

## **Ardian Fullani: Issues related to the Bank of Albania's activities**

Speech by Mr Ardian Fullani, Governor of the Bank of Albania, at a regional meeting, Saranda, 24 September 2007.

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Honourable participants,

It is my special pleasure to come back to your wonderful city. Today's meeting is held in the framework of the new communication strategy of the Bank of Albania with various groups of interest. Meetings in different regions of Albania help us better understand the specifics characterising certain geographic areas, raising the premises for an ever more harmonic and complete development at the country's level.

I would like to elaborate with you some issues related to the Bank of Albania's activity, which I think, from the viewpoint of coverage and effects, involve all the groups of interest participating in this meeting.

First I would like to deal briefly with the issue of communication. Nowadays it is widely accepted that chances for long-term success become a reality if one is capable of communicating in proper language, with proper actors and on due time. More concretely, the central bank should constantly communicate simply and transparently with all market stakeholders, including the broad public, in order to be efficient and forward-looking. This is a necessary premise to guarantee institutional credibility, real independence and a sound accountability.

For a long time from now the Bank of Albania has started to think in a forward-looking way about this process and I may actually declare that we have already started to obtain the first fruits. According to different estimates, we deem that market efficiency is increasing, inflation expectations are anchored around our target, while the awareness of financial stability has been constantly increasing.

Notwithstanding the above, our claims in terms of information and clarification of Bank of Albania's decision-making are greater.

Proper language translation and understanding of the strategic and operational decisions (monetary policy decisions) is our strategic target. Our ambition in this regard is great and I would invite all the stakeholders in general and the banking system in particular to make more efforts for cooperation.

The Bank of Albania is confident that the financial market in Albania has already created a complete physiognomy. The participation of many foreign institutions of international reputation is a testimony in this regard. Recently its efficiency is enhanced, reflected in both, the traded volume and the reduced interest rate volatility. However, the Bank of Albania has noticed that the market should develop better and faster. Presently, I am of the opinion that there are no objective reasons that would weaken the financial market efficiency and in consequence the transmission of monetary policy to the economy.

The banking system has got all the possibilities and should interpret more correctly all the signals of the Bank of Albania, on due time and intensity. Also, the banking system should be seriously prepared not only with the respective structures, but also with professional human resources. This is a standard requirement, a postulate of modern times, to which we all should be committed at maximum.

I would let you know that the Bank of Albania has already prepared and soon enough will launch a specific package, centred on the efficiency of the financial market, particularly of the banking one. A new law on repurchase agreements, regulatory changes in required reserve

maintaining and calculation, rarefaction of Treasury bill auctions from the viewpoint of time, and presentation of the base rate are part of this package.

All these measures will be implemented as a sole package and will revolutionize the inter-bank market operation, a vital link of the financial market for monetary policy transmission to the economy. On the other hand, they would make the operational tactics of the Bank of Albania more efficient. I invite the banking system to become part of this process, actively participating in all consultations of the case that will precede the launching of this package. Its suggestions and comments are welcomed at any moment.

Monetary policy decision-making of the Bank of Albania is the second issue I would like to deal with. I would like to repeat once more that consumer price stability is the primary target of the institution I govern. Recently, I believe you have had the occasion to comprehend from the statement of the Bank of Albania Supervisory Council that the risk for an inflationary environment is present. Also, we have enlisted in our statements the probable factors, which according to our considerations make the concern real for inflationary pressures to the economy.

The data disclosed by INSTAT show that the annual inflation in August 2007 recorded 4.2 percent, somewhat above the upper limit of the targeted band of 2-4 percent. August recorded a high monthly rate, 2.1 percent, a wholly unusual figure compared to the preceding years.

I am confident that we have been understandable when evidencing in our analyses that the causes relate to unforeseeable factors (unforeseeable shocks) and other reasons that have to do with the demand of the economy for goods and services.

It should be underlined that during the current year the factors of first nature are numerous and relate to developments within the country and to "imported" developments from international economy. To be more concise, I would briefly highlight:

1. The energy crisis, which during this year appeared earlier than usual and according to different assessments, will continue beyond what the business may envisage in its plans at the beginning of each calendar year. Naturally, the effect of the lack of energy is very complex; it affects directly the productive capacities, creates additional cost (alternative source of energy) on final products, and increases the overall uncertainty. I think that these elements are sufficient to create ambiguity in the markets, generating inflationary premises in the economy.
2. During this year we have been faced with another problem. It has to do with an international conjuncture of raised prices, which exerts its impact on our market of goods and services. Fuels and cereals are more vulnerable by this conjuncture. The needs of our economy for these two articles are increasing, while the domestic resources are limited, making Albania dependant on imports, and in consequence on international market prices.
3. In general, the economy demand is estimated to have been high at end of 2006 and in the major part of 2007. This fact is evidenced in the large credit growth to the economy, in further enlargement of the current account, in increased imports of such goods as vehicles, household electrical appliances, and machinery and equipment. Generally, the increased demand at a certain period of time means inflationary pressures on the economy; therefore we have reasons to be seriously concerned about this problem.
4. Nowadays, public expectations for future inflationary developments are in the focus of the efforts of each central bank to ensure long-term price stability. More concretely, it has to do with the perceptions that every economic agent creates about future inflation. In some cases, these expectations are mostly based also on the facts verified in the past. But, successful is that central bank, which succeeds in anchoring these public expectations with a numeric target that it considers as the

optimal rate of inflation. Therefore, we are much focused in this direction, and I would like to once more emphasise in this meeting the Bank of Albania's attitude, that we remain determined in our efforts to keep inflationary expectations anchored around 3 percent, a figure that constitutes also our numeric target.

