

BTI 2008 | Albania Country Report

Status Index	1-10	7.07	# 33 of 125	
Democracy	1-10	7.50	# 32 of 125	➔
Market Economy	1-10	6.64	# 40 of 125	↗
Management Index	1-10	5.58	# 45 of 125	

scale: 1 (lowest) to 10 (highest) score rank trend

This report is part of the Bertelsmann Transformation Index (BTI) 2008. The BTI is a global ranking of transition processes in which the state of democracy and market economic systems as well as the quality of political management in 125 transition and developing countries are evaluated.

The BTI is a joint project of the Bertelsmann Stiftung and the Center for Applied Policy Research (C•A•P) at Munich University.

More on the BTI at <http://www.bertelsmann-transformation-index.de/>

Please cite as follows: Bertelsmann Stiftung, *BTI 2008 – Albania Country Report*. Gütersloh: Bertelsmann Stiftung, 2007.

© 2007 Bertelsmann Stiftung, Gütersloh

Key Indicators

Population	mn.	3.1	HDI	0.78	GDP p.c.	\$	4,729
Pop. growth ¹	% p.a.	0.6	HDI rank of 177	73	Gini Index		31.1
Life expectancy	years	75	UN Education Index	0.88	Poverty ³	%	10.0
Urban population	%	45.4	Gender equality ²	-	Aid per capita	\$	104.1

Sources: UNDP, Human Development Report 2006 | The World Bank, World Development Indicators 2007 | OECD Development Assistance Committee 2006. Footnotes: (1) Average annual growth rate 1990-2005. (2) Gender Empowerment Measure (GEM). (3) Percentage of population living on less than \$2 a day.

Executive Summary

Parliamentary elections on 3 July 2005 marked the first peaceful political change ever in Albania's young democracy. The political class's mature behavior after the elections was one of the European Union's main reasons for offering Albania the Stabilization and Association Agreement (SAA), which was signed by Sali Berisha on 12 June 2006. Albania plays a constructive role in the region, and its economy is growing. Brain drain is slowly decreasing as increasingly more high-level job opportunities are emerging in Albania. Despite these positive developments, the challenges facing one of Europe's poorest countries have not diminished. Among the most important challenges is the struggle against corruption, as Albania has one of the most corrupt systems in all of Europe. The socialist government was accused of tolerating increasing levels of corruption during its eight years in power. This culminated in a scandal that resulted in the party being voted out in 2005. The success or failure of Prime Minister Berisha's new government and its "clean hands" policy will be measured against the way in which it handles corruption. Advancing reforms and improving living standards are also key challenges for the government. Albania's infrastructure is deficient and it faces severe energy supply problems that have not been targeted adequately. Prison torture and violence against women are further problems, both of which have been spotlighted by Amnesty International and other organizations. Security also remains an issue. Even though the constitution, which was adopted by popular referendum in 1998, proclaims the independence of the legislative, executive and judicial branches, the political class continues to impose its will on all branches of government. Albania has a very active and liberal civil society accompanied by a diverse media landscape, both of which have a significant impact on policy-making. These two factors will prove crucial to Albania's ongoing process of transformation. The political atmosphere between the two main rival political parties has always been tense and constitutes a significant obstacle to Albania's transformation. Most recently, arguments between the

two blocs over the issue of voter identification certificates broke out into a political crisis in the winter of 2006. This was resolved only with international help in January 2007. Therefore, local elections held in February 2007 and the next presidential election (summer 2007) were regarded as another important test of Albania's suitability for further EU integration.

History and Characteristics of Transformation

Albania's social upheaval, which began in 1990, has evolved in an uneven and contradictory manner. The legacy of 40 years of communist dictatorship, bunker-like isolation and an extremely underdeveloped economy left its mark throughout the entire country and on its people. The public had no experience with democracy or a market economy. Albania had the characteristics of a developing country. Albania thus must undergo multiple transitions: political transition from the continent's harshest dictatorship to democracy; economic transition from the most centralized economy in Europe to an unfettered market economy; social transition from a rural society to an urban society; and a psychological transition from the most isolated society in Europe to an open society.

