

# ALBANIA DEVELOPMENT FINANCE ASSESSMENT



JOINT SDG FUND





# ALBANIA

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*\*At the time of writing, the Ministry of Finance and Economy had not yet been separated into the Ministry of Finance, and Ministry of Economy, Culture and Innovation. As such, the report makes reference to the Ministry of Finance and Economy.*

# EXECUTIVE SUMMARY

The DFA is a comprehensive review of a country's financial landscape, which helps identify strengths and weaknesses in the financial system and how they affect its development objectives as well as its progress towards achievement of the SDGs. This report explores financing instruments and mechanisms, policies, institutions, and capacities in place in Albania, with the aim of highlighting: existing resources, policies, institutions, capacities, and monitoring tools; emerging initiatives to strengthen resource mobilization, policies, institutions, capacities, and monitoring; and future opportunities to further strengthen policies, institutions, capacities, and monitoring to aim for a more integrated approach to development financing.

## Albania's Development Financing Needs

Albania is a small economy and highly vulnerable to regional and international trends. In recent years, the economic and political developments in neighbouring countries such as Greece and the wider EU economies, the Covid-19 pandemic, the war in Ukraine, and the rise in global energy and fuel prices have had substantial implications for economic growth and macroeconomic trends in the country. Despite its growth, the productivity of the Albanian economy remains well below the EU average. The services sector is the largest contributor (45%) to the GDP during 2005-2021, followed by agriculture (18.4%), construction, and industry. Despite employing 33.8% of the population, the agriculture sector offers the lowest wages. Public sector wages in general remain 30% higher than private sector. The labour market displays an unemployment rate of 11.8%, with substantially higher youth unemployment (27.1%), and a systemic gender gap. **EU acces-**

**sion is a long-held aspiration for the country and sits at the heart of the country's vision for development and democratization reforms.** The National Strategy or Development and European Integration 2023-2030 (NSDEI) and the National Plan for European Integration (NPEI) are the foundations that orient the planning and financial programming of the sectorial and cross-sectorial strategic framework. Yet, despite efforts at successfully completing the costing exercise for all policy and strategy documents, no clear financial analysis of their implementation, including funding gaps and resource mobilization challenges and risks, has been included due to lack of sufficient data. As such, it is hard to link NSDEI and NPEI strategic measures to the country's Medium-Term Budgeting Program (MTBP).

**The four sectorial priorities defined in NSDEI are agriculture and rural development, tourism, energy and natural resources, and digitalization.** The initial post-1991 focus on economic and structural reforms, the establishment of a market economy, and strengthening of administrative capacities of public institutions have, in subsequent decades, been replaced with sectorial and infrastructure development. Access to energy has a profound impact on Albania's economy, with energy shortages and price spikes disrupting production and raising costs for consumers. Therefore, investing in energy infrastructure and technologies that promote efficiency, sustainability, and affordability is essential for economic growth. NSDEI dedicates a special chapter to the Agenda on Sustainable Economic Development, Connectivity and Green Growth.

**The National Single Project Pipeline (NSPP) is an important instrument for operationalizing**

**the NSDEI, sectorial strategies and government priorities, and transforming the latter into concrete projects.** The NSPP is a strategic medium- and long-term prioritization instrument established in 2015, which defines the list of the strategic projects in the country, orients foreign and domestic sources of funding towards priorities, and connects long-term priorities with MTBP. There are 145 strategic projects in the pipeline for the period 2024-2026, the majority of which partially matured and non-matured. The EIP for the WB 2021-2027 notes that out of 227 projects, 29 are funder implementation with 100% of the financing guaranteed. The financial gap amounts 89% of EIP total financing needs.

**Despite the growing significance of crisis- and development-driven public investments over the last two decades as the primary driver of economic development, Public Investment Management (PIM) systems need further improvements** to address compliance with guidelines for the selection and approval of new investment projects as part of the budgeting process, guaranteeing value for money considerations during the PPP selection procedures and integration of shocks response related expenditures in the budgetary processes.

