INTERNATIONAL MONETARY FUND

IMF Country Report No. 15/129

ALBANIA

May 2015

FOURTH REVIEW UNDER THE EXTENDED ARRANGEMENT AND REQUEST FOR MODIFICATION AND WAIVER OF APPLICABILITY OF PERFORMANCE CRITERIA—STAFF REPORT; AND PRESS RELEASE

In the context of the fourth review under the Extended Arrangement and request for modification and waiver of applicability of performance criteria, the following documents have been released and are included in this package:

- The **Staff Report** prepared by a staff team of the IMF for the Executive Board's consideration on a lapse of time basis, following discussions that ended on March 17, 2015, with the officials of Albania on economic developments and policies underpinning the IMF arrangement under the Extended Fund Facility. Based on information available at the time of these discussions, the staff report was completed on April 28, 2015
- A **Staff Supplement** updating information on recent developments.
- A **Press Release**

The documents listed below have been or will be separately released.

Letter of Intent sent to the IMF by the authorities of Albania*
Memorandum of Economic and Financial Policies by the authorities of Albania*
Technical Memorandum of Understanding*

*Also included in Staff Report

The policy of publication of staff reports and other documents allows for the deletion of market-sensitive information.

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International Monetary Fund
Washington, D.C.

ALBANIA

April 28, 2015

FOURTH REVIEW UNDER THE EXTENDED ARRANGEMENT AND REQUEST FOR MODIFICATION AND WAIVER OF APPLICABILITY OF PERFORMANCE CRITERIA

KEY ISSUES

Background: In February 2014, the Executive Board approved a three-year Extended Arrangement with access equivalent to SDR 295.42 million (492.4 percent of quota). So far, three purchases totaling the equivalent of SDR 94.2 million have been made, and another one equivalent to SDR 28.88 million will be made available upon completion of the fourth review.

Recent Economic Developments: Economic recovery is underway, but growth remains below potential. The low oil price is expected to have a muted effect on growth and on the balance of payments, as pass-through is weak and Albania is only a small net oil exporter. High non-performing loans (NPLs) make banks risk-averse, and credit growth remains sluggish despite monetary easing.

Program Performance and Risks: The program is on track. All end-December 2014 and continuous performance criteria (PCs) and most indicative targets (ITs) were met, with comfortable margins. An exception was the IT on new domestic arrears, which was missed by a small margin; the authorities will repay the arrears by end-April and have taken other corrective measures to prevent arrears from recurring. Inflation has been slightly below the inner band prescribed under the inflation consultation clause. All but one structural benchmarks (SBs) were implemented, though two more were delayed. Delays in the appointment of a new central bank governor as well as in procurement postponed the hiring of an external expert to assist the Bank of Albania's Audit Committee from February to May 2015. Program risks emanate from external disinflationary pressures, the complexity of electricity sector reforms, and the need for sustained political commitment to fiscal adjustment. The authorities request, and staff supports, a modification of PCs for August and December 2015, and a waiver of applicability for all end-April 2015 PCs.

Policy Recommendations: The authorities should shield the 2015 budget deficit target from the risk of falling oil royalties and external disinflationary pressures. Reducing public debt over the medium term will require political commitment to sustain the significant fiscal consolidation which began in 2014. The central bank's cautious monetary easing is broadly appropriate. Addressing the high stock of NPLs is crucial for reviving credit. The micro-prudential focus on the fastest-growing segments of the banking system is appropriate. Regulatory gaps in nonbank supervision should be filled promptly. While the early results from the authorities' ambitious power sector reform have been impressive, sustaining the effort is critical.

Approved By
Masato Miyazaki and James Gordon

Discussions were held in Tirana during March 4–17, 2015. Staff team: Mr. Ilahi (head), Mr. Cabezon, Mr. Gaertner, Mr. Slavov (all EUR), Ms. Gerling (FAD), and Mr. Ismail (SPR). Mr. Reinke (Resident Representative) and Ms. Spahia (local economist) assisted the mission. Mr. Gordon (EUR) and Mr. Senatore (OED) joined some of the meetings. The mission met with the Prime Minister, the Ministers of Finance, Economy, and Energy, the Bank of Albania Governor, other senior officials and parliamentarians, and representatives of banks and the private sector. HQ support was provided by Dustin Smith and Patricia Mendoza (EUR).

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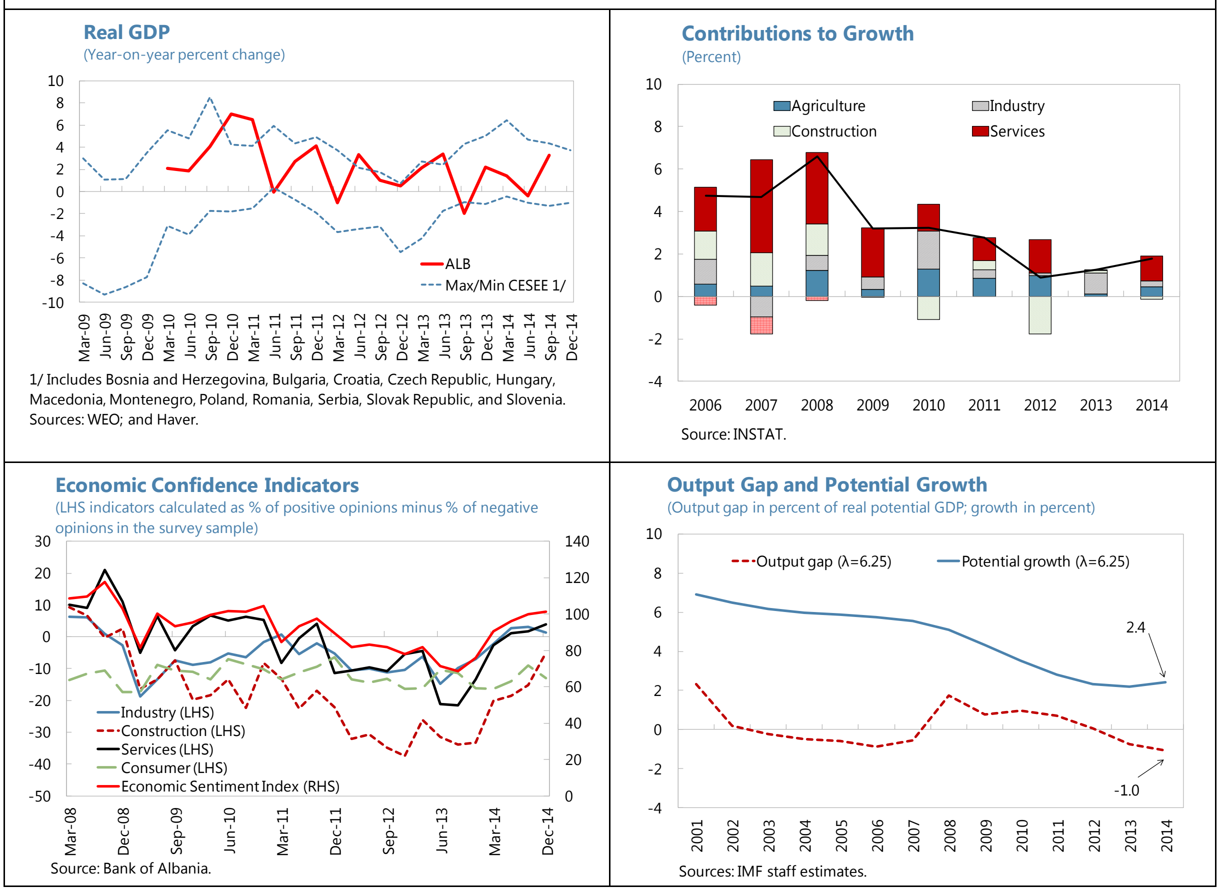
CONTEXT AND DEVELOPMENTS

1. The economic recovery is broad-based. Real GDP is estimated to have grown by 2 percent in 2014. Tourism, agriculture, and textile manufacturing have been important drivers (Figure 1 and MEFP ¶2). Confidence is improving, though growth remains below potential. The unemployment rate is high, at 18 percent (2014:Q4), but employment has increased in the past year.

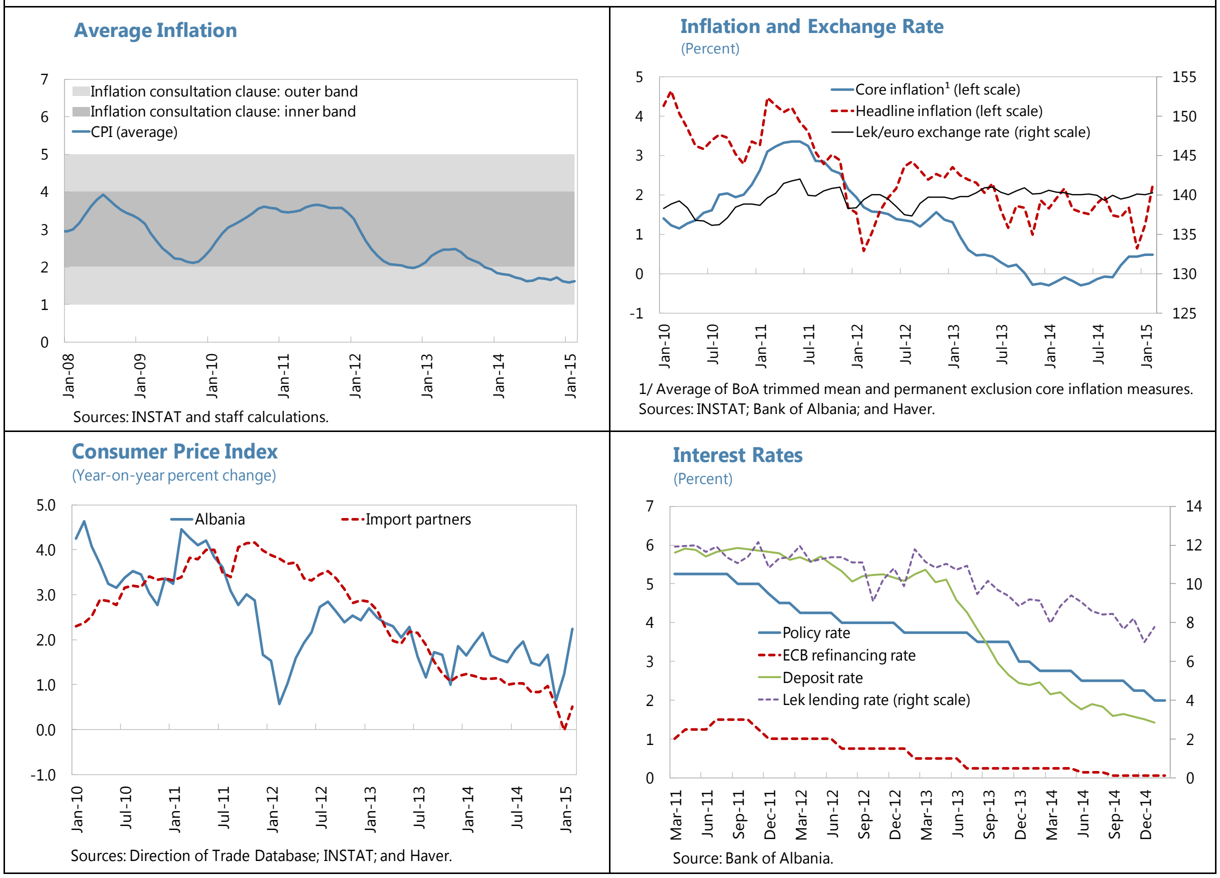
2. There has been political consensus on some key issues recently, even though the political atmosphere has been turbulent. Some recent parliamentary appointments of public officials were made with cross party consensus, despite continuing deadlock on many other issues. Local elections, scheduled for June, could affect policymaking in the period ahead.

Figure 1. Albania: Output and Growth Developments



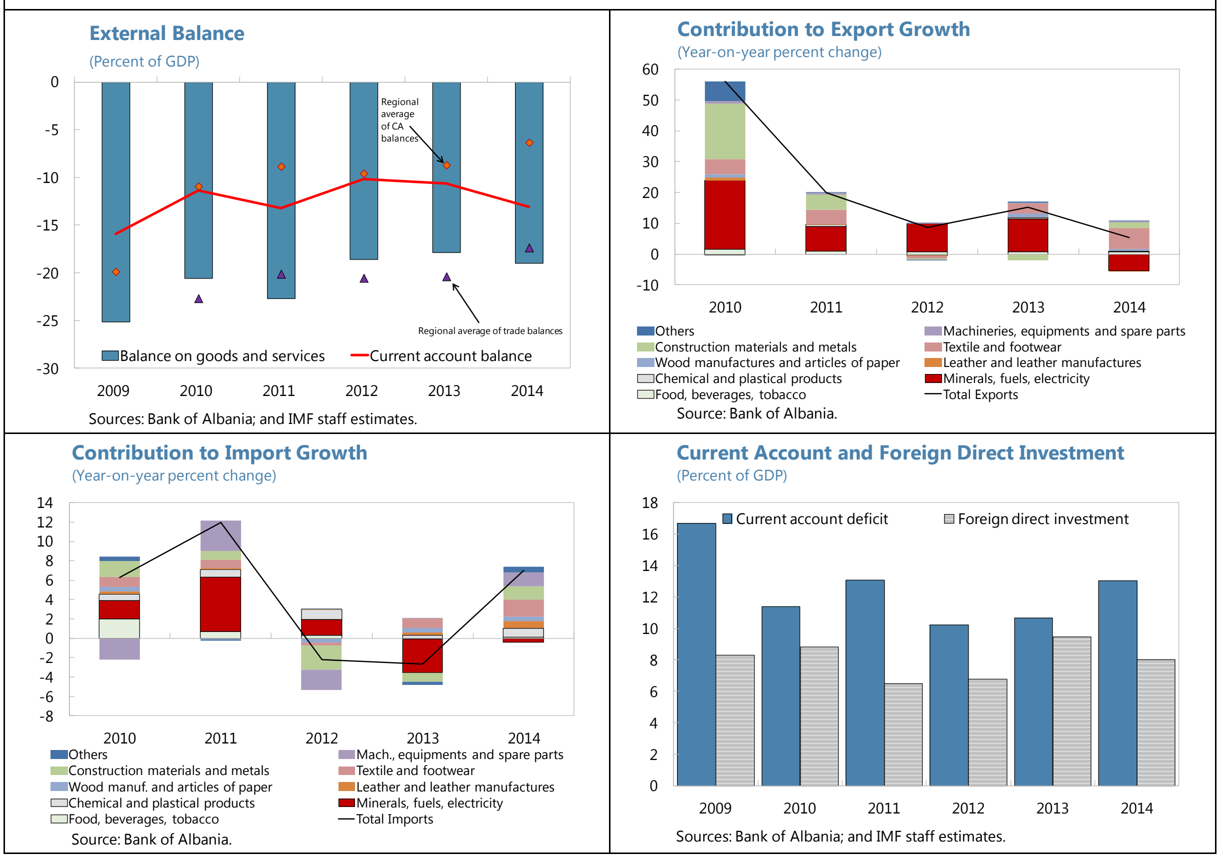
3. Inflation remains weak despite monetary easing (Figure 2 and MEFP ¶14). Average inflation declined to 1.6 percent in 2014, largely because of a strong harvest and imported disinflation. The negative output gap also exerted downward pressure on prices. Core inflation has remained positive and generally stable. Following the 75 bps cuts in 2014, the BoA lowered its policy rate by another 25 bps in January 2015, to a historic low of 2 percent. Lek lending rates and T-bill yields have been declining steadily, thus easing budget financing costs.

Figure 2. Albania: Price Developments



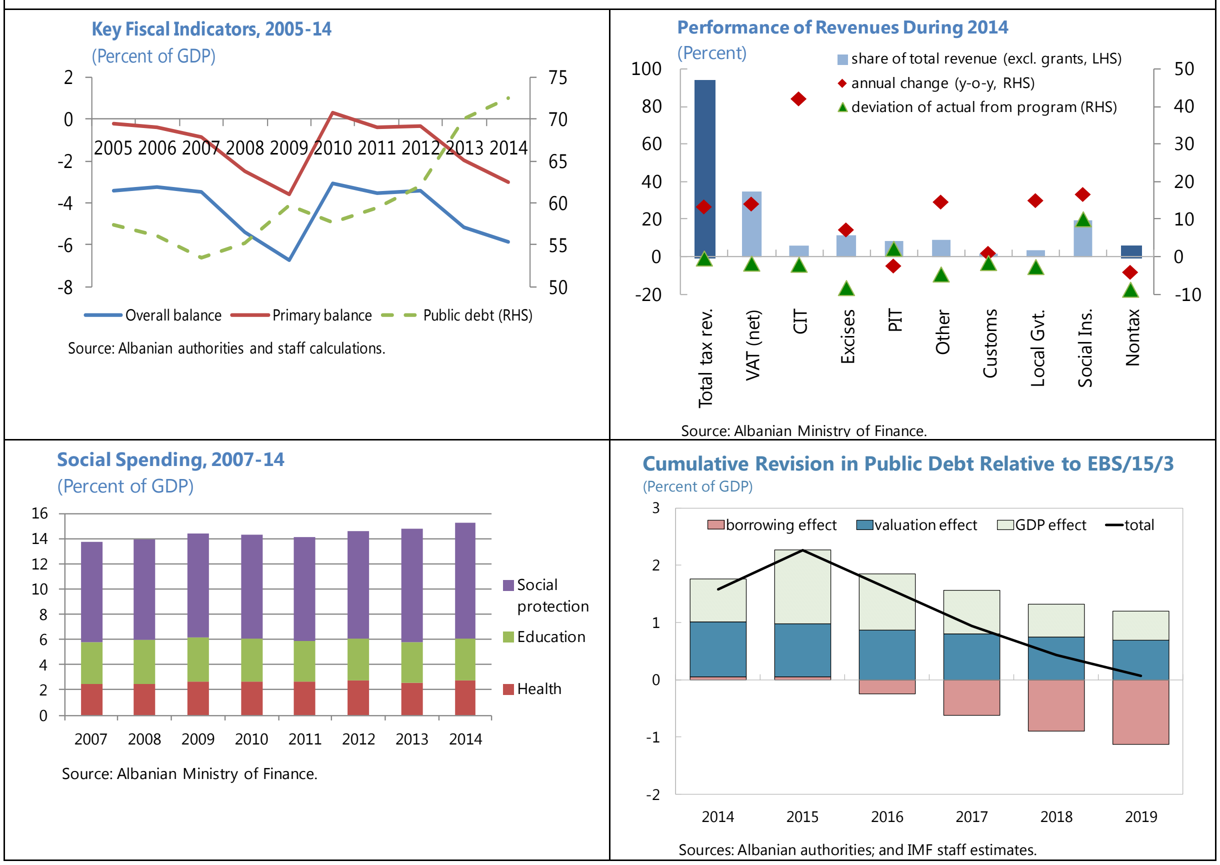
4. The external current account worsened in 2014 (Figure 3 and MEFP ¶13)**.** Non-oil exports, especially textiles and footwear, continued to grow as a share of GDP. However, the trade deficit widened with the economic recovery, and because of emergency electricity imports in H1. A continued decline in remittances, primarily those coming from the EU, added to a widening of the current account deficit. On the financing side, FDI declined following a spike in 2013 associated with hydropower privatization, and because of falling investment in the oil sector. Nevertheless, over half of the current account deficit was financed by FDI inflows, and the rest through government external financing. Reserve cover improved slightly and the euro/lek exchange rate was stable.

Figure 3. Albania: External Developments



5. The 2014 budget outturn was in line with program targets, but there were some unanticipated shifts in composition (Figure 4 and MEFP ¶7)**.** The increase in the overall deficit to 5.8 percent of GDP (from 5.2 percent in 2013) reflects rapid growth in expenditure, mainly as a result of accounting for power subsidies and policy lending to the sector (0.9 percent of GDP). An amnesty-driven surge in social insurance contributions more than compensated for minor shortfalls in other revenue categories. Lower operations and maintenance spending created space for health-related social insurance and electricity guarantees.[1] The capital expenditure outturn was 10 percent lower than envisaged in the original 2014 budget, reflecting staffing and coordination issues stemming from the intra-governmental transfer of responsibility for monitoring capital spending in early 2014. The debt-to-GDP ratio jumped to 72.6 percent of GDP at end-2014, from the 71 percent projected earlier, mainly because of valuation changes in the debt stock (arising from depreciation of lek against the dollar) and a lower-than-projected nominal GDP (from a lower deflator).

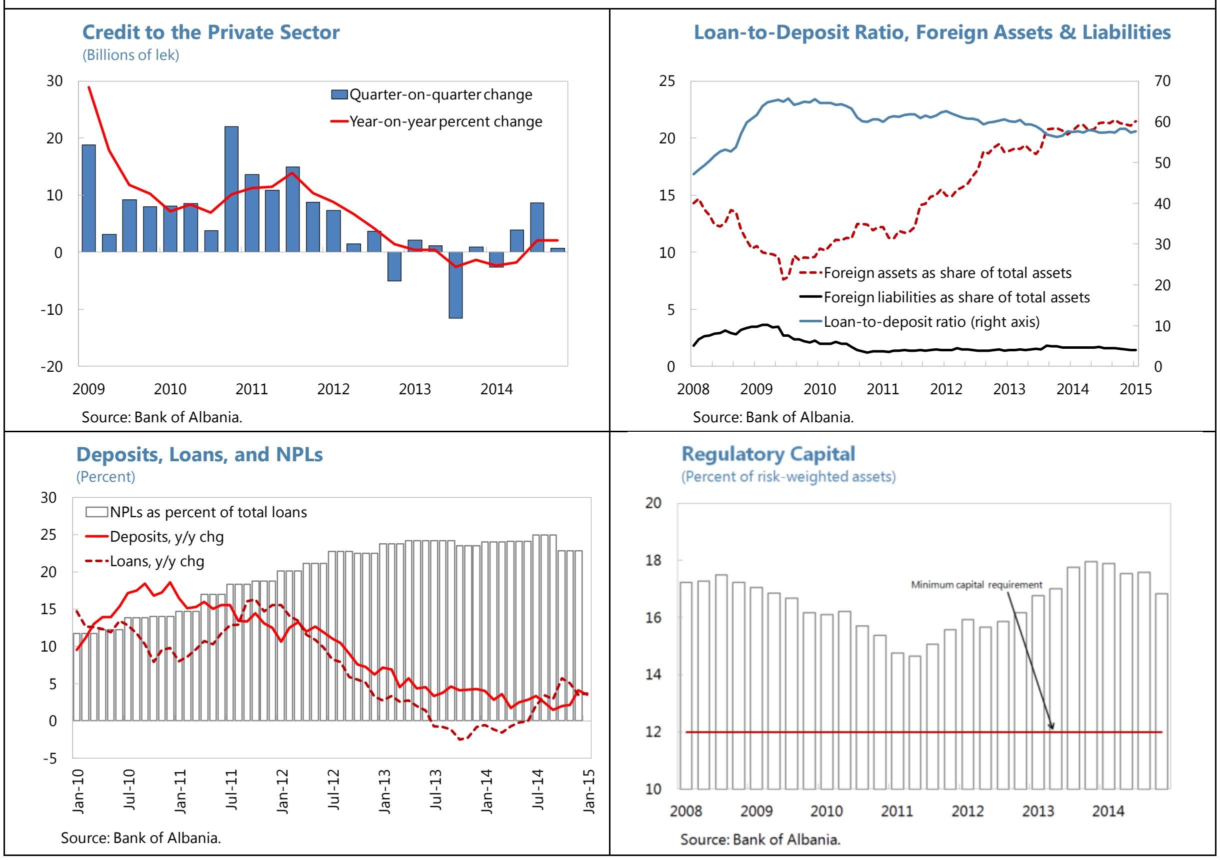
Figure 4. Albania: Fiscal Developments



[1] Overall social spending under the program rose in 2014.

