

dzfjkl

Albania: Poverty Reduction Strategy Paper—Annual Progress Report

Poverty Reduction Strategy Papers (PRSPs) are prepared by member countries in broad consultation with stakeholders and development partners, including the staffs of the World Bank and the IMF. Updated every three years with annual progress reports, they describe the country's macroeconomic, structural, and social policies in support of growth and poverty reduction, as well as associated external financing needs and major sources of financing. This country document for **Albania**, dated **June 2005**, is being made available on the IMF website by agreement with the member country as a service to users of the IMF website.

To assist the IMF in evaluating the publication policy, reader comments are invited and may be sent by e-mail to publicationpolicy@imf.org.

Copies of this report are available to the public from

International Monetary Fund • Publication Services
700 19th Street, N.W. • Washington, D.C. 20431
Telephone: (202) 623-7430 • Telefax: (202) 623-7201
E-mail: publications@imf.org • Internet: <http://www.imf.org>

Price: \$15.00 a copy

**International Monetary Fund
Washington, D.C.**



REPUBLIC OF ALBANIA
MINISTRY OF FINANCE

Progress Report on Implementation
of the National Strategy
for Socio-Economic Development
during 2004

Objectives and long-term vision
Priority Action Plan 2005-2008

June 2005

ACKNOWLEDGEMENTS

Albanian Government gives a very special attention to the National Strategy for Socio-Economic Development, NSSED, in formulating, implementing, monitoring and updating it. The current document testifies to it.

NSSED is increasingly considered as a basic document that combines the main agendas of government for reducing poverty, for guaranteeing a sustainable economic growth, for achieving the Millennium Goals, for integrating the country into NATO, EU and the region etc. Governance modernization has been one of the biggest challenges that the Government of Albania has been faced. Designing and approval by the Albanian Government of the Integrated Planning System constitute an important step towards the establishment and strengthening of the entire strategic planning system, medium-term budgeting, public investments administration, foreign aid coordination, EU integration process, planning of sector and cross-cutting strategies etc.

NSSED is creating a mid-term and a long-term vision of the development of the country by seeing it as an increasingly open and clear process that enables a large-scale participation of all contributors, such as: parliament, civil society, local communities, business community, political spectrum, scholars and scientists and other interest groups. NSSED constantly and thoughtfully has been consulted with our international partners that encourage Albania in its efforts to carry out the developing and integrating reforms.

Considering this document as a significant piece of work, I wish to express my appreciation for performing the assigned task to the Ministry of Finance, the NSSED Department, the Monitoring and Evaluation Units, Technical Working Groups, at all the Line Ministries, INSTAT and to other public institutions involved.

I wish to express my gratitude to the World Bank and to DFID for their essential technical support in providing this document. I fully appreciate the role of IMF, PNUD, OSCE, USAID, Dutch Government, UNICEF, OXFAM, MADA which assisted in implementing and updating NSSED, raised the scale of participation, and facilitated the consultations with parliament, civil society and other interest groups.

I owe all the Albanian experts a debt of gratitude for their part in providing this document: Adrian Civici, Gelardina Ducka, Kloalda Kamberi, Evis Zykaj, Venera Demiri, Luiza Jano, Sybi Hida, Milva Ekonomi, etc.

PRIME MINISTER

FATOS NANO

Table of Contents

1	The NSSED and strategic planning in Albania	4
2	Macroeconomic conditions	9
3	Socioeconomic conditions	22
4	Progress with the implementation of the NSSED	37
5	Monitoring and evaluation	84
6	Recommendations for the MTBP 2006-2008	92

Annexes

Annex 1	Selected monitoring indicators	98
Annex 2	Mid-term plan of priority actions	100
Annex 3	Sector and crosscutting strategies	125
Annex 4	Public expenditure management calendar	127

List of Tables and Figures

Table 2.1	Key macroeconomic indicators	9
Table 2.2	Sectoral structure and growth	10
Table 2.3	Main macroeconomic indicators for 2005	20
Table 2.4	Main fiscal indicators for 2005, as a proportion of GDP (%)	20
Table 3.1	Headcount poverty changes between 2002 and 2003	23
Table 3.2	Changes in estimated per capita consumption between 2002 and 2003	23
Table 3.3	Self-rated health status of individuals aged 15 and over, 2002 (%)	28
Table 3.4	Mean usage of health services, 2002 and 2003	30
Table 3.5	Relationship between smoking and self-rated health status of men, 2003	30
Table 3.6	Labour force participation according to the 1989 and 2001 Census	31
Table 3.7	Employment status of working age individuals, 2002	32
Table 3.8	Employment status of working age individuals, 2002 and 2003 (%)	33

Table 4.1	Fight against drugs	39
Table 4.2	Local government spending, in Lek million	43
Table 4.3	Selected performance indicators of the anti-corruption action plan	46
Table 4.4	Maritime transport indicators	56
Table 4.5	Air transport indicators	57
Table 4.6	Telecommunications sector indicators	57
Table 4.7	Average cost per student in 2004, in Lek	63
Table 4.8	New and reconstructed health centres and outpatient clinics	68
Table 4.9	Number of compulsory and voluntary contributors to social insurance	74
Table 4.10	Activities of the Environment Inspectorate in 2004	75
Table 4.11	Access to financial services in rural areas	80
Table 4.12	Activities of Saving-Credit Associations	80
Table 4.13	Food quality controls, 2003-2004	81
Table 5.1	Main NSSED objectives	85
Table 5.2	Millennium Development Goals, selected indicators	86
Table A1.1	Selected monitoring indicators	99
Figure 1.1	Albania's proposed planning architecture	5
Figure 2.1	Economic growth in Albania and selected countries, 1998-2004	10
Figure 2.2	Lek exchange rate with the Euro and the dollar	13
Figure 3.1	Enrolment status of children aged 7 - 18 years, 2002	27
Figure 3.2	Self-rated health status by housing conditions in urban areas, 2002	29
Figure 3.3	Self-rated health status by housing conditions in rural areas, 2002	29
Figure 3.4	Unemployment rate according to the standard and relaxed definitions	33
Figure 3.4	Water source and quality, 2002 and 2003	35
Figure 3.5	Perception of the electricity service quality between 2003 and 2002	36
Figure 4.1	Execution of cases by Bailiff's Offices	38
Figure 4.2	Proportion of unconditional local government grant, revenues and small business tax to total spending 1999-2004	44
Figure 4.3	Number of tourists and revenue from tourism, 2002-2004	54

Figure 4.4	Structure of energy consumption	55
Figure 4.5	Licenses provided to private sector health providers	68
Figure 6.1	Expenditure in priority sectors as proportion of total, 2002-2004	92
Figure 6.2	Capital expenditure in priority sectors as proportion of total, 2002-2004	93

1 The NSSED and strategic planning in Albania

Albania has made enormous strides in recent years with greatly improved economic performance and sustained growth. The NSSED established a multi-year plan to combat poverty and strengthen governance. A permanent organisation was established in the Ministry of Finance, a deputy ministers' network was created to ensure coordination, consultations with civil society were undertaken, ministries compiled detailed 4-year plans, and attempts were made to link these plans to higher level goals and objectives. Two annual progress reports have been approved and publicly distributed that offered the opportunity for debate on policy issues.

However, the policy challenges over the next decade will intensify as Albania pursues European and NATO membership, enhances its economic competitiveness, and moves steadily towards the Millennium Development Goals. The pace, scope and complexity of demands on decision makers and the public administration will continue to increase.

To address necessary improvements and in the framework of its own objective to modernise, the government established in April 2004, by order of the Prime Minister, a Technical Secretariat for donor coordination to develop a strategic, integrated, and accountable planning architecture for Albania. The objectives of the Secretariat are to:

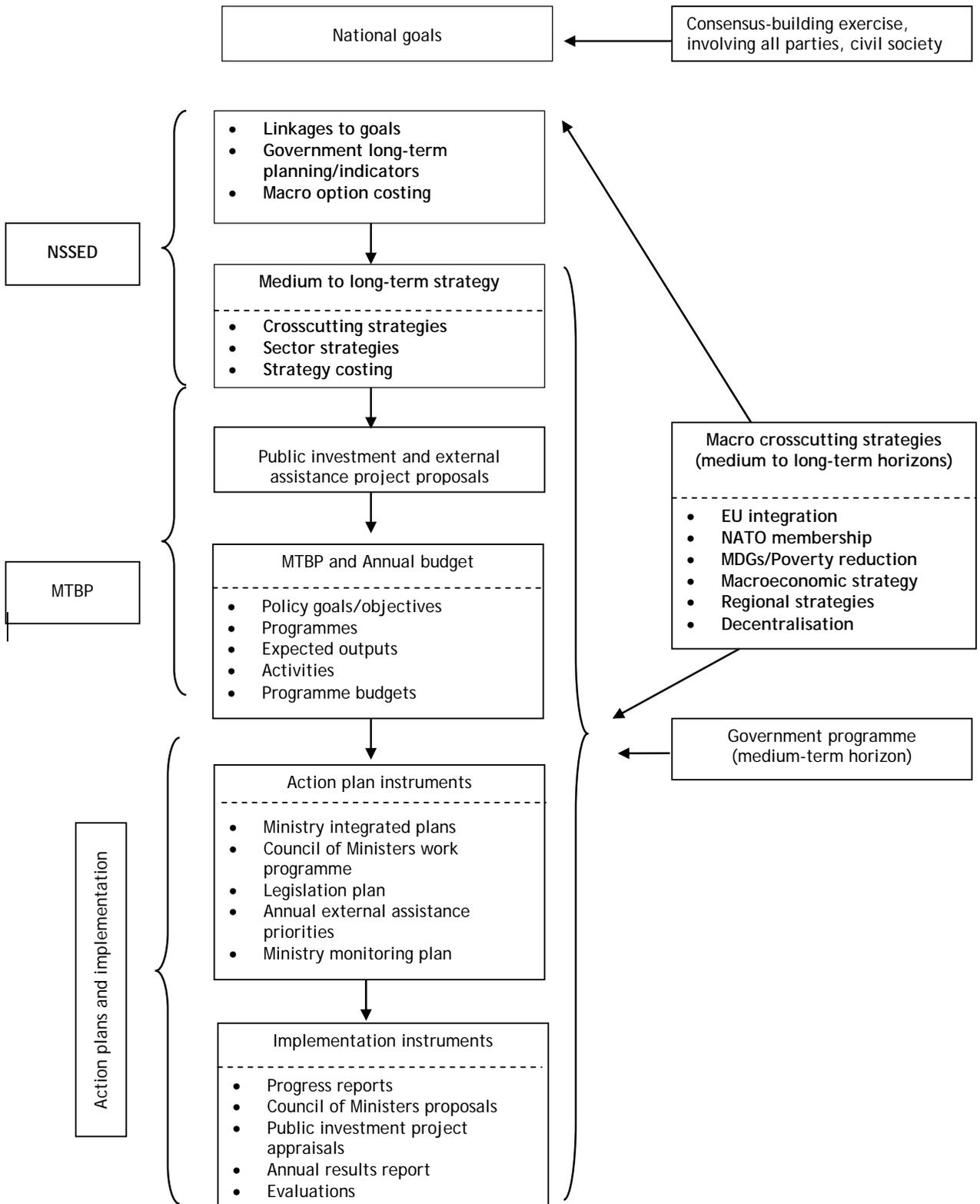
- better enable the Council of Ministers to provide strategic policy direction within a sound fiscal framework;
- harmonise and streamline existing systems within a new, integrated planning system;
- ensure that external assistance effectively supports the Government's strategic priorities;
- realign organisational structures to deliver the new system; and
- identify implementation requirements to phase in the proposed changes.

The Technical Secretariat consists of six members representing the Prime Minister's Office, the Ministry of Finance, the Ministry of Economy, the Ministry of European Integration and the Department of Policy Development and Coordination at the Council of Ministers. In collaboration with international experts, the Secretariat developed a functional organisational structure to guarantee a long-term institutional solution of aid coordination and government planning. A final proposal was prepared in January 2005. This was reviewed and approved by the Economic Policies Committee in March 2005 and by the government in April 2005. In May 2005, a joint conference was organised by the Government and Donor Technical Secretariats to launch the document. An action plan for the implementation will be prepared and approved in June 2005.

The proposal presents a new planning architecture for decision makers. Its proposals are wide-ranging and with significant implications for government decision making, strategic planning, medium-term budgeting, public investment management, external assistance management, European Union integration planning, government programme planning, sector and crosscutting strategies, legislation planning, monitoring and database support, reporting of results and accountability, the organisation and the role of affected departments in central institutions and line ministries.

As Figure 1.1 suggests, the pillars for a new planning architecture already exist. The challenge is not in building up a new system but in reshaping, harmonising and connecting existing fragments that are currently not fully connected.

Figure 1.1 Albania's proposed planning architecture



If the planning system is to be more strategic:

- decision makers must be more actively engaged at the outset rather than the conclusion of the planning process and be provided with high quality policy options that clearly identify the fiscal impacts of various choices;
- the NSSED must shift its focus from short- to medium-term ministry action plans to medium to long-term planning for all national priorities without losing its poverty reduction emphasis;
- the NSSED must create a policy-driven system in which a medium-term policy framework, comprising mutually consistent sector and crosscutting strategies, supports long-term national goals and advises the government on strategic priority options;
- the government must annually establish strategic policy priorities within the context of the government's macroeconomic framework; this will, in turn, guide the setting of ministry medium-term budget ceilings;
- the NSSED and Medium-Term Budget Programme (MTBP) priority planning process should be formulated within the programme budget structure; programme expenditure decisions accordingly will depend on related policy goals/objectives and expected results;
- public investment (domestic and foreign-funded) and technical assistance projects must be identified in advance of specific planning exercises and be derived from sector strategies;
- an annual external assistance priorities document must be developed, as a product of the planning process, to enable informed deliberations with donors that link external assistance needs to government priorities; and
- the Council of Ministers' annual legislative and decision-making programme must similarly derive from the strategic planning process delivered through the NSSED and the MTBP

If the planning system is to be integrated:

- policy and financial planning must be presented as components of a single planning system;
- public investment and external assistance must be recognised as key contributors to policy goals and objectives within the NSSED and MTBP frameworks;
- European Union integration planning must be reflected in all phases of the planning process;
- the Government Programme and cross-cutting strategies (e.g. decentralisation, anti-corruption) must similarly be incorporated within the planning architecture; and
- monitoring must be designed to track performance against major priorities of all frameworks

If the planning system is to be accountable:

- the roles of decision makers, central institutions, and line ministries in overseeing and delivering the new architecture need to be clarified;
- clear, meaningful statements of expected results must be provided for each programme;
- sufficient resources must be allocated to approved legal commitments; unfunded legislative mandates will not proceed to Parliament;
- accurate, timely information on achieved versus expected results must be provided in an annual report made available to Parliament and the public;
- consultations undertaken through NSSED with civil society and expert external groups must be adapted and strengthened as an essential component of policy development;
- active monitoring by the centre must focus only on the significant commitments; and
- line ministries must be delegated sufficient authority and resources to manage effectively

These design parameters establish the framework for the proposed integrated planning system. The next section reviews the key implication of the new system for the operation of the NSSED.

The NSSED in the Integrated Planning System

The main implication of the Integrated Planning System for the NSSED is that it will evolve into a comprehensive strategic planning framework. Its focus will accordingly shift towards medium to long-term planning, ensuring that coherent, costed, mutually consistent sector and cross-cutting strategies are developed and that these support the national vision and serve as the policy basis for the annual MTBP process. The position of the NSSED in the annual budget calendar and the links between institutions are further elaborated in Annex 4.

While retaining responsibility for the poverty reduction strategy, the primary mandate of the NSSED Department will be to ensure that all national goals, including EU and NATO membership, the MDGs, good governance and decentralisation, are appropriately reflected. Rather than monitoring ministry action plans, the NSSED will identify high-level indicators and use specialised research to determine how well Albania is progressing towards its medium- and long-term goals.

The key process improvements for NSSED will be to clarify its own planning architecture, focusing on medium to long-term planning, and to expand its scope to cover all national and government priorities. In addition, it will develop a transition plan whereby the existing sector and crosscutting strategies (see Annex 3) approved by the government are reviewed for ongoing relevance and adherence to newly-developed standards. Attempts will be made to cost these strategies to ensure that each one reflects internal tradeoffs and to assist the government make choices between competing strategies. It should be emphasised that indicative costing at this level is far from precise and that only through the MTBP process will detailed tradeoffs emerge.

Sector strategies will be the linchpin of the new system, integrating policy and financial planning and connecting medium- and long-term planning with budget formulation. They will need to be frequently reviewed to ensure they reflect the current policy influences exerted on that sector. As sector strategies do not yet exist in all sectors, the NSSED Department will be mandated to initiate a multi-year process to assess and adapt existing sector strategies and work directly with ministries on developing new ones.

To summarise, in making this shift to a policy-based, strategic planning framework, the NSSED Department will be:

- identifying linkages to national goals
- developing and monitoring high-level indicators
- overseeing indicative costing of medium- and long-term strategies
- overseeing cross-cutting strategies
- overseeing sector strategies
- developing poverty reduction policy directions
- integrating coherent regional and decentralisation strategies
- advising on policy implications of MTBP expenditure ceilings

A process to revise the NSSED is expected to begin in late 2005 and run throughout 2006. The NSSED Department will coordinate the government's participation in the exercise and will ensure coherence between the 3- to 5-year medium-term strategy and the national goals. The extent to which all of these functions can be fully carried out will also depend on institutional changes to build the capacity of the NSSED Department.

Structure of the Progress Report

In the 4th Review Under the Poverty Reduction and Growth Facility (July 2004), the government committed itself to a new NSSD progress report, "taking into account the recommendations of the joint staff assessment of the 2004 progress report". The envisaged reform of the planning system is the key government response to fulfil its commitment. These changes will take place over the next few years. This Progress Report takes a number of steps in this direction.

Chapter 2 reviews the macroeconomic developments: economic growth and the structure of the gross domestic product, the balance of payments, exchange rate movements, the structure of exports, public finance, revenue collection, monetary policy, inflation and the labour market. The macroeconomic projections of the Ministry of Finance are presented at the end of the chapter along with a brief discussion of current thoughts within government to build capacity in developing alternative macroeconomic scenarios for policy purposes.

Chapter 3 provides an overview of socioeconomic conditions. The findings are primarily based on the 2002 and 2003 waves of the Living Standards Measurement Survey, which is the foundation of the poverty monitoring system. The update on the poverty profile is based on an analysis by a research team at the FAO. It suggests that high rates of economic growth over recent years have a positive impact on living standards. Other aspects of living conditions, such as education, health, employment, water and electricity, are also discussed. This analysis was conducted using skills developed within the NSSD Department.

Chapter 4 presents the line ministry responses with respect to the implementation of NSSD activities. A number of line ministries received a special response form with questions focusing explicitly on policy issues. An extended discussion of issues related to the decentralisation and European integration strategies is included. The NSSD Department also initiated two studies that used statistical data to inform policy questions; their results are summarised. The findings of numerous other studies that have touched upon policy issues are presented throughout the chapter to inform policy discussions.

Chapter 5 summarises the progress in the implementation of the NSSD in terms of the key indicators and the Millennium Development Goals. This year, the NSSD Progress Report also doubles as the MDG Progress Report. This is part of the attempt to shift the focus to outcome and impact indicators, a process that will be completed during the revision of the NSSD. Annex 1 includes a supplementary list of indicators that provide a basis for discussions on monitoring that will take place over the next few months.

On the basis of the progress achieved and the remaining challenges, Chapter 6 provides a set of recommendations to inform this year's Medium-Term Budget Programme process. In response to calls for closer links between the two processes, the NSSD and Budget Departments have worked closely together in the preparation of this year's Progress Report. In previous years, line ministries were almost simultaneously requested to submit matrices of mid-term policy priorities for the two planning processes. To avoid duplication of effort and to minimise the possibility that priorities are not embedded in the public expenditure management process, this year's NSSD Progress Report priority matrices constitute the ministries' contribution to the first planning stage of the MTBP process, namely the Programme Policy Review / Sector Expenditure Strategy. This was decided in view of the fact that over the coming years the NSSD Department will gradually assume the responsibility for the coordination of precisely these sector strategies. The matrices are presented in Annex 2. Although the process is incomplete, it represents a marked improvement in terms of a critical process that aims to link policies to the budget.

2 Macroeconomic conditions

Economic developments during 2004 have followed a similar pattern to 2003 and have consolidated the progress made since 1998, with the following key features:

- Relatively high economic growth (at about 6% in real terms);
- Low annual inflation (at 2.9%);
- Decreasing deficit of the government budget (down to 4.6% of GDP);
- Improvements in the balance of payments, with an increase in reserves;
- Strong exchange rate.

If the current progress in Albania can be maintained over the next decade, the incidence of relative poverty should be halved, absolute poverty will be eliminated, average incomes will be nearly double their current levels and the gap between Albania and neighbouring countries will be substantially reduced. The main macroeconomic indicators for 1998-2004 are given in the table below:

Table 2.1 Key macroeconomic indicators

		Unit	1998	1999	2000	2001	2002	2003	2004
Population		Million	3.35	3.37	3.23	3.08	3.10	3.10	3.12
Inflation (average)		%	20.9	0.4	0.0	3.1	5.2	2.4	2.9
Exchange rate		Lek / \$US	150.6	137.7	143.7	143.5	140.2	121.9	102.8
		Lek / Euro		147.0	132.6	128.5	132.4	137.5	127.7
Output									
Gross Product	Domestic	Lek billion	412.3	474.3	530.9	588.7	630.0	695.1	780.1
Gross Product	Domestic	\$ billion	2.7	3.4	3.7	4.1	4.5	5.7	7.6
Real GDP growth		%	12.7	10.1	7.3	7.2	3.4	6.0	6.0
GDP per capita		Lek thousand	122.9	140.6	164.3	191.4	203.4	223.9	249.9
GDP per capita		\$	816	1021	1143	1334	1450	1837	2431
Public finance									
Total revenue		Lek billion	102.5	123.2	130.6	145.6	154.6	167.2	184.4
Total expenditure		Lek billion	141.6	165.7	170.6	186.1	192.5	201.2	222.4
Overall deficit		Lek billion	-39.1	-42.5	-40.0	-40.4	-37.9	-33.9	-38.1
Total revenue		% GDP	24.9	26.0	24.6	24.7	24.5	22.4	23.6
Total expenditure		% GDP	34.3	34.9	32.1	31.6	30.6	27.0	28.5
Overall deficit		% GDP	-9.5	-9.0	-7.5	-6.9	-6.0	-4.6	-4.9
Internal debt		% GDP	36.2	37.4	42.6	39.6	38.8	38.0	37.8
External debt		% GDP	36.9	32.3	31.6	28.2	24.4	23.3	18.3
Balance of payments									
Trade balance		\$ million	-604	-663	-821	-1027	-1155	-1336	-1579
Exports		\$ million	208	275	255	305	330	447	603
Imports		\$ million	812	938	1076	1332	1485	1783	2182
Transfers		\$ million	520	353	533	571	613	842	1043
Reserves		\$ million	384	482	608	754	860	1026	1374
Reserves	- Import cover	Months	3.7	3.8	4.2	4.3	4.3	4.7	5.2
Trade balance		% GDP	-22.1	-19.2	-22.2	-25.0	-25.7	-21.9	-20.8

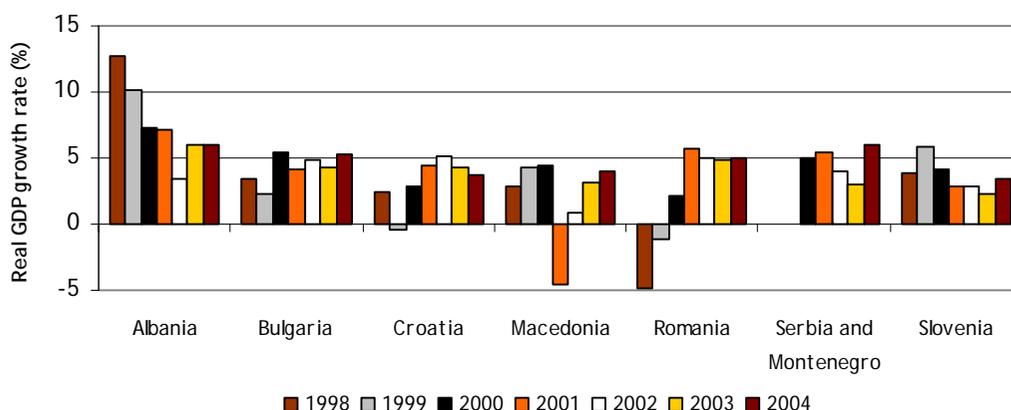
Export growth rate	%	31.1	32.3	-7.2	19.3	8.4	35.4	35.0
Import growth rate	%	17.0	15.5	14.8	23.7	11.6	20.1	22.4

Source: Ministry of Finance, Macroeconomic Department

2.1 ECONOMIC GROWTH

Economic growth is the main factor in reducing poverty and stabilising Albania’s macro-economy. Figure 2.1 below presents real growth over the past 7 years, showing that Albania has consistently managed to achieve high economic growth since 1998. During 2004 real GDP growth was estimated to be 6%.

Figure 2.1 Economic growth in Albania and selected countries, 1998-2004



Source: IMF Country reports; the figures for 2004 are projections

The combination of high growth and a decline in the resident population of Albania (by about 3.4% since the year 2000), has led to a doubling of per capita incomes, in Lek, over the last 7 years. Nevertheless, GDP per capita still remains very low compared with other countries and its increase constitutes one of the strongest challenges for the future. Real increase in the GDP for the period 1998-2004 in Albania and neighbouring countries is given in Table 2.2.

The sectoral composition of growth in 2004 has followed a similar pattern to the previous year, as shown in Table 2.2. Construction and transport have continued to grow strongly, while industry and agriculture are growing at a lower rate than the national average.

Table 2.2 Sectoral structure and growth

	Structure of GDP (%)		Real growth rate (%)	
	2003	2004	2003	2004
Total	100	100	6.0	6.0
Industry	10.2	9.9	2.7	3.1
Agriculture	24.7	24.0	3.0	3.0
Construction	9.1	9.5	11.3	10.6
Transport	10.0	10.4	10.8	10.1

Services	46.1	46.3	6.4	6.4
----------	------	------	-----	-----

Source: INSTAT

Agriculture continues to be one the most important sectors of our economy, contributing 24% of GDP and 58% of employment in 2004. Real growth in agriculture is estimated to be 3%, as a result of adequate climate conditions, investment in new production and technologies, especially in agro-industry, and improved power supplies. Good levels of production have led to low prices. Despite the strong Lek, there has been an increase in agricultural exports and domestic agricultural products have competed successfully against imports.

