



ALBANIAN ASSOCIATION OF BANKS  
SHOQATA SHQIPTARE E BANKAVE

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# CONTRIBUTION OF THE BANKING SECTOR TO THE ALBANIAN ECONOMY AND SOCIETY

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JANUARY 2018





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This study was conducted by Op2M, Croatia,  
as commissioned by the Albanian Association of Banks.  
Special thanks go to Mr. Stjepan ANIC, Mr. Indrit BANKA and  
Mr. Vladimir DAVCEV



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## Structure of the study

<i>Executive Summary</i>	7
<i>Introduction</i>	8
<b>1. Banking sector contribution to the economy</b>	<b>9</b>
<i>1.1 Banking sector and economic growth in Albania</i>	10
1.1.1 Contribution of banking sector to the achievement of GDP in Albania	11
1.1.2 The growth trend of the banking sector	11
1.1.3 Banks as the crucial and almost only source of capital for the economy, comparison with other countries in the region	13
<i>1.2 Understanding the importance of banks on public finances</i>	14
1.2.1 Banks partnership with the state in continuous financing of the budget and financial support of banks for the functioning of the country and its system	14
1.2.2 Support of banks to the state during financial crisis	15
1.2.3 The contribution of banks for efficient state treasury operations	16
1.2.4 Contribution of banking industry to the budget through paid taxes	17
<i>1.3 Economic dimensions of financial development</i>	18
1.3.1 The responsibility of the banking sector to manage credit risks and the responsibility for recovery of liquidity in the economy	18
1.3.2 Supporting economic activities of: (i) SMEs segment, and (ii) individuals. How much the banking industry has loaned for the period?	19
1.3.3 Evidence of deposits in banking sector (short, medium and long term)	20
1.3.4 Trends of banking industry development during the period, including banks new products during 2009- 2016	20
1.3.5 Banks investments to technologies.	21
<b>2. Banks and the Society</b>	<b>22</b>
<i>2.1 Financial intermediation as a public good</i>	22
2.1.1 The contribution to the transposition from a cash economy to a non-cash economy	22
2.1.2 Deposits and loans	23
2.1.3 Banks support citizens in purchasing real estate properties, Responsible risk management	23

2.1.4 The role of alternative channels development and modernization of the customers demand	24
2.1.5 Payments and other services provide efficiency to the society in its everyday activities	25
<i>2.2 Employment and Social responsibility</i>	25
2.2.1 Employment in the banking sector	25
2.2.2 Banks' donations and sponsorships as per Social Corporate Responsibility	26
2.2.3 Banks and financial education.	27
<b>3. Development perspectives and Banking in a regional context under the Financial Sector lenses</b>	27
<i>3.1 Regulatory perspective and future development of banks business models</i>	28
<i>3.2 Cross-impact of development of financial sector entities such as investment funds, further market exchange concepts and insurance</i>	30
<i>3.3 SEE economic perspective and its impact</i>	30
<b>4. Conclusions on economic and social impact</b>	32
<i>4.1 Key assumptions on economic and social impact of modern banking sector and comparison with current state in Albania</i>	32
<i>4.2 Conclusion on the key critical impact and aspects of the importance of the Albanian banking sector to economy and society</i>	32

## Executive Summary

The banking sector in Albania has increasingly become of paramount importance for the sustainable development and social welfare of the country's economy. Strong evidences provide sufficient arguments in support of this conclusion that is widely recognized by local and international institutional actors, as well as citizens and customers themselves.

With a value added of 3.1% of the GDP from the financial sector and a total volume of financing to economic agents that counts for 40.5 percent of country's total economic production, banks can now be considered as macro-economically systemic and an engine of growth for the economy. The total lending to the private sector and to individuals has grown 8.8 times from 2004 to 2016, while banks' assets have reached 95 percent compared to the GDP. Total contribution of banking sector in the state budget in 2016 peaked 6.7 billion ALL at a time when the Albanian banking sector was profitable, well capitalized and liquid, guaranteeing continuous financing to economic activities. Considered as an important employer regarding working conditions, career development opportunities and providing a solid basis for social benefits for employees, the banking sector in Albania is more than ever before considered as an indispensable driving force behind the harmonious qualitative growth for the economy and the society.

## Introduction

Banks are the driving force behind financial development and these financial intermediation institutions are instrumental in smoothing frictions between economic agents and allowing Pareto optimal allocation of resources in an economy. In line with the general economic structure, banks serve to pave the way toward a sustainable growth.

Through this analytical study entrusted by the Albanian Association of Banks, the Op2M team of experts diagnoses the state of art of banks contribution to the economy and society in Albania for the period 2004 – 2016, gathering and utilizing all data available and aiming to draw projections on the potential of financial development – economic growth synergy in the future.

The methodological approach used to draft this study follows the main research goal, with a view to understand the impact and positive spillovers that the banking sector has in the society and the Albanian economy. Contribution of banks to the economy is evaluated in the light of the role of banks in financing productive activities that result supportive to the country's economic growth. Meanwhile, contribution to society is evaluated by measuring the social impact of banks activity through their Corporate Social Responsibilities agenda and their structural role in contributing to public finances.

The study begins with the analysis of banks important function in support of Albania's economic growth and social development to follow then with a consideration of the development perspectives of the banking sector in a regional context under the lenses of present stance of financial industry. Conclusions on the positive economic and social impact of banks will be based on key assumptions regarding modern banking sector and on the comparison with the current state in Albania. Final remarks will be drawn on key critical aspects of the importance of the Albanian banking sector for the country's economy.



## 1. Banking sector contribution to the economy

Economic importance of banks in a society starts with their structural crucial role of pooling savings and allocating resources in the economy towards financially reliable economic agents. The interest rates applied by financial institutions reflect the competitiveness and completeness of financial markets.

Furthermore, banks provide the private sector with highly qualified expertise, enabling the financial intermediaries to contribute in reducing risks in the economy.

Optimal operational management is qualitatively bolstered by financial services industries that are continuously aiming for higher productivity gains.

Banks serve as key players in formalizing the economy and enhancing the positive impact by exercising their role as fiscal agents, which is crucial in contributing to the reduction of tax evasion phenomenon, the reduction of transactions costs for the economy and the creation of a more enabling environment for the country's business development in long term.

When it comes to customer needs, banking products are quite beneficial in individual terms, by facilitating receiving and execution of payments anywhere in the world, helping to optimally allocate personal funds, protect and save money, but also manage and control them accurately. The banking sector helps citizens to grow their savings through investment options and term deposits. "Peace of mind" is the overall best term to illustrate the banks significance for citizens, which could be generally agreed without hesitance.

The relationship between the financial sector development and economic growth has always been in focus of economists' theoretical and empirical research analyses, in the form of contributing efforts trying to better understand and effectively utilize compounding effects and mechanisms of this economic phenomenon in favour of growth. Financial development process in itself has evolved over time as a result of more efficient and productive financial markets and their incremental influence on growth.

An investigation of the nexus between financial development and economic growth in SEE economies shows that credit to private sector appear positive for growth. In fact, early theoretical deductions stress out that development of financial intermediaries in support of entrepreneurial initiatives positively impact the economic growth by channelling the sources of funding towards the most efficient innovative ideas in the market destined to succeed, and eventually impulse growth in economy. Loans provided by intermediaries are considered essential to finance efficient productive processes that eventually generate surplus in firms' financial state. Inventions that are feasible in production terms are considered as positively supportive to efficient growth of production firms.

However, in the course of years, there have also been controversial voices that by focusing in the improvement of the neo-classical growth model, the role of financial intermediaries is considered to be overstressed. However, many agree that economic growth creates the necessary stimulus for the "financial superstructure", with a view to maximize profits and further consolidate, while in turn, financial development paves the way for further growth. Economic development is described as a joint causality between financial intermediaries' expansion and positive economic growth, accompanied by a declining income inequality while the economy reaches the "maturity stage". Their contribution consists in introducing a system of rules

in which financial intermediation and economic growth are endogenous by determination and in emphasizing the crucial importance of banks, insurance companies and other financial intermediaries in providing their expertise to economic agents for properly analysing the market information to optimize the allocation of funds towards higher returns and to minimize risks. Competitive financial intermediaries' (banks) development influences an optimal resources allocation in economy that positively affects for higher real economic growth rates. For academics, this is an interesting approach in providing theoretical arguments stating that the competitive development of banks has a positive impact in economic growth through the effects of "spillover externalities" resulting from increasing rates of return on capital investments and consequently growing productivity, considering that competitive financial intermediaries as deposit money banks tend to allocate resources to the most profitable investment opportunities, which favour the creation of an enabling environment in support of incremental rates of return on capital. On the other hand, the rush of economic agents towards higher rates causes the reduction of savings in economy, less resources accumulation in intermediaries and, as a result, a potential drop in financing power of money deposit, eventually causing a slow-down in the growth pace, if this continues in long run. Despite the fact that this is usually seen as a positive finance-growth relation in literature, part of the researchers' attention needs to be focused on the cases when financial development negatively affects the savings rate and as consequence of lower resources channelled through intermediaries, the growth rate slows down. In addition, it is still unclear why in some economies the fast growth of financial development is accompanied by standard monotonous rates of economic growth. In conclusion, for obtaining better understanding on specific financial market-growth causality, firstly we need to focus on specific markets of interest, given the fact that different economies manifest different characteristics conditioning the relation in focus of this study.<sup>1</sup>

## 1.1 Banking sector and economic growth in Albania

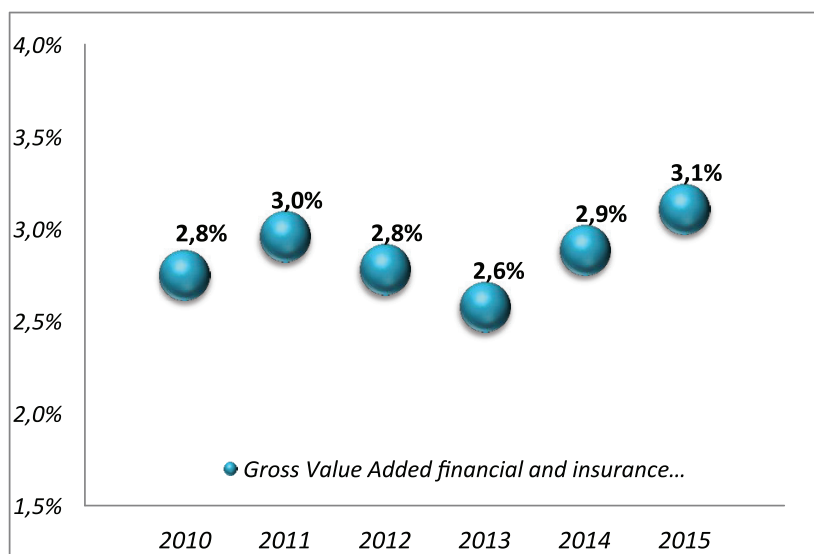
- In Albania, a total number of 16 banks are operational, which feature a total of 498 branches well spread all around the country.
- Banking sector serves as the working place for 6950 employees in total.
- Total volume of assets in the Albanian banking sector to date reaches the value of 1'407'286 mln ALL.
- Banks are the main financing source for the economy in general, and by the end of 2016, the total lending of banks to the economy reached a significant level of 40.5% of the Gross Domestic Product.
- As banks serve as the main safe shelter for economic agents in the economy, the total deposits amounted to 745.526 mln ALL by 2016.
- The total volume of the outstanding loans for the economy by the end of the study period amounted to 600.367 mln ALL.
- In 2016, the Albanian banking sector resulted in positive profit after tax amounting to 9.270 mln ALL.