The 1992 elections brought the newly formed Democratic Party of Albania (PDSH) to power. Ineffective economic renewal and deficiencies in the perception and development of Albanian democracy threatened to boil over during the crisis of 1997. The crisis was triggered by questionable investment transactions that pushed a large portion of the population to the brink of ruin. International mediation allowed for early elections, which brought the Socialist Party (PSSH) – the successor to the Communist Party of Labor – to power. The murder of the PDSH politician Azem Hajdari in September 1998, the debates over the final approval of a new constitution in November 1998, the Kosovo war in 1998 – 1999 and the Macedonian crisis in 2001 further aggravated Albania's instability. After parliamentary elections in the summer of 2001, members of the PSSH attempted political manipulation because their party had held on to only a slim majority. This resulted in a parliamentary boycott by the PDSH. The situation led to another confrontation in the 2002 presidential election. External pressure resulted in the election of the consensus candidate Alfred Moisiu, a former general. Local elections in 2003 failed to bring progress. During these years, Socialist Party Chair Fatos Nano eliminated all significant opposition within the party. In September 2004, a group of parliamentarians, led by former socialist Prime Minister Ilir Meta, founded the Socialist Movement for Integration. On the right side of the political spectrum, 2004 saw the founding of another political force, the Movement for National Development, headed by Leka Zogu, the son of Albania's former monarch, King Zog I. The movement is comprised of several small political parties, such as Legaliteti, PDR and Balli Kombetar. The 2005 parliamentary elections, in which

Albania witnessed its first peaceful and orderly transfer of power, confirmed a consistent trend toward improving electoral conduct and an improved electoral framework. Former President Sali Berisha became prime minister. His PDSH won 56 out of 140 seats and is the leading party in the right-wing governing coalition. With its allies, it has a potential majority of a little over 80 seats.

The Socialist Party, led by Tirana Mayor Edi Rama, together with its left-of-center allies, has a strong say on issues requiring a qualified majority. This is particularly the case regarding electoral reform and the election of the president. Both votes require a three-fifths majority in parliament. Furthermore, the law on the electoral process requires the participation of the parliamentary opposition in the management of the elections. The dialogue between the ruling coalition and the opposition was characterized by displays of acrimony. This situation has had an impact upon electoral reform efforts and preparations for the upcoming local elections. Under the mediation of President Alfred Moisiu, international involvement helped Albania overcome a serious political crisis on the question of voter identification certificates on 12 January 2007. After being in limbo for two months, local elections are now scheduled for 18 February. The success of the July 2005 elections enhanced Albania's Euro-Atlantic integration prospects. In June 2006, Albania signed the Stabilization and Association Agreement (SAA) with the European Union. According to German Ambassador Hans Peter Annan, these elections are considered to be a test of Albania's suitability for further EU integration. The fact that the Council of Europe decided to continue monitoring Albania in January 2007, even though the latter had already signed the SAA, signals concerns over the country's continued shaky development. The government has taken measures to fight crime and the mafia and to spur economic activity and trade. Albania's economy continues to show strong growth and inflation remains low. But energy shortages and serious infrastructure deficiencies contribute to a poor business environment.

Albania maintains good relations with its neighbors. It has signed (and in most cases implemented) free-trade agreements with all its neighbors, including Kosovo. In December 2006, it signed an agreement with CEFTA (Central European Free Trade Agreement). Together with Croatia and Macedonia, Albania endeavors to become a member of NATO in 2008. Albania is actively contributing to the "war against terrorism" with troops in Iraq and Afghanistan.

Transformation Status

I. Democracy

1 | Stateness

The state's monopoly on the use of force is anchored in the constitution. Public order and safety are largely ensured. However, hotspots like Lazarat in the south are still problematic. In some remote areas of the north, the Kanun, an ancient ethical code of conduct with elements of self-administered justice, is still carried out. The government has declared its fight against corruption, bribery and organized crime to be a major task.