However, agricultural growth is below the national average growth rate, and is constrained by a number of issues, including emigration from rural areas and the legal framework on property. Agricultural growth is of particular importance to Albania, in view of the very low productivity of the agricultural and agro-industrial system inherited from the past. Further measures are needed to promote the commercialisation of agriculture, both for exports and domestic markets, and to encourage new technologies.

Growth in **industry** is also about 3% and has been dominated by the energy sector, which grew by around 48.9 %, because of investment, reform and favourable weather conditions. Growth of the energy sector remains one of the key elements of national strategy, both for economic and social development. In contrast, the metallurgical industry declined by 68.3 % in total, despite an increase in steel production. The manufacture of leather-shoes and chemicals grew by 25.3 % and 19.2 % respectively, while wood processing declined by about 4.3 %. The petroleum sub-sector grew at 7.6 %, despite a decline in volumes. The textile and confectionary industry both grew at about 3.4 %.

Transport grew by 10.1 % in 2004 and this has been dominated by road transport. Port activity has grown by 5.9%. Railway traffic has declined by 24.2% in volume, with a 15% decline in the value of passenger traffic and a 19.3% decline in goods traffic. The government is committed to improving the situation of the railway system and carrying out an efficient privatisation.

Construction is one of the most dynamic sectors of the Albanian economy, with a real growth of 10.6% in 2004. Construction activity is concentrated in the major urban centres. Private sector construction is mainly focused on flats and buildings for families, which comprise about 81.6% of the total financing of private construction. State participation in the construction sector is mainly focused on infrastructure and engineering constructions. State financing for engineering constructions constitute 84.8 % of total state financed construction, but is 69 % above the level achieved in 2003.

An analysis of future prospects for construction, based on construction permits issued during 2004, does not look optimistic. Problems appear to be associated with the limited number of construction permits issued, along with constraints on state investment, rather than with private investment capacity and demand.

Services contribute 46.3% of GDP and grew at a rate of 6.4% in 2004, slightly above the national average. Post and telecommunications have increased rapidly, as a result of improvements in service quality, although reforms and price changes in the telecommunications market have led to some major changes. Reforms and restructuring at Albtelekom remain a priority, in preparation for privatisation. Tourism is a major part of the service sector: during 2004 it is estimated to have generated \$673m in revenues, marking an increase of over 29% compared to 2003, with increases in visitor numbers and expenditure per person.

Public debate on economic growth and poverty

The NSSD Department organised a public debate in March 2005 to discuss the sources of economic growth in Albania and the impact of growth on poverty. The debate was attended by about 50 people, from a variety of public, private and voluntary organisations. It was launched by a statement from the Minister of Finance, which stressed the need for growth to incorporate social dimensions, as well as economic dimensions, in order to be sustainable. This will involve increased emphasis on human development, civil society and government transparency.

Discussion was stimulated by presentations covering: regional experience with economic growth; the national macroeconomic situation; the sources of economic growth; and the linkages between growth and poverty.

Participants were invited to fill in a questionnaire indicating the importance of different sectors and constraints for economic growth and for poverty alleviation. They were also divided into groups, and asked to define the key actions which would: a) promote economic growth; and b) promote poverty alleviation.

There was broad agreement about the actions required to promote economic growth, as already defined in the NSSD. However, there are a wide variety of views about the relative importance of these different actions. **Infrastructure** and **private investment** were widely stated as high priorities, but there were differences on the following issues:

- One group argued that the **financial sector** should have a high priority, whilst others argued that this would have little impact until financial institutions started offering services to a wider variety of activities.
- It was argued by 2 groups that modernising and commercialising the **agricultural sector** should be given the highest priority, in view of current employment patterns and the potential for reducing poverty in rural areas. However, the view was also expressed that economic growth in recent years had come largely by shifting from agriculture to more productive sectors and that this should continue.
- Contrast views were also expressed on the relative importance of **barriers to investment**, including the definition and enforcement of administrative, regulatory and legislative controls. One group placed this as the top priority, whilst another argued that growth had already been occurring without strong enforcement, and could continue to do so.
- One group placed **free trade and exports** as a high priority, whilst the others did not. There was some discussion about the complex nature of free trade impact on the economy.
- **Property status** and its use for collateral was considered as important by a number of individuals, but did not emerge as a key priority during group discussions.
- A number of people mentioned the importance of **tourism**, as a key source of economic growth and there was a debate about the importance of supporting a type of tourism which would have the widest possible benefits for the local economy. **Environmental** issues were not raised in the debate, except as a constraint for tourism development.

The discussion on poverty reduction supported the assertion that economic growth was the main priority and would lead to poverty reduction. One group argued that **education** needed particular attention, whilst another group reminded the debate that there were disagreements on what type of skills and attitudes were required for poverty reduction.

2.2 BALANCE OF PAYMENTS AND EXCHANGE RATE

The overall balance of payments in 2004 has seen some marked improvements, with a strong surplus of \$288 million, compared with \$100 million in the same period in the previous year. Key trends in the **current account** in 2004 have followed a similar pattern to last year.

- Exports were \$603 million, increasing by 35%, despite the strong Lek. The fastest growing exports were in minerals, fuel and electrical power and in construction materials and metals. Textiles and shoes dominate exports and grew modestly. The least successful sector was wooden and paper products.
- Imports totalled \$2182 million during 2004, increasing by 22%. The highest increases were in machinery, equipment and spare parts and in chemical and plastic products. There was a decline in imports of minerals, fuel and energy, as a result of the recovery of domestic electricity production.
- The trade deficit worsened to \$1579 million in 2004, 21% higher than the previous year. However, this picture is exaggerated by the weak dollar. The prospects for continued improvements in trade are good, as opportunities arising from free trade agreements are taken up, especially if the current strength of the Lek is moderated.
- The service balance during the period had a deficit of about \$24 million, compared with a deficit of \$83 million for the same period in 2003. This improvement is largely explained by the rapid increase in tourism receipts, as a result of improvements in infrastructure and service quality.
- Net factor income was almost unchanged since 2003, with a positive balance of \$168 million.
- Net private transfers increased by 25% during 2004, to \$978 million. These are dominated by remittances.

The **capital account** has improved during 2004. Capital transfers had a surplus of \$132 million in 2004, down 16% on 2003, whilst the financial account had a surplus of \$399 million, up 97.5%. Currency reserves increased by \$348 million during 2004 to \$1374 million and were sufficient to cover 5.2 months imports of goods and services.

Figure 2.2 Lek exchange rate with the Euro and the dollar



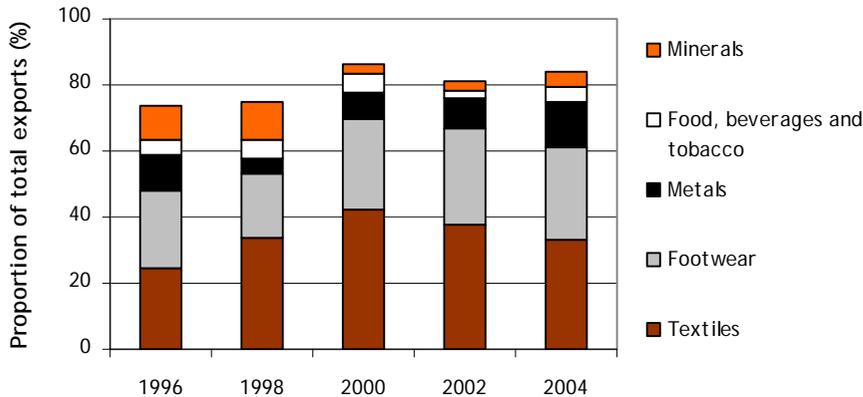
The strong balance of payments performance, has led to a continued appreciation of exchange rates (see Figure 2.2). During 2004, the average annual exchange rate reached 102.76 Lek/\$ and 127.66 Lek/Euro, reflecting the weakness of the dollar on international markets. In addition to

the balance of payments situation, the strengthening of the local currency in recent years has been caused by greater public trust in the financial system, high real interest rates and lower demand for government financing.

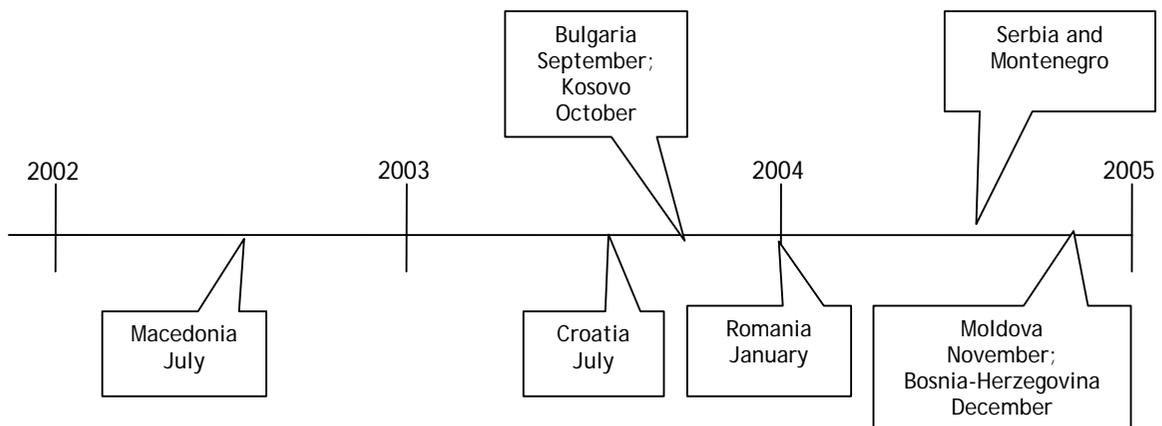
The strengthening of Lek has advantages and disadvantages. On the negative side, trade competitiveness is reduced. There are lower export earnings, lower earnings from foreign exchange savings and remittances, and lower customs revenue. On the positive side, there is lower inflation due to cheaper imports, greater trust and investment in economy, cheaper debt service and incentives to sell locally, rather than export.

Export structure

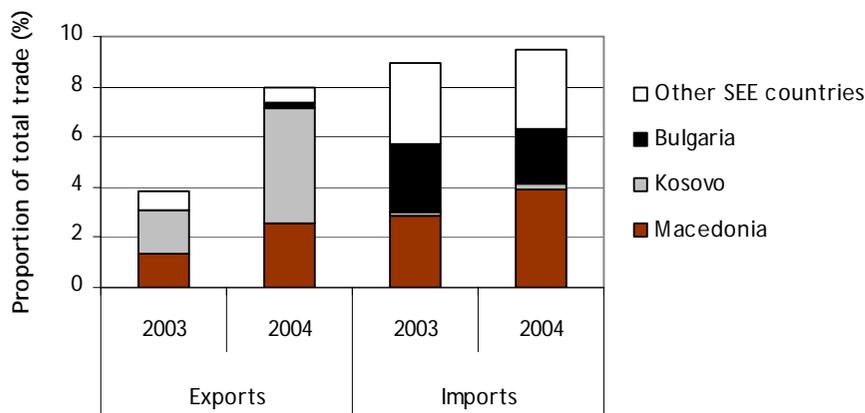
Export activity increasingly concentrates in 5 sectors although there have been changes in recent years. Textile exports peaked in 2000 but their relative share has been declining since. Mineral (petroleum) and metal (chromium and locks) exports were declining throughout the 1990s but have returned to positive growth.



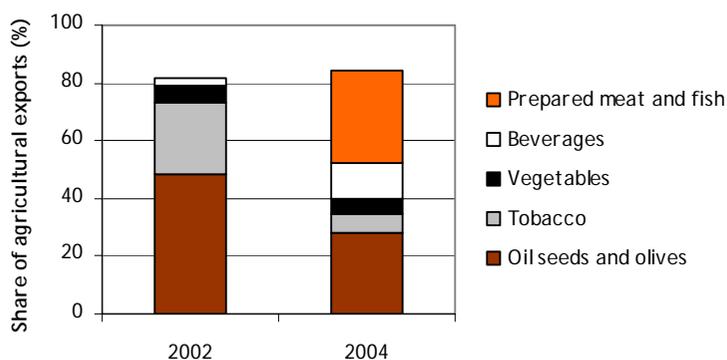
The share of footwear exports, the single biggest exported item, has remained constant since 2000. All exports from this sector during 2004 were directed to Italy from where they are often re-exported. The potential for increasing footwear exports to European markets is substantial as a result of geographic advantages and cheap labour.



European Union countries continue to absorb 90% of Albania's exports and are the source of 2/3 of its imports. Regional markets offer new opportunities after the free trade agreements signed between 2002 and 2004. Exports to these countries increased substantially between 2003 and 2004, notably to Kosovo and Macedonia, which has helped to reduce the overall trade deficit of Albania with South-East Europe.



There have been notable changes in the composition of agricultural and agro-industrial exports in the last couple of years. There were no exports from the prepared meat sector in 2002 but they made up a third of the total in 2004. Similarly, the share of beverage exports (especially bottled water and juices) increased almost fivefold in the same period. Attention now needs to turn to gaining access to foreign markets and developing business practices.



Note: The figures for 2004 refer to the period January-September.

Source: Albanian Centre for International Trade, Albanian Foreign Trade Report

2.3 PUBLIC FINANCE

Budget revenues in 2004 were equivalent to 23.6% of GDP, which is 10.2% higher than 2003, in nominal terms. As a proportion of GDP, 2004 saw a small decline in public revenues, from 24.1% in 2003. Total revenue was 93.1% of budget, with tax revenues at 97.3%. These figures have been achieved despite a reduction in customs revenue associated with the weak dollar. Improvements have been made across all sources of revenue, and in particular for tax revenues, which account for 90% of revenue. Nevertheless, revenues are still low in comparison to other countries in the region. This is due partly to weak revenue collection and partly to the large size

of the informal sector, and, in particular, agriculture. Key features of revenue in 2004 are as follows:

- Revenue from foreign grants was about the same in 2004 as in 2003 in dollar terms, but fell from 0.38% to 0.31% of GDP.
- Tax revenues account for 90% of total revenues and increased from 20.9% to 21.3% of GDP. Actual tax revenues were 97.3% of budget.
- VAT has increased by 15% in Lek terms and is about 1.8% above budget, reflecting improvements in VAT administration, resulting in better registration and collection rates.
- Excise collection has increased by 29% in Lek terms but was still only 97.3% of budget. This is partly caused by exceptional events on fuel excises and unfulfilled potential for increasing excise collection on alcoholic drinks.
- Profit taxes also increased strongly, by 24% in Lek, and were 7.3% above budget. This resulted from improvements in analysis, inspection and collection of arrears.
- Small business taxes were 38% higher than in 2003, and were roughly in line with budget. There were considerable advances in administration, although there is still scope for further improvements.
- Personal income tax increased by only 6.8% in nominal terms, and was only 84% of budget. Part of this may be explained by reductions in tax on savings income, as a result of declining interest rates. However, the relatively poor performance on the various elements of personal income tax is a major challenge in the next few years.
- National tax revenues were 3% lower than in 2003, and were 85.6% of budget. Road circulation tax was roughly in line with budget, but problems have been experienced in collecting taxes on radio-television usage and a number of other taxes, such as carbon taxes, foreign vehicles and plastic packaging.
- Revenue collected by the customs administration is 10.5% higher than last year, and about 97.8% of budget. Customs duties account for most of the shortfall, with excise and VAT on trade both showing a strong increase, in line with the budget. If exchange rates had been maintained at the levels expected in the budget, revenue from customs administration would have been about 8% higher, and would therefore have been well above budget. This would have resulted in total public revenue being at 24.3% of GDP, showing an improvement on 2003.
- Non-tax revenues are 76.8% of budget. The majority of the budget shortfall was caused by low profits from the Bank of Albania. However, all other items were also below budget, including the revenues of budget institutions and revenues from dividends, fines and sequestrations.
- Revenues from local government during 2004 were 15.3% lower than budget, although they were 21.3% higher than last year. There were shortfalls in property tax (640 million), agricultural land tax (206 million), vehicle registration tax (239 million) and local taxes (662 million). Only revenues from small business taxes were higher than budget by Lek 16 million. They increased to 1.2% as proportion of GDP, compared to 1.1% in the previous year.

Constraints to raising taxes: an institutional perspective

Tax collection is lagging in Albania compared to its neighbouring countries. In addition, it should not be forgotten that revenue from the informal sector is not recovered either. The latest estimate¹ using alternative methods inferred that the size of the Albanian informal economy is at least 30% of the GDP.

It is vital to broaden and secure the revenue base. The government has a well-developed plan to modernise tax administration and receives advice and technical assistance to strengthen collection efforts. A report by the IMF has suggested changes in the value-added tax and the coverage of profit tax, simplification of personal income tax rates, and increases in excise taxes on vehicles, alcohol, tobacco, and petroleum products.

However, a recent study² points out that in the long term an increase in government revenue cannot simply be met with administrative measures. Norms of behaviour and perceptions are critical to achieve tax compliance. The analysis was based on a household survey in the area of Tirana that obtained evidence on the incidence of tax evasion and assessed its relation to individual attitudes. The results showed that people with pessimistic attitudes about formal institutions, such as the tax and audit authorities, were more likely to evade small business income tax. A strategy to raise government revenues will not be effective unless it is built around attempts to establish confidence in public institutions.

Sources: ¹ M Muço et al. (2004) Private sector and labour market developments in Albania: Formal versus informal, Vienna Institute for International Economic Studies; ² K Gërxhani (2004) Tax evasion in transition: outcome of an institutional clash? European Economic Review, Volume 48, pp.729-745

Public expenditure has grown steadily during the last 7 years, although it has declined as a proportion of GDP. Current expenditures for 2004 were about 8.5% higher than the previous year or 99.2 % of budget. As a proportion of GDP, current expenditures declined from 24.4% in 2003 to 23.6 % in 2004. Salaries were below budget (at 97.5% of budget), whilst other expenditures were over budget, including operational expenses (107.6%), social and health insurance (101.5%) and other expenses (114.7%). Subsidies were also above budget (at 122.8%) largely because of the use of contingency funds for to clear old obligations for KESH, without which subsidies would have been 6% below budget. Local government expenditure was about 90.3% of budget because of the delays in approving local council budgets.

Capital expenditures were 70% of budget in 2004, but were still 21.6% higher than 2003, in nominal terms. This level of capital expenditure was strongly influenced by foreign financing which was 46% below budget and 19% lower than in 2003. Problems with foreign financing of projects affect many government ministries. Domestically financed investment was 51% higher than last year, although it was still only 89% of budget. Problems with slow domestically financed investment were found mainly in the Ministries of Foreign Affairs, Justice and Public Order.

The **public deficit**, as a proportion of GDP, has declined from nearly 10% in 1998 to 4.9% in 2004. Besides, there has been an increase in revenue from privatisation compared to the previous year. As a consequence the internal financing of the budget deficit has been reduced considerably. There has been some rationalisation of existing domestic debt and soft credits to state owned companies have been reduced, further reducing the crowding out effect on private credit. The domestic debt of government has declined from 42.6% of GDP in 2000, to 37.8% at the end of 2004 and the terms of this debt have improved.

With regards to effects on the interest cost, calculations to the end of 2004 show savings up to Lek 1.9 billion for internal debt and Lek 720 million for external debt. The main factor is continuous reduction of all sorts of short-term and mid-term instruments.

2.4 MONETARY POLICY AND INFLATION

The annual growth rate of **money supply** at the end of 2004 was 13.1%, which was higher than in 2003. However, the main monetary ratios (such as M2 to foreign currency and M3 to money outside banks) have remained stable and the banking sector remains sound.

The **base interest rate** has seen a gradual decline during 2004. This has decreased the cost of borrowing and increased the level of credit in the economy, which has expanded by 30% in 2004, reaching Lek 70 billion. The structure continues to be oriented towards mid-term and long-term credits, thus responding to the country's needs for increased investment in production capacities. Trade, construction and real estate continue to dominate borrowing, but there was some increase in supply of credit to agriculture and agro-processing and some decline in credit for trade. At the same time, there has been an increase in the proportion of credit in Lek, although 82% of credit is still in foreign currency.

The stable monetary situation has led to continued stable prices and Albanian inflation has remained below the levels of neighbouring countries. Annual **inflation** was 2.9% in 2004, compared with 2.4% in 2003. Low inflation has been the result of lower seasonal prices of agricultural products, control over the increase in budget expenditures and appreciation of the local currency, which has offset the risk of imported inflation from increased prices of oil and other imported products. The low inflation has been achieved despite some increases in administered prices, partly in preparation for privatisation. There have also been some increases in market-based prices, particularly during vacations when consumer spending is boosted by returning Albanians.

2.5 LABOUR MARKET

Economic growth has had an impact on employment indicators, although this impact is difficult to quantify due to the informality of the labour market and the economy in general. The unemployment level was estimated at 14.4% in 2004, showing a slight improvement from 15.0% in 2003 and a major improvement from 18.4% in 1999. This rate compares favourably with the official unemployment rate in other countries in Eastern Europe, although the comparison is difficult to make, given the different treatment of the informal sector. Improvements in employment have been mainly due to employment in the private non-agricultural sector, which accounts for 22% of the total.

In recent years, the government has implemented a policy to increase average salaries in the public sector by an annual average of 5-10%. Priority has been given to the sectors of education, health and defence, which have the largest number of employees. At the same time, pensions have been increased in both rural and urban areas. In 2004, the average salary in the public sector reached Lek 24957, which is 14% higher than in 2003 and double the average salary in 1998.

Despite continuous improvements from year to year, a problem still remains with the payment of social insurance contributions by employees and employers. These indicators remain at low levels especially in the private sector.

2.6 MACROECONOMIC PROJECTIONS

The government's macroeconomic projections are defined in the Medium Term Budget Programme (MTBP) for the period 2005-2007. These are based on continued stability:

- Sustaining economic growth at a level of 6 %,
- Maintaining an annual inflation rate at the interval 2-4%,
- Preserving foreign currency reserves at the level 4 to 4.5 months import cover, and
- Reducing the deficit of the balance of payments current account, with exports growing faster than imports.

Economic growth in 2005 is expected to be based first on the growth of the services and construction sectors, accompanied by an increase in transport, agriculture and industry.

Some of the main macroeconomic indicators for 2005 are given in Table 2.3:

Table 2.3 Main macroeconomic indicators for 2005

	Unit	2004	2005	Growth rate (%)
GDP at current prices	Lek million	780100	857300	9.9
Real GDP growth rate	%	6.0	6.0	
GDP per capita	\$	2431	2575	5.9
Inflation (average)	%	2.9	2.4	-17.2
Exchange rate	Lek/\$	102.8	106.0	3.1
Trade balance	\$ million	-1579	-1981	25.5
Exports	\$ million	603	766	27.0
Imports	\$ million	2182	2747	25.9

Reforms in the tax and customs administration, combined with efforts to reduce the informal economy, will increase the total budget revenues from 23.6% to 24.1% of GDP. This is equivalent to an 11.9% increase in revenue in nominal terms. All forms of revenue will increase, with tax revenues (notably personal income tax) and social contributions increasing slightly faster than the rest. Expenditure will remain constant as a proportion of GDP, allowing for a 6% real increase in public spending.

Table 2.4 Main fiscal indicators for 2005, as a proportion of GDP (%)

	2004	2005
Total revenues	23.6	24.1
Total expenditure	28.5	29.0
Deficit	-4.9	-4.9

The main objective of monetary policy during 2005 will continue to be the preservation of the annual inflation rate at 2-4 %. This objective will be achieved by maintaining the increase in money supply at a level in line with the increase of nominal GDP, and assuming some progress in the rate of money circulation. Macroeconomic stability will lead to a continued decline in interest rates and expansion of credit in the economy.

Methodology of macroeconomic projections

The macroeconomic projections are generated by a model which uses independent projections of underlying (or final) demand in the economy and then calculates the level of domestic economic activity needed to meet this demand, using input-output analysis. The final demand of the economy is defined as: government spending (current and capital); exports (of goods and services, including tourism); and private spending (both on investment and consumption). A part of private income is also projected independently (spending of government transfers and income from abroad), whilst spending of income earned domestically is calculated from the input-output analysis. Projections are made as follows:

- Government spending is projected by the Budget Department at the Ministry of Finance, based on the Medium-Term Budget Programme process.
- Exports of goods are projected by the Ministry of Finance in discussion with IMF.
- Exports of services (mainly tourism) are projected by the Macroeconomic Department at the Ministry of Finance to grow at 10% per year.
- Government transfers to households are projected from budget and Medium-Term Budget Programme data.
- Private income from overseas (mainly remittances) is projected from Ministry of Finance and IMF figures.
- Independent projections are made of private investment and food consumption, leaving a residual of private income for other consumption goods.

The sectoral composition of each element of final demand is assumed to be constant. The model then uses input-output analysis to calculate the level of output which is necessary to produce the demand from these underlying forces. The input-output analysis also produces estimates of private income from domestic activity and of imports of goods and services, both to economic activities and for household consumption. The model then calculates government revenue, based on the tax incidence on economic activities. This provides a projected government deficit. Expenditure can then be re-specified and the model is run again, to achieve the desired deficit.

The government is currently working on medium term projections to 2008 and extending to some additional years. This work has initially been done using the Ministry of Finance macroeconomic model described above. However, extending the macro model to include a fuller picture of the macroeconomy has raised a number of issues, which are being debated within government bodies. In particular, the Ministry of Finance aims to compare the conclusions from the macroeconomic model with the conclusions from more typical macroeconomic consistency frameworks, such as those used by the IMF and the World Bank.

The government is also working on the definition of a number of scenarios, which will help to illustrate the range of possible macroeconomic outcomes. This will help in setting revenue projections within a range, so that government expenditure can be planned to take place at different rates of progress.

3 Socioeconomic conditions

This section uses statistical data to look at some key aspects of socio-economic conditions in 2002 and 2003. The main point of interest is to update the poverty profile. Evidence on education, health, the labour market and utilities is also presented. The main source of information is the Living Standards Measurement Survey (LSMS) carried out by INSTAT.

3.1 POVERTY

Last year's Progress Report presented the evidence on the level of poverty in Albania using the data of the 2002 LSMS, which surveyed a nationally representative sample of 3600 households. The headcount rate of poverty was calculated as the proportion of individuals who were consuming below the amount necessary to cover the need for basic food and non-food items. Poverty measures based on consumption are preferred to measures based on income for two reasons. First, households are less likely to report their income accurately. Second, income may vary a lot between different years, while consumption is more stable over time and therefore describes the welfare of households better. The resulting poverty headcount in 2002 for Albania was 25.4%.