**Within the Western Balkans, Albania recorded a more moderate contraction in economic growth in 2020 and is rated among the countries with the highest growth in 2021.** Albania ranked second in the region in terms of GDP growth for 2022. Albania has lower GDP per capita than the WB6 regional average. It ranks with the second lowest level of unemployment rate in the region, and, together with Serbia, the lowest level of regional youth unemployment rate (although it stands at double the EU average). The 2021 and 2022 inflation rate for Albania remains lower than in other Balkan countries, partly due to subsidized energy prices which has also negatively influenced the debt stock. Albania ranks third in the Western Balkan region in terms of FDI as a percentage of GDP, although the effective number of FDI source countries and companies and the FDI target sectors remain very limited. The country also ranks the second lowest regionally in terms of 'Doing Business'.

**Public tax revenues as a percentage of GDP in Albania are low (29.1%) compared to the EU (42%) and the WB average (35%).** Despite having similar or higher tax rates compared to the peer countries, Albania has shown lower

revenue generation over the years due to informal economy, a narrow tax base, and efficiency problems in tax administration and collection – something that has resulted in low VAT productivity. Like other Western Balkan countries, Albania projects a return to the fiscal consolidation path in the upcoming medium-term period as lower fiscal stimulus is expected to be required compared to the recent three years. Albania's debt level is the second highest among the Western Balkan countries, currently facing relatively high, but controlled rollover risks, yet public debt is expected to gradually decline in the upcoming medium-term period, despised the increased interest rates.

**The COVID-19 pandemic highlighted the importance of proactive investment to build comprehensive and resilient social protection systems.** With a registered population of just over 2.8 million people and a shrinking demographics, Albania continues to face poverty and inequality are challenges even despite improvements in its Human Development Index in recent years. Although the country's means-tested social assistance program, Ndihma Ekonomike (NE), provides support to families and individuals in need, active social protection policies such as the economic reintegration of the working age beneficiaries into labour market remain a priority and a challenge. Despite boasting the highest life expectancy in the region, Albania needs to increase both the level and efficiency of education, health, and social protection expenditures to match the levels of investment in human capital in peer countries including the WB6 and the STEE7 countries.

#### **Landscape of current development finance flows**

In Albania, tax revenues are the main contributor to public revenues, with grants and non-tax revenues, including ODA and budget support, representing an insignificant share of total public revenues by comparison. Direct income taxes are a weak contributor to the budget revenues, representing around 18-20% of tax revenues, with indirect taxes generating almost twice the budget revenues in comparison, implying a weak redistributive impact. The three largest contributors to tax revenues are social insurance, VAT, and excise taxes, though VAT remains the primary source of tax revenues (35.4% of in FY2022). The VAT threshold in Albania is low compared to the region, and although its reduction was aimed at fighting informality, the tax

administration still lacks the capacity to achieve the expected results from this policy. Only 54% of total VAT revenues are collected compared to the set benchmarks (EU average 61%). As such, the relationship between tax revenue growth and GDP growth has become more irregular in recent years. According to MTRS, increasing tax revenue to 2.3-3.0% of GDP is necessary to finance additional public spending and support reform measures in the coming years.

**The effectiveness of a progressive tax scheme, introduced in 2014 as part of a fiscal reform program aimed at reducing societal inequalities and disparities, has been hindered by the under-declaration and under-reporting of taxable income.** The country is estimated to have lost around 5.6% of its GDP due to indirect tax exemptions, including VAT compliance gaps and tax evasion. The VAT compliance gap was nearly twice the EU average in 2015. It is estimated that reducing tax exemptions, including VAT, could result in an additional 0.2% of GDP in annual tax revenues. Other measures to raise public revenues could include introduction of intermediate tax brackets and an increase in the highest threshold for personal income tax, bringing self-employment under the labour income taxation scheme, reducing VAT/excises/national taxes exemptions, and increasing property taxes. Given that VAT is the main contributor to budget revenues, a robust and stable VAT is of considerable importance. Although social security contributions account for 6% of GDP, bringing the ratio of direct taxes closer to that of indirect taxes, their significance still fall behind that of tax revenues. Contributory revenues are only able to cover 60% of the total social protection expenditures, indicating a significant gap in the system's ability to provide adequate social protection for citizens, resulting in only a 9% share of social protection expenditures in GDP.

