under the guideline of the European Commission, the WB6 countries have established the National Investment Committees, which are in charge of elaborating the draft Single Project Pipelines. This new framework puts a strong emphasis on NIC's capacity to become a comprehensive and detailed planning and prioritisation mechanism, able to ensure the country's budgetary resources and fiscal space, along with

¹¹ Mario Holzner, Robert Stehrer & Hermine Vidovic, "*Infrastructure Investment in the Western Balkans*", Vienna Institute for International Economic Studies (WIIW), Research Report, nr. 407, September 2015, pp. 22-26.

¹²Ibid., p. 33.

¹³ More information on the WBIF financing procedures are available at: <https://www.wbif.eu/About%20WBIF>

¹⁴ European Commission, Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions, *EU Enlargement Strategy*, COM(2015) 611 final, Brussels, 10.11.2015, p. 9.

¹⁵ European Commission, *EU Enlargement Strategy 2015*, *op.cit.*, p. 10.

contracting the loans and implementing the investment projects on time.¹⁶ For the implementation, the WB6 countries will be technically assisted by the Coordination Office for International Financial Institutions (IFICO) – a group of highly qualified external consultants contracted through European Commission.

Overall, it still remain to be assessed to what extent and at what speed Albania and the rest of the Western Balkans countries will manage to succeed in adapting their internal institutions to the required standards, as well as to timely implement the already approved investment projects, having in mind the present macro-economic conditions and size of the public debt.

1.4 The ‘Berlin projects’ in Albania

Regarding the financing mechanism, it can be argued that the ‘Berlin Process’ only underlines the regional dimension of the connectivity projects. Initially, WBIF selected the projects to be financed “on the basis of regional and/or country needs and their consistency with EU accession priorities”.¹⁷ An example of this approach has been the rural road infrastructure improvements. In the latest calls for projects it has been stressed the ‘regional dimension’ of the infrastructure projects in energy and transport as a precondition to placing them in the European framework.

The new large-scale transport and energy projects mentioned in the Final Declarations of Berlin and Vienna, have been previously identified under the SEETO Comprehensive Network Projects¹⁸ and the Energy Community PECE list (Projects of Energy Community Interest)¹⁹. These projects have either received grant funding or have been identified as beneficiaries for EU grants, in order to complement the loan financed under the Western Balkans Investment Framework.

Concretely, the last call for proposal clearly indicates that:

- For the energy sector: “*Investment projects that feature on the list of Projects of Energy Community Interest (PECE) adopted by the Ministerial Council of the Energy Community Treaty in October 2013 will receive particular attention*”²⁰;
- In the transport sector it is also clearly stated the regional dimension: “*WBIF projects, particularly regional ones, must be part of the SEETO Comprehensive Network and/or included in EC policies and SEETO Memorandum of Understanding*”²¹.

In Vienna, Albania got approval for co-funding just one project, the 400 kV interconnection transmission line Elbasan – Bitola (MK). This constitutes the most important electricity project and the estimated cost amounts to 129 million EUR.²² The investment in the Albanian section of the transmission line is equal to 70

¹⁶ Ibid.

¹⁷ Western Balkans Investment Framework, “*A new approach to financial support*”, 12 November 2010, p. 2, available at: http://ec.europa.eu/enlargement/pdf/western-balkans-conference/wbif-a4-def_en.pdf

¹⁸ More information on SEETO Comprehensive Network Projects is available at: <http://www.seetoint.org/projects/seeto-comprehensive-network-projects/>

¹⁹ Energy Community, “*Development and application of methodology to identify Projects of Energy Community Interest*”, Final Report, Vienna, 26 September 2013, available at: https://www.energy-community.org/portal/page/portal/ENC_HOME/DOCS/2558181/0633975AD4927B9CE053C92FA8C06338

²⁰ Western Balkans Investment Framework, “*Practical Guidelines for WBIF Project Application and Submission*”, January 2014, p. 8.

²¹ Ibid., p. 9.