However, obtaining consumption data on an annual basis is very costly and INSTAT is only collecting consumption information again in 2005. Instead, the Albanian poverty monitoring system has been designed on the assumption that poverty can be monitored using fewer data but applying statistical techniques to substitute for the lack of full information. A second round of the LSMS was conducted in 2003. About half of the households that were interviewed in 2002 were re-visited in 2003. The 2003 questionnaire included most of the questions that were asked in 2002 but did not include detailed questions on consumption. In order to assess whether the level of poverty changed between the two years, a research team from the Food and Agriculture Organisation used a methodology consisting of three steps. In the first step, all variables that were collected in both years were identified.

In the second step, the researchers assessed which variables were most closely associated with the level of household consumption in 2002. A number of variables were found to be correlated with consumption to a statistically significant degree. For example, controlling for all other characteristics, if a household possessed a washing machine then it was less likely to have low consumption. This statistical analysis estimated how strong the association of each household characteristic was with the level of consumption and the likelihood of poverty. These characteristics may change for any household from one year to another. For example, a household may have purchased a washing machine between 2002 and 2003. It may be therefore inferred that their living conditions had changed to the better.

The third step involved the use of these coefficients of correlation between consumption and household characteristics from the 2002 LSMS to predict the level of consumption using the 2003 LSMS data on household characteristics. This analysis was carried out for the national sample, as well as for the urban and rural sub-samples separately. Table 3.1 shows the results of this analysis. The first column reports the actual level of poverty calculated by the 2002 LSMS data. As mentioned above, the headcount rate of poverty in 2002 was 25.4%. The second column reports the predicted level of poverty for 2002 using the statistical model described above. This is not identical to the actual level of poverty because a prediction can only be approximate. The important comparison is between the second and the third column, which shows the predicted level of consumption in 2003 using the results of the statistical model. The estimated poverty level appears to have fallen by about 16% or three percentage points between the two years. The fall has been much smaller in rural areas.

Table 3.1 Headcount poverty changes between 2002 and 2003

	2002 Actual	2002 Estimated (panel sub-sample)	2003 Estimated (panel sub-sample)	Percentage change between 2002 and 2003 (%)
Total	25.4	20.4	17.1	-16.2
Urban	19.5	13.2	10.7	-18.9
Rural	29.6	24.3	22.9	-5.8

Source: C Azzarri et al. (2005) Monitoring poverty without consumption data: an application using the Albania panel survey, ESA Working Paper No. 05-01, Food and Agriculture Organisation

It is very important to stress that these are not the actual levels of poverty. A precise estimate has to wait for the results of the 2005 LSMS, which has solicited consumption information. However, the evidence in Table 3.1 can be used to argue that the poverty situation has been improving and that the benefits are more visible in urban areas. Table 3.2 translates the results of the model in terms of the predicted change in monthly per capita consumption. Compared to 2002, when the calculated average per capita consumption was Lek 7679, consumption in 2003 is estimated to have increased to Lek 8116 or by 5.7%. This is consistent with the observed rates of economic growth at the level of 6% in recent years.

Table 3.2 Changes in estimated per capita consumption between 2002 and 2003

	Urban	Rural	Total
Per capita consumption in 2002 (Lek per month)	8,311	7,072	7,679
Per capita consumption in 2003 (Lek per month)	8,844	7,249	8,116
Difference in consumption (Lek per month)	533	177	437
Difference in consumption (%)	6.4	2.5	5.7

Source: C Azzarri et al. (2005) Monitoring poverty without consumption data: an application using the Albania panel survey, ESA Working Paper No. 05-01, Food and Agriculture Organisation

Subjective poverty

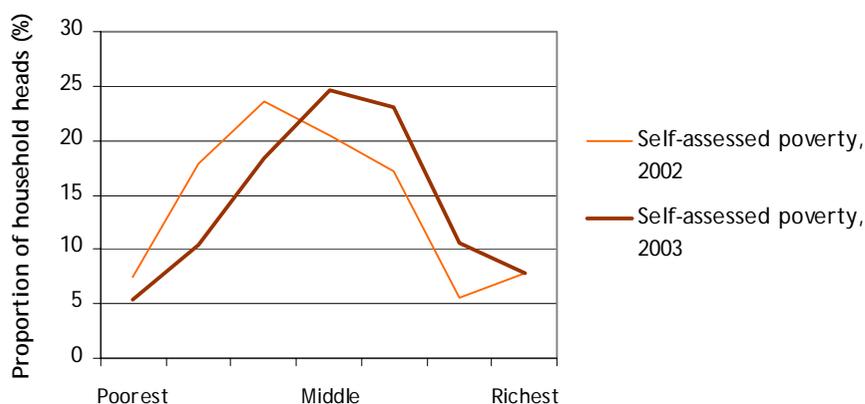
The LSMS also asks households to assess their financial situation. Respondents are asked to imagine a ladder where the poorest stand on the lowest step and the richest on the highest step and report where they would place themselves. Such subjective measures of poverty are not perfectly correlated with objective measures of poverty. The reasons for differences vary:

People may not equate their poverty with income or expenditure alone. While objective measures relate to consumption poverty, subjective measures may also be capturing factors such as risk exposure, vulnerability, and other non-monetary dimensions of deprivation.

Quantitative measures of poverty are based on absolute poverty lines, but the way people feel about their welfare depends on their position relative to people with whom they like to compare themselves.

A recent study ¹ using the 2002 LSMS found that although the objective poverty status helps explain the subjective assessment to a large extent, there were substantial differences between objective and subjective welfare across households of different size. In particular, among households composed by one person, the incidence of subjective poverty is highest, while the incidence of objective poverty per capita is lowest. Households with one member are in large part (75%) old pensioners living alone: the mean age of the respondents in this group is 63 years as opposed to an average age for the total sample of 48 years. Households headed by women are also disproportionately represented in this group: 69% against an average 12% in the total sample. Also, 54% of the respondents in this group are single female pensioners; 56% are female widows; 64% suffer from chronic illnesses against an average of 28% in the total sample.

The analysis supports the argument that people's perception of own welfare can be used to complement traditional poverty analysis. If one trusts subjective rankings, subjective poverty measurements can be a source of information for policy purposes. This makes it also interesting to observe trends. Both the 2002 and 2003 waves of the LSMS contain the same question on subjective welfare. As the following graph suggests ², perceptions have improved between 2002 and 2003. A higher proportion of respondents placed themselves among the better off in 2003.



Sources: ¹ G Carletto and A Zezza (2004) Being poor, feeling poorer: Combining objective and subjective measures of welfare in Albania, ESA Working Paper No. 04-12, Food and Agriculture Organisation; ² INSTAT

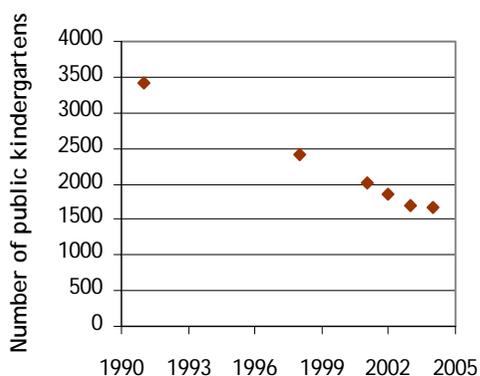
Protection of children's rights

In Albania, a third of children live below the poverty line. This is a higher proportion than the average for the national population because poorer households tend to have more children. Poverty leads to poor nutrition. According to the 2000 Multiple Indicator Cluster Survey, among children under the age of 5:

- 14% was characterised by moderate and 4.4% by significant underweight
- 31.7% had minor and 17.3% had significant shortcomings in development
- 11% had minor and 3.6% had significant shortcomings in nourishment

Children of mothers with secondary or higher education were less likely to be underweight. An analysis of the 3 indicators showed that the problems were more common among children aged 6-11 months and among boys. An issue of concern remains the growth of anaemia or iron deficiency. By 2002, though, the LSMS had found that rates of malnutrition were slightly on the decrease.

Another problem that affects children's lives is the retreat of early childhood education. In 1990, enrolment in preschool education among 3-6 year olds was 44%. This fell sharply to 28% in 1992 and has since been increasing but not recovered to the original levels (34% in 2001)¹. Enrolment of children in poor families is about half that of children from well-off households. A leading reason has been the closure of public preschools, as shown below. Compared to 1990, the number of kindergartens had fallen by 60% in urban areas and by 49% in rural areas in 2004.



Poverty denies children some of their fundamental human rights. The risk to go through poverty during childhood is high in Albania. Long-term unemployment has had a negative impact on the economic and social status of families. Households headed by women are at a higher risk from poverty. About 32.8% or 293,000 children in Albania live below minimum standards² (less than \$2 per day). Furthermore, Albanian children are facing other dangers emerging during transition, such as dropouts, violence, blood-feud, trafficking, exploitation, criminality, etc.

In spite of continuous improvements in child health, infant mortality, mortality under five years of age and maternal mortality are among the highest in the region, though a decrease has been noticed in the last decade. Infant mortality has decreased from 30.8 per 1,000 live births in 1989 to 16 deaths in 2003³. The rate of infant mortality and the number of underweight births indicate a deterioration of mothers' health and nutrition. Another indicator in this respect is the increase of anaemia as result of iron deficiency.

According to a number of official documents³, a pronounced decrease of children attending pre-school education has been observed in recent years. This is a result of migratory movements inside and outside the country, irregular urbanisation in some areas of the country, destruction of

infrastructure and lack of security. Only 5% of the total budget of education is allocated to pre-school education⁴.

The inheritance of a completely destroyed environment will have serious and long-term effects on children, who are particularly at risk to the effects of air, earth and water pollution. An increase in the number of deaths in children under five years of age related to conditions of the environment, such as high level of pollution and deteriorated sanitation, has been noticed, which highlights a direct link between children diseases and air pollution.

Considering some of the serious problems related to children rights and policies to be undertaken in protecting such rights, the National Strategy for Children was approved in June 2005. It is expected that the Action Plan will be approved later in June. As envisaged by the strategy, a State Committee for Children will be established to monitor and coordinate the activities of units operating in the field of children rights at the national and local levels.

The National Strategy for Children aims at establishing institutional structures and ensuring sufficient financial and human resources to accomplish obligations deriving from the Convention On the Rights of the Child. The fundamental principle in designing social policies to implement the strategy will be to ensure equal opportunities to all children, regardless of their age, sex, ethnicity, ability, status of birth etc. Priority will be given to marginalised social groups lacking parental care, exploited or ill-treated children or children with disabilities, street children and children from poor families.

To this end, a system of institutions will be created and social policy reforms will be carried out, in order to protect children from all forms of violence, exploitation and ill-treatment; to ensure living conditions for children in a family environment and, where it is not possible, to offer alternative care, giving priority to care in social families; to offer equal opportunities to children with limited abilities; to improve health care and service for mother and child; to build a modern educational system, ensuring appropriate conditions to all children to complete their obligatory education; and to establish a system of services that protect working children.

With the view of measuring the progress in implementing policies, a system of indicators and a database will be created, in harmony with the national system of monitoring the NSSD and the Millennium Development Goals. Reports will be prepared every year on the progress in implementing the strategy and the Action Plan.

Sources: ¹ Innocenti Social Monitor, Economic growth and child poverty in the CEE/CIS and the Baltic States, October 2004; ² Social Indicators 2004, UNICEF; ³ Common Country Assessment: Albania 2004; ⁴ Ministry of Education and Science, 2003

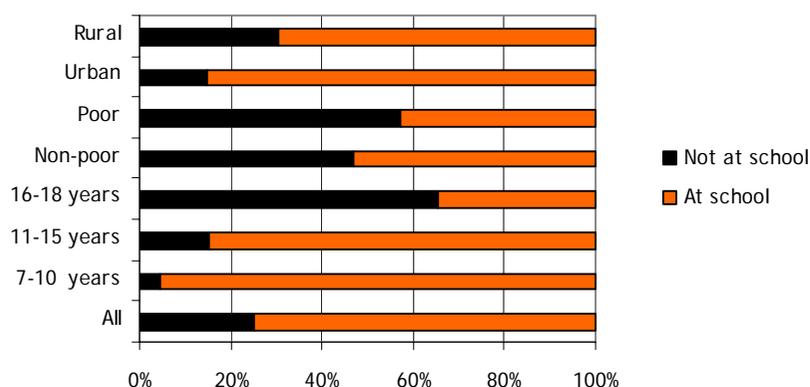
3.2 EDUCATION

Education is a key policy area with a well-educated and skilled workforce being central to increasing economic growth and development. The levels of education in the LSMS panel for those aged over 22 years in 2002 were relatively low with 17.7% having 4-year primary education, 45.1% with 8-year primary education, 14.7% with secondary school education, 15.1% with vocational education and 7.4% with a university level education.

Looking at enrolment rates in school for those aged 7-18 years in 2002, 75% of this age group were enrolled in school or education. Figure 3.1 shows enrolment rates by age group, poverty status of the household and urban or rural area. Those aged 16 - 18 years were least likely to be enrolled (35%) compared to 85% of 11-15 year olds and 95% of those aged 7-11 years. Children

from poor households were less likely to be in school or education than children from non-poor households. Children in urban areas were more likely than those in rural areas to be enrolled in school or education (85% in urban areas compared to 69.5% in rural areas).

Figure 3.1 Enrolment status of children aged 7 - 18 years, 2002



Even though children in rural areas were less likely to be enrolled in school, the effect of the poverty status of the household is more marked in urban areas than in rural areas. Of children in poor households in urban areas, over one quarter (26%) were not enrolled in school compared to 17% of non-poor children in urban areas, a percentage point difference of 9%. In rural areas, non-poor children were only 4% more likely to be enrolled in school than poor children.

Those who were not enrolled in school were asked for the reason. The main reason given was that they had completed their studies or had no interest in continuing in education (54%), followed by having other work to do, including agricultural work (16%) and the school being too far way (15%) even though this last reason applied in rural areas only. Of those who were not enrolled in 2002, 50% were working as farm workers, 5.5% were employees, 2% were self-employed, 29% were unemployed and 13.5% had some other status e.g. ill, housewife.

Dropout rates as children become older are of concern. The key ages where the risk of dropping out is greatest are from 13 to 16 years. In 2002, 6% of 13-year olds were not in school, increasing to 23% at 14, 42% at 15 and 60% at 16 years of age.

Changes between 2002 and 2003 for 15 - 18 year olds

Using the panel component of the LSMS for 2002 and 2003 the dropout rates for 15 - 18 year olds who were in education in 2002 can be seen. Of those who were in education in 2002, 86.4% were enrolled at both years while 13.6% were not enrolled in education by 2003. The dropout rate varies by age with those aged 15 in 2002 being most likely to drop out by 2003 (25%) compared to 10% of those aged 16 in 2002 and 6% of those aged 17 in 2002. So the dropout rate is greatest between the ages of 15 to 16 years, something which is in line with the legal age for leaving formal education and the typical completion age of 8 years in primary education.

3.3 HEALTH

Respondents on the LSMS were asked to rate their own health. Overall, the majority of respondents (69%) rated their health as being very good or good, 19% said it was average and 12% rated their health as being poor or very poor. There are some differences between men and

women, with men being less likely than women to rate their health as average or poor/very poor. Of those rating their health as poor or very poor, 35% were men and 65% were women. Self-rated health status also varies by age group with the older age groups being more likely to rate their health as poor or very poor. Table 3.3 shows the self-rated health status reported by respondents aged 15 years and over in 2002. Those with a chronic illness or disability were significantly more likely to rate their health as poor or very poor (85% compared to just 15% of those with no chronic illness).

At each year of the panel survey respondents have been asked to rate their housing conditions according to whether they are very good, appropriate for living, inappropriate for living and under construction (mostly incomplete). Those living in poor housing conditions were more likely to report having poor health. Of those saying they had poor health 15.5% were living in poor housing conditions compared to 11% reporting good health. There was also an association between poverty and poor health with 25% of those with poor health living in a poor household compared to 22% of those who had good health.

Table 3.3 Self-rated health status of individuals aged 15 and over, 2002 (%)

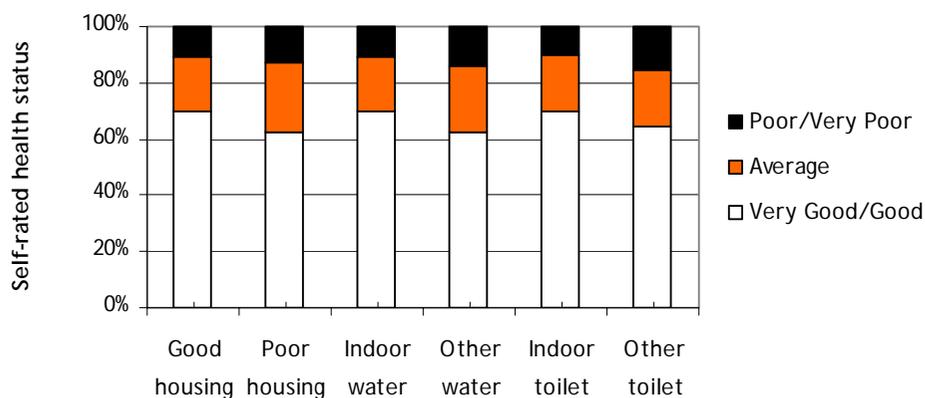
		Health status			Total number of observations
		Very good / Good	Average	Poor / Very poor	
Suffers from chronic illness	Yes	4.2	45.3	85.4	1095
	No	95.8	54.7	14.6	3911
Housing conditions	Good	89.4	87.0	84.5	4417
	Poor	10.6	13.0	15.5	582
Poverty status	Non-poor	77.7	78.9	74.7	3865
	Poor	22.3	21.1	25.3	1134
All		68.8	19.4	11.8	100
Number of observations		3440	972	594	5006

Health status in urban and rural areas

Households were asked about their main source of water according to whether they had running water inside the dwelling, running water outside the dwelling, used a water truck, public tap, spring or well, river lake pond or some other source. They were also asked if they had a toilet inside the house, 2 or more toilets inside the house, a toilet outside the house, or some other type of toilet.

There were some clear differences between health status and housing conditions in urban and rural areas. On the whole, people living in urban areas reported better health and also having better housing conditions than those living in rural areas. Looking first at urban areas, 69.5% of those in good housing conditions rated their health status as very good/good compared to 62% of those in poor housing (Figure 3.2). A similar pattern can be seen with indoor running water and indoor sanitation, with those having these facilities reporting better health.

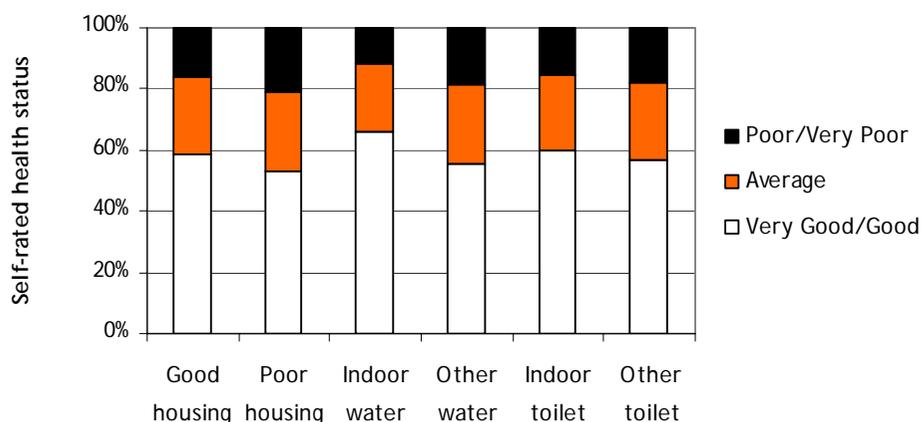
Figure 3.2 Self-rated health status by housing conditions in urban areas, 2002



Looking at rural areas, there are some marked differences compared to urban areas. In total, 16.5% of rural households were living in poor housing conditions compared to 6% in urban areas. In rural areas, 23% of respondents were living in a house with no indoor water compared to 12% of respondents in urban areas. Just 38% of people in rural areas were living in a house with an indoor toilet compared to 86% of those in urban areas.

In rural areas, 59% of respondents living in good housing conditions had good health compared to 53% in poor housing conditions (Figure 3.3). In the case of rural areas, those who had poor health were also more likely to have no indoor water or indoor toilet but the differences are greater than in urban areas. Of those with no indoor water, 18.5% rated their health as poor/very poor compared to 12% of those with indoor running water. Similarly, those with an indoor toilet rated their health better than those with some other type of toilet.

Figure 3.3 Self-rated health status by housing conditions in rural areas, 2002



Usage of health services

Respondents were asked how many times they had used a public ambulatory service, visited a private doctor or seen a nurse, paramedic or midwife in the past 4 weeks. They were also asked how many times in the past twelve months they had been admitted to hospital and been to a

dentist. In total, 38.8% of all respondents had used at least one of these services when surveyed in 2002 and 36.5% had used at least one in 2003. In 2002, 23.5% of respondents had gone to the dentist in the past twelve months but in relation to services used in the past 4 weeks the public ambulatory service was the most frequently used by all respondents, with 15.7% of people using this service.

In 2003, the results are similar, with 22.3% of respondents visiting the dentist in the past twelve months and 11.3% using the public ambulatory service in the past 4 weeks. Table 3.4 gives the mean number of visits to each of these types of services. In 2002 the service with the highest mean number of visits in the past 4 weeks was paramedic or midwife, 5.78 visits for those using this service and 0.16 for the whole population. However, relatively few respondents used this service which suggests high usage by a limited group of people. The public ambulatory had the next highest mean usage at 1.54 visits in the past 4 weeks for those who used it. This was also the service most used by the whole population with 0.24 visits on average.

Those living in poor households had a lower mean usage of health services even though the differences were not substantial compared to non-poor households, a pattern which was similar in both 2002 and 2003. In general, the mean usage of health services in 2003 was slightly lower than in 2002 even though the differences are not great.

Table 3.4 Mean usage of health services, 2002 and 2003

Type of service used	2002		2003	
	Mean number of visits by the population	Mean number of visits by individuals who used the service	Mean number of visits by the population	Mean number of visits by individuals who used the service
In past 4 weeks				
Public ambulatory	0.24	1.54	0.16	1.36
Private doctor	0.03	1.45	0.03	1.38
Nurse / Paramedic / Midwife	0.16	5.78	0.11	4.62
Outpatient visit to hospital	0.01	NA	0.07	1.52
In past 12 months				
Admission to hospital	0.06	1.28	0.06	1.25
Dentist	0.66	2.79	0.56	2.48

Smoking

In 2003 respondents were asked whether they smoked cigarettes and smoking is associated with reporting having worse health. The data are reported for men only as the percentage of women reporting smoking in the survey was very low and may not be reliable. It may be the case that women are more reluctant to admit they smoke, as it is not seen as being socially desirable or acceptable for them to smoke. Almost one third of men smoke (31%). Smokers were less likely to report having good health than non-smokers with 69.6% of smokers having good health compared to 76.1% of non-smokers.

Table 3.5 Relationship between smoking and self-rated health status of men, 2003

Health status	Non-smoker	Smoker	Total number of observations
Very good / Good (%)	76.1	69.6	1703

Average (%)	15.3	19.8	385
Poor / Very poor (%)	8.6	10.6	217
Total number of observations	1579	726	2305

3.4 LABOUR MARKET

Labour force participation

The labour force in Albania was calculated to be 1.3 million in the 2001 Census or lower by 15% since 1989. The workforce lost more than a quarter of women and 5% of men. In 1989, there were only slight differences in labour force participation between men and women. By 2001, gender equality had disappeared, as only half of the adult women were active in the labour market and the proportion of inactive women had doubled. Labour force participation among men remained roughly the same but its composition changed as the share of the employed fell (61% relative to 71% in 1989) and the share of unemployed rose (14% relative to 6%). The size of the male labour force was reduced in absolute numbers as a result of emigration.

Table 3.6 Labour force participation according to the 1989 and 2001 Census

	1989			2001		
	Male	Female	Total	Male	Female	Total
In thousand						
Employed	779	664	1443	650	392	1042
Unemployed	62	94	157	150	155	306
Total active	842	758	1600	800	548	1347
Inactive	249	283	532	269	554	823
Total (aged 15 years or more)	1090	1041	2132	1069	1101	2170
As percentage						
Employed	71.5	63.8	67.7	60.8	35.6	48.0
Unemployed	5.7	9.0	7.3	14.0	14.1	14.1
Total active	77.2	72.8	75.0	74.8	49.7	62.1
Inactive	22.8	27.2	25.0	25.2	50.3	37.9
Total (aged 15 years or more)	100	100	100	100	100	100

Source: People and work in Albania, Population and Housing Census Research Publication, INSTAT, 2004

It is important to keep in mind that the notions of employment and unemployment have changed since 1989 and are not easily comparable. However, some changes are unambiguous, such as the drop in the female participation rate. Despite the high emigration rate of men, it appears that women have not substituted them in the domestic economy, not even in rural areas or agricultural activities. Female employment decreased mostly in urban areas for several reasons: the closure of factories, the increasing significance of male-oriented activities, such as trade and construction, and internal migration to urban areas, as women face more problems entering the urban labour market in the current economic environment.

Employment

Measuring employment is fraught with difficulties in the context of a Census. Many people do not consider activity in the informal sector as equivalent to being employed. Respondents have sometimes an incentive not to report their real employment status. For example, according to

the Census, the employment rate of 46-year-old women jumps by 20 percentage points relative to the rate of 45-year-old women. One of the likely explanations relates to social insurance rules for former employees of agricultural enterprises and members of their families. To enjoy a pension starting at age 55, women must have been employed for at least 10 years. Many women believed that claiming to be employed would be useful to earn a pension.

The direct and probing interviews used in the LSMS were designed to capture the employment status of the population better than the Census. Table 3.7 shows that men are more likely than women to be in employment (55% of the employed were men). At the same time, women are more likely than men to be inactive (69%) or unemployed (53%). Of those aged 15-34 years, 54% were in employment, while of those aged 35-54 years 52% were in employment. The unemployed were most likely to be aged 15-34 years (36.6%) and those who were inactive were more likely to be in the younger age group of 15-34 year olds.