6. Credit to the private sector is recovering, albeit slowly, as low asset quality makes banks cautious (Figure 5)**.** Credit growth was a moderate 2 percent in 2014, despite repeated monetary easing and ample system liquidity, with one domestic bank accounting for most of the increase. NPLs were high at end-2014, at 23 percent of total loans, but have declined slightly from their peak of 25 percent in September 2014, because of arrears clearance by the government as well as policy initiatives to tackle high NPLs. NPLs net of provisions have fallen to below 8 percent of total loans, helping mitigate financial stability risks. While capital adequacy ratios have been falling in the last year, system-wide capitalization still exceeds regulatory minima, as do liquidity buffers.

Figure 5. Albania: Financial Developments



PROGRAM PERFORMANCE

7. The program is broadly on track (MEFP ¶7-8 and MEFP Tables 1–2a)**:**

- **All end-December 2014 and continuous PCs and all but one ITs were met, with comfortable margins.** The authorities are seeking a waiver of applicability for all end-April 2015 PCs, for which data are not yet available (staff has no evidence that these PCs will not be met). The IT on the accumulation of central government domestic arrears was missed by a small margin (0.02 percent of GDP). However, the authorities will pay all accumulated arrears by end-April 2015 and have begun including a clause in new public works contracts that stipulates that accelerating project work will constitute a contract violation. Reforming the VAT refund process by moving to automatic refunds and risk-based auditing of refund claims will also help.

- **All but one SBs were implemented, though two more were delayed.** Delays in the appointment of a new central bank governor and in procurement affected the hiring of an external expert to assist BoA's Audit Committee (now expected by end-May 2015).

8. Inflation was slightly below the inner band prescribed under the inflation consultation clause (MEFP ¶4, 24)**.** Staff and the authorities concurred that the decline in inflation did not warrant policy action at this stage, apart from continuing with cautious monetary easing. Inflation is expected to rise above the lower end of the band over the medium term, as the output gap narrows and inflation in trading partners picks up. The BoA continues to refine its forward guidance to align expectations with the monetary policy objective.

POLICY DISCUSSIONS

A. Outlook and Risks

9. The near-term outlook is broadly unchanged from the combined second and third reviews:

- **Growth is expected to pick up in 2015** (MEFP ¶5)**.** Real GDP growth is expected to increase to 3 percent, driven by continued recovery in domestic demand, which is expected to offset reductions in oil output and investment and the recent damage from floods. Domestic demand will be supported by the easing of private sector liquidity constraints through continued government arrears clearance and reduction in bank risk aversion, as the government's multi-pronged efforts to tackle high NPLs begin to bear fruit. Improvements in confidence, low interest rates, and a recovery in public investment will also help support demand. The decline in retail oil prices in relation to international oil price changes has been relatively small because of high specific excise taxes, and is expected to have a positive, but somewhat muted impact on consumption (Box 1).

- **Inflation will remain modest.** With the negative output gap persisting in 2015, together with falling import prices, particularly of fuel, inflation pressures will remain contained.

Inflation is expected to get closer to BoA's 3 percent target, as domestic demand picks up.[2]

- **The current account deficit will remain elevated in 2015**. Imports will rise, from investments in large energy-related projects, such as the Trans Adriatic Pipeline and the Statkraft/Devoll hydropower projects. The underlying current account, which excludes such temporary factors, will improve somewhat (Table 3a). Reserve cover is expected to remain broadly unchanged, thanks to FDI flows and new external borrowing.

10. The medium-term outlook is generally favorable. Growth is expected to rise to 4½ percent over the medium term, underpinned by payoff from the substantial structural reforms, including those to improve the business climate, and the resulting increase in private investment. In addition, momentum should be aided by: (i) the recovery in trading partners; (ii) a pick-up in investment and production in the energy sector; and (iii) a boost in confidence as Albania advances through the EU accession process. Reserve cover is expected to remain adequate, at above four months of imports.

11. The balance of risks remains tilted downwards. While the recent oil price decline should have some positive impact on households and non-oil corporates, it could also further scale back investment and output in the sector (Box 1). A weaker recovery, combined with the electoral calendar, could test the authorities' perseverance with reforms and fiscal adjustment. Albania's public debt remains high and is subject to rollover risk (DSA). An exacerbation of the situation in Greece—home to many Albanian migrants and the location of three parents of Albanian banks—could put pressure on remittances, though the subsidiary status of Greek banks in Albania mitigates the risks. Albania's trade with Greece is now relatively small (3 percent of the total).

B. Improving Debt Dynamics and Implementing Structural Fiscal Reforms

12. To support sustainable growth and strengthen the economy's resilience to shocks the authorities reaffirmed their commitment to gradually reduce the public debt burden. (MEFP ¶9)**.** The significant drop in global oil prices has led to a downward revision of the 2014 and 2015 GDP deflator and nominal GDP—the latter is now projected to be 2 percent lower in 2015 than envisaged earlier. At the same time, a stronger dollar has pushed up the lek value of dollar-denominated public debt. The combined impact of these two exogenous shocks has been an increase in the public debt-to-GDP ratio by over 2 ppt in 2015 (Figure 4). While cognizant of the risks that excessive consolidation may have on the nascent recovery, the authorities

[2] In January, BoA's Supervisory Council removed the tolerance band of ±1 percent around the inflation target of 3 percent, largely to better anchor public expectations and improve monetary transmission. The change is not expected to have any impact on BoA's conduct of monetary policy.

reaffirmed their commitment to lowering the public debt-GDP ratio to below 60 percent by 2018, as envisaged earlier.

13. The authorities are committed to protecting the 2015 budget deficit target from the risks stemming from falling global oil prices and external disinflationary pressures (text table and MEFP ¶10)**.** To preserve the nominal budget deficit target for 2015, the lower base effect from 2014 and lower oil-related royalties (worth 0.4 percent of GDP) will be offset by a downward revision of the conservatively budgeted interest bill for 2015 and beyond. The government will also save the excess proceeds from telecom license fees (about 0.1 percent of GDP), as a buffer. Going forward, the authorities agreed in principle to start using the primary fiscal balance as the intermediate target for fiscal policy.

Fiscal Consolidation, 2012-19

(Percent of GDP, unless otherwise specified)

	(Bln leks)		(Percent of GDP)								
	2015		2012	2013	2014	2015		2016	2017	2018	2019
	EBS/ 15/3	Proj.	Act.	Act.	Act.	EBS/ 15/3	Proj.		Proj.		
Revenues	411.5	405.3	24.7	23.7	26.2	27.6	27.7	28.1	28.1	28.1	28.1
of which : Tax revenue	377.1	370.9	22.5	21.7	24.0	25.3	25.4	25.5	25.5	25.5	25.5
Expenditures	483.6	477.5	28.2	28.9	32.1	32.4	32.7	31.7	30.4	31.0	30.9
of which : Energy sector spending 1/					0.9	1.2	1.2	0.9	0.6	0.6	0.2
Current expenditure	387.2	378.2	23.6	24.1	24.9	25.9	25.9	25.5	25.3	26.0	26.1
Capital expenditure	67.9	67.9	4.6	4.8	4.3	4.5	4.6	4.6	4.6	4.6	4.6
Other spending	28.5	31.4	0.0	0.0	2.8	1.9	2.1	1.7	0.5	0.5	0.2
Unidentified measures						0.0	0.0	1.5	0.7	0.7	0.4
Unidentified measures (cumulative)						0.0	0.0	1.5	2.2	3.0	3.4
Overall balance	-72.1	-72.1	-3.4	-5.2	-5.8	-4.8	-4.9	-2.1	0.0	0.0	0.5
Overall balance excl. arrears clearance	-52.1	-52.1			-3.4	-3.5	-3.6	-1.0	0.0	0.0	0.5
Primary balance	-22.8	-28.7	-0.3	-2.0	-3.0	-1.5	-2.0	0.7	2.7	2.6	2.9
Public debt	1,056	1,068	62.0	70.1	72.6	70.8	73.0	69.1	64.1	59.4	54.5
Domestic debt			35.2	43.4	43.1	39.5	40.0	35.6	32.7	29.7	26.8
Foreign debt			26.8	26.7	29.5	31.3	33.0	33.5	31.4	29.6	27.8
Memo											
Nominal GDP (in bln leks)				1,365	1,399	1,492	1,462	1,568	1,692	1,825	1,967
Public debt (in bln leks)	1,056	1,068	828	957	1,015	1,056	1,068	1,083	1,084	1,083	1,072

Sources: Albanian authorities; IMF staff estimates and projections.

1/ Energy spending includes energy sector subsidies, compensation for the poor, and policy net lending. Prior to 2014, energy subsidies were not recorded in the fiscal accounts, but handled through extra-budgetary guarantees and debt-financed policy net lending.

14. The authorities are addressing potential risks to their baseline fiscal framework (MEFP ¶11-12)**:**

- **Fiscal support for the electricity sector.** While the authorities are off to a strong start in implementing an ambitious power sector reform, developed with World Bank help, there is considerable implementation uncertainty in the period ahead, and the sector will remain a fiscal drain over the medium term, as it is gradually weaned away from public support. Abundant rains have helped so far this year, but heavy dependence on hydropower means that rainfall variation will continue to be a fiscal risk. To mitigate risks, the authorities will take additional measures, if needed, to meet the end-year deficit target for 2015.

- **Public-Private Partnerships (PPPs).** To leverage scarce public resources, the authorities have ambitious plans to establish new PPPs. Given the substantial fiscal risks associated with such arrangements, the authorities plan to follow international best practice and to transparently account for the fiscal costs and contingent liabilities of these projects in the fiscal accounts and debt statistics. They welcome further TA from the Fund and other international partners to help assess their legal and regulatory framework.

- **Capital expenditure.** Commitments on existing investment projects continue to exceed the envelope of the authorities' medium-term budget framework (MTBF). To minimize risks from such unbudgeted commitments, the authorities plan to prioritize all outstanding infrastructure projects using transparent criteria, and with the aim of cancelling or rescheduling low-priority projects (SB). They will publish a list of all MTBF projects to signal their intention not to implement projects excluded from the list.

- **Property compensation claims.** The large number of cases filed at the European Court of Human Rights (ECHR) in Strasbourg by owners of properties expropriated under the communist regime is posing risks to the government's budget in 2015 and beyond. To tackle these, an interagency working group headed by the Deputy Prime Minister is compiling a registry of all potential cases that might end up before the ECHR, and is also working on a comprehensive and fair solution.

- **Disability benefits.** The authorities are working with the World Bank on a medium-term project to reform disability benefits in order to strengthen controls and reduce fraud. In the mean time, by end-June 2015 the Council of Ministers will issue and publish a decree that reduces disability benefits in certain cases where they have been deemed too generous. This measure is expected to yield 0.4 billion lek (0.03 percent of GDP) in estimated savings in 2015.

15. Ambitious structural fiscal reforms are also planned (MEFP ¶13–20 and MEFP Table 2b)**:**

- **Tax administration.** A new corporate strategy for the General Directorate of Taxation (GDT) has been formally endorsed by MoF. Henceforth, a dedicated Refund Unit will coordinate refund efforts nationwide, and the authorities will introduce risk-based auditing by June 2015 (SB). Improved coordination between the GDT and the General Directorate of Customs (GDC) will enhance reform efforts. Finally, the authorities are committed to introducing a valuation-based property tax by end-2017, with a fiscal cadastre to be put in place by end-2016 (SB).

- **Expenditure policy**. Pension reform approved by Parliament in July 2014 became effective in early 2015, and the stronger incentive to participate in the system has led to a surge in the number of people re-joining the scheme. A draft law that reforms the supplementary pension scheme for high government officials has been approved by the Council of Ministers and submitted to Parliament, where approval is expected by end-June 2015.

- **Public financial management**. The authorities will extend the Albanian Government Financial Information System (AGFIS) to 15 budgetary institutions by end-2015 (SB). They will also amend several laws to incorporate multi-year commitment limits by end-2015 so as to further strengthen the MTBF (SB). While these reforms will help prevent the creation of new arrears, the authorities acknowledge that complete elimination of new arrears will take time, because of capacity constraints in the government and public institutions. The authorities will, in consultation with IMF TA, take steps to shore up the credibility of their MTBF, as a prerequisite for eventually re-introducing a fiscal rule. Clearance of the pre-2014 stock of arrears will proceed concurrently with auditing and verification of payments. The authorities will strengthen further the process for evaluating, selecting, executing, and monitoring public investment projects, including by conducting a review of public investment management, and by publishing a short manual that spells out the public investment process.

C. Safeguarding Financial Stability and Unlocking Credit

16. With inflation falling below the inner band under the inflation consultation clause, monetary easing is expected to continue in the near term (MEFP ¶22–24)**.** The impact of monetary easing on credit has been generally mild because of high bank risk aversion, weak private sector balance sheets, and extensive euroization, all of which thwart the monetary transmission mechanism. The exchange rate remains fully flexible and determined entirely by market forces. The BoA is concerned that lowering the lek-euro interest rate differential below a certain level could lead to heightened exchange rate volatility, thereby aggravating financial stability risks, as about a half of foreign currency denominated loans are unhedged.

17. Continued vigilance is needed to preserve financial stability (MEFP ¶25–27)**.** Financial stability risks arising from the high NPL level are mitigated by an adequate provisioning cover. Nonetheless, BoA continues to monitor closely individual banks' resilience to risks and uses stress tests to assess capital adequacy and liquidity, with a micro-prudential focus on the fastest-growing segments of the banking system. It is also reinforcing the supervisory process by focusing on governance and internal controls, and implementing the recommendations of the 2013 FSAP on risk-based supervision and crisis preparedness.

18. The authorities are intensifying efforts to tackle the NPL problem (MEFP ¶28–29)**.** Notwithstanding significant efforts over the last three years, the NPL problem has persisted. Performance of the courts, particularly in the context of collateral execution, is a major issue. Lags in loan reclassification mean that the government's clearance of arrears has had limited immediate effects on the NPL ratio, and the full impact might take longer to materialize. Mandatory loan write-offs, which came into force in early 2015, should help. The authorities plan to take a fresh look at the problem, by forming a high-level working group to develop an overarching strategy by end-September 2015 to address the NPL issue. A deputy minister is expected to be the point person for this reform. The BoA is intensifying efforts to facilitate loan restructuring by developing recovery and resolution plans for large borrowers with problem loans. In addition, the authorities are reviewing the commercial bankruptcy framework so as to facilitate the restructuring of private balance sheets, and have requested IMF TA. Improvements in the process of foreclosing on and repossessing collateral are also needed.

19. Nonbank supervision needs strengthening (MEFP ¶30)**.** While the rapid growth of investment funds in recent years is a welcome sign of financial deepening, there is also a need to strengthen the regulatory and supervisory framework in which these funds operate. The authorities are revising the regulations on liquidity requirements and asset valuation for investment funds in line with IMF and World Bank TA. Of the two remaining vacancies on the Board of the Albanian Financial Supervisory Authority (AFSA), one was filled in March and the other one is expected to be filled by end-May 2015. This should facilitate the adoption of new regulations by end-June 2015 (SB). To minimize risks, the authorities will refrain from issuing new investment funds licenses in the interim period.

20. There has been progress in rebuilding BoA's credibility, following the events in 2014. (MEFP ¶31)**.** A new governor and internal auditor were appointed in February and April, respectively. By end-July, BoA will submit the audits for the end-September and end-December 2014 program data (SB). The BoA will also implement the recommendations of the 2014 Safeguards Assessment mission. In particular, an external expert to assist the Audit Committee will be hired in May 2015. By end-September 2015, the BoA will complete an external review of vault security and related internal controls. In addition, internal and external assessments of the internal audit function are planned for 2015. The BoA will finalize the audits in progress and develop a risk-based internal audit plan for 2015. Finally, the BoA will adopt IFRS for its 2015 financial statements.

D. Advancing Structural Reforms

21. Sustained implementation of electricity reform would gradually ease risks to public finances (MEFP ¶32-33)**.** Fiscal support to the power sector continues to pose a heavy burden on public finances; it comes in several forms, including public guarantees, policy net lending, and compensation of the poor. Once implemented, the new power sector law will restructure the relationship among the public companies responsible for electricity generation, transmission, and distribution. The law will also set in place a schedule for moving all medium-voltage customers out of the regulated tariff structure by end-2017, beginning with 35KV customers by end-2015 (SB). The authorities plan to undertake a review of their current tariff methodology, in cooperation with the World Bank, so as to make tariff adjustments more frequent and less discretionary. Targeted transfers will continue to compensate the most vulnerable social groups affected by the reform.

PROGRAM DESIGN AND RISKS

22. The authorities request, and staff supports, a waiver of applicability for all end-April PCs, as data are unavailable and there is no indication that these PCs will not be met. All PCs for end-December 2014 were met.

23. The authorities propose, and staff supports, the following modifications to program conditionality (MEFP Tables 1–2)**:**

- The revised fiscal framework, in particular the downward revision of the conservatively budgeted interest bill to protect the 2015 deficit target from risks stemming from falling oil prices, justifies tightening the government expenditure ceilings for August and December 2015, as well as the budget deficit target for August 2015. It also justifies minor revisions to the NIR floors for August and December 2015.

- The floor on net international reserves (NIR) is set at three months of import cover, based solely on reserve adequacy needs, and there is no reserve money targeting under the program. Therefore, the adjustor on NIR for shortfalls in external budget support is deemed unnecessary.

- Because of procurement delays, the deadlines for the SBs related to rolling out the AGFIS and creating a fiscal cadastre are modified from September 2015 to December 2015 and December 2016, respectively.

24. The program remains fully financed. The World Bank is providing a Policy Based Guarantee to enable the authorities to secure a commercial bank loan of €250 million around mid-2015, while the authorities have begun preparations to roll over the €300 million Eurobond that matures in November 2015. The EU has also committed a €40 million grant for balance of payments support over 2015-18, to be disbursed in four equal tranches linked to the implementation of Albania's recently adopted PFM reform strategy.

25. Albania is expected to meet repayment obligations to the Fund (Table 7)**.** By the end of the extended arrangement, Fund credit outstanding is projected to be 3.1 percent of GDP, or 14.4 percent of gross reserves. After peaking at 43 percent of GDP in 2016, external debt will decline to 38 percent of GDP by 2019, with external public debt falling from 34 to 28 percent of GDP. The current account deficit is projected to remain high over the medium term, but it is largely driven by FDI-financed import-intensive infrastructure projects, such as the Trans Adriatic Pipeline and the Statkraft/Devoll hydropower projects. When completed, these projects will increase the country's export capacity and reduce its dependence on imports. Risks to the capacity to repay are further mitigated by the authorities' strong commitment during the first year of the program, including their willingness to move ahead with difficult structural reforms, and Albania's strong record of repaying the Fund.

26. Risks to the program remain elevated. Political and social tensions could rise ahead of local elections in mid-2015 and affect implementation of the ambitious reform agenda. Savings from the electricity sector reform are subject to implementation risk, and will require sustained political commitment over the medium term. Other program risks include uncertainty about growth prospects in partner countries, further deterioration in the terms of trade from downward pressures on prices of commodity exports, higher than expected judgments by the ECHR, and a worsening in bank credit quality. Factors mitigating these risks include the prospect for EU accession which provides a catalyst for reform, as well as extensive TA by the Fund and other donors.

STAFF APPRAISAL

27. The recovery appears on track but downside risks persist and economic activity remains below potential. To significantly raise living standards and reduce macroeconomic imbalances, Albania will need sustained and high economic growth over the medium term. To boost Albania's growth potential and maintain macroeconomic stability, the authorities should persevere with their reform program, on which they have been making solid progress to date.

28. Program implementation has been strong in the first year. Program targets were broadly met, and with comfortable margins. Nevertheless, the fiscal over-performance was largely the result of significant under-execution in capital expenditure. Such unintended fiscal retrenchment undermines the recovery. The authorities should strengthen their capacity to execute public investment projects.

29. Commitment to preserving budget targets is welcome. The authorities' determination to protect their 2015 budget deficit target from the risks from falling global oil prices, external disinflationary pressures and other shocks is an important signal of their continuing commitment to restore debt sustainability. Steadfast fiscal consolidation in 2016 and beyond would help them lower public debt to below 60 percent of GDP by end-2018. The use of the primary balance as an intermediate fiscal policy target, starting with the 2016 budget, would supplement the medium-term debt anchor of the program.

30. Sustained effort is urgently needed to tackle fiscal risks. Uncertainties stem primarily from the size of property compensation claims and the large stock of unbudgeted investment projects which could lead to future arrears. Staff supports the authorities' commitment to tackle these risks and to implement ambitious reforms to improve revenue administration and public financial management.

31. Continued progress on power sector reform would also mitigate fiscal risks. The authorities' commitment to reforms is encouraging, as are the early results, but steadfast implementation will be critical, especially given the history of failed attempts. Staff welcomes the commitment to provide targeted support to the poor to compensate for tariff reform.

32. The BoA's cautious monetary easing is broadly appropriate. The central bank should maintain its policy stance as long as inflation expectations remain well-anchored and financial stability concerns from exchange rate depreciation are contained. Rebuilding BoA's credibility and safeguarding its independence are both critical for fulfilling its mandate.

33. Tackling high NPLs forcefully and comprehensively is essential for easing bank risk aversion which continues to militate against credit revival and a broader recovery. The authorities' commitment to develop an overarching strategy to address the NPL issue is welcome, but this needs to be followed up with direct and tangible actions—particularly with regard to the judicial process in dealing with collateral. BoA should also continue to closely monitor bank balance sheets to ensure banks meet capital and liquidity requirements. The BoA's microprudential focus on the fastest-growing segments of the banking system is appropriate. Staff urges the authorities to quickly fill the regulatory gaps in nonbank supervision.

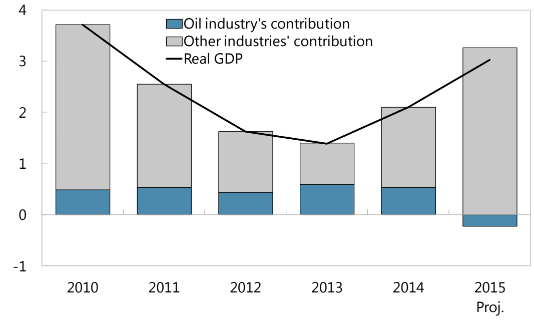
34. In light of the progress so far and the authorities' policy commitments going forward, staff supports the completion of the Fourth Review under the Extended Arrangement, as well as the modification and waiver of applicability of performance criteria.

