

Ardian Fullani: Strengthening linkages in South East Europe. Policy anchors and business perspectives

Speech by Mr Ardian Fullani, Governor of the Bank of Albania, at the joint conference of the Bank of Albania and the University of Oxford “Strengthening linkages in South East Europe. Policy anchors and business perspectives”, Tirana, 19 September 2013.

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Your Excellency Prime Minister of Albania,

Honourable guests from the University of Oxford,

Dear representatives of the diplomatic corps and academia, dear participants,

I have the pleasure and honour to open this joint conference of the Bank of Albania and the University of Oxford, on strengthening the linkages between the economies in our region. Three years ago, in September 2010, we invited the University of Oxford to support the academic discussion of the Bank of Albania on the economic growth model and its regional character. At that moment, this debate was misinterpreted as a discussion on the advantages of the market economy and alternative philosophies of the economic organisation of a society. Nonetheless, after three years, we all find that the economic growth model has become the main topic of academic, economic and political debate.

For a number of years, our economy has been under the grip of the global crisis, reflected mainly in a decelerated economic activity. Consequently, investments and lending to the economy slowed down, deteriorating, at the same time, the private and public sector balances.

In spite of these developments, the Albanian economy has managed to maintain price stability and the overall macroeconomic and financial balances. The Albanian financial system has proven highly immune. Despite the economic growth slowdown, overall, this system remains liquid, well capitalised and profitable, reflecting the prudent work of the Bank of Albania over the pre-crisis years.

Bank of Albania’s prudent policies and the reaction of the banking sector enabled the system to avoid extreme problems, which would require the use of public funds. We should bear in mind that various banking groups from EU countries, heavily hit by the crisis, operate in Albania.

The stability of the banking sector has been at the heart of work of the Bank of Albania, focusing on both financial stability and banking supervision, and on monetary policy and liquidity management.

The Bank of Albania has been proactive and has anticipated problems, aligning itself and the role of its policies with global developments and the domestic market state of affairs.

The dim global financial and economic situation has dictated the need to redefine the role of institutions, including the central bank. Presently, the central banks have turned to macroprudential measures, because the traditional mechanisms of monetary policy transmission are suffering from burdened balance sheets of the private and public economic agents. To better coordinate this role and monitor the economy, central banks around the world are supporting their monetary policy with the necessary macroprudential measures. These global developments find the Bank of Albania well prepared and equipped with the required experience. Its structure is similar to the one being adopted by the European Central Bank and other central banks in developed countries. Moreover, the Bank of Albania has now several years of successful experience in employing countercyclical measures to manage the country’s macroeconomic and financial equilibrium.

I would like to underscore the change of risk coefficients for controlling the expansion of lending in foreign currency, and the introduction of limits of credit to collateral ratio for controlling the size of debt in the economy.... to mention just a few.

One of the most important lessons from the global crisis is that addressing the monetary stability (i.e. price stability) and financial stability issues independently does not provide an optimal solution and is crisis-prone. The economy functions as a complex mechanism with often fragile and interdependent equilibria, which do not respect boundaries of institutional responsibilities. For each economy, there is only one interest rate, only one critical mass of financial intermediation and a fragile equilibrium of financial sector balances that guarantee sustainable and long-term development for the country. Harmonising these three objectives is a prerequisite for maintaining the financial equilibrium of the economy. Therefore, their identification and harmonisation under one roof is considered as the optimum solution to guarantee the country's economic and financial stability. For that reason, one of the most pursued practices for post crisis institutional regulation is not only unification of supervisors of the financial system, but also their institutional integration with other functions of the central bank.