²² Holzner, Stehrer & Vidovic, *op.cit.*, p. 24.

million EUR; 80% of the value is in loan form and will be covered by KfW Development Bank, whereas the remaining 20% will be co-financed by the IPA II in grant form.²³ This joint investment is part of the European Commission's initiative to establish an East-West electricity transmission corridor between Bulgaria, Macedonia, Albania, Montenegro and Italy.²⁴

As a result, the last Albanian projects, submitted under the WBIF in the sectors of energy and transport, are clearly regional:

- WB12-ALB-ENE-01 “Detail design for 400 kV OHTL interconnection Elbasan-Bitola (Albanian part)”;
- WB13-ALB-TRA-01 “FS for the rehabilitation of the railway line Durres-Pogradec-Lin and new rail line link to border with former Yugoslav republic of Macedonia”;

The two projects mentioned in the Vienna Summit as ‘new entries’, and eligible for WBIF support, are:

- “400 kV OHTL interconnection Fier-Elbasan-Bitola (Albanian part)” co-financing of investment; and,
- “Feasibility study for Adriatic-Ionian Highway/expressway (Route 1 and Route 2)” as a technical assistance grant.

“The Feasibility study for Adriatic-Ionian Highway/expressway” was approved by the WBIF Steering Committee meeting of 16 December 2015 held in Paris.

1.5 Institutional set up in Albania and ‘Berlin projects’ pipeline

Albania has been using the already existing WBIF mechanism for the preparation of the connectivity project-financing documents. Since last year, WBIF's “New methodology to support Infrastructure Projects in the Western Balkans” has introduced the following novelties:

- investments co-financing scheme;
- clear distinction between ‘national’ and ‘regional’ projects;
- establishment of an institutionalized mechanism.

This methodology aims to identify, prepare and select for funding the prioritized investment projects, regardless of the source of funding, through the establishment the National Investment Committee and of the Single Project Pipeline. The establishment and functioning of the latter one is ‘key’ to the approval of investment co-financing grants for regional projects, and future soft technical assistance projects within the WBIF framework.

Thus far, in Albania there has been settled the Strategic Planning Committee – a decision-making structure headed by the Prime Minister. Currently, this structure plays also the role of the National Investment Committee, taking on the principles of ownership, strategic coherence, long-term sustainability

²³ Vienna Western Balkans Summit 2015, Addendum, Annex 1, Connectivity Agenda, Co-financing of Investment Projects in the Western Balkans in 2015, p. 4.

²⁴ Western Balkans Investment Framework (WBIF), Albania – the Former Yugoslav Republic of Macedonia Power Interconnection (II): Grid Section in the Former Yugoslav Republic of Macedonia, p.1, available at: http://ec.europa.eu/enlargement/pdf/publication/2015/20150820_wbif_cf_1002_mkd_ene.pdf

and transparency, as well as political commitment for the final approval of the list of projects included in the Single Project Pipeline.

During July – August 2015, with an Order issued by the Leading Minister, there have been established four Sectorial Strategic Management Groups (SSMGs) in transport, energy, environment and social issues. The task of the SSMGs is to prepare the Project Identification Fiches (PIF), as well as to score and to rank the PIFs in compliance with the agreed strategic relevance criteria, which will result at the end in the creation of the Single Sector Project Pipeline.

The preparation of the national Single Project Pipeline is under the competencies of the Strategic Planning and Development Unit (part of the Department for Development, Financing and Foreign Aid) at the Prime Minister’s Office). The Strategic Planning and Development Unit, as part of the Secretariat of the Strategic Planning Committee/NIC, has led and coordinated the overall process with line ministries and involved institutions for the finalization of the Single Sector Project Pipelines, as well as preparation and approval of the Single Project Pipeline by the Strategic Planning Committee/National Investment Committee.

By mid-September, the total number of submitted Project Identification Fiches amounted to 112. In the meantime, it has been reduced to 78 (as shown in table 1) prioritising the projects with the highest quality. Their quality was affected mainly by the scarcity of personnel, lack of an approved National Strategy for Development and Integration 2015-2020, and of a Sector Strategy for Transport and Energy for the timeframe 2015-2020.