Box 1. The Impact of Lower Oil Prices on Albania

The impact of the recent decline in the international oil price is expected to be moderate, including:

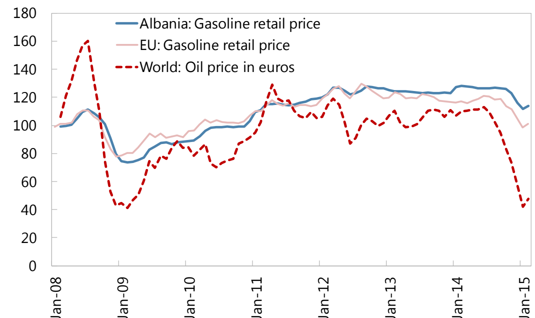
- **A modest effect on economic growth.** The oil industry's contribution to growth was about 0.5 ppt in 2010–14. Domestic crude oil production is projected to decrease in 2015 and the largest producer has halved planned investment. The negative effect on growth is expected to be partly offset by a boost to consumption and non-oil investment.
- **A moderate downward revision in inflation for 2015.** The disinflationary impact would be moderate, given the low pass-through historically and the recent hike in the excise tax on gasoline.
- **A downward revision of fiscal revenues in 2015,** reflecting the direct effects of lower oil prices on oil-related royalties. The impact on company profits and thus CIT collections would only materialize in 2016, because of reporting lag.
- **A neutral immediate impact on the current account, but potentially negative effects over the medium term.** While the exports of crude and imports of refined products have fallen largely in tandem, the decline in projected FDI to the oil sector has long-term implications for output and exports.

Albania: Real GDP Growth
(In percent)



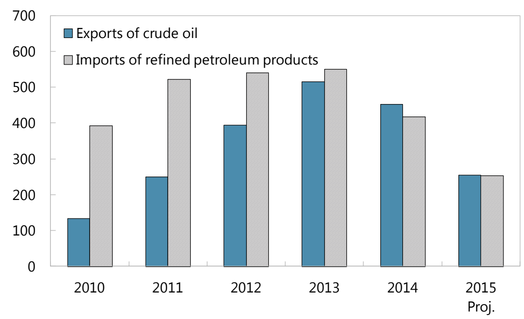
Sources: Albanian authorities; and IMF staff estimates.

World Crude Oil Price and Domestic Gasoline Prices
(Index Dec-2007=100)



Sources: Albanian authorities; and IMF staff estimates.

Albania: Trade in Crude Oil and Refined Petroleum Products
(In millions of euros)



Source: IMF staff estimates.

Table 1. Albania: Basic Indicators and Macroeconomic Framework, 2011–19

	2011	2012	2013	2014		2015		2016	2017	2018	2019
				Prog.	Proj.	Prog.	Rev. Prog.	Projections			
Real sector											
Real GDP 1/	2.5	1.6	1.4	2.1	2.1	3.0	3.0	4.0	4.5	4.5	4.5
Consumer Price Index (avg.)	3.4	2.0	1.9	1.6	1.6	2.2	2.0	2.5	2.9	3.0	3.0
Consumer Price Index (eop)	1.7	2.4	1.9	0.7	0.7	2.4	2.2	2.8	3.0	3.0	3.0
GDP deflator	2.3	1.0	0.8	1.4	0.4	2.5	1.4	3.1	3.3	3.2	3.1
Saving-investment balance											
Foreign savings	13.2	10.2	10.7	13.3	13.0	14.3	13.2	13.8	13.8	12.1	9.2
National savings	20.6	19.9	17.8	17.6	16.7	19.0	16.7	17.4	19.1	18.8	19.7
Public	1.6	0.8	-0.8	0.2	0.6	0.6	0.7	2.5	3.3	3.3	3.5
Private	19.0	19.1	18.6	17.4	16.1	18.4	16.1	14.9	15.8	15.5	16.2
Investment	33.8	30.1	28.5	30.8	29.7	33.4	29.9	31.2	32.9	30.9	28.9
Public	6.1	5.1	4.8	4.0	4.3	4.5	4.6	4.6	4.6	4.6	4.6
Private	27.7	24.9	23.7	26.9	25.4	28.8	25.2	26.6	28.3	26.3	24.3
Fiscal sector					(Percent of GDP)						
Total revenue and grants	25.4	24.7	23.7	26.0	26.2	27.6	27.7	28.1	28.1	28.1	28.1
Tax revenue	23.4	22.5	21.7	23.8	24.0	25.3	25.4	25.5	25.5	25.5	25.5
Total expenditure	28.9	28.2	28.9	31.8	32.1	32.4	32.7	31.7	30.4	31.0	30.9
Of which: Repayment of end-2013 stock of unpaid bills and arrears				2.5	2.4	1.3	1.4	1.1			
Primary	25.8	25.1	25.7	29.0	29.2	29.1	29.7	28.9	27.6	28.4	28.5
Interest	3.2	3.1	3.2	2.8	2.9	3.3	3.0	2.8	2.7	2.6	2.4
Unidentified measures (cumulative)				0.0	0.0	0.0	0.0	1.5	2.2	3.0	3.4
Overall balance	-3.5	-3.4	-5.2	-5.7	-5.8	-4.8	-4.9	-2.1	0.0	0.0	0.5
Primary balance	-0.4	-0.3	-2.0	-2.9	-3.0	-1.5	-2.0	0.7	2.7	2.6	2.9
Financing	3.5	3.4	5.2	5.7	5.8	4.8	4.9	1.2	0.0	0.0	-0.5
Of which: Domestic	2.0	2.0	4.4	2.7	3.4	0.8	0.1	-0.6	-0.3	-0.6	-0.8
Of which: Foreign	1.5	1.4	0.8	3.0	2.4	4.0	4.8	1.8	0.4	0.5	0.3
Public Debt	59.4	62.0	70.1	71.0	72.6	70.8	73.0	69.1	64.1	59.4	54.5
Domestic	33.7	35.2	43.4	42.2	43.1	39.5	40.0	35.6	32.7	29.7	26.8
Of which: Unpaid bills and arrears			5.2	2.6	2.7	1.1	1.2	0.0			
External	25.7	26.8	26.7	28.8	29.5	31.3	33.0	33.5	31.4	29.6	27.8
Monetary indicators				(Growth rate in percent, unless otherwise indicated)							
Broad money growth	9.2	5.0	2.3	3.8	4.0	5.5	4.9	7.0	7.7	7.7	7.6
Private credit growth	10.4	1.4	-1.4	3.0	2.0	5.4	5.3	6.8	7.3	7.5	7.9
Velocity (nominal GDP/broad money)	1.2	1.2	1.2	1.2	1.2	1.2	1.2	1.2	1.2	1.2	1.2
Interest rate (3-mth T-bills, end-period)	5.3	5.0	3.4	3.1	3.1	…	…	…	…	…	…
BoA repo rate (in percent)	4.8	4.0	3.0	2.3	2.3	…	…	…	…	…	…
External sector											
Trade balance (goods and services)	-22.7	-18.7	-17.9	-19.7	-19.0	-20.7	-19.0	-19.4	-19.3	-17.4	-14.4
Current account balance	-13.2	-10.2	-10.7	-14.0	-13.0	-15.2	-13.1	-13.8	-13.8	-12.1	-9.2
Gross international reserves (in billions of Euros)	1.9	2.0	2.0	2.1	2.2	2.3	2.4	2.5	2.6	2.7	2.8
(In months of imports of goods and services)	4.6	4.6	4.3	4.3	4.6	4.3	4.6	4.4	4.3	4.3	4.3
(Relative to external debt service)	7.8	6.6	6.7	6.6	6.8	3.4	3.5	5.8	5.2	4.9	4.4
(In percent of broad money)	24.8	24.5	24.6	25.2	25.7	25.4	26.6	26.0	25.2	24.3	23.5
Change in REER (eop, in percent; +=appreciation)	-0.9	-0.2	1.0	…	2.5	…	…	…	…	…	…
Memorandum items											
Nominal GDP (in billions of lek) 1/	1301	1335	1365	1414	1399	1492	1462	1568	1692	1825	1967
Output gap (percent, - = gap)	0.7	0.0	-0.7	-1.0	-1.0	-1.0	-1.1	-0.9	-0.7	-0.4	0.0

Sources: Albanian authorities; and IMF staff estimates and projections.

1/ In July 2014, INSTAT revised real GDP numbers for 2008-2012 and quarterly GVA numbers for 2013. The revisions reflect improvements in data sources and compilation methods, and closer alignment with ESA2010/SNA2008 standards. The revisions were conducted under the guidance of IMF statistical TA.

Table 2a. Albania: General Government Operations, 2011–19

(Percent of GDP)

	2011	2012	2013	2014		2015		2016	2017	2018	2019
				Prog.	Proj.	Prog.	Rev. Prog.		Projection		
Total revenue and grants	25.4	24.7	23.7	26.0	26.2	27.6	27.7	28.1	28.1	28.1	28.1
Tax revenue	23.4	22.5	21.7	23.8	24.0	25.3	25.4	25.5	25.5	25.5	25.5
VAT	9.2	8.7	7.9	8.9	8.8	9.1	9.1	9.1	9.1	9.1	9.1
Profit tax	1.5	1.3	1.1	1.5	1.5	1.6	1.6	1.6	1.6	1.6	1.6
Excise tax	3.1	2.7	2.8	3.1	2.9	3.5	3.4	3.5	3.5	3.5	3.5
Personal income tax	2.2	2.1	2.2	2.0	2.1	2.4	2.6	2.6	2.6	2.6	2.6
Customs duties	0.5	0.5	0.4	0.4	0.4	0.4	0.4	0.4	0.4	0.4	0.4
Other taxes	1.6	2.1	2.1	2.4	2.3	2.9	2.6	2.7	2.7	2.7	2.7
Local government revenue 1/	0.9	0.8	0.8	0.9	0.9	0.9	0.9	0.9	0.9	0.9	0.9
Social insurance contributions	4.4	4.3	4.4	4.5	5.0	4.6	4.7	4.7	4.7	4.7	4.7
Non-tax revenue	1.7	1.8	1.6	1.6	1.5	1.5	1.5	1.7	1.7	1.7	1.7
Grants	0.3	0.4	0.4	0.6	0.7	0.8	0.8	0.8	0.8	0.8	0.8
Total expenditure	28.9	28.2	28.9	31.8	32.1	32.4	32.7	31.7	30.4	31.0	30.9
Current expenditure	23.5	23.6	24.1	25.3	24.9	25.9	25.9	25.5	25.3	26.0	26.1
Personnel cost	5.2	5.2	5.2	5.2	5.1	5.1	5.2	5.2	5.2	5.2	5.2
Interest	3.2	3.1	3.2	2.8	2.9	3.3	3.0	2.8	2.7	2.6	2.4
Operations & maintenance	2.5	2.5	2.4	2.7	2.2	2.7	2.7	2.7	2.7	2.7	2.7
Subsidies	0.3	0.1	0.1	0.7	0.6	1.1	0.9	0.7	0.6	1.5	1.8
Energy guarantees				0.5	0.5	0.9	0.7	0.6	0.3	0.3	0.1
Nonenergy guarantees				0.0	0.0	0.1	0.1	0.0	0.2	1.1	1.6
Other				0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1
Social insurance outlays	8.8	9.0	9.4	9.6	9.9	9.6	9.8	9.8	9.8	9.8	9.8
Local government expenditure	2.2	2.0	2.2	2.6	2.4	2.5	2.5	2.5	2.5	2.5	2.5
Social protection transfers	1.4	1.5	1.7	1.7	1.8	1.6	1.7	1.7	1.7	1.7	1.7
Of which: Compensation for the poor (electricity, other)				0.0	0.0	0.1	0.1	0.1	0.1	0.1	0.1
Capital expenditure	5.4	4.6	4.8	4.0	4.3	4.5	4.6	4.6	4.6	4.6	4.6
Domestically financed	3.2	2.1	2.7	2.3	2.4	2.0	2.1	1.7	2.5	2.8	3.2
Foreign financed	2.1	2.6	2.1	1.7	1.9	2.5	2.6	2.9	2.1	1.8	1.4
Other	0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Lending minus repayment	0.0	0.0	0.0	0.0	0.4	0.2	0.4	0.3	0.2	0.2	0.0
Reserve and contingency funds 2/	0.0	0.0	0.0	0.1	0.0	0.4	0.4	0.3	0.3	0.2	0.2
Repayment of end-2013 stock of unpaid bills and arrears				2.5	2.4	1.3	1.4	1.1	0.0	0.0	0.0
Unidentified measures (cumulative)				0.0	0.0	0.0	0.0	1.5	2.2	3.0	3.4
Overall balance	-3.5	-3.4	-5.2	-5.7	-5.8	-4.8	-4.9	-2.1	0.0	0.0	0.5
Financing	3.5	3.4	5.2	5.7	5.8	4.8	4.9	1.2	0.0	0.0	-0.5
Domestic	2.0	2.0	4.4	2.7	3.4	0.8	0.1	-0.6	-0.3	-0.6	-0.8
Privatization receipts	0.0	0.1	1.2	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Net borrowing	2.2	1.9	3.4	2.7	3.2	0.8	0.1	-0.6	-0.3	-0.6	-0.8
Other	-0.2	0.0	-0.2	0.0	0.2	0.0	0.0	0.0	0.0	0.0	0.0
Foreign	1.5	1.4	0.8	3.0	2.4	4.0	4.8	1.8	0.4	0.5	0.3
Accumulation of arrears 3/	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Financing gap (+=gap) 4/				0.0	0.0	0.0	0.0	0.9	0.0	0.0	0.0
World Bank				0.0	0.0	0.0	0.0	0.7			
Residual financing (e.g., EU)				0.0	0.0	0.0	0.0	0.2			
IMF				0.0	0.0	0.0	0.0	0.0			
Memorandum Items:											
Primary balance	-0.4	-0.3	-2.0	-2.9	-3.0	-1.5	-2.0	0.7	2.7	2.6	2.9
Overall balance excl. repayment of end-2013 stock of unpaid bills and arrears				-3.3	-3.4	-3.5	-3.6	-1.0	0.0	0.0	0.5
Overall balance excl. repayment of end-2013 stock of unpaid bills and arrears, and new guarantees				-2.7	-2.9	-2.5	-2.8	-0.4	0.4	1.4	2.2
Current balance excl. grants	1.6	0.8	-0.8	0.1	0.6	0.6	0.8	3.2	4.1	4.1	4.4
Public Debt	59.4	62.0	70.1	71.0	72.6	70.8	73.0	69.1	64.1	59.4	54.5
Domestic	33.7	35.2	43.4	42.2	43.1	39.5	40.0	35.6	32.7	29.7	26.8
Of which: Unpaid bills and arrears			5.2	2.6	2.7	1.1	1.2	0.0			
External	25.7	26.8	26.7	28.8	29.5	31.3	33.0	33.5	31.4	29.6	27.8
Direct government external debt	22.6	23.9	24.4	26.8	27.4	29.5	31.2	32.0	30.0	27.5	24.3
Government guaranteed external debt	3.0	2.8	2.3	2.0	2.0	1.8	1.8	1.5	1.5	2.2	3.5
GDP (in billions of leks)	1301	1335	1365	1414	1399	1492	1462	1568	1692	1825	1967

Sources: Albanian authorities; and IMF staff estimates and projections.

1/ It includes the property tax, the simplified profit tax for small businesses, and other local taxes.
2/ Spending contingencies are reported according to their economic classification at outurn.
3/ As reflected in official data and not accounting for arrears accumulated outside of the budget prior to 2014.
4/ Following the approval of the program, Fund purchases are reported under foreign financing. Similarly, funding by the World Bank for 2014 has been been secured and is reported in foreign financing.

Table 2b. Albania: General Government Operations, 2011–19
(Billions of leks)

	2011	2012	2013	2014		2015		2016	2017	2018	2019
				Prog.	Proj.	Prog.	Rev. Prog.	Projection			
Total revenue and grants	330.4	330.4	323.7	367.9	366.7	411.5	405.3	440.0	475.0	512.4	552.1
Tax revenue	303.9	300.9	296.4	336.8	335.9	377.1	370.9	400.2	432.0	466.0	502.2
VAT	119.2	116.5	108.5	125.8	123.7	135.3	133.1	143.0	154.4	166.5	179.5
Profit tax	19.7	16.9	15.1	21.9	21.5	23.5	23.1	24.8	26.7	28.8	31.1
Excise tax	40.4	36.4	38.2	44.5	40.9	51.7	49.9	55.2	59.6	64.2	69.2
Personal income tax	28.0	28.0	29.6	28.2	28.9	35.3	38.1	40.9	44.1	47.6	51.3
Customs duties	6.9	6.1	5.8	5.9	5.9	6.2	6.1	6.5	7.0	7.6	8.2
Other taxes	21.4	28.7	28.5	34.2	32.6	42.7	38.7	42.0	45.5	49.0	52.7
Local government revenue 1/	11.8	10.9	10.8	12.8	12.4	13.5	13.1	14.1	15.2	16.4	17.7
Social insurance contributions	56.6	57.4	60.0	63.5	70.0	68.9	68.8	73.8	79.6	85.9	92.5
Non-tax revenue	22.7	24.0	21.6	22.6	20.7	22.4	22.4	27.0	29.1	31.4	33.8
Grants	3.8	5.6	5.7	8.5	10.2	12.0	12.0	12.9	13.9	15.0	16.1
Total expenditure	376.2	376.2	394.1	449.0	448.4	483.6	477.5	497.1	513.4	565.8	608.1
Current expenditure	305.6	314.6	328.6	357.0	348.1	387.2	378.2	399.4	427.7	474.0	513.8
Personnel cost	67.4	69.4	70.7	73.7	71.4	76.3	76.3	81.8	88.3	95.3	102.7
Interest	41.1	41.5	43.3	39.7	40.1	49.3	43.4	44.0	46.1	46.9	46.6
Operations & maintenance	33.0	33.5	32.4	37.5	30.8	39.7	39.7	42.5	45.9	49.5	53.4
Subsidies	3.3	1.9	1.6	9.2	8.4	16.5	13.4	11.2	10.2	26.5	35.5
Energy guarantees				7.0	6.7	13.1	10.2	8.8	4.5	4.8	1.3
Nonenergy guarantees				0.6	0.1	1.7	1.5	0.6	3.7	19.5	31.8
Other				1.6	1.6	1.8	1.8	1.9	2.0	2.2	2.4
Social insurance outlays	113.9	120.3	127.6	135.9	138.7	143.7	143.7	154.0	166.2	179.3	193.3
Local government expenditure	28.1	27.3	29.8	37.2	33.0	37.2	37.2	39.4	42.6	45.9	49.5
Social protection transfers	18.7	20.7	23.2	23.8	25.5	24.5	24.5	26.3	28.3	30.6	33.0
Of which: Compensation for the poor (electricity, other)				0.0	0.0	1.6	1.6	1.7	1.9	2.0	2.2
Capital expenditure	70.6	61.7	65.5	56.1	60.6	67.9	67.9	71.6	77.2	83.3	89.8
Domestically financed	41.1	27.4	36.7	32.0	34.0	30.1	30.1	26.0	42.2	51.0	62.6
Foreign financed	27.9	34.3	28.8	24.0	26.6	37.8	37.8	45.6	35.0	32.3	27.2
Other	1.6	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Lending minus repayment	0.0	0.0	0.0	0.0	5.9	3.0	5.9	4.0	4.0	4.0	0.0
Reserve and contingency funds 2/	0.0	0.0	0.0	0.9	0.0	5.5	5.5	4.5	4.5	4.5	4.5
Repayment of end-2013 stock of unpaid bills and arrears				35.0	33.8	20.0	20.0	17.7	0.0	0.0	0.0
Unidentified measures (cumulative)				0.0	0.0	0.0	0.0	23.8	37.8	54.1	66.6
Overall balance	-45.7	-45.9	-70.4	-81.1	-81.7	-72.1	-72.1	-33.2	-0.6	0.7	10.6
Financing	45.7	45.9	70.4	81.0	81.7	72.1	72.1	18.5	0.6	-0.7	-10.6
Domestic	26.1	26.5	59.6	38.2	47.5	11.8	1.8	-9.3	-5.6	-10.2	-16.2
Privatization receipts	0.4	1.2	16.7	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Net borrowing	28.2	24.8	46.3	38.1	45.0	11.8	1.8	-9.3	-5.6	-10.2	-16.2
Other	-2.5	0.5	-3.4	0.0	2.5	0.0	0.0	0.0	0.0	0.0	0.0
Foreign	19.7	19.4	10.8	42.9	34.3	60.3	70.3	27.8	6.2	9.4	5.6
Accumulation of arrears 3/	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Financing gap (+=gap) 4/				0.0	0.0	0.0	0.0	14.8	0.0	0.0	0.0
World Bank				0.0	0.0	0.0	0.0	11.2			
Residual financing (e.g., EU)				0.0	0.0	0.0	0.0	3.5			
IMF				0.0	0.0	0.0	0.0	0.0			
Memorandum Items:											
Primary balance	-4.6	-4.4	-27.1	-41.4	-41.7	-22.8	-28.7	10.8	45.5	47.6	57.2
Overall balance excl. repayment of end-2013 stock of unpaid bills and arrears				-46.1	-47.9	-52.1	-52.1	-15.6	-0.6	0.7	10.6
Overall balance excl. repayment of end-2013 stock of unpaid bills and arrears, and new guarantees				-38.5	-41.1	-37.4	-40.4	-6.2	7.5	25.0	43.7
Current balance excl. grants	21.0	10.2	-10.7	2.0	8.5	9.5	12.4	49.4	69.0	75.3	86.5
Public Debt	772.7	828.3	956.6	1003.7	1015.4	1055.8	1067.6	1083.1	1083.8	1083.1	1072.5
Domestic	438.8	470.6	592.7	596.9	603.2	588.7	585.0	558.0	552.5	542.3	526.2
Of which: Unpaid bills and arrears			71.5	36.5	37.7	16.5	17.7	0.0			
External	333.9	357.6	363.9	406.8	412.3	467.1	482.5	525.1	531.3	540.7	546.3
Direct government external debt	294.3	319.8	332.5	378.4	383.7	440.4	455.6	500.9	506.8	501.3	477.8
Government guaranteed external debt	39.7	37.8	31.4	28.4	28.5	26.7	26.9	24.2	24.5	39.5	68.5

Sources: Albanian authorities; and IMF staff estimates and projections.

1/ It includes the property tax, the simplified profit tax for small businesses, and other local taxes.
2/ Spending contingencies are reported according to their economic classification at outurn.
3/ As reflected in official data and not accounting for arrears accumulated outside of the budget prior to 2014.
4/ Following the approval of the program, Fund purchases are reported under foreign financing. Similarly, funding by the World Bank for 2014 has been secured and is reported in foreign financing.