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<sup>1</sup> Bagehot (1873), Schumpeter (1912), Robinson (1952) Lucas (1988) Rama (2015) Greenwood and Jovanovic (1990), Bencivenga and Smith (1991)

### 1.1.1 Contribution of banking sector to the achievement of GDP in Albania

Graph 1. Contribution of financial sector to country's GDP



Source: Institute of Statistics

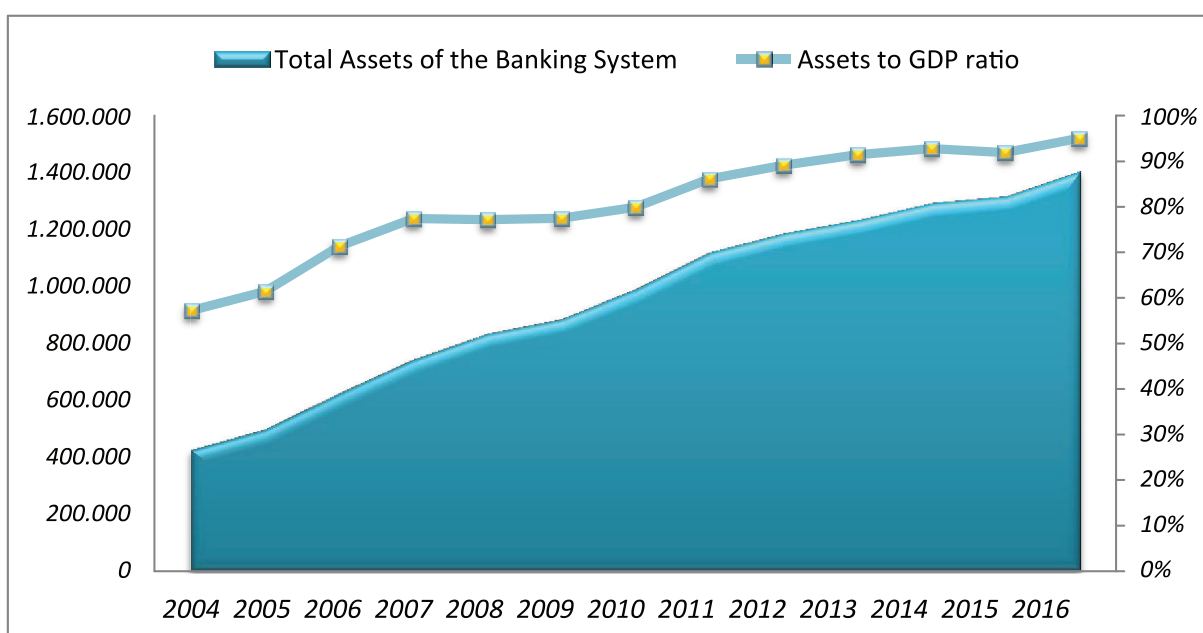
The banking sector stands at the epicentre of the financial intermediary institutions in Albania. This is due to the fact that when we talk about the contribution of the financial sector to the country's gross domestic product, it primarily means the banking sector role in support of economic activities.

Thus, the financial sector contribution to the GDP declined following the sovereign debt crisis in Greece and Italy, two main economic and trading partners of Albania with Italian and Greek banks in the system, being manifested in lower value added by 2012 and 2013. However, from 2013, the value added of the financial sector to GDP rebounded to reach the highest level of the last years regarding the gross value added.

### 1.1.2 The growth trend of the banking sector

The banking sector has preserved its upward growth trend in the period of study 2004-2016. Due to the sound financial conditions of the banking sector, the financial crisis did not affect its growth with assets amounting nearly to the total value of the country's GDP. By 2016, the total assets of the banking sector amounted to 140.7285,86 million ALL or around 95% of the GDP.

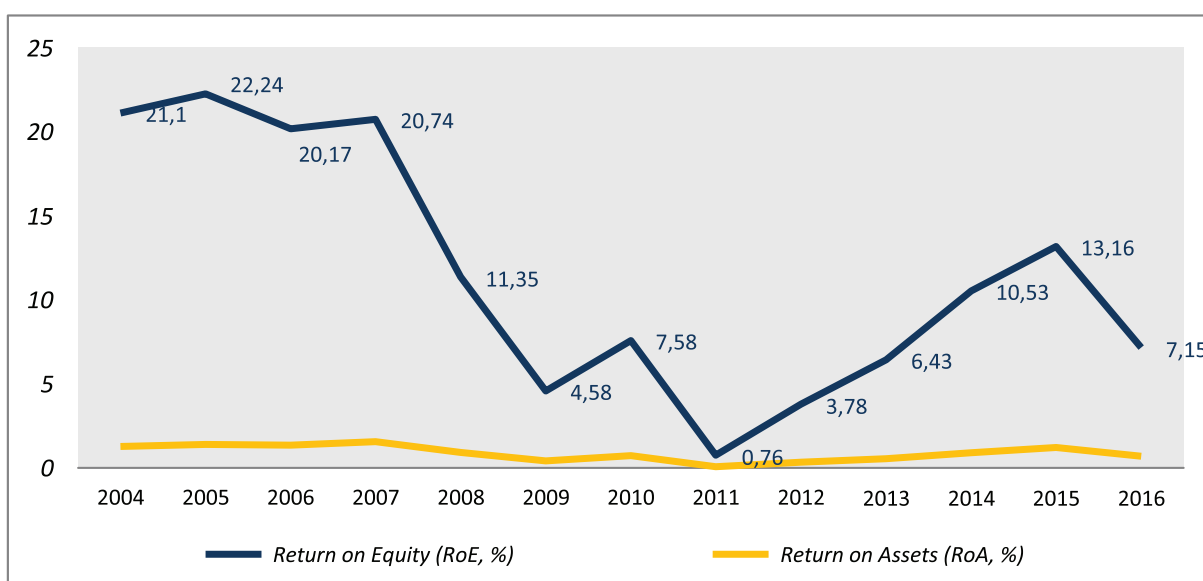
Graph 2. The trend of the banking sector growth



Source: Bank of Albania

Albanian banking sector has managed to keep a positive profitability outlook despite the financial and the sovereign debt crises that affected neighbouring countries. Of course, the negative economic spillover effects were transmitted in the economy but this did not affect the banking sector overall soundness and stability. However, the financial crisis negatively impacted profits of the banking sector in 2008-2009 with repercussions also in 2011 and lower profits in 2016, which reflected a slower lending activity from the side of banks.

Graphs 3. Profitability position of the Albanian Banking Sector

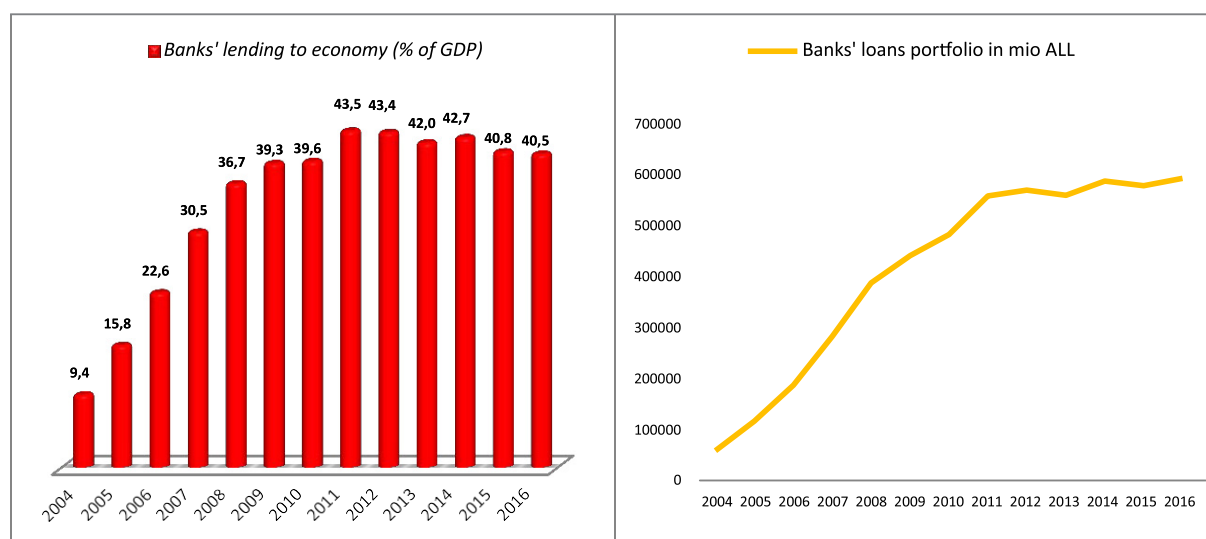


Source: Bank of Albania

### 1.1.3 Banks as the crucial and almost only source of capital for the economy, comparison with other countries in the region

The banking sector in Albania has served as the primary lending source for the economy. Banks' lending to the economy as a ratio to GDP peaked in 2011, prior to sovereign debt crisis of the main trading partners. Since then, the lending activity has plateaued manifesting a downward trend, but banks and the central bank are committed to increase financing.

