Executive Board Minutes 20/113-1

November 23, 2020–10:00 a.m.

Albania—First Post-Program Monitoring Discussions

Documents: EBS/20/167

Staff: Sun, EUR; Sommer, SPR

Length: 44 minutes

ISSUED: July 26, 2022
APPROVAL: August 2, 2022

CEDA OGADA
Secretary

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[1] Minutes are the official record of a formal Board meeting in which the Board may adopt decisions and reach understandings related to the business of the Fund. Staff background documents issued before the meeting are the principal basis for the meeting. Preliminary "gray" or "buff" statements by Executive Directors and staff's responses to Directors' technical questions are circulated prior to the meeting. Adopted decisions and/or summings up—the Chair's "sense of the meeting" or policy conclusions/recommendations—are issued after the meeting. The minutes include all these elements, as well as the discussion record (a verbatim transcript of the discussion lightly edited for clarity). Minutes are made public consistent with the IMF's Transparency Policy and Open Archives Policy.

THE ACTING CHAIR'S SUMMING UP

Executive Directors agreed with the thrust of the staff appraisal. They commended the Albanian authorities for maintaining macroeconomic and financial stability thus far, and welcomed their responses to support lives and livelihoods in response to the November 2019 earthquake and the COVID-19 pandemic. Albania's capacity to repay the Fund is adequate, with a sizeable reserve cover and flexible exchange rate as important shock absorbers. However, risks have risen stemming from the pandemic, elevated fiscal deficits and public debt, weaknesses in management of public finances, and a relatively high level of non-performing loans (NPLs) and euroization. Moreover, considerable uncertainty and downside risks surround the projected recovery for 2021-22. In this context, Directors emphasized the importance of contingency planning and recommended that the authorities stand ready to take further measures to preserve macroeconomic and financial stability.

Directors stressed that support for the economy needs to continue in 2021, but should be temporary and targeted, subject to transparency and accountability. They urged the authorities to regularize as soon as possible extraordinary measures in public financial management (PFM) taken during the emergency and to subject reconstruction funds to adequate PFM controls. Directors recommended that the cyclical boost to revenues be used to achieve a larger deficit reduction in 2021 than is consistent with the budget and to build a buffer for contingencies. Directors welcomed recent amendment to the fiscal rules.

Addressing structural weaknesses in public finances can better support investment in human and physical capital. A sound medium-term revenue strategy should be adopted and implemented without further delay. Frequent, ad hoc changes to tax policy and tax amnesty schemes should be avoided. Directors also stressed the need to strengthen PFM, and manage increasing fiscal risks, including from public-private partnerships and recent government guarantees. They underlined the need to prevent new arrears and continued efforts to strengthen the AML/CFT framework.

Directors underscored the need to safeguard financial stability while supporting borrowers hit by the shocks. They recommended that supervisors closely monitor and carefully manage risks, including by guiding banks' restructuring of credit portfolios. Directors supported retaining restrictions on dividend distributions to safeguard banks' capital positions. They encouraged the authorities to further improve the NPL resolution framework and align the regulatory framework with international standards.

EXECUTIVE BOARD ATTENDANCE[2]

T. Zhang, Acting Chair

Executive Directors	Alternate Executive Directors
	W. Nakunyada (AE)
	R. N'Sonde (AF)
	B. Lischinsky (AG), Temporary
	C. White (AP)
	R. Velloso (BR), Temporary
	Z. Zhang (CC)
	R. Moral Betere (CE), Temporary
L. Levonian (CO)	
D. Palotai (EC)	
A. Buisse (FF)	
	K. Merk (GR)
S. Bhalla (IN)	
D. Fanizza (IT)	
	K. Chikada (JA)
	M. El Qorchi (MD)
	P. Al-Riffai (MI), Temporary
	A. De Lannoy (NE)
	J. Sigurgeirsson (NO)
A. Mozhin (RU)	
M. Mouminah (SA)	
	F. Mochtar (ST)
P. Trabinski (SZ)	
	D. Andreicut (UK), Temporary
	R. Farber (US), Temporary

C. McDonald, Acting Secretary
S. Kalra, Summing Up Officer
R. Smith Yee, Board Operations Officer
L. Nagy-Baker, Verbatim Reporting Officer

Also Present
Communications Department: G. Vilkas. European Central Bank: K. Nikolaou, R. Rueffer. European Department: J. Decressin, S. Eble, A. Khachatryan, P. Kopyrski, M. Pinat, Y. Sun. Finance Department: L. Chidawaya. Legal Department: J. Ams, G. Jackson. Monetary and

[2] For countries in each constituency, please see the Constituency Codes in the annex.

Capital Markets Department: U. Das. Secretary's Department: B. Zhao. Strategy, Policy, and Review Department: D. Milkov, M. Sommer. World Bank Group: C. Ungerer. Executive Director: A. Andrianarivelo (AF), A. Mahasandana (ST), M. Mahmoud (MI), P. Moreno (CE), R. von Kleist (GR). Alternate Executive Director: H. Azal (EC), C. Just (EC), F. O'Brolchain (CO), O. Odonye (AE), L. Palei (RU), P. Rozan (FF). Senior Advisors to Executive Directors: K. Badsi (MD), Z. Mohammed (BR), T. Nguema-Affane (AF), T. Sitima-wina (AE), N. Thiruvenkadam (IN), M. Zhunusbekova (SZ). Advisors to Executive Directors: J. Corvalan (AG), K. Dacharux (ST), O. Diakite (AF), F. Dogan (EC), R. Edwards (CO), Rachel Lyngaas (US), T. Krahnke (GR), M. Merhi (MI), P. Mooney (CO), A. Muradov (SZ), A. Olhaye (AF), T. Persico (IT), D. Shestakov (RU), M. Shimada (JA), L. Siliva (AP), I. Skrivere (NO), Y. Yang (CC), Z. Zedginidze (NE), C. Roman (FF).

DISCUSSION RECORD[3]

The Acting Chair (Mr. Zhang):

The subject of this session is Albania, first post program monitoring. World Bank staff is also attending this session. And 20 gray statements were issued by Directors.

The Albanian authorities responded promptly to the November 2019 earthquake and the COVID-19 pandemic, and they have commendably managed to maintain macroeconomic and financial stability so far. Like many other countries in Europe, Albania is now facing a surge in infections, leading to major uncertainties and growing downside risks around the projected gradual recovery in 2021-2022. I am very pleased to see in the buff statement that Mr. Fanizza and Mr. Persico stressed the authorities' strong commitment to a sound macroeconomic framework, including fiscal and debt sustainability. I am also pleased that there is a broad agreement between the authorities and staff on the policies needed to address near- and medium-term challenges.

Mr. Fanizza:

My Albanian authorities would like to thank staff and management for the continuous policy dialogue, the emergency financial support, and the use of capacity development. I would also like to thank my Board colleagues for their support to the authorities' emergency policies and for the useful comments that our office will promptly convey.

I will focus on a few issues raised by Directors in their gray statements, but I would like to make a general point. Albania has been a success story of Fund-supported policy reforms. Following the successful completion of the Extended Fund Facility (EFF) in 2017, policy dialogue continued as the authorities managed to reduce the public-debt-to-GDP ratio to 77.5 percent at the end of 2019 with structural reforms efforts that helped to raise GDP growth to record levels for the year. The earthquake and the COVID pandemic changed the picture. The authorities expect GDP to contract substantially in 2020 and the debt to jump as a percentage of GDP because also of much-needed emergency spending.

[3] Edited for clarity.

The authorities plan to resume their consolidation efforts already in 2021 with a sizeable improvement of the primary balance in 2021 that will go on until its deficit is eliminated and the debt-to-GDP ratio is back to about 70 percent in 2022. This constitutes a remarkable effort and commitment to fiscal consolidation. I do not believe it will be useful or even credible to do more.

As regards revenue projections for 2020, my Albanian authorities have informed me that the figures for September, October, and November of this year are very encouraging, although it is a bit early for November. They believe that the budget for 2020 has managed to achieve important savings.

On debt management, the authorities have successfully tapped international financial markets to satisfy their emergency financing, but the bulk of the external debt remains towards multilateral and bilateral trade at concessional rates. Moreover, the authorities have made headway in lengthening the maturity of domestic debt. All of this should help with debt sustainability.

On emergency spending, the Ministry of Finance has allocated about 80 percent of the budgeted amount to spending units that, however, because of the COVID, could have implemented only part of this amount. There has been a significant acceleration in actual spending in the last month, and about 28 percent of the total commitments have been actually spent.

Also, on emergency funds, the authorities are monitoring closely how they are spent. The Supreme Audit Institution will publish the results of the audits of both earthquake and pandemic-related spending in 2021 and their ex post validation.

On structural reforms, I would reiterate the authorities' commitment to implementing their agenda on the path toward accession to the European Union. They have stepped up their efforts to address anti-money laundering issues, for instance, by establishing a register of beneficial owners. Also, in response to the concern raised by several Directors about the proposed tax amnesty law, I would note that the parliamentary process will take all the needed time to make sure that the law minimizes possible adverse effects. It will not be passed lightly.

On macroprudential rules that were loosened in response to the pandemic crisis, Bank of Albania plans to tighten them back in 2021, unless, of course, the second wave of the pandemic has a large impact on the conditions we would like to see. They will plan to keep the decision to restrict the distribution of dividends from commercial banks.

On the capacity to repay the Fund, the authorities are glad of staff's favorable assessment, but they would like to recall their perfect track record under the several previous arrangements. And on Fund arrangements, there were questions about the possibility of a new arrangement. In the short-term at least, the authorities do not see it and they would regard an arrangement with the Fund as a last resort possibility. They believe they should be able to manage the situation by themselves.

Finally, they want to make sure that Board knows that they will stand ready to put in place all the required measures to alleviate the impact of a second wave of contagion in the country.

The staff representative from the European Department (Ms. Sun):

I would like to thank Directors for their insightful comments and technical questions, which we have addressed in writing. My remarks will focus on broader questions about options to mitigate adverse risks, including those that may arise from delays in structural reforms. Continued close cooperation among key development partners with a clear prioritization of reforms should help to maintain focus and positive pressures towards the delivery of concrete results in Albania. In particular, the leverage of EU is high given that the EU integration process has long served as a key reform anchor in Albania. Institution building could also help to mitigate a political risk around the delivery of structural reforms.

On the risk of a more severe pandemic, staff analysis shows that larger twin deficits could arise in such an adverse scenario, which will require further adjustment and additional financing. In a baseline, we do not see a financing gap. This is the adverse scenario. In this adverse scenario, the authorities would need to target new measures to ensure adequate healthcare and social spending and identify options for budgeted reallocations and additional financing. In such an adverse scenario, one could consider a financial arrangement with the Fund. This arrangement could provide an anchor for necessary adjustment and catalyze additional financial support from others.

Ms. Andreicut:

We agree with staff's recommendations and did not issue a gray statement. We would like to highlight four brief points.

First, we welcome staff's finding that Albania's capacity to repay the Fund remains adequate under the baseline, although we take note of existing vulnerabilities, particularly the large gross financing needs. We welcome the important shock-absorbing role placed by Albania's reserve coverage, flexible exchange rate, ongoing access to international capital markets, and development partners financing.

Second, we welcome the authorities' sustained efforts to contain the pandemic and earthquake shocks. We commend the authorities for their comprehensive policy response and would like to highlight the importance of maintaining support to prevent scarring. We agree with staff that support measures should be temporary and targeted.

Third, we take note of the good shape of the banking sector and welcome progress made in aligning the domestic regularly framework with international standards. At the same time, we agree that further efforts are needed, as outlined by staff.

Finally, we encourage the authorities to continue strengthening Albania's AML/CFT framework following FATF's identification of strategic deficiencies in February this year. We also agree with staff that tax amnesty schemes should be avoided.

Mr. Velloso:

We issued a comprehensive gray statement. I will make a few points for emphasis.

First and foremost, we would like to express our sympathies to the Albanian authorities and the Albanian people. Most countries are dealing only with the effects of the global pandemic, and this is hard enough. Albania must deal not only with the pandemic but also with the consequences of last year's powerful earthquake. We, therefore, commend the authorities for their efforts in tackling these dual shocks and for broadly maintaining macroeconomic and financial stability under very challenging circumstances. We support the temporary widening of the fiscal deficit to protect lives and livelihoods. However, as we stressed in our gray statement, fiscal stimulus during this time of crisis should remain temporary, transparent, and well-focused on the needs of the most vulnerable.

As was stressed in the buff statement by Mr. Fanizza and Mr. Persico, we take positive note that the authorities intend to resume their fiscal consolidation efforts once the pandemic abates and the earthquake-related reconstruction needs are addressed. Going forward, gradual but determined fiscal consolidation will be critical to maintain public debt sustainability. In this context, we encourage the authorities to strengthen revenue mobilization and to enhance further the country's public financial management systems (PFMs), including cash and debt management. We take positive note that the banking sector is well capitalized and stable. However, non-performing loans (NPs) might increase due to the impact of the pandemic on households and businesses. The authorities should therefore continue to monitor closely the banking system with a view to detect early signs of stress and to reduce risks to financial stability.

Mr. Buisse:

I issued a gray statement, so I will limit myself to the following remarks for emphasis.

First, to acknowledge that despite the large-scale exogenous shocks that Albania faced in a short period of time, the authorities have managed to maintain macroeconomic and financial stability. They have shown responsiveness in coping with the consequences of these shocks, and I commend the reconstruction efforts after the 2019 earthquake, as well as their actions to strengthen medical care and support households and businesses in the context of the COVID-19 outbreak. I especially support the efforts to ensure transparency, accountability, and adequate PFM controls in their emergency spending.