**Limited access to reliable data undermines public revenue and expenditure projections and planning.** On the public revenue side, differences exist between the revenue values indicators from their initial planning to their revision and actual execution. Such unrealistic forecasting has rendered planning based on forecast budget figures more challenging. On the public expenditure side, the published budget provides information on current and capital expenditures by program but does not include details on the total costs of projects. There are also substantial differences between projected

and actual public expenditure values, with the discrepancies growing in recent years, partly in response to consecutive shocks that have further undermined budget forecasting. Deviations from the originally planned levels of budget expenditure primarily reflect ongoing weaknesses in public finance management rather than an inability to meet revenue targets.

**Over the years, social protection has consistently been the primary beneficiary (25-30%) of public expenditures, although social protection spending remains significantly lower than the EU average.** Around 82.4% of social protection spending is allocated to pensions. Several challenges continue to face the public pension scheme in Albania, including low participation rates of the working-age population as contributors, high levels of informality, and low participation rates in the pension contribution scheme among farmers, youth emigration, and an anticipated increase in the number of beneficiaries in the coming years. As a result, the social insurance scheme is largely subsidized by the government, thus contributing to high fiscal deficit. After pensions, general public services, such as housing and community amenities, economic affairs, health, and education, are the second-highest beneficiary of public expenditures. Both domestic and foreign interest expenditures are increasing due to growing public debt, macroeconomic risks, and global developments.

**Consecutive shocks in recent years (including the 2019 earthquake, the Covid-19 pandemic, and the war in Ukraine) raised the need for expansionary fiscal policy to bolster the economy, resulting in an upturn in capital expenditure since 2021.** This took the form of wage subsidies, increased social spending, and two credit guarantees through commercial banks to ease salary payments and release financing for private sector capital and investment needs. Subsidies constitute an insignificant component of current expenditures in relation to GDP while tax exemptions are used more frequently to supporting target groups or provide incentives to various sectors of the economy. Similar to the other Western Balkan economies, Albania struggles to control current expenditures on public wages and pensions, challenging the fiscal consolidation efforts. In this context, enhancing the sustainability of the public administration and pensions systems and better targeting of social transfers are important priorities.

**The crises-induced expansionary fiscal policy**

**coupled with a sharp economic slowdown have widened the fiscal deficit and increased public debt despite the preceding years' fiscal consolidation efforts.** The country's fiscal deficit reached 3.7% of GDP at the end of 2022, showing a decreasing trend after the increase of 2020. The fiscal deficit is financed through domestic funds, including privatization receipts, domestic borrowing, change in the liquidity stock of the Treasure Single Account (TSA), as well as through foreign funds, including long-term loans and budget support. Public debt stood at 64.6% of GDP at the end of FY2022, which is still higher than the regional average of 59%.

**Although the public debt ratio is high, it remains sustainable and can be serviced, repaid, refinanced, and restructured in an orderly manner.** Public debt is vulnerable to potential growth-related shocks such as economic downturns, interest rate increases, and exchange rate fluctuations. The country's foreign debt is more sensitive to currency depreciation than to interest rate increases. Foreign exchange reserves can play a crucial role in mitigating this risk. Nevertheless, Albania is expected to face high gross financing needs during 2022-2026, equivalent to an average annual level of 23% of GDP. Revenue mobilization, together with the improved assessment of fiscal risks (including particularly the State-Owned Enterprises [SoEs] arrears and the Public-Private Partnership payments and guarantees obligations) are crucial for maintaining a stable fiscal position and reducing potential risks to debt sustainability.

**Public-Private Partnerships (PPPs) have been used in recent years for attracting capital investments in strategic public sectors, aiming to ease the budgetary burden and to create fiscal space.** Lack of comprehensive analysis of the value for money and fiscal risks associated with PPPs/concessions indicates the government failure to regularly monitor the PPP contracts. The energy sector has attracted the most awarded concessionary contracts, followed by transport. Despite this, the Albanian energy sector is not financially self-sustainable, with many SoEs also engaged in this sector. Governance of SoEs in the energy sector is deemed weak, and the country has been cautioned about the high contingent liabilities associated with SoEs, that could adversely impact the debt ratio and fiscal risks. Subsidized electricity prices for households and SMEs discourage energy efficiency measures and strain fiscal accounts.