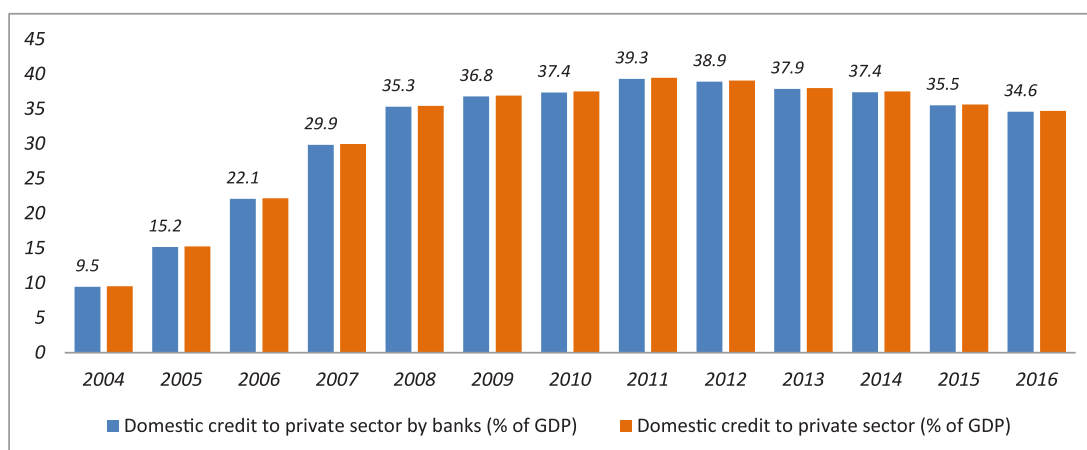
Graphs 4. Banks' lending to the economy (in % of GDP and mln ALL)



Source: Bank of Albania

As the following graph shows, banks in Albania are the main and almost the only source of funding to the private sector in the Albanian economy. Microfinance institutions and saving-lending unions count for around 2 to 3 percent of the total lending to the private sector economy.

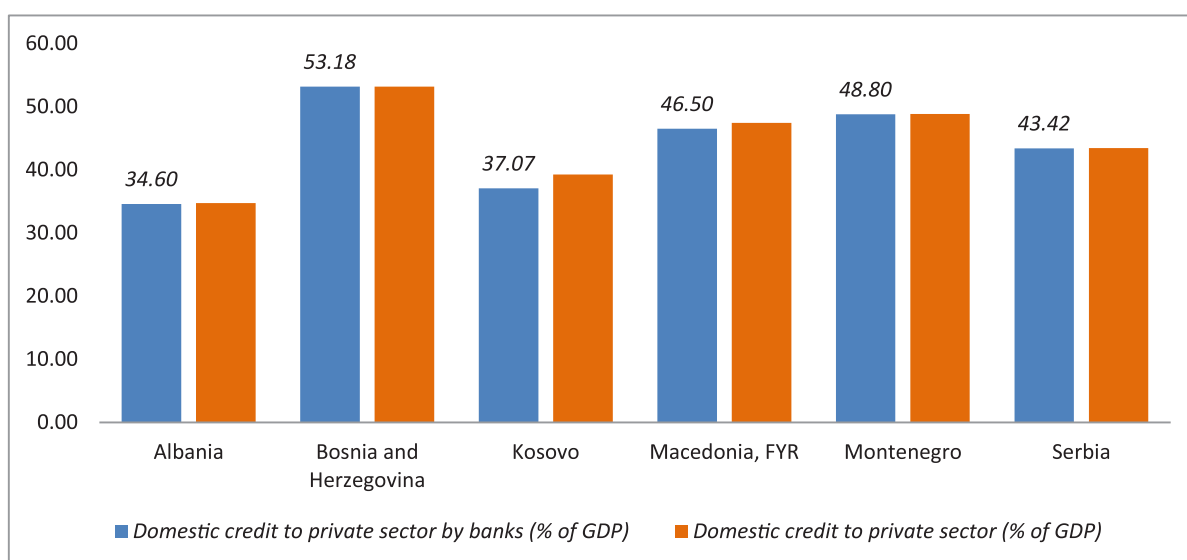
Graph 5: Banks' lending to the economy



Source: World Bank

The same applies when it comes to a regional look. Banks are the main financial intermediaries that perform financing support to the private sector in the Western Balkans. However, comparing to other countries in the region, it is possible to understand that Albania has the lowest rate of domestic credit to the private sector in proportion to the Gross Domestic Product.

Graph 6: Lending to the economy by banks in the Western Balkans Six countries



Source: World Bank

## 1.2 Understanding the importance of the banks on public finances

### 1.2.1 Banks partnership with the state in continuous financing of the budget and financial support of banks for the functioning of the country and its system

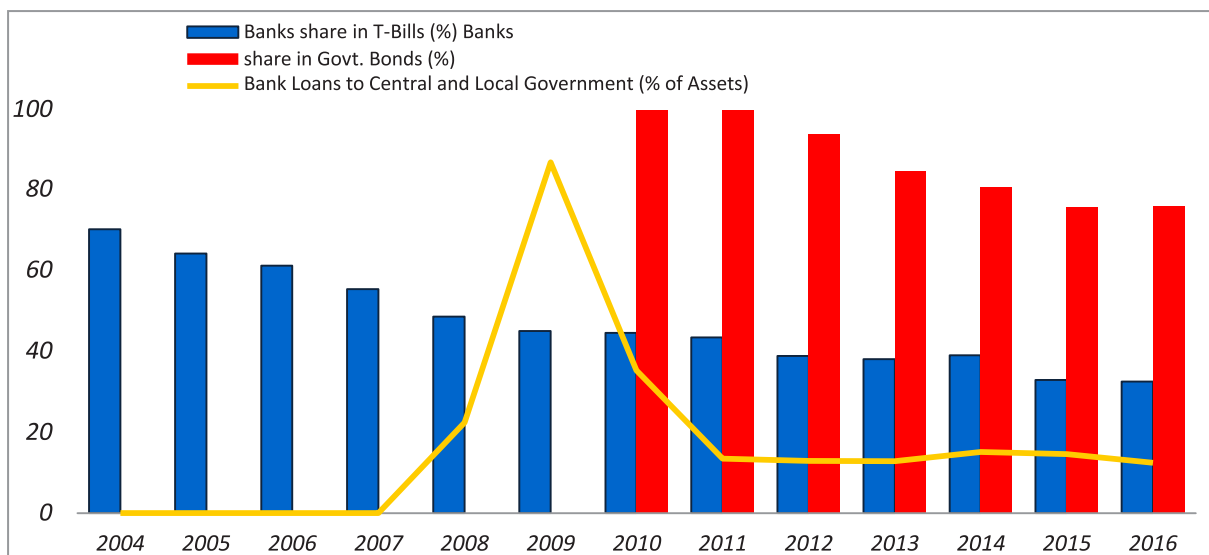
The Albanian banks started to buy Government bonds in 2010 and they continue to be the main long-term sovereign debt holders in the economy with more than 75% of total debt. While volume of T-bills held by banks has constantly declined since 2004. It still counts for 32,4% of the total T-Bills issued.

However, in addition to the public debt burden, banks have played an instrumental role in supporting the central and local government with financing, with the highest level spiking in 2009.

Table 1: Banking sector as holder of the Albanian public debt and loans to central and local Government

	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016
Banks share in T-Bills (%)	70,0	64,0	61,0	55,3	48,5	44,9	44,4	43,3	38,8	38,0	38,9	32,8	32,4
Banks share in Govt. Bonds (%)							99,4	99,4	93,3	84,1	80,3	75,4	75,7
Bank Loans to Central and Local Government (% of Assets)	0,0	0,0	0,0	0,0	22,3	86,5	35,2	13,4	12,9	12,8	15,1	14,6	12,4

Graph 7: Banks share in Government bonds and lending to central and local Government

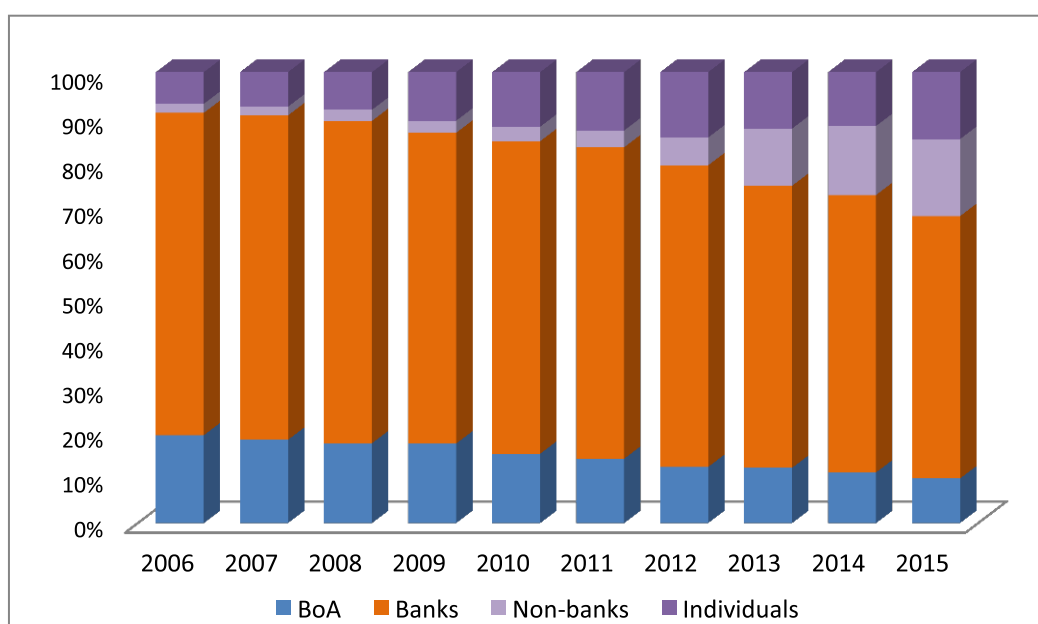


Source: Bank of Albania, Ministry of Finance

### 1.2.2 Support of banks to the state during the financial crisis

Banks continue to be the main debt-holder in the country, with a substantial share of the sovereign debt being held by them, nearly 60% of the total burden. Banks play an instrumental role also in facilitating citizens' purchase of the public debt.

Graph 8: Banks share in Government bonds and lending to central and local Government



Source: Bank of Albania, Ministry of Finance

After the financial crises of 2009, the banking sector in Albania closely cooperated with the Bank of Albania and the Ministry of Finances to enable the minimization of the crises effects in the economy. This collaborative attitude supported the efficient management of the liquidity situation of the banking sector, oriented lending towards national currency and influenced the preserving of parameters for financial stability and capitalization of activity. Eventually, the situation entered into a qualitative improvement stage, following the resumption of the process of public deposit growth in the banking sector, which gradually and steadily took place in the second quarter of 2009 and continued at satisfactory paces. During this period, banks showed due diligence and accountability.