Monopoly on the use of force

In general, there is fundamental agreement about who qualifies as a citizen of Albania; therefore, it is not a politically relevant issue. All citizens possess the same civil rights, and the majority acknowledges the state's constitution on a fundamental level. The Greek and several smaller minorities have their own party, the Party for the Protection of Human Rights (PBDNJ), which is represented in parliament, regionally active and influential. Neighboring countries such as Greece and Macedonia carefully observe whether Albania respects minority rights. There is positive discrimination in many cases (schools, dual citizenship, etc.). Some Roma groups are less integrated and suffer discrimination.

State identity

Albania is largely defined as a secular state. Church and state are separate, and the political process is secular. Religious dogmas have no noteworthy influence on politics or law, or on societal integration. There have never been feuds among communities, and inter-religious marriages are normal. The liberal post-communist political environment enabled various sects to establish themselves, but their acceptance in society is low.

No interference of religious dogmas

The state's basic infrastructure extends throughout the country, but its operation is deficient to some extent. Administration reform aimed at overcoming bureaucracy and enhancing decentralization is still in its initial phase. Due to a burdensome bureaucracy, lack of interaction/cooperation between different sectors and low wages, administration remains fragile and civil servants corruptible.

Basic administration

2 | Political Participation

During the last decade of transition, the international community's concerns about electoral conduct have been one of the main obstacles to Albania's European integration. The constitution approved by referendum in 1998 guarantees universal suffrage, as well as the right to campaign for office. Nonetheless, actual election conduct has exposed problems in the process, leading to several revisions of the existing electoral law. The peaceful elections of 2005 and the peaceful handover of power from the Socialist to the Democratic Party opened the door for negotiations with the European Union on the Stabilization and Association Agreement (SAA), which was signed in June 2006. In the run-up to the 2007 local elections, serious procedural problems concerning voter registration arose again. The OSCE criticized Albania for failing to establish a unified electoral register. A provision within the electoral law designed to increase mutual trust between opposition and governing coalition gave the opposition the opportunity to effectively block the electoral process through boycott. In January 2007, the Albanian Helsinki Committee stated in an interview with Deutsche Welle that there was still a high degree of hate speech and tension in the campaigns. The atmosphere during the election was distrustful and accusatory.

Free and fair elections

Albania is a parliamentary democracy. The prime minister (Sali Berisha) is a dominant and powerful person and institution. The state's vulnerability to private sector interests is one of the country's most serious problems. In Albania's case, the three-way symbiosis between politics, business and the media threatens to use or capture the state for private interests. Some business groups exert a significant influence on government decisions, while other influence the opposition's position. State capture also manifests itself in politicians' control of powerful or even illegal businesses, which has significant implications for the formulation of laws, rules, and government policies. In some cases, owners of suspicious businesses enter politics and come to occupy positions in the state administration or seats in the assembly, only to use the influence for their own interests.

Effective power to govern

Freedom of assembly is unrestricted within the basic democratic order. Demonstrations against the government have played an important role in the democratic process. The most recent incidence was in 2004 when the Democratic Party of Albania used mass demonstrations to mobilize against the socialist government. The legal environment in Albania does not restrict the development of the NGO sector. NGOs can register fairly easily and face little interference in terms of their internal management. They are also allowed to engage in a broad range of activities. On the whole, international and domestic NGOs have been able to function with little governmental interference. NGOs and their representatives are able to operate freely within existing laws, and they can freely address matters of public debate as well as express criticism.