Table 3.7 Employment status of working age individuals, 2002

	Employed	Unemployed	Inactive	Total number of observations
Gender				
Male	54.9	46.8	30.9	1997
Female	45.1	53.2	69.1	2176
Age				
15-34	54.0	13.2	32.8	1901
35-54	52.4	36.6	27.3	1874
55-over	9.1	2.8	19.6	398
Highest qualification				
Up to 8 years	57.6	58.6	69.5	2179
Secondary / Vocational	31.5	36.8	26.7	1170
University	10.9	4.6	3.8	309
Total	61.7	16.0	22.3	

Note: Working age is defined as 15-64 years for men and 15-59 years for women.

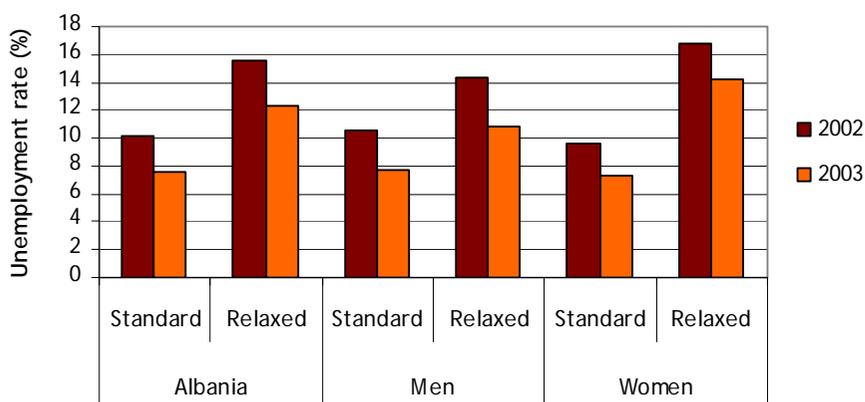
Of those who were in employment, the majority (58%) had up to 8 years education, 31% had a secondary or vocational education and 11% had a university qualification. This reflects the relatively low levels of educational qualifications in the population as a whole and is in line with the fact that most people work in agriculture (53%) and construction (10%). According to the 2001 Census, about a third of all jobs held were temporary, seasonal or occasional.

Unemployment

One of the key differences between the Census and the LSMS assessments of the labour market is the fact that it resulted in a lower unemployment rate for women, as many women were not systematically searching for a job. The LSMS is better placed to distinguish the boundaries between discouraged unemployment and inactivity.

The trend in unemployment has been downward between 2002 and 2003 according to the LSMS. INSTAT uses 2 definitions. The standard definition of unemployment requires that the individual has actively engaged in some type of job search. The relaxed definition of unemployment also includes seasonal workers or discouraged job seekers, who may be considered as unemployed even though their attachment to the labour force is marginal. Under both definitions, the unemployment rate appears to have fallen by 2 percentage points between the 2 years, which is a substantial achievement. This improvement in employment indicators ties in with the current rates of economic growth.

Figure 3.4 Unemployment rate according to the standard and relaxed definitions



Source: INSTAT calculations with the 2002 and 2003 LSMS data

The LSMS design, which interviews the same individuals each year, allows a comparison of the employment status across years for the same respondents. Table 3.8 shows the employment status for individuals of working age interviewed in 2002 and 2003 and shows that there is a quite a lot of movement between employment states. The percent highlighted in bold on the diagonal shows those who were in the same employment status at each year of the survey. The percentage off the diagonal shows those who had changed their employment status by 2003.

The data suggest that for those who are in employment their status is relatively secure: 87.5% of these people were in employment at both years of the survey. Those who were unemployed in 2002 were the least stable category with just 39.5% giving the same response at both years. On the contrary, 39.6% had moved into employment by 2003 while 21.1% had become inactive, providing some positive evidence that over one third of the unemployed had found employment within a year.

Table 3.8 Employment status of working age individuals, 2002 and 2003 (%)

		2002		
		Employed	Unemployed	Inactive
2003	Employed	87.5	39.6	20.6
	Unemployed	4.8	39.3	11.2
	Inactive	7.7	21.1	68.2
		100	100	100

Those who were not working were asked about their job search behaviour and how they had gone about looking for work. When people were asked in 2002 about their efforts to find a job, 64% of them said that they had looked for work through friends or a relative, 26% through a labour office and 4% through contacting the employer. The length of time people spend looking for work varies but for many people it is a long process. On average, 32% of respondents who were not in work in 2002 had been looking for work from between 12 to 23 months and at 2003, 42% of respondents had spent up to 2 years looking for work. With relatively long periods of unemployment, there is a danger that some people may stop trying to find work.

Investing the earnings from international migration

The decision to migrate is considered the result of a joint decision by members of a household and assumes that the household members share the costs and benefits of this decision. This explains the motivation of migrants to remit earnings to household members.

Earnings from migration do not only return to Albania in the form of remittances by household members who reside permanently abroad but is also brought back by temporary migrants who spend limited parts of the year outside the country. Short-term migration is a less well known phenomenon. Evidence on it is provided by the 2002 LSMS. The survey included information on the migration history of individuals who had been abroad for at least 3 months at any time between 1997 and 2001 but were in Albania at the time of the survey. A fifth of households have members who have been temporary migrants, whereas a third of households have members who are permanent migrants.

A study based on these data¹ shows that households with temporary migrants are larger than the average Albanian household. Households whose members migrate temporarily to Greece tend to live in rural areas of the central and mountain zones, are poorer and less educated. Households whose members migrate temporarily to Italy tend to originate from the rural areas of the coastal zones, are better off and more educated than the average household.

Characteristics of households with temporary migrant members	No migrants	Migrants to Greece	Migrants to Italy
Household size (members)	4.2	4.7	4.5
Average education (years)	8.6	8.4	9.4
Monthly consumption per capita (Lek)	7841	7019	9205
Living in rural areas of the coastal zone (%)	80	13	7
Living in rural areas of the central zone (%)	77	20	3
Living in rural areas of the mountain zone (%)	76	19	5
Proportion of households (%)	82	13	5

An important policy question is how to steer the income that migrants, whether temporary or permanent, bring back to the country. If income from migration is invested in productive activities, then it could help create jobs in these rural areas and perhaps reduce the flow of migration. A study that used the results of a specific survey in the Korca region² examined the effects of migration and remittance income on the productivity of agricultural households. The results showed that households without migrant members were less efficient in farming. A potential explanation is that the recipients of assistance lower their effort in the knowledge that remittance income guarantees a certain level of welfare.

Although remittances may well be used for investment outside agriculture, complementary evidence from the LSMS confirms that they are most commonly used to pay for basic necessities and durable goods. The government has been formulating a migration strategy with support from the International Organisation of Migration, which will also include actions to facilitate the flow of remittances into business activity. Building confidence and increasing the efficiency of the banking sector is considered a necessary step³.

Sources: ¹ G Carletto et al. (2004) Internal mobility and international migration in Albania, ESA Working Paper No. 04-13, Food and Agriculture Organisation; ² E Germenji and J Swinnen (2004) Impact of remittances on household-based farms in rural Albania, Paper presented at the conference on 'New perspectives on Albanian migration and development', Korca, September 2004; ³ E Uruçi and I Gedeshi (2003) Remittances management in Albania, Centro Studi di Politica Internazionale Working Paper 5/2003

3.5 WATER AND ELECTRICITY

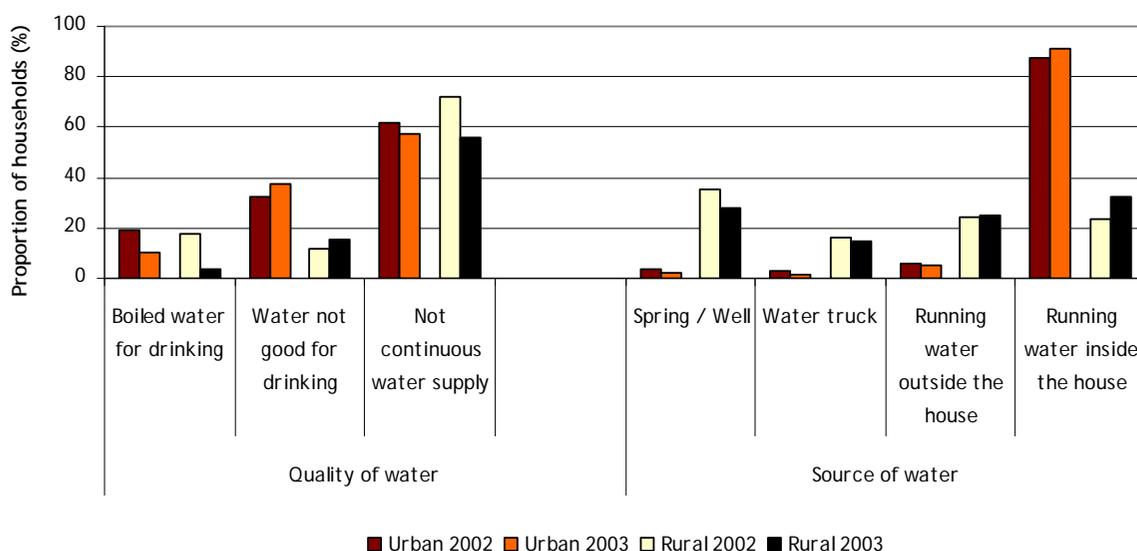
Access to basic facilities such as water and electricity are indicators of households' quality of life and as noted in the health section earlier, those who did not have access to running water and sanitation within their house tended to report worse health.

Water supply and quality

Of all households in 2002, 50% had running water inside the dwelling, 17% had running water outside the dwelling, 22% used water from a spring, well or river while 11% used a public tap or water truck. Just under one third of households (32%) had a continuous supply of water and poor households were less likely than non-poor households to have running water or a continuous supply.

Figure 3.4 presents indicators of access and quality of water supply in urban and rural areas in 2002 and 2003. Urban households were more likely than rural households to have running water inside their dwelling. In contrast, rural households, where water was more likely to be from a spring or well, reported higher water quality levels in the sense that it was more often suitable for drinking. Similarly, those in rural areas were less likely to say that they boiled their drinking water than those in urban areas.

Figure 3.4 Water source and quality, 2002 and 2003



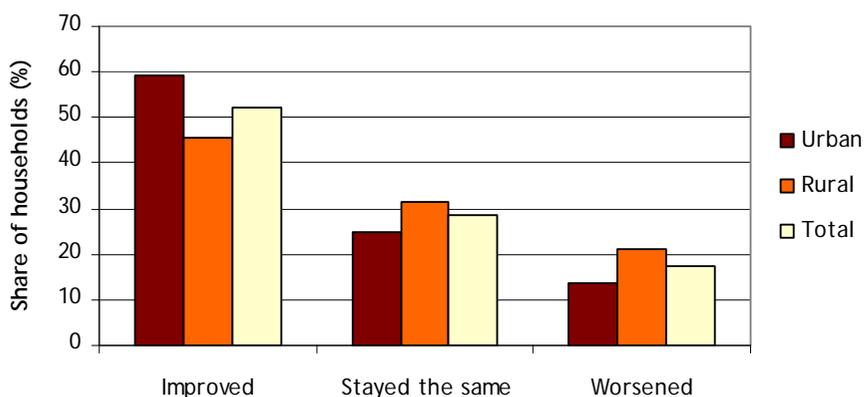
Between 2002 and 2003, there were improvements in water indicators, although the inequities between urban and rural areas remained broadly the same. Overall, there was an increase in the proportion of households with running water inside their dwelling to 60%. Conditions improved for rural areas where the proportion of households with running water inside the house increased from 24% in 2002 to 33% in 2003. In 2003, rural areas were as likely as urban areas to have a continuous water supply and the continuous supply had improved in all areas. The proportion of households reporting that their water was not good for drinking increased slightly in 2003 but on the other hand the percentage boiling their drinking water fell in both urban and rural areas. However, this may in part be because more households used bottled water for drinking (an increase from 40.3% of households in 2002 to 44.1% in 2003).

For households with running water either inside or outside the house, the average supply fell from 5.5 to 4.9 hours per day between 2002 and 2003. However, the mean for all households increased slightly from 1.9 to 2.0 hours per day during the same period. Urban areas were supplied with water 3 hours per day on average, while in rural areas the average supply was just 1 hour.

Electricity

Improving the electricity supply is considered a priority, in particular to improve the regularity of the supply and reduce the number of electricity cuts experienced by households and businesses. In 2002, 13.5% of households in the LSMS said they never had any electricity cuts, 5.6% had cuts several times a month, 8.6% had cuts several times a week and 77.2% had cuts every day. For those experiencing cuts, the mean number of hours per day without electricity in the month before the survey was 8.6 hours. Urban households had on average no electricity for 7.2 hours per day and rural households for 9.5 hours per day.

Figure 3.5 Perception of the electricity service quality between 2003 and 2002



In 2003, the mean number of hours households had no electricity had fallen to an average of 4.8 hours per day. In urban areas the mean was 3.5 hours and in rural areas 6 hours per day. In 2003 households were also asked whether they thought the electricity service had improved over the past year. The majority (52%), thought that the service had improved over the past year while a further 28.5% thought it had stayed the same. Only 17.5% thought that the electricity service was worse than the year before. Figure 3.5 shows the distribution by urban and rural areas. Households in urban areas were more likely than those in rural areas to say that the electricity service had improved in the past year while those in rural areas were more likely to say that it had remained the same or worsened.

4 Progress with the implementation of the NSSD

4.1 GOVERNANCE

According to the NSSD, the success of institutional and legal reforms is considered an indispensable condition in achieving mid-term growth and poverty reduction objectives. Economic growth requires continuous improvements in the performance of public institutions, while poverty reduction needs an open and comprehensive decision-making process for all social groups, the poor, vulnerable and unprotected in particular.

The institutional reforms in general aim at: (i) further improving the balance between different levels of powers; (ii) increasing programming capacities of institutions; (iii) increasing their efficiency in implementing policies and legislation; (iv) increasing fiscal efficiency; (v) strengthening accountability and improving public services; (vi) democratisation, increased transparency and reduction of corruption.

Strengthening of the rule of law is a key factor of stability and economic growth, as well as of success of reforms. The mid-term priority of the government has been to increase the efficiency of public institutions: (i) establishing/strengthening responsible institutions specialised in drafting, implementing and monitoring policies and laws; (ii) strengthening institutional interaction; (iv) strengthening public accountability of functionaries and institutions; (v) adopting instruments to motivate public functionaries; and (vi) improving available means and technology.

The priority directions of institutional and legal reform in the framework of NSSD are: (i) strengthen public order and fight against organised crime; (ii) fight against corruption at all levels of administration; (iii) reform the judicial system; (iv) deepen the reform in public administration; (v) radically improve fiscal management; and (vi) deepen the reform of government decentralisation.

The foreign policy priorities are: (i) intensification of political and diplomatic action toward European and Euro-Atlantic integration; (ii) encouragement and strengthening of bilateral and multilateral co-operation at European and international level; (iii) development of regional moderating role and intensification of relations of all-round cooperation with all countries in the region; (iv) development of dynamic diplomatic action to generate an increasing positive image of the country and extension of the country's presence and role in international forums and organisations; (v) development of legal framework of bilateral and multilateral co-operation; (vi) further strengthening of diplomatic action to facilitate free movement of people; and (vii) increased interest about Albanian diaspora.

In spite of positive progress in institutional and legal reforms, in recent years in particular, the ability of institutions to effectively implement the law needs to be further improved.

Justice

The judicial reform represents one of most important directions of institutional reforms. According to the NSSD, the directions of judicial reform are: (i) improvement of the quality of judicial/legislative process through developing the quality of normative acts; (ii) improvement of professional level of judges, attorneys, advocates, court administrators and the mechanisms of their motivation; (iii) strengthening and institutional improvement of the justice system (self-organisation and self-control of the judiciary), rationalisation of organisational / territorial / functional structure and strengthening of other institutions related to the judiciary, such as the Ministry of Justice, Office of the Attorney General, Bailiff's Office, and judicial police.

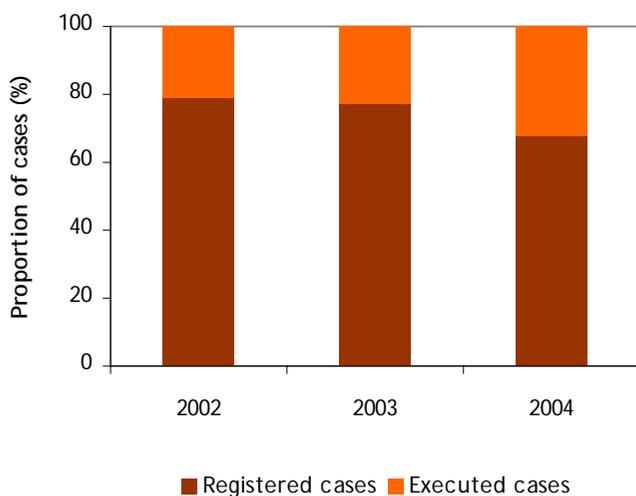
Increase transparency and improve management of judicial proceedings In 2004 a management system of court cases has been established, which automated the process of case administration in three pilot courts. The system will be established in other courts during 2005. Decisions of the High Court were published for the first time, while the publication of decisions of regional appeal courts is pending.

The statistics sector in the Ministry of Justice collects unified procedural, administrative, investigative and judicial data from first instance courts, courts of appeal, the High Court, the Office of Attorney General, the General Directorate of Prisons and the Bailiff's Office.

Increase implementation rate of judicial decisions The Internal Regulation of the Execution Service and the Evaluation System of Judicial Bailiffs were approved in 2004 to ensure success in carrying out executive titles, opening thus the way to professional categorisation of any judicial executor. A guiding commentary 'On unified modules of procedural activity of judicial execution service' was prepared, which will unify judgement in performing execution actions and at the same time will prevent ill-treatment or misinterpretation of actions by judicial bailiffs.

During 2004 the High Court has reviewed 58% of 3033 submitted cases (3747 in 2003), against 54.5% of cases in 2003. Figure 4.1 shows that Bailiff's Offices have increased the speed of carrying out cases and executive titles to 61% of registered cases in 2004 in comparison to 33% in 2003 and 20% in 2002.

Figure 4.1 Execution of cases by Bailiff's Offices



In spite of work done, the legal framework of the Judicial Execution Service is incomplete. This prevents completing execution titles, especially in cases when debtor or creditor is the state. In 2004, the Bailiff's Office executed 3355 cases where creditor/debtor is the state, out of 6870 registered, compared to 579 cases executed in 2003, out of 6500 registered.

Improve prison and detention system A number of investments have been made in 2004 to improve conditions in the detention system under the authority of the Ministry of Justice. About 760 persons are detained in these institutions, or less than half of the total number of detained persons, while the other part is held in police station premises under the authority of the Ministry of Public Order.

Investments are made in the prison system to increase capacities and reduce overpopulation of existing prisons by adding 610 places in 2004. Investments have been made also to improve the

heating and sanitation systems. The issue of overpopulation of prisons is expected to be solved definitively in 2006 due to planned investments, which will add 700 more places according to EU standards.

Public order

The government priorities in 2004 were: (i) institutional reform; (ii) prevention and fight against crime; (iii) prevention and reduction of conflicts and illegitimate actions; (iv) increased security for citizens in exercising guaranteed rights and freedoms.

Internal structural reorganisation to increase police efficiency In 2004: (i) there was a marked separation of the political from the technical level, as the police managed its own budget; (ii) the Border and Migration Department was established; and (iii) the Department of Coordination and Control of Territory was established.

Fight against trafficking and criminal activities The main directions of activity have been: (i) improving legal and organic structures; (ii) identifying the geographic extent and criminal nature of illegal trafficking; (iii) increasing the level of cooperation and the coordination of actions with other bodies of public administration, at the central and local levels; (iv) strengthening continuously the cooperation with the Serious Crimes Attorney's Office, in particular the task force for information exchange and joint operations; (v) drafting the Action Plan of Anti-trafficking for the National Strategy for Children to be approved by the government.

Fight against drug trafficking In 2004, the National Strategy Against Drugs (2004-2010) and the Action Plan were drafted. The responsible structures have focused their work on identifying actions and persons involved in drug trafficking and on cooperating and coordinating activities of public institutions in reducing supply and demand.

Table 4.1 Fight against drugs

	2003	2004
Number of cultivated and eliminated plants (roots)	186,000	77,000
Heroin seized (kg)	114.7	240.6
Prosecuted	281	395
Arrested	247	297
Tried	9	39
Escaped	29	59

Source: Ministry of Public Order

Fight against economic and financial crime In 2004, 1339 offences were identified and 1323 of them were revealed, involving 31 criminal groups with 114 members, out of which 80 were arrested. Activities have focused on: (i) Reorganisation of structures in the fight against money from criminal activities; (ii) Investigation and intensification of work to identify movable and immovable properties that are products of criminal activity; (iii) Approval of the Action Plan on 'Prevention and fight against corruption 2003-2004'.

Fight against terrorism The main objective has been to prevent, expose and strike against crimes related to terrorism and against life and property. In 2004, 5117 penal offences were identified, or 1452 more than in 2003, and 3352 or 69% of them were revealed. The service has been strengthened and measures were taken to cooperate with the police regarding the control in diplomatic missions of Western countries, in the framework of preventive measures against eventual terrorist acts.

Police ranks Nominations in various functions of the State Police are made according to the rank of officers. In the framework of clearing the police from corrupt elements, a number of disciplinary measures have been taken. In 2004, 323 critical reports were sent to the Attorney's Office related to 307 police subjects, out of which 24 of high ranks, 88 of middle ranks and 211 of basic ranks. Of them 52 were arrested.

Border control and regional cooperation Strengthening of border security has been seen in the context of facilitating the legal passage of citizens and vehicles. A law 'On entry, stay and treatment of foreign citizens in the Republic of Albania' was approved. About 456 foreign subjects were refused entry in Albania because they lacked necessary documents, as against 425 refusals in 2003. The regulation 'On administration, maintenance, and use of services of floating and radio locative means' has been drafted and approved. The regulation on organisation of work in airports and ports has been revised.

Road safety In 2004, there were 734 road accidents that caused the death of 282 citizens and the injury of 186 others. Compared to 2003, there was an increase in the number of accidents, which is explained by the fact that light accidents were also included. Controls of documents, vehicles and driving schools have been intensified. A study on road safety conditions, the level of accidents, and problems related to the improvement of road infrastructure was prepared to plan measures to prevent accidents. About 440,176 fines amounting to Lek 414,782,568 were issued. About 91% of the total volume and 87% of the total value of these fines was collected. Another achievement was the procurement of speed and alcohol measuring instruments throughout the country.

Radio-communication system The objective is full computerisation of the State Police and electronic management of information. A functioning data transmission network in the Border Police Departments is completed, ensuring high-speed connection with border posts. A National System of Communication in HF frequency has been established for Regional Police Departments. Mini systems of radio-communication in UHF have also been established. Automatic systems of surveillance and recording are built in border posts.

Public administration

According to the NSSD, the deepening of the public administration reform aims at: (i) clearly determining the responsibilities, authority and accountability of public institutions and functionaries; and (ii) strengthening the separation of political and civil service levels and ensuring sustainability of the civil administration. The main directions of the reform are: (i) complete the reform of institutional structures; (ii) reform internal control; (iii) fully implement the status of civil servant and re-draft the status of political employee; and (iv) improve public information.

The total number of positions in the civil service was 1697 or 0.8% more compared to 2003. In 2004, 330 new civil servants were appointed, against 277 appointed in 2003, which reduced the number of vacant positions by 10.7%. The Civil Service Commission annulled 2.1% of competitions in 2004 for not observing the rules. The average number of applicants for a procedure was 10 candidates, against 8 candidates in 2003 and 5 in 2001.

Institutional restructuring The Ministry of European Integration was created in 2004 to achieve the commitments of the government in the Stabilisation and Association process. The Ministry of Justice, the Ministry of Territorial Adjustment and Tourism, and the Ministry of Education have undergone radical changes in their functional structure. In compliance with the law on internal control, the structure of internal auditing units in line ministries has been changed. In order to implement the National Strategy of Information and Communication Technology, small IT units have been established and strengthened in institutions. The terms of reference and classification of supporting structures in line ministries, such as the juridical, economic, and human resources management departments, have been unified in 2004.

During 2004, the Department of Public Administration established the inventory of all Council of Ministers dependent institutions, the line ministries and independent institutions (including data on the establishment of the institution, the legal basis for functioning, organisation, structure, wages of employees, services offered etc.), which opened the way for a functional and structural review in 2005.

Civil service The law on civil servants began to apply in 2004 also for employees of the Public Procurement Agency, the tax, customs and other authorities. Civil service training focused on capacity building in institutional management, European integration issues and human resource management. Attendance increased to 2090 persons in 2004, up from 1215 in 2003.

Wage reform The categories of 'specialist' and 'head of division' were established in line ministries in 2004 (except for the Ministry of Youth, Culture and Sports in which they will be introduced in 2005) and in ten Council of Ministers dependent institutions and ministries. A separate fund for wage reform has been included in the Medium Term Budget Programme.

Decentralisation

Following on from the National Strategy for Decentralisation and Local Autonomy (1999) the NSEED highlighted the importance of decentralisation for growth and poverty reduction. The strategy was to proceed cautiously step by step recognising both that decentralisation is a crosscutting strategy and therefore an integrated part of a number of sectors and that there needed to be readiness to take on responsibilities on the part of local government. In addition it was important to ensure the appropriate legislative framework was in place. The NSEED laid out 3 objectives to be attained by 2004 with support in implementation from the Local Government Law (2000). In summary, these were:

- The decentralisation of exclusive, shared and delegated functions to local government with the appropriate legislation. The aim was to give local government increased decision making rights in setting priorities, use of resources and monitoring of service performance.
- The provision of increased opportunities for resourcing of local government including improved distribution of national financial resources and the transfer of immovable property.
- The application of the same principles by local and central government in governance, administrative and financial reform (in particular, the status of civil servants, financial management, inclusion of community in governance and extension of anti-corruption measures).

Functions of local government

The Law on Functioning and Organisation of Local Governments distinguishes between 3 types of functions to be performed by local governments.

- **Exclusive functions** Local governments exercise full administrative, service, investment and regulatory authority over them. They are financed primarily from the general budget of the local government. They relate mainly to the provision of: (i) local infrastructure (local roads, street lighting and public services, urban planning, urban transport, waste collection and disposal, water supply); (ii) social, cultural and sporting activities; (iii) local economic development activities (public markets, SME support, information and infrastructure etc.).
- **Shared functions** They are undertaken jointly by central government and local governments. Where these functions are performed according to nationally set standards they can be expected to be financed by conditional transfers from the central government budget. Shared functions include pre-tertiary education, primary health services, social assistance, public order and environmental protection. In each of these areas the precise administrative and financing arrangements involved in sharing have yet to be defined.
- **Delegated functions** Local governments perform these as agents of the central government, for example in operating a particular service or facility. These functions are wholly financed by transfers from the central government budget.