Second, while on the short-term the use of fiscal policy is warranted to protect the economy and livelihoods, there is a need to work expeditiously on a medium-term fiscal strategy when the existing large debt stocks and significant fiscal risks highlighted in the report and the financing vulnerabilities and encourage the authorities to deepen the work on a strategy to reach their primary fiscal balance in 2023. The whole idea is to balance Albania's development needs with the need to rebuild with room for fiscal policy maneuver and limit external pressure.

Indeed, external financing requirements remain large and subject to currency risks and to the current account, and the current account is expected to widen considerably this year. Clearly outlining a policy path, in particular on the fiscal side, should help ensure successful Eurobond issuance going forward. Working on the euroization of the economy should also remain a priority in this context.

Third and finally, I would like to encourage the central bank to continue monitoring closely the financial sector. Efforts to strengthen the AML/CFT framework should continue in line with the recommendation from the Financial Action Task Force (FATF) and MONEYVAL.

Finally, on the tax amnesty law, I hope the current review by Parliament will help take into account comments from MONEYVAL, European Commission, as well as other stakeholders.

Mr. Palotai:

In addition to the gray statement, which we issued, I would only emphasize a few points.

First, on the fiscal, we would like to emphasize the weaknesses in the fiscal side and significant downside risks, which require a reprioritization in public expenditures and also strengthening of revenue mobilization to meet the much-needed spending for the most vulnerable and also to facilitate a speedier recovery on the economy. We do encourage the authorities to build on the substantial TA they have received from the Fund in revenue administration and the blueprint for tax policy that should contribute to a raising of an additional 2 or 3 percent of GDP revenue over the next five years.

Second, a valid thought-through contingency planning should be a priority, also considering the high share of PPPs, public guarantees, and high debt levels.

Third, to address the high level of NPLs, we urge the authorities to take measures, including to actively implement an insolvency framework. Strengthening bank supervision and regulation will be of utmost importance to increase market confidence and ensure financial sector health.

Finally, we regret that despite extensive TA, the public fiscal risk assessment model diagnostic tools have not generated tangible results due to data constraints and technical capacity. Does staff see a reasonable chance for improvement this year?

Mr. Nakunyada:

We issued a gray statement and would like to emphasize a few points.

First, we commend the Albanian authorities for maintaining macroeconomic stability while tackling the shocks from the COVID-19 pandemic and the aftereffects of the November 2019 earthquake. Nevertheless, we note that risks to the outlook remain, and we underscore the importance of contingency planning in view of the uncertainty around the pandemic and the trajectory of the recovery.

Second, we are encouraged that Albania's capacity to repay remains adequate despite rising risks. We draw our assurance from the sizeable reserve buffers and the flexible exchange rate that remains important as a shock absorber against external shocks.

Third, we urge the authorities to continue close monitoring of remaining pockets of vulnerability in the financial sector. That said, we are encouraged by the authorities' intensified efforts to address identified AML/CFT shortcomings, as highlighted by Mr. Fanizza this morning.

Finally, like many Directors, we view temporary targeted and transparent measures as important to support the recovery. In this regard, we view large-scale reconstruction to support the recovery process as warranted.

Mr. Corvalan:

We issued a gray statement supporting the authorities' determination to sustain macroeconomic and financial stability despite two sizeable negative shocks that hit the country and are encouraged by their swift responses to address urgent health system requirements, protect employment, and support the firms.

We take this opportunity to encourage the authorities that despite the current juncture, to accelerate major transformations identified in areas specified in the report. This policy action will counteract detrimental dynamics that may be affecting the medium-term outlook of the economy. Emphasis on revenue-based consolidation is warranted, and additional efforts to address some weaknesses in public finances through medium-term revenue strategy seems appropriate. The ability to create some room for fiscal policy maneuver in the future puts a premium on investor confidence on the good trajectory of the economy.

Mr. Mochtar:

We have issued a gray statement, so we will just make some points for emphasis.

First, we recognize the Albanian authorities have navigated the country through significant shocks, from the earthquake and pandemic on the back of the twin deficits and limited policy space. We commend their efforts, responsiveness, and resilience through these challenging times. We also take a positive note of staff assessment that Albania's financing needs are met and that their capacity to repay the Fund is adequate.

Second, although the widening fiscal deficit may be warranted in the face of the two consecutive shocks, going forward the authorities are encouraged to put priority for securing more fiscal space through consolidation and tax system enhancement, which would put fiscal sustainability on a firmer path. We take comfort in staff baseline projection that Albania's public-debt-to-GDP ratio will decline gradually over the medium-term and welcome the authorities' intention to keep the level of public debt in check.

Third, the high level of NPLs is a cause of concern and future vulnerability. To this end, we encourage close monitoring and any preparation for the future surge in NPLs, including encouraging loan restructuring and putting the existing insolvency framework into effect. Despite the early plan of action, we still find large uncertainty with regard to pandemic path. Early dealing with debt and insolvencies will help banks and allow them to support the recovery more effectively going forward. We would like to echo staff and many chairs in reiterating the importance of contingency planning against the more severe pandemic scenario.

Last but not least, we encourage the authorities to continue to address deficiencies in the AML/CFT framework. The identified areas of shortcomings should be strengthened without delay.

Ms. Moral:

We have not issued a gray statement, but we generally share the staff's appraisal and would like to emphasize only on a few issues.

First, I would like to commend Albania's authorities for their prompt response to both shocks, the devastating earthquake and the ongoing COVID-19 pandemic, which has helped to maintain Albania's macroeconomic and financial stability. While in the short-term the authorities should concentrate on containing social and economic impact of both shocks, moving forward, the government should target their efforts and start their consolidation efforts.

On the fiscal front, we would highlight the importance of continuing efforts to build a more efficient and transparent tax system. On the expenditure side, Albania needs to strengthen the efficiency, transparency, and accountability of their procurement and public investment administration. This is going to be crucial as it works hard on the reconstruction spending.

We would stress the need to be vigilant on Albania's public debt even if currently assessed as sustainable and successfully issued recently in the markets and secure other external financing lines. The structure of public debt is generally unfavorable with growing financing needs, coupled with refinancing risk and compounded by the lack of depth of the local capital market. We agree with staff on the need to further extend maturities and prepare mitigation strategies to address possible tightening of domestic financing conditions.

Mr. Farber:

The authorities took decisive measures to tackle the twin shocks of the November 2019 earthquake and COVID-19 pandemic, and we express our sympathies to the Albanian people.

We take positive note that the RFI helped free up resources and boost liquidity, enabling the authorities to better tackle these twin shocks. We welcome the authorities' intention to resume their fiscal consolidation efforts once the COVID-19 emergency is over and earthquake reconstruction needs have been addressed, as highlighted in Mr. Fanizza and Mr. Persico's buff statement. In the meantime, we encourage the authorities to create the fiscal space required to protect the most vulnerable, contain nonpriority spending, and improve expenditure efficiency, particularly given the recent rise in COVID-19 cases.

As many Executive Directors have highlighted in their gray statements, the authorities' implementation of a medium-term revenue strategy in 2021 will help underpin the return to fiscal consolidation. We also urge their continued focus on reforms to public investment management and governance, including by following through on their commitment to conduct and publish an audit of earthquake- and pandemic-related spending in 2021.

Finally, we encourage staff and the authorities to continue monitoring risks in the banking system. The full impact of these crises has not yet materialized on bank balance sheets.

The staff representative from the European Department (Ms. Sun):

There is only one follow-up question regarding the management of fiscal risks. We certainly hope reform momentum will pick up after general elections scheduled for next April. In the meantime, we have been laying down the groundwork with follow-up technical assistance (TA) in several areas. This year, we have delivered technical assistance both remotely and TA missions, regarding management of government guarantees and also continued technical assistance on tax administrations. We also provided assistance regarding how to strengthen cash management and improving coordination on debt and liquidity management.

Mr. Fanizza:

I would like to thank my colleagues for their insightful comments and for their support and will relay the comments to my Albanian authorities. And, again, thanks also to management and staff.

The Chair adjourned the discussion.

ANNEX

- Staff's Statement
- Gray Statements
- Staff's Responses to Executive Director's Technical Questions
- Constituency Codes

BUFF/20/22

November 18, 2020

Statement by the Staff Representative on Albania
Executive Board Meeting
November 23, 2020

This statement provides information that became available after the staff report was issued on November 6, 2020. The thrust of the staff appraisal remains unchanged.

1. **The authorities have recently tightened restrictions in the face of a surge of infections.** The 7-day average of daily new cases per million people rose to 184 as of November 17th. But a low test rate and a high test positivity rate (around 25 percent) mean that the true spread cannot be gauged with good confidence. Several nationwide restrictions went into effect on November 11th and will last for at least three weeks, including a night curfew (10pm-6am) allowing only movements for health emergency and essential needs. Additional measures were announced on November 17th to limit social and political gatherings. The scale of the restrictions announced so far is much milder than the spring lockdown. But given the fluid situation, the authorities are reviewing measures on an ongoing basis.

2. **On November 16th the Parliament approved the 2021 budget with a headline deficit of 6.5 percent of GDP, as in the staff report.** Major changes to the draft submitted to the Parliament include an additional allocation to the COVID health spending (Lek1.2 billion or 0.07 percent of GDP) and a temporary increase of unemployment and social assistance payments (Lek2.5 billion or 0.15 percent of GDP). Financing of the additional spending is provided by increasing the already optimistic tax revenue projection in the budget. Staff now expects the 2021 deficit to reach 6.3 percent of GDP, slightly higher than the 6.1 percent of GDP in the staff report.

DOCUMENT OF INTERNATIONAL MONETARY FUND AND FOR OFFICIAL USE ONLY

BUFF/ED/20/155

November 19, 2020

Statement by Mr. Fanizza and Mr. Persico on Albania
Executive Board Meeting 20/113
November 23, 2020

I. Introduction

On behalf of our Albanian authorities, we would like to thank very much both staff and management for the constructive policy dialogue following the request for a purchase under the RFI. Fund's support greatly facilitated their response to both the November 2019 earthquake, and the COVID-19 pandemic.

When impacted by these two shocks, the Albanian economy had set on a stable growth path, with growth projected at the time to continue at 3 percent in 2020. The devastating earthquake and the ongoing COVID-19 pandemic radically changed the outlook. The earthquake caused damage estimated close to 7 percent of GDP. The authorities had to pause their reconstruction efforts to contain the COVID-19 outbreak, and they quickly acted to support the affected households and businesses with good results that suggest a recovery will start to materialize in 2021.

The authorities have followed a flexible approach in response to emergency needs but have paid attention to keep a sound macroeconomic framework as a basis for an economic rebound once the emergency is over. Despite the challenging conditions, the authorities aim at lowering the fiscal deficit in 2021 and bringing the debt-to-GDP ratio soon on a downward path. The country's financing needs are fully met and the country's capacity to repay the Fund is adequate. The monetary policy accommodative stance remains appropriate and is complemented by targeted macro-prudential stimulus. Furthermore, Bank of Albania (BoA) expects a gradual increase towards its 3 percent target by end 2022. Financial markets are calm, and the banking sector is liquid and sound. BoA is looking forward for a gradual normalization and stand ready to respond, even considering unconventional measures, in case downside risks materialize.

II. The Outlook

The measures adopted to limit the spread of the COVID-19 pandemic have affected both aggregate production and demand starting from Q1-2020. From the production side, construction, manufacturing, mining and quarrying, as well as services, accounted for the largest negative contributions. From the demand side, the fall in GDP is mostly attributed to the decrease in private investment and private consumption. The Albanian authorities project growth to rebound in 2021 (5 percent) from the expected fall in 2020, broadly in line with the staff's projections, as a result in part of a run-up of reconstruction efforts.

There have been encouraging signs from in-land tourism inflows, which may partially offset the drop of in-flight in 2021 and help to bring the deficit of the external current accounts to 7 percent of GDP in 2021, down from 9 percent in 2020. The external reserve position is expected to remain comfortable, partially reflecting the successful placement of the Eurobond in June 2020. Inflation is likely to continue to stay low and below the BoA 3 percent target until the end of 2022.

III. Policy Responses and Reforms

Fiscal Policy

The 2020 Budget Law has been revised on three occasions to respond to evolving emergency needs. The reviews (approved in March, April and July) provided increased resources for the anti-COVID social and economic packages, in part, through re-prioritization of spending that reflected substantially lower than originally budgeted outlays for the reconstruction because of COVID slowdown. To date, out of the originally ALL 34 billion allocated for the reconstruction only ALL 2.6 billion have been spent by beneficiaries.

The Budget Law for 2021 envisages a deficit of 6.5 percent of GDP, down from 8.4 in 2020. However, the Ministry of Finance and Economy (MOFE) is confident that prudent budgetary implementation will keep the actual deficit well below the budgetary target, close to the staff's recommended level of 5.2 percent of GDP. Moreover, the authorities believe that, if needed, they will be able to identify policy actions to contain the deficit, following the 2021 parliamentary elections.

The authorities intend to resume their fiscal consolidation efforts, once the COVID emergency is over and the reconstruction needs are addressed. The main objective of fiscal policy will be to bring back the debt-to-GDP ratio to a downward path, all in compliance with the fiscal rules set by the Organic Budget Law enacted in July 2020. The main operational anchor will be the primary balance that should shift into a balance by 2023. The overall objective is to bring the debt to about 68.5 percent of GDP by 2025**.**

On financing needs, the recent RFI, coupled to the June 2020 Eurobond issuance, secured satisfactory levels of liquidity. Moreover, Albania is benefitting from Macro-Financial Assistance from the EU (Euro 180 million), a first tranche will be disbursed by end 2020. The 2020 budgetary deficit (8.4 percent of GDP) is fully financed. Despite a likely drop in revenue collections this year, the authorities are confident they will keep domestic financing comfortably below 3 percent of GDP over the next 5 years. Moreover, a new Eurobond issue is planned for 2022.