Table 1: Berlin Projects Pipeline by November 2015

No.	Sector	No. of submitted PIFs	No. of assessed projects	Estimated cost/sector (in million EUR)
1	Energy	13	13	175
2	Transport	13	13	1.193
3	Environment	20	20	508
4	Social issues	32	17*	165
Total		78	63	2 041

Source: PMO and Authors’ own elaboration.

*Projects in education field are not included.

As can be noticed, the total cost for the implementation of the 78 fiches is approximately equal to 2.041 million EUR. By mid-December 2015, once the final Single Project Pipeline was approved by the Strategic Planning and Development Unit, it was presented to both EU and WBIF. It was composed of 15 projects owing a regional dimension and 24 national relevant projects. These 39 projects require a total financing of 1.899 billion Euro and the financing gap is equal to 92% (since only 141 million Euro will be covered through grants/loans or budget).

At this stage, the key challenge concerns the identification of the available fiscal space for the financing of these projects. This will clarify the size of financial window available for national co-financing of the projects. In the short run, Albania, like almost all the WB6 countries, faces high unemployment and low growth rates, along with high public debt concerns. The squeeze of public finance may affect the co-financing factor of the above projects and hence their feasibility. Also, no assessment exists as yet on their efficiency and cost-effectiveness as compared with other potential public investment impacting the budget spending.

2. Albania in the ‘Berlin Process’

2.1 Economic transformation in Albania

Albania has undergone a major economic transformation over the past 25 years. It opened up to global trade and became increasingly export-oriented, expanded the role of the private sector, dismantled regulations that stifled business development, and began to build institutions needed to support a market system. The result of these efforts has been robust economic growth, a significant rise in incomes, living standards, and enhanced macroeconomic stability.²⁵

However, the process of structural transformation began to stall in the mid-2000s, in the face of vested interests and as reform fatigue set in, structural obstacles begin to surface and to build up. The de-industrialisation, the development of internationally non-marketable services, the development of low added-value manufacturing activities, the severe under-development of agriculture, etc., are some of the few distortions of the economic tissue of Albania. Clear evidence of the weaknesses in the region’s economic model can be found in the extremely high unemployment rates. A continuing brain drain is one of the main problems that all countries face. Poverty is in many countries still unacceptably high.

One sector that has been entirely transformed by the foreign investments is banking. Starting in the early 2000s, the foreign investments into banking, combined with increased deposit bases, boosted the private sector credit. However, important financial sector reforms remain to be done – Albania is the case in point where for example, the part of the nonperforming loans (NPL) is 20.9%.²⁶ Tackling the large stock of NPLs is a priority if credit is to support the economic recovery.

Perhaps the biggest flaw in the Albanian economic model of after the ‘90s has been the chronic underutilization of human resources – both scientific and vocational ones. According to the available evidence, skill gap is particularly severe.²⁷ As a result, a market without proper market institutions has been left to decide on everything: from the re-allocation of financial capital²⁸ to the re-allocation of human capital.

Currently, Albania is focussed on an impressive swathe of economic reforms ranging from the fight against informality, to the reform of education and vocational educational training sectors. Manufacturing, energy, tourism and agro-industry, education and services will remain in the focus of the government for the years to come.

²⁵ International Monetary Fund, “*The Western Balkans: 15 Years of Economic Transition*”, Regional Economic Issues, Special Report, March 2015.

²⁶ Bank nonperforming loans to total gross loans are the value of nonperforming loans divided by the total value of the loan portfolio (including nonperforming loans before the deduction of specific loan-loss provisions). This indicator is valued to be 20.9% at the end of June 2015, according to “The Financial Stability Report (FSR) 2015 H1” of the Bank of Albania.

²⁷ European Training Foundation, “*Skills 2020 Albania*”, Working Document, Version of 26 June 2014, available at: [http://www.etf.europa.eu/webatt.nsf/0/27795DDDCBD2353DAC1257D6400322D57/\\$file/FRAME%20Skills%202020%20Albania.pdf](http://www.etf.europa.eu/webatt.nsf/0/27795DDDCBD2353DAC1257D6400322D57/$file/FRAME%20Skills%202020%20Albania.pdf)

²⁸ Ardian Hackaj, “*Bunkeret e Demokracise*”, Panorama Newspaper, 15 November 2012. The miss-allocation of capital in Albania after 1990 has been dealt with in the analysis “The Bunkers of Democracy”. It is argued that the accumulated amount wasted in non-productive assets such as unsold apartments and / or gas stations equals the amount wasted by the communist regime to build 700,00 bunkers during the period 1945 - 1990.

