

Ardian Fullani: Imagine the future – for a better economic cooperation. Economic chamber's and bank's responsibilities

Speech by Mr Ardian Fullani, Governor of the Bank of Albania, at the 10th Vienna Economic Forum, Vienna, 7 May 2014.

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Dear Ladies and Gentlemen,

Dear colleagues and participants of the Vienna Economic Forum,

I am honoured and delighted to return and speak to such a constructive and important economic forum, discussing with you the economic development topics, which affect the present and the future of our economies.

The topic of this forum is very important for the economies of the South East Europe. It creates the proper environment, which enables the examination of the problems faced by our economies during the crises. We can certainly draw few lessons from what we have learned during the recent years, following the global economic and financial crises. These discussions and the harmonization of economic policies will help us to project a strong coordinated economic structure for the long term future of our economies.

It is particularly important to converge here in Vienna and discuss the cooperation issue because one of the obvious outcomes (lessons) of the developments during the recent years is that the economic developments in particular for small open economies of the South East European region, are not local or regional anymore. Just like the flu, it is rather unexceptional and highly transmittable from one economy to the other, from one sector of the economy to the other.

Most importantly, European economies and their financial systems, among which the Austrian financial system enjoys a significant share of the market, define the globalization for the region and are, to a large extent, important determinants for the success or failure of these economies. Given the large share of the European financial groups, they have and will play an important role in the transmission of global shocks in the region. What is more important, they have a significant role in the transmission of legislative and regulative shocks carried over by European monetary and supervisory authorities. The size is such that even a simple change in the future business plans of a single European financial institution can transform into real shocks for the economies of the region.

It became evident during the crisis and afterwards that an increase in risk and uncertainty, led to increased incentives for banks to withdraw from the Emerging Europe economies. Though this was mostly prevented due to increased cooperation through institutions such as the Vienna Initiative, the concerns from our perspective have not completely dissipated. In this respect the business plan of EU based groups can play a potentially important role in the nature and outcomes of this cooperation. The crisis showed few weakness in the model of growth adopted by the emerging economies of South East Europe, but is also true that, to some extent this behaviour was also encouraged by the development strategies of financial groups in the region, as it is also true that there was also some weakness in the coordination and collaboration between different European Union institutions, such as monetary policies (ECB), fiscal policies (of member countries) and the inexistence of specific mechanisms (such as bailout funds) to safeguard the European Union during difficult economic times.

This conference pays homage to these lessons, while acknowledging the importance of coordination, by mutually collaborating in multidimensional institutional levels, within the region and with our common partner countries. We in the region hope that our foreign partners share this same view.

The Albanian economy and its financial market share similar characteristics with the other economies of the region. Our main trade and financial partners come from the EU economy. Therefore, developments in the EU are directly and indirectly transmitted and play an important role in economic developments in Albania. Our reliance on EU affected not only our economic development but also constrained the effect of policy measures.

Several European banking groups operate in the Albanian financial sector. These entities brought into the Albanian market a lot of valuable know-how and experience, playing, thus, a crucial role in the financial integration of the Albanian economy to the European Union. However, EU supervisory regulations and risk requirements for European financial groups, along with the approach in which they are implemented, are posing significant constrains on our economy and the efficiency of monetary policy to respond to economic developments. Faced with new and stringent capital and risk requirements, banks are trying to comply by adjusting their future business plans and the size and composition of their balance sheets in the economies of the region.

These tighter regulations approved by European Supervisory and Banking Authorities and, subsequently, implemented by parent banks have already been accompanied by a decreasing level of credit to the economy. Our research shows that further tightening of crediting, due to the legal reforms currently under way, could have an important effect not only on economic activity but also on commercial bank asset quality itself, in particular situation with non-performing loans. A deterioration of economic activity would play out mostly in the same way, leading to worsening of NPL ratio, leading to smaller banks' profit and tighter capital constrains, along with slower growth. This second channel is seen as arguably more dangerous, with the empirical research pointing out that the elasticities are close to twice as large for a shock of similar size.

Such adjustments are imposing significant constrains on our economies. More directly, we have observed a decrease in financial intermediation, by tightened lending procedures even for economies or sectors that were doing ok during the crises. As a result, this was reflected in stagnating investments and slowing down dynamics of the Albanian economy, both in the private and public sectors. Moreover, current business practices and policy orientations are imposing significant constrains in the efficiency of monetary policy transmission mechanism, and the ability of authorities to provide much needed stimulus to the economy.

It is understandable that banks would have to be careful, prudent and responsible given the current situation with non-performing loans; however, they must also consider the fact that credit and financial intermediation is important for growth, which, in turn, can improve the ability of economic agents to repay their loans. This is especially true for particular sectors like agriculture and agro-business, which, so far, have not benefited from credit expansion, but have large untapped potential for growth.

The era of an economic growth model, led mainly by the domestic consumption, is now gone. Banks, their European headquarters and their supervisory authorities should work together with authorities of host countries to develop a new long-term and sustainable economic growth model. This new model needs to be based on investments in productive sectors of the economy. Our products and services need to be competitive not only in the home market, but they should also offer comparative advantages in the regional and European Union markets. It is clear that cooperation is the only choice for the future.

For more than 15 years now, the European integration, in all its politic, economic and financial dimensions, has been main driving force for the economic and social prosperity of South East European region. EU represents the main trading partner, a large share of FDI, by far the biggest investor in the Banking System. Our countries have undergone through structural reforms, adaptations of regulatory and legislative frameworks, institutional adaptations to adjust to these partnerships.

Led by the European integration process, countries of the region have also signed bilateral free trade agreements among them. Our studies at Bank of Albania show that these free

trade agreements have positively affected trade flows among West Balkan countries. However, these studies also suggest that trade flows among Balkan countries are below their potentials. The aims of these bilateral free trade agreements are to create a regional free trade area among West Balkan countries.

Authorities in South East European countries have shown signs of consistent regional collaboration; however, they need to make additional efforts to unify and harmonize their legal, institutional, regulatory and infrastructural frameworks. These efforts need to be supported by a clear commitment by EU financial groups to the region's small open economies. The development of the regional markets for products and factors, investment in education and improvement of human capital, exploitation of economies of scale and comparative advantages, will depend on the availability of credit and investment and the financial support of the banking system. In this respect, EU financial groups will be instrumental factors for building bridges of cooperation among economies of the region and its transformation into a larger, better integrated, more competitive, more profitable and prosperous economy, eventually leading to a prosperous economic future through economic cooperation. In this respect, I encourage foreign groups to adopt a regional rather than a country specific view when considering their future in the region. It goes without saying that any policy that restricts commitment and exposure of EU financial groups in the region does not support economic cooperation among our countries. It rather creates a struggling environment and a less prosperous future for all economies of the region.

The Western Balkans region offers great opportunities and profitable perspectives for EU-based corporations and financial groups. The harmonization of above-mentioned reforms will create an even more attractive environment for different private entities interested in investing in our region. I invite EU financial groups to see the region under this perspective.

European institutions and financial groups should support and become a positive force to facilitate, smoothen and support regional economic cooperation, which will lead to a better prosperous future and a faster European integration process of the region.

Thank you for your attention!