Table 3a. Albania: Balance of Payments, 2011–19[1]

(Percent of GDP)

	2011	2012	2013	2014	2015	2016	2017	2018	2019
				Projection					
Current account	-13.2	-10.2	-10.7	-13.0	-13.1	-13.8	-13.8	-12.1	-9.2
Balance of goods and services	-22.7	-18.7	-17.9	-19.0	-19.0	-19.4	-19.3	-17.4	-14.4
Trade Balance (goods)	-24.2	-20.9	-17.7	-24.7	-24.8	-25.2	-25.5	-24.4	-22.3
Exports	15.2	15.9	18.1	12.4	11.1	11.5	12.0	12.4	12.9
Of which: Energy	3.2	4.2	5.6	4.5	3.1	3.4	3.6	3.7	3.8
Imports	39.4	36.8	35.7	37.0	35.9	36.8	37.5	36.8	35.1
Of which: Energy	7.4	7.9	6.5	6.2	4.3	4.5	4.5	4.3	4.2
Services (net)	1.5	2.2	-0.2	5.7	5.8	5.9	6.2	6.9	7.8
Income balance	-0.3	-0.7	0.2	-0.8	-1.0	-1.2	-1.3	-1.3	-1.2
Of which: Interest due	1.0	1.0	0.5	0.9	1.2	1.3	1.4	1.3	1.3
Current transfers	9.8	9.2	7.0	6.7	6.9	6.8	6.8	6.6	6.4
Capital and Financial account	10.3	8.1	8.6	8.9	4.4	10.0	11.7	10.3	7.5
Capital transfers	0.9	0.9	0.5	0.9	0.9	0.8	0.7	0.7	0.6
Direct investment, net	6.6	6.8	9.5	8.0	7.7	9.4	10.5	9.6	7.6
Private borrowing, net	2.6	0.5	-0.2	1.3	1.3	1.3	1.3	1.3	1.3
Government Medium- and long-term loans, net	1.6	2.1	1.1	0.5	-2.0	1.0	0.0	-0.3	-1.2
Project loans	2.2	2.8	1.8	1.7	2.4	2.5	1.6	1.3	0.7
Amortization (includes Eurobond bullet payment)	-0.6	-0.6	-0.8	-1.1	-4.3	-1.5	-1.6	-1.6	-1.9
Government Guaranteed Borrowing, net	0.0	-0.1	-0.2	-0.2	-0.1	-0.2	0.0	0.8	1.5
Disbursement	0.2	0.1	0.1	0.0	0.1	0.0	0.2	1.1	1.6
Amortization	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.3	0.1
Other flows	-1.3	-2.0	-2.1	-1.5	-3.3	-2.3	-0.9	-1.8	-2.3
Of which: Changes in commercial bank NFA	-1.0	-2.1	-2.4	-2.0	-2.1	-2.4	-2.5	-2.6	-2.5
Errors and omissions 2/	2.6	2.9	3.1	3.0	2.9	2.8	2.7	2.6	2.5
Net balance	-0.3	0.8	1.1	-1.1	-5.8	-1.0	0.6	0.8	0.8
Available financing	0.3	-0.8	-1.1	1.1	5.8	0.9	-0.6	-0.8	-0.8
Change in net reserves (increase = -) 3/	0.3	-0.8	-1.1	-1.1	-1.1	-0.9	-0.9	-0.8	-0.8
IMF (budget support)	…	…	…	0.5	1.6	1.0	0.3	0.0	0.0
World Bank (DPL)	…	…	…	1.7	0.0	0.0	0.0	0.0	0.0
World Bank (PBG)	…	…	…	0.0	2.4	0.0	0.0	0.0	0.0
Commercial loans (eurobond)	0.0	0.0	0.0	0.0	2.9	0.0	0.0	0.0	0.0
Prospective financing 4/	…	…	…	…	…	0.9	…	…	…
Expected EU Macro-Financial Assistance	…	…	…	…	…	0.2	…	…	…
IFIs (World Bank inc. PBG, EU)	…	…	…	…	…	0.7	…	…	…
Other	…	…	…	…	…	0.0	…	…	…
Memorandum items:									
Exports of Goods and Services (percent of GDP)	34.0	33.4	35.1	37.1	36.3	36.7	37.3	38.0	38.7
Imports of Goods and Services (percent of GDP)	56.8	52.1	52.9	56.1	55.3	56.1	56.6	55.4	53.2
Current Account (percent of GDP)									
excluding TAP, Statkraft related imports	-13.2	-10.2	-10.7	-13.0	-12.2	-11.8	-10.9	-9.9	-8.6
Balance of goods and services									
excluding TAP, Statkraft related imports	-22.7	-18.7	-17.9	-19.0	-18.1	-17.4	-16.4	-15.2	-13.8

Sources: Ministry of Finance; Bank of Albania; donors; and IMF staff estimates and projections.

1/ Historical data for 2011-13 reflect old BPM5 estimates which record insourcing services as goods. The data from 2014 onwards reflect BPM6 treatment of textile insourced manufacturing, which is recorded as services.

2/ Includes unidentified flows of private transfers, which are projected to decline gradually over the medium term with the decline in remittances as a share of GDP.

3/ Net of valuation changes in 2011–13. In projections for 2014–19, valuation effects are assumed to be zero.

4/ Following the approval of the program, Fund purchases are reported under available financing. Similarly, funding by the World Bank for 2014 -15 has been secured and is reported in available financing.

Table 3b. Albania: Balance of Payments, 2011–19[1]

(Millions of euros)

	2011	2012	2013	2014	2015	2016	2017	2018	2019
						Projection			
Current account	-1,225	-978	-1,036	-1,303	-1,367	-1,528	-1,643	-1,549	-1,269
Balance of goods and services	-2,107	-1,786	-1,737	-1,896	-1,979	-2,148	-2,297	-2,236	-1,996
Trade Balance (goods)	-2,242	-1,999	-1,720	-2,465	-2,584	-2,800	-3,041	-3,126	-3,075
Exports	1,406	1,526	1,756	1,238	1,153	1,280	1,432	1,598	1,776
Of which: Energy	297	407	545	450	320	377	429	481	531
Imports	3,647	3,525	3,476	3,703	3,737	4,079	4,473	4,724	4,851
Of which: Energy	682	754	631	615	446	497	531	554	575
Services (net)	135	213	-18	568	606	652	744	891	1,078
Income balance	-25	-72	21	-77	-103	-137	-157	-161	-160
Of which: Interest due	92	94	51	90	121	141	162	172	177
Current transfers	906	880	680	670	715	757	811	848	887
Capital and Financial account	954	779	838	892	459	1,110	1,393	1,324	1,035
Capital transfers	85	81	48	87	90	85	85	85	85
Direct investment, net	609	648	923	801	797	1,046	1,254	1,236	1,046
Private borrowing, net	237	48	-15	130	135	143	154	166	178
Government Medium- and long-term loans, net	152	205	105	51	-204	109	5	-40	-167
Project loans	206	268	180	165	246	275	194	168	96
Amortization (includes Eurobond bullet payment)	-54	-62	-74	-114	-450	-166	-189	-207	-264
Government Guaranteed Borrowing, net	-4	-12	-17	-22	-11	-19	2	106	206
Disbursement	16	10	5	0	13	4	26	138	225
Amortization	21	22	22	23	24	24	24	32	19
Other flows	-125	-191	-206	-155	-348	-253	-108	-228	-313
Of Which: Changes in commercial bank NFA	-90	-197	-230	-202	-220	-270	-300	-340	-350
Errors and omissions 2/	243	276	301	300	302	311	322	334	345
Net balance	-29	77	103	-111	-606	-107	72	109	112
Available financing	29	-77	-104	111	606	101	-72	-109	-112
Change in net reserves (increase = -) 3/	29	-77	-104	-109	-111	-105	-108	-109	-112
IMF (budget support)	…	…	…	54	167	107	36	0	0
World Bank (DPL)	…	…	…	166	0	0	0	0	0
World Bank (PBG)	…	…	…	…	250	…	…	…	…
Commercial loans (eurobond)	0	0	0	0	300	0	0	0	0
Prospective financing 4/	…	…	…	…	…	99	…	…	…
Expected EU Macro-Financial Assistance	…	…	…	…	…	25	…	…	…
IFIs (World Bank inc. PBG, EU)	…	…	…	…	…	74	…	…	…
Other	…	…	…	…	…	0	…	…	…
Memorandum items:									
Nominal GDP	9,261	9,573	9,728	9,995	10,400	11,091	11,925	12,836	13,816
Gross international reserves	1,913	1,972	2,015	2,192	2,362	2,462	2,562	2,662	2,762
(months of imports of goods and services)	4.6	4.6	4.3	4.6	4.6	4.4	4.3	4.3	4.3
Balance of goods and services (percent of GDP)	-22.7	-18.7	-17.9	-19.0	-19.0	-19.4	-19.3	-17.4	-14.4
Current account (percent of GDP)	-13.2	-10.2	-10.7	-13.0	-13.1	-13.8	-13.8	-12.1	-9.2
Debt service (percent of exports of goods and services) 5/	1.3	0.5	-0.1	2.9	13.0	5.2	5.1	5.2	4.9
Debt service (percent of central government revenues) 5/	1.8	0.6	-0.1	4.3	19.3	7.8	7.8	8.1	7.7
Total external debt stock (percent of GDP) 6/	34.8	35.6	34.4	36.9	41.3	42.4	40.7	39.1	37.4
Exports of Goods and Services (millions of Euros)	3,153	3,199	3,411	3,713	3,771	4,071	4,454	4,879	5,349
Imports of Goods and Services (millions of Euros)	5,260	4,985	5,149	5,609	5,750	6,219	6,751	7,115	7,345
Volume of Exports of Goods and Services (percent chang	1.7	-2.2	5.5	15.5	4.8	4.9	6.7	7.2	7.5
Volume of Imports of Goods and Services (percent chang	3.3	-7.7	4.1	10.8	4.3	7.1	7.4	4.5	2.4
Terms of trade (percent change) 7/	-0.5	1.1	1.9	-4.1	-1.4	1.9	1.4	1.3	1.2

Sources: Ministry of Finance; Bank of Albania; donors; and IMFstaff estimates and projections.

1/ Historical data for 2011-13 reflect old BPM5 estimates which record insourcing services as goods. The data from 2014 onwards reflect BPM6 treatment of textile insourced manufacturing, which is recorded as services.

2/ Includes unidentified flows of private transfers, which are projected to decline gradually over the medium term with the decline in remittances as a share of GDP.

3/ Net of valuation changes in 2011–13. In projections for 2014–19, valuation effects are assumed to be zero.

4/ Following the approval of the program, Fund purchases are reported under available financing. Similarly, funding by the World Bank for 2014-15 has been secured and is reported in available financing.

5/ Public and publicly guaranteed debt only.

6/ Public and private external debt, including arrears. Debt stock converted into Lek at the e-o-p exchange rate.

7/ Fund Staff estimates and projections.

Table 4a. Albania: Monetary Survey, 2011–16

(Billions of leks, unless otherwise indicated; end-period)

	2011	2012	2013	2014		2015		2016
				Prog.	Act.	Prog.	Rev. Prog.	
Net foreign assets	389	451	479	518	525	576	583	638
Bank of Albania	256	267	274	286	292	305	318	334
Commercial banks	133	185	205	232	233	271	265	305
Net domestic assets	681	672	670	674	670	682	671	703
Ceiling on general government guarantees								
Claims on central government, net	359	351	363	382	378	395	378	374
Bank of Albania	54	52	43	42	47	42	47	47
Commercial banks	305	299	320	340	331	353	331	326
Claims on public enterprises	19	24	25	25	27	25	26	26
Claims on the private sector	513	521	513	529	524	553	551	589
In leks	177	192	195	201	207	210	218	233
In foreign currency	336	328	318	328	317	343	334	356
Other items, net	-209	-223	-231	-262	-259	-291	-285	-286
Broad money	1,070	1,123	1,149	1,192	1,195	1,259	1,254	1,341
Currency outside banks	195	193	199	209	218	220	228	244
Deposits	875	931	950	984	977	1,038	1,025	1,097
Domestic currency	452	477	494	512	505	540	529	566
Foreign currency	423	454	456	472	473	498	496	530
Memorandum items:								
Broad money growth (% change)	9.2	5.0	2.3	3.8	4.0	5.5	4.9	7.0
Reserve money growth (% change)	2.2	2.7	3.5	3.4	8.1	5.3	5.8	5.1
Private sector credit growth (% change)	10.4	1.4	-1.4	3.1	2.0	4.5	5.3	6.8
Broad money (as percent of GDP)	82.3	84.1	84.2	84.3	85.4	84.3	85.8	85.5
Private sector credit (as percent of GDP)	39.5	39.0	37.6	37.4	37.4	37.1	37.7	37.6
Velocity (nominal GDP/broad money)	1.2	1.2	1.2	1.2	1.2	1.2	1.2	1.2
Money multiplier (absolute values)	3.7	3.8	3.7	3.7	3.6	3.7	3.6	3.6
Currency (as share of broad money)	18.2	17.2	17.3	17.5	18.2	17.5	18.2	18.2
Foreign currency deposits/total deposits	48.3	48.8	48.0	48.0	48.4	48.0	48.4	48.4
Gross reserves (millions of euros)	1,913	1,972	2,015	2,148	2,192	2,278	2,362	2,462

Sources: Bank of Albania; and IMF staff estimates.

Table 4b. Albania: Summary of Accounts of the Central Bank, 2011–16

(Billions of leks, unless otherwise indicated; end-period)

	2011	2012	2013	2014		2015		2016
				Prog.	Act.	Prog.	Rev. Prog.	
Net foreign assets	256	267	274	286	292	305	318	334
Assets	276	288	294	313	319	332	345	361
Liabilities	21	22	20	27	27	26	27	27
Net domestic assets	34	31	34	33	41	30	34	36
Ceiling on general government guarantees								
Domestic credit	81	75	66	65	75	62	68	70
Net claims on central government	54	52	43	42	47	42	47	47
Assets	64	65	65	64	64	64	64	64
Liabilities	10	13	22	22	17	22	17	17
Other credit	27	24	23	23	27	21	21	23
Private sector	2	2	2	2	2	2	2	2
Commercial banks	25	22	22	21	26	19	19	21
Other items, net (assets = +)	-47	-44	-32	-32	-34	-32	-34	-34
Reserve money	290	298	308	319	333	336	352	370
Currency in circulation	195	193	199	209	218	220	228	244
Bank reserves	95	105	109	110	115	115	124	126
Other nonbank deposits	0	0	0	0	0	0	0	0

Sources: Bank of Albania; and IMF staff estimates.

Table 5. Albania: IMF Core Indicators of Financial Soundness, 2007–14

		Dec-07	Dec-08	Dec-09	Dec-10	Dec-11	Mar-12	Jun-12	Sep-12	Dec-12	Mar-13	Jun-13	Sep-13	Dec-13	Mar-14	Jun-14	Sep-14	Dec-14
I	Capital-based																	
(i)	Regulatory capital as a percent of risk-weighted assets	17.1	17.2	16.17	15.4	15.6	15.9	15.7	15.9	16.2	16.8	17.0	17.8	18.0	17.9	17.5	17.6	16.8
(ii)	Regulatory Tier 1 capital as a percent of risk-weighted assets	16.0	16.3	15.3	14.5	14.3	14.7	14.5	14.5	14.6	15.2	15.4	14.8	14.9	14.8	14.5	14.5	13.8
(iii)	Capital as a percent of total assets																	
	Regulatory Tier 1 capital as a percent of total assets	5.8	6.7	8.7	8.6	8.1	8.3	8.0	7.9	7.9	8.2	7.9	7.7	7.7	7.6	7.5	7.6	7.4
	Regulatory capital as a percent of total assets	6.2	7.0	9.2	9.1	8.8	9.0	8.6	8.6	8.8	9.0	8.8	9.2	9.3	9.2	9.0	9.2	9.0
	Shareholders' equity as a percent of total assets	7.6	8.6	9.6	9.4	8.7	8.7	8.6	8.5	8.6	8.6	8.5	8.3	8.4	8.4	8.3	8.5	8.6
(iv)	Nonperforming loans net of provisions as a percent of capital																	
	As a percent of regulatory Tier 1 capital	12.0	27.2	29.9	38.1	56.6	58.8	60.5	64.9	61.8	62.8	62.5	54.7	48.5	50.7	49.0	53.0	46.7
	As a percent of regulatory capital	11.2	25.7	28.2	35.9	52.0	54.2	55.8	59.5	55.6	57.0	56.4	45.4	40.2	41.8	40.5	43.8	38.3
	As a percent of shareholders' equity	9.1	21.1	27.1	34.8	52.6	56.0	56.3	60.8	56.9	59.4	58.4	50.7	44.8	45.8	44.2	47.3	40.2
(v)	Return on equity (ROE) (annual basis)	20.7	11.4	4.6	7.6	0.8	8.0	4.8	4.2	3.8	5.2	2.9	-1.7	6.4	17.2	10.4	11.0	10.5
(vi)	Net open position in foreign exchange as a percent of capital																	
	As a percent of regulatory Tier 1 capital	1.8	4.5	4.1	5.3	4.3	4.3	6.5	4.5	4.1	4.0	4.5	5.2	4.9	7.8	5.9	8.3	10.4
	As a percent of regulatory capital	1.7	4.3	3.9	5.0	3.9	4.0	6.0	4.1	3.7	3.6	4.0	4.3	4.1	6.5	4.9	6.8	8.5
	As a percent of shareholders' equity	1.4	3.5	3.7	4.9	4.0	4.1	6.1	4.2	3.8	3.8	4.2	4.8	4.5	7.1	5.3	7.4	8.9
II	Asset-based																	
(vii)	Liquid assets as a percent of total assets (Liquid-asset ratio) 1/	49.8	42.8	27.6	25.9	26.5	29.0	35.9	29.0	29.4	29.4	27.4	29.2	27.6	30.9	32.7	32.4	31.9
(viii)	Liquid assets as a percent of short-term liabilities 1/	55.6	104.7	32.6	30.6	33.1	36.1	36.0	35.8	34.9	34.9	33.8	36.5	34.7	39.1	41.4	41.2	40.4
(ix)	Return on assets (ROA) (net income to average total assets, annual)	1.6	0.9	0.4	0.7	0.1	0.7	0.4	0.4	0.3	0.4	0.3	-0.1	0.5	1.5	0.9	0.9	0.9
(x)	Nonperforming loans (gross) as a percent of total loans	3.4	6.6	10.5	14.0	18.8	20.1	21.1	22.7	22.5	23.7	24.2	24.2	23.5	24.0	24.1	25.0	22.8
III	Income and expense-based																	
(xii)	Interest margin to gross income	92.7	106.5	119.6	118.9	147.7	119.7	129.5	130.6	130.4	123.6	131.2	148.3	112.6	95.4	106.0	109.6	113.1
(xiii)	Noninterest expenses to gross income	58.5	69.6	83.0	75.5	91.3	71.7	80.4	82.2	85.0	78.7	87.5	98.3	74.7	54.7	66.0	95.7	68.4
IV	Memorandum items																	
	Other (noncore) indicators:																	
	Customer deposits as a percent of total (non-interbank) loans	215.5	162.6	154.3	166.4	163.2	164.0	168.1	172.3	171.6	171.9	173.9	180.9	180.8	183.0	183.3	181.9	180.2
	Foreign currency-denominated loans to total loans	72.5	72.6	70.2	69.8	67.9	68.2	67.1	66.5	64.5	64.8	64.5	63.7	63.0	62.6	62.1	62.1	62.4
	Foreign currency-denominated liabilities as a percent of total liabilities	46.9	48.5	48.9	51.0	51.9	52.1	52.3	53.7	52.6	52.4	51.8	52.9	52.8	52.5	52.4	52.7	52.4
	Other indicators:																	
	Risk weighted assets as a percent of total assets	36.4	40.8	56.7	59.2	56.5	56.3	55.2	54.5	54.2	53.7	51.7	52.0	52.1	51.5	51.6	52.5	53.6
	Total loans as a percent of total assets	39.4	47.6	50.8	49.6	50.5	50.2	49.4	48.5	48.6	48.6	48.1	46.0	45.9	45.2	45.2	45.4	46.0
	Total loans as a percent of shareholders' equity	516.4	555.1	530.2	527.0	581.9	578.8	575.5	573.6	567.4	562.4	566.7	555.0	548.8	536.2	544.9	531.1	536.3

Source: Bank of Albania.

1/ Definitions of liquid assets and short term liabilities were changed in October 2009.

Table 6. Albania: Schedule of Reviews and Purchases[1]

Date[2]	Millions of SDR	In Percent of Quota	Conditions
February 28, 2014	23.55	39.3	Board approval of arrangement
June 30, 2014	23.55	39.3	Observance of end-March 2014 and continuous performance criteria and completion of first review
September 15, 2014	…	…	Observance of end-June 2014 and continuous performance criteria and completion of second review
February 20, 2015[3]	47.1	78.5	Observance of end-September 2014 and continuous performance criteria and completion of second and third reviews
April 15, 2015	28.88	48.1	Observance of end-December 2014 and continuous performance criteria and completion of fourth review
July 15, 2015	28.88	48.1	Observance of end-April 2015 and continuous performance criteria and completion of fifth review
November 15, 2015	28.88	48.1	Observance of end-August 2015 and continuous performance criteria and completion of sixth review
March 15, 2016	28.65	47.75	Observance of end-December 2015 and continuous performance criteria and completion of seventh review
July 15, 2016	28.65	47.75	Observance of end-April 2016 and continuous performance criteria and completion of eighth review
November 15, 2016	28.65	47.75	Observance of end-August 2016 and continuous performance criteria and completion of ninth review
February 15, 2017	28.63	47.71	Observance of end-November 2016 and continuous performance criteria and completion of tenth review
Total	**295.42**	**492.4**	

[1] Albania's IMF quota is SDR 60 million.
[2] The dates in this column reflect Board meeting dates for reviews that have passed and availability dates for reviews yet to be completed.
[3] Purchases sum the total available upon completion of the second and third reviews.

Table 7. Albania: Indicators of Capacity to Repay the Fund, 2011–19[1,2]

(Under Obligated Repurchase Schedule; in millions of SDRs)

	2011	2012	2013	2014	2015	2016	2017	2018	2019
					Projections				
Fund repurchases and charges									
In millions of SDRs	7.8	6.8	6.8	6.1	5.9	6.7	9.4	12.8	23.9
In millions of euro	9.1	8.0	7.6	7.2	7.3	8.3	11.7	15.8	29.3
In percent of gross international reserves	0.5	0.4	0.4	0.3	0.3	0.3	0.5	0.6	1.1
In percent of exports of goods and services	0.3	0.2	0.2	0.2	0.2	0.2	0.3	0.3	0.5
In percent of GDP	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.2
In percent of external public debt	0.4	0.3	0.3	0.2	0.2	0.2	0.3	0.4	0.8
In percent of quota	15.9	11.3	11.3	10.1	9.8	11.2	15.7	21.3	39.8
Fund credit outstanding (end of period)									
In millions of SDRs	29.9	23.2	16.4	57.7	187.1	270.1	296.8	291.7	277.3
In millions of euro	35.1	27.2	18.4	68.1	233.7	336.8	368.5	360.5	340.7
In percent of gross international reserves	1.9	1.4	0.9	3.2	9.9	13.7	14.4	13.5	12.3
In percent of exports of goods and services	1.1	0.9	0.5	1.8	6.2	8.3	8.3	7.4	6.4
In percent of GDP	0.4	0.3	0.2	0.7	2.2	3.0	3.1	2.8	2.5
In percent of external public debt	1.4	1.0	0.7	2.4	6.9	9.1	9.8	9.5	8.8
In percent of quota	61.4	38.7	27.3	96.1	311.8	450.2	494.6	486.2	462.2
Memorandum items:									
Gross international reserves	1598	1691	1803	1830	1891	1974	2063	2154	2248
Exports of goods and services	2688	2727	3039	3142	3019	3265	3587	3949	4354
GDP	7894	8163	8666	8459	8325	8896	9605	10388	11245
External public debt	2079	2233	2351	2445	2718	2966	3014	3087	3156
Quota	48.7	60.0	60.0	60.0	60.0	60.0	60.0	60.0	60.0

Source: Fund staff estimates.