The authorities are keen to implement the Fund's TA recommendations on liquidity management and have already implemented the earlier recommendation on how to better manage the Treasury Single Account (TSA). In fact, TSA balances account were only slightly above the envisaged 1 percent of GDP upper bound of the recommended range ceiling (ALL 15-20 billion range); going forward the level should be comfortably within the foresaw range.

The stock of VAT arrears to small taxpayers has been almost totally repaid (with the exception of ALL 79 million) and will not weight on the business climate. The remaining stock of ALL 12 billion is due to just three large taxpayers and are in the process to be cleared by mid-2021.Therefore, the authorities believe that the potential adverse effects of arrears, described by staff, on market perception and business climate will not materialize.

The authorities have started an in-depth reorganization of the tax system. In this regard, they will consider staff's advice on rationalization. Furthermore, the tax amnesty law is being reviewed by a parliamentary commission, and will take into account comments from Money Val, the European Commission, as well as stakeholders (involved in parliamentary auditions). The authorities have stepped up their efforts to address the remaining deficiencies highlighted by the Money Val assessment. The MOFE is moving ahead with the related action plan; the main actions regard: land registry, beneficiary owner register, data sharing, licensing process supervision, sanctions enforcement, and the management of seizes/confiscated assets.

Monetary policy and financial sector.

In response to the adverse shocks, the BoA has further eased its monetary policy stance and applied judicious and targeted macro-prudential stimulus. The monetary stimulus was delivered by cutting the policy rate to a new historical low of 0.5% and by switching to fixed-price full-allotment liquidity injection operations. On the other hand, regulatory accommodation was delivered through a temporary relaxation of credit provisioning rules, aimed at encouraging credit restructuring and a time-limited deferral of loan installment payments. These measures were aimed at reducing debt-servicing costs, encouraging new lending, and improving the cash-flow of crisis-hit businesses.

Pursuant to these actions, both volatility and risk premia in domestic financial markets stabilized quickly. In addition, credit to the private sector continued to grow, greatly facilitating the liquidity situation of businesses and households.

BOA expects a subdued inflation profile in the coming year, followed by a gradual increase towards its 3 percent target by end 2022. This projection reflects its baseline scenario of a gradual improvement in the cyclical position of the economy, aided by several factors: favorable domestic financial conditions, improving external demand, and growing confidence.

The banking sector remains sound, liquid and well-capitalized. While the crisis impact on the bank balance sheets' is yet to be fully materialized, the BoA stress-tests indicate the banking sector is robust enough to withstand its impact. The BoA will step up its on- and off-site supervision of the banking sector in compliance with its risk-based approach. Furthermore, the BoA will normalize its macroprudential policy stance within 2020: BoA aims to promote the transparency of the balance sheets of the banking sector in order to identify any potential sign of weakness and undertake timely remedial action.

While the baseline scenario remains positive, the accommodative monetary policy stance remains appropriate and any policy normalization will be only gradual and data driven. The prolonged monetary accommodation will account for the expected gradual withdrawal of fiscal stimulus over the next couple of years and will deliver an appropriate policy mix. The BoA will continue to give to the markets proper guidance on the expected likely path of the policy interest rate and the rationale behind its decision-making.

However, the balance of risks remains on the downside. While additional conventional monetary policy space remains, the BoA assesses it is both limited and likely to run into diminishing returns. Depending on the incidence and magnitude of the shocks, the BoA would consider using unconventional instruments as a last resort of policy accommodation**.** Being mindful of their potential pitfalls, their deployment will only be considered under extreme circumstances, pursuant a careful cost-benefit analysis of alternative policy instruments, and a diligent consultation with the IMF staff. Under current analysis, a potential quantitative easing program offers the best cost-benefit profile. Such a tool would help to raise liquidity, to lower risk premia in the domestic financial markets and to promote bank lending. The BoA concurs with staff that the QE adoption should not be seen and neither constitute an unlimited financing of deficit and that clear communication would be key. At the same time, the actual employment of any unconventional instruments will account for the nature of the shock and the relative effectiveness of any policy instrument.

The impact of the twin shocks on institutional investors has been very limited. Stress test to assess the COVID impact showed a good performance and stable prospects. Health-related insurances have not been subject to additional pressures, because COVID cases are treated only in public hospital, i.e. free of charge. On the earthquake impact, there are some administrative delays (on demolition's decisions by the local authorities), but there are no liquidity issues on the insurance market as only 2.5 percent of impacted building was insured – usually because of existing bank's loans. Although, investment funds were required to update their key risk assessment as they will not be protected by (COVID-related) public guarantee scheme.

Energy Sector

The authorities are pushing forward with the reform of the energy sector, also with the support from the World Bank-backed consolidation plan. In particular, the road map toward liberalization and the instalment of the free market and power exchange (APEX) is progressing according with the timeline (should be in place in Q2 2021). The new framework would meet the requirement of the EU regulation on independent compliance, while would maintain a universal supplier – with de-regulated prices – to compensate eventual temporary lower supply. The envisaged division of the current public sectorial companies is progressing and should be completed at the end of the year.

GRAY/20/3427

November 19, 2020

Statement by Mr. Lischinsky and Mr. Corvalan Mendoza on Albania (Preliminary)
Executive Board Meeting 20/113
November 23, 2020

We thank staff for the first Post-Program Monitoring report on Albania and Mr. Fanizza and Mr. Persico for their comprehensive Buff statement.

We take positive note of the authorities' commitment to maintain macroeconomic and financial stability, despite two sizeable negative shocks that hit the country. The first was an earthquake in November 2019 and, by March 2020, the second shock materialized with the Covid-19 pandemic. The combination of these external and unanticipated events hurt tourism, remittances flows, external demand, and FDI. Nevertheless, swift responses from the authorities to address health system requirements, protect employment, and take care of most vulnerable population are welcome steps, which are well explained in Annex I of the report.

The policy responses have put a strain on the fiscal, financial, and monetary sectors, which might temporarily disrupt Albania's efforts to tackle elevated public debt (82 percent of GDP by the end of this year), manage fiscal risks, and curve a relatively high level of non-performing loans in the financial market. For the latter, decisive policy actions of the central bank, added to the ample international reserves and flexible exchange rate mechanism in place, are appropriate to cushion the shocks and should remain in the future as the first line of defense of the economy. We also take positive note from the Buff statement that "[w]hile the crisis impact on the bank balance sheets' is yet to be fully materialized, the BoA stress-tests indicate the banking sector is robust enough to withstand its impact". In this regard, it is encouraging to know that on- and off-site supervision of the banking sector, in compliance with its risk-based approach, is being implemented by the central bank.

On the fiscal front, emphasis on revenue-based consolidation will remain critical. We encourage the authorities to renew their efforts to address structural weaknesses in public finances. To sustain the higher spending needs of the population and the economy, a Medium-Term Revenue Strategy (MTRS) might be needed much sooner rather than later. Assuming the base line scenario materializes, and recovery takes hold from 2021 onwards, room for fiscal policy maneuver will be needed. The MTRS will prove handy for the authorities to minimize the increasing fiscal risks in the medium term. For instance, public investment management and the quality of public spending need strengthening to contain PPPs and recent government guarantee liabilities, as well as avoiding new arrears going forward. The latter affects investor confidence in the private sector′s normal functioning.

We take positive note of the ability of the country to access international financial markets to finance its urgent needs. We also observe as a positive outcome in the continuous progress towards EU integration and, *we would like to hear more details from staff on the BoA′s repo line with the ECB for 400 million euros.*

With these comments, we wish the people of Albania every success in their future endeavors in this challenging time.

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GRAY/20/3429

November 19, 2020

Statement by Mr. Nakunyada and Mr. Sitima-wina on Albania
(Preliminary)
Executive Board Meeting 20/113
November 23, 2020

We commend the Albanian authorities for maintaining macroeconomic and financial stability despite the twin shocks triggered by an earthquake and the COVID-19 pandemic. Reflecting the repercussions of the pandemic, growth is projected to contract sharply in 2020, underpinned by substantial declines in tourism, remittances, and FDI as well as the slowdown in reconstruction projects. Looking ahead, growth prospects remain challenged by the uncertain evolution of the pandemic, and key risks emanating from elevated public deficits and debt, weaknesses in public finances, and a high level of non-performing loans (NPLs) and euroization. Against this background, sustained support would be required as well as the gradual rebuilding of fiscal space as the recovery takes hold. Concurrently, attendant financial vulnerabilities should be carefully managed.

We are encouraged that Albania's capacity to repay remains adequate despite rising risks. We draw our assurance from the sizeable reserve coverage on the back of IMF emergency support, and a flexible exchange rate that remains important in absorbing external shocks. In addition, we note that rollover risks are adequately mitigated by Albania's access to development partners' financing and the captive domestic financial market. Market confidence has also been enhanced by the repo line established with the ECB. Further, Albania's recent issuance of a Eurobond attests to its continued access to international financial markets. Importantly, the prevailing macroeconomic stability indicate that repayment risks to the Fund are contained.

Large scale reconstruction to support recovery and spending to cushion vulnerable households and firms is warranted given the severe impact of the shocks on the economy. In this context, we see merit in fiscal policy measures that balance supporting the economy and addressing development gaps while creating additional fiscal space. We, however, urge the authorities to ensure that support to vulnerable households and firms remains well targeted with clear communication regarding the temporary nature of the support. We also urge the authorities to strengthen public investment management, given the envisaged increases in capital expenditure. To this effect, a rigorous process to prepare, prioritize, and evaluate all public investment projects, including Public-Private Partnerships (PPPs) would be essential to optimize investment returns.

More generally, priority should be attached to enhancing public finance management including through strengthening cash and debt management, while avoiding accumulation of arrears. This would be critical to create fiscal space to address the country's human development needs. However, the elevated fiscal risks emanating from the potential materialization of contingent liabilities should be closely monitored. That said, we welcome the authorities' commitment to strengthen revenue administration and implement a medium-term revenue strategy (MTRS). As noted in Mr. Fanizza and Mr. Persico's informative Buff statement, we also welcome the authorities' intention to resume fiscal consolidation efforts with a view to bring the debt-to-GDP ratio on a downward path, once the COVID pandemic abates.

Safeguarding financial sector stability remains critical to support a sustainable and resilient recovery. While the banking system has remained liquid and stable, pockets of vulnerabilities remain. Considering that the impact of large shocks may not be immediate on banks' balance sheets, we underscore the importance of enhancing both onsite and off-site supervision and effective management of associated risks. In view of the high level of NPLs, the Bank of Albania (BOA) should continue to monitor and guide banks' restructuring of credit portfolios. In this context, we encourage the efforts to improve the NPL resolution framework, align the regulatory framework with international standards, and manage risks from related-party lending and large exposures. Further, we see merit in the restrictions imposed on the distribution of bank dividends until banks' capital positions are assessed to be adequate to absorb the losses from the shocks. Concurrently, the risk of capital erosion emanating from declining profitability should be closely monitored. In addition, we stress the need to urgently address AML/CFT deficiencies to enhance the integrity of the financial system, given the gray listing of the country by FATF and MONEYVAL.

We welcome the authorities' readiness to take further measures as needed to preserve macroeconomic and financial stability. Looking ahead, contingent planning would be critical in view of the uncertainty around the pandemic and the trajectory for recovery. On the fiscal side, we concur that well measured budget revisions would continue to provide the flexibility needed to address uncertainties. In addition, further monetary accommodation and quantitative easing to reduce the credit risk premium would be appropriate should downside risks materialize. In parallel, we encourage the steadfast progress in overall strengthening of institutions and completion of important reforms that are central to the country's integration into the European union.

GRAY/20/3430

November 19, 2020

Statement by Mr. Bevilaqua, Ms. Mohammed, and Mr. Velloso on Albania (Preliminary)
Executive Board Meeting 20/113
November 23, 2020

We thank staff for the helpful report and Mr. Fanizza and Mr. Persico for their insightful statement. The Albanian authorities are facing daunting challenges from last year's earthquake and the global COVID-19 pandemic that have severely disrupted economic activity. We broadly concur with the thrust of staff's appraisal and would like to highlight the following points.

We commend the authorities' swift response to the pandemic. As a second wave of infections moves across Europe, we encourage the authorities to remain steadfast in their efforts to protect lives and livelihoods, while underscoring that emergency support measures should remain temporary, well targeted and transparent. Considering the significant downside risks to the outlook, like staff, we see merit in preserving liquidity buffers by containing non-priority spending and in developing a concrete contingency plan to preserve macroeconomic and financial stability, while protecting the most vulnerable and an adequate healthcare provision.

As the pandemic eases, earthquake-related reconstruction needs are addressed, and a recovery takes hold, we encourage the authorities to implement a gradual but determined medium-term fiscal consolidation strategy. We welcome the authorities' commitment to adopting a strategy to bolster the tax system and improve revenue mobilization over time. Strengthening public investment management and mitigating fiscal risks—including by PPPs and SOEs—are of utmost importance to ensure that future fiscal consolidation efforts would not be derailed. *Could staff comment on the next steps envisaged by the authorities to better integrate fiscal risks mitigation and monitoring into the budget process?*

While the banking system is liquid and stable, pockets of vulnerabilities exist. The near-term priority to monitor and guide prudent bank loan restructuring where necessary seems appropriate. However, as the pandemic enters a new phase, NPLs could rise. We therefore encourage the authorities to continue strengthening bank supervision to detect early signs of distress in the system.

We take note of staff's assessment that public debt remains sustainable and gross financing needs are manageable. However, as public debt is projected to exceed 80 percent of GDP in 2020-21 and gross financing needs are expected to be substantial, the authorities should actively try to mitigate rollover risks, including by increasing their efforts to secure, on more favorable terms, debt refinancing as well as additional financing from Albania's development partners.