2.2 Economic Position of Albania

Due to the inefficient structure of the economy that Albania inherited from the communist regime, the transition process led to restructuring of the economy's composition. Starting from 1990 the share of the industry sector has dramatically dropped to about 16.8% in 2015.²⁹ The narrowing of industry sector provided usable resources to the other sectors, like construction, services, etc.

The Albania Report 2015 published by the European Commission, as part of the EU Enlargement Strategy 2015-2019, outlines that the monitoring of the economic criteria should be seen in the context of the increased importance of economic governance in the enlargement process. The 'Berlin Process' and Vienna Final Declaration envisage that the economic policy and its governance in the Western Balkan countries will be further enhanced through the preparation of annual National Economic Reform Programs. In this context, the participating States agree on the need of sectorial structural reforms, aiming to improve physical and human capital, industrial structures, the business environment and trade integration in order to boost competitiveness, employment and long-term growth in the Western Balkan countries.

The National Economic Reform Programme of the Albanian government outlines the obstacles to growth, which consist of the following:

- Macroeconomic vulnerabilities and high risk premium related with high public debt level;
- High government arrears to the private businesses, which have hampered confidence of the private sector;
- High level of NPL, which is constraining banks to expand lending activities;
- Rule of law and a not so friendly business environment;
- Large informality still reigning in the economy and hampering competition;
- Structural problems in the energy sector which otherwise has great growth potential;
- Rigid labour market potential linked also with the low quality level of private universities;
- Regulatory restrictions for the business operations.

Since 2013 the government arrears to the private sector have been cleared (even though through an increase of the public debt); the NPL have remained constant notwithstanding the expected roll-over effect of the payment of the arrears – from 24.9% in 2014 to 20.9% in June 2015³⁰; the “friendliness of the business environment” has gone on seesaw as per the World Bank Doing Business (-35 positions for 2016³¹ after a remarkable progression the year before); the informality has been fiercely fought in 2015 and is bringing the first positive results; the energy sector has drastically improved following the reforms, bringing the nationalised energy distribution company (OSHEE) to contribute positively in the state budget, and the energy production company (KESH) to pay taxes in arrears.³² The reform in education has produced a new law promoting the quality through competition mostly in the higher education, even if the impact on the labour market is not being felt yet.

²⁹Trading Economics, “Albania Industrial Production 2012-2015”, available at:

<http://www.tradingeconomics.com/albania/industrial-production>

³⁰ Bank of Albania, “The Financial Stability Report (FSR) 2015 H1”.

³¹ World Bank Group, Doing Business, “Ease of doing business in Albania”, available at:

<http://www.doingbusiness.org/data/exploreeconomies/albania/>

³² Monitor Magazine, 20 Octobre 2015.

In conclusion, the current Albanian government is in the middle of many strategic reforms and committed to complete them. On the other side, the continuing crisis lingering in the major trade partners, the lowering prices of raw materials (among the biggest exports of Albania), the weak macro-economic stability as translated by the increasing level of public debt, impact negatively the pace of the reforms. The small size of the Albanian market makes it necessary the coordination with the other WB6 partners in order to increase visibility and attraction of the foreign investors.

2.3 Economic relations between Albania, Western Balkans and the EU countries

Albania is part of the Stabilization and Association Process since 2006, which provides a comprehensive roadmap towards the accession for the Western Balkans. From the perspective of EU economic relations, the signing of the Stabilisation and Association Agreement is also assuming the enhanced capacities of Albanian economy to cope with the competitiveness of the single market and to make full use of the facilities that are offered therein.

