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Theoretical Treatment of the Balance of Payments

Abstract

The balance of payments is constructed based on fundamental ideas and concepts to ensure consistent and standardized recording of economic transactions and other changes contained in it. The primary principles are:

1. Dual registration scheme

2. Guidelines for differentiating between resident and non-resident units

3. Transaction assessment

4. Timestamp of transactions recorded in this ledger.

Nevertheless, constraints in information sources often hinder the accurate recording of transactions in terms of timing and value.

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1. Introduction

The balance of payments is a statistical report that systematically describes a country's economic interactions with the rest of the world during a specific period. The main objective of the balance of payments is to enable the examination of the effects of transactions and other modifications in a nation's economy. The balance of payments is an integral component of the System of National Accounts (SNA).

The Balance of Payments statement details the origins and allocations of money. Any transaction resulting in a withdrawal of funds from a foreign country is classified as a source of capital, whereas any transaction leading to an outflow of funds to another country is classified as a usage.

The balance of payments encompasses transactions beyond only payments or collections. IN

Indeed, its activity encompasses economic actions where the transaction and the monthly liquidation are temporally distinct. This balance also includes transactions that may not involve any form of monetary settlement, such as assistance, barter amongst interconnected economic organizations, etc.

The international community is interested in the balance of payments because it indicates a country's transactions with the global economy. International users include important partners as well as international organizations, particularly those of which the country is a member. It is crucial to maintain consistency in the terminology, presentation, and structure of the balance of payments to meet both national and international interests. The International Monetary Fund has created the Balance of Payments Manual to guarantee consistency across its member countries. The first edition was published in 1948, and the most recent (sixth) edition was released in January 2010. Albania's balance of payments fundamental principles and classification framework are solely derived from the fifth edition of the International Monetary Fund manual.

This article aims to evaluate the Balance of Payments of Albania comprehensively, examining all its components to gain an analytical understanding of them and the variables that impact the Balance of Payments' evolution over time. A comparison analysis has been conducted with certain countries in the region to achieve this.

2. Materials and Methods

2.1. Dual registration

Under the double registration system, every transaction needs to be recorded twice with equal values, one as a credit (positive) and the other as a debit (negative). The whole sum of credit entries must be equal to the total sum of debit entries, resulting in a net balance of zero. Information is typically gathered from many sources, and estimations are used where data is lacking. The total of debit and credit amounts might lead to a final credit or debit balance. To balance the accounts, this amount is intentionally recorded with the opposite sign in the "Net Errors and Omissions" category.

The double registration system records the following in credits: 1. The export of commodities and services generates active income. 2. Financial items leading to a decrease in a country's international financial assets or a rise in foreign liabilities. Similarly, debit records include: 1. imports of goods and services; 2. payable income (passive income); and 3. transactions indicating an increase in foreign financial assets or a decrease in foreign liabilities. Entries in this system are displayed in pairs with matching debits and credits. For instance, in an export transaction where payment was processed via the banking system, it leads to a credit entry for the export and a debit entry for the rise in foreign currency. Repaying a loan through the banking system involves a debit entry to decrease liabilities and a credit entry to decrease foreign assets.

Transactions that cannot be automatically matched necessitate the input of a distinct balancing item. This component is essential for unilateral transfers, which refer to material and financial aid that one government receives from another.

2.1.1. Residents

The balance of payments concerns the financial transactions between a country's residents and non-residents. It is essential to establish a clear distinction between residents and non-residents within an economy. The notions of economic region and center of economic interest are utilized as a "measure" to determine residency.

An institutional unit is deemed a resident of a country when its primary economic activities are located within the economic boundaries of that country.

The economic territory of a country refers to the geographical area under the government's administration where people, products, and capital move without restrictions. The economic boundaries may not necessarily align with the geographical boundaries.

An entity establishes a Center of Economic Interest in a country by having a headquarters, production facility, or other premises within the country's economic territory where it conducts significant economic activities and transactions for an indefinite or long period of time.

2.1.2. ASSESSMENT

The manual suggests using the market price as a standard unit for assessing the balance of payment transactions. This price is the monetary value agreed upon between a willing buyer and a willing seller based only on business factors.

The price documented in accounts or trade reports is often the market price or a close approximation of it. The transaction price is an estimate employed in practice due to its close approach to the ideal market estimate.

Transfers or borrowing arrangements between interdependent firms may result in transactions being valued at prices that deviate from market pricing due to their unique connections. These examples deviate from the market price principle.

Albania's balance of payments transactions are reported in USD. This assessment necessitates converting all transactions from Lek or other currencies to USD using the prevailing market rate at the time of the transaction.

The rate utilized in practice varies based on the source of the transaction data and recording processes.

2.1.3. Registration time

It is crucial that both parties involved in a transaction are accounted for simultaneously in the balance of payments, which can be determined utilizing several data sources. Similarly, various transactions should be documented using a standardized and consistent method of capturing timestamps.

The current Manual of the International Monetary Fund recommends that transactions in the balance of payments methodology should be registered at the moment of the change of ownership. Transactions are recorded in the current account at the moment when there is a change in legal possession of the goods.

• service performance

• Generating reinvested earnings for direct investors

• maturation of interests and dividends

For transfers without compensation like taxes and penalties, registration occurs when they are due. For other transfers, registration happens when ownership of goods changes hands or services are provided.

Ownership transfer for capital account transactions is recognized as occurring at the time when the transactions are officially recorded in the transactors' books. Registrations for loan withdrawals should be based on the actual disbursement, not on the agreement or authorization. Repayment registrations should be submitted when the loans mature, not on the date of payment.

2.1.4. Economic transactions included in the Balance of Payments.

The balance of payments encompasses all economic transactions, not just payments. An economic transaction takes place when ownership of economic value is transferred.

The transactions in the balance of payments mostly result from contact between a resident and a non-resident party. It is important to mention that the persons involved in the transactions, obligations, and foreign financial instruments can be either residents or non-residents. These transactions will only be included in the balance of payments if they involve the transfer of claims or obligations between parties that are classified differently for statistical purposes.

The balance of payments includes several forms of transactions and other adjustments.

a) Transactions

Exchanges are regarded as the most crucial and abundant transactions in the balance of payments. This group comprises transactions in which one party offers an economic value to another party and receives an equivalent value in return. Economic values are primarily classified as tangible resources (goods, services, and income) and financial assets. Parties involved in the transaction are residents of different economies, unless they are exchanging foreign financial instruments within the same economy.

c) Transfers

Transfer transactions include one party giving economic value to another party without receiving the same value in return, distinguishing them from exchanges. The economic value that is not accounted for in one part of the transaction is reflected on the balance sheet by being recorded under the item "Transfers," in adherence to the double-entry accounting system.

Migrant transfers are a unique form of unpaid transfer. A migrant who changes their residency status undergoes a unique statistical analysis. Migration happens when a person's place of living shifts from one economy to another due to a change of residence. When this transformation happens, the migrant's property in the old economy (their nation of origin) becomes a liability of the new economy towards the old economy. The claims and duties of a migrant towards the residents of one economy are transferred to the next economy. Responsibilities and commitments of the migrant towards inhabitants of the new economy transform into responsibilities and commitments among residents of the same economy. The agreed-upon net worth of the aforementioned adjustments is documented in unilateral transfers. In theory, these transactions involve the property, obligations, and claims of migrants, but in fact, it is better to merely document monetary transfers. When a person relocates, any cash they bring with them is documented as a rise in foreign currency (debt) and as a unilateral transfer (credit).