**Although private investment levels have grown substantially since the late 1990s compared to public finance, they play a much smaller role in financing economic development in Albania.** This to some extent stems from the country's relatively recent and challenging process of privatization in the post-1991 phase (including the disastrous collapse of the pyramid schemes in 1997) – which implied that a large portion of privatization over the last three decades has been in the form of a transition of ownership from SoEs to private sector entities, rather than an entry of new private investments into the market. This has also implied a slow and weak growth of the financial instruments, products, and markets to support private investments.

**Albania's financial system suffers from low levels of development and is dominated by banks, holding 90% of the financial sector's assets and the primary source of lending to the public and private sectors.** The full privatization of the state-owned shares in the banking sector was achieved in 2009, with 12 banks operating in the country in 2022. An estimated 75% of the country's financial market is owned by five banks. The relatively recent history of privatization in Albania together with the disastrous collapse of the pyramid schemes in 1997, further explains the relatively weak private investment landscape, trends, and instruments in the country. The nominal value of bank lending rose from 10% of GDP in 1998 to 33.4% in 2022, with the largest weight of lending (72%) to private non-financial corporations, particularly wholesale and retail trade, followed by construction, manufacturing, and electricity and gas supply. The rate of banks' Non-Performing Loans (NPL) has declined from 25% in 2014 to 5% in September 2023, demonstrating a major improvement in banks' management of loans. Banks' lending to the central and local government reached its highest level in 2021 showing the sector's important role in supporting financing for public investments and government interventions at times of crisis. Banks remain the main debtholder in the country, holding more than 63% of Albania's total burden of the sovereign debt in 2022.

**The Tirana Stock Exchange (TSE), established in 1996 as an attempt at developing the Albanian capital market and facilitating the mass privatizations at the time, was suspended in 2022.** The malfunctioning of the TSE and the



eventual suspension of its license are considered to be a result of a number of factors, including the interruption of the mass privatization and the collapse in investor confidence in financial institutions after the 1997 pyramid schemes crisis, lack of adequate and efficient market infrastructure for issuing, trading, clearing and settlement, and lack of crucial institutions for effective functioning of a capital market resulted in. Established in 2014, the Albanian Securities Exchange (ALSE) is the country's first licensed private institution for securities exchange. ALSE initially traded only in government securities, until the establishment of a Central Securities Depository (CSD) for non-governmental securities, named the Albanian Securities Register (ALREG) in 2019. Although ALSE and ALREG provide the complete technical infrastructure for listing and trading the corporate securities in LEK, no Albanian companies are yet listed, and as such, do not yet fulfil the mission to mobilize financing for the Albanian companies which continue to fully rely on bank credits. Approval of the 2020 Law on Capital Markets has been a crucially important development in terms of increasing investors' trust in financial markets and offering better protection of their interests.

**The government securities market and the private placement bond market constitute the most active segments of the Albanian securities market, while equities, corporate bonds with public offering and derivatives market are still absent.** The banks and institutional investors are the largest buyers of government bonds and bills in the primary market on their account and on behalf of their clients, while households still own only a small percentage of government securities as their investments take the traditional form of bank deposits. Currently the Albanian Government remains the sole issuer of government securities. The Primary Dealer System, implemented in Albania since 2018, intends to develop the government securities market and encourage the secondary market and liquidity increase, though no evidence exists yet on its impact on the development of the secondary market. The increase in the number of issues of corporate bonds has remained very limited given the number of participating investors. This is because the Albanian capital market lacks brokers, investment companies and intermediate institutions, which normally should be the banks themselves. Since September 2023 "Eurizon Capital" is authorized as an investment fund under the Inte-

sa SanPaolo Group to create opportunities for Albanian investors to have a direct access to European Markets for investments in collective mutual funds within the EU.