1/ Projections are based on current interest rates for PRGF and the EFF.
2/ End-of-year value.

Annex I. Debt Sustainability Analysis (DSA)

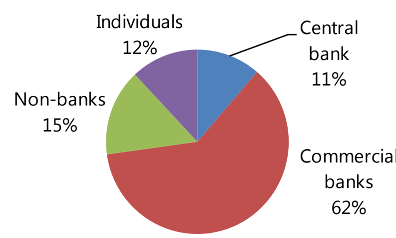
Albania's public debt remains high and subject to a variety of risks, most notably rollover risks and exposure to shocks. In 2014, the authorities embarked on a fiscal adjustment path that has slowed down the pace of debt accumulation, with the public debt-to-GDP ratio expected to begin declining in 2016. Over the medium term, continued substantial fiscal consolidation is crucial to put debt on a downward trajectory and mitigate risks to debt sustainability.

Background

1. Albania's public debt-to-GDP ratio stood at 72.6 percent as of end-2014. Of the total, most public debt–defined as general government gross debt–remains domestic (59 percent), medium- to long-term (72 percent), denominated in domestic currency (55 percent) and in the hands of domestic creditors (61 percent). Public debt includes guaranteed debt (5 percent), outstanding domestic arrears and unpaid bills (4 percent), as well as a negligible share of local government debt (0.08 percent). Commercial banks remain the main holder of domestic debt (62 percent), although nonbanks have quintupled their share over the past four years. The share of external debt owed to multilateral creditors has further increased (to about 60 percent), at the expense of a declining share owed to official bilateral (21 percent) and private creditors (19 percent).

Domestic Public Debt By Holder

(2014, Percent of Total)



2. The sharp increase in debt in recent years slowed down substantially in 2014, despite the fact that public support to the electricity sector was incorporated in public debt statistics. Fast rising debt led to the breach and ultimate removal of the authorities' 60 percent of GDP debt ceiling in 2012. In 2013, a widening fiscal deficit and the recognition of a stock of domestic arrears and unpaid bills of about 5.2 percent of GDP led to an increase of the debt-to-GDP ratio by another 8 percentage points. Despite embarking on an ambitious reform for the electricity sector which includes incorporating public support to the sector in the public debt statistics, the authorities managed to slow down debt accumulation to 2½ percentage points in 2014.

3. Following the guidelines on public DSAs in market access countries, Albania is considered a high-scrutiny case. In particular, Albania meets the following criteria: i) current (and projected) public debt exceeding 50 percent of GDP; and ii) gross financing needs exceeding 10percent of GDP.

4. The macroeconomic assumptions underpinning the DSA are in line with the updated macroeconomic adjustment program. The medium term will see a gradual recovery of real growth to about 4.5 percent, supported by a solid implementation of structural reforms, rebounding confidence, and higher private investment flows. Inflation expectations will remain anchored, keeping inflation close to the central bank's 3 percent target. Building on the fiscal consolidation achieved in 2014, fiscal adjustment is expected to continue as programmed and lead to a reduction in the public debt-to-GDP level starting in 2016 and to a positive overall balance from 2019 onwards. The stock of domestic unpaid bills and arrears recognized at end-2013 is expected to be paid off by end-2016. The share of external financing will increase, mainly reflecting policy efforts to shift from short-term domestic to long-term external sources, including through increased financing from the IMF and the World Bank.[1]

5. The current account deficit is expected to decline gradually, as higher investment widens the export base and fiscal consolidation squeezes import demand.

Public DSA Results

A. Baseline

6. Under the baseline scenario, Albania's public debt will decline gradually over the medium term, albeit remaining at elevated levels. The authorities remain committed to further slowing down debt accumulation to reach 73 percent of GDP in 2015 and to subsequently begin lowering the debt burden with the aim of bringing it below 60 percent of GDP by end-2018. Even at this level, debt would continue to pose significant risks because of i) high rollover needs; ii) rising interest rates; iii) the large exposure of the domestic financial sector; and iv) vulnerability to growth and terms of trade shocks. Debt reduction is expected to remain the key fiscal objective over the medium term.

7. Public debt under the baseline scenario is susceptible to a range of risks, arising from the composition of the financing profile and the projected pace of fiscal adjustment.

- *Risks from the composition of the financing profile*. Although the authorities have started lengthening the maturity profile and increasing the external share of public debt, about half of central government domestic direct debt was short-term at end-2014. It will decline only gradually over time, with rollover risks persisting in the near term. At the same time, public gross financing needs in 2015 will remain elevated above the 15 percent of GDP early-warning benchmark associated with past debt crises. These are projected to substantially decline afterwards. While the creditor base is currently weighted heavily toward banks, there is expected to be further diversification towards nonbank institutions (e.g., domestic investment funds) over the medium term. On the other hand, interest rate risk is increasing with the lengthening of maturities, but is mitigated somewhat by the lack of a secondary market. Finally, exchange rate risk has been rising with foreign currency debt expanding over the medium term, but is mitigated by Albania's comfortable level of reserves.

[1] The IMF program will continue to provide financing until 2017. Moreover, the World Bank will provide a Policy Based Guarantee (PBG) to enable the authorities to secure a commercial bank loan of €250 million around mid-2015. The authorities have also begun preparations to roll over the €300 million Eurobond that matures in November 2015.

- *Risks from a slower-than-projected fiscal adjustment*. Two alternative standardized scenarios—one based on extending historical performance[2] and the other one on maintaining a constant primary balance regime[3]—suggest that reducing public debt below 60 percent of GDP by 2018 would require persistence with fiscal adjustment. Indeed, by 2020, public debt would continue to grow above 80 percent of GDP under the historical scenario and slowly decline to 65 percent of GDP by 2018 under the constant primary balance scenario.

8. The baseline scenario represents the most realistic outlook, reflecting recent policy performance and other countries' experience.

- *Limited validity of the historical and constant primary balance scenarios*. The historical performance of the past 10 years is not representative of the current policy environment. The new government that took office in 2013 has broken with the past, when high growth and easy financing conditions led to pro-cyclical fiscal policy which, in turn, fueled the accumulation of public debt and unacknowledged domestic arrears. Instead, the new government successfully embarked on fiscal consolidation in 2014 and accompanying reforms, including of fiscal institutions. Given significant risks for macroeconomic stability as well as largely untested financing constraints, the authorities remain committed to reducing the public debt burden by improving the primary balance over the medium term.
- *Other countries' experience*. Relative to other countries, the track record of projecting macroeconomic variables (especially growth, primary balance, and inflation) does not reveal a systematic one-sided bias. The forecast errors are broadly within the interquartile range and the planned fiscal adjustment effort is broadly typical of other countries' adjustment experiences.

B. Stress Tests

9. Both, macroeconomic and fiscal shocks can significantly increase public debt and gross financing needs relative to the baseline throughout the projection period. Among all stress test scenarios,[4] Albania shows the highest vulnerability to a combined macro–fiscal shock. It would lead to a further increase in the debt-to-GDP ratio to 73.1 percent in 2016, followed by a gradual decline to just below 59 percent by 2020. Gross financing needs would be permanently higher relative to

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[2] Under the historical scenario, real GDP growth, the primary balance, and real interest rates are set at their historical average of the past 10 years while other variables are the same as in the baseline.

[3] Under the constant primary balance scenario, the primary balance remains unchanged compared to the first projection year (in percent of GDP), while all other variables are the same as in the baseline.

[4] Stress tests include shocks to macro variables (i.e., real interest rate, real GDP growth, real exchange rate), fiscal variables (i.e., primary balance), and a combination of macro and fiscal variables which incorporates the largest effect of individual shocks on all variables.

the baseline (e.g., by almost 4 percentage points of GDP in 2020). The second worst case scenario would be a growth shock (i.e., a reduction in real GDP growth by one standard deviation for two consecutive years). This would lead to an increase in the debt-to-GDP ratio to 71.2 percent by 2016, followed by a gradual decline to about 55 percent by 2020.

10. Fan charts further illustrate the possible evolution of debt over the medium term based on simulating a large number of shocks to macroeconomic variables.[5] These simulations suggest that under a symmetric distribution, the debt stock could range between 43 and 58 percent of GDP by 2020. However, under a restricted distribution (which precludes a positive shock to the primary balance), debt could increase up to 62 percent of GDP by 2020 relative to the baseline scenario of just below 50 percent.

External Debt Sustainability

11. External debt is projected to rise gradually over the medium-term, as public debt composition shifts from short-term domestic to long-term external sources. Public external borrowing will drive external debt to peak near 43 percent of GDP in 2016 before gradually declining to 38 percent by 2019. During this period, private external borrowing is expected to remain relatively contained at 1½ percent of GDP, with the bulk of private foreign financing coming through foreign direct investment, including for large projects such as the Trans-Adriatic Pipeline and the Statkraft/Devoll Hydropower project.

12. Stress tests show that external debt dynamics can significantly worsen in the event of shocks to the real exchange rate and the current account. Under a 30 percent depreciation shock, external debt would peak at 53 percent of GDP in 2016 before declining to 47 percent by 2019. While the lek has depreciated against the U.S. dollar over the last year, tracking movements in the euro, this has had a small impact on external debt which is mainly denominated in euros and SDRs. However, the real effective exchange rate has been relatively stable over the last several years. Under a shock to the current account by half a standard deviation (around 1.7 percent of GDP), external debt would peak at 46 percent of GDP by 2016 and remain near that level.

Conclusion

13. Despite the significant fiscal adjustment in 2014, Albania's debt remains high and poses significant risks. As highlighted in red in the standardized heat map, shocks related to growth, the primary balance, interest rates, and the exchange rate push Albania's debt and gross financing needs above relevant benchmarks, providing early warning signs of emerging risks. Specifically, both under the baseline and various shock scenarios, Albania's debt exceeds the 70 percent of GDP benchmark and gross financing needs exceed the 15 percent of GDP benchmark. Finally, changes in the debt profile pose moderate risks (yellow in the heat map), with the exception

[5] Fan charts show a spectrum of possible outcomes for the level of debt based on a probabilistic view of uncertainty around the baseline.

of external financing requirements which pose a high risk (red) and changes in short term debt which pose low risks (green).

14. Addressing the risks associated with high debt remains critical for Albania's macroeconomic stability. High debt is associated with lower growth and may thwart the recovery. High debt also means higher vulnerability to shocks. Even stabilizing debt at high levels requires large primary surpluses for many years which may be politically difficult to sustain. Finally, high debt is associated with high rollover requirements which increase vulnerability to sudden shifts in market perceptions.

Albania Public Sector Debt Sustainability Analysis (DSA) - Baseline Scenario

(in percent of GDP unless otherwise indicated)

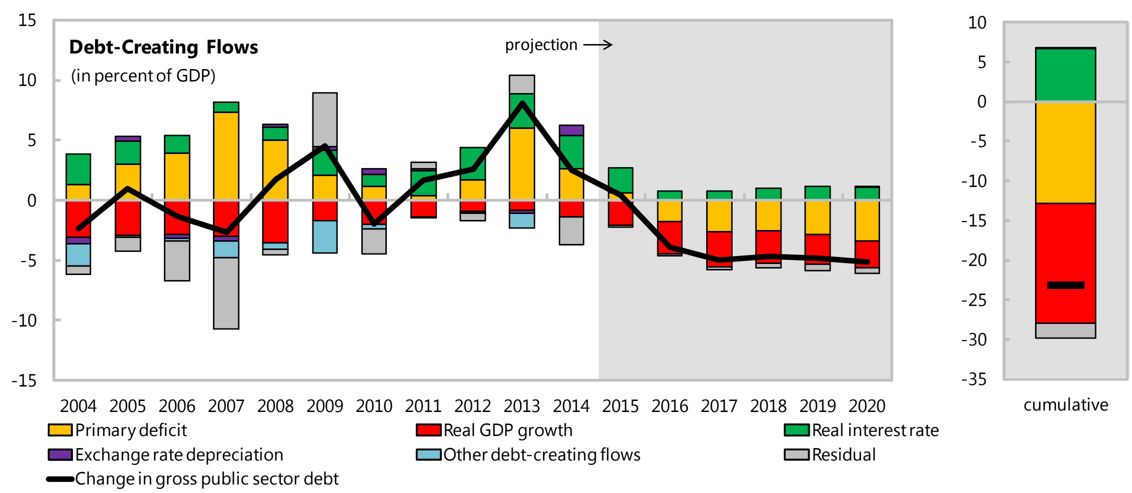
Debt, Economic and Market Indicators [1/]

	Actual			Projections					
	2004-2012 [2/]	2013	2014	2015	2016	2017	2018	2019	2020
Nominal gross public debt	57.5	70.1	72.6	73.0	69.1	64.1	59.4	54.5	49.4
Of which: guarantees	3.3	3.8	3.9	3.7	3.5	3.2	3.0	2.8	2.6
Public gross financing needs	48.6	39.9	36.6	31.4	16.5	16.5	14.6	14.6	14.4
Real GDP growth (in percent)	4.6	1.4	2.1	3.0	4.0	4.5	4.5	4.5	4.5
Inflation (GDP deflator, in percent)	2.8	0.8	0.4	1.4	3.1	3.3	3.2	3.1	3.1
Nominal GDP growth (in percent)	7.6	2.2	2.5	4.5	7.2	7.9	7.9	7.8	7.7
Effective interest rate (in percent) [4/]	6.2	5.6	4.4	4.5	4.3	4.6	5.0	5.3	5.3

As of January 20, 2015		
Sovereign Spreads		
Spread (bp) 3/		185
5Y CDS (bp)		n.a.
Ratings	Foreign	Local
Moody's	B1	B1
S&Ps	B	B
Fitch	n.a.	n.a.

Contribution to Changes in Public Debt

	Actual			Projections							
	2004-2012	2013	2014	2015	2016	2017	2018	2019	2020	cumulative	debt-stabilizing primary balance [9/]
Change in gross public sector debt	0.4	8.1	2.5	0.4	-3.9	-5.0	-4.7	-4.8	-5.1	-23.2	
Identified debt-creating flows	1.4	6.6	4.8	0.6	-3.8	-4.8	-4.3	-4.3	-4.7	-21.3	
Primary deficit 5/	2.9	6.0	2.6	0.6	-1.8	-2.7	-2.6	-2.9	-3.4	-12.8	-1.2
Primary (noninterest) revenue and gra	25.6	23.7	26.2	26.9	29.0	30.6	30.6	31.0	31.5	179.6	
Primary (noninterest) expenditure 5/	28.4	29.7	28.8	27.5	27.2	27.9	28.0	28.1	28.1	166.7	
Automatic debt dynamics [6/]	-0.6	1.8	2.2	0.0	-2.0	-2.1	-1.7	-1.4	-1.2	-8.4	
Interest rate/growth differential [7/]	-0.7	2.1	1.3	0.0	-2.0	-2.1	-1.7	-1.4	-1.2	-8.4	
Of which: real interest rate	1.8	2.9	2.7	2.1	0.8	0.8	0.9	1.1	1.0	6.7	
Of which: real GDP growth	-2.4	-0.8	-1.4	-2.1	-2.7	-2.9	-2.7	-2.5	-2.3	-15.1	
Exchange rate depreciation [8/]	0.0	-0.3	0.9	…	…	…	…	…	…	…	
Other identified debt-creating flows	-0.8	-1.2	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Net privatization proceeds (negative)	-0.8	-1.2	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Contingent liabilities	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
(Specify)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Residual, including arrears changes [9/]	-1.1	1.5	-2.3	-0.1	-0.1	-0.2	-0.4	-0.5	-0.5	-1.9	



Source: IMF staff.

1/ Public sector is defined as general government and includes public guarantees, defined as domestic and external guarantees for the energy and non-energy sector.

2/ Based on available data.

3/ Bond Spread over German Bonds.

4/ Defined as interest payments divided by debt stock (excluding guarantees) at the end of previous year.

5/ The DSA includes unallocated measures in revenues and expenditures, but excludes domestic arrears clearance from expenditures (which are included in domestic debt amortization).

6/ Derived as [(r - π(1+g) - g + ae(1+r)]/(1+g+π+gπ)) times previous period debt ratio, with r = interest rate; π = growth rate of GDP deflator; g = real GDP growth rate; a = share of foreign-currency denominated debt; and e = nominal exchange rate depreciation (measured by increase in local currency value of U.S. dollar).

7/ The real interest rate contribution is derived from the numerator in footnote 6 as r - π (1+g) and the real growth contribution as -g.

8/ The exchange rate contribution is derived from the numerator in footnote 6 as ae(1+r).

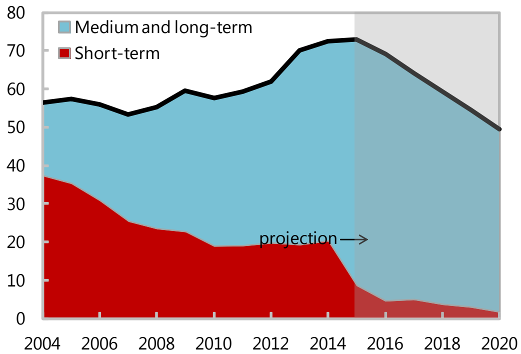
9/ Includes changes in the stock of arrears, guarantees, asset changes, and interest revenues (if any). For projections, includes exchange rate changes during the projection period.

10/ Assumes that key variables (real GDP growth, real interest rate, and other identified debt-creating flows) remain at the level of the last projection year.

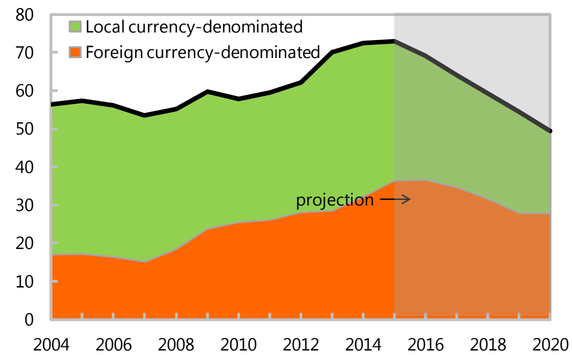
Albania Public DSA - Composition of Public Debt and Alternative Scenarios

Composition of Public Debt

By Maturity
(in percent of GDP)



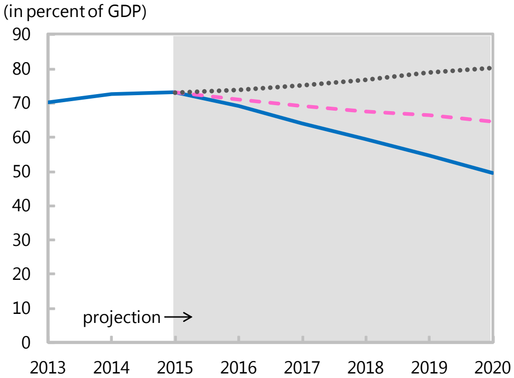
By Currency
(in percent of GDP)



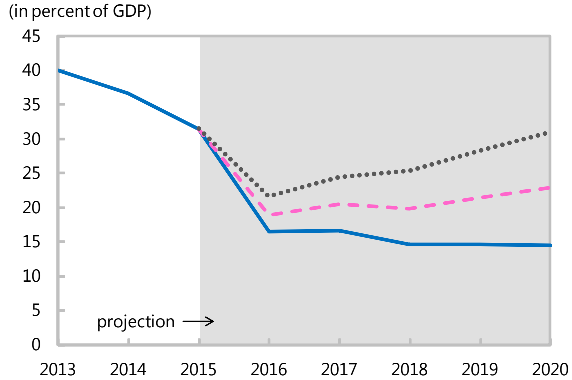
Alternative Scenarios

Baseline   Historical   Constant Primary Balance

Gross Nominal Public Debt
(in percent of GDP)



Public Gross Financing Needs
(in percent of GDP)



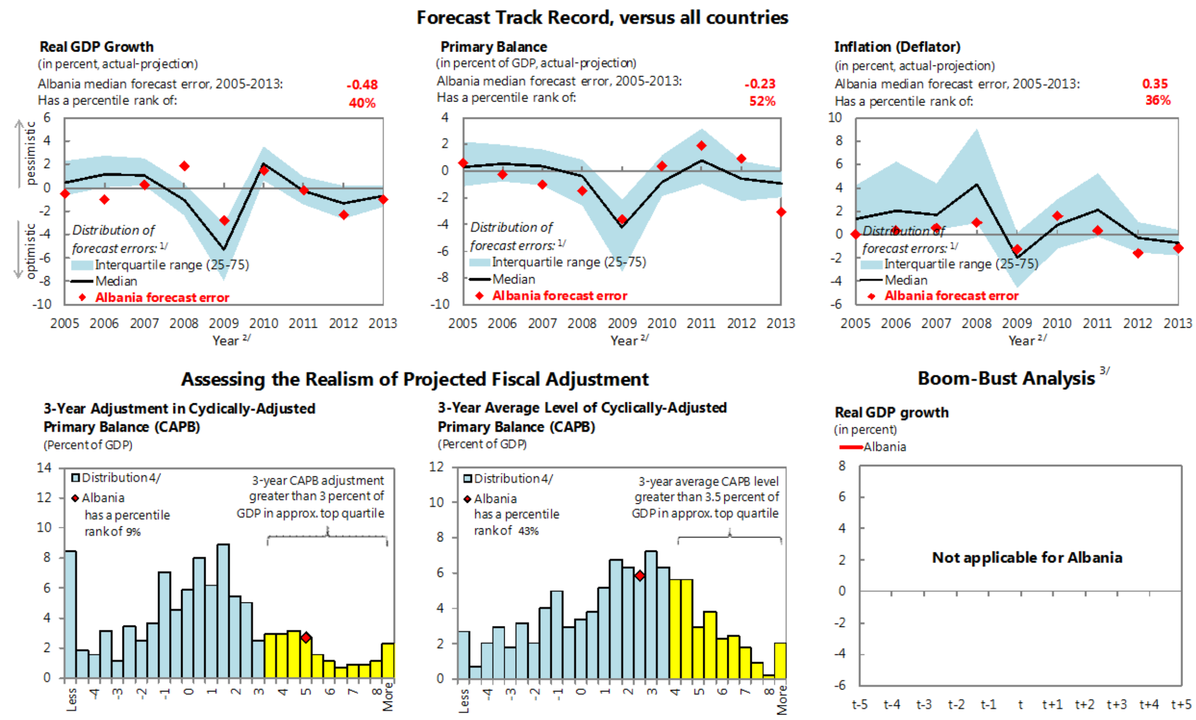
Underlying Assumptions
(in percent)

Baseline Scenario	2015	2016	2017	2018	2019	2020
Real GDP growth	3.0	4.0	4.5	4.5	4.5	4.5
Inflation	1.4	3.1	3.3	3.2	3.1	3.1
Primary Balance	-0.6	1.8	2.7	2.6	2.9	3.4
Effective interest rate	4.5	4.3	4.6	5.0	5.3	5.3
Constant Primary Balance Scenario						
Real GDP growth	3.0	4.0	4.5	4.5	4.5	4.5
Inflation	1.4	3.1	3.3	3.2	3.1	3.1
Primary Balance	-0.6	-0.6	-0.6	-0.6	-0.6	-0.6
Effective interest rate	4.5	4.3	4.6	4.9	5.3	5.3

Historical Scenario	2015	2016	2017	2018	2019	2020
Real GDP growth	3.0	3.9	3.9	3.9	3.9	3.9
Inflation	1.4	3.1	3.3	3.2	3.1	3.1
Primary Balance	-0.6	-3.3	-3.3	-3.3	-3.3	-3.3
Effective interest rate	4.5	4.3	5.0	5.6	6.1	6.3

Source: IMF staff.