Association / assembly rights

The right to free expression for citizens, organizations and the media is guaranteed by the constitution. Restrictions on journalists have significantly decreased. The media system provides for a plurality of opinions, with every party and organization having their own mouthpiece. The media market is nevertheless vibrant, chaotic, not transparent and quite fragmented. Today, nearly everything can be published in Albania without any negative consequences. Ethical standards are low, and media organizations compete for scandals and news. Public perception of the media's credibility has decreased significantly, but at the same time, the media plays an important role as watchdog. In what appears to be a misunderstanding of politically balanced reporting, public television (TVSH) also continues to provide excessive and unreflective coverage of the election campaigns of all relevant political parties. Albanian Radio and Television (RTSH), the umbrella organization of both public radio and television, is regulated by the 1998 Law on Public Broadcasting. The law establishes the station as an independent public broadcaster financed through a license fee, which is collected from every household through the Electric Power Company (KESH). It establishes a board of governors that is de jure independent from political influence. However, at OSCE-mediated round-table talks in the fall of 2006, the governing party and the opposition agreed to establish a quota for members of the board to be appointed by the political opposition. This triggered the resignation of the then newly appointed head of the board, author Fatos Lubonja. Lubonja resigned in protest of what he considered undue politicization of the board by a political bazaar and unprincipled compromise rather than proper parliamentary procedure. Though there is no open or covert government influence, personnel within the institution are not rotated out. There is also a lack of journalistic self-confidence at RTSH compared to the more daring private competitors.

Freedom of expression

3 | Rule of Law

The separation of powers between the legislature, executive and judiciary is fragile and intermittently damaged by jurisdictional arguments and conflicts over constitutional interpretation. Fundamentally though, a restoration of balance is sought. Albania's deficiency in the separation of powers is a main obstacle to the country's democratization and its integration in Europe. The tendency to identify the state with the party in power is still a prevailing phenomenon.

Separation of powers

The judiciary is institutionally differentiated, but its decisions and doctrine are still partly subordinated to political authorities. In the last several years, the judiciary's independence has been repeatedly jeopardized by interference from politicians of both the governing party and the opposition. A special parliamentary investigative commission resulted in a recommendation that the president dismiss the prosecutor general. The president subsequently rejected this recommendation. Following a two-month investigation led by Berisha, parliament

Independent judiciary

voted on 24 July 2006 to recommend to President Alfred Moisiu that Prosecutor General Theodhori Sollaku be removed. Berisha accused Sollaku of incompetence and of failing to prosecute organized crime. Moisiu, however, declined to sack Sollaku, citing opposition complaints that the investigation of Sollaku's activities was illegal and violated parliamentary procedures. Public trust in the judiciary is also undermined by lawyers' and judges' lack of professional experience, blackmail and corruption. On 26 January 2007, Moisiu brought together representatives of policy and administration to fight criminal acts against judges and public prosecutors. This was a reaction to individual threats and criminal acts targeting judicial officials. However, these were typically cases of criminal, not politically motivated crimes.

The legal prosecution of corruption remains one of Albania's most challenging tasks. Corrupt officeholders are not prosecuted adequately. Anti-corruption rhetoric, rather than the anti-corruption actions, prevail in Albania. The fight against corruption has been more of a political tool, often being just an end in itself, rather than an earnest attempt to prosecute the corrupt. As long as top functionaries are not held legally accountable, faith in the administration of justice will be limited. Former Prime Minister Nano's anti-corruption campaign in 2003 became a farce when he returned ministers to power who had previously been fired for corruption. Prime Minister Berisha proclaimed a clean hands policy, but Albania scored only 2.6 on Transparency International's 2006 Corruption Perceptions Index. The government argued that the report's findings are based on data from the time of the former socialist government. The conflict involving General Prosecutor Theodiri Sollaku, whom Berisha publicly accused of corruption and failure to pursue organized crime, remains unresolved. President Alfred Moisiu refused to sign off on the sacking of Sollaku.

Prosecution of
office abuse

Cases of civil rights violations are decreasing. However, Amnesty International's 2006 report revealed evidence that the use of torture is still practiced by the police. Violence against women is also a severe problem in the country, and surveys indicate that domestic violence is common, affecting up to 40% of women. According to Freedom House, the human rights situation can be described as follows: "in practice there is no systematic attempt by the state to curb fundamental human rights and freedoms, nor is there a systematic effort to ensure them."

