

Westin: We're leaving, be careful with the taxes

Interview by Eltion Hoxha

The Resident Representative of the IMF in Albania, Ann-Margret Westin, speaks for "Shekulli" on the domestic developments

"The IMF would have wanted more progress over the years in tax administration. A more prudent fiscal policy is warranted in 2009"

The IMF Resident Representative in Albania comments on the sectors that will be affected by the crisis

IMF: "Where the global crisis will hit

"Our projections for 2009 growth is 3.5-4%. If credit increases, it could be more than 4%"

Status

We will keep giving advice on economic policy, the key differences from the current program mode is that we will have less frequent interaction with Albania and, in the absence of a program, we will have less of a say in economic policy making.

The Crisis

The advice

Given the current global financial crisis, it is more important than ever that the government pursues sound macroeconomic policies. The message we are trying to convey at this juncture is that this is the time to err on the side of caution.

A more constrained fiscal policy in 2009 compared with 2008 will be a key part of such prudent policies. In light of the tighter financing conditions this year, we agreed with the authorities to reduce the 2009 budget deficit to below 4 percent to avoid crowding out private sector investment.

Taxes

Looking ahead, we are still looking for an anchor for fiscal policy, in absence of a Fund program; a commitment to a fiscal rule, e.g. an expenditure or deficit rule, would help strengthen fiscal discipline and reduce public debt.

Growth in 2008

Given some concerns regarding new business classifications, there are reasons to believe that the recently released QGDP estimates overestimate the true level of growth. E.g., the formalization of the economy might be reported as increased economic activity through an increase in registered VAT payments. Hence, for the moment we are maintaining our estimate of 6 percent real GDP growth in 2008.

Growth in 2009

We are also maintaining our 3.5–4 percent real growth forecast for 2009. If credit availability becomes better than we projected, growth this year might be even higher than 4 percent.

Graduation

At the same time, in the current global uncertain environment and given that this is an election year, many would argue that caution is of essence now. In fact, there are countries where the government and the opposition have come together to sign a Fund arrangement ahead of an election, in order to bolster confidence.

Albania will no longer be under the direct supervision of the IMF, but only certain parameters will be monitored. More specifically, what will the role of the IMF in Albania be starting from February?

As Albania's current 3-year PRGF/EFF arrangement with the IMF (the "Fund") now is expiring, Albania's interaction with the Fund will mainly be limited to the Article IV Consultations and to our Technical Assistance (TA) and training programs. There will of course also continue to be opportunities to meet and discuss during the Annual and Spring Meetings.

The Article IV Consultations are at the heart of IMF's surveillance activities. The IMF is mandated to oversee the international monetary system and monitor the economic and financial policies of our 185 member countries. An Article IV mission visits the country every or every other year to gather information and exchange views with government and central bank officials. We also meet with other stakeholders, such as parliamentarians and representatives of business, labor unions, and civil society. The findings of the mission are presented in a Staff Report that we submit to our Executive Board, where we highlight possible risks to stability and growth and advise on needed policy adjustments.

It is worth noting that ever since Albania joined the Fund in 1991, we have been undertaking Article IV Consultations with Albania so this is nothing new; the last such consultation took place last spring. So while we will keep giving advice on economic policy, the key differences from the current program mode is that we will have less frequent interaction with Albania and, in the absence of a program, we will have less of a say in economic policy making. Rather, we will serve as an outside advisor that periodically provides advice.

Albania will also continue to have access to TA. However, outside of a program context, Albania might have to start paying for part of this assistance in the future, given forthcoming reforms at the Fund.

1. ***Ms. Westin, the conclusion of the IMF mission in Albania has divided the public opinion in two camps: one camp demands the extension of the IMF assistance to our country and the other camp declares that Albania does not need an extended mission. Do you think that the government can function without the help of the IMF?***

First just to note that whenever there is an IMF-supported lending program it is always at the country's request. Second, our lending programs are never meant to last for forever but the aim is of course for countries to "graduate" from Fund financing at some stage. The key question, and this is a judgment call, is of course when to draw the line and move out of Fund-supported lending programs and into a pure surveillance mood.

Some countries take a more cautious approach, sticking with a pre-cautionary Fund program for a while as an insurance to foreign investors that economic policies are on track. An example is Serbia, which just signed a pre-cautionary agreement with us. Other countries emphasize that the fact that the country does not request a Fund arrangement in and of itself sends a positive signal to investors that the country has matured enough to go it alone.

Albania has come a long way and over the last program it has matured from a low-income economy to now join the club of emerging markets. In this sense, one could argue that Albania would be ready to graduate from Fund financing.

At the same time, in the current global uncertain environment and given that this is an election year, many would argue that caution is of essence now. In fact, there are countries where the government and the opposition have come together to sign a Fund arrangement ahead of an election, in order to bolster confidence.