Your Excellency Prime Minister of Albania,

Dear participants,

Unquestionably, in the long term, economic growth of a country is determined by the labour force and its qualification, productivity, technology and innovation capacities; as well as the capital accumulation scale, which in itself, reflects both social preferences and fiscal stimuli and the development level of the financial system. These three sets of factors are conditioned by the economic structure of a country and they are encouraged and stimulated through structural reforms. Again, in the long term, economic growth is determined only by the structural reforms and the degree of competitiveness of our economy vis-à-vis our trading partners and the global market. On the other hand, the duty of the fiscal and monetary policies is to avoid short-term deviations of the economy from this long-term trend and create a sustainable environment for the country's economic and financial development.

The Albanian economy has already started its journey towards integration with the European Union. The ultimate goal of this process is to improve the economic welfare. It also implies to fully integrate with the trading, industrial and financial chains; adopt a unique economic management philosophy, a unique regulatory and institutional practice; and acknowledge the harmonised rules of the game applied throughout the European area.

In this context, I would like to highlight two key moments:

- **First, the European integration process should be our strongest anchor for structural reforms:** legal, regulatory, institutional, infrastructural, or political ones. Albania has still a long way to go and the peculiarities of our economy provide the necessary space to calibrate these models in accordance with the comparative advantages and primary needs of the country. However, I believe it would be useful to have all the reforms integrated in a unique vision of integration.
- **Second, the Albanian businesses should do a lot more to hasten the integration process.** It should be more active to adopt advanced technologies, and production and management processes.

Likewise, the Albanian financial sector should be more visionary in its policies and priorities about the distribution of financial resources, and work harder to attract more foreign investments and build bridges of cooperation with local businesses.

We have rightly underlined that regional cooperation is a necessary move that should precede the European integration process. The economies of the region are small compared

to our trading partners, but the establishment of unified zones in terms of customs duties, legal systems and practices, integration of financial practices and development policies provides the right incentives to attract foreign investments and empower our negotiation capacities with international partners.

Concluding, I would like to reiterate that the Bank of Albania considers the economic and financial stability of the country as a prerequisite for sustainable and long-term development. Now, this is no longer a theoretical matter of disciplining the behaviour of politics towards the economy, nor is it a discussion on respecting the equality of generations. It is a bitter lesson learned from the latest crisis and a tangible reality for many countries of the euro area. We have persistently invited policymakers and economic agents in the country to partake in this vision.

As the country's monetary authority mandated to guarantee price stability, we have worked and will continue to do so to ensure a low-inflation environment. This environment boosts the guarantees for savers and investors for their long-term plans and provides for financial system development. The Bank of Albania implements a modern monetary policy based on the most advanced principles of central banking, and employs instruments and communication approach in line with ECB practices. The commitment of the Bank of Albania to maintain price stability is the polar star of our work. ***Drafting and implementing the monetary policy independently, exclusively in the function of price stability, is one of the domestic anchors of the Albanian economy, which should be preserved and strengthened.***

In parallel, the Bank of Albania deems that the Albanian economy needs two additional anchors: financial stability and fiscal stability.

Our regulatory and supervisory function over the banking system, which accounts for 95% of the financial system in Albania, has proven successful in guaranteeing the country's financial stability. This function has been carried out and is discharged in line with the international best practices, in constant cooperation with homologous institutions and other international partners.

The possibility to have an integrated vision of economic and financial developments, and to combine but not mix the monetary policy with macroprudential measures, has enhanced the effectiveness of Bank of Albania's actions, and has contributed to better achieving the two individual objectives: financial stability and price stability. ***The institutional regulation, which has proven effective and is in line with the latest global trends, should continue to function as a second anchor of domestic economic anchors.***

Finally, the Bank of Albania deems that Albania should immediately establish not only a clear and transparent fiscal rule, but also an effective one to discipline the fiscal policy and maintain the trust of financial markets in public finance soundness.

This third anchor would complete the framework of domestic anchors of economic policy. Together with the close cooperation with international financial institutions, it would provide a consistent and transparent framework for the country's development. Provision of liquidity and solvency of the Albanian economy through bilateral and multilateral partnerships is a priority for central bank policies. This vision and partnership should become the axis of cooperation between national institutions.