

## ■ ALBANIA

# Poverty in a prolonged transition



Albania remains one of the poorest countries in Europe despite progress with transition reforms initiated in the early 1990s after 45 years of communist rule, and its significant cumulative growth - among the highest of all transition economies.

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### Economic growth - a success story

In 1991 Albania left behind 45 years of communism and set forth as a democratic country. After 14 years of transition the country has a stabilized market economy that has grown significantly. However it remains one of the poorest countries in Europe and its GDP per capita in 2003 represented only 6.5% of the European Union (EU) average.<sup>1</sup> Albania has attracted only modest amounts of foreign direct investment (FDI) compared to other South-eastern European countries. At the end of 2004, cumulative FDI was approximately USD 1.3 billion. The informal sector makes up a large part of the economy with its contribution to gross domestic product (GDP) estimated at 25%.<sup>2</sup> Bank credit to the private sector is one of the lowest among transition economies. The Government's weak revenue collection system forces it to cut back on investment spending. Trade continues to be largely dominated by imports with the value of exports remaining at one-fifth the value of imports. In agricultural production, which is a key contributor to growth, this ratio is one to ten. As a result there are many concerns about the extent to which macro-economic measures have contributed to the real development of the country and the degree to which growth rates experienced to date will continue in the future.

Rapid economic growth, considered by the Government and by international institutions to be an impressive success model among the transition economies,<sup>3</sup> was the result of private sector-driven reforms initiated in 1991.<sup>4</sup> After a significant decline in production during the initial transition phase the economy grew by an average annual rate of 7%

to 8%.<sup>5</sup> The real GDP per capita increased from USD 680 in 1990 to approximately USD 1,938 in 2003. Inflation fell sharply from a monthly rate of 10% to 15% in 1992 (annual 120% to 180%) to an annual average rate of 6% in 1995. All agricultural land was distributed to farmers, the privatization of almost all state-owned enterprises was completed (at present a few strategic enterprises are in the process of being privatized), price controls were abolished, and trade and payment regimes were liberalized. Improved revenue collection and the application of a hard budget constraint consolidated the financial sector. As a result, the current account deficit decreased sharply from 60% of GDP in 1991 to 7.6% in 2003. The old socialist banking system has been totally transformed. The state-owned banks have been privatized and new private domestic and foreign banks have been licensed. In addition, the high volume of remittances (USD 400 million annually on average) is an important factor for economic growth.<sup>6</sup> In 2003 remittances constituted about 14% of GDP.

The positive trend which characterized the period after 1993 was reversed during 1997 as a result of the collapse of financial pyramid schemes which attracted large volumes of funds from private deposits, especially from remittances. However confidence in the economy was restored by the successful implementation of an ambitious stabilization programme which started in 1998. During the last five years, inflation has been kept under control at an annual average rate of 3.3%.

### “Surprised” by poverty

Albanians today enjoy more freedom and democracy and their hope is to shorten the transition period during which the country transforms itself from an emerging state to an EU member state. Albanian laws and regulations are increasingly being approximated to EU standards. However in an environment dominated by very low economic and social development levels, implementation remains problematic.

The poverty headcount rate in 2002 was 25.4% and average consumption was approximately ALL 7,800 (USD 79) per capita per month. When the poverty line is estimated at ALL 4,891 (USD 49.56)

per capita per month and the extreme poverty line at ALL 3,047 (USD 30.87) per capita per month, one quarter of Albanians are considered poor and about 5% of the population is estimated to be unable to meet basic food requirements. Poverty is higher in rural and especially in mountainous areas, at 29.6% and 44.5% respectively. This is mainly due to the limited incomes generated by small, fragmented<sup>7</sup> agriculture holdings (four to five plots per farm on average); an underdeveloped land market; very traditional methods of agricultural production; and poor transportation access to markets. Poverty is present throughout the country but the Northern regions are most affected with about 43% of the population in Dibra, 40% in Kukes, 37% in Lezha and 33% in the Shkodra region currently living below the poverty line.<sup>8</sup>