In the same path, banks' lending to the central and local Government reached the highest level in 2009, showing how important the banking sector in Albania was to support financing for public investments and Government interventions during a crisis time.

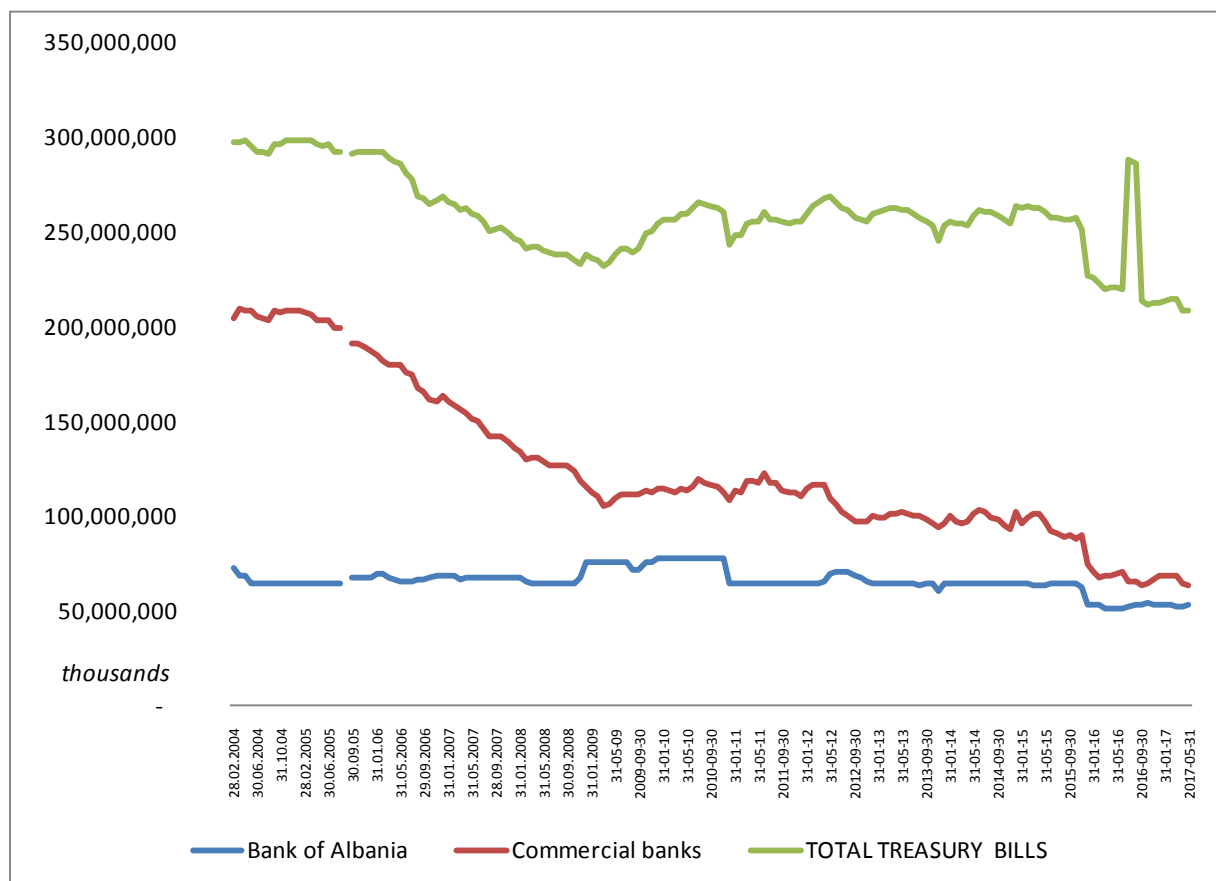
### 1.2.3 The contribution of banks for efficient state treasury operations

Due to continuous lowering of policy interest rate, Treasury Bills have become less attractive in terms of returns and as result, banks purchases of these debt titles have sharply fallen. Instead, banks have shifted their attention on Govt. bonds becoming main debt holders in the economy.

Second level banks in Albania play an instrumental role in facilitating, enabling citizens to invest their savings and revenues in purchasing treasury bills, making it easier for the Government to sell its' public debt.



Graph 9: Treasury operations



Source: Bank of Albania

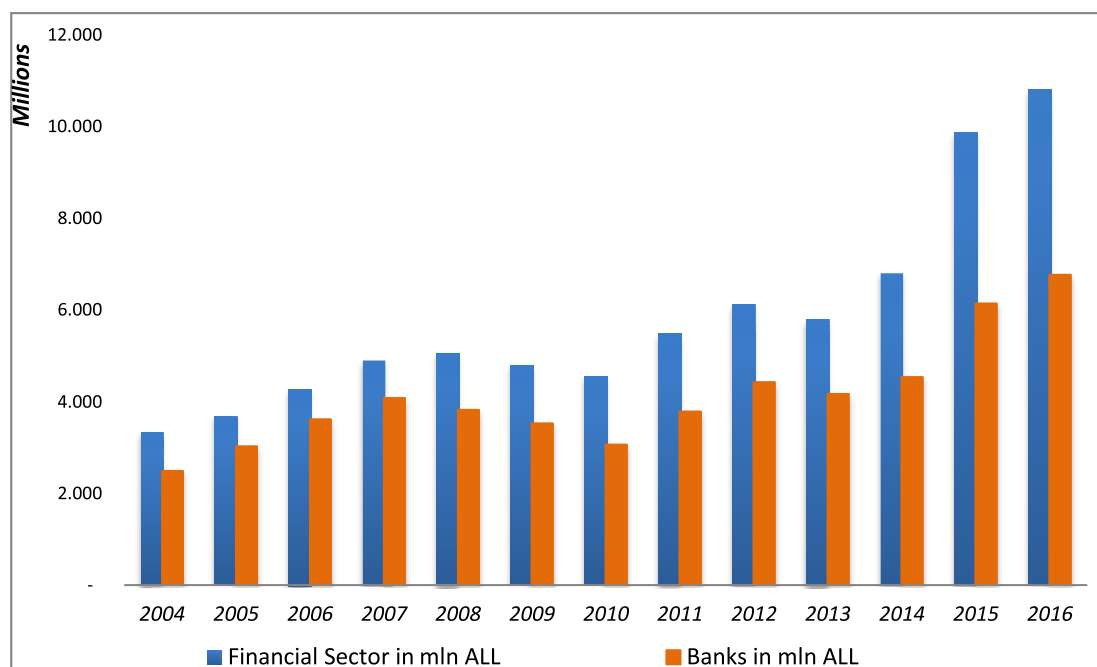
### 1.2.4 Contribution of banking sector to the budget through paid taxes and other contributions, and comparison with other sectors

Contribution of the financial system to state budget in general and banks in specific has maintained its positive incremental path, reflecting in this way a continuous genuine growth of the banking sector due to the support that banks provide to productive activities of the economy and households.

In 2016, the total contribution of the banking sector amounted to 6,76 billion ALL and this being the highest level of contributions in the period under study.

Reading the numbers, it is possible to understand that insurance companies, pension and investments funds contributions have manifested growth in tax contributions.

Graph 10: Contribution of banking industry to the budget through paid taxes



Source: General Tax Directorate

## 1.3 Economic dimensions of financial development

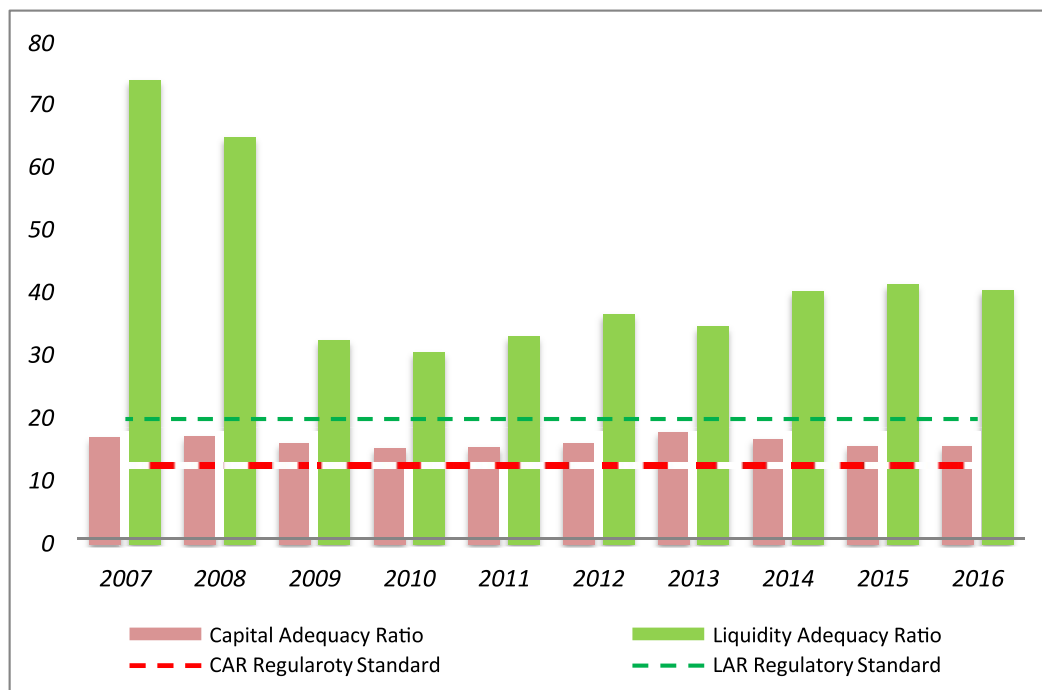
### 1.3.1 The responsibility of the banking sector to manage credit risks and the responsibility for recovery of liquidity in the economy

As mentioned above, the concept of financial development underlines the importance of banks in an economy as a crucial actor in risk management related to the financial activity. At the present, the Albanian banking sector is well capitalized and its liquidity has been constantly above the regulatory level of liquidity adequacy ratio of 20%, hence consolidating confidence in banking sector.

Referring to the latest Financial Stability Report of the Bank of Albania<sup>2</sup>, the liquidity position of the banking sector in Albania stands at good levels. The liquidity indicators, both in ALL and foreign currency, stand above the minimum regulatory level. Deposits remain the main source of financing, covering almost twice the volume of loans for the sector. The banking sector maintains a good liquidity position with a considerable outstanding ratio of client deposits to loans. In December 2016, the deposit-to-loans ratio registered 192.8% (loans-to-deposits 51.9%). By currency, this ratio registered 220.1% for the domestic currency and 173.6% for foreign currency. Liquid assets in banks' balance sheets remain high, while lending performed below potential. At the end of 2016, liquid assets accounted for 31.3% of total assets of the banking sector, slightly downward during the period, by 0.3 percentage points. The other liquidity indicator, "liquid assets/total short-term liabilities", also trended down by 0.5 percentage points to 40.6%.