The NSSD Progress Reports of 2002 and 2003 documented the progress of decentralisation particularly in water supply, health, education and financial management. In August 2004, the study 'Albania: Decentralisation in Transition' was published by the World Bank. This study provides an independent assessment of the decentralisation process. It concludes that:

"Although Albania is far from completing the design of political, administrative and fiscal decentralisation that would be able to satisfactorily improve service delivery, governance and accountability, it has to be acknowledged that considerable progress has been made in establishing the basic institutions and legal framework, as well as in implementing policies towards decentralisation".

Decentralisation is, as was envisaged, a slow process of change but steady steps are being taken and the government remains fully committed. A summary of the progress in 2004 is presented below.

Local government fragmentation An ad-hoc Parliamentary Commission has been set up to facilitate change in the territorial divisions prior to the 2006 local elections. The fragmented nature of local government with 309 communes and 65 municipalities belonging to 12 regions presents a challenge to social and economic development. This is exacerbated by internal migration which reduces the functioning of small units.

Local government property So far twelve local government units have completed the inventory of all public properties and lands and have had those designated as local government premises transferred.

Legal framework The highest priority identified in the National Strategy for Decentralisation was to prepare a package of laws that would enable decentralisation to local government to be implemented. In 2000 the new legal framework was established with the passing of 2 organic laws 'On the organisation and functioning of local governments' (8652/2000) and the 'On the administrative-territorial division' (8653/2000). Since then several laws and regulations have been passed. In 2004 there was an amendment to Law 8652. The prime purpose was to increase competencies of village heads in the Commune Councils.

Assignment of responsibilities and expenditure allocation The assignment of responsibilities along with increased expenditures progressed in 2004, albeit slowly. According to the MTBP (2004-2006), local government expenditures, excluding those financed by conditional transfers from line ministry budgets, were projected to increase from 1.9% of GDP in 2002 to 2.1% of GDP in 2006. This increase was to reflect the government's commitment to the expansion of local government as providers of services and to ensure these services were more adequately financed. In 2004, local government expenditure was 2% of GDP. A breakdown of expenditure by source of revenue is provided in Table 4.2.

Table 4.2 Local government spending, in Lek million

	1999	2000	2001	2002	2003	2004
Local government grant	5134	4595	4943	9073 ¹	6627	6622
Local revenues	885	1315	2038	2676	4979	5553
Small business tax	1188	1641	1974	2548	2944	4060

Source: Ministry of Finance

¹ In 2002 the decision was taken to allocate health operation and maintenance expenditure as an unconditional grant to local government. Due to eventually limited allocations made by local government to that purpose, the grant was converted back into a conditional transfer in 2003.

Exclusive functions The following places took place in 2004:

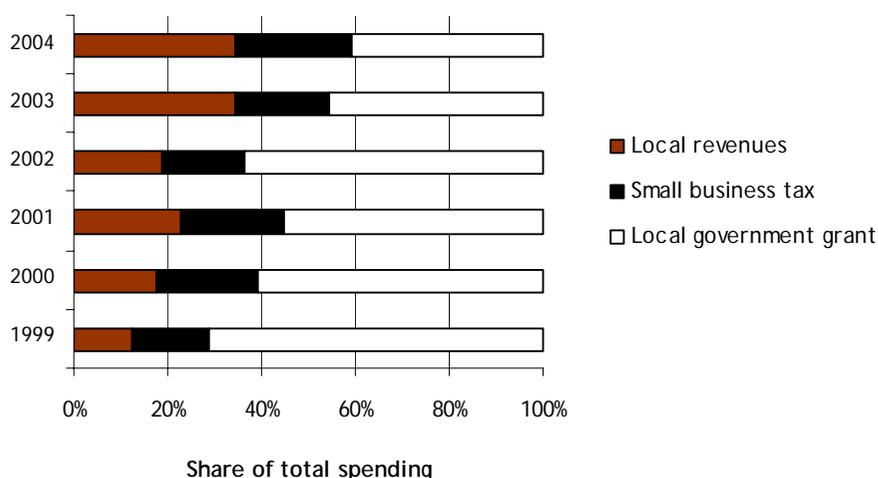
- Water supply and sanitation In 2002, the decentralisation policy for water supply and sewerage was approved by the Council of Ministers. All assets and water systems were to have been transferred by 2004 (see the discussion on water and sanitation in a later section). However, while the inventory of water supply systems was completed only 8 water utilities inclusive of 131 systems were transferred to municipalities and communes. Despite the legal and administrative challenges it is planned to complete this process in 2005 although not all local governments are enthusiastic about the transfer under current arrangements.
- Urban public transportation and traffic regulation Public transport licensing is since 2003 a competency of local government. The majority of competencies have been delegated to municipalities and communes, while the regional councils have the authority to licence public and goods transport between municipalities and communes within the region, according to the standards of the Ministry of Transport and Telecommunications.
- Urban planning and land management While this is an exclusive function, the current legal framework does not allow for local government to take full responsibility for urban planning. In 2005/06 a new law on urban planning will be drafted to clarify the competencies of local government and central government.
- Housing In 2004 the law 'On social programmes for housing of city dwellers' was passed. Financing for this policy will be through central government contribution and municipalities from their taxes on immovable property (see the discussion on urban development in Section 4.3).

Shared and delegated functions The delineation of specific competencies is still in the process of development. While few functions have been shared or delegated to local government, policy papers approved in 2004 in health, education and social services should lay the basis for future decentralisation of functions. Following on from the success of the Community Jobs pilot scheme (see the discussion on social assistance in Section 4.4) local government in 2005 will have the competence to administrate social assistance funds either as cash payments or as payment for work on public labour schemes and community services. Currently local government has little decision making power in education or health. A number of ministries are developing their regional structures to enable greater delegation of decision making power.

Local government will also be transferred the property rights over health clinics and schools with the proviso that the building remains used for its original purpose.

Revenue autonomy Increased revenue autonomy is essential for the development of local government. The local government's revenues consist of (i) local revenues, and (ii) revenues generated from national revenue sharing. These include (i) unconditional transfers, (ii) conditional transfers, and (iii) shared taxes. Conditional transfers are proportionally a lot larger than unconditional transfers. This means that revenue autonomy is still relatively limited. Block grants (given since 1999) for operation and maintenance for pre-tertiary education facilities, primary health facilities and for payment of salaries and economic aid transfers continue. Local revenue collection has improved significantly since the adoption of the fiscal package in December 2002. In 2004 own local government revenues were Lek 9.6 billion up from Lek 7.9 billion in 2003 (see Figure 4.2). The proportion of revenues from the state budget (local government grant) has decreased over the past 5 years.

Figure 4.2 Proportion of unconditional local government grant, revenues and small business tax to total spending 1999-2004



Smaller municipalities and rural areas are having more difficulty in gaining local revenue. The revenues of the small business tax are concentrated in Tirana, Durrës, Elbasan and Korçë. To help reduce disparities the government is reforming the system of unconditional transfers. The information database on local governments that is used for determining fiscal equalisation was improved. In 2004, there were special fiscal equalisation measures taken for 156 mountain communes and 37 municipalities and in 2005 this will be extended to a quarter of mountain communes and 45 municipalities. For 80 of the poorest communes there is extra compensation. In 2005, the responsibility for investment funds in pre-tertiary education and primary health care will be transferred as a block grant. The decentralisation strategy proposed the sharing of 15% of personal income tax to communes and municipalities and of 5% of company profit tax to communes, municipalities and regions.

Role of Regional Councils The role envisaged for Regional Councils in the decentralisation strategy was one of taking responsibility for coordinating and harmonising policies among communes/municipalities consistent with the regional policies of the central government. The region is permitted to deliver public goods and services as decided by the Regional Council and within the limits of the law. The regional councils remain motivated to define and develop their role within local government. There are pilot projects that expand the role of the council. For example, in 4 regions there are regional committees for planning community services. The

delegation for managing capital investment and for urban planning from smaller local government units will expand their activities. Regional development strategies are being developed but the regions do not have the responsibility or financial means to implement these strategies or the clout to influence the sectors on the development and coordination of their decentralisation policies.

The sources of Regional Council revenues are the unconditional block grant from the state budget (Lek 941 million in 2004 or 15% of the total unconditional block grant to local government) and a transfer from municipalities and communes of 4% of their revenue collection (though this amount is not being enforced). Regional Councils do not have the competency to raise own-revenue.

Institutional strengthening There is concern that local government does not have the capacity to respond to an increase in the rate of decentralisation. Pilot projects decentralising responsibilities to local governments that meet particular criteria are one mechanism used to test how decentralisation might work in practice. For example, the transfer of capital expenditure budgets mentioned above followed on from a successful pilot in Tirana municipality.

Encouragement of citizen participation in local government, which will ultimately strengthen accountability, is occurring in projects throughout the country. At least eleven municipalities held citizen perception surveys in 2004. A citizen survey conducted in Tirana Municipality in 2003 influenced the priorities in the 2004/05 budget. Pilot projects in participatory budgeting, conducted in 2 communes and 2 cities in 2004, are designed to increase the accountability of local government through engaging citizens, building trust and improving service delivery. These projects can be linked to the work of the Albanian Development Fund, as they provide a method for prioritising investment projects. The second phase of Community Works Project began in 2004.

Local level capacity building, essential ultimately for accountability and transparency is beginning to occur and qualitative feedback suggests that participants in local level forums are more articulate than 4 years ago. Unfortunately, while a strategy was approved in 2004, the Training Agency for Local Government is not yet funded sufficiently to be functional. Some progress has been made on capacity building of local administrations through human resource development centres operating in Fier, Kukes and Gjirokaster, supported by UNDP. With local government acquiring greater responsibility, it is important that modern standards of monitoring service delivery and accounting for expenditures are adopted. The line ministries still have weak monitoring capacity and the draft law on internal audit, planned for 2004, for local government has not yet been completed.

Donor coordination In order to improve donor support, a Thematic Group on Decentralisation was established in 2004 with an online database for donor programmes in local government. The aim is to increase the cooperation and harmonisation of donor interventions.

Despite considerable achievements, the original 3-year objectives of the NSSD have yet to be fully achieved. The vision of decentralisation remains in place, however the complexity of the challenges has led to a slower pace than originally envisaged. There is a need now to update the decentralisation strategy of 1999, based on achievements to date, and to ensure integration with sector strategies. The revised strategy will need to focus on the fragmentation of local government, further assignment of responsibilities, strengthening of local government institutions (including the regions), building capacity for implementation and monitoring at central and local government level, ensuring local revenue autonomy and improving the transfer/grant system. A medium term work plan has already been drafted by the National Committee for Decentralisation and presented to the Council of Europe.

Anti-corruption

Prevention and fight against corruption remains one of the priorities of the government. The anti-corruption strategy focuses on three key elements: (i) strengthening of the rule of law; (ii) prevention; and (iii) education and public participation. The monitoring of the Action Plan is based on performance indicators. In the period 2003-2004, out of 119 planned measures, 105 or 90% of the total were accomplished.

Strengthening of structures The High Court of Serious Crimes, as well as respective local courts and attorney's offices, were established in 2004. A task force to investigate penal offences in the field of organised crime and a department for the fight against organised crime and the protection of witnesses were set up in the General Department of State Police. The National Committee of Coordination for the Prevention of Money Laundering was created.

Legal reform The legal framework for public procurement, declaration of wealth, financial obligations of elected persons and some civil servants, competition, rules of ethics in public administration, procedures for external activities of civil servants and donations, and conflict of interest were improved in 2004.

In the penal field, the code of penal procedures on special investigation means in the Republic of Albania has been improved. In addition, it is worth mentioning the law on the protection of witnesses and collaborators of justice, the law organisation and functioning of courts dealing with serious crimes, the ratification of the additional protocol to the penal convention on corruption, measures against financing of terrorism, the implementation of the European Penal Convention on Corruption, the law on prevention and fighting organised crime etc.

Table 4.3 Selected performance indicators of the anti-corruption action plan

	2003	2004		2003	2004
Disciplinary actions against judges			Sanctions against police authorities		
Dismissed	4	4	Disciplinary measures	1715	2334
Disciplinary measures	8	4	Administrative measures	326	729
Sanctions by the High State Control			Convictions	138	323
Disciplinary measures	344	196	Offences in exercise of public duties		
Administrative measures	142	73	Accused	224	258
Convictions	11	25	Prosecuted	111	159
Sanctions by General Department of Audit			Convicted	76	47
Disciplinary measures	696	1713	Offences related to customs and tariffs		
Administrative measures	2012	2309	Accused	145	123
Convictions	37	36	Prosecuted	185	291
			Convicted	141	233

European integration

During 2004, substantial progress has been made in the negotiations of the Stabilisation and Association Agreement (SAA). There were 6 rounds of negotiation were concluded, of which 2 were political and 4 technical. Albania is close to finalising the SAA negotiation with the European Union. The first reading of the Agreement has been finalised. In respective articles of the agreement, transition periods proposed by the Albanian side have been accepted; in view of finalising the text, some complaints and protocols contained in the agreement remain to be reviewed. The main achievements of these rounds are the following:

- A first reading of 135 articles of the SAA was completed
- Issues of trade in primary and agro-processing products were negotiated, as agricultural sector liberalisation is expected to progress over the next 5 years
- The financial effects in the Albanian economy, as a result of implementing the liberalisation of custom tariffs, were calculated
- The treatment of Title 8 'Cooperation policies', which contains 25 articles, including bilateral co-operation in all areas of the *acquis communautaire*
- The quality of technical negotiations to support the official government proposals for the formulation of articles and their transition period was improved.

Discussions in the framework of the Consultative Task Force between the EU and Albania and the Technical Working Groups have focused on assessing progress in the preparation of the 2005 parliamentary elections, the fight against organised crime, migration and related issues, respect of human rights and minorities, freedom of expression and media as well as compensation and restitution of property. These meetings serve as a technical monitoring tool through which information is exchanged and legal and institutional problems are identified.

Since November 2004, the Stabilisation and Association process (SAP) countries have been included under the umbrella of Directorate General Enlargement, a very significant move that expresses the support of the EU.

The European Partnership agreement will assist greatly in identifying short and medium-term priorities to come closer to EU membership. The government prepared the Action Plan for the Implementation of European Partnership Priorities which was approved by Council of Ministers Decision 634 in August 2004. This plan represents the effort of the Albanian institutions to identify the structural measures needed to achieve priority objectives of the SAP in the short (1-2 years) and medium term (3-4 years). Its implementation will strengthen institutions and public administration, approximate EU legislation, and increase effectiveness to implement reforms.

The government has also embarked on the design of the Action Plan for the Approximation of Legislation. This will be the basic tool for planning, prioritising and monitoring the European integration process. A draft plan has been finalised and has been sent for comments and approval to the Council of Ministers.

This plan is expected to be approved in the first half of 2005. It is divided in two phases: (i) definition of objectives and description of the present situation; the key element is to understand and compare national commitments in the SAP in light of the gradual approximation of legislation and build administrative capacities for its implementation; (ii) identification of appropriate measures for the accomplishment of the objectives. The plan covers a ten-year period, divided in short-term and medium-term periods. A task force is established to monitor it, as provided by the Council of Ministers Decision no. 634. The plan will be constantly updated in terms of administrative capacity, the calculation of financial costs to coincide with the period of drafting of the annual budget, and the review of implementation staff.

In the framework of intensifying collaboration and sharing experiences with other countries involved in the SAA as well as new member countries of the EU, collaboration protocols were signed with Croatia, Macedonia, Poland and Hungary. These protocols aim at promoting the development of relationships in order to accelerate membership.

EU support for implementation of European integration process priorities

- The CARDS programme remains a very important financial tool for fulfilling the objectives of the European integration process. Financial support through the CARDS programme over the period 2001-2006 will reach €278.4 million concentrated in 5 main directions: justice and home affairs - €119.1 million (42.7%); economic and social development - €90.1 million

(32.4%); strengthening of administrative capacity - €37.5 million (13.5%); environment and natural resources - €18.5 million (6.7%); democratic stabilisation - €9 million (3.2%); and other - €4.2 million (1.5%). The European Commission has developed its financial assistance strategy for third countries over the period 2007-2013. The CARDS Programme will be substituted by the Pre-Accession Instrument, which will cover not only the candidate countries but also potential candidates, like Albania.

- The European Union Council decided in April 2004 to offer additional assistance of €25 million of direct budget support to Albania, which consists of a €16 million grant component and a €9 million credit component.
- The Regional CARDS programme finances regional projects in which 2 or more Western Balkan countries participate. Albania will continue to be part of the Regional CARDS programme in 2005-2006.
- Funds from the Neighbourhood Programmes will enable coordination with other programmes that are implemented by border regions in Italy and Greece to increase cross-border cooperation.
- Albania can participate in 25 Community Programmes which until now they have only been open to member countries. These are sector programmes that offer project-based assistance.
- It is now also possible to participate in the TAIEX Programme to adapt the national legislation to the *acquis communautaire*.

In the framework of increasing transparency and accountability, one of the main objectives of the Ministry of European Integration has been to raise public awareness of the integration process. A Strategy of Information and Communication with the Public was drafted and approved in December 2004, which is designed to offer mechanisms providing deeper knowledge on the process of European integration, on commitments and obligations toward such a process, and on the rights and benefits for all Albanian citizens.

NATO membership and regional cooperation

In the framework of NATO membership, the Mid-term Strategy of NATO Membership, aiming at coordination and planning of activities to achieve membership has been completed. In the framework of regional cooperation, the development of political dialogue has been intensified and 49 high and very high level visits were conducted. Seven rounds of diplomatic consultations took place and 23 different documents related to bilateral relations were signed. Three sessions of joint commissions of border, economy and free trade issues were convened. Applying the spirit of dialogue and understanding with all regional factors, the Albanian diplomacy has managed to promote the image of Albania as a factor of stability and peace in the region.

Important progress is noticed in relation to international responsibilities and commitments of Albania during 2004. For the first time, Albania has become a member of the United Nations Economic and Social Council for the period 2005-2007, which represents a success of the Albanian diplomacy at a crucial moment for the image of the country, which has encouraged its institutional capacities to play a more active role internationally. Another achievement has been the completion of national reports on implementation of six major conventions of the United Nations on human rights. A new package of measures to facilitate free movement of Albanian citizens has been drafted and approved in the framework of the Action Plan to Facilitate Movement of Citizens, aiming at improving services and protecting Albanian citizens abroad. This is already reflected in the issuing of passports for Albanians in other countries

Another direction of the activity of the Ministry of Foreign Affairs is the completion of the matrix of draft-acts. About 71 agreements, 25 draft decisions and 54 draft laws have been signed and sent to the Council of Ministers for approval. These data show that the Ministry of Foreign Affairs has exceeded planned objectives, applying a systematic monitoring of implementation of its

duties. During 2004, in co-operation with other central institutions, the Ministry of Foreign Affairs completed procedures to make Albania a party in a number of international instruments.

Statistics

Statistical information plays a key role in the decision making process by improving the quality of statistics in time and space. Transforming information into a public good requires not only transparency and impartiality but also a system to monitor performance. After the approval of the Statistical Law in 2004, INSTAT designed a 5-year programme for official statistics to ensure sustainable progress and to fulfil its mission. The programme was submitted to the Council of Ministers and will be approved by Parliament in 2005. It is the first programme designed by INSTAT since its foundation as an independent institution in 1993 and aims to:

- Build and empower the system's identity and the image of official statistics.
- Develop the statistical culture in the country and to promote the use of statistical methods with data coming from the public administration.
- Disseminate the statistical culture and stimulate the need for statistical information.
- Integrate and harmonise the methods used in producing the statistical information, in accordance with the European and international requirements and recommendations.
- Ensure statistical cooperation between all statistical agencies.
- Improve the dissemination of statistics
- Improve the statistical structures

Economic statistics In 2004, INSTAT carried out a structural survey of economic enterprises whose results have been published in 2005. In order to allow the preliminary estimation of GDP with shorter lags, INSTAT introduced improvements in the methodology of calculating macroeconomic aggregate data and national accounts following the European System of Accounts 1995. It also started piloting quarterly estimation of GDP to better assist decision makers. This will be based on econometric methods, annual GDP data, and data from the sales index, applying relevant deflators. The full implementation of the methodology will be completed in 2006.

Social statistics INSTAT carried out the third wave of the LSMS in 2004 and began preparations for a full-scale LSMS in 2005. Even though some progress was achieved in the collaboration with the data users group that improved the design of the questionnaire to address public policies, participation in the group remains poor. Line ministries began using LSMS data to analyse the impact of their policies. In 2004, two line ministries carried out policy impact analyses using LSMS data combined with administrative data.

Collaboration with other institutions In order to maximise the use of administrative statistics and improve the quality of data, INSTAT has worked with the General Directorates of Taxation and Customs, the Ministry of Agriculture and Food, and the Bank of Albania. Memoranda of understanding will allow INSTAT access to primary data and will ensure the use of microdata and further collaboration on necessary improvements to the collection of statistical information.

Even after the approval by Parliament of the Statistical Law and the statistical programme, the government funds for its implementation (LSMS, household budget survey, labour force survey) are not guaranteed. This plan of surveys is intended to complete the collection of individual and household data that allow an in-depth analysis of social and economic conditions as well as to provide the decision and policy makers with the analytical instruments.

4.2 PRIVATE SECTOR

Development of small and medium-sized enterprises

During 2004 over 7500 new businesses were created and it is expected that up to 8,000-9,000 businesses will do so in the coming years. The implementation of the European Charter for small and medium-sized enterprises represents one of the most important agreements on the agenda of the European Commission for Western Balkans. Its principles include improvement of legislation and regulatory framework of SME, improvement of tariff and fiscal systems, reduction of initial costs of setting up a new business, development of training system for entrepreneurship, improvement of electronic communication of businesses, and increase of efficiency of representation of interests of business. Such principles make the axis of the Albanian government policy in the development of SME.

Attention was paid during 2004 to extend schemes of micro-credits in urban and rural areas. The volume of credit for SME increased, the portfolios of micro-credits were improved and institutions of micro-credit were strengthened by transferring funds to Foundation BESA and the Rural Development Fund. The banking network was enlarged, the number of private banks increased, and they were spreading throughout the country.

A Fund for Guaranteeing Credits to SME is expected to be set up in 2005 with the support of an Italian government €30 million loan to be used as follows: (i) €25 million soft credit to build up a credit line; (ii) €2.5 million soft credit to establish a Guarantee Fund; and (iii) €2.5 million grant, as technical assistance for creation of the Fund.

Albanian Development Fund

Since 1993, the Albanian Development Fund has been carrying out projects aiming to improve local infrastructure and to promote private sector development, especially among the poor. In 2004, activities were based on agreements with the Islamic Development Bank (rural infrastructure), the CARDS programme (local community development), KfW (social investment), the World Bank (community works), and the Council of Europe Bank. More than 150 investment sub-projects worth Lek 1.8 billion were contracted. The majority of resources were allocated to road (57%) and water supply (11%) projects.

In terms of operation, the manual of procedures was updated to reflect changes made in strategy and structure, including the commitment to align priorities with the NSSED. About 300 local infrastructure priorities were re-evaluated by specialised social inspectors in collaboration with local government units. A participatory methodology for sub-project preparation, implementation and evaluation was developed. In addition, the Fund has begun organising tenders in communes/municipalities (rather than at the headquarters) to increase the responsibility and general capacity of local representatives.

The main problems that affected operations in 2004 were: the late disbursements of funds by some donors; the delays in the signing of the contract for the community works project due to the new manual of procedures that changed the bidder eligibility criteria; the failure of local units to plan expenditure for sub-projects in their 2004 budget (up to 10% of the total), and the negative role of some commune representatives in procurement and maintenance. The Fund wants to ensure that projects are not only embedded in a longer-term vision of community development, but also contains a robust community-based monitoring and evaluation component, as well.

Foreign direct investment

Foreign direct investments in 2004 amounted to \$341 million, the highest figure in the last five years, as against \$178 million in 2003. This growth is the result of privatisation of strategic sectors and concessionary contracts. In 2004 there operated in Albania 1755 foreign companies, which have employed 4408 persons.

According to a recent evaluation made by SACE, Albania has a smaller business risk now, having moved from level 7 to level 6.

The Albanian government approved the study of FIAS in August 2003 and started implementing it in 2004. The areas where the Action Plan achieved most progress are: the tax and tariff sector, enlarging the basis of taxpayers and simplifying of custom procedures, precipitating clearance and facilitating physical infrastructure of land and construction procedures regarding approval of legal acts on property and restitution and legalisation of immovable property.

The main difficulties in the implementation of Action Plan occur in the field of administrative appeals because certain legal aspects are not being implemented and the respective structures have not been established. Further progress is hampered by the lack of urban regulatory plans throughout the country; the National Strategy of Urban Development will be accomplished with the assistance of the World Bank.

Another general difficulty concerning implementation of the Action Plan has been timely reporting, which did not reach information the Prime Minister's cabinet and the international institutions concerned in time.

Trade liberalisation and export promotion

Eight free trade agreements were ratified in March 2004, which adds to the 29 agreements concluded in the region. Their full implementation started in December 2004.

Exports of Albania to South East Europe countries of free trade reached €32.5 million in 2004 as against €16.7 million in 2003. Trade with countries of the region increased 6.7%. The import-export ratio was 1.9 as against 8.8 in 2003. The most successful exports have been those with Bulgaria and Kosovo, with a quite positive balance. Imports from countries of the region reached €116.4 million in 2004 as against €98.6 million in 2003; in percentage terms growth was 5.7% as compared to 6.1% the previous year.

The use of quotas in agricultural production in 2004 was very low, both in exports and imports. In trade with Bulgaria, 85% of the vigna mungo beans quota was used, while in other products the use of quotas was very low; with Kosovo, 50% of the beer quota was used; with Croatia 74% of plants and fruit trees quota was used; with Macedonia 50% of the quota for products such as tomato, cucumber, and fruits was used; almost no quotas were used in trade with Romania, and Serbia and Montenegro.

Since the free trade agreement with Macedonia came into force in July 2002, Albanian exports doubled with 24 new products in 2003 and 30 new products in 2004. Exports to Macedonia increased by 149% in 2004 relative to 2003, reaching €624 thousand. While imports increased 16% in 2003, 49% of the increase was for food articles. The export-import ratio improved from 1:22 in 2002 to 1:9 in 2003. The only product whose exports fell was medicinal plants.