**Despite its very small share in financial intermediation (4%), micro-finance plays a crucial role in serving individuals, farmers and small businesses that do not have access to the banking system.** The Albanian microfinance sector is composed of Non-Bank Financial Institutions (NBFI), providing microcredit and other types of lending such as financial leasing or factoring, and Savings Loans Associations (SLA). About 45% of the loan portfolio granted by NBFI is to individuals, with the rest to the business sector. Most of Albania's Micro-Finance Institutions (MFI) follow a socially responsible policy targeting financially excluded individuals and disadvantaged areas. The sector has evolved in line with the socio-economic developments of the country and the growing market demands, offering products and services that raise living standards for individuals and support free enterprise for micro-businesses but also ensuring sustainability in quality of life and consolidation of local business activity, especially family businesses. MFIs' development and strategic repositioning over time means that they now represent a diversified set of actors, shareholders, and clients.

**Small and Medium-sized Enterprises (SMEs) constitute 99.8% of all enterprises and 81.6% of employment in Albania yet struggle to access finance.** Despite the Law on SMEs that provides the legal framework for various forms of financial support to SMEs, limited access to finance, especially bank loans, remains a major challenge. This is mainly due to high informality (especially in agriculture), limited availability of collateral and low levels of financial capacity. Due to the specifics of the admission criteria, the participation rates in donor-financed SME financing schemes remain low. Enhancing SMEs' access to finance, through increasing the effectiveness of existing grant schemes and introducing and promoting new financial tools and instruments can contribute to strengthening the competitiveness of SMEs.

**The first investment fund in Albania was established in 2011.** The number of such funds increased to 12 funds by 2022, with combined net assets amounting to 4% of GDP and 4% of financial sector assets. The sector's growth has been driven by inflows from (mainly retail) inves-

tors as well as positive returns on assets (mainly domestic sovereign bonds). The sector is highly concentrated, with the largest fund accounting for 62% of total investment funds' assets and the three largest investment funds accounting for 95% of the sector's assets. The first private pension fund was approved in 2010, following the licensing of the management company of voluntary pension funds, with 4 management companies, 4 pension funds and 6 depositories currently operating in the Albanian voluntary pension funds market. The growth of the net assets of the voluntary pension funds market, as well as their investment value and membership have grown substantially over the period 2012-2022.

**International foreign aid has lent crucial support to Albania's development needs, its preparation for EU membership, and its crisis response over the last three decades.**

Sectorial foreign aid priorities have evolved over time: whereas in the 1990s aid focused on sectors such as transport and communication, agriculture, and private enterprise development, the 2000s instead prioritized energy, water, social development, and rule of law, and the 2010s allocate more aid towards governance, energy, and financial services. Aid allocation towards critical economic sectors such as water and agriculture, and social sectors such as health and education has declined significantly over time. The EU has been Albania's largest donor, providing 100% grant assistance within the framework of the EU financing Instrument for Pre-Accession (IPA). IPA II that covered the period 2013-2020 was disbursed through various instruments such as conditional budget support focusing on policy areas such as Democracy and Governance, Rule of Law, Economic Governance, Competitiveness, and Growth. Currently, there is under implementation IPA III covering the period 2021-2027. The growing dominance of Other Official Flows (OOF), most of which accompanies non-concessional interest rates, over Official Development Assistance (ODA) as the dominant aid modality has increased Albania's debt levels and pressured domestic budget. While the 1990s was dominated by ODA flows (grants and soft loans) towards humanitarian and balance of payment support, the 2000s witnessed a growing use of OOF. Given the pressure to reduce the debt to GDP ratio, capital investments (which are typically covered by OOF) could be subject to suspension, further impacting the budgeting process, the realization of investment projects, and potentially disrupting the implementation of gov-

ernment policies. Therefore, reorienting aid flows towards ODA loans remains very important for the years to come. Greater alignment between aid allocation and strategic NSDEI pillars is also vital for maximizing aid efficiency and effectiveness.