Given Albania's strategic AML/CFT deficiencies, we encourage the authorities to intensify their efforts to address the shortcomings identified by FATF and MONEYVAL and to avoid tax amnesty schemes. *Could staff elaborate on the timetable and concrete actions that the authorities envisage in this area?*

Finally, we take positive note that the RFI disbursement in April provided timely relief to Albania and helped mobilize assistance from other IFIs.

With these remarks we wish the Albanian authorities success.

GRAY/20/3431

November 19, 2020

Statement by Mr. Sigurgeirsson and Ms. Skrivere on Albania
(Preliminary)
Executive Board Meeting 20/113
November 23, 2020

We thank staff for the good report and Mr. Fanizza and Mr. Persico for their informative Buff statement. Despite having faced two major consecutive shocks – the severe earthquake in late-2019 and the ongoing COVID pandemic – the Albanian authorities have broadly maintained macroeconomic and financial stability. Nevertheless, the risks remain elevated, which calls for careful contingency planning and intensified efforts to address structural vulnerabilities. **We broadly share staff's appraisal and offer the following comments on fiscal policy, transparency and accountability, debt sustainability, and financial integrity issues for emphasis.**

With worsening fiscal balances, there is a strong need to provide temporary and targeted support to address the crisis, while containing non-priority spending and improving spending efficiency. We note from the staff statement that the 2021 budget, which was recently approved by the Parliament, includes additional spending, which is financed by increasing the already optimistic tax revenue projection. We stress the need for a contingency plan, in case revenue projections do not materialize, or if the outlook deteriorates further. We agree with staff that as the economy recovers, the authorities should aim towards a larger deficit reduction. On the revenue side, we share staff's views on the benefits of a simple, predictable, and transparent tax system. We encourage further efforts to broaden the tax base, improve compliance, and strengthen tax administration capacity. On the expenditure side, we recognize the reconstruction needs caused by the earthquake. At the same time, we note with concern the longstanding weaknesses in public investment management. We urge the authorities to strengthen procurement and public investment administration efficiency, transparency, and accountability. Additional efforts are needed to monitor and manage potential contingent liabilities stemming from PPPs, government guarantees, and SOEs.

We welcome the authorities' commitment to fiscal prudence, transparency, and accountability. We take note of the Supreme Audit Institution's plans to conduct and publish an audit of earthquake- and pandemic-related spending in 2021, including auditing relevant procurement procedures and ex-post validation of delivery. We look forward to seeing the outcome of this process in future staff reports. Additionally, we recall that when requesting the RFI support in spring, the authorities in their Letter of Intent committed to undertake a safeguards assessment, in collaboration with IMF staff, providing IMF staff with BoA's most recently completed external audit reports and coordinating meetings of IMF staff with the staff in charge of these issues in the central bank and external auditors. *Could staff provide an update on the implementation of these commitments?*

While staff assesses Albania's public debt as sustainable, the high debt level and particularly the elevated gross financing needs are a cause for concern. While the immediate priority is to address the ongoing pandemic-related challenges, we stress the importance of returning to a debt reduction strategy once the crisis subsides. We note with concern that gross financing needs remain elevated and breach the 15 percent threshold over staff's forecast horizon. We agree with staff on the need to further extend maturities and prepare mitigation strategies to address possible tightening of domestic financing conditions.

We stress the need to address remaining strategic AML/CFT deficiencies. We note that a new law for the Register of Beneficial Owners entered into force in September, and a public register is to be established during the first half of next year. *Could staff provide further details on other key reforms that would be needed for Albania to be removed from the FATF graylist, as well as the authorities' action plans and possible timeline to address the shortcomings in their AML/CFT framework?*

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GRAY/20/3432

November 19, 2020

Statement by Ms. Shortino, Mr. Farber, and Ms. Lyngaas on Albania (Preliminary)
Executive Board Meeting 20/113
November 23, 2020

We thank staff for this comprehensive and timely report and Mr. Fanizza and Mr. Persico for their help Buff statement. Albania continues to be severely affected by the aftermath of the November 2019 earthquake and the COVID-19 pandemic. We commend the authorities for taking decisive measures to tackle these twin shocks. The RFI disbursement helped free up resources to tackle these concurrent crises; foreign reserves have increased, and the exchange rate has remained broadly stable. **We encourage the authorities to pursue additional reform measures supported by a follow-on Upper Credit Tranche-quality program.**

<u>Fiscal policy and expenditure efficiency.</u> We agree that the sizeable increase in the fiscal deficit – from 2 percent of GDP in 2019 to a projected 6.8 percent in 2020 – is warranted to cushion the impact of shocks. However, we note that there will be a significant decline in revenue projected over this period, while total expenditures remain under-executed compared to the budget. We urge the authorities to create the fiscal space required for supporting essential activities and protecting the most vulnerable by containing non-priority spending and improving expenditure efficiency. In this regard, we support staff's view that short-cuts implemented to public financial management as part of the emergency response should be reversed and reconstruction funds should be subject to adequate controls. Public investment management and governance reforms should also be prioritized, and we are concerned that staff note a reform slowdown. *Can staff*

comment on why earthquake reconstruction spending has only reached 8% of the budgeted annual amount as of September?

Debt and risks. Staff projections on public debt appear to be supported by somewhat optimistic medium-term growth assumptions. We are also concerned that public-private partnerships (PPPs) were excluded from public debt estimates in the DSA, and that information on risks stemming from government guarantees and state-owned enterprise (SOE) debt were not adequately addressed in this report. Given the rollover risks emanating from the short maturity of domestic public debt, we encourage the debt management authorities to engage with staff on potential operations to lengthen average maturities. *We would welcome staff comment on the scale of below-the-line public debt and its impact on DSA assumptions. Could staff also provide more information on what will underpin the 12-percentage point decline in public debt projected between 2020 and 2025?*

Financial sector. We encourage staff and the authorities to continue to monitor risks to the banking system, given the exceptionally large shocks. *We would welcome an update from staff on what measures the authorities are working on with respect to NPL resolution.*

GRAY/20/3433

November 19, 2020

Statement by Mr. Chikada and Mr. Shimada on Albania
(Preliminary)
Executive Board Meeting 20/113
November 23, 2020

We thank staff for the first Post-Program Monitoring (PPM) report on Albania and Mr. Mr. Fanizza and Mr. Persico for their insightful Buff statement. Albania has been hit by dual shocks, the earthquake in 2019 followed by the COVID-19 pandemic. We commend the authorities' swift policy actions to mitigate economic impact from the shocks and welcome that the Fund's emergency financing has catalyzed other donor financings. As the crisis abates, the authorities should accelerate the long-standing reforms, especially in the area of public financial management (PFM), to concurrently and prudently address the increased public debt and the necessity for capital investments. As we broadly agree with staff appraisals, we will provide the following comments for emphasis.

We take a positive note of Albania's resilience to the dual shocks, however, high uncertainty and downside risks due to the pandemic warrant vigilance and contingency planning. The country's sizeable reserve coverage and flexible exchange rate remain important shock absorbers, and it is encouraging that Albania continues to tap international markets and the recent established repo line between the ECB and the Bank of Albania (BOA) would anchor the market confidence in the country. However, the increased public debt would warrant due attention considering the country's weak PFM. We also note that the country may need to seek additional Fund's support to fill the financing gap going forward, should the recovery stagnate, as shown in an illustrative adverse scenario in Annex III.

As the pandemic abates, PFM should be strengthened to concurrently and prudently address the increased public debt and the necessity for capital investments. Given the increased public debt, it is important for the authorities to increase revenue while warranting essential capital expenditures, given the huge infrastructure gap in the country. In this regard, we concur with staff on the importance to complete, adopt, and start implementing a sound

Medium-Term Revenue Strategy (MTRS) in 2021. For steady implementation of MRTS, we see it essential for the authorities to improve their institutional capacity. C*ould staff elaborate the role of the Fund's as well as other development partners' capacity development in these areas?* Regarding transparency and accountability of fiscal expenditure, we welcome that the Supreme Audit Institution plans to conduct and publish an audit of earthquake- and pandemic-related spending in 2021, and we expect that the result of audit will be discussed in the next PPM.

Financial sectors warrant closer monitoring to prevent macro-financial feedback loops. We positively note that the banking sector is well capitalized, and the BOA has injected ample liquidity to the banking system to mitigate the economic impact. However, the NPLs ratio is still high compared with peer countries, and the banks' asset quality could deteriorate further, considering the concentration of credit exposure to the service sector, which the pandemic has severely hit. In this regard, we have concern that some regulatory forbearance measures, notably the relaxation of loan classification and provisioning rules, would veil the reality of banking sector. We therefore urge the authorities to limit such measures be literally temporary, and to monitor the situation closely.

GRAY/20/3434

November 19, 2020

Statement by Mr. Trabinski and Mr. Muradov on Albania
(Preliminary)
Executive Board Meeting 20/113
November 23, 2020

We thank staff for the informative report and Mr. Fanizza and Mr. Persico for their helpful Buff statement. Albania experienced a set of shocks related first to the 2019 earthquake and later the COVID-19 pandemic that resulted in a further deterioration of growth prospects, as well as threatened macroeconomic and financial stability. Considering the increasing chance of a second wave of infections, the outlook is subject to major uncertainties and risks are tilted to the downside. We welcome the authorities' prompt response to the shocks and offer the following comments for emphasis.

We acknowledge that the main challenges lie in public finance. The original 2020 budget has been revised several times to include earthquake reconstruction, additional healthcare spending and support for affected businesses and households. However, the shocks revealed structural weaknesses, especially on the fiscal side. The existing small fiscal space limited the volume and scope of the support package for affected business and individuals. We agree with staff's view that non-priority spending needs to be limited to make room for adequate health care provision and social protection for the most vulnerable. In this regard, we encourage the authorities to consider revenue-based fiscal consolidation once the pandemic abates. While we welcome the authorities' work on the Medium-Term Revenue Strategy, *we would appreciate staff's comment on the precise timeline for the adoption of the MTRS.*

Increasing fiscal risks need to be duly managed and public investment management strengthened. We emphasize the increasing fiscal risks arising from public investment and the Public Private Partnerships (PPP). In this context, we urge the authorities to address existing weaknesses in public investment management with a view to improve the quality of capital spending. More specifically, designing an effective public investment management cycle would be paramount. *Could staff comment on whether the authorities considered conducting a PIMA in the current context?* In addition, monitoring of government guarantees and risks stemming from SOEs would be important. We welcome the commitment of the

Albanian Supreme State Audit Institution (ALSAI) to take a more prominent role in the process of PPP oversight.

We welcome the prompt response of the BOA to alleviate the impact of the shocks to the financial sector. We take good note of the resiliency of the Albanian banking sector. Going forward, we encourage the authorities to closely monitor the existing vulnerabilities given the already high level of NPLs compared to regional peers and the likelihood of their further increase. We agree with staff that a near-term priority would be to closely monitor and guide banks' restructuring of credit portfolios. *In this context, it would be interesting to hear from staff how they asses the efficiency of the insolvency framework in Albania.* We commend the BOA for the accommodative monetary stance and regulatory measures enacted to ensure liquidity in the financial sector following the shocks. We also commend the authorities for strengthening the BOA's capacity for monetary policy formulation, supervision and financial stability monitoring. We encourage staff to work closely with the authorities in improving further the BOA's regulatory and supervisory framework, including with respect to responding to new challenges amidst the current uncertainty.

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Revised: 11/23/20

November 19, 2020

Statement by Mr. Mochtar and Mr. Dacharux on Albania
(Preliminary)
Executive Board Meeting 20/113
November 23, 2020

We thank staff for the comprehensive report and Mr. Fanizza and Mr. Persico for their buff statement.

Albania has been hit with two large shocks from the November 2019 earthquake and followed by the COVID-19 pandemic, **which together had led the economy into a sharp contraction.** The impact of the lockdown to restricted number of foreign tourists and together with the effect of lower tax revenues and the need for stimulus and reconstruction package had resulted in twin deficits and widening gross financing needs. We noted staff's estimate that the RFI disbursed in April had helped cushion the Albanian economy from a sharper downturn, while providing support for the country's level of international reserves.

We welcome staff's projection for a gradual recovery for Albania's economy next year, despite remain vigilant considering several risks. Gradual recovery outlook is supported by the authorities' timely policy responses in virus containment, increases in expenditures especially on health and private sector support measures, as well as accommodative monetary policy stance. We also note staff's assessment that Albania's capacity to repay remains adequate under baseline assumptions. Nevertheless, we share staff assessment on some risks that should be monitored closely. Those are starting from further rounds of pandemic to the rising of fiscal deficit and debt, public finance weaknesses, and high level of NPLs.

That said, we would like to emphasize three areas that warrant the authorities' actions and close monitoring going forward:

1) **Public finances: There needs to be a careful balance between providing near-term policy support and maintaining fiscal sustainability in the medium term.** Compared with the region, Albania's public debt remains high, and gross financing needs are projected to rise in the medium term. We concur with staff's recommendation for fiscal support to deal with the recent shocks to be temporary and targeted, and rendered with transparency and accountability. We underscore the importance of steadfast implementation of the medium-term tax reform, particularly the MTRS, in order to ensure fiscal sustainability and add more room to fiscal space. Fiscal accounts should also properly take into consideration the contingent liabilities from PPP projects and SOEs' finance.
2) **Corporate and Banking sector: The impact of the earthquake and the pandemic to the corporate and banking sector balance sheets as well as their indebtedness require careful monitoring and management.** Despite the declining trend since GFC, Albania's NPLs remain high compared to peers and could rise in the face of worsening pandemic, especially given the large proportion of NFC loans concentrated in service sectors. This warrants an enhanced monitoring system. In addition, we encourage the authorities to introduce necessary reforms to strengthen its insolvency and debt restructuring frameworks to more ably cope with the expected spike in corporate distress and NPLs and facilitate the necessary reallocation of resources across the economy. In this connection, we acknowledge the authorities' commitment to preserve stability with additional measures as needed.
3) **Structural reforms:** In order to improve investment sentiment and secure sustainable growth, attention to address structural and institutional weaknesses should continue to be a priority. In addition to strengthening PPP governance, efforts on economic diversification, rules of law reinforcement, and electricity sector reforms would likely pay off over the medium term. *To this end, we would like to seek staff's elaboration on the plan to mitigate the risks that may arise from delay in structural reforms, including longer than expected outcomes?*

With these remarks, we wish the authorities every success.