Albania Public DSA – Realism of Baseline Assumptions



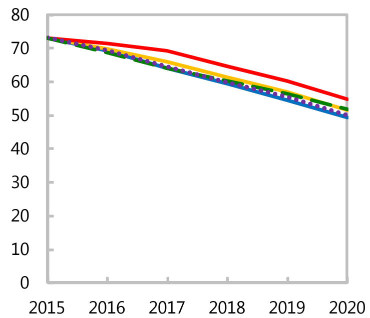
Source : IMF Staff.
1/ Plotted distribution includes all countries, percentile rank refers to all countries.
2/ Projections made in the spring WEO vintage of the preceding year.
3/ Not applicable for Albania, as it meets neither the positive output gap criterion nor the private credit growth criterion.
4/ Data cover annual obervations from 1990 to 2011 for advanced and emerging economies with debt greater than 60 percent of GDP. Percent of sample on vertical axis.

Albania Public DSA - Stress Tests

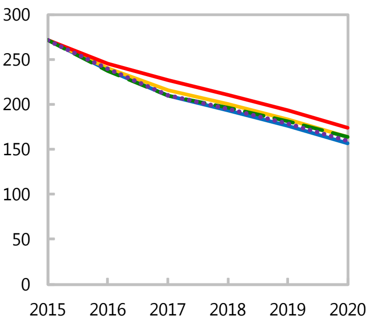
Macro-Fiscal Stress Tests

Baseline — Real GDP Growth Shock — Primary Balance Shock — Real Exchange Rate Shock — Real Interest Rate Shock

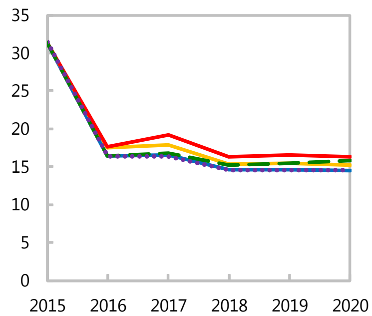
Gross Nominal Public Debt
(in percent of GDP)



Gross Nominal Public Debt
(in percent of Revenue)



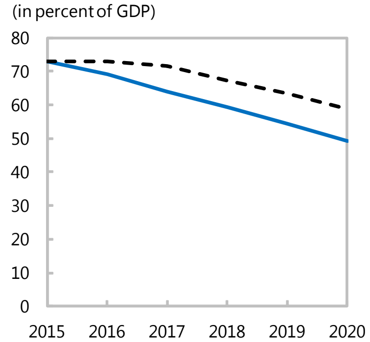
Public Gross Financing Needs
(in percent of GDP)



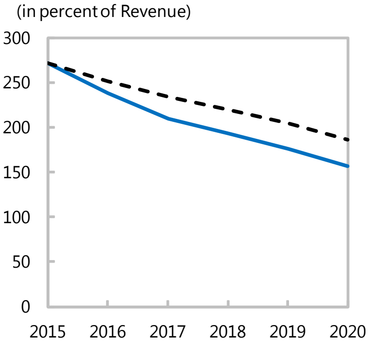
Additional Stress Tests

Baseline — Combined Macro-Fiscal Shock

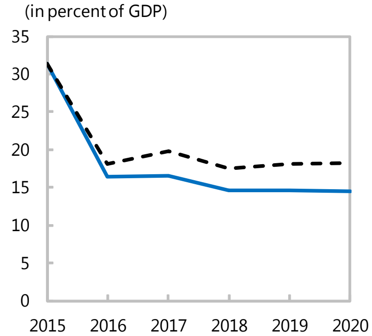
Gross Nominal Public Debt
(in percent of GDP)



Gross Nominal Public Debt
(in percent of Revenue)



Public Gross Financing Needs
(in percent of GDP)



Underlying Assumptions
(in percent)

Primary Balance Shock	2015	2016	2017	2018	2019	2020
Real GDP growth	3.0	4.0	4.5	4.5	4.5	4.5
Inflation	1.4	3.1	3.3	3.2	3.1	3.1
Primary balance	-0.6	0.7	1.6	2.6	2.9	3.4
Effective interest rate	4.5	4.3	4.7	5.1	5.3	5.3
Real Interest Rate Shock						
Real GDP growth	3.0	4.0	4.5	4.5	4.5	4.5
Inflation	1.4	3.1	3.3	3.2	3.1	3.1
Primary balance	-0.6	1.8	2.7	2.6	2.9	3.4
Effective interest rate	4.5	4.3	5.2	6.0	6.6	6.8
Combined Shock						
Real GDP growth	3.0	1.9	2.4	4.5	4.5	4.5
Inflation	1.4	2.6	2.7	3.2	3.1	3.1
Primary balance	-0.6	0.7	1.2	2.6	2.9	3.4
Effective interest rate	4.5	4.4	5.2	6.0	6.6	6.8

Real GDP Growth Shock	2015	2016	2017	2018	2019	2020
Real GDP growth	3.0	1.9	2.4	4.5	4.5	4.5
Inflation	1.4	2.6	2.7	3.2	3.1	3.1
Primary balance	-0.6	1.1	1.2	2.6	2.9	3.4
Effective interest rate	4.5	4.3	4.7	5.1	5.3	5.3
Real Exchange Rate Shock						
Real GDP growth	3.0	4.0	4.5	4.5	4.5	4.5
Inflation	1.4	4.1	3.3	3.2	3.1	3.1
Primary balance	-0.6	1.8	2.7	2.6	2.9	3.4
Effective interest rate	4.5	4.4	4.6	4.9	5.2	5.3

Source: IMF staff.

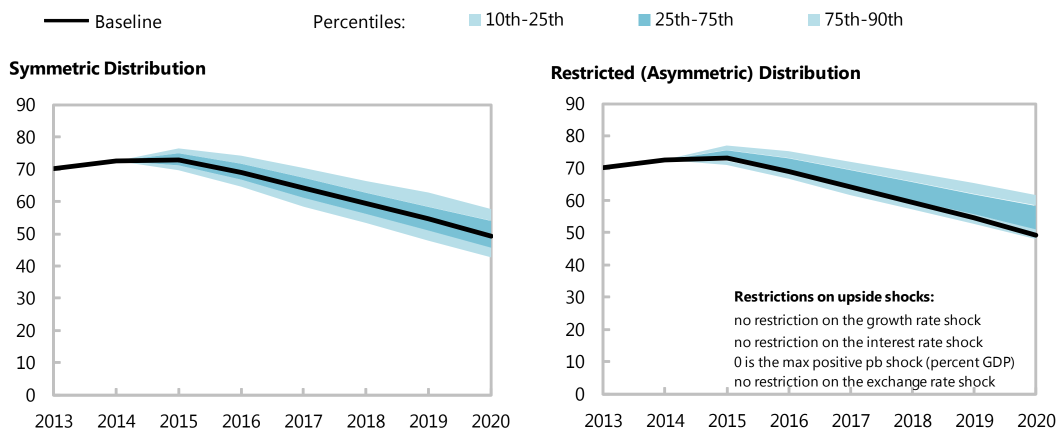
Albania Public DSA Risk Assessment

Heat Map

Debt level [1/]	Real GDP Growth Shock	Primary Balance Shock	Real Interest Rate Shock	Exchange Rate Shock	Contingent Liability shock
Gross financing needs [2/]	Real GDP Growth Shock	Primary Balance Shock	Real Interest Rate Shock	Exchange Rate Shock	Contingent Liability Shock
Debt profile [3/]	Market Perception	External Financing Requirements	Change in the Share of Short-Term Debt	Public Debt Held by Non-Residents	Foreign Currency Debt

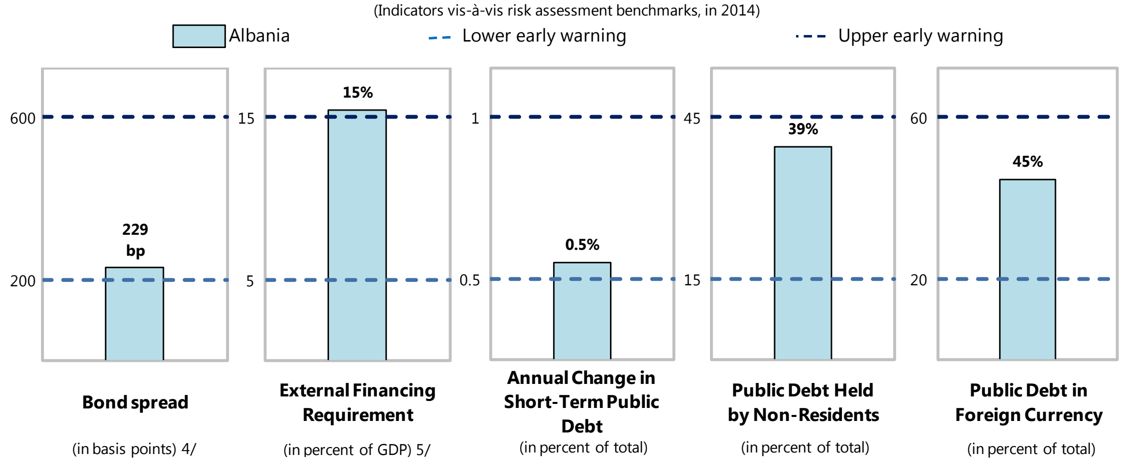
Evolution of Predictive Densities of Gross Nominal Public Debt

(in percent of GDP)



Debt Profile Vulnerabilities

(Indicators vis-à-vis risk assessment benchmarks, in 2014)



Source: IMF staff.

1/ The cell is highlighted in green if debt burden benchmark of 70% is not exceeded under the specific shock or baseline, yellow if exceeded under specific shock but not baseline, red if benchmark is exceeded under baseline, white if stress test is not relevant.

2/ The cell is highlighted in green if gross financing needs benchmark of 15% is not exceeded under the specific shock or baseline, yellow if exceeded under specific shock but not baseline, red if benchmark is exceeded under baseline, white if stress test is not relevant.

3/ The cell is highlighted in green if country value is less than the lower risk-assessment benchmark, red if country value exceeds the upper risk-assessment benchmark, yellow if country value is between the lower and upper risk-assessment benchmarks. If data are unavailable or indicator is not relevant, cell is white.
Lower and upper risk-assessment benchmarks are:

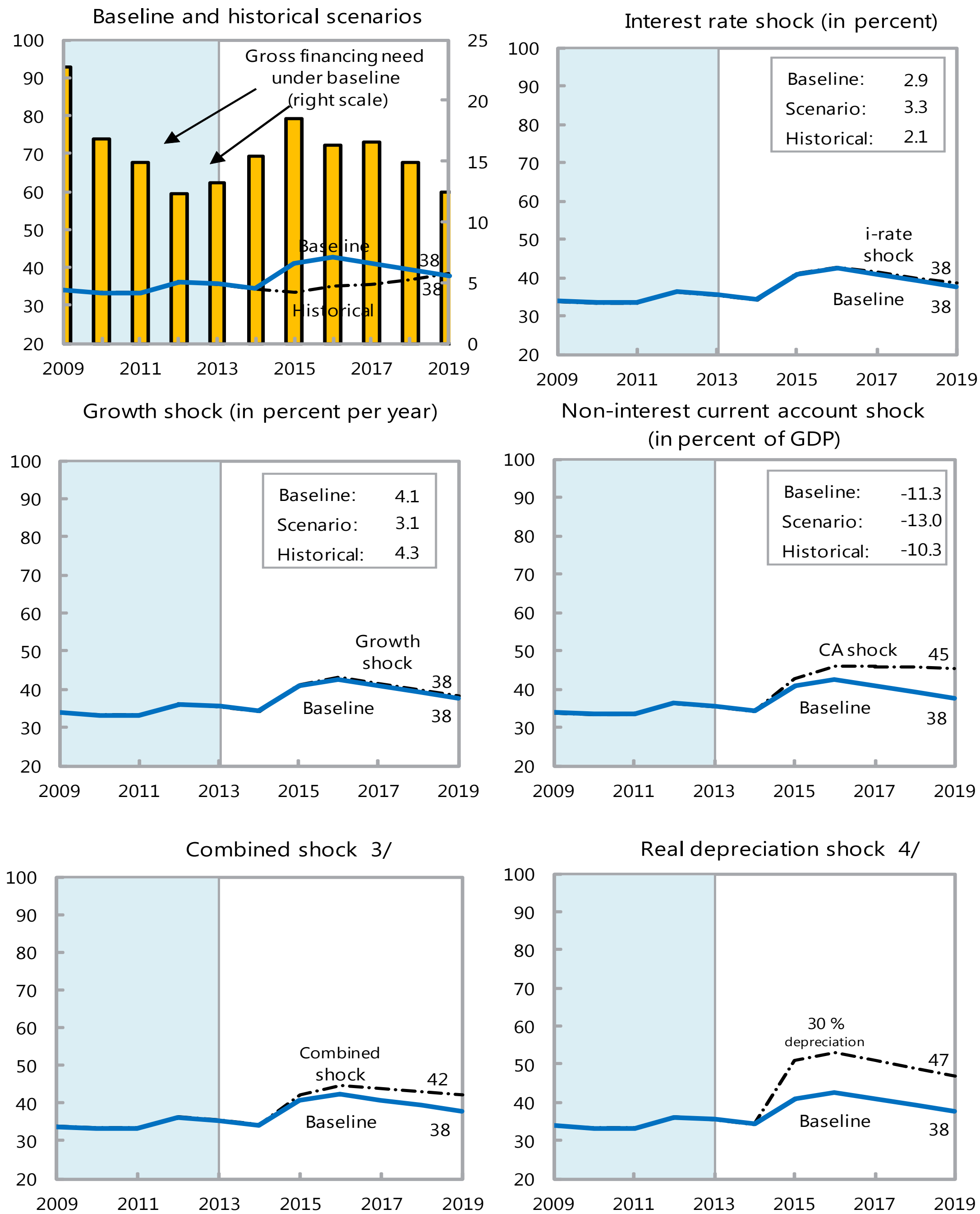
200 and 600 basis points for bond spreads; 5 and 15 percent of GDP for external financing requirement; 0.5 and 1 percent for change in the share of short-term debt; 15 and 45 percent for the public debt held by non-residents; and 20 and 60 percent for the share of foreign-currency denominated debt.

4/ Bond Spread over German Bonds, an average over the last 3 months, 22-Oct-14 through 20-Jan-15.

5/ External financing requirement is defined as the sum of current account deficit, amortization of medium and long-term total external debt, and short-term total external debt at the end of previous period.

Albania: External Debt Sustainability: Bound Tests 1/ 2/

(External debt in percent of GDP)



Sources: International Monetary Fund, country desk data, and staff estimates.

1/ Shaded areas represent actual data. Individual shocks are permanent one-half standard deviation shocks. Figures in the boxes represent average projections for the respective variables in the baseline and scenario being presented. Ten-year historical average for the variable is also shown.

2/ For historical scenarios, the historical averages are calculated over the ten-year period, and the information is used to project debt dynamics five years ahead.

3/ Permanent 1/4 standard deviation shocks applied to real interest rate, growth rate, and current account balance.

4/ One-time real depreciation of 30 percent occurs in 2010.

Appendix I. Letter of Intent

April 28, 2015

Ms. Christine Lagarde
Managing Director
International Monetary Fund
Washington, DC 20431

Dear Ms. Lagarde:

1. The Extended Arrangement approved on February 28, 2014, by the Executive Board of the International Monetary Fund (IMF) remains the main anchor of our economic policies. The attached Memorandum of Economic and Financial policies (MEFP) reviews progress in implementing the program and outlines the policies that the government and the Bank of Albania will pursue over the next twelve months.

2. Performance under the program has been strong. All end-December 2014 and continuous performance criteria and all but one indicative targets were met, with comfortable margins. All but one structural benchmarks were implemented, though two more were delayed. We are currently awaiting data to assess all four end-April performance criteria (a waiver of applicability is being requested for them, and we expect them to be met). The indicative target on the accumulation of new arrears was missed by a small margin. These arrears will be settled by end-April and the government has implemented remedial measures. Inflation was slightly below the inner band prescribed under the inflation consultation clause. The Bank of Albania (BoA) and Fund staff agreed that given the policy of cautious monetary easing and forward guidance, there is no need for other policy action regarding inflation. BoA expects inflation to converge to the medium-term target and is expanding the use of forward guidance to align expectations to its monetary policy objective. The time needed for consensus building in the selection of a new central bank governor, together with procurement delays, postponed the hiring an external expert to assist BoA's Audit Committee; this is now expected to happen in May 2015.

3. Our policy priorities over the next twelve months will focus on pursuing fiscal consolidation, safeguarding financial sector stability, reviving credit growth, and implementing growth-enhancing reforms. In this context, we are committed to pursuing, among other things, an ambitious electricity sector reform, as well as reforms in the areas of public financial management, tax administration, and expenditure policy.

4. Implementation of our program will be monitored by the Fund through reviews, quantitative

performance criteria, indicative targets, and structural benchmarks, as described in the attached MEFP and Technical Memorandum of Understanding (TMU). While we are confident that the policies described in the MEFP are adequate to achieve program objectives, we stand ready to take additional measures that may be required for this purpose. In accordance with the Fund's policies, we will consult with the Fund on the adoption of such measures in advance of revisions to the policies contained in this letter and the MEFP.

5. The government of Albania will provide the IMF with such information as it may request to monitor progress in economic and financial policy implementation.

6. In view of the strong program performance to date and the strength of policy commitments in the period ahead, we request that the Executive Board of the IMF complete the fourth review under the Extended Arrangement. We request a waiver of applicability for the performance criteria on general government overall cash deficit and expenditure and on BoA's net international reserves and increase in credit to the general government, given the unavailability of end-April data for assessing these quantitative targets. We request the modification of performance criteria, as described in Table 1 of the MEFP. Finally, we request the purchase of SDR 28.88 million, following completion of the fourth review by the IMF's Executive Board.

7. We wish to make this letter available to the public, along with the attached MEFP and TMU, as well as the IMF staff report on the fourth review under the EFF. We therefore authorize their publication and posting on the IMF website, subject to Executive Board approval. These documents will also be posted on the official websites of the Albanian government.

Sincerely,

/s/	/s/	/s/
Shkelqim Cani	Gent Sejko	Arben Ahmetaj
Minister of Finance	Governor, Bank of Albania	Minister of Economic Development

Attachments: Memorandum of Economic and Financial Policies
Technical Memorandum of Understanding

Attachment I. Memorandum of Economic and Financial Policies

1. This Memorandum lays out the Government of Albania's policy priorities for the period ahead, supported by the IMF's EFF. Our policies seek to generate higher medium-term growth that results in higher living standards and better employment opportunities for Albanians. Achieving these goals will require sustained efforts to reduce debt-related vulnerabilities, place public finances on a sustainable footing, and unlock structural constraints to medium-term growth.

Recent Economic Developments

2. Output recovered in 2014, after a sharp slowdown in growth in 2012–13. Real GDP is estimated to have grown by around 2 percent in 2014, supported by increased private demand and the expansion of the service sector. Improved financing conditions, higher confidence, and continued arrears clearance boosted household consumption and private investment.

3. External imbalances widened in 2014. The current account deficit reached 13 percent of GDP, a 2.3 percent deterioration compared to 2013. The increase in the current account deficit reflects subdued oil exports and rapid growth in imports of intermediate goods and electricity (in the first half of 2014). After several years of continuous decline, remittances stabilized in 2014. The current account deficit was largely financed by non-debt creating flows such as FDI. Gross international reserves cover around 4.4 months of imports of goods and services.

4. The negative output gap alongside declining foreign prices resulted in low headline inflation. Annual inflation averaged 1.6 percent in 2014. Core inflation bottomed out in Q4 of 2014 and started rising in early 2015, reflecting a pickup in underlying inflation dynamics. However, inflation remains below the medium-term target of 3 percent of the Bank of Albania (BoA), which has lowered its policy rate to a record low of 2 percent.

Outlook

5. The moderate recovery is expected to strengthen during 2015. However, inflation will remain below BoA's target in the short term. Real GDP growth is projected to accelerate gradually to about 4 percent in 2016, despite the damage done by recent floods and the headwinds facing the domestic oil extraction sector, a key growth driver in recent years. The growth acceleration is expected to be driven by rising domestic demand benefiting from low energy prices and interest rates, improved confidence, and a gradual recovery in bank lending. Public sector demand is expected to grow minimally in 2015. Despite a gradual buildup of price pressures, inflation is likely to remain below the BoA's inflation target for some time.

6. The external account deficit is likely to remain elevated in 2015. Imports are projected to grow on the back of large infrastructure projects (TAP and the Statkraft/Devoll hydropower plant), while exports are expected to be impacted negatively by falling commodity prices. The current account deficit is estimated to stay around 13 percent of GDP, more than half of which would be financed by FDI. Over the medium term, the current account deficit is expected to narrow somewhat because of improvements in export capacity, expenditure switching away from imports, and the lower import needs of the big FDI projects.

Program Implementation

7. All end-December 2014 and continuous performance criteria and all but one indicative targets were met, with comfortable margins (Table 1). The ceilings on the government's cash deficit and expenditure ceiling were met due to the under-execution in current and capital spending which offset overruns in net lending to the electricity sector. The lower inner band under the Inflation Consultation Clause was missed because of disinflationary pressures from foreign trade partners and the persistent negative output gap. The zero ceiling on the accumulation of central government domestic arrears was not met. Results from the quarterly survey of ten key ministries and the GDT show an accumulation of 0.3 billion lek of new arrears at end-2014 (0.02 percent of GDP). The bulk of new arrears were accumulated by the GDT and the Ministry of Transport (on road construction projects). All accumulated arrears will be repaid by end-April 2015. In addition, as a remedial measure, MoF has issued an instruction to line ministries informing them that reallocations within their budgets, in order to accommodate individual projects exceeding their allocations, would be possible only with permission from MoF and the Ministry of the Economy (MoE). This instruction has also been published.

8. All but one structural benchmarks were implemented, though two more were delayed (Table 2a):

- In the area of public financial management, the regular report on arrears paid was published on time, while the survey on the new accumulation of arrears was expanded to five additional key ministries and also published online for the first time. The survey's expansion and publication caused some delay past the March 15 deadline; going forward, we expect to publish it on time. The external auditors for non-tax claims and for VAT refunds are expected to complete their work before their end-April deadlines. Rather than wait for the final report of the external auditor on arrears payments for non-tax claims, MoF published its action plan to tackle the weaknesses identified in the auditor's interim reports.

- In the area of tax administration, the Risk Management Unit has been established and has commenced operations. The new software for the IT system at GDT has been installed and testing has started. With help from Fund TA, the GDT has prepared its new corporate strategy and MoF has formally endorsed it.