Unemployment is a chronic problem aggravated by the geographic concentration of businesses in the country and by their small size. In 2004 about 82.7% of all active enterprises were located in the capital Tirana and six other major districts. The remaining 17.3% were located in the other 29 districts. In addition about 84% of active enterprises are very small with only one employee.<sup>9</sup> The very optimistic figure of 14.65% unemployment<sup>10</sup> reported at the end of 2004 was calculated using the number of unemployed people in urban areas but it was meant to represent both the urban and rural workforce. In fact, the rural workforce, which represents about 46% of the total active population, is significantly underemployed. As a result, national unemployment is much higher than reported. Considering the size of the active labour force the average national unemployment rate corresponds to 47%, with this figure surpassing 50% in many districts. For example, in June 2004 the active labour force numbered 6,300 in the Dibra district while there were 3,517 registered unemployed job seekers in the same region. This corresponds to an unemployment

1 World Bank, *Albania-Sustaining Growth Beyond Transition*. 2004, p. 1.

2 Organisation for Economic Co-operation and Development (OECD), *Tackling the policy challenge of dealing with informal economy in Albania*. 2004, p. 10.

3 The World Bank, *op cit*.

4 Albania inherited from the communist regime a very centralized and collectivized economy, the absence of ownership rights and a very strict price control regime.

5 The macroeconomic data refer to Instituti i Statistikës (INSTAT - Institute of Statistics), annual publications.

6 After 1990, more than one-fourth of the total population of the country emigrated mainly to Greece and Italy.

7 The average farm size is 1.1 hectares.

8 INSTAT, *A Profile of Poverty and Living Standards in Albania*. Tirana, 2004.

9 Foreign Investment Advisory Service (FIAS), *Administrative and Regulatory Cost Survey*. 2004, p. 12.

10 National Employment Service, *Annual Report*. Tirana, 2004, p. 4.



rate of 56%.<sup>11</sup> Employment possibilities in these districts remain very limited due to the low state of development of the private sector.

Although women represent 51% of the economically active population, their participation in the labour market compared to men remains low. At the national level, the unemployment rate in 2003 was 18.5% for women and 12.9% for men. In almost all cities employment opportunities for women are approximately half that which exist for men. While women make up 40% of those employed in the central government administration, they represent only 24% of department heads, 9% of vice-ministers, 5% of ministers, and less than 6% of members of Parliament. No woman is the head of any parliamentary commission. In addition, women only represent 17% of business managers in the private sector.<sup>12</sup>

Various non-income dimensions of poverty and deprivation greatly aggravate the income poverty factors mentioned above. Access to basic services is very low especially in rural areas. At the national level, in 2002, 68% of the population had access to piped water inside their dwelling, but in rural areas the proportion was only 46%.<sup>13</sup>

The education system must continue to operate with run-down and often inadequate facilities, under-qualified teachers and outdated curricula. This situation has been further complicated by rural-urban migration and low teacher motivation. As a result the illiteracy rate in 2002 stood at about 10.3% (in the population aged 18 and above) when illiteracy had been completely eradicated during the communist regime. It is estimated that there is a "hidden" dropout rate of 10% in rural areas due to the practice of combining classes of different levels. Secondary school attendance rates vary drastically between urban and rural areas where the enrolment ratios are 48% and 22% respectively.

The quality and availability of health services is also very low and the sector suffers from poor infrastructure, lack of technology at all levels of care and low motivation of its qualified staff. Currently the health services operation cost per person is about USD 50 compared to the EU average of USD 1,900.