Simulated transactions

Transactions can be mimicked without actual items being exchanged in certain situations. An example is when profits are reinvested in foreign direct investment firms for the benefit of foreign investors. Reinvested profits are accounted for in foreign direct investment income. Simultaneously, a corresponding entry is made in the financial account under the direct investment category to represent the growth in the investor's direct investment in the company.

2.1.5. Classification used in the Albanian Balance of Payments.

The primary categorization used for the balance of payments involves categorizing data into the current account and the capital and financial account. Special transactions are traditionally included in one account or the other to some extent. The current account consists of irreversible transactions, while the capital and financial accounts record reversible transactions involving liabilities and foreign financial instruments.

2.1.6. Current account

The current account encompasses all exchanges between Albanian residents and non-residents, including products, services, income, and unilateral transfers.

(a) Commodities (as per trade balance)

This category pertains to moveable items that change ownership from residents to non-residents (exports) and vice versa from non-residents to residents (imports), with some exceptions.

Services

This category pertains to services offered by residents to non-residents (credit) and by non-residents to residents (debit). This category also encompasses a small portion of transactions involving commodities that are inseparable from the accompanying services, such as goods bought by visitors. The services are categorized into the following groups:

• Transportation services • insurance services

• Travel services; • Other services

Income

This category covers income received either from non-residents (credit) or from residents (debit). This item is subdivided as follows:

• Earnings from employment; • Profits from investments

(d) Current transfers

Current transfers are accounting entries used to record changes in ownership of tangible assets (goods or services) between residents and non-residents without any accompanying payment. Current transfers are categorized as state aid from abroad, delivery from overseas, and others.

2.1.7. Capital and financial account

The capital and financial account is comprised of two sections: the capital account and the financial account.

The capital account deals with capital transfers and transactions involving non-physical, non-financial assets.

A capital transfer involves transferring ownership of a fixed asset or releasing a debtor from an obligation. These transfers are balance entries made when ownership of financial assets shifts between residents and non-residents without any accompanying payment.

The financial account pertains to transactions involving Albania's international assets and obligations. The registrations are categorized based on the following criteria:

• Investment direction

• Investment vehicle

The primary classifications of the financial account, liabilities and assets, indicate the orientation of investments. Within liabilities, for example, Capital investments refer to foreign investments in Albania and Albanian investments abroad. Capital inflows to Albania are categorized as liabilities, whereas capital outflows from Albania are categorized as assets.

Within the financial account, capital flows are categorized as direct investments, portfolio investments, and other investments under the principal assets and liabilities items.

2.1.8. reserves

Since the gold standard era (Bretton Woods), when the focus was on monetary gold, attention has shifted to various other forms of state foreign exchange reserves. It has been deemed appropriate for the balance of payments to specifically reflect components considered foreign currency reserves by monetary authorities, used to address balance of payments requirements. The Balance of Payments Manual defines reserves as foreign financial assets that fall under the control of a nation's monetary authorities and are available for addressing international payment imbalances, intervening in foreign exchange markets, and other uses. The Reserve Assets category includes monetary gold, SDR, reserve positions in the fund, foreign exchange, and other claims.

The International Monetary Fund utilizes the following equation:

$$\textit{Balance of payments} = \textit{Current account} - \textit{Capital and financial account} \pm \textit{Net errors and omissions}$$

3. Results

3.1. The stability of the current account in Albania

Albania's current account has been consistently in deficit since the early 1990s. The experts have determined that the current account deficit in Albania is generally constant by analyzing the theoretical and practical factors. The ongoing decline in trade could seriously jeopardize the delicate stability. The authorities need to focus on the current account deficit by implementing structural improvements, economic policy adjustments, and incentives to enhance competitiveness. The main focus of the efforts should be to reduce the expansion of the trade imbalance.

Substantial trade imbalances in goods are the primary factors contributing to current account deficits. Albania's trade balance has shown an increasing deficit since the start of the transition period. The deficits are caused by the sluggish export performance, which accounts for an average of 7% of GDP, and the increasing increase of imports, estimated at approximately 30% of GDP. The results indicate a clear difficulty regarding the competitiveness of Albanian exports and the significant growth of consumption due to several structural problems. Based on the trade figures from the Bank of Albania, around 37% of imports are consumer items, with the remainder being made up of capital and intermediate commodities. This distribution provides insights into Albania's capacity to enhance investments and stimulate long-term economic growth. An analysis of the import components shows a significantly greater proportion allocated to consumption compared to other uses of imports, raising doubts about the sustainability of the current account.

There are multiple methods to evaluate your existing account. The current account, in terms of national accounts, signifies the disparity between Albanian savings and investments. As previously mentioned, these two components can provide crucial indicators of the integrity of the current account. The analysis of the external imbalance in savings and investments reveals that rising current account deficits correspond to concurrent increases in the average rates of investments and savings. Thus, the lack of a distinct pattern in savings and investments, coupled with a reduced fiscal deficit, complicates the evaluation of the sustainability features of the current account.

However, the potential drawback of heavily depending on capital inflows to address the current account deficit is the danger of these inflows leading to actual exchange rate appreciation. Capital inflows have a greater impact on the currency rate because of the significant foreign cash flows from Albanian immigrants in the form of remittances transferred to Albania. Remittances experienced a notable rise at the start of the transition and have now leveled out at approximately 11% of GDP. An undervaluation of the local currency's exchange rate has been seen in recent months. This is beneficial for boosting exports, and the economy should capitalize on this opportunity to enhance its export sector.

The country's huge external debt burden is another significant element that exacerbates the sustainability of the existing deficit. Approximately 60% of the GDP is the entire state debt, with 23% of the GDP being external debt, which rose in 2009.

It is challenging to pinpoint a specific item or element in the current account that can potentially transform trade deficits into surpluses.

3.2. Analysis of the Balance of Payments in Albania and the Balkans

3.2.1. Balance of payments fluctuations over the years

From 1996 to 2006, Albania's current account deficit averaged around 300 million euros a year, reaching its lowest point in 1996 and its peak in 2005. Excluding 1997, the current account deficit as a percentage of GDP varied around 4% for the initial five-year period and approximately 8% for the subsequent five-year period. In 1997, the trade deficit rose due to a decline in incoming current transfers, resulting in the current deficit increasing three times compared to the previous year. The current deficit surged from 2% to 11% of GDP. Between 2007 and 2008, the current deficit increased dramatically, reaching nominal numbers around 3–4 times higher than the average of the preceding years. The current deficit as a proportion of GDP climbed by around 4 percentage points in each of the two years, reaching 10.6% and 15.5%, respectively.