<sup>2</sup> [https://www.bankofalbania.org/web/Financial\\_Stability\\_Report\\_2016\\_H2\\_7752\\_2.php](https://www.bankofalbania.org/web/Financial_Stability_Report_2016_H2_7752_2.php)

Graph 11: Financial Soundness Indicators in %



Source: Bank of Albania

### 1.3.2 Supporting economic activities of: (i) SMEs segment, and (ii) individuals. How much the banking industry has loaned for the period (loans already repaid)?

Banks in the Albanian economy serve to economic agents in offering all financial services available in support of their productive activities. This has been the important reason why banks have kept a substantial pace of growth in terms of assets by serving to the society and economy. As the graph shows, after the crises banks have been more prudent in their lending activity and this is reflected in the plateau that loans to private sector and individuals manifest after 2011.

Table 2: Banking activity in providing services and products to the economy.

in mln ALL	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016
<b>Total Assets</b>	426440,3	496562	624279	742855	834139	886310	990631	1120168	1187983	1234321	1293721	1317843	1407286
<b>Loans to private sector and individuals</b>	64824,7	118071	186572	273496	365425	410805	456820	529830	545000	531239,6	560711	551679	570622
Short-term loans	18712,2	33313,6	50497,2	73928	102940	113533	128660	156760	162085	159391,8	168284	165451	162080
Medium term loans	24560,7	38818,7	60491,6	72871,7	78720	88081,6	99882,6	116335	114453	100480,2	105816	106081	120405
Long term loans	10983,4	29346,7	37312,4	63746,5	100922	110209	124003	144756	155116	159172,8	174891	172676	180850
Real estate loans	10568,4	16532,5	38223,2	62871,2	82385	98221,9	103787	111236	113102	111569,1	111071	105661	105369
Finance lease contracts	-	59,9	47,4	78,2	458,2	759,3	488,3	743,6	243,7	625,7	649	1810,5	1918,5
Loans to public administration	-	-	-	-	1857	7656,8	3554,1	1535,1	1587,9	1655,7	2031,3	1975	1781
Other customer accounts	4974,2	8985	10292,6	17058,8	26843,8	27579,6	26115,7	30317,1	26919	30204,3	28557,6	28535,6	24461,9
Securities Transactions	29750	60395,2	91954,2	133317	166742	177727	210663	244172	256682	302410,5	327792	307608	368362

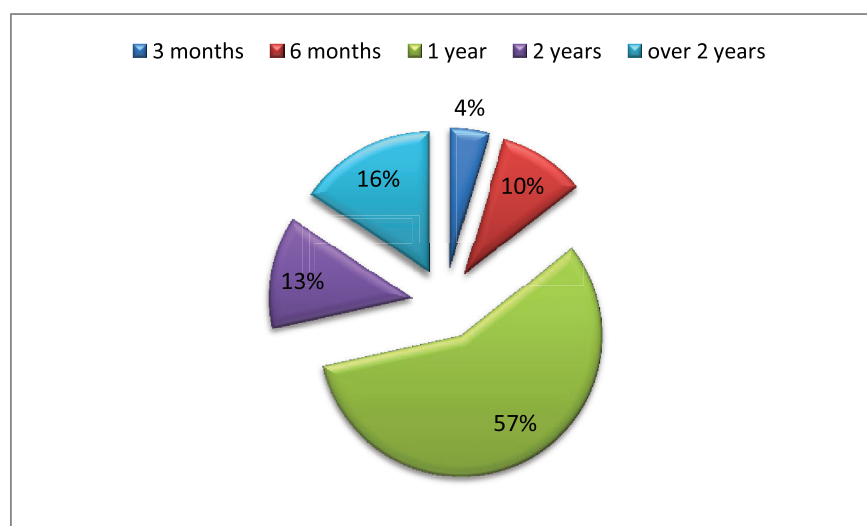
Source: Bank of Albania

### 1.3.3 Evidence of deposits in banking sector (short, medium and long term)

While deposits have become less attractive for the general public as the interest rates have touched the bottom, households continue to consider them as an alternative. One-year deposits represent the majority of deposits stock by the end of 2016.

It is possible to notice that Albanian savers prefer long rather than short term maturities for their savings.

Graph 12: Deposits with agreed maturity December 2016



Source: Bank of Albania

### 1.3.4 Trends of banking industry development during the period, including banks new products during 2009- 2016

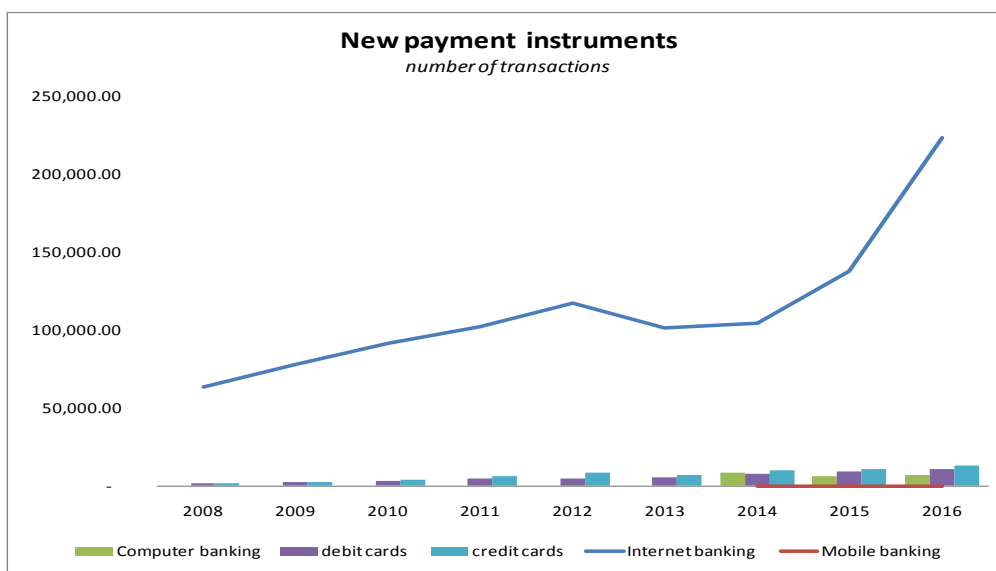
During these last years, internet banking has soared in the Albanian banking services mosaic with more than 223.000 transactions in 2016 and with a total volume of 1.256.879 million ALL with individuals ahead of businesses. Computer and mobile banking started to be used in 2014 and are fast gaining popularity. Credit cards have kept ahead of debit cards in terms of number of transactions processed through their use.

Table 3: Number of transactions with new banking services and products

	2008	2009	2010	2011	2012	2013	2014	2015	2016
<i>Internet banking</i>	63,422	78,156	91,274	102,070	117,233	101,092	104,532	137,803	223,110
<i>Mobile banking</i>							77.39	46	140
<i>Computer banking</i>							8,614.7	6,268	7,413
Debit cards	2,014	2,566	3,151	4,719	4,740	5,739	7,914.90	9,059	11,061
Credit cards	2,182	2,756	4,287	6,195	8,657	6,772	10,006.15	11,082	13,360

Source: Bank of Albania

Graph 13: Number of transactions with new banking services and products



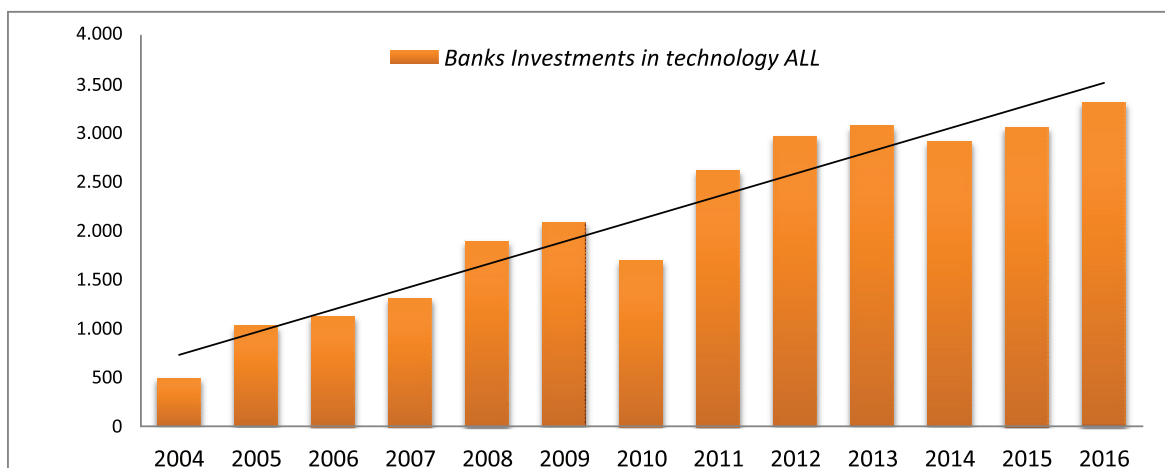
Source: Bank of Albania

### 1.3.5 Banks investments to technologies

Investments in new technologies is a priority of commercial banks operating in Albania when it comes to quality standards of service provision. Because of this reason, banks have invested significant amounts in hardware and software upgrading from their annual budget. In 2016, the total value of investments reached the amount of 3.3 billion ALL.

As projections on the future could be drawn, banks will continue to serve as innovation hubs for adapting new technologies always in service to the citizens.