GRAY/20/3436

November 19, 2020

Statement by Ms. Levonian, Mr. O'Brolchain, and Mr. Mooney on Albania
(Preliminary)
Executive Board Meeting 20/113
November 23, 2020

We thank staff for their comprehensive report and Mr. Fanizza and Mr. Persico for their helpful Buff statement. Albania has been severely impacted by the effects of a major earthquake and the COVID-19 pandemic shock. Macroeconomic and financial stability have so far been maintained as a result of the authorities' prompt response to the shocks. Appropriately, the authorities' actions have been focused on enhancing the health system, containing the spread of the virus, supporting the most vulnerable population, and rehabilitating damaged infrastructure. We agree with the thrust of staff's assessment and offer the following points for emphasis.

The authorities' ongoing efforts to amend the Budget Law to respond to evolving emergency needs, as outlined in the Buff statement, are reassuring. In this regard, we agree with staff that measures should be targeted to protect the most vulnerable. In the short term, we welcome the authorities' commitment to fiscal discipline and spending reallocation. In that regard, we urge the authorities to complete the preparation of the proposed Medium-Term Revenue Strategy (MTRS) and to push forward with its implementation. An increase in revenue will support the financing of investments and reduce public debt. We concur with staff that the proposed tax amnesty law would negatively impact on tax compliance and revenue generation.

We positively note that the banking system has remained liquid and stable since the onset of the crisis. However, risks persist and, despite a very large decline since 2014, an increase in non-performing loans appears likely. Closer monitoring as well as implementing regulatory and supervisory measures such as risk assessments of banks portfolios, and strengthening the capital and liquidity framework, are required. We welcome the BoA's commitment to strengthening its macroprudential rules before the end of 2020.

Governance and transparency are crucial, **and in this regard, we welcome the authorities' pledge to conduct and publish an audit of earthquake and pandemic-related spending in 2021.** We positively note the institution of a new law for the register of beneficial ownership and the establishment of an associated public register. We urge the authorities to strengthen the AML/CFT framework in line with the recommendations in the recent FATF report. Furthermore, we support the strengthening of public sector investment management, especially the monitoring of private public partnerships, and encourage staff to provide such technical support where appropriate.

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GRAY/20/3437

November 19, 2020

Statement by Mr. Bhalla and Mr. Natarajan on Albania
(Preliminary)
Executive Board Meeting 20/113
November 23, 2020

1. We thank the staff for their crisp report on Albania's first post-program monitoring and Mr. Fanizza and Mr. Persico for the useful buff. Albania is severely affected because of two successive shocks - severe earthquake in November 2019 and the COVID-19 pandemic. Financial assistance under Rapid Financial Instrument (RFI) in April 2020 has provided timely relief to mitigate the adverse socio-economic consequences. As the authorities are working on gradually rebuilding the economy, close monitoring of the economic vulnerabilities and institutional weaknesses is required for ensuring a sustained recovery.

2. The twin shocks are expected to result in contraction of economy between 6 to 7.5 percent in 2020. Though the recovery is expected to strengthen in 2021, the increasing new infections in other European countries can dampen the prospects due to weaker remittances, tourism, external demand and FDI.

3. Fiscal stress has increased, and the deficit is expected to increase from 2 percent in 2019 to 6.8 percent in 2020. This is attributed in almost equal measure to fall in revenue by 2.1 percent and rise in expenditure by 2.7 percent. Targeted tax relief measures and an efficient tax administration can play important role in strengthening the public finances. We welcome the authorities' commitment to fiscal prudence and transparency, and the efforts to prepare a medium-term revenue strategy. Public debt is expected to increase from 67.8 percent in 2019 to 81.9 percent in 2020. *Can the staff comment on the extent of short-term debt servicing requirements and vulnerabilities arising due to this?*

4. The banking system is currently stable and liquid. We encourage the authorities to closely monitor the level of non-performing loans and capital adequacy in the weak banks. Inflation which increased due to the spike in food prices in April '20 has moderated to about 1.5 percent in September. Current account deficit is expected to increase from 8 percent in 2019 to about 11 percent in 2020. We encourage the

authorities to strengthen the AML/CFT framework to mitigate from the shocks due to these risks.

5. Finally, we wish the authorities the best in their efforts.

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GRAY/20/3438

November 19, 2020

Statement by Mr. Buissé, Mr. Rozan, and Mr. Roman on Albania (Preliminary)
Executive Board Meeting 20/113
November 23, 2020

We thank staff for the excellent paper and Mr. Fanizza and Mr. Persico for their insightful buff statement. We broadly share the thrust of the staff appraisal and wish to make the following remarks for emphasis.

Albania has been faced with two large scale exogenous shocks in a very short period of time, an earthquake and the pandemic, that severely affected the economic outlook. GDP growth in 2020 has been revised down by about 11 percentage points relative to the pre-earthquake baseline scenario, to -7.5 percent. The authorities have shown responsiveness in coping with the consequences of these shocks, and we commend their reconstruction efforts after the 2019 earthquake, as well as their actions to strengthen medical care and support households and businesses in the context of the Covid-19 outbreak. In this difficult context, the authorities have managed to maintain macroeconomic and financial stability. However, the crisis has put a strain on the budget with the deficit expected to rise in 2020 (-8.4%), at the time where debt and fiscal risks were already a concern prior to the shocks. As the crisis abates, the authorities will have to implement a medium-term fiscal strategy to reduce fiscal risks and enhance revenue mobilization.

While on the short term, the use of fiscal policy is warranted to protect the economy, there will be a need for a medium term fiscal strategy, in order to balance Albania's development gaps with the need to rebuild room for fiscal policy maneuver and limit external pressures. In the short run, the policy package to support firms and people appears adequate. As risks are on the downside, we concur with staff that authorities should work on contingency measures, and we welcome the attention dedicated to this topic in the report. We support the efforts of the authorities to ensure transparency, accountability, and adequate PFM controls in their emergency spending, and welcome in this regard the Supreme Audit Institution's plan to conduct and publish an audit of earthquake- and pandemic-related spending in 2021. **Given the existing large debt stock, as well as the significant fiscal risks highlighted in the report, the authorities should work on a strategy to reach their primary fiscal balance in 2023**, so as to return to a downward debt trajectory and to generate buffers for future shocks. Working on this now would help give more predictability to households and companies. In this regard, we concur with staff on the importance of completing and start implementing a sound medium-term revenue strategy. We encourage the authorities to contain non-priority spending and to improve spending efficiency. We underline the importance to strengthen public investment management and governance and transparency of PPPs, and to upgrade the capacity of the Ministry of Finance to do so.

External financing requirements remain large, at 22.5% of GDP in 2019, and subject to currency risks, and the current account is expected to widen considerably this year. We note that the financing gap that existed at the time of the RFI request last April has since been covered thanks to the RFI disbursement and a Eurobond issuance of €650 million. The recently established a repo line of €400 million with the ECB should further enhance market confidence. We encourage the authorities to look for the best market conditions for the expected issuance of new Eurobonds, in a context where sovereign spreads that jumped after the outbreak have not yet come back to their pre-crisis level. Clearly outlining a policy path, in particular on the fiscal side, should help ensure successful Eurobond issuance. Working on de-euroization of the economy should also remain a priority in this context.

We encourage the Central Bank to continue monitoring closely the financial sector. The banking system remains liquid and stable. However, going forward, banks' balance sheet should be carefully analyzed, as the fallout of the crisis on corporates' solvency and liquidity start to materialize. Prudent bank loan restructuring should be conducted with adequate BoA guidance. We underline the importance of returning to the normal rules on loan classification and provisioning in this regard. In view of the likely surge in NPLs, we encourage the authorities to swiftly and credibly operationalize and enforce the insolvency and resolution framework. We concur with staff that restrictions on bank dividend distributions should be retained until banks' capital position is assessed to be sufficient to absorb the losses from the shocks.

Efforts to strengthen the AML/CFT framework should continue and tax amnesty schemes should be avoided. As Albania was listed by the FATF in February 2020 as a country with strategic AML/CFT deficiencies, it is important to continue to effectively address the shortcomings identified by FATF and MONEYVAL without delay. We welcome the indication by the authorities that they will not pass the tax amnesty law until concerns expressed by domestic stakeholders and the international community are addressed.

GRAY/20/3439
Revised

November 19, 2020

Statement by Mr. Mouminah, Mr. Alkhareif, and Mr. Aldrees on Albania (Preliminary)
Executive Board Meeting 20/113
November 23, 2020

We thank staff for the well-written report and Mr. Fanizza and Mr. Persico for their helpful Buff statement. We are in broad agreement with staff's assessments and policy recommendations and would like to highlight the following points for emphasis.

1. **It is encouraging to note that Albania has maintained macroeconomic stability despite the severe impact inflicted by the two shocks.** In this vein, we agree that the temporary widening in fiscal deficit is appropriate to accommodate priority spending. We welcome the authorities' efforts to ensure well-targeted and transparent emergency measures, which need to be cost-effective and carefully assessed. We are comforted to note that Albania's capacity to repay the Fund is adequate and that associated risks, albeit high, remain contained and manageable. Also, we are reassured to note that Albania's reserves are expected to be adequate over the medium-term.

2. **In light of the downside risks, we urge the authorities to step up their efforts to preserve fiscal sustainability.** In this context, we welcome authorities' commitment to fiscal prudence and encourage them to pursue fiscal consolidation to put debt back into a downward trajectory once the pandemic recedes. This could be supported by further efforts to enhance domestic revenue mobilization, including through the finalization and adoption of the MTRS while improving PFM as well as investment and debt management. We agree with staff on the need to establish a unified process for preparing, prioritizing, and evaluating all public investment projects, including Public-Private Partnerships (PPPs). Also, continued efforts to clear existing arrears and prevent further build up are warranted. In view of the fiscal risks, we support staff's views regarding the need to identify contingency measures.

3. **We take positive note that the banking sector remains liquid and stable.** We welcome the measures taken by authorities to safeguard financial stability and encourage continued vigilance given the heightened financial vulnerabilities. Notably, we urge the

authorities to step up their efforts in addressing the AML/CFT deficiencies, especially given the gray listing by FATF and MONEYVAL. Here, we are encouraged by the Bank of Albania's continued policy actions and interventions to address the current challenging conditions. *Separately, we* invite *staff to elaborate on the growing balance sheet risks arising from large currency depreciation pressures given the unhedged foreign currency loans.*

With these remarks, we wish the authorities every success in their policy endeavors.

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GRAY/20/3440

November 19, 2020

Statement by Mr. Mohieldin and Ms. Al-Riffai on Albania
(Preliminary)
Executive Board Meeting 20/113
November 23, 2020

We thank staff for their report and Messr. Fanizza and Persico on their informative Buff statement. Albania has been hit by twin shocks, the strongest earthquake in forty years on November 26 of 2019, which caused damage to an estimated 7 percent of GDP, and the COVID pandemic. The authorities are rightly focusing their efforts on protecting lives and livelihoods as well as on continuing to rebuild after the devastating effects of the earthquake. However, the recent shocks are straining public finances and the balance of payments and limiting capacity to proceed with planned reforms. We broadly concur with staff's appraisal and offer the following points for focus.

The fiscal deficit has understandably increased on the back of the recent twin shocks which necessitated elevated spending on covid-related spending as well as reconstruction. Financing the budget will require a drawdown of the government's deposits and using some of the excess reserves of the public health and pension funds, which would greatly reduce the already limited liquidity buffers. We therefore see merit in staff's advice to contain nonpriority spending to optimize spending on health care, social protection, capital spending, and building up liquidity buffers for contingencies. To that end, addressing the structural weaknesses in public finance are of importance. That includes, strengthening public investment management and the quality of public spending, containing and managing elevated fiscal risks, including from PPPs and the recent government guarantees, and avoiding new arrears. Furthermore, though capacity is understandably constrained in the near term, we encourage the authorities to continue with the adoption of a medium-term revenue strategy to generate the resources needed to achieve Albania's sustainable development goals and ensure debt sustainability. *Can staff shed light on the rationale behind permanently removing the profit tax for businesses with annual turnovers up to Lek14 million?* We encourage strengthening the AML/CFT framework and avoiding tax amnesty schemes and the overall improvement of the efficiency of the tax system. *Can staff provide some background on the Albania Investment Corporation (AIC) and why they view that once operational, it would bring about new fiscal risks?* We welcome that the authorities intend to resume their fiscal consolidation efforts once the crisis subsides and the reconstruction needs are addressed. The recent amendment to the fiscal rules requiring a primary balance of at least zero from 2023 onward is welcome. However, given the uncertainty around the pandemic and the pace of economic recovery, we see a need for contingency planning and welcome the authorities' willingness to take additional actions if need be.

Monetary policy stance has appropriately eased and is complemented by targeted macro-prudential stimulus. The banking sector is sound, liquid and well-capitalized and we are reassured that improved asset quality and capital buffers in recent years have reinforced the loss absorption capacity of the banking sector. Furthermore, the Bank of Albania has taken strides in aligning the regulatory framework with international standards and has adopted more intensive supervision. We thank staff for the chapter detailing the recent development in financial regulations and encourage the authorities to maintain their vigilance over the sector considering the elevated uncertainties still present around the timing and pace of the economic recovery. We take note from the Buff statement that should the monetary authorities consider deploying unconventional instruments, they will involve Fund staff in consultation.