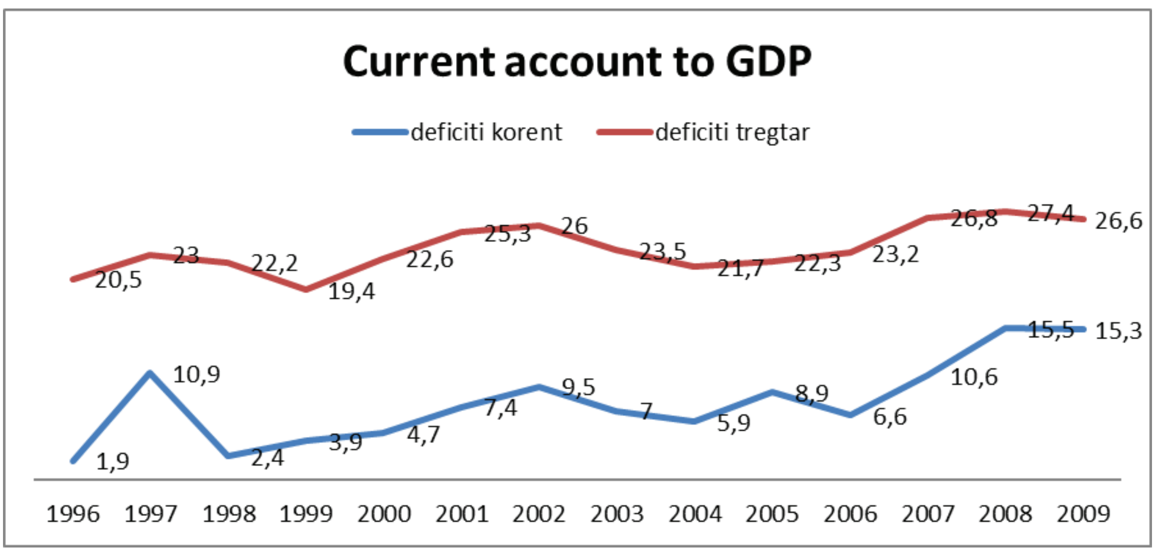


Figure 1 – Chart of current account against GDP

The capital and financial accounts developed in the opposite direction from 1996 to 2008, mirroring the increase in the current deficit. Foreign investments, capital transfers, and borrowing from abroad have completely funded the current deficit and also boosted the country's foreign exchange reserves by approximately 2.5% of GDP each year throughout this period. By the end of 2008, reserve balances amounted to 1.7 billion euros, which was adequate to finance 4.2 months of imports of goods and services. The balance item "net errors and omissions" frequently displays significant amounts comparable to the change in reserve assets, primarily as a result of data reporting issues and unrecorded operations.

Albania's balance of payments has consistently shown a merchandise trade imbalance, which has been the primary cause of the current account deficit for many years. Between 1996 and 2008, the merchandise trade deficit rose from 500 million euros to 2,400 million euros, representing an increase from 20% to 28% of GDP. The trade deficit expanded quickly, particularly in the years 2000–2001 and 2005–2008. Imports have consistently exceeded exports over this period. The ratio reached its lowest point between 2000 and 2002, at approximately 23-24%. The ratio has been steadily increasing over the past 4–5 years, reaching 27.4% in 2008. The substantial disparity in the values of imports and exports, along with their respective growth rates over the years, has led to a widening of the goods deficit. Trade balances by commodity groupings show deficits in nearly all categories, with deficits increasing year over year. The surge in merchandise imports is driven by the increasing demand for investment and consumption from both the governmental and private sectors.

The consistent growth of the trade deficit in goods has had a detrimental impact on the country's external situation, placing strain on the ongoing increase of the current deficit. The primary funding for the trade imbalance in the current account has come from current transfers, ranging in value from 300 to 1000 million euros, or 10% to 18% of GDP. The services account and the income account have typically been in equilibrium or shown slight surpluses. Current transfers primarily comprise remittances from Albanian emigrants, predominantly situated in Europe. Between 2000 and 2007, inward current transfers showed significant and positive growth rates in nominal terms. The ratio of net current transfers to GDP varied between 14 and 15% from 2000 onwards, dropping to around 11% in 2008.

When examining Albania's global transactions, it is important to highlight the services sector's performance. Despite occasional slight surpluses or deficits over the past 11 years, the total volume of incoming and departing service transactions has been significant and on pace with the trade activity of products. Income and expenses for services during this period accounted for around 70–80% of the volume of goods traded. Starting in 1999, revenues and expenditures for services have consistently grown by over 20% annually, reaching transaction volumes of 2.4, 2.8, and 3.3 billion euros in 2006, 2007, and 2008.

Services have shown strong competition with products in exports, in addition to their high yearly growth rates. Over the past decade, Albania has generated approximately twice as much revenue from exports of services as from exports of products. Travel, transportation, communication, and business services are the most significant categories within the services sector.

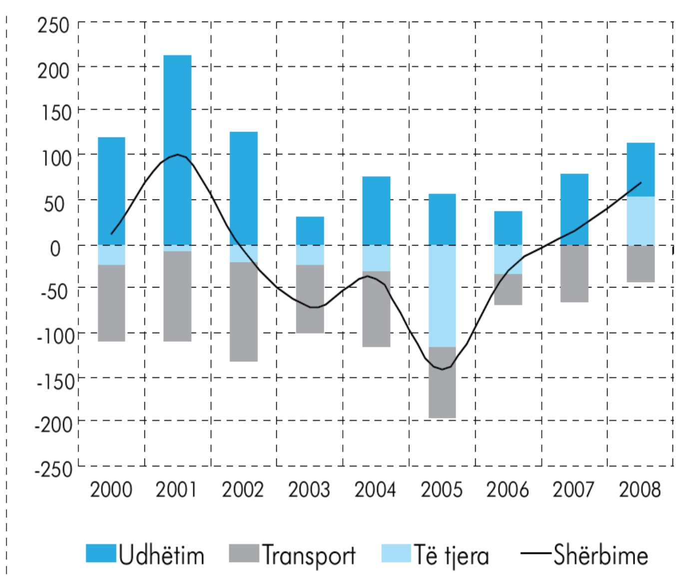


Figure 2 - The graph of the balance of services for the years 2000-2008 (in million euros)

Direct investment and capital transfers have been the primary drivers of changes in the capital and financial accounts for the majority of the last ten years. The other investments primarily included public and private borrowing as well as commercial loans. Privatizing state-owned firms has greatly increased the influx of foreign cash into the country, especially in the initial years of the transition. Over the past 4-5 years, these inputs have accounted for a smaller portion of total input investments. The gross external debt was anticipated to be 2.6 billion euros by the end of 2008. State borrowing constitutes

70% of resident debt commitments, primarily in the form of long-term borrowing. Approximately half of these debts are attributed to the general government, while the remaining portion is split between the banking system and other sectors of the economy, accounting for 30% and 20% of the total, respectively.

3.2.2. Progress of the Balance of Payments during the years 2008-2009.

The challenges experienced by the global economy and financial markets in 2008 have impacted and been mirrored in the external status of numerous countries and economic areas. The extent and impact of external shocks vary based on the current and capital flows, as well as the external sector's proportion in each country's economy. Countries that experienced the most pronounced effects of the global crisis on their balance of payments were those with high levels of international openness and those that relied on quick and short-term capital inflows to sustain their recent rapid growth. The group of developing countries in Central Europe, Southern and South-Eastern Europe, as well as the Baltic countries, are particularly impacted by these trends. Decreasing export markets in European developed countries, reduced capital inflows, and uncertainty about capital outflows or returns, along with negative effects in countries with unstable exchange rates, have resulted in declining balances in current and capital accounts for most of these countries. Nations with limited receptivity to short-term money from Western nations have experienced the repercussions of the global crisis through reduced foreign direct investment and a deceleration or decrease in remittances from immigrants. Several developed and developing countries urgently require support in the form of funding from the International Monetary Fund due to the concerns described above.

The years 2008–2009 were marked by significant global economic events that impacted the Albanian economy. We will conduct a thorough review of all components of the balance of payments to track its progress during this period.