Graph 14: Investing in new technologies by banks



Source: Albanian Association of Banks, 15 banks

## 2. Banks and the Society

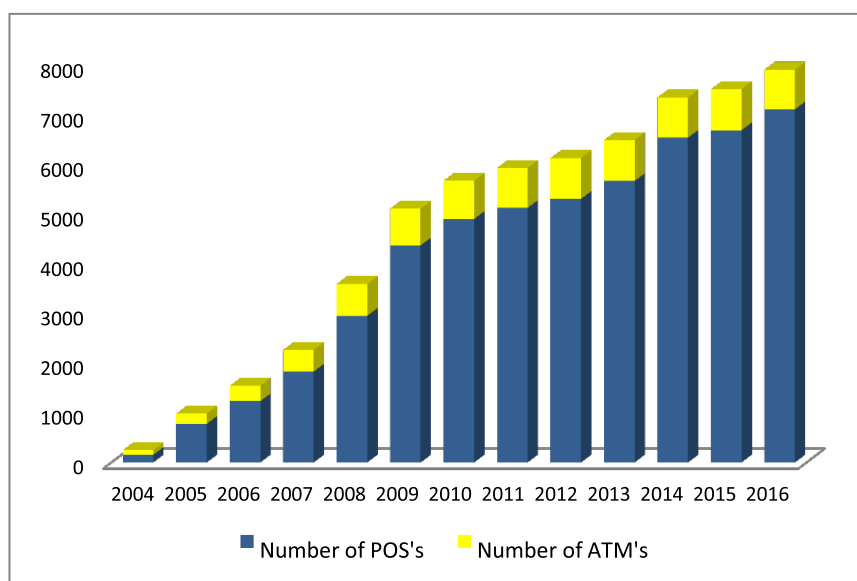
### 2.1 Financial intermediation as a public good

The process performed by banks which consists of accepting savings from a depositor and then lending or allocating these funds to a borrower, is recognised as financial intermediation. The banking business operates on the financial intermediation modality of financial institutions in the meaning that banks lend out money at relatively higher interest rates while receiving money on deposit at relatively lower interest rates. In theory, this is financial intermediation that in Albania, as well as in all economies worldwide, is considered to be an indispensable function of financial institutions supporting the economy and economic agents. There are many the cases indeed when financial intermediation is considered to be a public good because of its fundamental importance in boosting economic development and productive activities in the economy of a country.

#### 2.1.1 The contribution to the transposition from a cash economy to a non-cash economy

One of the main functions that the banking sector has performed outstandingly well in Albania is the shift from a cash economy to a non-cash economy at a relatively high pace during the period of study. The fast-increasing number of POS's in the economy throughout the country represents the best example of this transposition. Thus, the exponential increase in the number of POSs nationwide is the clearest example of the fundamental switch that costumers are making when it comes to payment instruments. Another element indicating the increasing role of banks in optimizing cash usage in the economy is the growing number of ATMs which, despite much lower in terms of numbers comparing to POS's, has also grown more than eight-fold.

Graph 14: Investing in new technologies by banks



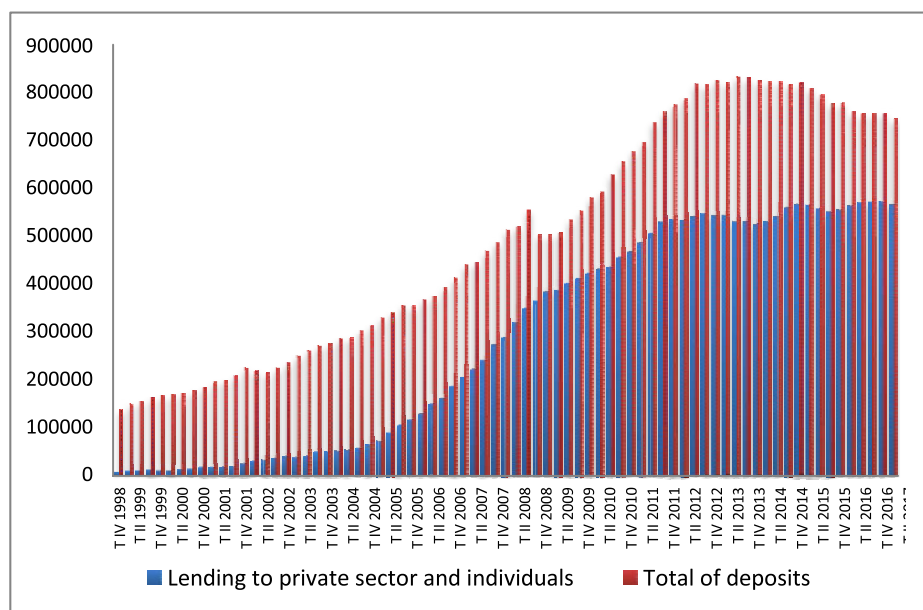
	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016
<b>Number of POS's</b>	155	779	1234	1832	2953	4370	4903	5126	5307	5668	6540	6689	7111
<b>Number of ATM's</b>	93	205	309	433	642	741	771	805	823	822	811	826	800

Source: Bank of Albania, Albanian Association of Banks

## 2.1.2 Deposits and loans

The financial crises turned banks more prudent in their lending activity in Albania and this is noticed from 2010 and onwards, while the debt crisis was followed by an increase of deposits levels, whereas loans to deposits ratio still remains lower than the 2009 peak in time.

Graph 15: Lending to private sector and individuals and total deposits in Albanian Banking sector

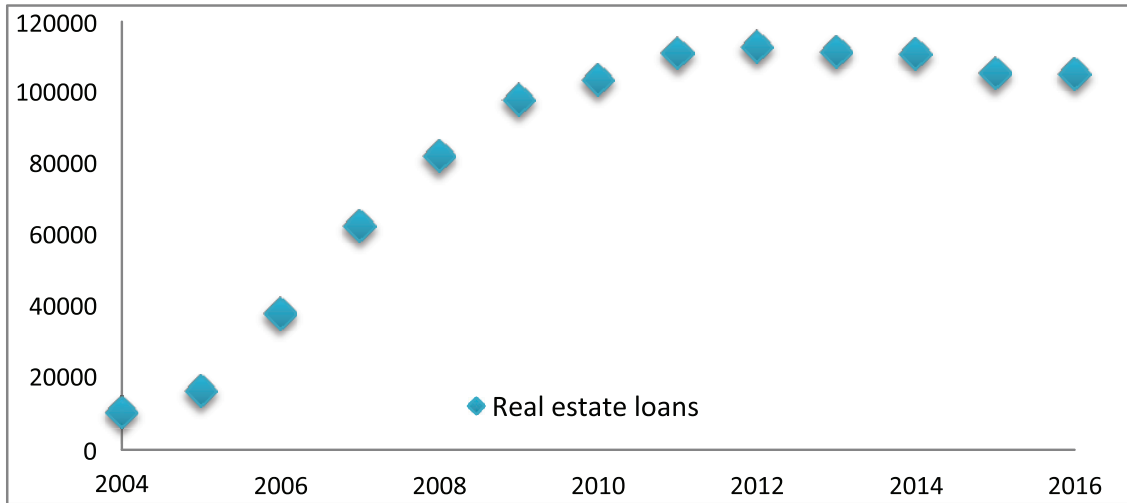


Source: Bank of Albania

## 2.1.3 Banks support citizens in purchasing real estate properties, Responsible risk management

Banks have been supportive toward economic agents in financing purchases of real estate and investments. However, from 2012 and onwards, the trend has lowered. The role of banks in facilitating the purchase of real estate properties in parallel contributes to the risk management, by allocating resources to economic agents, who are considered reliable for financing and having the proper financial characteristics of good borrowers in a long term aspect.

Graph 16: Real Estate aimed loans in support of private investment

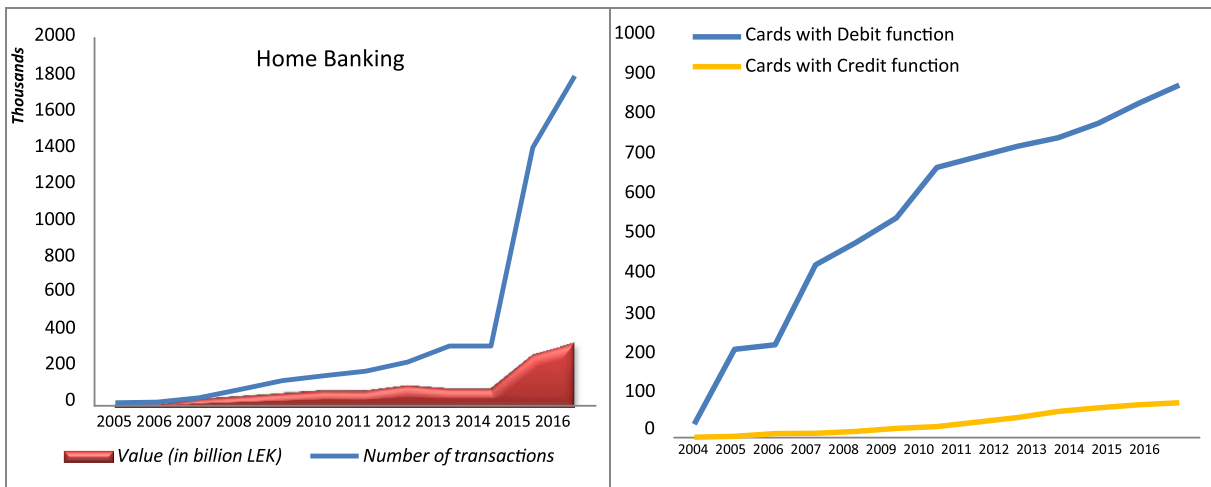


Source: Bank of Albania

### 2.1.4 The role of alternative channels development and modernization of the customers demand

2014 marked an impressive exponential growth of the home banking activity in terms of both number of transactions and value of total volume. Debit cards have become an indispensable mean for customers, who during the last two years have turned their attention towards home banking. On an overall picture, banks in Albania have served to develop alternative payment channels in response to costumers' needs, in synchrony with modern banking trends and the modern demands of Albanian clients in search for higher service standards.

Graph 17: Home banking, credit and debit cards transactions



Source: Bank of Albania, Albanian Association of Banks



## 2.1.5 Payments and other services provide efficiency to the society in its everyday activities

Banks' services to the society are multidimensional and, of course, one of the main services is the provision of the electronic payments system to costumers and citizens. The role of electronic payments in society is crucial in increasing the efficiency of payments execution, by saving time and costs. Different empirical studies show an increase of the level of spending for goods and services by the society, which is only due to the facilitation provided by electronic payment systems provided by banks. Consumption and economic growth are boosted while transaction costs are reduced due to the competition in the banking sector.