EU is Albania's dominant trading partner, with especially strong links with Italy. Albania has increased its openness to trade, with total imports and exports rising from 86 % in 2008 to 92.3 % of the GDP in 2014.³³ The EU remains Albania's largest trading partner by far, with a total share of 77.4 % of its goods exports and 61.1 % of its goods imports in 2014.³⁴ During the same year, the EU has mainly imported from the Western Balkans:

- machinery and transport equipment (26.5%);
- miscellaneous manufactured articles (21.3%); and,
- manufactured goods classified chiefly by materials (19.8%).³⁵

Whereas the EU's exports towards the WB6 countries consist of:

- machinery and transport equipment (27.0%);
- manufactured goods classified chiefly by material (23.4%);
- chemicals (14.2%); and,
- mineral fuels (12.3%).³⁶

Per country, Italy remains the main trading partner of Albania as can be seen from the table below³⁷:

³³ European Commission, *EU Enlargement Strategy 2015*, *op.cit.*, p. 31.

³⁴ *Ibid.*, p. 79.

³⁵ European Commission, *“Trade Policy : Western Balkans”*, 7 May 2015, available at: <http://ec.europa.eu/trade/policy/countries-and-regions/regions/western-balkans/>

³⁶ *Ibid.*

³⁷ KPMG in Albania, *“Investment in Albania”*, 2015, available at:

<https://www.kpmg.com/AL/en/IssuesAndInsights/ArticlesPublications/Brochures/Documents/2015-Investment-in-Albania-body-print-FINAL-web1.pdf>

Table 2: Main trading partners

Main destinations of exports, 2014 (% of the total)		Main origins of imports, 2014 (% of the total)	
Italy	52	Italy	24
Spain	7	Greece	13
Kosovo	7	Russia	10
Malta	6	Serbia	6
Other countries	28	Other countries	47

Source: Customs Authority Duty of Albania

According to the data above, it can be noticed the importance of EU as a trading partner both as a bloc and as a composition of individual countries. This picture can also be applied for the FDI. However, the importance of FDI for the economic growth of WB6 has been the cause of a “race to the bottom” amongst WB6 partners mainly through fiscal “facilitation”. Macedonia and Serbia have intensively used direct aids to attract foreign investments, sometime in direct competition, not only with other WB6, but with their own domestic investors.³⁸

The new argument of joint economic governance replaces the “beggar thy neighbour” approach with a strategic, jointly planned, coordinated and implemented approach based on complementarity and on synergies. The starting point of this approach is the identification of the comparative advantage for each WB6 country and its embedment in the regional supply chain or the EU one. In theory this should not be very ground-breaking. All the former Yugoslav countries (except Albania) were fully integrated only 20 years ago. They also speak similar (if not the same) language, hence the economic cooperation is not a new concept for them.

From a recent study carried out by OECD, within the project "Next Generation Competitiveness", the following sectors need to be prioritised by WB economies:³⁹

³⁸ Svetlana Cenic et al., “A New Initiative for Stability and Prosperity in the Western Balkans”, Friedrich Ebert Stiftung, June 2015, available at: <http://library.fes.de/pdf-files/id-moe/11385.pdf>

³⁹ OECD, “Making Regional Value Chains happen in the Western Balkans”, power point presentation, Paris, 13 June 2013, available at: <http://www.slideshare.net/OECDpsd/making-regional-value-chains-happen-in-the-western-balkans>

Table 3: Sectors prioritised by WB economies

	ALB	BIH	HRV	MKD	MNE	SRB
Metal industry						
Textile, Apparel						
Wood processing						
Agro-food						
Mining						
Construction						
Automotive						
Pharmaceuticals						
ICT						
Tourism						
Banking						
Energy						

Source: OECD (2013).

The table above shows that, Albania has a comparative advantage in the sectors of metal industry, textile, apparel, agro-food, mining, tourism and energy. The success in raising the volume of exchanges will depend on close regional cooperation through the development of value chains, especially in the above-mentioned sectors where complementarities exist. Identifying barriers limiting the value chain development and taking actions to reduce these barriers is crucial for trade facilitation. In the framework of the ‘Berlin Process’, and more particularly with reference to ‘trade facilitation’ section in the Vienna Final Declaration, the Western Balkan countries have committed at the Vienna Summit to bring to a successful closure the on-going negotiations in CEFTA on a framework agreement to facilitate trade.