We wish the authorities well in overcoming the pandemic and in their plans and progress towards EU integration.

GRAY/20/3441

November 19, 2020

Statement by Mr. White and Mr. Tui Siliva on Albania
(Preliminary)
Executive Board Meeting 20/113
November 23, 2020

We thank staff for the informative report and Mr. Fanizza and Mr. Persico for the helpful Buff statement. We note the twin shocks – earthquake and pandemic – that have heavily impacted Albania and we commend the authorities for maintaining macroeconomic and financial stability in the face of these challenges. We note staff's assessment that Albania's capacity to repay the Fund is adequate in the baseline scenario, and that foreign reserves are adequate in the medium term. However, we remain concerned about the risks from weaknesses in public finances, including elevated public debt and large gross financing needs. Further efforts to mitigate these risks and vulnerabilities are needed, including reforms supportive of broader economy rebuilding. We broadly agree with staff's analysis and offer the following comments for emphasis.

Continued PFM reforms and adequate controls are important to strengthen fiscal discipline. We note the ongoing preparation of the Medium-Term Revenue Strategy to review and redesign the tax system, and encourage staff to collaborate with the authorities to ensure the timely and successful finalization of this initiative which is central to the fiscal strategy. Higher revenues together with expenditure controls, particularly on capital, will create space for adequate health and social spending, a buffer for contingencies and support the reduction of public debt. Reforms in cash management and lengthening of debt maturities are also important. Strengthening public investment management particularly in respect of PPPs, the use of government guarantees and SOE performance will further support the balance sheet.

Monitoring of financial sector vulnerabilities should be further strengthened. The staff report anticipates a surge in NPLs that will impact the banking sector though the authorities expect this to be manageable. To protect against this, we encourage staff to continue to work with authorities on the resolution framework. As balance sheet impacts may take some time to emerge, the restriction on dividend distributions remains prudent and the BOA should strengthen supervision through greater use of onsite inspections. Ongoing efforts to strengthen the AML/CFT framework need to continue.

The nature of the pandemic warrants contingency planning. We note the authorities' readiness to take further measures as needed to preserve macroeconomic stability. Given the uncertainty associated with the pandemic, and with the elevated debt levels, we support staff's emphasis on the importance of contingency planning that focuses on health care provision, protecting the most vulnerable, financing options, and financial stability.

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GRAY/20/3442

November 19, 2020

Statement by Mr. N'Sonde and Mr. Nguema-Affane on Albania
(Preliminary)
Executive Board Meeting 20/113
November 23, 2020

We thank staff for the well-written report and Mr. Fanizza and Mr. Persico for their informative Buff statement.

We welcome Albania's prompt response to the 2019 earthquake and the COVID-19 pandemic that have severely affected the country's externally-dependent economy and its population. Measures taken to address the two shocks have enabled the authorities to maintain macroeconomic and financial stability despite a deterioration of related indicators. We are pleased that the RFI resources have contributed to mitigate the impact of the shocks and mobilize additional external financing. We note that Albania's capacity to repay the Fund remains adequate and higher risks thereto are nevertheless manageable thanks to, among others, continued access to multilateral and capital market financing.

Looking ahead, tackling persistent macroeconomic vulnerabilities remains key to enhance resilience to future shocks. The outlook is positive as economic activity is expected to recover in the near-term from a large contraction in 2020 caused by the strong containment measures and fall in external demand. That said, it remains subject to the uncertainty about the pandemic path, which has increased with recent pickup in infection cases and imposition of new movement restrictions. Policies going forward should continue to focus on addressing macroeconomic vulnerabilities, including high public debt and gross financing needs and financial sector weaknesses. Support measures should be reversed once the pandemic abates and economic recovery firms up. *Could staff elaborate on developments in the labor market and informality in Albania?*

Fiscal policy should remain prudent going forward to rebuild buffers and improve fiscal and debt sustainability. Priority in the fiscal program in the wake of the two shocks has been rightly accorded to supporting reconstruction efforts, households and businesses while providing the necessary health care to the people affected by the novel coronavirus.

However, the fiscal position and debt situation have deteriorated significantly amid lower revenue and dwindling buffers in the face of large financing needs. Against this background, we agree that fiscal policy should be calibrated toward continuing support for the economic recovery while reducing public debt and rebuilding buffers for eventual contingencies. The 2021 budget which contemplates a lower fiscal deficit and a reduction of VAT arrears is reassuring in this regard.

In particular, scaling up domestic revenue mobilization and public financial management (PFM) reforms will be key to rebuild fiscal space. While we support the authorities' efforts to enhance revenue administration and reform its tax system, we share staff concern about tax exemptions—which could hinder revenue performance–and the tax amnesty law which could give way to money laundering. We note the ongoing review of the draft amnesty law by the Parliament and welcome actions being taken to address the strategic AML/CFT identified by Money Val. We look forward to the completion and implementation of the medium-term revenue strategy (MTRS) to boost revenue collection. Continued efforts to strengthen PFM and investment management are needed to improve efficiency of spending. Also, a close monitoring of PPPs, SOEs, and government guarantees would help contain rising fiscal risks. We encourage the authorities to remove the mitigation measures and phase out emergency PFM procedures as soon as the pandemic abates.

Monetary and financial sector policies have been appropriately supportive of banks and their clients and should continue to adapt to economic conditions. We are pleased that the banking system is overall healthy despite a lower profitability and high, yet declining, NPLs. We note the deposit and credit growth underpinned by the accommodative monetary policy and measures to support businesses and borrowers affected by the pandemic. We welcome the central bank's readiness for more monetary stimulus and quantitative easing given the limited room for further monetary policy loosening. That said, given the expectation of higher NPLs, the central bank should continue to closely monitor banks' restructuring of credit loans while further enhancing the supervision and resolution frameworks to reduce risks to financial stability. The authorities are encouraged to consider staff's recommendation on maintaining loan classification and provisioning rules to better assess banks' losses, while aligning the regulatory framework with international standards. *We would appreciate staff assessment of the domestic capital markets and international capital flows in Albania*.

We agree that pursuing structural reforms will also be required to strengthen macroeconomic stability and further advance towards EU integration. We note that the reform momentum is slowing down in the run-up to the general elections in 2021. *Could staff indicate the main areas where reforms are slowing down and where further reforms are needed to advance towards entry into the European Union?*

With these remarks, we wish the Albanian authorities every success in their endeavors.

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GRAY/20/3443

November 19, 2020

Statement by Mr. De Lannoy and Mr. Zedginidze on Albania
(Preliminary)
Executive Board Meeting 20/113
November 23, 2020

We thank staff for the informative report and Mr. Fanizza and Mr. Persico for the helpful Buff statement. The COVID-19 pandemic and consequences of last year's earthquake continue to affect economic activity in Albania. We welcome the authorities' actions to counter the economic challenges and their commitment to continue with the structural reform agenda. The current policy mix, fiscal expansion with monetary accommodation in the near term, helps contain the social and economic impact of shocks and spur growth. Structural reforms, however, are essential for a robust recovery and for limiting downside risks to the outlook. We welcome the Fund's engagement with Albania through Post-Program Monitoring and share staff's assessment. We would like to emphasize following:

While near-term fiscal stance relaxing is warranted to support households and firms, medium-term fiscal consolidation is vital to limit public debt risks. Albania's small open economy, depending on FDI, tourism and remittances, is severely affected by the COVID-19 pandemic, adding to the severe economic damage that was caused by the earthquake last year. Tackling these challenges requires increasing healthcare and social spending. High debt and gross financing needs, however, constitute an important vulnerability. We note that according to the DSA, public debt is sustainable but assumes a steep decline of dept from above 80 percent of GDP in 2020 to below 70 percent of GDP in 2025. Also, gross financing needs are ranging from 19 to 24 percent of GDP each year. In this regard, adopting and adhering to a sound Medium-Term Revenue Strategy is essential. We welcome the authorities' ongoing effort to strengthen domestic revenue generation. We also welcome the new amendments to the fiscal rule, which mandate a balanced or positive primary balance from 2023.

Addressing governance concerns, infrastructure gaps and skill mismatches is critical for fostering sustainable growth. We agree with staff that progress on this front is vital for improving the investment climate and promoting export-led growth. Improving corporate governance will promote competition and private investment. Mobilizing tax revenues will create fiscal space to invest in infrastructure and address skill-mismatches. Staff's analysis notes increasing fiscal risks stemming from PPPs, government guarantees and SOEs. Addressing these concerns should be high on the authorities' agenda. Similarly, we emphasize the importance to address the AML/CFT shortcomings identified by FATF and MONEYVAL. *Additional staff views on governance diagnostics in Albania would be welcome.*

GRAY/20/3444

November 19, 2020

Statement by Mr. Palotai, Mr. Azal, and Mr. Dogan on Albania
(Preliminary)
Executive Board Meeting 20/113
November 23, 2020

We thank staff for the comprehensive report, and Messrs. Fanizza and Persico for their informative Buff statement. While the financial resources disbursed under the RFI provided some relief from the heightened balance of payments pressures caused by the November 2019 earthquake and the COVID-19 pandemic, Albania's economic outlook remains gloomy. Uncertainty about a prolonged pandemic, a deteriorating fiscal position, a high level of non-performing loans (NPLs), unhedged FX loans, as well as weaknesses in economic governance weigh on the economy. The forthcoming elections could delay much needed progress.

Pressing ahead with fiscal consolidation is key to ensure the sustainability of public finances and public debt. We emphasize that a decisive and credible medium-term fiscal framework is crucial to put the fiscal deficit on a downward trend. We urge the authorities to take the necessary measures to address structural weaknesses, especially in public investment management and quality of spending. In that vein, strengthening the tax system through phasing out exemptions and avoiding amnesty with streamlined tax procedures and an improved tax administration are essential steps for mobilizing revenues and creating room for fiscal policy which in turn would rein in the elevated public debt. Considering the high share of PPP projects in GDP (projected to reach 50 percent in 2021), we join staff in calling on the authorities to rationalize PPP projects. *To what extent have the authorities engaged with the Fund on capacity building to identify and mitigate the risks from PPPs, through technical assistance and the Public Fiscal Risk Assessment Model diagnostic tool?*

Accommodative monetary policy with grater exchange rate flexibility can play a crucial role for mitigating external imbalances. Additional adverse risks including more severe pandemic fallouts could weigh on the fiscal and current account deficit and create external financing needs and exacerbate roll over risks. While Albania was able to successfully place a Eurobond taking advantage of loose global monetary conditions and the recently established repo line with the ECB together with relatively high foreign reserves gives some assurance, *staff's comments on other policy options would be welcome also in view of the* *significant political risks to successfully implement necessary adjustment measures. Can staff also elaborate on their recommendations to address the large share of unhedged FX loans.*

Strengthening financial sector regulation and supervision and reducing NPLs are vital for financial stability and economic recovery. Risks to the financial sector stability have been amplified since the start of the pandemic. In this regard, we encourage the authorities to adopt a time-bound plan to efficient supervision and resolution program and regulatory framework based on international standards. We agree with staff on restructuring loans for borrowers hit by shocks and on the restriction on dividend distribution through end-2020. We note that reducing NPLs would give a positive signal to commercial banks to lend for private sector investment. *Staff's elaboration on a possible NPL resolution strategy would be welcome.* Finally, addressing the shortcomings in the AML/CFT framework to remove Albania from the FATF list of countries with strategic deficiencies should be a priority.

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GRAY/20/3445

November 19, 2020

Statement by Mr. Palei and Mr. Shestakov on Albania
(Preliminary)
Executive Board Meeting 20/113
November 23, 2020

We thank staff for the comprehensive report and Mr. Fanizza and Mr. Persico for their informative buff statement. The COVID-19 pandemic hit the Albanian economy when it had not fully recovered from the November 2019 earthquake. In these challenging circumstances the authorities have responded promptly to secure macroeconomic and financial stability while protecting lives. According to staff, Albania's outlook is subject to major uncertainty with rising downside risks as the second wave of the pandemic is spreading across Europe. These risks are exacerbated by the country's long-standing governance vulnerabilities, shrinking fiscal space, and growing share of non-performing loans. The Albanian authorities need to adopt an ambitious reform agenda. In order to address the country's structural constraints to growth, steady and credible implementation of reforms is necessary during the recovery phase.

The authorities have responded to the shocks with an appropriate mix of monetary policy easing and fiscal stimulus. The Bank of Albania had cut policy rate to 0.5%, which makes further monetary accommodation challenging. In the beginning of 2020, the authorities had focused on earthquake reconstruction spending. However, when the COVID-19 pandemic hit the economy, government spending was increased to ramp up health care measures and to support businesses and households. Flexible exchange rate of *the lek* continues to play an important role as a shock absorber, while targeted FX interventions ensure smooth adjustments. The international reserves are projected to stay at a comfortable level of 165 percent of ARA metric at end-2020. The recently established repo line between the ECB and the BOA would help to provide additional support to the country. The April RFI disbursement from the Fund also played an important catalytic role, attracting support from other IFIs.

Fiscal consolidation would be necessary in the medium term to put public debt on a sustainable path. We welcome the Albanian authorities' commitment to fiscal transparency and take positive note of their plans to conduct and publish an audit of earthquake and pandemic-related spending in 2021. During the recovery phase the adoption and implementation of a sound Medium-Term Revenue Strategy should be among the authorities' key priorities. Such a strategy would help with revenue mobilization and, hence, public debt sustainability.

There is an urgent need to address weaknesses in economic governance and institutions. In February 2020, Albania was included by the FATF in its grey list, which means that the country had strategic AML/CFT deficiencies. We concur with staff that the proposed tax amnesty law should only be enacted after addressing the governance vulnerabilities and money laundering risks. *Are there any plans for technical assistance from the Fund on the AML/CFT framework?*

With these remarks, we wish the authorities all the success.