The transition experience shows that significant economic growth and impressive macro-economic indicators are not sufficient to improve income and ensure equity in human development

across the country. The very slow effects of the macro-economic growth approach in human development "surprised" the Government. Although poverty was evident since the beginning of transition, the first poverty reduction strategy<sup>14</sup> was drawn up only in 2001, ten years after the collapse of the communist regime. The recommendations of the national Millennium Development Goals (MDG) report<sup>15</sup> and the *Human Development Report*<sup>16</sup> further sensitized decision-makers and the general public to consider a more spatially-oriented approach to transition. Consequently a local development dimension began to be articulated in the National Strategy for Social and Economic Development (NSSED) and the national MDG targets and indicators were disaggregated at a regional level.

### Financing development

The NSSED represents the principal programming document in Albania: it optimistically harmonizes priority interventions with some policy objectives and targets, considering both the MDGs and EU integration. Its aim is to alleviate poverty and to narrow the large economic and social gap between Albania and the EU. Some of the main objectives for 2015 include doubling the nominal GDP per capita; reducing by half the current rate of absolute poverty and eliminating extreme poverty; reaching an enrolment rate of 100% in basic education and 90% in secondary education; ensuring that children complete at least 13.5 years of education; and ensuring full access to better quality health services. Recent assessments show that there is a good chance that Albania will achieve these objectives. However in order for this to happen, improved policies, stronger institutions and additional local and international financial resources are required.<sup>17</sup>

In the absence of long-term expenditure programmes it is difficult to provide a cost estimate for achieving the above objectives. Nevertheless they represent important financial requirements. In the health sector, for instance, the share of annual financing by the state budget needs to be tripled in order to reach the actual average level of financing in South-eastern European countries. These expenditures are conditioned to a substantial increase in state budget revenues through the removal of multiple administrative barriers to investments; the support of a pro-active private sector development strat-

egy export- and productivity-oriented; and the expansion of access to international trade through an increase in the quality and quantity of human capital. Additional international financing is also needed. The aspiration that Albania exceeds the threshold to qualify for international development agencies' resources by 2005 (based on the successful economic growth) seems too unrealistic and risks prolonging further the transition period. In turn, this will negatively impact the country's efforts to address the root causes of poverty, the achievement of the MDGs and integration with the EU. It is now almost certain that the longer the transition period continues and the greater Albania-EU disparities are, the greater the cost of EU integration will be.

The financial contribution of international donors continues to be essential to Albania's progress. However the quality of foreign aid is being taken into consideration less and less by Albanian authorities and international donors. At present there is evidence of overlapping interventions, while the efficiency of some programmes is questionable, and there is a clear tendency for priority to be given to technical assistance over development investment support programs. An effective donor coordination mechanism is also lacking. There is a large number of projects underway which are based on various aid policies and have different management approaches. This splinters assistance into multiple high-cost management units and bypasses administration. A large number of project management and project implementation units function in parallel with the local public administration. Very often central administration, local authorities, local and foreign non-governmental organizations, and donor agencies independently run parallel projects in the same location. There is a need for the Albanian authorities and international donors to coordinate their efforts and align them with NSSED priorities, and to better harmonize their financing with the State budget requirement at least for investment projects. They must also adopt a common results-based management approach and transfer project management responsibilities, step-by-step, to the local authorities. ■

11 Human Development Promotion Centre (HDPC), *Promoting Local Development through MDGs-Dibra Region*. Tirana, 2004, p. 18.

12 INSTAT, *Women and Men in Albania*. 2004, p. 12.

13 WHO-UNICEF, Joint Monitoring Programme for Water Supply and Sanitation, [www.wssinfo.org/en/watquery.html](http://www.wssinfo.org/en/watquery.html).

14 In Albania this is named National Strategy for Social and Economic Development (NSSED)

15 United Nations Development Programme (UNDP)/HDPC. *The Albanian Response to the Millennium Development Goals*. Tirana, 2002, pp. 15 and 57.

16 UNDP/HDPC. *National Human Development Report 2002. Challenges of Local Governance and Regional Development*, Tirana, 2003, p. 38.

17 UNDP/HDPC (2002), *op cit*, p. 8.