Exports to Romania increased and imports decreased by 26% in 2004, improving the trade deficit for the first time since 1997. The trade deficit with Bosnia also fell by 23% compared to 2003. Kosovo and Macedonia represent the largest market for Albanian exports. Exports to Kosovo increased to €12 million, while imports reached €8.4 million or six times more than a year ago.

While exports with Croatia reached €300 thousand in 2004, or six times more than in 2003, imports increased by 23.5% reaching €2 million.

The main sources of data for monitoring free trade agreements are the General Directorate of Customs, INSTAT, the Trade Bulletin, the WTO Secretariat, the Department of Promotion of Business, the Ministry of Economy, and the Albanian Centre for International Trade (which publishes periodical reports on foreign trade). The improvement of the system of monitoring progress of free trade agreements is linked with the establishment of the ASYCUDA system. The system was installed in most of the branches of customs in main cities in 2004, which opens the way for deeper analyses of quotas and the implementation of negotiated parameters of open agricultural trade in 2005.

Facilitation of customs procedures

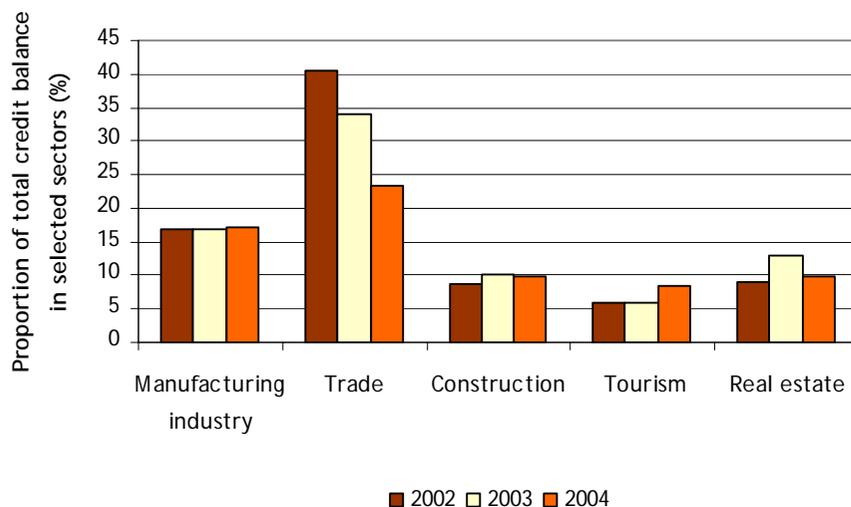
This study by the Albanian Centre for International Trade was published in 2004. Its findings draw partly on a survey of 250 companies involved in import and export activities, customs and transportation agencies. Some of the main conclusions of the research paper follow:

- Custom clearance time has been reduced by more than half compared to the 5.3 days recorded in an Administrative and Regulatory Cost Survey by the Foreign Investment Advisory Service (FIAS) in 2002. This is mainly credited to the introduction of new information processing technologies such as the ASYCUDA system. However, the study suggests that there is scope for further reduction, through simplification of documentation requirements, improvement of information systems and adoption of the best international practices.
- Businesses continue to incur higher operation costs by approximately 5% because of what they perceive as discretion in the application of customs legislation, especially with respect to reference prices. According to the study's estimates, about 70% of the total import volume is cleared through reference prices, which is against GATT Article VII. Poor communication practices and lack of transparency regarding information are also important concerns from the business point of view.
- The Albanian customs legislation has been adapted to the EU legislation. However, further trade facilitation measures, notably investments on the physical and human infrastructure network of institutions involved with trade policy implementation and especially the customs administration, could potentially achieve benefits amounting up to \$200 million.

Source: S Xhepa, N Begaj and A Gugu, Facilitation of customs' procedures and business relations with the customs' administration, November 2004, Albanian Centre for International Trade

Banking system activity and supervision

Lending activities by banks have entered a stable expansion phase. Data from the Central Bank of Albania show that the ratio of credit to GDP has increased from 6% in 2002 to 9% in 2004 (or Lek 70 billion). This development is the result of the banks' growing management experience, improvements in general socioeconomic conditions, and regulatory legislation. There has also been a change in the composition towards longer-term credit during the same period. Credit is being re-directed away from commercial activities, as shown in the figure below¹, although it is not entirely clear whether production activities have been receiving more credit instead; the sector whose share has grown most since 2002 is that of unclassified, miscellaneous activities.



The independent supervision of the financial system is a responsibility of the Bank of Albania, which publishes an annual report on the banking system. The latest report² made three observations. First, the level of credit risk may be increasing following the strengthening of competition after the privatisation of the Savings Bank, the large number of potential new clients, and the fact that lending is mainly done in foreign currency at a time of continuing appreciation of the Lek. Among other, this calls for portfolio diversification by economic sector. Second, the report raised the possibility of banking market saturation in terms of the number of operating banks. Third, attention should focus on the risk control and monitoring arrangements.

Sources: ¹ Bank of Albania, Monetary Policy Report, March 2005; ² Bank of Albania, Banking Supervision Annual Report 2003, July 2004

State aid

State aid is considered as one of priority areas in the framework of the European integration process. Its obligations are determined in articles 70 and 71 of the Stabilisation and Association Agreement where it is clearly stated that there is a need to prepare the legal framework, harmonised with the *acquis communautaire*, and establish an independent structure that will monitor financial schemes of state aid and individual assistance implemented in Albania. In this framework, the Department of State Aid has been established in the Ministry of Economy and the Law no. 9374 'On state aid' was approved.

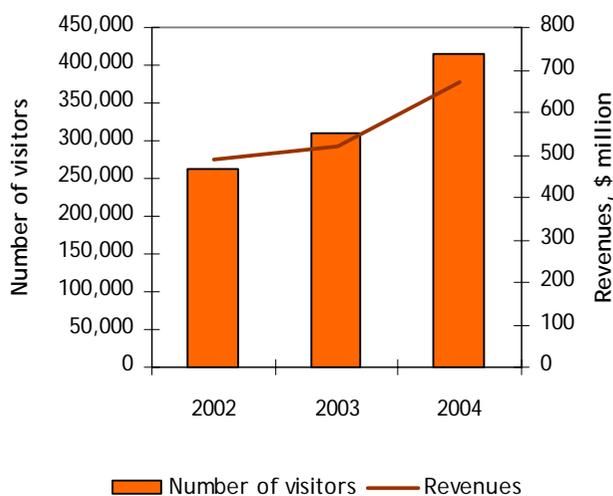
Tourism

In 2004 the Tourism Development Strategy and Action Plan were approved. The most important development for this year was the approval of the project on 'Integrated coastal zone management and cleanup'. Objectives include zoning strategies, environmental analysis, planning for tourism development, design of regulations, investment strategies for infrastructure and application of geographic information systems. The implementation of this strategy will open the way to stable tourism development in Albania.

In 2004 a number of measures and policies were implemented to promote the country and its tourism potential and attract tourists from international markets, mainly from Western Europe as well as the region. Particular attention focused on Albanians from Kosovo and Macedonia. To A Pavilion of Albanian Tourism was organised in Prishtina to present the tourist options in Albania to the Kosovo market, along with a tour of tourist agency representatives from Kosovo in Albania, organised by the Ministry of Territorial Adjustment and Tourism in co-operation with the municipalities of Durres and Vlora.

All actors have widely supported the promotion of tourism in 2004 and financial support doubled since 2003. The 2004 tourist season ran well because of cooperation between central and local institutions, providing regular water and energy, waste cleaning, transport safety, health service and intensive information by media. The Ministry of Territorial Adjustment and Tourism has financed the provision of cleaning equipment to assist local government in cleaning beaches. There was marked growth in the number of tourists and tourism revenues in 2004.

Figure 4.3 Number of tourists and revenue from tourism, 2002-2004



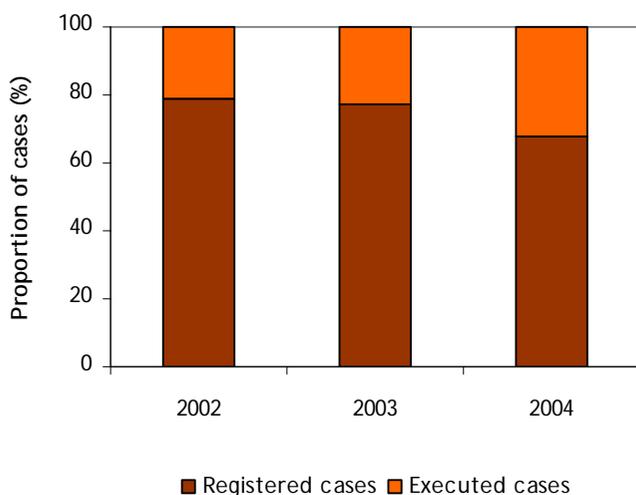
4.3 INFRASTRUCTURE

Energy and mining

The National Strategy of Energy was approved in July 2003, with the aim to: (i) rehabilitate and strengthen existing power stations; (ii) rehabilitate and strengthen the Fier thermo power plant; (iii) enable conditions for construction of new generating sources; (iv) give concession in cashing electrical energy invoices as a measure to improve liquidity; (v) prepare privatisation / concession of distribution.

In 2004, investments in the energy sector reached Lek 12.7 billion. The loss in network declined to 36.6% compared to 39.3% in 2003 and 53.5% in 2000. The production of electrical energy in 2004 continued to rely on hydro power in 98% compared to 2% on thermo energy production.

Figure 4.4 Structure of energy consumption



Legal and institutional reform. The tariff reform has been ongoing for three years, achieving a gradual increase in the price of electric energy with the intention to cover costs. Regarding the reform of the legal framework, it must be emphasised that the law on the sector of electrical energy grants full competencies to the Regulatory Agency of Electrical Energy, divests the state of rights in the electrical energy sector and in particular of the previous right in determining prices and tariffs, creating thus a more effective and completely transparent process.

Division of Albanian Power Corporation (KESH) in legally separate units. In order to achieve this objective and attract lowest-cost necessary investments, the preparation of market in the electrical energy sector is taken forward through restructuring and separation of functions of production, transmission and distribution.

Hydrocarbons. The design of a strategy for the hydrocarbons sector started in 2004 and will be completed in two phases. The main objective of this strategy is to define key steps for the development of this sector in Albania, in compliance with the National Strategy for Energy. The privatisation of public oil companies is already one of the major directions of the strategy and policy of the Albanian government. During 2004 the work focused on the following directions: a tender for Servcom in Fier was announced, the auction for Transnafta in Patos was prepared (to take place during 2005) and the process of privatising Mechanical Oil Plant in Kuçovë, Mechanical Plant in Patos, and the shares of ARMO and Albpetrol by competition began.

Transport and telecommunications

Ensuring the 'construction of a roads network ensuring speed and safety, increase of operational capacities in sea transport, ensuring a stable position and a dynamic increase in the air transport market and encouraging combined transport options and developing an information society' has been a government priority. The transport and telecommunications sector made up 10% of GDP in 2003 and 10.4% in 2004.

The National Transport Master Plan is currently with the Council of Ministers for approval. This plan, along with the transport sector strategy, will provide the umbrella for future actions. Commercialisation of transport services is a clear government strategy.

Road transport In the past year, 100 km of national roads were constructed, 373 km were rehabilitated and 730 km maintained. The priorities for road transport are the rehabilitation and construction of the national roads network, the development of a maintenance system for road infrastructure and improvements in traffic safety. The implementation of a functional maintenance system began in 2004, which will reduce accidents and travel costs. A \$30 million World Bank loan (2002-2007) is being used for the maintenance of 1000 km of national roads (a responsibility of the central government) and 1000 km of rural roads (a responsibility of local governments). During 2004, 24 contracts for national roads and 18 contracts for rural roads worth \$21 million were signed with private contractors for routine and winter maintenance.

Railway transport Following an agreement with the Government of Montenegro to open the rail link between the 2 countries, around 57,400 tonnes of goods were transported in 2004 up from 16,900 tonnes in 2003. The total cost for the rehabilitation of the 36 km long rail line to Montenegro was Lek 383 million and was completed in 2004. A feasibility study has shown that a rail link to Macedonia, initially for transporting goods, should prove economically viable. 3km of railway will need to be constructed to complete the link at an estimated cost of €5-6 million to be co-financed by the governments of Italy and Albania. This conclusion is not in agreement with the National Transport Master Plan, which recommends closing the line between Lin and Pogradec.

Maritime transport The priority has been to rehabilitate and increase the operating capacity of sea ports and to increase the commercial nature of activities and services provided.

Table 4.4 Maritime transport indicators

Port	Number of ships processed		Processing capacity (in thousand tonnes)		Volume loaded and unloaded (in thousand tonnes)	
	2002	2004	2002	2004	2002	2004
Durres	1098	1274	3320	3500	2181	2960
Vlora	365	240	500	500	504	301
Saranda	46	81	60	108	82	73
Shengjin	223	192	350	400	347	293
Total	1732	1787	4230	4508	3114	3627

The most positive development was the completion of the rehabilitation of the port of Durres, after a \$23 million project that led to increased capacity and security. Studies for the improvement of the port of Vlora have been completed. A reason for the reduction in the use of the port of Vlora was the reduced need to import construction materials. There was continued implementation of the 1999 plan for the ports of Saranda and Shengjin. The privatisation of the Durres Port Authority has led to improved services and volumes. Operations that have been privatised include loading and unloading, piloting, shipping agents services and cleaning.

The Maritime Code has been approved by the Council of Ministers and the parliamentary commissions. There has been progress in aligning Albanian legislation with a wide range of international conventions and laws. This will facilitate international movement of Albanian owned ships. The Albanian Maritime Authority, which will ensure better management of port infrastructure, has not yet been established. This is planned for 2006

Air transport The government priority has been the rehabilitation and increase in the operating capacity of the national airport and the modernisation of air traffic control. In 2004 there has been an increase in passengers, flights, and flyovers.

Table 4.5 Air transport indicators

	2004	Growth relative to 2003 (%)
Passengers	649,750	15.7
Flights	6,757	16.3
Flyovers	90,655	11.5

Security standards have improved at Mother Theresa Airport. The National Air Traffic Agency has completed the first phase of a 4-year project for improvement of air traffic control. In November 2004 the concession for Mother Theresa Airport in Tirana was signed with the German-American consortium 'Tirana Airport Partners', which grants exclusive transport rights for international goods and passengers into Albania. The consortium will provide an investment of €82 million over 20 years, which will be the basis for service improvements and increased security. These will include construction of the new passenger terminal with a capacity up to 3 million passengers per year, enlargement of the landing/take-off runway, completion of the perimeteric fencing, provision of operating equipment and increased capacity for security.

The Air Traffic Master Plan prepared by the Directorate of Civil Aviation has been completed and is waiting approval from the Council of Ministers. Its recommendations include an increase in the number of airports for passengers and air freight. These recommendations are not in agreement with the draft National Transport Master Plan, which concluded that, because distances are very short, internal air transport in Albania is a non-economic option (except that the private sector might have an interest in developing some services e.g. charter services, helicopter services). In 2004 \$18 million was spent on the construction of Kukes Airport. This will be completed in 2005.

Telecommunications The government strategy has been to introduce competition into the telecommunications sector and to implement the European Union framework for electronic communications. In 2004 there was an increase in subscribers and geographical coverage. The mobile phone network now covers 74% of Albania and 87% of the population. 39% of the population have mobile phones (up from 32% in 2003) compared to 7.5% with fixed line telephones (no real change since 2003). There are over 55 operators providing services including internet access, prepaid cards, and data transmission. The number of internet users now exceeds 40,000 (up from 30,000 in 2003).

Table 4.6 Telecommunications sector indicators

	2004	Growth relative to 2003 (%)
Fixed line subscribers	265,000	7

Public telephones	320,000	15
Mobile line subscribers	1,283,000	16

In 2004 the National Telecommunications Regulator ruled that the interconnection agreements between Albtelekom and the 2 mobile telephone operators AMC and Vodafone Albania are partly invalid. As a result, in line with government strategy of liberalisation, the government removed Albtelekom's exclusivity in offering international calls. However the current regulatory framework prevents the licensing of additional operators to provide national and international phone services and the licensing of agents to provide fixed line services in urban areas. Terms of reference have been drawn up for consultancy support in preparing policies and a regulatory framework for the telecommunication sector in line with the European Union directives of 2002.

The Regulator also declared that AMC and Vodafone are very powerful operators in the market. Greater market choice was provided by the approval of the license for a third mobile phone operator, Eagle Mobile, which is owned 100% by Albtelekom.

Postal services The number of post offices increased from 565 in 2003 to 613 in 2004. There are now 11 licensed postal operators, 2 more than last year. The volume of mail delivered went up from 5 million to 5.9 million pieces. The objective is to achieve full liberalisation of the postal service by 2009. In 2004 the government passed an amendment to the law 'On postal services in the Republic of Albania'. However, while a decision was taken in August 2003 to establish a Postal Regulatory Authority, this has not yet happened.

Water and sanitation

The Water Supply and Wastewater Strategy (2003) set out to tackle 2 problems: intermittent water supply and poor water quality. 'Inadequate maintenance and repair, and lack of metering and operational control, have resulted in excessive water losses, estimated to be greater than 43% of water production in all cities' (p.9). Decentralisation and the development of private sector management should ultimately improve the technical and financial situation. In 2004, the average piped water supply to the population was 14 hours a day, an increase of 3 hours from 2003. The number of clients for piped water reached 24,000 in 2004 up from 11,000 in 2003.

Network infrastructure and management In 2003, 90% of the water utilities were being subsidised by the government mainly through arrears with government institutions and state enterprises. In 2004, the budget provided Lek 1.7 billion of operational subsidies and donor and government combined provision of investment grants and loans to water utilities were worth \$48 million. Transparency has been improved with implementation of criteria for eligibility for support to water utilities. The goal is to phase out state subsidies for operation and maintenance in the 4 cities in the Municipal Water and Wastewater Project by 2007. There is ongoing development of management and technical capacity for staff in water utilities and in the 2 ministries which needs to continue.

Households which are listed for social assistance qualify for water allowance, once a meter has been installed. Water utilities are provided with lists by local government. In the 4 districts participating in the pilot project this allowance has been set at 20 litres per capita. Water meters are being installed (supported by donor funds). In 2004, 1600 were installed in private enterprises, 500 in public institutions and 12,500 in households. There is 90% coverage in Korca, Kucove and Kruja districts and 60% coverage in a range of cities including Tirana, Kavaja, Saranda, Vlora, Fier, and Burrel. At the same time computerized billing systems are being introduced. Water metering accompanied by public information campaigns helps to increase payments.

To date only one private concession contract for water and sanitation has been awarded (in Elbasan). This contract includes special tariffs for 1300 households that receive social assistance. In 2003, 2 management contracts have been let to private operators, the first for Kavaja and the second for 4 cities (Durrës, Fier, Lezha and Saranda).

Water quality While Albania has adopted international standards for water quality, these are proving very difficult to attain given the aging infrastructure, lack of wastewater treatment facilities, and lack of technical expertise and equipment. Inspection of water quality through the Sanitation Inspectorate is a responsibility of the Ministry of Health. Offices throughout the country are responsible for monitoring water quality and they report to local authorities. The Ministry of Environment is responsible for the quality of wastewater and sewerage.

Decentralisation In 2004 the Council of Ministers approved guidelines on the transfer of water and sewerage system property to local government. Of the 54 water utilities, 8 were transferred to local government, inclusive of 131 systems of water supply. In order for transfers to occur, water utility obligations (mainly to KESH) need to be settled by central government. It is too early to identify benefits from these transfers. The governance arrangements of the water utilities will not change for 2 years; then the local government can determine whether privatisation occurs and what form it takes. To speed up the process of transfer of water utilities, an action plan has been prepared between the Ministry Territorial Adjustment and Tourism, the Ministry of Economy and the Ministry of Finance.

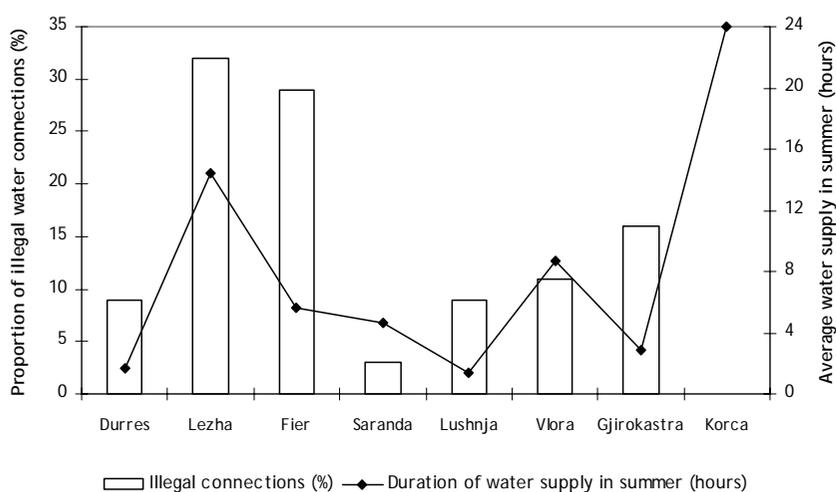
Decentralisation and water sector reforms: a poverty and social impact analysis

Based on the decentralisation law and the water supply and wastewater strategy, the government has initiated reforms, which involve:

- Transferring powers from the central to the local government, including responsibilities for investment, operational decision-making and tariff-setting; and
- Clarifying the financial situation of each water utility to facilitate their transformation into corporations that will ensure their financial sustainability.

There remain key constraints for the transfer of utilities to local government, such as their debts to KESH, the limited ability of local government to generate investment funds from sources other than the block grant, and weak administrative and technical capacities.

The Municipal Water and Wastewater Project is helping to accelerate the pace of reform in 4 towns by financing the costs of a management contract awarded to a private operator to improve incentives for service delivery and serve as a positive example. In these 4 target towns, local government authorities have been supported by institutional changes and an investment fund. The towns are characterised by high rates of internal migration and large unplanned settlements that put additional pressure on already poorly maintained supply networks: the number of illegal connections has increased with the result that the quality of service, in terms of duration of supply, quality and pressure, has deteriorated.



The World Bank and the United Nations Development Programme sponsored an analysis of the likely poverty and social impact of this reform. The study aimed to compare the 4 target towns with 4 other towns that follow the traditional model of public management. The survey team interviewed key informants in central and local government, organised focus group discussions with representative groups of customers and surveyed about 700 households during 2002-2003. The study had 3 objectives:

1. Set baselines to assess consumer perceptions of water service delivery and measure the distributional impacts of reform on the well being of the urban poor with respect to access to water and wastewater services and likely tariff increases.
2. Identify the main institutional issues of the reform.
3. Provide recommendations for sustaining the pace of reform, while mitigating negative impacts on vulnerable social groups.

Some of the key findings are the following:

- Poor households, which have settled in city fringes and new settlements, are less likely to be paying for water services. They face shorter water supply by up to 4 days per month compared to non-poor households. They are also more likely to establish illegal connections, travel to get water and dig wells in their yards. At the same time, they are less likely to use some of the other coping mechanisms, such as purchasing water tanks, water pumps, or water from vendors. Instead they use buckets or basins to store water.
- A proposed solution is the introduction of a lifeline service that will provide 20 litres per person every day for free. Although respondents have been broadly supportive, they are also aware of 2 drawbacks:
 1. The measure depends on meter installation but its cost is prohibitive for poor families;
 2. Existing mechanisms to identify poor households are not well developed
- On the other hand, the current flat rate billing system needs to be discontinued if water abuses are to be controlled and operational and management costs to be covered.
- Insufficient provision of information accounts for ambiguities and tensions among stakeholders. Despite the presence of several institutional tools, local government authorities are not yet exercising the new rights and competencies assigned by law.

Source: Decentralization and water sector privatization in Albania, World Bank and UNDP, December 2004

Rural water strategy In 2004 the Rural Water and Sanitation Agency was established as a part of the General Directorate of Water and Sanitation to support the formation of community water associations for water supply. In future this agency will become independent though retaining a close liaison with the Directorate. It will establish 6 branches which will examine applications from community water associations for funds and assistance.

Water reserves The National Strategy for Water Resources was updated in 2004. This resolved conflicts inherent in the earlier strategy (1996) and clarified competencies for different levels of government and different government agencies.

Urban development

Sustainability in urban development is the long term objective of the government. In the medium term, the main priorities are halting the process of urban degradation, reducing urban poverty and creating conditions for long term urban development.

High-growth urban areas In 2004 urban planning activities intensified. City limits were expanded to include areas settled informally by internal migrants. In 2002 an order was passed enforcing the 14 largest cities to prepare urban plans. By the end of 2004, 4 plans have been completed, and 12 cities have completed a plan for their inner-city area. In 2004 the law 'On legitimisation of informal areas' was passed and an agency established for its implementation. This law enables these areas to be treated as urban zones for provision of infrastructure and services.

Urban land management The resolution of land ownership continues to be a high priority and a difficult issue. Urban land development is stalled through conflicts over compensation for owners from pre-communist times. Registration of public properties is not completed, whereas registration of private property in accordance with the standards set by the Immovable Property Registration Project has been completed in 90% of rural areas but only 10-15% of urban areas.

Immovable Property Registration System

The NSSD plan to achieve growth relies on enhancing the country's market institutions. Increased property right security, especially related to land, was considered a priority measure. This was an issue that was brought up during the original consultations by the Business Consultative Council. Since the mid-1990s, Albania has opted for a modern Immovable Property Registration System to resolve ambiguities over land ownership rights and establish a functional land market. However, despite the fact that almost 90% of properties in rural areas have been registered, the respective proportion in urban areas is only 10-15%. There appears to be an increasing trend for land transactions to be conducted outside the Registration Offices.

A recent report by an expert involved in setting up the Immovable Property Registration System has reviewed the reasons for the limited effectiveness of the system. The staff in Registration Offices has not been trained sufficiently to develop a professional attitude in their interactions with citizens. The procedures for using and updating the digital database are largely ignored. The costs for individuals to register their property, which includes but is not limited to the transaction tax, are too high. Some of the key principles upon which the system is based are no longer manifest. The kartelas (property registers) are not reliable sources of information about ownership and interested individuals need to take extra steps for verification.

If the confidence of the public has been eroded, radical steps may be necessary. These would involve transferring the responsibility for the registration functions to institutions with an intrinsic interest in the preservation of the system. Local government officials or private registration offices are mentioned as examples to be considered.