Table 1 - Main indicators of the Balance of Payments

	Million Euros			To the GDP		
	2007	2008	2009	2007	2008	2009
Current account	-831.0	-1370.3	-1327.0	-10.6	-15.5	-15.3
Trade balance (goods)	-2104.0	-2431.5	-2303.7	-26.8	-27.4	-26.6
- export	786.0	917.5	750.7	9.9	10.4	8.9
-import	-2890	-3348.9	-3054.4	-36.8	-37.8	-35.3
Services	12.0	69.4	120.9	0.2	0.8	1.4
Net income	217.0	54.9	-78.7	2.8	0.6	-0.9
Current transfers (net)	1043.0	936.8	934.5	13.3	10.6	10.8
Capital and financial account	848.4	1580.9	1018.2	10.9	17.8	11.8
Errors and omissions	131.2	-18.7	273.7	1.7	-0.2	3.2
Overall balance	149.0	191.9	-32.0	1.9	2.2	-0.4

3.2.3. Current account

In 2008, the Albanian economy's foreign sector showed a deficit in the current account and a surplus in the capital and financial accounts based on balance of payments transactions. In 2008, the current account saw a rise in both income and expenses. In 2008, the year concluded with a deficit of 1.3 billion euros, which was 60% larger than the previous year. An increase of around 330 million euros in the trade deficit, a loss of 160 million euros in the income surplus, and a fall of 106 million euros in the surplus of current transfers have collectively led to the widening of the deficit by almost 540 million euros. The services category surplus has significantly improved, increasing from 12 million euros to 70 million euros compared to a year before.

In 2009, the current account deficit decreased by around 3% due to a decrease in domestic demand and challenging global economic conditions. The Albanian economy's focus on imports led to a reduction in the balance of payments deficit due to changes in the external sector structure. Decreased external demand led to a drop in exports, even if the exchange rate was dropping. However, the negative net income and decrease in remittances were offset by the significant growth in the service account surplus, leading to a slight decrease in the current account deficit.

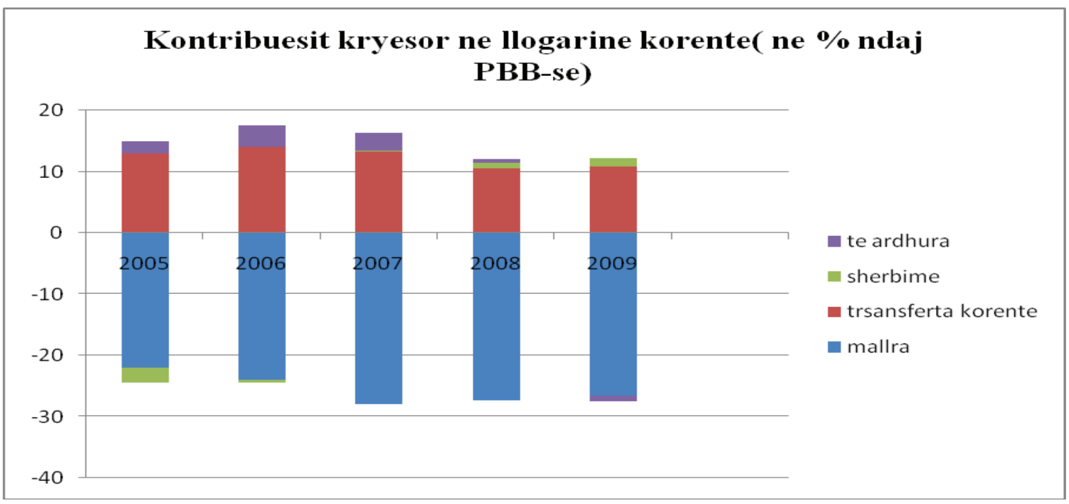


Figure 3 – Main contributors to the current account

3.2.4. Trade in goods

Goods commerce remained the primary component of the current account, making up approximately 45% of current transactions. In 2008, goods imports totaled approximately 3.3 billion euros, and exports amounted to around 900 million euros. Exports have also shown a good annual rise of 16–17%, similar to imports. The current rates are notably lower than those from a year ago and similar to the growth rate in 2006. The import-export coverage ratio has stayed stable at 27.4% compared to the last two years.

In 2008, the metals commodity category experienced the most significant growth. Exports from the extractive and processing industrial sectors rose by 18% compared to the previous year. Exports of agricultural products, primarily focused on processed meat and fish products, along with oilseeds, experienced a modest rise in 2008.

The import categories with the most significant annual growth in 2008 were "fuel," "machinery and equipment," "chemical products," and "processed goods." The majority of the overall import value was attributed to the category of "processed goods" (24%), with the category of "machinery and equipment" following closely behind (22%).

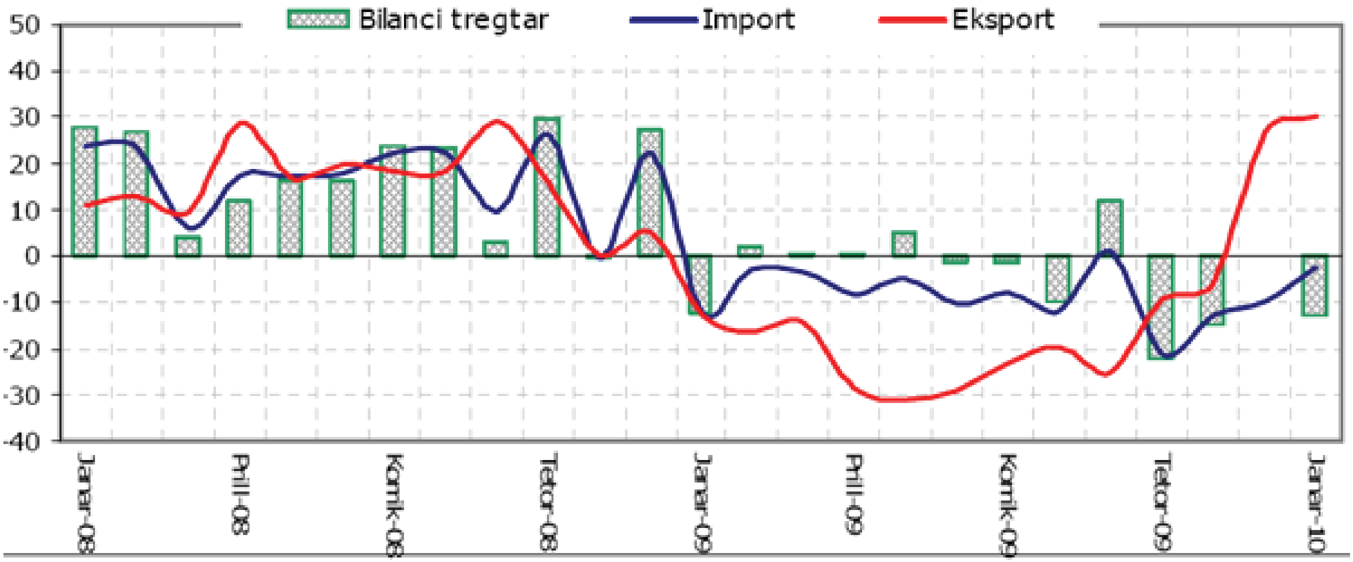


Figure 4 – Trade balance chart

In 2009, our country experienced a decrease in external commercial activity due to the worsening economic indicators of our main trading partners. The economy's level of openness was calculated at 46.2% of GDP, which is 4.5 percentage points lower than the previous year. The import-to-export coverage ratio has fallen by 2.6% compared to 2008.