To this end, we will continue to orient our political and operational decision-making towards the meeting of this target".

As a final issue I would like to consider another major objective of the Bank of Albania, the one related to financial stability. As you may already know the Bank of Albania is the licensing and supervisory authority of the banking system and of some other segments of the financial system (non-banking financial institutions and foreign exchange bureaus). Being simultaneously even an important decision-making authority in the area of the financial and economic policies, it is understandable that a delicate challenge remains the harmonisation between both major priorities: effective monetary policy without damaging the financial stability and financial stability without damaging the monetary policy effectiveness.

Currently this is the trendiest issue. Many experts, decision-makers, academics are laying great emphasis on this problem and they rank the financial stability as a principal, which if shaken it takes upon itself the entire infrastructure from which it arose, from which it was nourished and grown. Therefore, I consider it important to come back and back to this issue.

Due to our not very distant history, I think that prudence in terms of financial stability is never excessive. I would like to assure you that the Albanian banking system is in a sound financial position, capitalised and profitable. Consolidation of the banking system through mergers and acquisitions, aiming at attracting internationally well-known investor with non-contestable experience in banking business is the prevailing philosophy in this regard. I believe that we have been successful in this direction. Recently there have been new entries in the system, highlighting internationally well-known banks, such as Intesa-San Paolo, Credit Agricol and Banka Societe Generale. As a conclusion, we may state that at present the Albanian banking system composition is appropriate, guaranteeing perspective support to the economy.

The entry of new banks has directly impacted on raising the value of the banking business in Albania, reflected, inter alia, in the increased competition among banks and aggressiveness of the banking system towards market share. The Bank of Albania deems that a reflection of this phenomenon is also the rapid growth of credit to the economy. More concretely, credit outstanding grew by 8 percentage points of GDP over three last years. In July '07 its annual growth was above 50 percent, which makes us believe that it may account for 28 % of gross domestic product at year end.

The Bank of Albania, in all its pronouncements, has argued that this phenomenon is a natural process that associates the banking business in every country. Also Albania, as most countries of the region, is under the rapid convergence process to certain parameters of the European Union.

To this end, we are completely aware of the fact that the growth rates will continue to be high. Leaving aside the probable effects on aggregate demand of the economy, I think that under the conditions of such rapid growth, the real challenge stands to the credit portfolio quality.

The Bank of Albania remains determined for the observance of the whole regulatory and supervisory package, which aims at guaranteeing a safe credit portfolio. We can not agree on some concepts crystallised recently, which make us understand that certain banks are running after the market share to the detriment of professional and rigorous treatment of applications for a loan.

Under the conditions when many objective obstacles exist, we deem that maximum prudence should be shown in extending loans. Let me remind you of the fact that we still inherit deficiencies in terms of ownership titles, collateral and its execution, address identification, property register and credit register. Non-recognition and non-acceptance of

the above deficiencies increases the likelihood that objectively or subjectively, decision-making for extending a loan may be wrong. I do not feel well when I see that in certain considerable cases, decision-making takes place within a short period of time, not sufficient enough to verify the case associating the credit practice.

I avail myself of this opportunity to require from the banking system to observe rigorously the banking supervision and risk management regulations. Given the current structures of credit stock to the economy, I consider it important to advise banks to seriously assess their exposure to foreign exchange risk and be prudent for its management.

Finally, I would draw the banking system attention also to another problem, which I have raised times ago. I have observed that there is greater prudence in terms of governance and internal audit, but there are problems in terms of transparency, window services, commission policies and recent innovations with electronic transactions.

Our support will not lack in this direction. You may consider the Bank of Albania as a possibility of permanent consultation and assistance. I would assure you that we are totally concentrated on and willing to support and assist any banking institution that aspires to bring innovation, Western practices and standards to Albania.

In conclusion, let me to say a few words about the city we are gathered today, about the potential and support the banking system will provide to it.

Today Saranda is one of the most culminant places and may be the best show-case of possibilities and quality of the Albanian tourism, of this important sector that presently contributes by 9 % to the country's gross domestic product.

Currently the figure of 1 million tourists a year has become a reality and its perspective goes even beyond, if we continue to pay necessary economic, social and institutional attention to tourism. Beyond such impressive figures, the tourism development is translated also into a constant improvement of Albania's image as a country under progress, of values it possesses and provides, of increased level of employment and revenues for many areas and strata of population, as provision of values of many environmental, historical and cultural, geographic and curative, economic and social potentials, etc.

Notwithstanding this optimistic situation, we should not forget that Albania is a Mediterranean country, found in one of the most developed tourism areas of the world, in one of the areas of the largest variety of types of tourism, and therefore in one of the areas where competition in tourism service is in its peak, where many of the countries of the region, with a very long tradition in this sector, have turned it into a real tourism industry.

Our objectives to improve rapidly and to solve qualitatively the problems of road infrastructure, water and electricity supply, sewerages, etc., should be attached to improved quality of services and implementation of standards, completion of regulatory and urban plans for all tourism areas, variety of types of tourism and tourism products. Besides the coastline tourism, which is dominant, the mountainous and rural tourism, cultural and historical tourism, archaeological and nature tourism, curative and sports tourism, massive and elite tourism should be also developed. All these are going to make the sector and the activity directly or indirectly related to tourism absorb more investments and loans, making banks, domestic and foreign businesses, private and institutional investors, etc., more interested and guaranteed for success.

You should be convinced that the banking business is observing you attentively, expecting a signal, a sparkle which is mostly at your hand. The standards are indispensable and should be respected. Therefore, I would invite the local government, the business community, the individuals of Saranda to be oriented towards the future, towards tourism and urban development models, similar to those of advanced countries.

Let me conclude by thanking you once more for your hospitality.