- In the area of financial sector governance, the time needed for consensus building in the selection of a new central bank governor, as well as procurement delays, postponed the hiring of an external expert to assist BoA's Audit Committee (now expected by end-May 2015). Finally, the authorities prepared their first quarterly survey of the consolidated arrears of state-owned enterprises in the electricity sector to the private sector.

Economic Policies for 2015

A. Fiscal Consolidation

9. **We commit to continuing with fiscal consolidation, as planned, in order to reduce debt-related vulnerabilities that hamper growth and cause macroeconomic instability.** We commit to achieving the 2015 program deficit target, as well as the programmed ceiling on expenditure. Over the medium term, we are committed to lowering the public debt-to-GDP ratio below 65 percent by the end of the program in 2017 and below 60 percent by 2018.

10. **The government has reassessed the 2015 fiscal program in light of current developments and the updated outlook.** Lower revenues from the oil sector of 6 billion lek (0.4 percent of GDP) in 2015 are being offset by a downward revision of a conservatively budgeted interest bill for 2015 and beyond. Moreover, the government is saving the excess proceeds from telecom license fees of 1.8 billion lek (0.1 percent of GDP) to guard against any underperformance in other revenues given the downside risks to inflation.

11. **Budget support to the electricity sector continues to pose a heavy burden on public finances, which is projected to decline over the medium term.** Budget support comes in several forms, including public guarantees, policy net lending, and compensation of the poor. The total stock of public guarantees to the sector increased to 3.3 percent of GDP at end-2014. The financial gap in the electricity sector reflects mostly low collection levels and large network losses. However, we are aggressively implementing an ambitious set of reforms in the sector (see below for details) that will resolve the structural imbalances and remove the need for government support by 2020. We therefore aim to limit public guarantees and policy net lending to the electricity sector to 15.8 billion lek in 2015, 12.8 billion lek in 2016, 9.8 billion lek in 2017, 8.8 billion lek in 2018, 1.3 billion lek in 2019, and zero in 2020. In addition, we have introduced targeted transfers to compensate the most vulnerable social groups for electricity tariff adjustments, amounting to 1.6 billion lek in 2015, which is kept constant as a share of GDP over 2016-20. To better track the impact of public support to the electricity sector on the government's fiscal position, we will monitor the overall fiscal balance including electricity sector support. We will also show explicitly as a memorandum item in our budget execution reports the amount of government guarantees and policy net lending to electricity companies. We will also publish on MoF's website details on all guarantees and policy net lending on a monthly basis. If government support to the electricity sector exceeds the annual programmed amount, we commit to taking offsetting measures to meet the program's fiscal targets.

12. **We are addressing other emerging and potential risks to the baseline fiscal framework:**

- **Property compensation claims:** The European Court of Human Rights (ECHR) in Strasbourg has begun to process another group of cases brought against the Albanian government by expropriated property owners. These are expected to be decided in 2015 and total compensation on these claims could reach 3 billion lek, on top of the 1.1 billion awarded in 2014. In view of the precedents established by these cases, additional claims for compensation may be filed. An interagency working group headed by the Deputy Prime

Minister is compiling a registry of all potential cases that might end up before the ECHR, and is also working on a comprehensive and fair solution.

- **Capital expenditure:** The amount of outstanding unbudgeted investment projects continues to exceed the government's ability to absorb them in its Medium-Term Budget Framework (MTBF). Our plans to prioritize all outstanding infrastructure projects and cancel or reschedule low-priority projects have been delayed because of legal difficulties and the threat of lawsuits. However, we are committed to tackling this issue forcefully in 2015. As a first step, we will re-assess all these projects. Next, a ranking will be approved by the Council of Ministers and posted on the websites of MoF and MoE by end-June 2015. The MoF will also publish a list of all projects that will be part of its MTBF to signal its intention not to implement projects excluded from the list. We also plan to add a clause to all new contracts stating that acceleration of project work without the MoF's approval will constitute a violation of the contract and render null and void any obligations to pay for such work.

- **Public Private Partnerships (PPPs):** PPPs can be an effective way to harness private sector know-how and management expertise. However, they could also pose substantial risks to public finances. We will ensure that our legal and regulatory framework applies to PPPs, that PPPs follow international best practice, and that their related fiscal costs and contingent liabilities are transparently accounted for in the fiscal accounts and debt statistics. Technical assistance from the Fund and other international partners will continue to help assess our current legal and regulatory framework and suggest recommendations for improvement.

- **Disability benefits:** Spending on disability benefits has risen sharply in recent years, in part because of weak controls and fraud. We are working with the World Bank on a medium-term project to reform them. Reform will begin in the second half of 2015, but will take time to complete and yield savings. Therefore, by end-June 2015 the Council of Ministers will issue and publish a decree that reduces the disability benefits in certain cases where they have been deemed too generous. The estimated savings for the 2015 fiscal year from these reforms are 0.4 billion lek.

13. Tax administration reforms are advancing to the next stage. A key priority for 2015 is the reform of the tax refund scheme. Once the risk module for VAT refunds is operational, risk-based auditing is expected to begin by June 2015. The restructuring of GDT's administration will lead to the creation of a dedicated Refund Unit to coordinate refund efforts nationwide, with regional inspectors undertaking related operational functions.

14. Closer cooperation and information sharing between the GDT and GDC will enhance revenue administration reform efforts. The Minister of Finance recently signed an order allowing the investigation departments of both institutions to jointly monitor the oil sector. Nevertheless, the merger of the two departments is a medium-term objective, and any related decisions will be taken in consultation with IMF staff.

15. We commit to introducing a valuation-based property tax by end-2017. The reform will be undertaken in consultation with Fund TA. As a first step, we plan to introduce a fiscal cadastre to assess tax for each property by end-2016.

16. We are reinforcing PFM to prevent the accumulation of new arrears. We plan to extend AGFIS to 15 budget institutions (accounting for 60 percent of the budget) and one local government by the end of 2015. However, progress is contingent upon the upgrade of the AGFIS server, which has been delayed and is now expected to be completed by the end of September 2015. Changes in the procurement, financial management and control, and budget laws to incorporate multi-year commitment limits by end-2015 will further strengthen the MTBF.

17. Arrears clearance will continue to advance in tandem with progress in the auditing and verification of paid arrears. Following the findings of the auditors' reports and after consultation with IMF staff, the clearance process may be accelerated beyond the annual budget allocation of 20 billion lek for 2015. However, as has been the case until now, if at any stage there are indications that the process is not proceeding in accordance with our Arrears Prevention and Clearance Strategy (APCS), arrears clearance will stop pending consultation with IMF staff. The High State Audit will continue to participate in regular meetings of the arrears clearance committee. Total arrears payments under the APCS will be limited to 72 billion lek. Any arrears above this amount will be paid using our own resources.

18. An ambitious pension reform approved by Parliament in July 2014 became effective in 2015. The stronger incentive to participate in the system has led to a surge in the number of people re-joining the scheme. A draft law that will increase the retirement age and contribution rates for the supplementary pension scheme for high government officials has been approved by the Council of Ministers and submitted to Parliament, where approval is expected by end-June 2015.

19. In consultation with IMF TA, we will take steps to shore up the credibility of our MTBF, as a prerequisite for re-introducing a fiscal rule. We will continue to align our budget projections and macro framework with those of the BoA and international financial institutions. By early September 2015, MoF and MoE will submit to the Strategic Planning Committee at the Office of the Prime Minister the principles for distinguishing between core allocations and new policy initiatives in public investment in the MTBF, in order to focus attention on the costing of new policies and to also prevent them from squeezing core allocations for resources. Starting with the 2017 budget, the MTBF will begin to make that distinction at the sectoral and programme level. In addition, the MTBF will contain an analysis of outturns vis-à-vis past vintages of the MTBF at the sectoral and programme level. It will also contain the total approved cost, the sunk cost so far, and remaining cost beyond the three-year window of the MTBF for all projects.

20. Our process for evaluating, selecting, executing, and monitoring public investment projects is adequate but can be improved further. All projects under consideration (above a certain threshold) are already subject to a feasibility study. MoF and MoE coordinate and share data with each other. The Strategic Planning Committee at the Office of the Prime Minister, of which MoF and MoE are both members, discusses the pipeline of future projects on a regular basis. To further strengthen coordination among the responsible line ministries in evaluating, selecting, executing, and monitoring investment projects, MoF together with MoE and the Office of the Prime Minister will conduct a detailed review of public investment management, with a focus on current institutional arrangements, internal organization, and resource needs by end-June 2015. By end-2015, MoF and MoE will compile and publish a short manual that spells out the public investment process, in order to provide a handy reference to the laws and regulations guiding the process. Finally, we will fast-track the implementation of the project management module under the Albanian Government Financial Information System (AGFIS) so that it is operational by end-2016.

21. Parliament recently approved a new Debt Management Law. It is in line with the international best practice and was drafted in close consultations with our international partners. In 2015, we are planning to issue a EUR 250 million international commercial loan supported by a Public Finance Policy Based Guarantee (PBG) of EUR 200 million from the World Bank, and a Eurobond of EUR 300 million. These operations will secure financing for the budget and help to refinance debt, particularly the outstanding Eurobond of EUR 300 million maturing in November 2015. They should also open space for bank lending to private sector.

B. Monetary and Exchange Rate Policy

22. The BoA remains committed to preserving price stability under its inflation-targeting framework. As defined in our recently updated Monetary Policy Document, the BoA aims to achieve an average CPI inflation of 3 percent over the medium term. The monetary policy decision-making process will be guided by the deviation of forecasted inflation from this objective, while striving to avoid excessive volatility in the real and financial sector. While the target applies to headline inflation, we will also monitor core inflation as a measure of underlying inflationary pressures. Inflation performance will continue to be monitored under the program through an Inflation Consultation Clause.

23. The exchange rate remains fully flexible and determined entirely by market forces. The BoA relies on indirect instruments (such as open market operations) to steer interest rates. Exchange rate flexibility complements our price stability objective and supports our operational framework for monetary policy. The BoA will also aim to maintain adequate reserve coverage over the medium term. For the duration of the program, we will not introduce or intensify restrictions on the making of payments and transfers for current international transactions, nor introduce or modify any multiple currency practices or conclude any bilateral payments agreements that would violate our obligations under Article VIII of the IMF's Articles of Agreement. Also, we will not introduce or intensify import restrictions for balance of payments reasons.

24. Monetary policy is likely to remain accommodative for the foreseeable future. The BoA will continue to assess its monetary policy stance in the context of the inflation outlook and the strength of the transmission mechanism. Inflationary pressures remain weak, given below-potential growth, low inflation abroad, and a slight downward drift in inflation expectations. Under these circumstances, monetary policy is likely to remain accommodative, and to be augmented by the BoA's forward guidance to the financial markets. The monetary policy transmission mechanism remains hampered by the high risk aversion among agents in the real and financial sectors. Furthermore, external financial conditions for the banking sector remain challenging. However, the improved financial performance of the banking system and the expected gradual rise in credit demand will strengthen the transmission of monetary impulses to the broader economy. In the period between the issuance of the new Eurobond and the repayment of the old one, the extra liquidity will be invested as part of BoA's international reserves. MoF will continue to coordinate with BoA on public debt and cash management.

C. Safeguarding Financial Sector Stability

25. The BoA is further reinforcing supervision. The overall supervisory process and on-site examinations, in particular, have emphasized imposing an enhanced quality of governance and risk administration, with a focus on the fastest-growing segments of the banking system. The BoA will continue to monitor banks' resilience to risks, in order to maintain adequate capital and liquidity positions, thus ensuring the stability of the banking system.

26. At the end of 2014 BoA decided to extend measures adopted earlier to counteract the slowdown in credit growth. These include changes to capital requirements designed to encourage moderate credit growth and discourage outflows to non-resident entities. The BoA will continue to carefully monitor banks' balance sheets in order to ensure that they will be able to comply with standard capital requirements once the changes described above expire in 2015.

27. More stringent capital adequacy requirements (standardized approach Basel II) came fully into force in January 2015. Many of the new requirements were implemented in previous years, including additional capital requirements for systemically important institutions and higher risk weights on foreign currency lending. Regarding Basel III, the BoA's new regulation on regulatory capital takes into consideration CRD IV, while we are assessing the impact of Basel III liquidity indicators on individual banks. CRD IV implies that Albanian subsidiaries of EU banks must increase to 100 percent the risk weight on assets denominated in Albanian currency, including Albanian government securities.

28. We are undertaking additional measures to facilitate problem loan restructuring. In cooperation with the World Bank, we are working on a project to facilitate it through developing recovery and resolution plans for large problem borrowers. Recent reforms to speed up collateral execution and increase loan write-offs are showing some results. Changes to the Civil Procedures Code intended to minimize execution suspension gaps came into effect in September 2013. This has contributed to an increase in collateral recoveries by 5 percentage points between September 2013 and December 2014. However, the volume of loans remaining in execution is very large, at 20 percent of the total stock. In addition, following amendments to the Tax Law in April 2014 to remove legal and technical impediments to loan write-offs, the stock of written-off loans increased by 28 percent in the second half of 2014. Finally, a new regulation requiring mandatory write-off of loans that have spent three years in the "loss" category came into force at the beginning of 2015. It will contribute to a projected reduction of NPLs by 3 percentage points by year-end.

29. We are committed to further regulatory and legal reforms to reduce NPLs to acceptable levels. The Albanian authorities are reviewing the commercial bankruptcy law in order to facilitate the restructuring of private balance sheets, and have requested IMF TA. We will form a high-level working group to develop a comprehensive strategy to address the NPL issue, including measures that address operational difficulties in resolution and collateral execution. The strategy will be approved by the Council of Ministers and BoA by end-September 2015.

30. AFSA will finalize changes to the regulatory framework for investment funds by end-June 2015. Of the remaining two vacancies on AFSA's Board, one was filled in March and the other one is expected to be filled by end-May 2015. This should allow us to move quickly to put in place the new regulations on liquidity requirements and asset valuation. In the meantime, we will not license any new investment funds.

31. The BoA is taking measures to implement the recommendations of the 2014 safeguards assessment. A new Inspector General was appointed in early April and the internal audit function will resume normal operations. Specifically, it will finalize the audits in progress and develop a risk-based internal audit plan for 2015. We will submit to the IMF the audits for the end-September and end-December 2014 program monetary data by end-July 2015, and an external assessment of vault security and related internal controls will be completed by end-September 2015. Internal and external assessments of the internal audit function are planned for 2015. In addition, by end-May 2015, we will appoint an external technical expert to assist the Audit Committee. Finally, the BoA will prepare its 2015 financial statements in accordance with IFRS by end-March 2016.

D. Structural Reforms

32. We are encouraged by the early results from our efforts to reduce losses and improve collections in the electricity sector. We launched a campaign in October 2014 to disconnect service for the nonpayment of bills and to enforce criminal penalties for electricity theft. As a result distribution losses—unbilled power as a share of total power entering the distribution system—fell from 45 percent in 2013 to 38 percent in 2014 and under 34 percent in the first quarter of 2015. Furthermore, the collection rate—bills collected as a share of total electricity bills—has improved from 72 percent in 2014 to over 86 percent in February 2015. We are committed to reducing distribution losses to 14 percent by 2019. We will ensure that budgetary, non-budgetary, and local government institutions make timely and full payments on their electricity bills. We are also moving forward with a performance management contract for the distribution company, and expect the due diligence documents to be ready by mid-2015.

33. The new power sector law is expected to be approved by Parliament by end-May 2015. The new law restructures the relationship among the three public power companies responsible for generation, transmission, and distribution (KESH, OST, and OSHEE), and moves toward further market liberalization, in line with the EU's 2009 Electricity Directive. The law sets in place a schedule for moving all medium-voltage customers out of the regulated tariff structure by end-2017, beginning with 35KV customers by end-2015. On completion, the share of deregulated consumption would increase from 13 to 40 percent. Following the tariff adjustments that went into effect at the beginning of 2015, we plan to undertake a review of our current tariff methodology in cooperation with the World Bank, in order to make tariff adjustments more frequent and automatic.

E. Statistics

34. INSTAT will continue with its efforts to improve the quality of macroeconomic statistics. INSTAT's data sourcing is hampered by poor cooperation from other government departments. Notably, GDT data needed for compiling the national accounts are not made available to INSTAT, due to legal uncertainties about data sharing. Under MoF's guidance, the GDT and INSTAT have signed a memorandum of understanding to facilitate the exchange of company-level data needed for the appropriate sectoral and regional classification of national accounts data.

Program Monitoring

35. We anticipate that the fifth program review will take place on or after July 15, 2015, and require observance of the conditionality for end-April 2015. Thereafter, reviews will occur every four months starting on or after November 15, 2015, and require observance of the conditionality for the most recent test date. The final review will take place on or after February 15, 2017 and require observance of the conditionality for end-November 2016.

Table 1. Albania: Quantitative Performance Criteria and Indicative Targets for 2014–16

(In billions of leks, unless otherwise indicated)

	2014												2015					2
	Mar			Jun			Sep			Dec			Apr	Aug		Dec		
	Prog.	Prog. Adj.	Act.	Prog.	Prog. Adj.	Act.	Prog.	Prog. Adj.	Act.	Prog.	Prog. Adj.	Act.	Prog.	Prog.	Rev. Prog.	Prog.	Rev. Prog.	P
I. Quantitative Performance Criteria																		
1. Floor on net international reserves of the BoA (EUR million)	1289		1463	1330		1495	1330		1525	1330	1119	1539	1507	1507	1509	1507	1510	1
2. Ceiling on general government overall cash deficit (cumulative) 2/ 3/	16.0	16.0	0.8	20.3	20.3	4.9	31.6	31.6	7.6	58.8	58.8	41.1	16.9	32.7	22.2	52.1	52.1	
3. Ceiling on general government expenditure (cumulative) 3/	…		…	194.9		180.1	300.9		274.3	423.5		407.8	141.6	292.9	280.0	463.6	457.5	1[illegible]
4. Ceiling on the increase of Bank of Albania credit to the general government (cumulative) 4/	0.0		-0.1	0.0		0.0	0.0		0.0	0.0		0.0	0.0	0.0		0.0		
II. Continuous Performance Criteria																		
5. Accumulation of new external payment arrears by the general government (EUR million)	0.0		0.0	0.0		0.04	0.0		0.0	0.0	…	0.0	0.0	0.0		0.0		
III. Inflation Consultation																		
6. 12-month percent change in consumer prices																		
Upper outer band	5.0			5.0			5.0			5.0			5.0	5.0		5.0		
Upper inner band	4.0			4.0			4.0			4.0			4.0	4.0		4.0		
Actual/center point	3.0		1.9	3.0		1.6	3.0		1.7	3.0		1.3	3.0	3.0		3.0		
Lower inner band	2.0			2.0			2.0			2.0			2.0	2.0		2.0		
Lower outer band	1.0			1.0			1.0			1.0			1.0	1.0		1.0		
IV. Indicative Targets																		
7. Ceiling on subsidies to the energy sector	…		…	…		…	…		…	…		…	4.4	8.7		13.1		
8. Average distribution losses by energy distribution company (OSHEE) (percent, cumulative from beginning of year)	…		…	…		…	…		…	…		37.8	37.0	34.5		34.0		2
9. Ceiling on contracting of nonenergy guarantees	…		…	…		…	…		…	…		…	0.0	0.0		0.0		
10. Ceiling on accumulation of central government domestic arrears (as reported by MoF's quarterly survey on arrears accumulation)	0.0		0.4	0.0		1.1	0.0		0.4	0.0		0.3	0.0	0.0		0.0		
11. Floor on clearance of central government domestic arrears 5/	0.0		1.0	1.0		19.1	1.0		25.9	14.2		33.8	5.0	10.0		15.0		

Source: Albanian authorities; and Fund staff estimates and projections.

1/ All adjustors are described in the Technical Memorandum of Understanding (TMU).

2/ Data revisions have led to adjustments for the outturn of the cash deficit for March, June, and September 2014, and for government expenditure for June and September 2014.

3/ Excluding arrears payment. The assessment of performance in 2014 will also exclude new energy and nonenergy guarantees (which were not part of the original PC but are now included in the fiscal framework).

4/ Indicative target through December 2014.

5/ General government for March 2014.

Table 2a. Albania: Structural Benchmarks for the April 2015 Test Date under the EFF Arrangement

	Structural Benchmarks	Test Date	Status	Remarks
	I. Public Financial Management			
1.	Publish a report on arrears paid (on a quarterly basis) on the MoF website (starting in June 2014).	Continuous	Met.	
2.	MoF to report quarterly survey results on new arrears accumulation among five key ministries (Transportation, Health, Education, Defense, and Justice) and GDT.	Continuous	Met.	
3.	MoF to expand the reporting of quarterly survey on arrears accumulation to five additional ministries (Interior, Agriculture, Finance, Economy, and Social Welfare) (starting with the period from October–December 2014) and publish it on the MoF's website.	Continuous	Met with a delay.	
4.	The MoF to prepare and publish an action plan with measures to address weaknesses identified in the auditor's report on non-tax claims payments.	Feb. 15, 2015	Met with a delay.	
5.	External auditor to complete the audit of 75 percent of outstanding non-tax claims paid through January 2015.	End-Apr. 2015	Met.	
6.	External auditor to complete verification of arrears payments on tax refunds.	End-Apr. 2015	Met.	
	II. Tax Administration			
7.	Establish and commence operations of a permanent Risk Management Unit (RMU) in GDT (see TMU).	End-March 2015	Met.	
8.	Install the new IT software at the central server site (NAIS) and commence testing.	End-Feb. 2015	Met.	
9.	The GDT to develop a corporate strategy for medium to long-term capacity building.	End-Mar. 2015	Met.	
	III. Financial Sector			
10.	Hire an external expert to assist the Audit Committee of the Bank of Albania.	End-Feb. 2015	Not met.	In progress, expected to be met by end-May.
	IV. Energy Sector			
11.	Prepare a quarterly survey of the gross consolidated arrears of the electricity sector (KESH, OST, OSHEE) to the private sector (starting with the period January–March 2015).	Continuous	Met.	

Table 2b. Albania: Proposed Structural Benchmarks for 2015–16 under the EFF Arrangement

Structural Benchmarks	Test Date	Status	Remarks
I. Public Financial Management			
1. Publish a quarterly report on arrears paid on MoF's website.	Continuous		
2. Publish a triannual report on new arrears accumulation in ten key ministries and the GDT on MoF's website.	Continuous		
3. Publish, on MoF's and MoE's websites, a report on the prioritization of all outstanding infrastructure projects, including a ranking approved by the CoM using transparent criteria.	End-June 2015		
4. Roll out the AGFIS to 15 budget institutions (see TMU).	End-Dec. 2015		
5. Change the Procurement Law, the Financial Management and Control Law, and the Budget Law to incorporate multi-year commitment limits.	End-Dec. 2015		
II. Tax Administration			
6. Commence auditing tax refunds on a risk basis.	End-June 2015		
7. Create a fiscal cadastre to assess tax for each property.	End-Dec. 2016		
III. Financial Sector and Central Banking			
8. BoA to submit to the IMF the audits for the end-September and end-December 2014 program data.	End-July 2015		
9. Albanian Financial Supervisory Authority (AFSA) to amend the regulatory framework for investment funds on asset valuation and liquidity requirements.	End-June 2015		
IV. Electricity Sector			
10. Prepare a quarterly survey of the gross consolidated arrears of the electricity sector (KESH, OST, OSHEE) to the private sector.	Continuous		
11. Remove 35KV medium-voltage consumers from the regulated tariff system.	End-Dec. 2015		

Attachment II. Technical Memorandum of Understanding

1. This Technical Memorandum of Understanding (TMU) defines the indicators used to monitor the program, and reflects the understandings between the Albanian authorities and the IMF. The TMU also defines the associated reporting requirements.