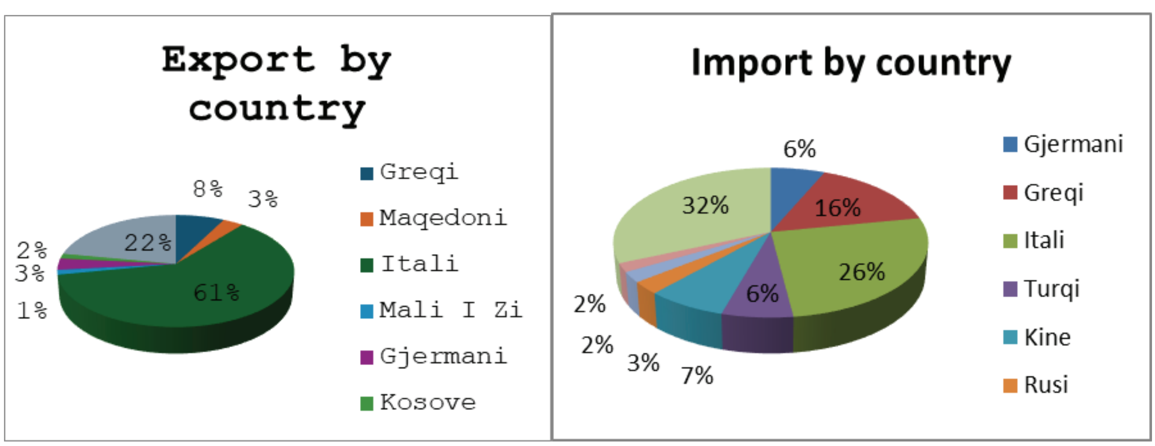


Figure 5 – Exp/Imp by country

Albania's foreign trade in products shows a low level of geographic diversification when considering the significance of various nations in its export and import activities. Italy and Greece engage in the majority of foreign trade. Italy's exports account for 61% of the total, while Greece's exports make up 8%. Our country imports 26% of its goods from Italy and 16% from Greece. Albania's exports are not well diversified, which renders them very susceptible to changes in its primary trading partners. While the global economy saw signs of recovery in the latter part of 2009, the economies of our primary allies, Greece and Italy, did not progress in a similar manner. The concentration of our country's exports to these nations negatively affected export progress in 2009. Greece purchased 7.6 billion ALL worth of goods from Albania this year, which is a 23% decline from the 9.9 billion ALL purchased the previous year. The weakening of the local currency compared to the common European currency is expected to have minimal effect on the growth of our exports due to decreasing international demand. Goods exports declined by around 18% over the previous year, while imports decreased by 9%.

Albania has limited product diversification in its commerce, making it vulnerable to internal and external factors that impact specific manufacturing activities or the trading of certain categories of goods.

The decline in foreign demand has a greater impact on the industrial sector's productivity. The primary export categories that led to this decrease in value were "raw materials and minerals," "processed goods," and "other processed goods," which accounted for approximately 76% of total exports in 2009. Exports in 2009 decreased by 18%, according to the research.

Table 2 – Export by commodity

Export	Food and live animals	Drink and smoke	Raw materials	Fuel	Processed goods	Machinery and equipment	Other processed goods	Chemical products	TOTAL
2008	424.62	2.62	108.31	81.88	232.30	149.90	411.57	10.35	917.5
2009	35.96	3.41	81.16	90.75	136.58	34.80	355.55	12.58	750.7

The combination of low pricing in the countries of origin and a decrease in domestic demand has helped offset the devaluation of the currency rate, resulting in a decline in the value of imports. In 2009, the decline in yearly imports was due to a 12.7% reduction in imports of "capital goods" and a 12% reduction in imports of "intermediate goods."

Table 3 – Import by goods

Import	Live foods and animals	Drink and smoke	Raw materials	Fuel	Processed goods	Machinery and equipment	Other processed goods	Chemical products	Total
2008	424.62	112.79	74.41	573.61	848.55	783.76	354.15	346.7	3348.9
2009	395.12	123.8	95.7	382.57	811.89	741.92	296.03	362.55	3054.4

3.2.5. Trade in services

Foreign trade contacts in the services sector have become a prominent feature in Albania's commercial interactions with other countries, contributing to the nation's development and global integration. Over the past five years, the yearly average growth rate of trade in services has been approximately 19%, surpassing the average growth rate of trade in goods, which has been 17%. In 2008, the net export of services was approximately 70 million euros, showing substantial growth from the previous year. Throughout the year, revenue generated from service exports increased at a quicker rate than spending on service imports. The enhancement of the net services position is primarily due to a substantial rise in income in the "other services" sector and the growth of the surplus in the "travel" sector, which has completely offset the deficit in transport and insurance services. In 2009, the net services balance increased by approximately 51.5 million euros compared to 2008, continuing its rising trend for the fourth year in a row.

The services sector's dynamics, marked by market liberalization, technological advancements in information services, diverse cultural services, and growing financial services, have demonstrated the sector's potential in global markets. The "travel" category continues to be the primary item in the service trade for Albania, encompassing the services received and given. Travel services are currently the primary source of foreign exchange flows for the Albanian economy.

3.2.6. Income

In 2008, the positive factor income balance of around 110 million euros decreased by 50% compared to the previous year. A significant increase in outflows from the balance of payments has offset the increase in foreign currency revenues, resulting in a decrease in the surplus from the previous year. Residents' foreign investment income decreased by around 17%, primarily due to a drop in the banking system's earnings from foreign financial institution securities. The moves led to an inflow of factorial income estimated at approximately 320 million euros, showing an annual growth rate of 14%. The outflow of factorial income amounted to 210 million euros, which is three times greater than the previous year. The rise in outflows is due to the growth in income outflows from profit or dividends received from non-resident units and overseas investors, as well as from income outflows from portfolio assets.

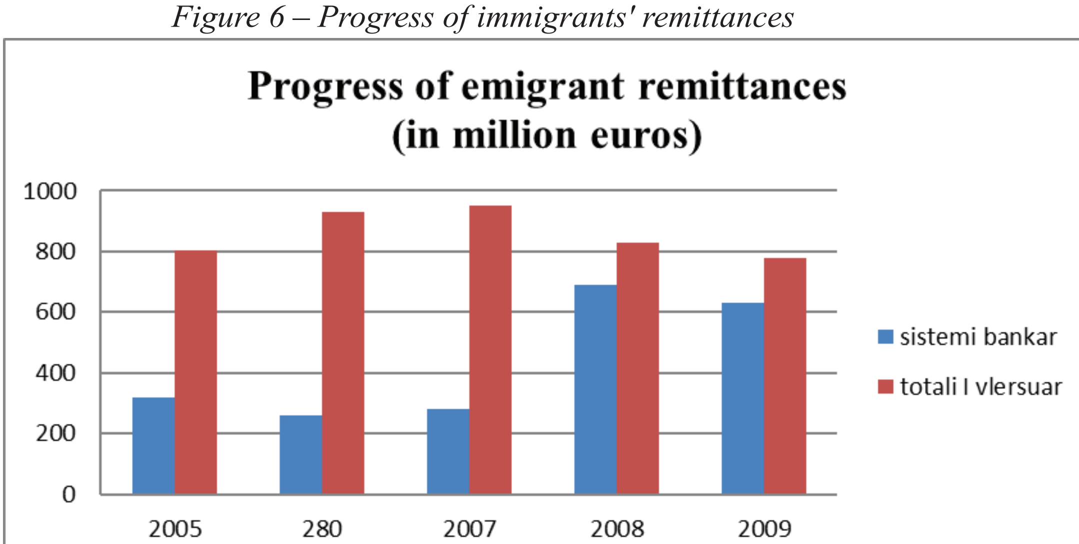
In 2009, we observed a shortfall in the net income account, mostly caused by the negative balance in the "investment income" category, surpassing the foreign currency inflows from income earned abroad.

3.2.7. Current transfers

Current transfers fully funded the current account deficit until 2007, but in the past 3 years, they only partially offset it.