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GRAY/20/3447

November 20, 2020

Statement by Mr. Hosseini, Mr. El Qorchi, and Mr. Badsi on Albania
(Preliminary)
Executive Board Meeting 20/113
November 23, 2020

We thank staff for the well-written report, and Mr. Fanizza and Mr. Persico for their helpful Buff statement.

Albania has been hit hard by the dual shocks of the November 2019 earthquake and the COVID-19 pandemic. Fund's RFI disbursement in April 2020 helped to mitigate the initial healthcare costs of the crisis, protect the vulnerable population, and support the economy. However, financing pressures continue to persist. After bottoming out in Q2 2020, the economy is expected to gradually recover, but the path of the recovery is closely dependent on the path of the pandemic, which is highly uncertain. We note that the authorities and staff agree on the outlook and near- and medium-term risks which are skewed to the downside. Furthermore, significant public debt vulnerabilities also continue to persist, including those arising from the rollover risk, the exchange rate risk, and high euroization. In this regard, we welcome the authorities' renewed commitment to macroeconomic and financial stability despite the challenging external environment. We are in broad agreement with the staff appraisal and take positive note of staff's assessment that Albania's capacity to repay the Fund is adequate. We limit our comments to the following.

We commend the authorities for their commitment to fiscal prudence, transparency, and accountability and encourage them to step up their efforts to implement the Medium-Term Revenue Strategy focusing on revenue mobilization, including through redesigning and streamlining the tax system. While we see merit in staff's recommendation to aim for a small primary surplus by 2023, we should also be cognizant of the risk of fiscal reform fatigue that would erode pubic support. In the present environment of tentative growth and uncertain outlook, it is important that the fiscal support is not withdrawn prematurely before its expected economic effects come to fruition. *Considering the 14 percent budgeted rise in public wages in 2021, while inflation is projected to remain low, we would appreciate staff comments on government's wage policy going forward. How do public sector wages* *compare with private sector wages and to what extent they have a knock-on effect on wages in the private sector?* Further, we call on the authorities to strengthen public investment management, improve the PPP framework, address high contingent liabilities stemming from PPP, and work towards clearing the remaining central and local government arrears. We are concerned about the projected rise over the medium-term in debt service payments arising from the expected increase in commercial borrowing.

We agree that the monetary policy stance and financial measures taken to alleviate the impact of the pandemic are appropriate. The banking sector seems to be well capitalized and liquid, but bank profitability is declining and the NPL ratios are still elevated. The authorities are strongly encouraged to strengthen banking regulation and supervision. While the incentive measures to ensure money market liquidity are important, the BoA is strongly encouraged to closely monitor the impact of the temporary relaxation of loan classification and provisioning rules. We look forward to the normalization of the macroprudential policy stance, as stated by Mr. Fanizza and Mr. Persico in their Buff statement. *Noting that the BoA switched its open market operations* from fixed amount of liquidity to unlimited amounts*, we invite staff to elaborate on collaterals that could be used in these operations, and in particular if any haircut rate is applied.* We believe that under the adverse scenario, the banking sector could come under stress, especially the few banks whose capital ratios are already barely above the regulatory requirements. *Could staff provide some details on the authorities' contingent plans in the event these banks are under serious financial distress particularly if their solvency is jeopardized?* Finally, we strongly urge the authorities to spare no efforts in strengthening the AML/CFT frameworks.

GRAY/20/3448

November 20, 2020

Statement by Mr. Zhang and Ms. Yang on Albania
(Preliminary)
Executive Board Meeting 20/113
November 23, 2020

We thank staff for the well-written report as well as Mr. Fanizza and Mr. Persico for their informative Buff statement. Albania's economy faced daunting challenges from the November 2019 earthquake and the COVID-19 pandemic. With the disbursement of RFI, the authorities took timely measures to maintain macroeconomic and financial stability. As the shocks subside and reconstruction spending picks up, the economy is expected to rebound gradually in 2021-22. We welcome the Fund's engagement with Albania through Post-Program Monitoring, broadly agree with staff's appraisal, and would limit our comments to the following for emphasis.

The fiscal support in 2020 and 2021 is warranted to cushion the impact of the shocks. We take positive note that the authorities have made three budget revisions to respond to evolving emergency needs, with the third revision on scaling up reconstruction and investment. However, we are concerned that out of the ALL 34 billion allocated for reconstruction spending, only ALL 2.6 billion has been spent by beneficiaries to date. *Could staff share a bit more on the reasons behind the slow execution, and whether it is pandemic related or due to other factors?* We also noticed the sizable increase in public wages in the 2021 budget. *Could staff elaborate on the nature of the wage rise and consideration behind the decision?* We also share staff's view that the authorities should contain non-priority spending and improve spending efficiency to make room for supporting essential activities and protecting the most vulnerable.

Financial regulation should be strengthened and close monitoring on financial sector vulnerabilities is needed. The BOA has made progress in aligning the regulatory framework with international standards and has adopted more intensive supervision. We are pleased to see that the banking sector remains sound, liquid, and well-capitalized amid the crisis. Given the full impact of the shocks may be visible after some time, close monitoring on vulnerabilities is warranted and further improvement on the resolution framework is needed.

We encourage the authorities to continue to strengthen the AML/CFT framework. As Albania was listed by the FATF as a country with strategic AML/CFT deficiencies, further efforts should be made to address the shortcomings. We welcome the new law for the Register of Beneficiary Owners that entered into force in September and a public register of beneficial owners to be established in the first half of 2021.

We take positive note that Albania's financing needs are fully met and its capacity to repay the Fund is adequate. Albania's sizable reserve and flexible exchange rate, together with continued access to international financial markets, helps to mitigate debt risks. Given the uncertain nature of the pandemic, contingency planning is welcomed to cover potential financing gaps. We take positive note of robust flows of FDI as it promotes productivity while helping to alleviate the debt burden. *Could staff elaborate on Albania's efforts to attract foreign investment and provide more details on Albania's foreign investment policies as well as the business environment? We would also like to know the latest developments on the EU membership negotiation.*

With these remarks, we wish the authorities every success in their policy endeavors.

Albania

Responses to Technical Questions Posed by Executive Directors in Advance of EBM/20/113, November 23, 2020

Staff's responses to technical and factual questions are below. Broader policy questions regarding challenges and risks to the reform agenda will be addressed in staff's oral intervention at the Board meeting.

Pandemic/Outlook

1. *Could staff elaborate on developments in the labor market and informality in Albania?*

- Until the COVID-19 outbreak, labor market indicators were showing positive developments: labor force participation was on an upward trend for both male and female, youth participation rate was increasing, and unemployment had reached an historically low level of 11.2 percent in 2019Q4. But the earthquake and pandemic have started to reverse these positive trends. Compared to 2019, the employment rate and labor force participation have declined by 2 percentage points in 2020Q2, while the unemployment rate has increased by 0.4 percentage points. Staff expects a further worsening of these indicators before the economy fully recovers from the shocks.

- Informality is high in Albania. The International Labor Organization estimates the informality reached 56.7 percent of total employment in 2019. Staff does not yet have data to assess the impact of the pandemic on informality. Indirect indicators of informality such as employment in the agricultural sector or unpaid family workers have not shown any increase so far since the beginning of the pandemic.

Fiscal Policy and Public Debt

2. *Can staff comment on why earthquake reconstruction spending has only reached 8% of the budgeted annual amount as of September?*

3. *Could staff share a bit more on the reasons behind the slow execution, and whether it is pandemic related or due to other factors?*

- Reconstruction activities were put on hold during the March-May lockdown at the onset of the pandemic and only fully resumed in the second half of the year. The authorities also face capacity constraint with structural weaknesses in public investment management. Reconstruction is a government priority, and spending is expected to ramp up in the last quarter. But staff does not project the budgeted amount of 2.2 percent of GDP to be fully spent in 2020.

4. *Can staff shed light on the rationale behind permanently removing the profit tax for businesses with annual turnovers up to Lek14 million?*

- The rationale as explained by the authorities is to support SMEs and employment in difficult times. Initially as part of the measures to mitigate the immediate impact of pandemic on businesses, the authorities removed the profit tax for all businesses with annual turnovers up to Lek14 million during 2020. Later this temporary measure was extended indefinitely, with the high turnover threshold undermining tax compliance.

5. ***Considering the 14 percent budgeted rise in public wages in 2021, while inflation is projected to remain low, we would appreciate staff comments on government's wage policy going forward. How do public sector wages compare with private sector wages and to what extent they have a knock-on effect on wages in the private sector?***

6. ***Could staff elaborate on the nature of the wage rise and consideration behind the decision?***

- The public wage increases in the 2021 budget are limited to health and education only and come after years of keeping nominal wages unchanged. The authorities' rationale for a substantial wage increase for doctors and nurses reflects not only the increased burden in dealing with the pandemic, but also the high migration of doctors and nurses to Western Europe in recent years which puts pressure on the human resources of the health sector. For doctors at least, public sector salaries are lower than in the private sector. Wages for teachers in the public sector compare favorably to those in the private sector. However, the government has difficulties in filling positions in remote areas and teachers have been working double shifts to help keep public schools open during the pandemic.

- Staff does not anticipate significant knock-on effects on wages in the private sector as (i) the public wage increases are limited to health and education and (ii) the economy is going through a downturn.

- Albania's public sector wage bill in percent of GDP is among the lowest in Western Balkans. Decisive efforts to increase revenue is key to ensure fiscal/debt sustainability while improving delivery of public services.

7. ***For steady implementation of MRTS, we see it essential for the authorities to improve their institutional capacity. Could staff elaborate the role of the Fund's as well as other development partners' capacity development in these areas?***

8. ***While we welcome the authorities' work on the Medium-Term Revenue Strategy, we would appreciate staff's comment on the precise timeline for the adoption of the MTRS.***

- The Fund has provided substantial TA in revenue administration, helping the authorities move toward a risk-based approach to tax administration. In response to the authorities' request for support and guidance in the preparation of a MTRS, FAD delivered extensive TA in 2019 to help the authorities identify reform options and design a blueprint for improvements in tax policy and tax administration that would enable authorities to raise an additional 2-3 percent of GDP in revenue over five years.

- Following the FAD TA, the authorities planned to complete and adopt a MTRS by mid-2020 according to their action plan. But the November 2019 earthquake and later the pandemic put these efforts on the backseat.

- Given the general elections in April 2021 and the need for public consultation, the authorities have postponed the timeline to complete and adopt a MTRS after the elections.

9. ***Could staff comment on the next steps envisaged by the authorities to better integrate fiscal risks mitigation and monitoring into the budget process?***

10. ***To what extent have the authorities engaged with the Fund on capacity building to identify and mitigate the risks from PPPs, through technical assistance and the Public Fiscal Risk Assessment Model diagnostic tool?***

- The Ministry of Finance and Economy (MOFE) established a Fiscal Risk Unit (FRU) in 2017 and has received substantial TA to increase the capacities of the unit. Over time the coverage and the depth of the Fiscal Risk Statement, now an integral part of the budget submission documents to the parliament, have increased. However, much more needs to be done to achieve a fully-fledged fiscal risk statement that quantifies all fiscal risks and provides strategies to mitigate them.

- The FRU monitors quarterly those PPPs with budget support and largest SOEs that pose fiscal risks to the budget. Some of these reports have been published, while others continue to be internal.

- The authorities have utilized extensive IMF, WB and EC technical assistance to introduce the Public Fiscal Risk Assessment Model diagnostic tool. However due to data constraints and limited technical capacity this process has not yet generated tangible assessment results.

11. ***Can staff provide some background on the Albania Investment Corporation (AIC) and why they view that once operational, it would bring about new fiscal risks?***

- From the initial set up of Albania Investment Corporation (AIC), it was understood that the AIC was intended as a vehicle to better manage idle state-owned assets, partly through investing these in commercial investment projects. However, the AIC legislation passed in late 2019 affords broad scope to the activities of the AIC including the potential use of the AIC as an off-budget investment vehicle. Its regulations, which have yet to be adopted, should ensure that the AIC will have a strictly commercial focus and will not depend on repeated capital injections by the government to cover losses.

12. ***Could staff comment on whether the authorities considered conducting a PIMA in the current context?***

- Albania has undergone a PIMA assessment in 2016. A range of follow-up TA activities were provided subsequently, to (i) improve the authorities' capacity in assessing risks related to PPPs; (ii) strengthen the gatekeeper function of the MOFE; and (iii) streamline and strengthen the procedures of selecting, evaluating, and assessing investment projects.

- Some progress was made with regard to the legal framework for PPPs and the gatekeeper role of MOFE. However, limited progress has been made in integrating PPPs and regular investment projects into the budget cycle to better prioritize and assess their full fiscal impact. A stringent project selection, preparation, and gateway process for all public investments including PPPs remains to be fully developed. Public investment continues to be divided into myriad of projects.

13. ***We would welcome staff comment on the scale of below-the-line public debt and its impact on DSA assumptions. Could staff also provide more information on what will underpin the 12-percentage point decline in public debt projected between 2020 and 2025?***

- In estimating public debt and conducting debt sustainability analysis, staff includes not only current debt and projected borrowing, but also contingent liabilities stemming from external and domestic public guarantees (e.g. energy and water), stock of central and local government arrears, and VAT refund arrears. In addition, the portion of government-funded PPPs that have payments reflected in budget spending are taken into account in public debt.

- The projected decline in public debt is mainly driven by cyclical recovery of the economy, reduction in fiscal deficit, and projected repayment of government arrears.