Households and other economic agents benefit from Electronic Payments in different ways:

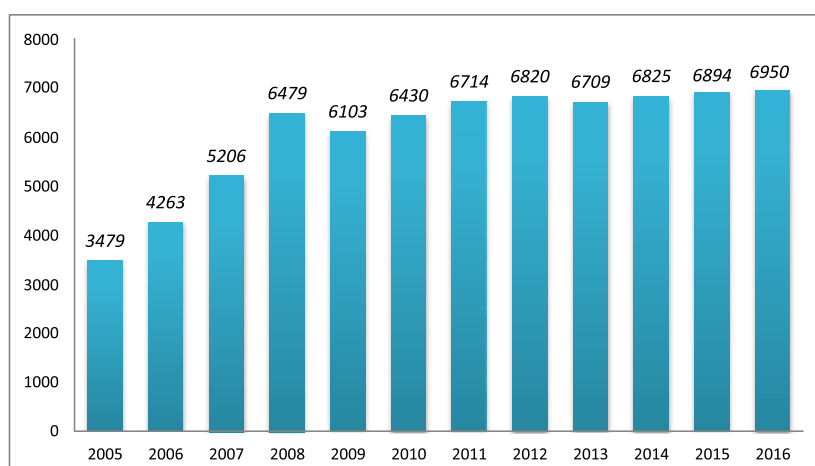
- Electronic payments provide access to financial resources.
- Access to credit helps calibrate periodic income with continuous consumption
- Cards provide consumers with the means to participate in digital economy.
- As electronic payments are safe, trust in electronic transactions further drives consumption.
- Debit and Credit cards provide convenience and lower business costs.
- Electronic payments reduce central bank costs in providing currency.
- Electronic transactions eliminate a substantial portion of the grey economy.

## 2.2 Employment and Social responsibility

### 2.2.1 Employment in the Banking sector

Employment numbers in the banking sector have fluctuated around the 2012 level, reflecting a prudent and consolidation period where banks are found during these last years. During the last decade, the number of employees in the banking sector has doubled and it is important to emphasize that also training and capacity building expenditures provided by banks for employees have grown substantially.

*Graph 18: Employment in the banking sector over the years*



Source: Albanian Association of Banks

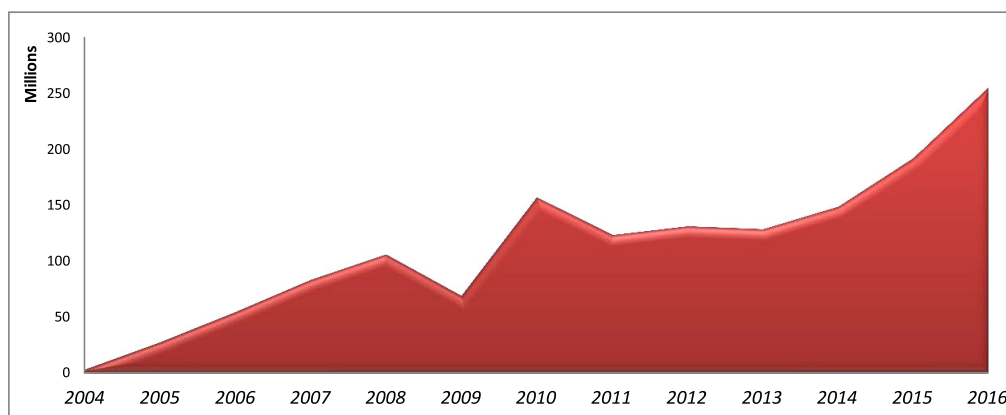
## 2.2.2 Banks' donations and sponsorships as per Social Corporate Responsibility

Banks in Albania have significantly contributed to the society following the UN 2030 Global Agenda for Sustainable Development.

The total Contribution during 2016 reached the significant total amount of 4.289.800 Euros, aimed at 15 from 17 Sustainable Development Goals. More concretely, for each of the goals would be:



Donations and sponsorships of banks to the society have kept growing during the period under analysis, as illustrated in the graph 19 below, featuring data obtained by the Albanian Association of Banks.



### 2.2.3 Banks and financial education.

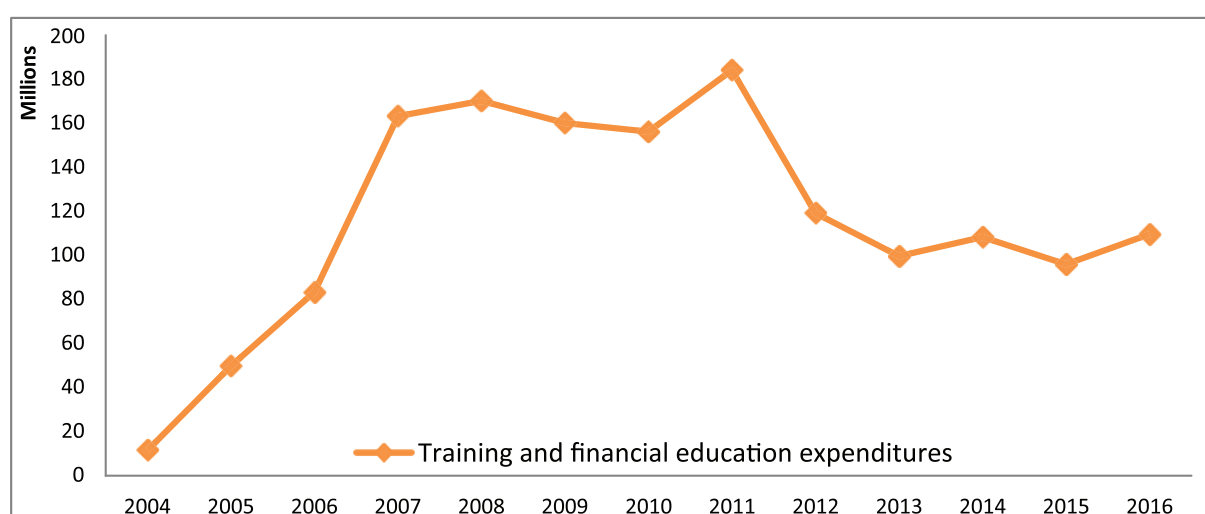
Financial Literacy remains a priority for banks in Albania, with AAB playing a key role in organizing and supporting financial education campaigns.

Innovative solutions facilitate easy access to education sources online for the general public.

Thanks to AAB cooperation with the Bank of Albania, the country joined the annual celebrations of the Global Money Week.

Training and financial education expenditures remained significant in terms of volume as a commitment of banks in building capacities in financial education.

Graph 19: Expenditures by banks for training and financial education



Source: Albanian Association of Banks

In 2016, the Albanian Association of Banks organized 23 training programmes. In this framework, AAB established sound cooperation with 12 national and international partners and more than 346 participants attended its activities.

The Albanian Association of Banks keeps growing in its mission to bring banks closer to the society and excellence in serving.

## 3. Development perspectives and Banking at a regional context under the Financial Sector lenses

Financial sectors in the Western Balkans are bank-centric:

- with relatively minor levels of capital market activity;
- negligible penetration of insurance products;
- generally insignificant non-bank financial institutions;

The banking sector is still dealing with the aftershocks of the global financial crisis that have weakened the financial sector asset quality and profitability.

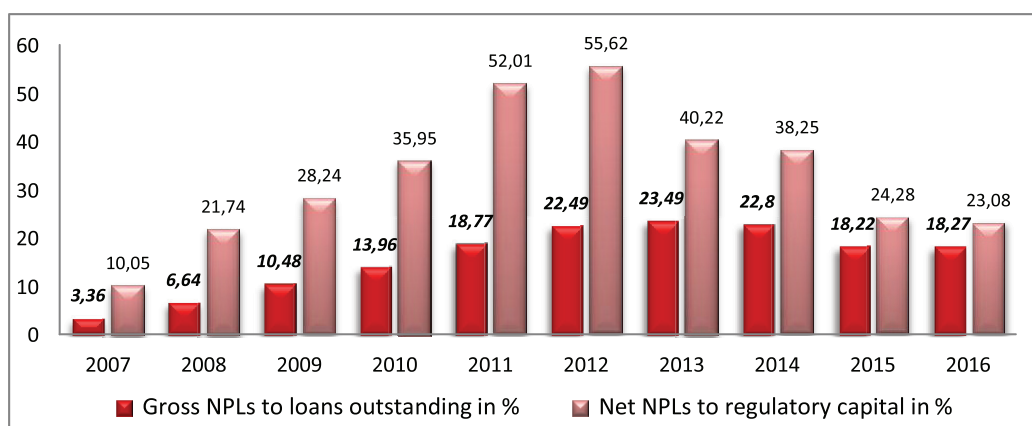
In particular SMEs, the backbone of Western Balkan economies, continue to have limited access to credit, which is associated with high cost and stringent conditions. SMEs suffer from structural capacity constraints and higher levels of informal transactions, reducing the quality of financial information.

### 3.1 Regulatory perspective and future development of banks business models

NPLs peaked in 2013, a time when sovereign debt crises effects started to get reflected in the Albanian economy on a considerable scale.

Due to a more prudent approach in their lending activity from the side of the banks and a package of measures introduced by the Bank of Albania, NPLs ratios have lowered onwards.

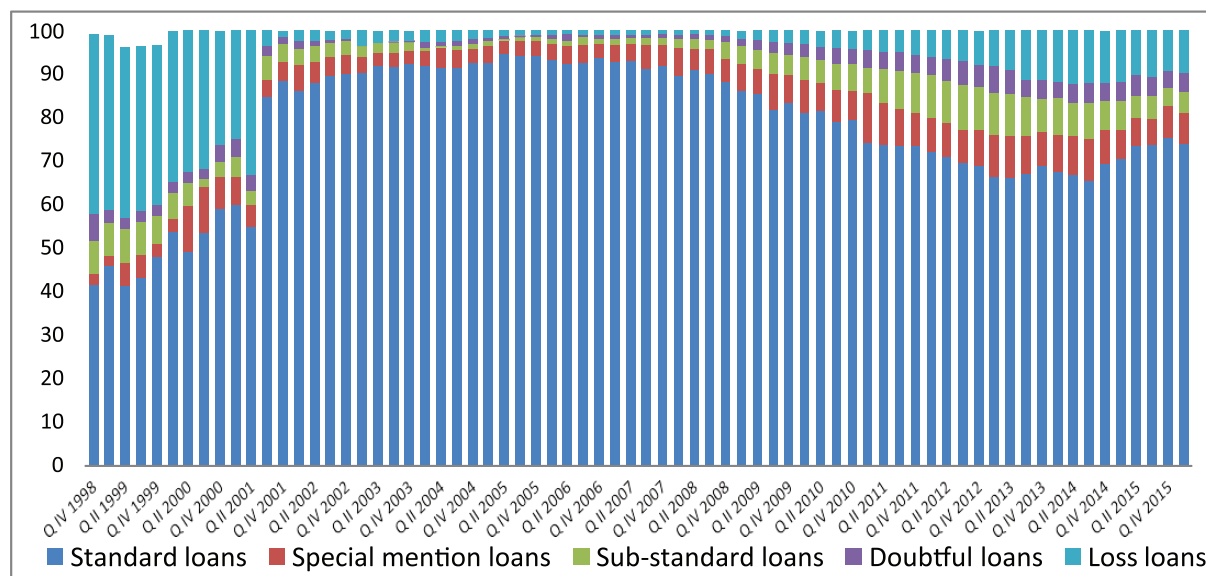
Graph 20: NPL's in the Albanian Banking sector



Source: Bank of Albania

The majority of NPLs in the Albanian banking sector consist of standard loans. However, since 2008, sub-standard and loss loans have grown in volume. Gross NPLs represent the outstanding amount of loans classified as sub-standard, doubtful, doubtful of loss, and loss, while Net NPLs represent the outstanding amount of gross NPLs, net of actual provisioning for the NPLs.