Source: J. David Stanfield, The creation of an Immovable Property Registration System in Albania, Symposium on land administration in post conflict areas, Commission 7 of the International Federation of Surveyors and UN-Habitat, April 2004

Urban waste The plans to establish 3 landfills in Lezha, Durres and Tirana have not yet been completed. The landfill in Lezha, started in August 2000 with Italian funds, ran into technical difficulties requiring additional funding. These have not yet been resolved with the donor. The negotiations for concessionary agreements in Durres and Tirana, which began in 1997, have not been finalised by the government due to lack of direct funds and a sustainable funding arrangement. A feasibility study is being conducted in Korca and Vlora for landfills. An agreement has been signed with the Government of Italy for the management of urban waste in Tirana. The idea to impose taxes for managing urban waste is proving difficult due to economic and social conditions. The Government of Albania is committed to a progressive integration of environmental policies to European standards and to adopting the principle 'who pollutes pays'.

Housing The National Housing Strategy (2001) proposes legal, financial and administrative measures to address the following priorities:

- Support the poor to ensure access to adequate housing through housing programmes. In 2004 the law 'On social programmes for the housing of city dwellers' was passed. These programmes include: controlled social rental housing programmes and - in special cases - rent subsidies, low cost housing programme (through cost control and credit), and sales of land with necessary infrastructure to municipalities for the implementation of social housing programmes.
- Develop financial mechanisms (credit for low-income families, private and institutional savings mobilisation, community savings schemes, credit mechanisms for joint ownership associations etc.) and public-private partnerships to expand access to housing. No credit line has yet been established, although the foundations were set for a pilot project that will be

implemented in 2005 to test alternatives to policy implementation without drawing down on central or local government budget by using credit lines with banks.

- Support urban renewal and building maintenance

4.4 HUMAN RESOURCES

Education

The NSSED gives priority to reforms and increased financing for the education sector. The strategy aims to (i) increase the participation of the population in education, particularly the poor and those living in remote areas; (ii) improve quality; and (iii) adjust the education system to the labour market's requirements. In 2003, public expenditure in education sector was Lek 21.237 billion, equivalent to 10% of total budget or 2.9% of GDP. In 2004, education expenditure increased to Lek 25.281 billion in 2004, equivalent to 10.7% of total budget or 2.8% of GDP.

Table 4.7 Average cost per student in 2004, in Lek

	Primary education	General secondary education	Vocational secondary education	Tertiary education
Cost per student	28000	25000	54000	81000

For 2005, the budget per general secondary school student is Lek 29,000, while for vocational education the budget is Lek 69,000 per student, excluding the technical equipment and furniture required provided by donor investment and the publishing costs of new textbooks.

Administrative and financial reform The Ministry of Education and Science is strengthening its organisational structure at the regional and district level. In 2004, 12 Regional Education Departments were established by the Ministry of Education with the responsibility to monitor education standards and inspect schools. A new inspection system was introduced to allow for quality assessment. The EMIS system is being used for improved communication with the districts and specifications for data inputs have been designed. The policy paper for decentralisation of functions in education was approved by the Council of Ministers. Capital expenditure for pre-tertiary education was given as an unconditional grant to the Tirana Municipality in 2004. This is being extended to all local government in 2005. Printing of school textbooks went to competitive tender in 2004. All education salaries were increased by 3.4%. Pre-tertiary teachers received an additional 8% and university staff received additional increases of between 30-70% which has widened the gap in salary levels. The Institute of Pedagogical Studies was divided into 2 semi autonomous agencies to improve their functioning: the Institute of Curricula and Standards and the Centre for Training and Qualification in Education. In the framework of the Bologna Declaration, a new curriculum framework to bring about the gradual integration of the national education system with education systems in Europe and the region was launched in 2004.

Distribution of resources across schools

Schools are not financially autonomous. They have neither a budget nor any money to fund even minor expenses. Instead, they receive resources in the following way:

- Salaries are funded out of the Ministry of Education and Science budget and transferred to the municipalities and communes through Regional Education Departments (conditional grant);
- Supplies and teaching materials are funded by the Ministry of Education and Science budget and transferred to Regional Education Departments. Inputs are distributed in kind to schools based on their demands at the beginning of and during the school year (conditional grant);
- Operation and maintenance expenses, as well as small repairs are directly funded by municipalities and communes (unconditional block grant - plus local resources, if any);
- Investments (construction, rehabilitation and equipment) are funded by the Ministry of Education and Science budget. The procurement is carried out by the District Education Office if the amount is less than Lek 10 million; otherwise it is done by the Ministry.

A study by the Ministry of Education and Science assessed the level of resources that are available to schools. It found that there were 2 types of inequality in the distribution.

First, there are disparities in the distribution of supplies and teaching materials across basic schools. While schools in the bottom fifth received on average Lek 20 per pupil per year, schools in the top fifth received more than Lek 5,000. The pattern was the same in 2002 and 2003.

Second, there are differences in the share of the unconditional grant allocated to education. The unconditional grant is not earmarked for education and municipalities and communes are expected to finance other public services from it as well. While municipalities and communes received roughly the same average amount in terms of block grant per capita, municipalities spent a much higher share of the grant for education (23%) compared to communes (13%).

While this is partly expected given the higher numbers of enrolled students in urban areas, it is interesting that there are big differences in terms of the share of the block grant allocated to education within municipalities and within communes. The bottom fifth of local government units spent as low as 5% of its grant on education, while the top fifth spent 31%. It is difficult to explain why such differences are observed. However, one finding was that the level of block grant per student in municipalities explains partly the share of the block grant allocated to education. This suggests that education expenditure is partly determined by the available resources, not only by need.

The study concludes that, while decentralisation is certainly needed, it should be accompanied by funding mechanisms promoting equity and efficiency. The study also recognises that improving the efficiency and equity of the financing mechanisms requires quick progress in the Education Management Information System. Information on personnel, salaries, as well as operation and maintenance expenses should be reported to the Ministry in order for it to be able to assess the financing mechanisms and guarantee equity.

Source: Ministry of Education and Science, Public expenditure tracking survey, October 2004

Pre-tertiary education The National Education Strategy for Pre-Tertiary Education was developed in 2004 with the recognition that reforming the education system was central to the achievement of economic and social growth. The strategy identifies 4 priority areas for the development of pre-tertiary education: governance and management of education, quality of teaching and learning, financing of education and capacity development. The strategy includes an action plan which will be integrated into the medium-term budget plan.

Currently, the average Albanian child is expected to spend 7.5 years less in school than the OECD average. Multiple factors account for children leaving or not enrolling in school including: poverty (families needing children to work), lack of public security, blood-feuds, poor teaching quality, low quality of school buildings, lack of value placed on education and lack of enforcement by local authorities. A broad range of initiatives are being taken to improve the quality of services and to increase enrolment rates for minority and socially excluded groups. Compulsory education was extended from 8 to 9 years for new enrolments in 2004. Some smaller schools have been merged with larger schools. Across the country free textbooks were provided to primary schools (and to the secondary schools of 80 poor communes) and additional scholarships were awarded. The Regional Education Departments and District Education Offices are required to report every 6 months on efforts to attract Roma students to school. A psychological service has been initiated by the Ministry of Education for school age children, whether or not they are attending school. Late in 2004, the project 'Second Chance' was initiated, which focuses on re-enrolling students who have dropped out. However, despite best efforts, enforcement of sanctions for non-attendance at schools is proving difficult.

Teacher training Out of 36,000 teachers in pre-tertiary education, there are 8,000 teachers without tertiary education qualification. Of these, 5,246 are employed in compulsory education. Since 2002-03, a part-time year-long training programme was held for 1,470 of these teachers in 10 districts. Of these, 980 received a certificate, making them eligible for permanent appointment and giving them entry level 2 in 2003-04. Unfortunately, the reorganisation of the Regional Education Departments and District Education Offices caused suspension of the programme. The plan is to continue it in future. An improvement in teaching standards and motivation has been observed of those teachers on the programme.

Effects of qualifications on school performance

According to the NSSD, the high share of teachers without university qualifications in basic education is a concern. The Institute of Pedagogical Studies has been designing training programmes that focus on unqualified teachers. The assumption is usually made that teachers without university education will have a negative impact on student learning achievement.

A study by the Ministry of Education and Science ¹ has examined whether this assumption is correct combining 3 sources of information. First, school performance data were available from the results of the Grade 8 national assessment in mathematics and language, which was coordinated in 2003 by the Centre for Educational Assessment and Examinations. Second, administrative data from the Ministry of Education and Science were used to obtain a measure of the average teacher qualifications in each school. The table below shows that a large proportion of teachers do not possess the desired academic qualification. This is particularly true in rural areas, where migration has caused a shortage of qualified teachers. Third, data from the Census and the poverty mapping exercise by INSTAT ² were collected to capture basic socioeconomic characteristics from the areas where the schools were located.

	Urban	Rural
School performance		
Average Grade 8 exam score in language [maximum = 100]	58.1	48.8
Average Grade 8 exam score in mathematics [maximum = 50]	26.5	23.4
Teacher education		
Proportion of teachers with secondary school education (%)	6.2	11.0
Proportion of teachers with pedagogical secondary school education (%)	17.7	33.3
Proportion of teachers with university education (%)	76.1	55.7
Teacher age		
Average age of teachers (years)	42.1	40.4
Socio-economic conditions		
Proportion of poor households in municipality / commune (%)	18.6	37.5
Education conditions		
School years attained by women aged 30-55 in municipality / commune	10.9	8.5

The results showed that school performance in Grade 8 examinations was negatively related to the proportion of teachers in the school that only possessed secondary education qualifications. This result was stronger in the language subject and in rural areas. On the contrary, the proportion of teachers with pedagogical secondary education qualifications did not affect school performance negatively. In the case of mathematics results in rural areas, the effect was even positive. This suggests that, among teachers without a university degree, training activities should focus on those teachers who do not have a pedagogical secondary education certificate.

At the outset, the study intended to evaluate the effect of the teacher training programme on school performance. However, the Ministry does not record the teachers who receive training. One of the study's recommendations is to keep a database at the central level that will allow an evaluation of the programme. In addition, the study recommends that the Ministry and INSTAT agree on a common identification number for schools to facilitate merging existing data sets.

Sources: ¹ Ministry of Education and Science, Policy impact analysis: Impact of teachers' qualifications on student performance; ² INSTAT (2004) Poverty and inequality mapping in Albania

Secondary vocational education During 2004 there was growing student motivation to enrol in vocational education. The number of students enrolled grew from 20,333 in 2002-03 to 21,909 in 2004. The vocational schools sometimes operate in excess of full capacity. The vocational education budget for capital investments has been increased in 2005. The labour market is increasingly demanding students coming from vocational schools (mainly plumbers, mechanics and tourism professions). The Ministry of Education have delegated the budget to a number of vocation schools. The practice has shown that these schools are more effective than ones managed by the local government. The most important development was the decision to establish the Vocational Education Agency in 2005 to increase the system's responsiveness to labour market needs. This will establish a framework of professions, improve curricula, and provide equipment and furniture for 4 schools and 4 centres for vocational training. The main constraints for decentralisation are the lack of capacity to support vocational education.

Higher education and scientific research The strategy aims to increase the autonomy of universities, improve the quality of teaching, align qualifications with European standards and increase the level of research. The budget for universities is 17.6% of the total education budget (0.6% for research). In 2004 there was an increase in financial autonomy for universities. However, this is restricted by the current organic budget law. A new funding formula was introduced to reduce disparities in funding between universities based on the disciplines offered and the professional qualifications that can be obtained. The research budget was allocated based on research projects being conducted by universities. The curricula for new entrants in 2005 have been revised.

Health

In the NSSD health has been identified as a priority sector since 2001. The target was for public expenditure in health to increase from 3% of GDP in 2001 to 3.2% by 2004. In 2003, public expenditure in the health sector was Lek 15.699 billion, equivalent to 7.8% of total budget or 2.11% of GDP. In 2004, public expenditure in the health sector increased to Lek 19.507 billion, equivalent to 8.67% of total budget or 2.31% of GDP.

The key plans and strategies for the sector are the Mental Health Policy (2003), the Strategy for Public Health Promotion (2003), the National Strategy for Integrated Management of Childhood Diseases (2003), the National Strategy for Prevention and Fight against HIV-AIDS (2004), the Long Term Strategy for the Development of the Albanian Health System (2004), and the Health Insurance Institute Plan (2004).

The Law 'On health services financing through health insurance' has been submitted for approval to the Council of Ministers and should be passed in 2005. Its objectives include: (i) the increase in effectiveness and efficiency in the use of resources; (ii) the increase in the access to and equality in health services nationwide; and (iii) the improvement of health indicators through interventions in specific areas.

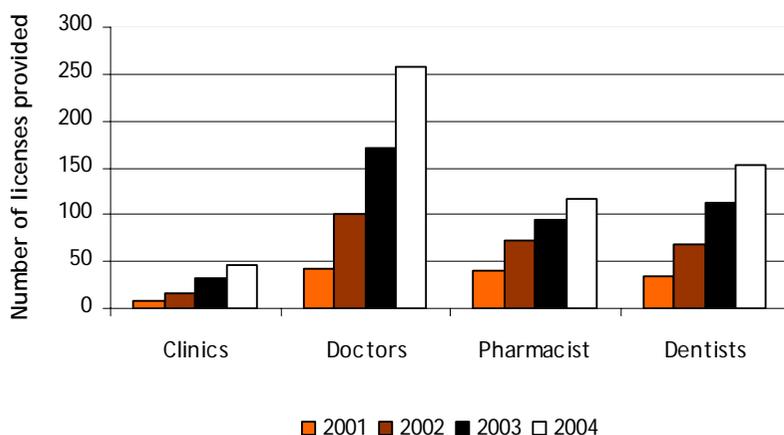
Planning, resource distribution and monitoring A criticism made of health service budgets is that allocations of resources have not been linked to need or to outputs. In 2004 the Ministry of Health developed a medium term budget plan for 2005-2007, which was then used to prepare the annual budget. A national health information system for human resources was established in 2004 which has already been used for appointments and as part of a training needs analysis. Studies are being completed in primary health care units and hospitals, which will provide information for future budgeting. The Ministry of Health centralised procurement of goods and services in 2004 which resulted in lower costs and greater efficiency.

Governance Informal fees to health service providers reinforce inequality and reduce access to health care. With poor working conditions including low pay, the health sector has lost a large number of personnel. The informal charging of fees by health service providers is supported by

patients desperate to receive a service and in some cases wanting access to medicines that are not available on the national drugs list. A number of measures have been implemented, which should reduce corruption. In the past year the Ministry has increased health service provider salaries by 12% and is giving 70% of additional revenues collected (from non-insured patients) to health personnel in the form of bonuses or direct remuneration. The remaining 30% is retained by the institution (equally split for capital investment and operational services).

Private sector regulation The private sector has expanded rapidly. Figure 4.5 shows new licenses issued between 2001-2004 for medical clinics, doctors, pharmacists and dentists. Regulation to ensure consumer protection is now being developed. A joint order was issued in 2004 by the Ministry of Health and the Ministry of Finance obliging private practitioners to produce their licence when registering for tax purposes. New rules and regulations have been written for diagnostic laboratories, which govern their function and set service standards. A new law 'On medicines and pharmaceutical services' requires pharmacists to gain a license which will last 5-10 years. The Ministry of Health is responsible for inspections.

Figure 4.5 Licenses provided to private sector health providers



Access to health services Primary health care is delivered through an extensive network of urban and rural health centres, which provide basic health care including preventative programmes. Infrastructural development in 2004 witnessed the completion of the construction of the network of health centres. In total, approximately 640 health centres give total coverage. While 171 new outpatient clinics were built, the network (which now has approximately 900 outpatient clinics) is only 50% completed.

Table 4.8 New and reconstructed health centres and outpatient clinics

	Number of facilities	Cost in million Lek
New health centres	21	66.4
New outpatient clinics	171	217.2
Reconstructed health centres and outpatient clinics	45	63.2
Total	237	346.8

There has been an increase in the number of patient contacts with the doctor at the health clinic and outpatient clinics. Information on whether this is proving a substitute for a visit to a

hospital, which patients have historically preferred to visit, is collected by the Living Standard Measurement Survey.

A needs' assessment followed by relocation or hiring of general practitioners has led the number of communes not covered by doctors to be reduced from 16 to 9 and an increase of general practitioners contracted to the Ministry of Health from 1567 in 2003 to 1593 in 2004. Incentives for working in remote and rural areas are being applied.

Albania has a ratio of 3.1 beds per 1000 inhabitants, one of the lowest in Europe. Bed occupancy in 2002 was 50.5% (the European average is 77%). Many Albanians who can afford to do so seek treatment abroad. Of the total health budget, 60% was spent on hospitals in 2004, down from 65% in 2003. With the objective of improving hospital performance, 6 hospitals are measuring performance indicators as part of a pilot project initiated by the World Health Organisation in 2002. This project will be evaluated at the end of 2005 and if successful, extended nationwide. For the 6 pilot hospitals, treatment protocols have been drafted which are aimed at improving treatment and hospital management.

Pharmaceuticals The national pharmaceutical policy is to provide safe and effective drugs at affordable prices. Pharmaceutical services are privatised and supply the market with a variety of drugs. However, there are problems with quality control, medicines labelled in foreign languages, abuse of drug pricing, lack of qualified pharmacists. In 2004, the law 'On medicines and pharmaceutical services' was passed in line with EU standards. It specifies that all pharmacies must be licensed and medicines provided by a technical manager or qualified pharmacist. To reduce the level of contraband medicines and improve safety, medicines will from 2005 have to be labelled in Albanian with the retail price indicated.

The National Centre for Pharmaceutical Control was reorganised with 2 new divisions, a division that distributes information on medicine through the pharmaceutical network (for example, whether they are imported, locally produced, registered or not) and a division responsible for registration of the effects and side effects of available medicines. The centralisation of procurement has allowed greater control over purchasing contracts and distribution.

Improving health indicators through specific interventions The Long Term Strategy for the Development of the Albanian Health System identifies the public health challenges as: cardiovascular diseases and cancer; traffic accidents; social and domestic violence; mental illness; and communicable diseases. The NSSED objective is to achieve 90-100% immunisation rates for vaccine preventable diseases in children and to ensure safe drinking water and foodstuffs. Contagious diseases are a concern, especially for poor and marginalised groups.

The government has achieved 95% immunisation rates for basic EPI antigens. The total cost of the immunisation programme is \$4.6 million with 90% funded by the government and 10% by UNICEF and GAVI. The National Programme for Tuberculosis control continues to implement the DOTS programme. The incidence for TB since 2000 has been 20-22 for 100,000 inhabitants. Plans for surveillance of meningitis and German measles are being introduced. Challenges in achieving coverage include difficulties in managing the supply chain at the local level and keeping track of a migrating population.

The National Strategy for Prevention and Fight against HIV-AIDS and its action plan was approved by the government in 2004. Antiretroviral medicines were supplied for the first time with the support of UNICEF. The Institute of Public Health now has diagnostic capacity and an action plan for establishing counselling centres and for promoting voluntary testing. An awareness campaign was conducted in schools. Sentinel surveillance is being used to identify problems among high-risk and marginalised groups.

Albania has a surveillance system for communicable disease (ALERT). Reported incidence of diarrhoeal diseases fell in 2004 from 1875 to 1722 per 100,000 inhabitants. Incidence

appears to be correlated with areas that have potable water. While surveillance can be further improved, causal factors need to be addressed.

Infant mortality In 2003 the National Strategy for Integrated Management of Childhood Diseases was developed. In 2004 pilot projects were initiated in 8 districts. Early evaluation of the pilot projects indicates improvement in diagnosing, treating and following up children by medical personnel as well as improved home care by parents. This suggests that a strategy for reducing infant mortality will follow a multi-pronged approach including training of health personnel, referral, health and nutrition education for families and the wider community. There are difficulties achieving coordination amongst the various stakeholders in the field.

Drugs, alcohol and tobacco While there is a shortage of quantitative data, it appears that smoking, drug and alcohol abuse are increasing in Albania especially among young people. In June 2004 the government signed the Convention on Tobacco Control. Draft anti-smoking legislation has been prepared and is with the Council of Ministers. The institutional structure for prevention and treatment of drug addiction is weak. A national strategy against drugs was launched in 2004. The SOROS foundation is financing a community level programme for methadone treatment, which is not currently provided by the government.

Mental health With the objective of providing access to mental health services of an international standard across Albania, a national Mental Health Policy was developed in 2003. In 2004 an action plan for implementation of the policy was drafted. It will be important to create the institutional framework for delivery of this plan, as action plans currently being prepared for psychiatric hospitals include objectives for deinstitutionalisation of patients who will need community based mental health care. The 6 pilot mental health centres in 5 cities which use a multi-sectoral approach are being evaluated. Around 60 general practitioners have been trained in these cities. Monitoring to date suggests that there is a need to increase the number of community services, staff them appropriately, increase the number of reimbursable medicines for psychiatric illnesses and provide long term accommodation in sheltered care.

Health insurance The Health Insurance Institute covers just over 80% of the population. In 2004, 14% of the population is direct contributor and 69% is insured by the state. From 2003, the Health Insurance Institute is responsible for the employment of general practitioners. The Ministry of Health determines vacancies and carries out quality control, while the Regional Health Authorities are included on the selection panel. In 2004, the Health Insurance Institute began funding a selection of medical interventions in the 4 tertiary hospitals. There are 2 draft laws in the pipeline: 'On financing health services through the health insurance system' and 'On funding health insurance' which will allow the Health Insurance Institute to have contracts with health providers for delivering services to insured people. In 2003 the Health Insurance Institute started a voluntary contribution scheme targeted at Albanians who work abroad and come back into the country for short periods of time and at uninsured Albanians not covered by the state; 2000 people are contributing to this scheme.

Social policy

Labour market policy

The development of the labour market and the promotion of employment is a key component of the NSSD because unemployment is one of the main components of poverty. In the long term, employment levels should rise as a result of economic growth and development of the private sector. While unemployment continues to fall, this tends to be associated with the reduction in total workforce. In 2004, the long term unemployed made up 66% of the total compared to 68% in 2003. Unemployment is 17.5% among women and 12.4% among men. Unemployment is higher in urban areas; however under-employment in rural areas is reflected in

the high number of farming households receiving partial economic assistance from the state (71,882 in 2003 and 71,354 in 2004).

Vocational training An important objective of current social policy is to encourage increased employment through vocational training and professional development in line with market needs, improved employment services and taking measures to formalise the labour market as per the National Strategy on Employment and Vocational Training (2002).

Objectives have been set to target vocational training to the registered unemployed and minority groups. Vocational training is also offered to employed people where necessary to adapt to the changing labour market. In Albania, there is a shortage of institutions for vocational training. As part of the planned geographic expansion, 2 new centres for vocational training were constructed in Elbasan and Fier in 2004, co-financed by the public budget and the CARDS programme. A nationwide needs assessment for professional skills was conducted (in addition to information routinely collected at the local level) and work has started on improving the curricula for professional development and setting of standards for professional qualifications that will be accepted internationally.

Economic assistance

The provision of economic assistance continues to be essential for the poor in Albania. With the aim of increasing social protection and reducing social exclusion and inequality, the policy on economic assistance is being continuously updated to improve coverage, level of assistance and effectiveness. The total payments in 2004 remained at the same level as in 2003 (Lek 4 billion). The recommendations from the 'Assessment of the criteria and indicators for the distribution of economic assistance' have yet to be implemented. Abuse of economic assistance has been declining and targeting of the poor has been improving. In 2002, 133,000 families were recipients of economic assistance. The number of recipient families decreased to 125,000 in 2004 with 60% receiving partial assistance. Although beneficiaries mainly come from rural areas, recipients of full assistance tend to be the unemployed in urban areas. Half of all beneficiaries are found in the regions of Shkoder, Kukes, Diber and Elbasan. These regions between them receive 45% of the total resources. A draft law 'On assistance and social services' was prepared in 2004. This law supports poverty reduction by expanding the categories of people eligible for benefits or the size of the benefit for some groups who are already eligible, for example people with disabilities. As part of a pilot scheme aimed at assisting recipients of economic aid to return to employment, 16 public works projects were implemented in 3 municipalities and 2 communes where full time employment was provided at minimum salary to beneficiaries.

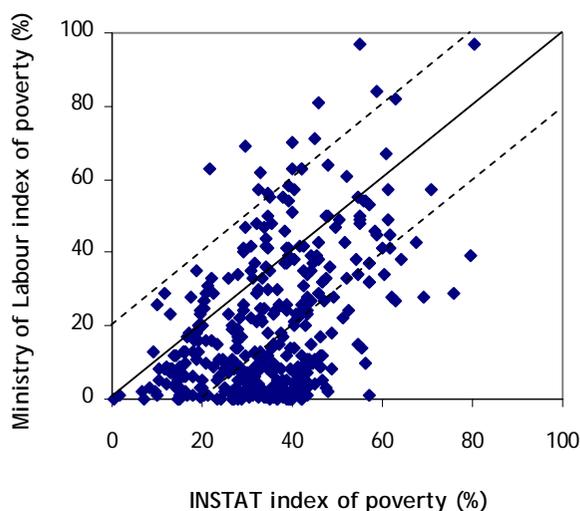
The distribution of economic assistance block grants to local government units

According to the NSSD, reassessing the mechanism for distributing economic assistance to improve targeting is a priority. Assistance is allocated in 2 stages. First, the central government allocates block grants to municipalities and communes. Second, these local government units distribute economic assistance to deserving families. A study by the Ministry of Labour and Social Affairs¹ has examined how well the first stage allocation is targeted.

In theory, the allocation of block grant funds is determined by a Council of Ministers decision dating from 1999 and is based on 8 indicators possibly related to local poverty conditions. However, no explicit formula links the indicators with the level of the grants. In addition, due to deficient data, the Council of Ministers decision is not implemented. In practice, the block grant calculation is based on requests and is therefore influenced strongly by previous allocations.

Since 2001, the government has been implementing a programme to collect socioeconomic data. Its cornerstones are the 2001 Census and the Living Standards Measurement Survey (LSMS). In 2004, INSTAT published a study² which ranks local government units by the extent of poverty. The INSTAT study first developed a model that predicted the level of household consumption using information from the 2002 LSMS. Then it projected the model on all the households in the country using the Census data. Although the INSTAT ranking is not definitive, it uses the richest sources of information and analyses them using an internationally accepted methodology.

The figure below compares the level of poverty by local government unit according to the State Social Services and the INSTAT poverty mapping study. Each municipality and commune is represented by a point. The poverty index used by the State Social Services is measured on the vertical axis, while the INSTAT index is measured on the horizontal axis. Although the 2 sources are positively related, there are many cases where the 2 measures diverge.