2. ***What have been the latest advises of the IMF for the Albanian government?***

Given the current global financial crisis, it is more important than ever that the government pursues sound macroeconomic policies. The message we are trying to convey at this juncture is that this is the time to err on the side of caution. A more constrained fiscal policy in 2009 compared with 2008 will be a key part of such prudent policies. In particular, in light of the tighter financing conditions this year, we agreed with the authorities to reduce the 2009 budget deficit to below 4 percent to avoid crowding out private sector investment. (The approved Budget Law stipulates a deficit of 4.2 percent of GDP; however, given known lags in capital spending implementation, we expect the end-year deficit at around 3.9 percent.) Also, with expenditure contingencies of almost 2 percent of GDP, the budget contains a

significant buffer. In the financial sector, the Bank of Albania (BoA) will need to continue its very able work in banking supervision and high-frequency monitoring.

3. ***Will the global crisis affect Albania, and if yes, what will be the most exposed sectors?***

The fact that the Albanian economy and financial system still are not completely integrated with the rest of the global economy has provided some buffer from the global financial credit crisis. The Albanian banking system had no direct exposure to the “toxic” instruments that were at the root of the credit crisis in the United States. However, almost all banks are foreign-owned and as parent banks in home countries might have been more affected by the global credit crisis, they have in turn made less funds available for their Albanian subsidiaries or branches. Hence, we would expect a slowdown in credit expansion, as banks get more cautious.

The Albanian economy will mainly be affected by the global economic downturn through a decline in export demand, investment, remittances, and, as mentioned, less availability of credit. Export demand might in particular hurt the re-exporting industry in shoes and clothing but other sectors will also be affected. Meanwhile, remittances have been key to boost household incomes and have been particularly important as a safeguard for the poorest households.

4. ***Ms Westin, if one makes a balance of the cooperation of the IMF with Albania, what could have been done better and what could not be achieved?***

First, just to say that a great success of Albania is the macroeconomic stability that has been achieved over the last several years, with high sustainable growth and low and stable inflation. This is an achievement of the Albanian authorities, i.e. the current and previous governments as well as the BoA, in collaboration with us.

Now, focusing on areas where we would have liked to see more progress, let me mention tax administration. Reforms now finally seem to be truly taking off at the General Department of Taxation, in large part helped by the Millennium Challenge Threshold Account and TA provided by us. We very much welcome these recent developments, as acknowledged by the latest TA mission last fall; at the same time, one would have hoped for more progress also in earlier years, given the significant amount of TA provided in this area not only by us but also by other donors.

Looking ahead, we are still looking for an anchor for fiscal policy, in absence of a Fund program; a commitment to a fiscal rule, e.g. an expenditure or deficit rule, would help strengthen fiscal discipline and reduce public debt.

5. *There has been much debate recently on growth. The IMF maintains its November projections for an annual growth of 6%. The PM refers to INSTAT for a quarterly GDP growth of 9,9% and the MoF has a projection of 7-8%. Do you think this debate is essential and how important is the projection of this figure?*

First, just to say that we very much welcome INSTAT's production of QGDP estimates and that we are happy to have been able to support this process through a TA expert.

The QGDP estimates are based on a subset of quarterly economic variables and are by definition less complete than annual GDP estimates. Their purpose is to give a more timely indication than the annual GDP estimates of where the economy is heading. The recently released QGDP estimates are the first of their kind and subject to further revisions. In particular, given some concerns regarding new business classifications, there are reasons to believe that the recently released QGDP estimates overestimate the true level of growth. E.g., the formalization of the economy might be reported as increased economic activity through an increase in registered VAT payments.

Hence, for the moment we are maintaining our estimate of 6 percent real GDP growth in 2008. While growth was stronger than predicted in the first half of the year, the current global economic slowdown will mainly impact growth in the fourth quarter, i.e., the last three months of 2008, and in 2009; in fact, already the third quarter of 2008 showed weakness compared with the first half of the year. We are also maintaining our 3.5–4 percent real growth forecast for 2009. If credit availability becomes better than we projected, growth this year might be even higher than 4 percent.

It is worth pointing out that these projections still point to very solid growth in Albania, in particular if you compare with other countries in the world and in the region. In our World Economic Outlook Update of November 2008, the growth rates for 2008–09 for virtually all countries in the world were revised downward. Also, our 3.7 percent 2009 growth forecast for Albania should be compared with the 2.5 percent average growth rate projected for Central and Eastern Europe for 2009.

A good understanding of the level and growth rate of GDP is of course essential for policy making and economic analysis. Looking ahead, as official data in Albania keeps improving through further refinements in methodology, better use of already existing official data sources, and the creation of new data sources, one would expect less of a debate on historical GDP numbers and growth projections. In particular, while I would expect more projections to become available as also the key private financial institutions, in particular the largest banks, start providing their own macroeconomic projections, I would also expect a convergence in the different growth forecasts.