Graph 21: NPLs composition



The financial sector authorities across the region are making progress in strengthening the banking sector regulation and oversight. All supervisory agencies in the Western Balkans are moving towards risk-based supervisory regimes, as well as implementation of Basel II and Basel III requirements. Moreover, all have implemented International Financial Reporting Standards (IFRS) for banks. However, countries are at different stages of implementation. Further progress is needed in implementation of risk-based regulatory and supervisory practices as well as linking regulatory capital requirement to commercial banks' market and credit risk. Additional focus should be directed to the implementation of new standards, such as enhanced supervision of systemically important banks, and recovery and resolution planning. Regulation in the areas of corporate governance and identification of ultimate beneficiary owners and related-party lending should also be strengthened.

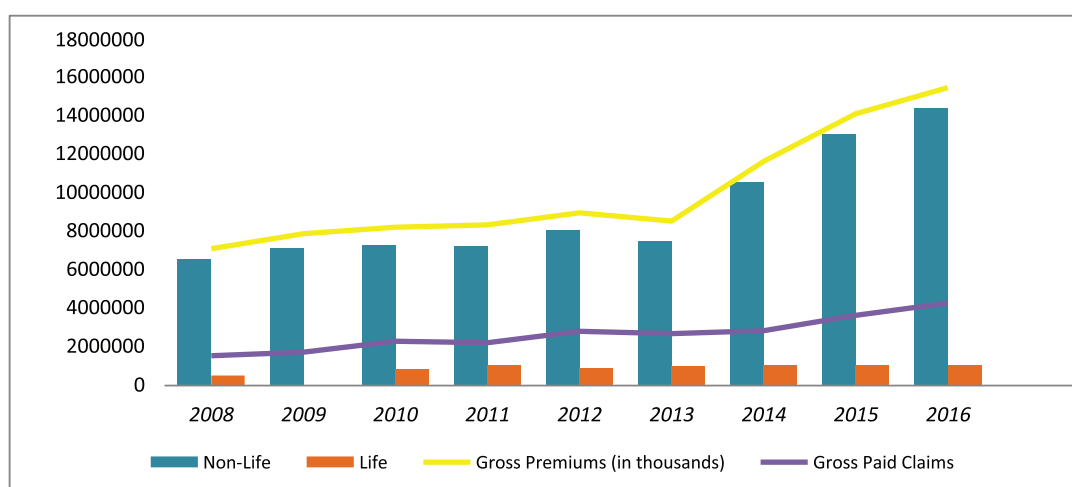
The main challenge for regulators across the Western Balkans is balancing the need for a stringent approach to supervising banks burdened with high levels of NPLs, while promoting debt restructuring for viable businesses. With the level of NPLs rising and economic growth feeble, supervisors need to find a balanced approach to incentivize banks to restructure viable borrowers, eliminate NPLs, and recapitalize if necessary. Supervisors need to enforce loan classification, realistic collateral valuation, and provisioning requirements more stringently. Rigorous enforcement, coupled with implementation of recapitalization plans where necessary, will encourage banks to resolve or write off problem loans more efficiently. However, until recently, regulators in most countries have offered some form of forbearance (for instance, on provisioning) in case of loan restructuring. This treatment may encourage banks to sustain viable borrowers, but could delay much needed balance sheet adjustment of troubled banks, while at the same time preventing lending to new borrowers.

### 3.2 Cross-impact of development of financial sector entities such as investment funds, further market exchange concepts and insurance

Insurance companies since 2013 have doubled their premiums collected, majority of them related to non-life insurance activity.

The increasing levels of Gross Paid Claims can be considered positive for the society. However, the gap between premiums collected remains high.

Graph 22: Insurance Sector in Albania



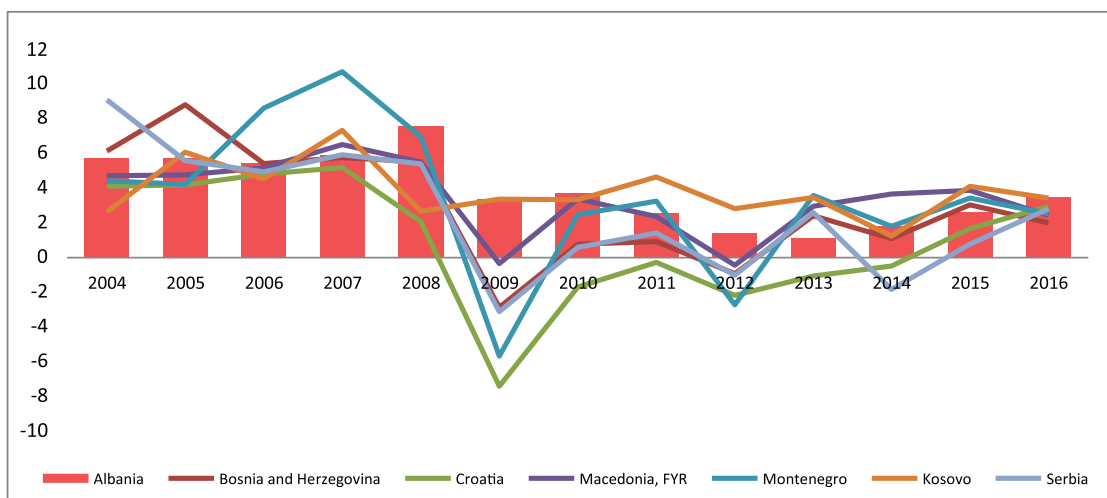
Source: Financial Supervision Authority

Pension Funds have also witnessed a high growth in terms of portfolio investments as well as membership. Thus, in 2016 pension funds totalled a portfolio of investments of 1.255 million ALL and 17317 members, of whom 9301 were women.

### 3.3 South-eastern Europe economic perspective and its impact

Albania keeps being one of the best performing economies In the South-eastern Europe. Its' economic growth is forecasted to average 4.1 percent of the GDP in the coming four years, an optimistic projection comparing to other neighbours. It is worth stressing that banks will be in support of productive activities to make this growth forecast be matched.

Graph 23: Economic Growth in South-eastern Europe in %



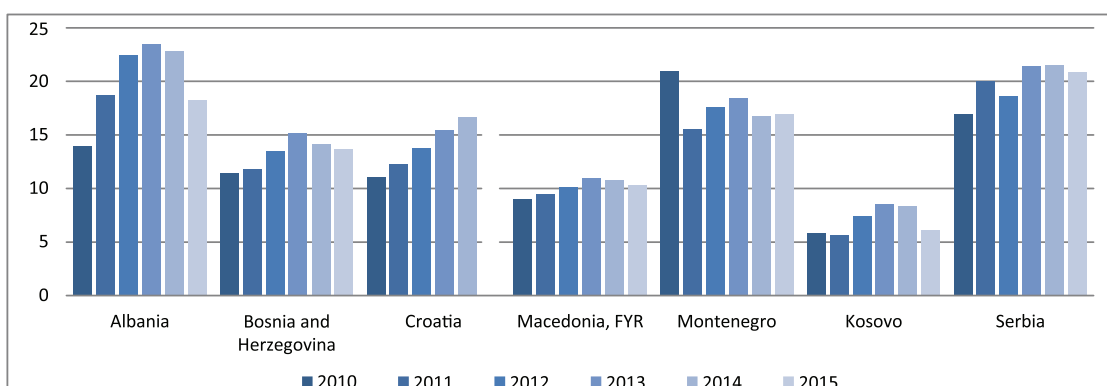
Source: World Bank

In 2014, Albania marked the highest level of NPLs in the region, reaching the peak of 23.39 %.

Kosovo and Macedonia have lower NPLs ratios compared to other banking sectors in the SEE Seven countries.

A similar path is seen in nonperforming loan levels in the SEE, reaching highs by 2013 to go lower in the following years.

Graph 24: NPLs in SEE Seven



Source: World Bank

## 4. Conclusions on economic and social impact

### 4.1 Key assumptions on economic and social impact of modern banking sector and comparison with current state in Albania

Banks in Albania exercise their activity in full synchrony with most updated trends in the banking industry. Modern banking sector in today's world has a structural crucial role for pooling savings and allocating resources to most productive economic agents.

Another paramount crucial factor for significantly contributing to the economy is the function of mitigating risks and enhancing fair competition.

Banks provide the private sector with highly qualified expertise and sound advice. Inducing optimal operational management in support of higher productivity.

Banks formalize the economy and play the role of fiscal agents, which is fundamental in contributing to reduce tax evasion, transaction costs by creating an enabling environment for business development.

### 4.2 Conclusions on the key critical impact and aspects of the importance of the Albanian banking sector to economy and society

Economic and Social impact of the banking sector in the Albanian economy is best illustrated by these concluding milestones:

- 3.1 percent of value added to GDP.
- Financing economic agents at the level of 40.5 percent of the country's GDP.
- 58.2 percent of total sovereign debt is held by 16 operating banks.
- Total lending to private sector and individuals has grown 8.8 times from 2004 to 2016.
- Banks' assets reaching 95 percent of the GDP.
- Total contribution of banking sector in taxes in 2016 peaked to 6.7 billion ALL.
- Albanian banking sector is profitable, well capitalized and liquid, by guaranteeing financing to economic activities.
- 6950 employees working in the banking sector nationwide.
- Banks support innovation by investing 3.3 billion ALL in new technologies in 2016.
- 4.530.000 Euros in support of sustainable development goals for the Albanian economy only during 2016.
- 1.5 billion ALL in sponsorships and donations for the society from 2004-'16.

During the last decade, the Banking Sector in Albania has turned into an indispensable factor for growth and development- duhet me bold si dhe në word for the country's economy and society.