2. The exchange rates for the purposes of the program are set at lek 140.25 = €1, lek 103.17 = $1, and lek 158.05 = SDR 1. The gold price is set at 920.18 oz = €1. These are the rates shown on the Bank of Albania's website as of November 30, 2013.[1]

3. For the purpose of the program, the central government includes extra-budgetary funds. The general government includes the central government, local governments, the Social Security Institute (SSI), and the Health Insurance Institute (HII).

4. The fiscal year starts on January 1 and ends on December 31.

Quantitative Performance Criteria

A. Floor on Net International Reserves of the BoA

Definition

5. Net international reserves (NIR) are defined as reserve assets minus reserve liabilities of the Bank of Albania. **Reserve assets** are readily available claims of the Bank of Albania on nonresidents denominated in foreign convertible currencies, and held for the purpose of meeting balance of payments financing needs, intervening in exchange markets, and other purposes. They include Bank of Albania holdings of monetary gold, SDRs, Albania's reserve position in the IMF, foreign currency cash, securities, and deposits abroad. Excluded from reserve assets are any assets that are pledged, collateralized, or otherwise encumbered; claims on residents; precious metals other than monetary gold; assets in nonconvertible currencies; illiquid assets; and claims on foreign exchange arising from derivatives in foreign currencies vis-à-vis domestic currency (such as futures, forwards, swaps, and options).

6. **Reserve liabilities** are defined as foreign exchange liabilities to residents and nonresidents of the Bank of Albania, irrespective of their maturity. They include: foreign currency reserves of commercial banks held at the Bank of Albania; foreign currency deposits of the government held at the Bank of Albania; all credit outstanding from the IMF that is a liability of the Bank of Albania; commitments to sell foreign exchange arising from derivatives (such as futures, forwards, swaps, and options); and all arrears on principal or interest payments to commercial banks, suppliers, or official export credit agencies. Reserve assets and reserve liabilities will both be expressed in euros, at the program exchange rate.

[1] http://www.bankofalbania.org/web/Time_series_22_2.php?evn=agregate_detaje&evb=agregate&cregtab_id=644&periudha_id=1

Reporting

7. Data will be provided by the BoA to the Fund with a lag of no more than five days past the test date.

B. Cumulative Ceiling on General Government Overall Modified Cash Deficit Excluding Arrears Payments

Definitions

8. The **overall modified cash deficit of the general government** will be measured from the financing side (below the line) at current exchange rates, based on the template below:

MODIFIED CASH BALANCE
Financing
Domestic
Privatization receipts (gross)
Domestic net borrowing (using residency criterion)
Central government net direct debt
Central government guarantees (drawings minus repayments)
Local government net direct debt
Other
Change in balance of government accounts at BoA
Change in balance of TSA bank account
Change in balance of S&HII's bank accounts
Trust accounts
On-Loan principal
Change in balance of government accounts outside BoA
Government accounts outside TSA (in commercial banks)
Transitory accounts – guarantees on custom duties
Cash in transit
Accounting items
Variance accrual-cash
Float
Liability to SSI (receipts minus payments)
Others
Foreign
Drawings
Long-term loans (all direct debt drawings included in Albania's official debt statistics, including loans for the energy sector, even if on-lent)
Budget support loans (drawings)
Guarantees (drawings)
Change of statistical account
Repayments (of direct and guaranteed debt)
Memo: arrears clearance

9. In determining the overall modified cash balance, the following considerations will apply:[2]

- Domestic borrowing is reported on a net basis and using the residency criterion. It covers bank loans, securities issued, overdraft accounts, and other debt instruments, less government deposits.
- Principal repayments include only principal paid by the government and not that by the actual borrower. In case a borrower repays the Ministry of Finance at a later point in time, principal is recorded under "on-loan principal."
- Foreign borrowing is reported on a gross basis and using the residency criterion. It covers disbursements by international financial institutions, bank loans, securities issued, overdraft accounts, and other debt instruments.
- "Change of statistical account" covers funds disbursed but not yet withdrawn and held by nonresidents in financial institutions for project-related spending.
- "Repayments" refers to all payments to nonresidents related to disbursements by international financial institutions, bank loans, securities, overdraft accounts, and other debt instruments.

10. The overall modified cash deficit will also include all new issuances of general government guarantees (excluding rollover) for the energy and non-energy sectors, as well as net policy lending.

11. Excluded from the calculation of the overall modified cash deficit of the general government are the arrears payments to be made in the context of the Arrears Prevention and Clearance Strategy (APCS). The amount of arrears paid will be identified using the verified arrears list and matching the list with the Treasury payment records. A summary of the total amount of arrears paid under the clearance strategy, as defined above, will be provided on a monthly basis.

Reporting

12. Data, including new guarantees and the amount of arrears payments under the APCS, will be provided to the Fund, using current exchange rates, with a lag of no more than 30 days after the test date for April and August test dates. For December test dates, data should be provided no more than 60 days after the test date.

Adjustors

13. The **ceiling on the overall modified cash deficit** of the general government will be adjusted upward (downward)—that is, the deficit target will be increased (reduced)—by:

- 50 percent of the privatization receipts, up to total privatization receipts of lek 15 billion in a given year. The programmed amount of privatization receipts in 2015 is zero.
- the excess (shortfall) of new energy guarantees, excluding rollover, issued during the course of the year up to a maximum of the annual budgeted allocation (lek 10.1 billion in 2015). The

[2] Cash balance data come from Treasury, the Debt Office, and the Bank of Albania.

adjustor will not apply to the end-year amount of new energy guarantees. Energy guarantees are defined as guarantees issued by the general government for the benefit of the electricity operators KESH, OST, and OSHEE. The programmed amount of new energy guarantees is lek 6.7 billion for August 2015 and lek 4.4 billion for April 2016.

C. Cumulative Ceiling on General Government Expenditure Excluding Arrears Payment

Definitions

14. **General government expenditure** covers spending on personnel, interest, operations and maintenance, subsidies, social insurance outlays, local government expenditures, other expenditures (social protection transfers), capital expenditure, reserve and contingency funds, and net lending, as reported in the government's monthly fiscal indicators table. For the purpose of this target, arrears payments are excluded from the calculation. The amount of arrears payment is identical to the number used in the calculation of the performance criterion on the modified cash deficit (Section B above).

Reporting

15. Data will be provided to the Fund, using current exchange rates, with a lag of no more than 30 days after the test date for April and August test dates. For December test dates, data should be provided no more than 60 days after the test date.

Adjustors

16. The **ceiling on expenditure** of the general government will be adjusted upward (downward) by:

- 50 percent of the privatization receipts, up to total privatization receipts of lek 15 billion in a given year. The programmed amount of privatization receipts in 2015 is zero.
- the excess (shortfall) of new energy guarantees, excluding rollover, issued during the course of the year up to a maximum of the annual budgeted allocation (lek 10.1 billion in 2015). The adjustor will not apply to the end-year amount of new energy guarantees. Energy guarantees are defined as guarantees issued by the general government for the benefit of the electricity operators KESH, OST, and OSHEE. The programmed amount of new energy guarantees is lek 6.7 billion for August 2015 and lek 4.4 billion for April 2016.

17. The **ceiling on expenditure** of the general government will be adjusted upward by:

- the excess of one-off revenues over programmed amounts, up to a maximum of lek 3 billion. One-off revenues are defined as revenues that accrue only in the current year (e.g., one-time fees from mobile operators). The programmed amount of one-off revenues is zero for 2015 and 2016.
- the excess of project grants over the programmed amount, up to a maximum of lek 15 billion in a given year. The programmed amount of project grants is lek 5.9 billion for August 2015, lek 10 billion for December 2015, and lek 2.55 billion for April 2016.

D. Cumulative Ceiling on the Increase of Bank of Albania Credit to the General Government

Definitions

18. **Credit of the central bank to the general government** is defined as outstanding claims of the Bank of Albania on the general government, including overdrafts, direct credit, and holdings of government securities excluding repo operations, advance distribution of profits, other technical receivables, and holdings of the Bank of Albania pension fund. For the purpose of this target, government securities will be valued at their original purchase price.

Reporting

19. Data will be provided by the BoA to the Fund on a monthly basis with a lag of no more than fifteen days.

Continuous Performance Criteria

A. Accumulation of New External Payment Arrears by the General Government

Definitions

20. External **debt** is determined according to the residency criterion. The term "debt"[3] will be understood to mean a current, i.e., not contingent, liability, created under a contractual arrangement through the provision of value in the form of assets (including currency) or services, and which requires the obligor to make one or more payments in the form of assets (including currency) or services, at some future point(s) in time. These payments will discharge the principal and/or interest liabilities incurred under the contract. Debt can take a number of forms, the primary ones being as follows:

- loans, i.e., advances of money to the obligor by the lender made on the basis of an undertaking that the obligor will repay the funds in the future (including deposits, bonds, debentures, commercial loans and buyers' credits) and temporary exchanges of assets that are equivalent to fully collateralized loans under which the obligor is required to repay the funds, and usually pay interest, by repurchasing the collateral from the buyer in the future (such as repurchase agreements and official swap arrangements);
- suppliers' credits, i.e., contracts where the supplier permits the obligor to defer payments until sometime after the date on which the goods are delivered or services are provided; and

[3] As defined in Guidelines on Performance Criteria with Respect to External Debt in Fund Arrangements, Decision No. 6230-(79/140), as amended.

- leases, i.e., arrangements under which property is provided which the lessee has the right to use for one or more specified period(s) of time that are usually shorter than the total expected service life of the property. For the purpose of the program, the debt is the present value (at the inception of the lease) of all lease payments expected to be made during the period of the agreement excluding those payments that cover the operation, repair, or maintenance of the property.

21. Under the definition of debt set out above, arrears, penalties, and judicially awarded damages arising from the failure to make payment under a contractual obligation that constitutes debt are debt. Failure to make payment on an obligation that is not considered debt under this definition (e.g., payment on delivery) will not give rise to debt.

22. Under the definition of debt set out above, external payments arrears consist of arrears of external debt obligations (principal and interest) falling due after the due date and grace period, as specified in the contract, has passed. Arrears resulting from nonpayment of debt service for which a clearance framework has been agreed or a rescheduling agreement is being sought are excluded from this definition.

23. The external arrears of the general government will be calculated based on the schedule of external payments obligations reported by the MoF. Data on external arrears will be reconciled with the relevant creditors, and any necessary adjustments will be incorporated in these targets as they occur.

24. This performance criterion does not cover arrears on trade credits and will apply on a continuous basis.

Reporting

25. The MoF will provide the final data on the external arrears of the general government to the Fund, with a lag of not more than two weeks after each month.

Adjustor

26. The performance criterion on the accumulation of new external payment arrears by the general government will exclude any arrears relating to obligations prior to 2014 which existed prior to the program but are now recognized.

Inflation Consultation

27. The triannual consultation bands apply to the 12-month rate of inflation in consumer prices as measured by the headline consumer price index (CPI) published by the INSTAT. Should the observed year-on-year rate of CPI inflation (4-month average) fall outside the outer bands, the authorities will complete a consultation with the IMF on their proposed policy response before requesting further purchases under the program. In addition, the BoA will conduct discussions with IMF staff should the observed year-on-year rate of CPI inflation (4-month average) fall outside the inner bands specified for the end of each quarter.

Indicative Targets

A. Ceiling on Subsidies to the Energy Sector

Definition

28. Subsidies **to the energy sector** are defined as new guarantees issued by the general government for the benefit of the electricity operators KESH, OST, and OSHEE, excluding rollover.

Reporting

29. Data will be provided to the Fund by the Ministry of Finance on a monthly basis with a lag of no more than thirty days.

B. Ceiling on Average Distribution Losses by OSHEE

Definition

30. **Average distribution losses** are defined as the difference between total electricity entering the distribution system and the amount of electricity billed to consumers by OSHEE, the energy distribution company, as a share of the total amount of electricity entering the distribution system. These are measured on a cumulative basis for each calendar year.

Reporting

31. Data will be provided to the Fund by the Ministry of Energy on a monthly basis with a lag of no more than thirty days.

C. Ceiling on Contracting of Nonenergy Guarantees

Definition

32. **Nonenergy guarantees** are defined as new guarantees issued by the general government, excluding those issued for the benefit of the electricity operators KESH, OST, and OSHEE.

Reporting

33. Data will be provided to the Fund by the Ministry of Finance on a monthly basis with a lag of no more than thirty days.

D. Ceiling on Accumulation of Central Government Domestic Arrears

Definition

34. Central **government domestic arrears** consist of domestic expenditure arrears of the central government and domestic tax refund arrears. Domestic expenditure arrears are defined as payments to residents determined by contractual agreements that remain unpaid 30 days after the due date specified by the contract, or, in the absence of a contractual definition, as determined by law.

35. Domestic **tax refund arrears** are defined as obligations on any valid tax refund claims in accordance with tax legislation that remain unpaid 60 days after the claim is submitted.

36. For the purpose of this target, the accumulation of domestic arrears will be monitored through MoF's triannual survey on arrears accumulation. The recording of invoices and tax refund claims should be cumulative, that is, the recording in each quarter should include all invoices/refund claims that have not been paid from the previous quarters, starting with 2014:Q1. The MoF should verify that the invoices/refunded claims reported in the survey are not already included in the arrears clearance database.

Reporting

37. The MoF should send to the Fund the consolidated data from the survey with a lag of no more than 75 days after each quarter.

E. Floor on the Clearance of Central Government Domestic Arrears

Definitions

38. **Central government domestic arrears** consist of domestic expenditure arrears of the central government and domestic tax refund arrears. Domestic expenditure arrears are defined as payments to residents determined by contractual agreements that remain unpaid 30 days after the due date specified by the contract, or, in the absence of a contractual definition, as determined by law. Domestic tax refund arrears are defined as obligations on any valid tax refund claims in accordance with tax legislation that remain unpaid 60 days after the claim is submitted. For the purpose of this target, domestic arrears consist of arrears submitted before December 31, 2013, that fall into the following categories:

- central government contracts;
- central government utility bills;
- disability benefits from social assistance programs;
- special funds, including payments for ex-persecuted prisoners and expropriations related to public construction works, and other special payments approved by the Council of Ministers;
- court orders, excluding cases in land restitution and compensation;
- local government contracts financed by central government;
- child registration subsidies;
- civil emergency;
- VAT refunds; and
- CIT returns.

39. Data will be collected through payments made under the arrears clearance strategy through the Treasury system.

Reporting

40. Data will be provided by the MoF to the Fund with a lag of no more than four weeks after the test date.

Structural Benchmarks

41. Publish a report on arrears paid (on a quarterly basis) on the MoF website (starting in June 2014). The report should be published within 60 days from the end of each quarter.

42. MoF to publish triannual survey results on new arrears accumulation in ten key ministries and GDT. The ministries covered are Transportation, Health, Education, Defense, Justice, Interior, Agriculture, Finance, Economy, and Social Welfare. The survey should be published within 75 days from the end of each trimester.

43. Roll out the AGFIS to 15 budget institutions (60 percent of budget). The 15 budget institutions are as follows: Council of Ministers, Ministry of Transport and Infrastructure, Road Authority, Ministry of Finance, National Agency of Information Society, Municipality of Tirana, Ministry of Welfare, Ministry of Education, Ministry of Agriculture, Agricultural and Rural Development Agency, Ministry of Health, Ministry of Interior, Ministry of Justice, Ministry of Defense, and Ministry of Energy.

44. In agreement with BoA and Albanian Financial Supervisory Authority (AFSA), amend the regulatory framework for investment funds on asset valuation and liquidity requirements. The amended regulations should:

a) require that the calculation of the unit value represent the proportionate share of the aggregate market value of the underlying assets of the fund; and
b) introduce liquidity requirements consistent with recent E.U. regulatory developments and the current level of development of the Albanian market.

45. Prepare a quarterly survey of the gross consolidated arrears of the electricity sector to the private sector. The survey should be prepared within 15 days from the end of each quarter.

Monitoring and Reporting Requirements

46. To facilitate the monitoring of program performance, the authorities will provide the following information on a monthly basis (except where noted).

The Bank of Albania will supply to the Fund:

i) the balance sheets of the Bank of Albania;
ii) the consolidated accounts of, separately, the commercial banks and the Savings and Loan Institutions (SLIs);
(iii) the monetary survey;
(iv) banking sector prudential indicators;
(v) the net foreign assets of the Bank of Albania and their components;
(vi) comprehensive information on reserve assets that are pledged, collateralized, or otherwise encumbered;
(vii) the foreign exchange cash flow of the Bank of Albania, including the level of NIR;
(viii) daily average exchange rates;
(ix) quarterly balance of payments data and updates of balance of payments estimates;
(x) inflation forecasts on a monthly basis; and

(xi) data on government deposits and net domestic financing.

The Ministry of Finance will supply to the Fund:

(i) the summary monthly fiscal table, including the overall budget deficit, on a modified cash basis;

(ii) issuance of treasury bills and bonds by the MoF, including gross value and cash received;

(iii) privatization receipts;

(iv) information on the contracting and guaranteeing of new debt;

(v) information on the stock of short-, medium- and long-term debt;

(vi) information on official grants for projects or budget support purposes;

(vii) information on the stock of expenditure arrears identified in the Arrears Prevention and Clearance Strategy, and progress in arrears repayment;

(viii) information on the accumulation of new arrears in central government ministries;

(ix) information on the implementation of stronger procurement and commitment controls;

(x) information on energy and non-energy guarantees issued by the general government, including on new issuance, drawings, repayments (called and non-called), interest (called and non-called), late returned principal and interest separately for domestic and external as well as energy and non-energy guarantees; and

(xi) monthly local government spending (esp. conditional and unconditional grants).

The General Directorate of Customs will supply to the Fund:

(i) detailed monthly data on customs revenues collected.

The General Directorate of Taxation will supply to the Fund:

(i) detailed monthly data on tax revenues collected;

(ii) information on progress in implementing business restructuring and IT reforms; and

(iii) information on the stock of VAT refunds claimed, refund arrears, and refunds paid out.

The Albanian Statistical Agency (INSTAT) will supply to the Fund:

(i) the consumer price index (CPI index) at the aggregated level and at the level of each individual item making up the basket;

(ii) the producer price index;

(iii) the construction cost index;

(iv) all short term indicators as they become available, as defined in INSTAT's quarterly publication "Conjoncture"; and

(v) preliminary estimates for quarterly GDP and preliminary estimates for annual GDP disaggregated by 22 sectors and distinguishing between the observed and unobserved economy.

ALBANIA

May 4, 2015

FOURTH REVIEW UNDER THE EXTENDED ARRANGEMENT AND REQUEST FOR MODIFICATION AND WAIVER OF APPLICABILITY OF PERFORMANCE CRITERIA—SUPPLEMENTARY INFORMATION

Prepared By European Department

This supplement provides information that has become available since the Staff Report was circulated to the Executive Board on April 29, 2015. The information does not alter the thrust of the staff appraisal.

The final structural benchmark for this review has been implemented on time. The external auditor for arrears payments on tax refunds has completed its work before the end-April deadline. Overall, the auditor's assessment is that so far refunds have been conducted in compliance with the laws and the government's Arrears Clearance and Prevention Strategy (ACPS). An updated table is attached.

Table 2a. Albania: Structural Benchmarks for the April 2015 Test Date under the EFF Arrangement

Structural Benchmarks	Test Date	Status	Remarks
I. Public Financial Management			
1. Publish a report on arrears paid (on a quarterly basis) on the MoF website (starting in June 2014).	Continuous	Met.	
2. MoF to report quarterly survey results on new arrears accumulation among five key ministries (Transportation, Health, Education, Defense, and Justice) and GDT.	Continuous	Met.	
3. MoF to expand the reporting of quarterly survey on arrears accumulation to five additional ministries (Interior, Agriculture, Finance, Economy, and Social Welfare) (starting with the period from October–December 2014) and publish it on the MoF's website.	Continuous	Met with a delay.	
4. The MoF to prepare and publish an action plan with measures to address weaknesses identified in the auditor's report on non-tax claims payments.	Feb. 15, 2015	Met with a delay.	
5. External auditor to complete the audit of 75 percent of outstanding non-tax claims paid through January 2015.	End-Apr. 2015	Met.	
6. External auditor to complete verification of arrears payments on tax refunds.	End-Apr. 2015	Met.	
II. Tax Administration			
7. Establish and commence operations of a permanent Risk Management Unit (RMU) in GDT (see TMU).	End-March 2015	Met.	
8. Install the new IT software at the central server site (NAIS) and commence testing.	End-Feb. 2015	Met.	
9. The GDT to develop a corporate strategy for medium to long-term capacity building.	End-Mar. 2015	Met.	
III. Financial Sector			
10. Hire an external expert to assist the Audit Committee of the Bank of Albania.	End-Feb. 2015	Not met.	In progress, expected to be met by end-May.
IV. Energy Sector			
11. Prepare a quarterly survey of the gross consolidated arrears of the electricity sector (KESH, OST, OSHEE) to the private sector (starting with the period January–March 2015).	Continuous	Met.	

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COMMUNICATIONS DEPARTMENT

Press Release No. 15/222
FOR IMMEDIATE RELEASE
May 14, 2015

International Monetary Fund
Washington, D.C. 20431 USA

IMF Executive Board Completes Fourth Review of Albania's EFF and Approves €36 Million Disbursement

The Executive Board of the International Monetary Fund (IMF) yesterday completed the fourth review of Albania's economic performance under the Extended-Fund Facility (EFF). Completion of the review enables an immediate disbursement of SDR 28.88 million (about €35.9 million), bringing the total disbursements to SDR 123.1 million (about €153.1 million). The decision was taken without a formal meeting[1].

All end-December 2014 and continuous performance criteria were met, with comfortable margins. All but one structural benchmarks were implemented.

Economic recovery is underway in Albania, but growth remains below potential. High non-performing loans (NPLs) make banks risk-averse, and credit growth remains sluggish despite monetary easing. Program risks emanate from external disinflationary pressures, the complexity of electricity sector reforms, and the need for sustained political commitment to fiscal adjustment.

The authorities should shield the 2015 budget deficit target from the risk of falling oil royalties and external disinflationary pressures. Reducing public debt over the medium term will require political commitment to sustain the significant fiscal consolidation which began in 2014. The central bank's cautious monetary easing is broadly appropriate. Addressing the high stock of NPLs is crucial for reviving credit. The micro-prudential focus on the fastest-growing segments of the banking system is appropriate. Regulatory gaps in nonbank supervision should be filled promptly. While the early results from the authorities' ambitious power sector reform have been impressive, sustaining the effort is critical.

The Executive Board approved a 36-month arrangement under the EFF for Albania on February 28, 2014 (see Press Release No. 14/81) in an amount equivalent to SDR 295.42 million (about €367.5 million, 492.4 percent of the country's quota in the Fund).

[1] The Executive Board takes decisions under its lapse-of-time procedures when it is agreed by the Board that a proposal can be considered without convening formal discussions.