The net current transfers in 2008 were approximately 940 million euros. The latter represented a 12% decline from the previous year's value of 950 million euros, with 830 million euros being remittances from immigrants. Indeed, a substantial portion of the present transfers consist of remittances from immigrants. Immigrant income is a significant source of livelihood for many Albanian households and has played a crucial role in the country's balance of payments and financing of current expenses since the early 1990s. The economic downturn in European countries, the USA, and other nations where Albanian immigrants reside is believed to have impacted the decrease in foreign exchange flows. These flows decreased by 12% in 2008 and further declined by 6.5% in 2009.

Figure 6 – Progress of immigrants' remittances



Estimated Total = Banking System + Transfer Agency

3.2.8. Capital and financial account

In 2008, the capital and financial accounts increased by around 80%; however, in 2009, they decreased by 50%, as shown in the graph.

In 2009, the capital and financial accounts experienced a decrease in surplus compared to 2008. The net flow in the capital and financial accounts was 1.02 billion euros, which is 562.7 million euros lower than in 2008. The decrease is primarily due to the decline in other investments and borrowing items. In 2007 and 2008, the capital and financial account surplus were able to cover 102.0 and 115.4 percent of the current account deficit, respectively; however, in the current scenario, they only cover 76.7 percent.

Foreign direct investments have a significant role in the country's financial commitments and the growth of capital and financial activities. Foreign direct investments in 2008 amounted to 653 million euros, marking a 36% increase from 2007. In 2009, there was a minor 3.4% rise in FDI. Albania has the lowest level of foreign investment in the region, notwithstanding its expansion. The World Bank reports that the total foreign investment per person in Albania is just $1160. Macedonia's indication is $1,379, Serbia's is $2,000, Montenegro's is $3,800, Bosnia's is $1,687, and Croatia's is $5,670.

Proceeds from privatizations have significantly contributed to the increase in foreign investments, which amounted to 220 million euros in 2009.

Albania experienced a notable rise in financial liabilities to the world and a decrease in assets held by residents abroad in 2008. Additionally, there was a decline in banks' short-term loans abroad, which decreased to 201 million euros in 2009. In contrast, the net borrowing flow in 2009 was 366.1 million euros, showing an 8.5% decrease compared to the previous year. This decline was mostly due to a reduction in private borrowing, which decreased by 39 million euros, or 53.6%, from the previous year.

The financial account with the most notable activity has been resident deposits in foreign banks. Portfolio investments had a substantial decline of approximately 70 million euros in 2008, with few changes occurring in 2009. This item has minimal significance and weight in the overall investments in Albania.

Albania's financial commitments increased by 396 million euros in 2009 due to capital inflows from borrowing through long-term and soft loans from outside. Private borrowing increased in 2008 but decreased by 53.6% in 2009 compared to the prior year.

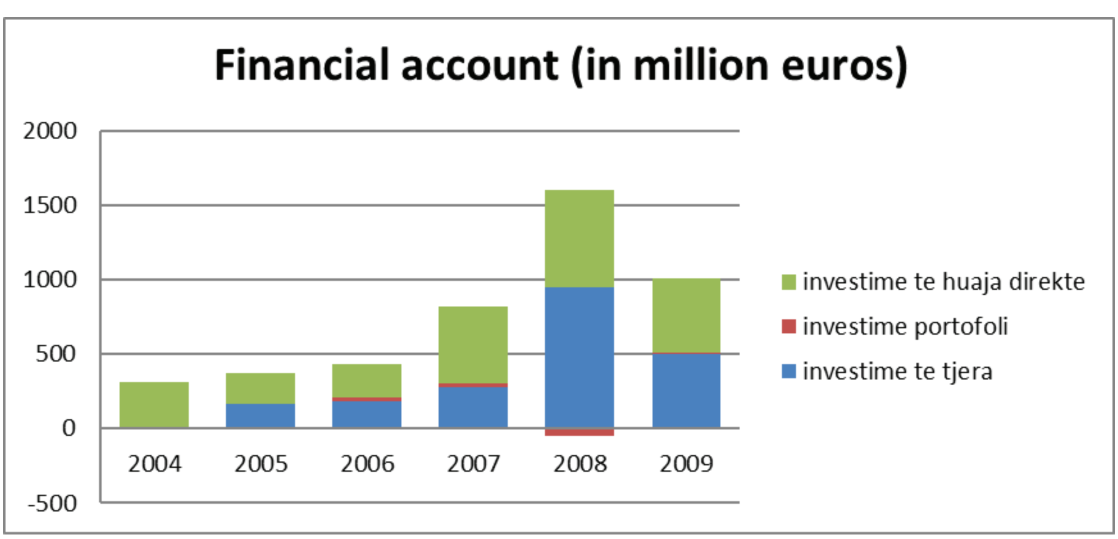


Figure 7 – Financial account

3.2.9. Comparison of the Balance of Payments in some of the Balkan countries.

Southeast European countries are undergoing a transformation and are facing a substantial imbalance in their current account balance of payments. To enhance the study of Albania's economic status, it is crucial to compare its current account, capital, and financial account with those of neighboring countries. However, only conducting a rudimentary comparison of these markers is insufficient. To enhance the distinction, it is beneficial to compare them with the gross domestic product. The following nations' balance of payments levels for 2009 are primarily based on the data.

Table 4 – Balance of payments by country

	Albania	Bulgaria	Romania	Macedonia	Montenegro	Serbia	SLOVENIA	BOSNIA	Kosovo
Current account	-1327	-2912.1	-5054	-483.25	-896.3	-1743	-340	-1201	-646
Trade balance	-2303.7	-4083.9	-6754	-1550.96	-1371.5	-4782	-621.2	-3912	-1690
Export	750.7	11783.2	29110	1920.92	296.3	5978	16203.4	2713	240
Import	-3054.4	-15867.2	-35864	-3471.88	-1667.8	-10760	-16824.6	-6625	-1930
Services	120.9	1367.2	-268	28	384.5	23	1022.2	235	135.3
Income (net)	-78.7	-727.3	-2131	-91.71	5.3	-502	-651	409	75.1
Transferta korente	934.5	531.9	4098	1131.41	85.3	3518	-90.3	1771	833.5
Capital and financial accounting	1018.2	2582.9	5806	466.14	860	1862	31.9	632	533.5

Table 5 – balance of payments by country to GDP

GDP	8673	33860	114860	6530	3542	38730	35050	12380	3792
% to GDP	Albania	Bulgaria	Romania	Macedonia	Montenegro	Serbia	Slovenia	Bosnia	Kosovo
Current account	-15.3 %	-8.6 %	-4.4 %	-7.4 %	-25.3 %	-4.5 %	-0.97 %	-9.7 %	-17 %
Trade balance	-26.6 %	-12.1 %	-5.8 %	-23.7 %	-38.75 %	-14.5%	-1.77 %	-31.6%	-44.5%
Export	8.9 %	34.8 %	25.3 %	29.4 %	8.4 %	18.2 %	46.4 %	21.9 %	6.3 %
Import	-35.3 %	-46.86%	-31.2 %	-53 %	-47.1 %	-32.7%	-48.2 %	-53.5%	-50.9%
Services	1.4 %	4 %	-0.23 %	0.42 %	10.8 %	0.07 %	3 %	1.9 %	3.56 %
Income (net)	-0.9 %	-2 %	-2 %	-1.4 %	0.1 %	-1.5 %	-1.86 %	3.3 %	1.98 %
Current transfer	10.8 %	1.6 %	3.5 %	17.3 %	2.4 %	10.7 %	-0.25 %	14.3 %	22 %
Capital and financial accounts	11.8 %	7.6 %	5 %	7.1 %	15.25%	5.66 %	0.1 %	5.1 %	14 %