Table 4: WB Economies Positions in Supply Chains - 2009

Industry	First stage	Intermediate stages	Final stages
Food, beverages and tobacco	SRB		BIH HRV MKD MNE
Textiles, Clothing			ALB BIH HRV MKD SRB
Wood and Cork		BIH HRV MNE SRB	ALB BIH
Paper, Printing and Publishing		ALB BIH HRV SRB	BIH SRB
Coke, Petroleum Products	HRV		
Rubber and Plastics		MKD SRB	
Basic Metals	BIH MNE	MKD SRB	
Fabricated metal products	BIH	ALB HRV MKD SRB	SRB
Electrical machinery, nec	HRV SRB		
Motor vehicles, Trailers	BIH		

Source: OECD (2013).

According to Albanian government analysis,⁴⁰ here are three ways in which the economic growth can be constantly encouraged in Albania through:

1. foreign loans and borrowings;
2. export of the raw material, some readymade products and of a certain category of services;
3. an economic restructuring and real structural reforms, the primary increase of the domestic product, diversification of the products and services, and mass adoption of new technologies.

In the government opinion, the third way reflects many positive examples worldwide and has generated constant long-term growth. Albania shall have to pursue specific economic growth policies with that focus. The key word, in this case, remains “increasing the domestic product rate and boosting exports”. That will enable the government to achieve GDP growth based on production and not consumption, like it used to happen in the prevailing model so far.

⁴⁰ Prime Minister’s Office, “The Economy”, available at: <http://www.kryeministria.al/en/program/economic-development/the-economy>

Conclusions

A joint economic strategy with the necessary reforms in the Western Balkans countries themselves is the only possibility to restart the catching up process. This could give a new impetus for the enlargement and integration process. It is highly appreciated that in ‘Berlin Process’ the economic and social issues play a bigger role, but balanced growth needs a comprehensive approach. A simplistic strategy of promoting the construction of the necessary infrastructure will not succeed, unless it is complemented by a strategy to support SMEs. The development cannot be based only on the construction sector, building roads (publicly financed) and houses (often financed by remittances). The region needs a parallel development of the infrastructure including better and faster rail connections and local public transport on the one hand, and a re-industrialization in connection with digital services on the other hand. Only such a balanced development may foster economic growth and create jobs for the younger, often better-educated and trained generation.

The ‘Berlin Process’ offers a unique opportunity for the WB6 to be better prepared and coordinated, so as to increase their weight in different negotiations, not only with EU, but also with other IFI or international organisations. Albania shares a similar profile and long term goal with its neighbours: a candidate country that wants to be integral part of the European Union family. However, the lingering financial and economic crisis, the migration flux and the very questions that EU is asking about where it wants to go for the next 10 to 30 years, render the cooperation with our neighbours even more necessary. This regional dimension of national policies can be illustrated with the speech of Prime Minister Rama in Hong Kong where he promoted Albania as a foothold in a market of 26 million inhabitants.⁴¹

On the strictly national level, Albanian institutions need to further work towards a better preparation of the infrastructure projects, starting with a better coordination of different line ministries. The fiscal space needs to be realistically taken into account when planning for financing, as well as the complexity and costs of maintenance period. On the ‘soft measures’, Albania holds the initiative on the Regional Youth Cooperation Office and should use this to increase and its profile and weight. Other issues such as VET or migration need also full attention to allow for a professional and fully coordinated participation of the country in the ‘Berlin Process’.

Last but not least, the civil society’s contribution remains one of the trump cards that Albania should use to achieve the pre-agreed objectives on an efficient participation in the process. The knowledge, energy, networks and resources of the Albanian civil society are an invaluable asset and should be used in close cooperation with the government (and eventually parliamentary) structures.

⁴¹ Edi Rama, “*Investimi ne Shqiperi do te thote investim ne nje treg 26 mln banoresh*”, Dita Newspaper, 28 October 2015, available at: <http://www.gazetadita.al/investimi-ne-shqiperi-do-te-thote-investim-ne-nje-treg-26-mln-banoresh/>

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