The study concludes that there is scope for a revision of the methodology used to calculate the level of block grants for economic assistance. The study also reveals that after large investments in the national statistical system, the use of data for policy should be improved.

Sources: ¹ Ministry of Labour and Social Affairs, Policy impact analysis: Distribution of economic assistance block grants; ² INSTAT (2004) Poverty and inequality mapping in Albania

Social services

According to the NSSED, a key to improving quality is the harmonisation of the services providing economic assistance with other social services. The NSSED has suggested that (i) residential care pass gradually onto community-based and mobile services; (ii) the range and location of services expand by need; (iii) participation of local government and civil society in the planning, funding and provision of social services increase; (iv) the sustainability, continuity and quality of services increase; and (v) participation of social business in financing and service provision be promoted.

The reform of the provision of social services continued in 2004 with the approval of the Law 'On assistance and social services' which provides for the decentralisation and modernisation of particular social services. These include: transferring residential care to local government; establishing new social services as determined by local government in properties transferred from the central government; and moving from residential care to community service or where not feasible, improving residential care. The establishment of a Social Fund will provide funding to support the decentralisation of social services. The development and application of general service standards is being piloted in 4 regional councils including specific standards for residential services for children for services for people with disabilities. The development of service standards will lead to the improvement of licensing of private providers.

Gender

There are 3 major areas of concern on the situation of women in Albania.

Equality One of the main achievements during last year was the approval of the law on 'Gender equality in the society' in July 2004, which sets the framework for equal rights of women and men. The law covers employment, education, decision-making processes, discrimination and sexual harassment. Staff from the Ministry of Education and the Ministry of Labour and Social Affairs has undergone gender mainstreaming training to increase the level of gender analysis in policy formulation.

Trafficking Combining data from a variety of sources, a recent report ¹ suggests that trafficking of women, mainly for sexual exploitation, continues. To improve the fight against trafficking, a law on 'Witness protection' was adopted by the government in March 2004. This law will contribute to the indictment and punishment of traffickers and will complement the existing body of legislation. In December 2004, the United Nations Development Fund for Women (UNIFEM), the Gender Alliance for Development Centre, and INSTAT initiated the project 'Creating economic opportunities for women in Albania: A strategy for prevention of trafficking', which will analyse the situation of women in Albania in relation to their economic rights and labour market status with an ultimate goal to create economic opportunities as a way to prevent trafficking. However, it is recognised ² that there are continuing weaknesses in preventing trafficking, enforcing legislation and rehabilitating victims.

Domestic violence In October 2004, different Albanian non-profit organisations formed an alliance to promote the Albanian legal framework against domestic violence. This initiative is focused on developing a draft law, organising public discussions and making representations to the decision-making institutions.

Sources: ¹ International Catholic Migration Commission, First Annual Report on Victims of Trafficking in South Eastern Europe, Country Report Albania, September 2003; ² National Human Development Report 2005

Social insurance

The strategy for social insurance continues to (i) aim for sustainability (reduce the dependency ratio from 1.04 beneficiaries per contributor in 2000 to 0.82 in 2020) (ii) increase the real level of benefits, (iii) increase contribution from people living in rural areas (iv) extend social insurance to cover people employed outside the country (v) reduce evasion.

In 2004 in order to reduce the evasion of social insurance contributions, responsibility for collection of contributions was partially transferred to the General Directorate of Taxation and this will be completed in 2005.

During 2004, the revenues from the voluntary social insurance scheme were 70% of those forecasted. In 2005, all necessary organisational measures will be taken for the publication and inclusion in the voluntary insurance scheme of all persons that are not included in the compulsory insurance scheme.

The level of contributions has continued to increase: there has been a 36% increase from 2002 to 2004. The biggest increase was from those self-employed in agriculture. Further improvements will be achieved through public awareness campaigns and targeting by the Social Insurance Institute. Employment promotion policies and increased control over the informal labour market have also increased the number of contributors. The ratio of the social insurance scheme deficit to GDP reduced from 0.28% in 2003 to 0.26% in 2004.

In order to increase the number of contributors, the government reduced the contribution rate of businesses from 42.5% to 38.5%. The implementation of the Law 'On exoneration of penalties for delays to social insurance' which was passed in 2003 led to a reduction in debts to the social insurance scheme from Lek 1.8 billion in 2003 to Lek 0.4 billion.

Revenues from contributions increased 10.2% in 2004 (Lek 3 billion) compared with 2003, which improved the dependency coefficient for the urban pension scheme. However, this was below target due to teething problems in the transfer for collection responsibility to the General Directorate of Taxation.

Table 4.9 Number of compulsory and voluntary contributors to social insurance

	2002	2003	2004
Urban	342,438	342,374	358,295
Rural	126,559	261,462	280,500
Total	468,997	603,836	638,795

The subsidy from the public budget to the pension fund in 2004 was Lek 964 million, a decrease of 52.3% compared to 2003.

Increased expenditure in 2004 included: an increase in the number of pensioners by 1700; funding the policy to increase and equalise urban and rural pension with an 8% increase for urban pensioners and a 15% increase for rural pensioners and equalisation measures for those that are operating under different laws dependent on year of retirement.

4.5 NATURAL RESOURCES

The government priorities are: sustainable management of natural resources, through rebuilding and enhancing local government structures for environmental management, control of illegal

harvesting operations, transferring of forest and pasture areas to the communes either in ownership or utility title; completion of legal framework on management, and finding ways for common state-community management of forest and pasture areas, especially for long-term lease of pastures; land protection from erosion through trees planting and mountain barrages; enforcement and extension of national and regional environmental and fishing organisations.

Strengthening of natural resource management at local level The registration process of forest and pasture areas at local government units was finalised in 2004. The valleys of Mat, Dibra, and the Liqenas commune in Korça, have been transferred under the authority of local government, and a big interest of the community on forests and their protection has been noticed, resulting in a better development of forest area during recent years. The Strategy of Forest and Pasture Areas Development and Institutional Reform and the law 'On forests' were approved in 2004.

Enhancement of structures of natural resources management In order to reduce land erosion, 180 ha of land, mainly in degraded area most affected from erosion, have been forested in 2004: 50 ha in Gramsh, 20 ha in Korça, 15 ha in Puka, in total 460,000 saplings. About 800 metres of mountain dams were constructed by DPPK, as a primary action to prevent erosion. About 820 ha of forest areas were improved (felling, rarefactions etc), there were projects on forest protection from fire in 50 ha, building of water mucks (30 pieces), and pastures improvement over 90 ha.

Environment

According to the NSSD, the priorities of the Albanian government for the environment sector are the prevention of the environmental degradation process, the creation of conditions for rehabilitation of polluted areas within basic safety standards and the increase in the sustainability of the use of natural resources in the mid-term period. Achievement of these objectives in mid-term period will ensure gradual achievement of environment standards in accordance with Albania's commitments under the EU association process.

The institutional enhancement of the Ministry of Environment, the Environment Inspectorate, the monitoring network and Institute of Environment, raising awareness and including local communities, civil society and business into consultative and decision-making structures, at local, regional and national level, were the focus of Ministry of Environment's activity.

The implementation of Inspectorate's Manual was piloted into three Regional Environment Agencies in 2004. The Environment Inspectorate has strengthened its control to ensure the implementation of the law; all results of control and undertaken measures by the inspectors have been announced in media.

Table 4.10 Activities of the Environment Inspectorate in 2004

Total number of inspections conducted	2495	Orders to suspend activities	72
Total of number of settled penalties	36	For failure to pay penalties in 2003	34
Total value of settled penalties (Lek million)	9.65	For failure to pay penalties in 2004	18
Total number of collected penalties	9	For not providing the Environment License	20
Total value of collected penalties (Lek million)	0.74	For other reasons	10
Percentage of penalties collected (%)	11.2	Orders to close activities	3

In order to facilitate the implementation of the legal framework for the environment, the Ministry of Environment prepared in 2004 a package of internal orders, guidelines and rules for defining the standards of control, public participation, environmental permissions, licensing

regulation, monitoring, and protection of air quality and vehicle discharge levels. Rules and procedures that need to be applied by Regional Environmental Agencies have been defined.

The process of approximation of environmental legislation, procedures and policies to the acquis communautaire began in 2004. Albania has started reporting priority data to the European Environmental Agency; performance for 2004 was estimated at 17%. Reporting includes CDDA and stocktaking of greenhouse gases. The establishment of the Environmental Monitoring Centre, which will ensure the necessary information for policy makers according to the standards of the European Environmental Agency, is expected to occur in 2005.

One of the priorities of Ministry of Environment is to increase public awareness on the importance of environmental protection and their inclusion in the decision-making process. The comprehensive sensibility campaign through electronic and written media has continued during 2004. In close collaboration with Council of Ministers' representatives, many meetings were organised with the participation of the public on licensing procedures for activities that have a great impact on environment, such as the construction of the Bushati Hydroelectric station, the construction of the Vlora TES, the authorisation for KURUM Company to import scrap, and the preparation of the strategy for implementing the Aarhus Convention.

Reduction of the existing pollution The most urgent rehabilitating interventions are: (a) intervention in hot spot areas; (b) elimination of toxic materials; (c) reduction of industrial pollution; and (d) reduction of dust in the air in some urban areas.

The nitrogen factory in Fier installed the plant for arsenic treatment in 2004, and as a result 1000 m³ of arsenic by River Seman have been concentrated. A range of feasibility studies were conducted in 2004 for the rehabilitation of the hot spot area in Porto Romano in Durres. The encapsulation of polluted area, a pre-investment study for rehabilitation of the hot areas of Vlora, a plan for rehabilitation of the PVC plant and a plan for urban waste management are anticipated to begin in 2005. The feasibility study and the project implementation for the hazard waste landfill have identified ten appropriate zones for its construction. The legal framework for phasing out the use of ozone depleting substances has been improved. The quantity of ozone depleting materials for the year 2002 has been reported.

In order to increase the capacity of staff included in environmental conservation, a range of training courses were organised during 2004 with the participation of environment technicians and customs officials on best practices to reduce ozone depleting materials used in refrigerators and air conditioning, on increasing the capacity of the General Directorate of Customs to control imports and exports of ozone depleting substances or equipments that comprise or use them, and on monitoring of ozone depleting substances.

Sustainable use of resources A high priority has been accorded in the NSSD to measures for: (a) determining and ensuring the rights of ownership and utilisation, including the transfer of ownership rights at regional level concerning forests, pastures etc; (b) re-classifying and expanding protected areas and establishing structures for their protection; and (c) investing and intervening for the rehabilitation of degraded areas.

Protection of Lake Oher The legal framework on the protection of cross-border lakes has been improved. All illegal activities undertaken around Lake Oher have been identified and closed. Lake Oher is monitored by the laboratory that provides data for the preparation of the report on environmental situation. The data of this report for the period 2003-2004 verify that the situation of the main parameters of water quality remains stationary.

Protection of coastal and lagoon eco-systems in the Mediterranean region Under a comprehensive process a range of activities were undertaken such as management plans, mapping of land usage, habitats and homes, as well as various analyses through GIS. A series of studies undertaken in 2004, to estimate chemical pollution in the Gulf of Vlora, to assess alternatives for the sustainable management of medicinal plants, to analyse stakeholders and

governance problems, to provide a logical framework for monitoring a programme of lagoon ecosystems to evaluate the environmental situation, will facilitate interventions on environment improvement.

Bio-security This project, which started in June 2004, has evaluated existing legislation that affects the use of modern technology, in terms of national, bilateral, and multilateral collaboration, in order to strengthen the capacities and application of bio-technology. An impact evaluation on permitting genetically modified organisms as marketable products was conducted, and a database on biotechnology, bio-security and other area of management and evaluation of risks were established. The final results of this project are expected to come up in 2005.

Agriculture and rural development

The NSSED and the Food and Agriculture Strategy constitute the strategic framework of agriculture and food sector, aiming at integrated rural development for poverty reduction through ensuring: (i) sustainable increase of the production and yields from agriculture, livestock and agro-processing; (ii) improved use of natural resources; (iii) increased access to and quality of rural services (education, health, social protection), potable water supply and sanitation, as well as rural transport infrastructure; and (iv) diversification of rural economy and increasing the employment and the revenues from non-agriculture activities in rural areas.

In 2004, the agriculture sector contribution to GDP was 24% and the annual growth rate was 3.1%. Annual growth of the agriculture sector including agro-processing and fishing was 4.4%. Exports of agricultural and livestock products increased by 14.7%, and imports by 2.1%.

There still remain some key constraints in accomplishing objectives such as the fragmentation of individual farms, the return and compensation of former owners, insufficient credit for the agricultural sector, advertising and finding market opportunities, and the lack of land ownership certificate.

Increase agricultural production

Development of land market and farm consolidation The main priority has been the realisation of land ownership reform, elementary registration, and enforcement of legislation in terms of eliminating the constraints that prevent land market and institutions enforcement. As a result of land reform, 450,000 farms with an average size of 1.2-1.3 ha, have been established. About 300 agricultural companies covering in total 3421.7 ha with an average size that varies between 2.5-400 ha have been established. Until December 2004, 98.9% of the total planned surface for land distribution was privatised, and in 97.6% of cases a land certificate was provided. In 2004, 277 cadastral zones completed the first registration, increasing the level of registration of rural cadastral zones at 2437 or 83.2 % of the total (82.4% of total cadastral zones).

In order to stimulate the land market, the tax on land transfers was reduced in November 2004 from 2.5% to 0.5% of land price. The number of private farms that expanded from their original size by 5-400 ha through buying, leasing or compensation has increased. In 2003, 3500 land transactions were realised and the forecasted figure for 2004 is 4000 transactions.

Land commissions have been working mainly on solving the disagreements created as the result of commissions' errors during the compilation of legal documentation and the preparation of the documentation for the registration system. Each region has established land management and protection departments, each commune/municipality has established a land management office, each district has established real estate registration offices and 7 communes and 1 municipality have digitalised land information.

Investments in irrigation/drainage systems The following are the defined priorities: rehabilitation of irrigation and drainage systems; restructuring of water enterprises and strengthening of Water Users Associations; transferring of responsibilities to Draining Boards; support to farmers undertaking irrigation scheme management. Management responsibility was transferred under 15 Draining Boards that had been created by the end of 2004. About 20.000 ha in irrigation and 25.000 ha in drainage were improved and rehabilitated; 5.000 ha have been protected from flood; hydrography protection capacities have been increased by 10% and ten barriers of reservoirs were rehabilitated. In 2004, 18 Water Users Association have been established which brought their total number to 580. In the framework of strengthening farmer participation, 4500 ha have been transferred under the authority of Water Users Association in 2004, which increased the total surface to 180.000 ha. Improvement in the irrigation and drainage infrastructure has gradually increased agricultural and livestock production, has improved its quality, and is increasing sector competitiveness to enter the regional market. Water Users Associations lack self-management and self-financing capacities. The state budget and foreign financing still provide financial and technical assistance.

Agriculture mechanisation and use of modern methods The priorities are the introduction of new technologies in production, support to the private sector, restructuring and strengthening of control institutions, and certification of seeds and saplings.

The most positive development during 2004 has been orienting policy to benefit farmers, increasing the quality of product processing by 10%, and increasing farmer income through grants. In 2004, 651 tractors (30-100KF), 1200 agriculture engines and 7 combine harvesters (100KF) have been sold through interest credits. About 220 persons benefited from 10 grants that were delivered through competition for technological items valued at \$146,627.

The petrol excise tax in the agricultural sector was cancelled in April 2004 which decreased petrol price by 45.26% and overall costs by 25-30%. The volume of mechanisation activities increased by 15%. The land area under cash crops increased by 15-20% and 43,500 farmers profited from the implementation of this policy. The quantity of petrol attracted has been 1700 tons, of which 65 owners of greenhouses with a surface of 28.9 ha have used 750 thousand litres. Nine new farms started to apply new technologies in milking cows, contemporary housing systems, and mechanisation of fodder producing; the total number of farms that apply this technology increased therefore to 38.

During 2004, 21 new stations in cattle, 2 in X and 1 in pigs, were opened. About 43% of the cow population was artificially inseminated; artificial hybridisation was applied to 32% of the inseminated population, which increased meat production by 10%. With the aim of improving the feeding technology, the fodder patterns have shifted to corn (as energy source) and alfalfa (as protein source). Processed feed makes up 50% of food consumed by the livestock. Four factories for livestock, 66 food processing centres, and 246 sale points of foods are operating, where around 85 million gross tons of foods are being prepared. Nine regional laboratories, 4 auto-control factory laboratories and one reference laboratory in IKZ are also operating. During 2004, greenhouse area increased by 107 ha with a Lek 1.6 billion investment.

Supporting agriculture and livestock services The government priorities in this area have been the rehabilitation and strengthening of agricultural research institutions and the establishment of a national centre of scientific research and agricultural advice, the inclusion of beneficiaries in the formulation process of research priorities, the expansion of the extension service in all districts and the improvement of laboratory infrastructure and their financing.

In 2004, regional agriculture and food directorates were established, and the structures of the extension services were reorganised; these were used by 110,000 farmers or a third of the total. In 2004, 23 information centres were set up, which were used by 59,770 farmers, and 17 of them were equipped. Public extension and agriculture advisory structures have conducted: 999 demonstrations with the participation of 9,636 farmers; 694 field days with the participation of

5,193 participants. 227 days of training with the participation of 1,689 individuals, of which 534 from private sector, and 867 days of training with the participation of 10,296 farmers.

Surveys conducted in different communes of the country for monitoring the level of adoption of research recommendations pointed out that around 60% of interviewed farmers have increased their capacities and extended their skills and 23% of them have applied them. In Dibra, Tirana and Durres, 77.9% of farmers were aware of extension, each specialist trained on average 63 farmers in a year, and 58.6% of farmers adopted the recommended practices in 2004; the proportion of productivity increase after the advice was given was 11%, production grew by 11.2%, and revenues increased by 11.8%. In Shkodra, Lezha and Kukes the productivity increase was 8.5% and the growth of production was 8.2% and revenues increased by 6.9%.

During 2004, 35 research projects were implemented; 31 research projects were conducted in several farms based on direct needs of farms. The State Institute of Seeds and Plants, the variety testing laboratory and the in-vitro laboratory of the genetic bank were restructured and provided with necessary equipment. Three regional laboratories on seeds testing were set up.

In order to control animal diseases and maintain the epidemiological situation clear from infection and zootechnical diseases, 100% of animals were vaccinated against anthrax (over 800.000 heads); 100% were tested for brucellosis (over 700.000 heads), while 5000 heads were found to be infected, were eliminated, and farmers compensated; 100% of tuberculosis search were completed (over 37.000 heads); the veterinary legal framework was improved and approximated with the EU standards.

Management of fishing and aquaculture activities The priorities are: enforcement and expansion of national and regional fishing associations, and enhancement of legal and institutional framework for monitoring and controlling fish resources.

In 2004, 9 Fishing Management Organisations were established in full structure, which started to direct coastal aquaculture production toward wrasse and bass and inland water aquaculture toward the production of trout and shrimps. These organisations distributed 1.2 million spawns in 2004 compared to 1.03 million spawns distributed in 2003.

Forest and pasture management The most important development has been the preparation and approval of the Strategy of Forest and Pasture Area Development and Institutional Reform. The approved law 'On forests' will serve as the main way to enhance structures of forest and pasture management. During 2004, in close collaboration with the Ministry of Local Government and Decentralisation, the registration of forest and pastures in all local government units was completed. The most problematic issue is the application of Law no.8744 'On transferring the public real estates under the authority of Local Governmental Units'. In the framework of the fight against land erosion, 180 ha foresting and 800m³ mountain barriers were completed.

Increase access to financial services The government priorities are: promoting the bank system to provide these services in rural areas, including and developing sustainable intermediaries, as a considerable part of financial sector, and establishing sustainable private networks of saving-credit associations in rural areas, based on credit funds.

The Albanian Saving-Credit Union, which supports technically and financially the saving-credit associations, during the 12 year of the rural credit programme has distributed over 30,000 credits for rural area inhabitants. Actually the Albanian Saving-Credit Union offers financial services for 41% of the villages in 8 districts (Tirana, Elbasan, Durres, Kavaja, Lushnja, Fier, Vlora, Gramsh).

Table 4.11 Access to financial services in rural areas

	2000	2002	2004
Number of Saving-Credit Associations	21	88	89
Number of members of Saving-Credit Associations	506	5,285	10,430
Number villages covered by Saving-Credit Associations	21	160	372

The credit committee of the Albanian Saving-Credit Union approved 226 applications for re-financing, presented by Saving-Credit Associations of a total value of Lek 238 million in 2004. The credit portfolio was increased as the result of three factors: increased volume of credit given to Saving-Credit Associations, decrease of credit portfolio in FKF and increase of deposits.

Table 4.12 Activities of Saving-Credit Associations

	2000	2001	2002	2003	2004
Union portfolio in Saving-Credit Associations (thousand)	421	1837	5060	7980	9314
Total number of active credits	4423	5277	6380	7621	7400
Average credit	605	698	851	1012	1258
Portfolio of Saving-Credit Associations networks (thousand)				9413	1227
Individual funds in Saving-Credit Associations networks (thousand)		168	468	1078	1645
Portfolio of deposits in network (thousand)		9	121	374	1030
Portfolio in risk (over 30 days)*	3.64%	2.41%	1.10%	0.85%	0.70%
Delay Credit (30 days) / Total of Credit					

During 2004, the associations have provided about Lek 1.3 million of financial resources. The financial results of these institutions are quite positive: at about Lek 1.2 million. During 2004, new low-cost financial resource agreements were signed with the Albanian Government, Swiss and Spanish Cooperation, UMCOR, RABOBANK and CEFA.

In 2004, MADA has restructured its central staff in order to increase the operational efficacy and cost effectiveness in processing activity.

Increase agro-processing activities

Ensuring support for agro-processing activities is a strategic decision for increasing the productivity of the agricultural sector. In 2004, the output of the agro-processing industry grew by 11.7% where the contribution of bread was 15.3%, of soft drinks 11.7%, and of cheese by 8.8%. Compared to 2003, the production of soft drinks increased by 41.4%, the production of beer by 92.2%, and the production of olive oil by 120.7%. The production of conserved fish, fruits and vegetables, and milk grew as well. In 2004, Lek 2 billion have been invested in agro-processing industry to install new lines with advanced technology for olive oil production, milk processing, refining of vegetable oil, fruit and vegetable processing etc.

Support marketing of agricultural food production

Strengthen internal structure of marketing The construction of the Lushnja and Korca markets in June 2003 had an impact in raising domestic production and reducing prices by 5%. During 2004, these markets traded 500 tons of agriculture products. In 2004, 10 collection centres were established which reduced transport costs by 20%. The preparation phase for construction of markets in Vlora and Shkodra has been finalised.

In the framework of promoting domestic production, two main fairs were organised in 2004: Agribusiness 2004 in Tirana and the International Fair in Bari. The excise tax for alcoholic drinks was reduced, a discriminating price for fuels was applied for fishing and agriculture, and lower VAT rates were applied on some agricultural and livestock articles that are extensively used in the food industry (milk, wheat, grapes, olive etc)

Legislation, food quality control, and consumer protection The legislation on quality, timeframe and trade conditions and the harmonisation of legislation on agriculture products with the EU have been improved. The Food Inspectorate has been restructured to enforce food controls, improve the network of food laboratories at the district level, the Food Control Regional Laboratory in Durres and the Analysis Department in IKU have been certified with ISO 9001, and technical assistance for the staff of the Food Control Regional Laboratory on HPLC for gas chromatograph and spectrophotometer and for atomic absorbent was provided. During 2004 the number of conducted analysis increased by about 9%.

Table 4.13 Food quality controls, 2003-2004

	2003	2004
Number of conducted analysis in food laboratories	37928	41800
Number of controls	18150	19509
Number of violations	165	168
Blocked and eliminated goods (kv)	3810	6255
Total revenues (Lek million)	7.382	44.913

Assessing the policies for the development of mountain areas

The National Forum for the Development of Mountain Areas was established in 2003 with the support of the International Fund for Agricultural Development and the Mountain Areas Development Agency (MADA) and the technical assistance of the Institute of Contemporary Studies and the Centre for Rural Studies. The objective of this Forum is to contribute to the formulation of a new vision for the development of these areas, to carry out various lobbying activities with decision makers, as well as to contribute to the process of defining priorities, to identify, design and implement social and economic development projects.

Work is continuing to set up and strengthen forums in 7 pilot districts (Kukes, Diber, Mirdite, Librazhd, Berat, Korça, Permet), to expand this initiative to other mountainous districts and to integrate them in one national Forum until the end of 2005. Meanwhile, the lobby of parliament members for the development of mountain areas established in 2003 has contributed to the creation of district groups and has had the first impacts on government policies in favour of mountain areas. Some examples of successful lobbying during 2003-2004 are the following:

- Strengthening of MADA and the Mountain Areas Finance Fund (MAFF);
- Adoption of fiscal equality rules in unconditional transfers to local government in mountain areas;
- Public investment on infrastructure and priority services in these areas;
- Attraction of attention of other donors to initiate development programmes in these areas.

The objectives at national level for 2005 are to:

- Develop a vision for mountain areas in the NSSD;
- Influence the MTBP and the draft 2006 budget in favour of mountain areas;
- Influence strategic documents and action plans to shift focus from relief to development;
- Improve the information provided to business and donors on development opportunities for mountain areas, on existing capacities, and on the potential for partnerships.

Representatives of the Forum for the Development of Mountain Areas in Permet, with the support of the Centre for Rural Studies and the Catholic Relief Services, carried out an impact assessment of the NSSD policies in Permet during 2004. The table below gives a summary of the main results from the assessment.

Satisfactory	Moderate	Not satisfactory
Veterinary prophylaxis Rehabilitation of national roads Electrical power supply Urban planning / administration Start-up of investments in agriculture, especially irrigation Reconstruction of schools and hospitals in urban and peri-urban zones of mountain areas	Viniculture and arboriculture Training health care providers, especially at auxiliary level Short-term training of teachers Infrastructure of health centres Promotion of cultural works Facilitation of administrative procedures for business Farming production Road network for communes Decentralisation	Rehabilitation of rural and tourist roads Teaching materials in rural schools Ambulances in rural areas Support to agro-industry and marketing Mechanisation and introduction of new agricultural technologies Protection of land from erosion Provision of health care and ambulatory centres with necessary equipment Access of farmers and business to credit Local government capacities Restoration of cultural monuments Prevention of forest and pasture degradation