Romania

Romania has one of the highest gross domestic products in the Balkans. Bulgaria's GDP is almost 13 times larger than Albania's, indicating a substantial disparity between the two countries. Romania has a trade deficit of 6.7 billion euros, which is very significant in the Balkans. When compared to the GDP, the trade deficit accounts for around 5.8%. This percentage is the smallest among the countries examined due to the magnitude of this country's GDP. Romania's exports, valued at approximately 29 billion euros, represent 25% of its GDP, while imports account for almost 31% of GDP, reflecting a well-established foreign trade sector in the country. Romania is classified as one of the countries with the lowest trade imbalance in the Balkans, despite several other countries in the region having larger export and import volumes. This trait signifies more stability for this country. Romania has a low level of net services to GDP, with a deficit of 268 million euros and a huge deficit of net income amounting to 2131 million euros. Similarly, current transfers show a large value in absolute terms, but it cannot be concluded that Romania's economy relies on immigrant inflows to address the trade imbalance. To address this gap and other deficits in the current account, inflows from the capital and financial accounts of 4% of GDP are necessary.

Comparatively, the Romanian economy is more developed and relies heavily on its external sector, whereas Albania attempts to address its substantial trade imbalance of 26% of GDP through current transfers and a relatively low level of net services.

Bulgaria

Bulgaria has a more advanced foreign trade sector while having a greater trade balance deficit than Romania. Exports account for 35% of GDP, while imports are at a high level of 47%, leading to a trade deficit of 12%. Since 2008, the deficit has dramatically fallen to 23% due to reduced domestic demand and decreasing capital inflows. A surplus of net services totaling 1.36 billion euros, or 4% of GDP, partially offsets the deficit. This indicates the significant role that service trade plays in Bulgaria's foreign trade, generating substantial foreign exchange income. The net income level in Balkan countries often shows a deficit ranging from 0-2%. Furthermore, current transfers do not hold significant importance for this country, as they often have more significance in nations with high rates of citizen migration. The capital and financial account surplus is 1% lower than the capital account deficit, resulting in incomplete coverage of the deficit.

Serbia

Serbia similarly maintains a low level of current account deficit. A significant disparity in the ratio of imports to exports is seen in this country. Serbia's imports exceed exports by a ratio of almost 2:1. In comparison to other nations in the region, Serbia's export level of 18.2% is considered uncompetitive, while its import level is average. A trade deficit of 14.5% arises from this variation. The net services amount to 23 million euros, which is quite insignificant when compared to the GDP. The weight of current transfers to GDP in this country is equivalent to that of Albania, around 11% of GDP. Hence, we might deduce that Serbia similarly heavily depends on immigrant remittances. Despite the significant trade balance disparity, the surplus in the current transfer account partially offsets the deficit. Net income, similar to many countries in the region, shows a deficit of 1.5% of GDP. The capital and financial accounts effectively offset the current account deficit in this country.

Macedonia

When examining Macedonia's current account and capital and financial accounts, we observe satisfactory levels comparable to those of other countries we have encountered. The composition of these accounts has distinct traits. Macedonia's imports of 3.4 billion euros account for over half of the GDP, indicating a heavy reliance on imports. Despite the substantial quantity of exports at 30% of GDP, a significant trade balance deficit is generated. The deficit is partially mitigated by the current transfers, which amount to 17% of GDP, the most in the area. The inflows of 1.1 billion euros offset the substantial outflows from imports and contribute to a significant current account imbalance. By the end of 2008, Macedonia was impacted by the economic crisis, resulting in a notable decrease in exports and a consistent level of imports, leading to a substantial current account deficit. In the latter part of 2009, the country had a notable recovery from the crisis, marked by a rise in exports and a reduction in the current deficit.

Montenegro

Montenegro's low GDP is attributed to political and geographical issues, as well as its relatively recent independence. This country has the biggest current account deficit as a percentage of GDP compared to other countries in the region, standing at 25% of GDP. The deficit in previous years was significantly bigger, but the decline in 2009 was primarily due to a reduction in imports, making it an unreliable indication. Montenegro's economy relies significantly on imports, which make up about 47% of its GDP. The significant import value indicates a substantial trade balance deficit, with Montenegro's exports accounting for 8% of GDP, resulting in a considerable import-export gap. This country's export level is similar to Albania's, but the trade balance deficit increases by 12% due to our country's lower import levels. Montenegro substantially depends on service exports, generating net revenues of 384 million euros (10.8% of GDP), a proportion that sets it apart from other countries in the region. Montenegro has successfully established competitiveness in the region's tourist sector, which holds the highest significance in service trade. Net income generates a substantial surplus, while current transfers have a minimal amount. Albania addresses its trade deficit through current transfers, while Montenegro employs trade in services to mitigate its imbalance. The finance account has a small value, while the capital account is mostly dominated by foreign direct investments. This account does not address the current deficit and results in a substantial deficit in the balance of payments. Typically, this deficit is offset by the "Net Errors and Omissions" account and the country's foreign exchange reserves.

Slovenia

Slovenia has a modest current account deficit and trade balance. This is mainly due to the high and nearly equal levels of exports and imports, which make up 46% and 48% of GDP, respectively. Slovenia has the greatest export-to-GDP ratio among the countries evaluated in the region. This country has a well-established foreign commerce system where the revenue generated from exports nearly offsets the expenses from imports, resulting in a trade deficit of 620 million euros. Slovenia's trade in services generates a surplus of around 1 billion euros, equivalent to 3% of its GDP, which is a typical amount for the country. Net income in all nations in the region shows surpluses at a modest value of 1.86% of GDP. Slovenia experiences a deficit in current transfers, suggesting that the outflow of remittances to other countries exceeds the intake, and there is not a significant amount of remittances coming from immigrants. The capital and financial account currently stand at around 32 million euros, showing a substantial decline from 2 billion euros in 2008. The fall is due to a decline in the financial account, particularly in foreign direct investments and bank loans.

Bosnia and Herzegovina

Bosnia-Herzegovina and Albania are potential candidates for visa liberalization and EU accession. A notable disparity is evident in the Balance of Payments accounts and their structure. Bosnia's current account deficit is approximately 10% of its GDP, which is 5% less than the proportion of this deficit in Albania's GDP. The trade imbalance in Bosnia is significant, amounting to 31.6% of the GDP. The deficit is a result of the high tax rate of 53.5% of GDP, which is one of the highest in the area. This country relies not only on imports but also on exports, which make up 21.9% of its GDP in export revenues, a figure that differs greatly from Albania's exports. Bosnia offsets its trade deficit with substantial transfer receipts totaling EUR 1.7 billion (14.3% of GDP) and a significant net income level of 3.3% of GDP. Bosnia generates a significant amount of income from non-residents, a trend not seen in other nations in the region, which have a deficit in this area. An equal exchange of services leads to a surplus of 235 million euros, equivalent to 1.9% of GDP. Surplus balances are responsible for decreasing the current account deficit to 9.7%. The IMF reported that the current deficit decreased more rapidly than predicted and is projected to continue declining, reaching a steady level. Bosnia's external competitiveness has enhanced as a result of a shift in export structure towards high-value industrial products. Structural problems have impeded the expansion of the financial account. Political instability, complex bureaucracies, corruption, and inadequate legislative frameworks have led to a decrease in foreign direct investments. These traits are also present in Albania, contributing to the limited investments in our nation.