**Remittances have been a major source of foreign exchange inflows to Albania, constituting a larger share of GDP than FDIs and export revenues, and contributing to financing trade deficit and poverty reduction.**

Currently, there are 1.4 million Albanian emigrants living in countries such as Greece, Italy, United States and Germany. Remittance inflows constitute 15-20% of GDP during the period 1996-2006, dropping to around an average of 9.5% in the period 2007-2022, mainly due to the increased GDP size. Given their resilience to internal shocks and their quick recovery in the face of crisis, remittance inflows have been not only a stable source of revenue for the economy but also a crucial financial resource for crisis response. As a major source of foreign exchange inflows, they also play a crucial role in financing the country's trade deficit, covering about 38.8% of it in 2022 and, therefore, of great importance to macroeconomic stability of the country. In the context of the country's weak social protection schemes, remittances continue to be an important form of social protection and poverty alleviation. Around 23-26% of households receive remittances, and the latter constitute the only source of household income for 24.4% of remittance-receiving households, and for the rest they account for 14-23% of their income.

**Despite the introduction of relevant Foreign Direct Investment (FDI) and privatization laws in the 1990s, high risks associated with political and social instability, low levels of economic diversification and a weak financial system have hampered FDI flows to Albania.**

The pyramid scheme crisis of 1997 was a blow to the country's efforts at creating a conducive foreign investment environment. FDI net inflows reached a low of around 1% of GDP by 1999 before starting a steady recovery, reaching over 11% of GDP by 2009 just before the onset of the Global Financial Crisis. Since then, FDI net inflows and the overall FDI stock have followed a declining trend as a percentage of GDP. Albania's vulnerability to external shocks, regional and global volatilities, ranging from the Eurozone crisis to the Covid-19 pandemic, have further undermined FDI flows to the country.

**Most FDIs since 2000 have been brownfield investments stemming from the privatization of**

**strategic State-Owned Enterprises (SoEs), with only a minor FDI share in the form of green-field investments.** Institutional and regulatory reforms, capacity improvements and economic developments since the early 2000s have aimed at enhancing the country's green-field investment climate, though the latter has never managed to surpass the brownfield investments. During the first 25 years of transition, energy, mining, infrastructure, manufacturing, agriculture, and food processing were the priority FDI sectors in Albania. Energy and power generation sectors have continued to attract the majority of green-field investments to date. In 2022, The FDI equalled 6.7% of GDP. Given the growing investor interest in the energy sector, it is important to ensure sufficient foreign investments are also drawn to other strategically important economic sectors.

**Illicit Financial Flows (IFFs) constitute a significant challenge to Albania, particularly in terms of their drain on potential private financial resources, their integration into official financial system, their large associated informal economies and associated cash flows, and their undermining of the state, state institutions and democratic cultures.** According to 2020 estimates, IFF in Albania represents around one fifth of the economy. Key reasons for the prevalence of illicit financial activity are the lack of institutional capacities, integrity, and development to keep up with the scale of trade. Progress has been made in establishing appropriate legal, regulatory, and enforcement mechanisms to counter IFFs in Albania, although the country still lacks formal procedures to measure and assess the extent and activities of the illegal economy and the criminal activities and products in circulation.

#### Key challenges in mobilizing development finance within an INFF framework

Albania is expected to see a steady economic growth and a gradual fiscal consolidation starting from 2023; however, a narrow focus on GDP growth will not address the country's development challenges. Investing in people, increasing firm productivity, building a more sustainable growth model, and strengthening public finances should be components of a stronger and more sustainable development strategy. Growth needs to become more green, more resilient, and more protective towards vulnerable groups, rendering financing more difficult but more sustainable. In addition, the fiscal space should be increased through revenue

mobilization through the deployment of extra fiscal resources, including foreign capital flows and mobilization of the domestic private capital inside and outside the financial institutions.