14. ***Public debt is expected to increase from 67.8 percent in 2019 to 81.9 percent in 2020. Can the staff comment on the extent of short-term debt servicing requirements and vulnerabilities arising due to this?***

- Albania's short-term debt servicing requirements and gross financing needs are large, reflecting high public debt and the short maturity of domestic public debt, which represents about 50 percent of total public debt. The average weighted maturity of domestic public debt increased from less than one year in 2011 to about 2.2 years as of June 2020.

- Key vulnerabilities arising from this include rollover risk, and exchange rate risk as FX commercial debt has increased, although external borrowing is mainly from development partners on more concessional terms. FX commercial debt has maturity of 5-7 years and no Eurobond repayment is expected in 2021.

- The authorities' ongoing efforts to lengthen maturity have reduced rollover risks and improved cost efficiency. Rollover risks have also been lessened by the ample liquidity of the banking system. The exchange rate has so far remained broadly stable.

- Nonetheless, strengthening debt management and further lengthening of maturities are needed to help reduce the still very high annual financing requirements, combined with the preparation of mitigation strategies to address possible tightening of financing conditions.

Financial and Monetary Policy

15. ***We would welcome an update from staff on what measures the authorities are working on with respect to NPL resolution.***

16. ***We note that reducing NPLs would give a positive signal to commercial banks to lend for private sector investment. Staff's elaboration on a possible NPL resolution strategy would be welcome.***

17. ***We agree with staff that a near-term priority would be to closely monitor and guide banks' restructuring of credit portfolios. In this context, it would be interesting to hear from staff how they asses the efficiency of the insolvency framework in Albania.***

- The authorities launched an NPL resolution strategy in 2015 that includes a new insolvency law, a new bailiff law, and amendments to the civil procedures and civil code. Since then, the new legislation on bankruptcy, bailiff procedures, and out-of-court agreement have been progressively implemented. There has also been progress in restructuring NPLs of large borrowers and changes of rules to accelerate loan write-offs.

- However, the implementation of the insolvency framework is hindered by the lack of bylaws (still unapproved) and disputed regulations over the functions and remunerations of bailiffs. The court resolution of NPLs also faces hurdles due to lack of qualified judges and temporary incapacitated courts due to ongoing vetting process.

18. ***Could staff provide some details on the authorities' contingent plans in the event these banks are under serious financial distress particularly if their solvency is jeopardized?***

- If a bank does not have available capital buffers to fully absorb losses, the BoA would instruct the bank in question to adopt a capital restoration plan, requiring capital injection from stakeholders.

- If a bank becomes nonviable, the BOA, as the bank resolution authority, has legal powers and tools to plan and carry out resolution actions as appropriate to minimize risks to the banking system.

19. ***Separately, we invite staff to elaborate on the growing balance sheet risks arising from large currency depreciation pressures given the unhedged foreign currency loans*.**

- Euroization remains high in Albania. FX deposits account for a little more than half of total deposits. The share of total bank loans in FX has been on the decline, but still represents about half of the total loans. Unhedged FX loans have declined, but still account for more than 20 percent of total loans in 2020Q3.

- Banks' net open FX position is small. However, in case of large currency depreciation pressures, financial stability risks could arise from unhedged FX borrowing and BOA's limited capacity as lender of last resort in FX. Thus far, the risks have been contained as the currency has remained broadly stable and the FX reserve coverage has remained sizeable.

20. ***Can staff also elaborate on their recommendations to address the large share of unhedged FX loans.***

- Consistent with past staff recommendations, the BOA started implementing a comprehensive de-euroization strategy in 2018, to increase awareness of the risks of FX borrowing and reduce incentives for FX deposits. The strategy seeks to reduce FX vulnerabilities while recognizing that an abrupt phase-in can encourage financial disintermediation or even foster unregulated borrowing. The gradual approach aims to monitor the implementation risks, while preserving the goal of increasing awareness of FX-borrowers and setting mechanisms for banks to internalize the cost of FX deposits.

21. ***We would appreciate staff assessment of the domestic capital markets and international capital flows in Albania.***

- Albania's domestic capital markets are small and inactive, dominated by government debt. Apart from a handful private corporate bond placements, only sovereign instruments are available for domestic trading, with limited secondary market liquidity.

- FDI has dominated international capital flows in recent years. The next two largest items of capital flows are official external borrowing to finance budget and projects and bank cross-border flows. Trade finance instruments are small and portfolio investments, including derivatives and hedging instruments, are limited.

22. ***Noting that the BoA switched its open market operations from fixed amount of liquidity to unlimited amounts, we invite staff to elaborate on collaterals that could be used in these operations, and in particular if any haircut rate is applied.***

- Collaterals are government securities. Haircut is based on maturity (3% for maturity up to 1 year, 6% for above 1 year).

Structural Reforms

23. ***Given Albania's strategic AML/CFT deficiencies, we encourage the authorities to intensify their efforts to address the shortcomings identified by FATF and MONEYVAL and to avoid tax amnesty schemes. Could staff elaborate on the timetable and concrete actions that the authorities envisage in this area?***

24. ***Could staff provide further details on other key reforms that would be needed for Albania to be removed from the FATF graylist, as well as the authorities' action plans and possible timeline to address the shortcomings in their AML/CFT framework?***

- Albania was listed in February 2020 by the Financial Action Task Force (FATF) as a country with strategic AML/CFT deficiencies. The country has committed to resolve the identified deficiencies in line with an agreed action plan including a timetable and has already made progress in improving its AML/CFT regime, including bringing into effect legislation to implement a register of beneficial owners in September 2020, taking measures to reduce the informal economy and use of cash, and establishing specialized teams and officials in each district to investigate and prosecute money laundering.

- The timeline for completion of the actions in the plan ranges from June 2021 - Feb 2022, with the majority of the actions due to be completed by October 2021. It is important that the authorities guard against slippage against the agreed timeline, as FATF measures progress against this timetable. FATF also allows countries to advance implementation to be delisted earlier than planned.

- The action plan covers six broad areas and sets out a detailed overview of the planned reforms with the key areas including: 1) Ensuring that accurate and up-to-date legal and beneficial ownership information is available on a timely basis; 2) Conducting additional in-depth analysis to understand its money laundering risks, and enhancing institutional coordination and cooperation; 3) Improving the timely handling of mutual legal assistance requests; 4) Establishing more effective mechanisms to detect and prevent criminals from owning or controlling Designated Non-Financial Business and Professionals; 5) Increasing the number and improving the sophistication of prosecutions and confiscations for money laundering; and 6) Improving the implementation of targeted financial sanctions.

25. ***Are there any plans for technical assistance from the Fund on the AML/CFT framework?***

- At present, a formal request for AML/CFT TA has not been received from the authorities.

26. ***Similarly, we emphasize the importance to address the AML/CFT shortcomings identified by FATF and MONEYVAL. Additional staff views on governance diagnostics in Albania would be welcome.***

- Albania's main areas of governance weakness include fiscal governance (revenue outcomes, procurement, PFM controls), AML/CFT, rule of law (contract enforcement, property rights, investor protection), and product market regulation.

27. ***Although international reserves hovers around a comfortable level, staff's elaborations are welcome on the necessary measures to address the large current account deficit.***

- The projected widening of the current account in 2020 reflects lower tourism receipts, remittances, and exports of good. The current account is expected to narrow somewhat from 2021 onward as the impact of the shocks abate. Albania's flexible exchange rate is an important shock absorber.

- However, Albania's structural current account deficit is sizeable. The reduction of external imbalances will hinge on efforts to increase domestic saving, particularly fiscal consolidation, and to improve investment climate and competitiveness of the economy, which have been hindered by governance concerns, infrastructure gaps, and skills shortages.

28. ***Could staff elaborate on Albania's efforts to attract foreign investment and provide more details on Albania's foreign investment policies as well as the business environment?***

- FDI has concentrated in the gas transmission and energy sector. Like other countries in the region, Albania has attempted to attract foreign investors by offering fiscal incentives, establishing free economic zones, and granting special legal protection for strategic investors, albeit with muted success.

- Albania's main bottlenecks to FDI remain weak property rights, contract enforcement, infrastructure and skills gaps, and weak institutions and governance concerns. Albania's proximity to EU, wage competitiveness, and multi-language labor force are pull factors for FDI.

29. ***Could staff indicate the main areas where reforms are slowing down and where further reforms are needed to advance towards entry into the European Union?***

30. ***We would also like to know the latest developments on the EU membership negotiation.***

- In March 2020 the EU decided to open accession negotiations with Albania. But before the negotiations can start, Albania needs to fulfil a set of preconditions, including progress with justice reform; a consensus-based electoral reform, a track record in the fight against crime and corruption, and amendment of media laws.

- While the EU commission deems there has been progress in most areas, some of these pre-conditions have not been met, including the functioning of the Constitutional Court and the Supreme Court, which are inoperative due to lack of quorum as the vetting process for judges is ongoing.

31. ***While Albania was able to successfully place a Eurobond taking advantage of loose global monetary conditions and the recently established repo line with the ECB together with relatively high foreign reserves gives some assurance, staff's comments on other policy options would be welcome also in view of the significant political risks to successfully implement necessary adjustment measures.***

- Staff will respond to this question during the Board meeting.

32. ***To this end, we would like to seek staff's elaboration on the plan to mitigate the risks that may arise from delay in structural reforms, including longer than expected outcomes?***

- Staff will respond to this question during the Board meeting.

Others

33. ***We take positive note of the ability of the country to access international financial markets to finance its urgent needs. We also observe as a positive outcome in the continuous progress towards EU integration and, we would like to hear more details from staff on the BoA's repo line with the ECB for 400 million euros***.

- In July, the ECB and the BOA set up a repo line arrangement to address potential euro liquidity needs of Albania financial institutions in case of market dysfunctions due to the COVID-19 shock. Under the repo line, the BOA is able to borrow up to €400 million from the ECB in exchange for adequate euro-denominated collaterals. The maximum maturity of each drawing is three months. The repo line will remain in place until the end of June 2021, unless an extension is decided.

34. ***Additionally, we recall that when requesting the RFI support in spring, the authorities in their Letter of Intent committed to undertake a safeguards assessment, in collaboration with IMF staff, providing IMF staff with BoA's most recently completed external audit reports and coordinating meetings of IMF staff with the staff in charge of these issues in the central bank and external auditors. Could staff provide an update on the implementation of these commitments?***

- Staff has received the necessary external audit reports for the Bank of Albania and the commitment for a future safeguards assessment still stands. For countries that received emergency financing, the safeguards policy requires that assessments be completed before the Board approval of any subsequent UCT arrangement. Owing to the significant pipeline of countries with emergency financing requests, staff are currently prioritizing safeguards assessments for countries that have requested or expressed interest in follow up UCT arrangements.

CONSTITUENCY CODES

OEDAE
Angola, Botswana, Burundi, Eritrea, Eswatini, Ethiopia, The Gambia, Kenya, Lesotho, Liberia, Malawi, Mozambique, Namibia, Nigeria, Sierra Leone, Somalia, South Africa, South Sudan, Sudan, Tanzania, Uganda, Zambia, and Zimbabwe

OEDAF
Benin, Burkina Faso, Cameroon, Central African Republic, Chad, Comoros, Democratic Republic of Congo, Republic of Congo, Côte d'Ivoire, Djibouti, Equatorial Guinea, Gabon, Guinea, Guinea Bissau, Madagascar, Mali, Mauritania, Mauritius, Niger, Rwanda, São Tomé & Príncipe, Senegal, Togo

OEDAG
Argentina, Bolivia, Chile, Paraguay, Peru, and Uruguay

OEDAP
Australia, Kiribati, Korea, Marshall Islands, Federated States of Micronesia, Mongolia, Nauru, New Zealand, Palau, Papua New Guinea, Samoa, Seychelles, Solomon Islands, Tuvalu, and Vanuatu

OEDBR
Brazil, Cabo Verde, Dominican Republic, Ecuador, Guyana, Haiti, Nicaragua, Panama, Suriname, Timor-Leste, and Trinidad and Tobago

OEDCC
China

OEDCE
Colombia, Costa Rica, El Salvador, Guatemala, Honduras, Mexico, and Spain

OEDCO
Antigua and Barbuda, The Bahamas, Barbados, Belize, Canada, Dominica, Grenada, Ireland, Jamaica, St. Kitts and Nevis, St. Lucia, and St. Vincent and the Grenadines

OEDEC
Austria, Belarus, Czech Republic, Hungary, Kosovo, Slovak Republic, Slovenia, and Turkey

OEDFF
France

OEDGR
Germany

OEDIN
Bangladesh, Bhutan, India, and Sri Lanka

OEDIT
Albania, Greece, Italy, Malta, Portugal, and San Marino

OEDJA
Japan

OEDMD
Afghanistan, Algeria, Ghana, Islamic Republic of Iran, Libya, Morocco, Pakistan, and Tunisia

OEDMI
Bahrain, Egypt, Iraq, Jordan, Kuwait, Lebanon, Maldives, Oman, Qatar, United Arab Emirates, and Yemen

OEDNE
Andorra, Armenia, Belgium, Bosnia and Herzegovina, Bulgaria, Croatia, Cyprus, Georgia, Israel, Luxembourg, Moldova, Montenegro, Netherlands, Republic of North Macedonia, Romania, and Ukraine

OEDNO
Denmark, Estonia, Finland, Iceland, Latvia, Lithuania, Norway, and Sweden

OEDRU
Russian Federation and Syrian Arab Republic

OEDSA
Saudi Arabia

OEDST
Brunei Darussalam, Cambodia, Fiji, Indonesia, Lao People's Democratic Republic, Malaysia, Myanmar, Nepal, Philippines, Singapore, Thailand, Tonga, and Vietnam

OEDSZ
Azerbaijan, Kazakhstan, Kyrgyz Republic, Poland, Serbia, Switzerland, Tajikistan, Turkmenistan, and Uzbekistan

OEDUK
United Kingdom

OEDUS
United States