Kosovo

Kosovo is the newest European country and often struggles to manage its deficits. Kosovo experiences a significant current account deficit of 17% of GDP, primarily due to its low level of exports. Consequently, Kosovo's trade deficit is one of the biggest in the area relative to its GDP. This country has a high import level, accounting for approximately half of its GDP, and a low export level of only 6% of GDP. Kosovo's economy is now import-dependent and needs to be rebuilt to become a producing economy that offers goods to the market. Kosovo is attempting to address the significant deficit caused by current transfers, which amount to 533 million euros, or 22% of GDP. Kosovar residents living in several European nations for an extended period have generated significant remittances to their homeland. Trade in services generates a surplus of 3.5% of GDP. Recent global economic crises have not significantly impacted Kosovo, indicating that its economy remains isolated from the world economy. In the future, this will impede the economic development of Kosovo.

Albania

Albania, Montenegro, and Kosovo have poor export levels, leading to substantial trade and current account deficits in Albania. Considering that Montenegro and Kosovo became independent states in 2006 and 2008, respectively, and given Kosovo's history of territorial and political issues, Albania's export levels have been unacceptably low, indicating limited business growth during the 20-year transition period. Imports are at 35% of GDP, which is lower than the regional average. Albania, Macedonia, Bosnia-Herzegovina, and Kosovo heavily depend on current transfer inflows to offset the substantial trade deficit that is a defining feature of these nations. Montenegro experiences a significant trade deficit but relies heavily on a trade surplus in services. Albania has an average net income in the region with a small deficit, whereas Bosnia-Herzegovina is the only country with a substantial net income surplus. Foreign direct investments have a significant impact on Albania's capital and financial account, resulting in a relatively high level. The excess in this account is insufficient to offset the substantial state of the current deficit.

4. Discussion

The ratio of the volume of foreign commerce (imports plus exports) to the Gross Domestic Product (GDP) is 44 percent, which is half the average of comparable countries in the region. Our economy relies on imports and the influx of immigrant labor.

It is true that the global financial and economic crisis did not have a significant impact on our economy. Paradoxically, the closed nature of our economy also shielded us from the crisis's effects. It is essential to implement a series of changes to open up the economy. We need to focus on expanding exports since increasing imports is not financially viable. Import growth is contingent on the population's purchasing power. An incentive package tailored to certain sectors is deemed necessary for Albanian exports. It is crucial to pinpoint the productive sectors with comparative advantages and establish tailored assistance programs for them.

Many Albanian products lack the necessary amount to secure contracts and quality certificates and face administrative hurdles in satisfying quality standards, particularly in the case of seafood. Albanian exports are somewhat varied, which increases their susceptibility to external shocks.

The active processing industry (fashions) is expected to continue to be the dominant sector in Albanian exports over the next few years. The products should be exported to a variety of countries.

The current organization of the agriculture and food production sectors is not conducive to expanding exports in this area. The majority of exported items consist of raw materials with minimal added value, such as medicinal herbs, raw hides, and vegetables. Exporting vegetables incurs substantial transportation costs and experiences significant losses despite their low added value. Focusing on a manufacturing plan for exporting high-value and precisely processed products is essential for improving the agro-food trade deficit. It also necessitates a significant investment in technology and identifying sustainable markets. Albanian producers should focus on using yield-increasing technology, enhancing product quality and appearance, and establishing enduring commercial partnerships.

Foreign Direct Investments (FDI) are a significant means of distributing technology that is underappreciated in Albania. Foreign direct investment (FDI) can greatly enhance technology transfer within a country by easing the exchange of information and knowledge about technology among local subsidiaries and promoting the spread of technology among domestic companies. Foreign direct investment (FDI) can lead to beneficial technological advancements for local companies through mechanisms such as employee training and expertise gained from working with international corporations, which can later be applied to domestic firms or new ventures. FDI has had a minimal impact on technical advancement in Albania.

The state must also collaborate and establish conducive conditions for the economy. Identify industries with the greatest potential for international competitiveness and provide strong support for exporting. Develop tailored support strategies for sectors with comparative advantages and enhance financing options for small and medium-sized businesses.

Establishing standards in the economy is essential, as it opens up export prospects and ensures confidence among partners through the construction of control structures. The platforms must assist manufacturing in a goal-oriented manner to enhance the competitiveness of "made in Albania" products in both domestic and international markets for them to be regarded as complete.

5. Conclusions

The balance of payments is a statistical summary that systematically presents a country's economic interactions with the rest of the world during a specific period. The international community finds it intriguing since it represents a country's interactions with the global economy. Albania's balance of payments categorization is founded on the fifth edition of the International Monetary Fund's manual.

None The primary classification used for the balance of payments involves organizing data into the current account and the capital and financial account. The current account consists of irreversible transactions, while the capital and financial account records reversible transactions involving liabilities and foreign financial instruments of an economy. There is no straightforward criterion to establish the sustainability of a current account deficit. Several factors should be utilized to evaluate the sustainability of the current account imbalance. The current account deficit in Albania is reasonably constant. Stability is delicate and might be severely compromised by the ongoing decline in trade. The authorities need to focus on the current account deficit by implementing structural improvements, economic policies, and incentives to enhance competitiveness.

From 1996 to 2006, omitting 1997, the current account deficit to GDP varied by 4% for the first five-year period and around 8% for the second five-year period. Between 2007 and 2008, the current deficit increased dramatically, reaching nominal numbers around 3–4 times higher than the average of the preceding years. The trade deficit has been increasing annually, reaching 27% in 2009. The increase in the trade deficit has had a detrimental impact on the current deficit. The primary funding for the trade imbalance in the current account comes from current transfers, predominantly remittances from immigrants.

Trade in services has consistently been a component of the balance of payments, with a significant volume of transactions.

Direct investments and capital transfers are the predominant components in the capital and financial accounts. Other investments primarily included public and private borrowing as well as commercial loans.

Albania has the third-biggest current account deficit in the area, following Montenegro and Kosovo. It is situated at the same level as exports, accounting for 9% of GDP.

Albania, Macedonia, Serbia, Bosnia-Herzegovina, and Kosovo heavily depend on the excess of current transfers. Montenegro and Bulgaria are the leading countries in service trade in the region.

The 2009 devaluation of the local currency had minimal effect on domestic exports because of adverse international and domestic circumstances. Internal reasons include adverse climatic circumstances, reliance on imported raw resources for domestic production, declining consumer demand, and inadequate government policy support.

The ratio of international trade volume to GDP is around half of the regional average. The Albanian economy is a consumption-based economy that focuses on imports, with current transfers being used to purchase these imports. The closure of our economy shielded us from the global crisis, but certain measures are necessary to reopen it.

Albanian exports lack diversification both in terms of products and trading partners, with Italy and Greece being the key countries for trade. The economy's limited diversity increased its susceptibility to external influences. Albania's export growth focuses on current items for existing markets rather than expanding the variety of products or target markets.

None of the Albanian enterprises are acquiring as much new knowledge and technology in capital goods as firms in other countries that import products with low capital intensity.

Albania has the lowest foreign direct investments per capita in the region, with a value of $1160, while experiencing a 3-5% annual rise in foreign direct investments throughout the years.

Albanian companies manufacture goods with minimal added value, poor technological sophistication, an unskilled workforce, and narrow profit margins. Albanian products face reduced competitiveness in the global market due to limited direct access to international markets, established long-term partnerships, and quality certifications.

To decrease the existing deficit and achieve a steady and similar level with regional countries, it is essential to develop policies that encourage exports. Albania should diversify its sources of income by enhancing the competitiveness of its products, rather than solely relying on immigrant remittances to address the deficit.

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