**Albania remains as one of the most risk-exposed countries in the region, yet there is a lack of clear measurement of the risks, inhibiting relevant policy responses.** Over the last decades, the country has experienced several risks such as macroeconomic shocks (1991), financial sector crisis (1997), natural disasters such as floods, fires as well as earthquakes (the most severe being the 2019 earthquake), the Covid-19 pandemic, and most recently the ramifications of the war in Ukraine – all of which have created important fiscal challenges for the economy. The Government of Albania lags in monitoring, reporting and managing such fiscal risks and suffers from a large insurance protection gap (both for public and private assets) and no sovereign insurance to provide budget support during emergencies. This explains the government's substantial funding gap in response to the multiple crises of the last years and the use of an ex-post policy approach in the form of budget cuts and reallocations, borrowing, or donor aid, which are costly and disruptive despite their rapidness. These measures have widened the country's fiscal deficit and debt burden (74.5% of GDP in 2021). Under the limited ex-ante sources of funds, public expenditures were reallocated through normative acts and crowding out important planned expenditures, presenting an opportunity cost in terms of forgone or delayed returns.

**Shadow economy in Albania is large and informal economic activity accounts for about 27% of GDP, with one-third of the country's workers are in the informal sector (over half in the agriculture sector is included).** In general, informality is driven by a weak institutional and regulatory environment, insufficient enforcement capacity of public authorities, corruption, and low awareness of its negative social implications. Widespread informality undermines competition, hinders efficient allocation of state and private resources, and reduces tax revenues and funding of social security systems. Reducing informal employment and a redesign of the relevant tax policies could help increase social contributions and income tax revenues in addition to raising employment and minimum wages. The fiscalization process that started in 2021 is expected to improve the avail-

ability of real-time information about economic activity. At the time of writing, no cross-cutting strategy to tackle informality has been drafted or adopted.

**Albania is experiencing a rapidly shrinking population due to emigration and declining birth rates, pressuring both the pension system and the labour market.** The share of pensioners to the total population has increased from 19% in 2010 to 22.6% in 2022. Although the contribution revenues have increased over the last decade, the 2022 level of deficit in the pension system is twice the deficit level in 2010. Underreporting of wages in the private sector impacts the pension contribution rates. The size of the 15–29-year-old age group has decreased by 30% over the period 1989-2020. The brain drain continues to be a highly costly phenomenon particularly for occupations that are difficult to fill in the labour market. Although the number of immigrants from other countries to Albania and returned emigrants have increased, this is insufficient to compensate the emigration numbers.

**Albania's existing social protection program (NE) has a limited impact on reducing poverty risk.** Around 21.8% of the population are at risk-of-poverty, but only 9% of the Albanian population are beneficiaries of the NE program – 95% of which is provided in the form of cash transfers. Local governments are responsible for social care provision, yet their fiscal space is insufficient to substantially increase social protection funding at the local level. While about one-third of public expenditure is allocated to social protection, this is still not comparable to the EU27 average, with ongoing problems persisting in terms of the targeting and adequacy, increased deficit in the public social insurance system, increased number of beneficiaries versus contributors due to the aging population, and the slight increase in the replacement rate for old age pensions.

**Significant financial resources are required to address strategic development and sectorial priorities.** The country's numerous strategic documents highlight the indicative cost of achieving the objectives set out in national development plans, however no complete financial scenarios are provided in terms of resource gaps and required fund mobilization strategies, or the impact of the financing gaps on the implementation of the strategy. A crucially import-

ant instrument to operationalize the NSDEI, sectorial strategies and government priorities in concrete national and regional megaprojects/projects is the National Single Project Pipeline (NSPP), which as of 2022 has listed 145 strategic projects the majority of which in non-matured and partially matured stage. Based on indicative budgets the financing needs are over 16 billion EUR.

### Recommendations for the INFF

This report offers a set of recommendations to inform the development of an integrated financing strategy to underpin Albania's sustainable development vision. The recommendations are organized into three main groups:

1. Overall financing strategy recommendations;
2. Recommendations specific to the financing of thematic priorities;
3. Recommendations to improve governance, monitoring, and reporting mechanisms for an INFF. Key strategies include reforming tax policies and administration, streamlining tax incentives, boosting public and private investment in sustainable development, and fostering a conducive environment for domestic and international finance.

The report emphasizes the critical role of coherent policies, institutional reforms, and strategic partnerships in achieving sustainable development goals, underscoring the necessity for Albania to adopt a multi-faceted approach to finance strategy that aligns with its long-term development vision and priorities.

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