Civil rights

4 | Stability of Democratic Institutions

Democratic institutions perform their functions in principle, but opportunities are often wasted due to friction between institutions and the interference of various political actors. Arguments between the ruling Democratic Party and the main opposition Socialist Party over jurisdiction and interpretation blocked the work of parliament and the government several times over the past few years. In recent

Performance of
democratic
institutions

years and throughout all parliamentary terms so far, political parties have made a habit of threatening parliamentary boycott or even walking out of the legislature for extended periods of time. This has generated an underdeveloped parliamentary culture, in which political compromises are often negotiated at round tables under international (in particular OSCE) mediation rather than in parliamentary commissions. The election of the consensus president, Alfred Moisiu, in 2002 increased institutional stability. His interventions have protected institutions and helped them to gain political independence.

Individual institutions of the democratic state are generally accepted by all relevant players. Nonetheless, strong actors, political parties and in particular the charismatic leaders of the two main parties play veto cards from time to time by boycotting the political process or ignoring it. This kind of political behavior is decreasing significantly, however.

Commitment to democratic institutions

5 | Political and Social Integration

The party system is fragmented between two main blocs – the Socialist Party (PSSH) and the Democratic Party (PDSH). Several small parties on the left and the right have limited social influence, which varies according to region and topic. They are important players when alliances or coalitions become necessary. Especially the Party for the Protection of Human Rights (PBDNJ), which represents ethnic minorities, has a strong independent profile within the party system. A Christian-democratic party has emerged, affecting the fragile equilibrium among the parties of the right-wing coalition. In general, all major parties are oriented toward personalities and functions rather than programmatic platforms. Although fundamentally established, the party system remains shaky. Both of the big, monolithic parties have been through splits and severe internal fights.

Party system

The topography of interest groups is not representative of society. Important social interests – gender issues, the fight against poverty, regional differences – are underrepresented. In recent years, the public has increasingly expressed an alienation from politics with its dwindling voter turnout. Political parties are becoming aware of this problem and are aiming to broaden their teams with well-educated and experienced professionals who have been trained abroad. Despite their large membership, the trade unions have become increasingly weak, and their influence is primarily limited to state-owned companies. Trade unions are linked with either one or the other political wing. The social awareness of belonging to a certain group of interests is growing in Albania. Increasingly, people think that the government doesn't address their interests properly. There are good examples of citizen's initiatives advocating group interests, in most cases organized by the "Mjaft" movement. Still, there is little public understanding that in a genuine democracy, political organizations are embedded

Interest groups

in a civil society. The political parties in Albania dominate and run the public scene.

A convincing majority of Albanians support democracy as well as the process of integration in Euro-Atlantic structures. Most people in Albania associate democracy first and foremost with freedom of movement and freedom of expression. On the other hand, democracy is perceived as a constant power struggle between political parties. There is little consciousness of democratic values and civic responsibility. However, the support of international donors, which generated a massive increase in NGOs since 1992, made it possible for some NGO representatives to be very active and influential in public life. Political interferences and difficulties with these actors decreased during the review period.

Consent to
democratic
norms

There is a robust but heterogeneous web of autonomous, self-organized groups, associations and organizations, and solid trust among the population. The civic organizational landscape is diverse. The number of legally registered NGOs is approximately 800 NGOs, approximately 200 of which are active. NGOs exist in most sectors, including human rights, environmental protection, women, education, youth, culture, economic development, health, disabilities and minority rights. The number of NGOs in cities outside Tirana and in the countryside has increased, as national NGOs and umbrella groups have expanded into other regions. NGOs are greatly dependent on foreign assistance and funds, and they are often more involved in implementing projects financed by foreign donors than in developing grass-root-structures and ideas. Patterns of civic political behavior have gained some credibility and attention through the repeated protest against abuse of power and corruption. An example of such activities is the internationally well-known anti-corruption movement MJAFT! (Enough!).

Associational
activities

II. Market Economy

6 | Level of Socioeconomic Development

Generally, high rates of steady economic growth have not sufficiently resulted in higher living standards, better health and welfare provisions, or greater educational or vocational training opportunities for the majority of the Albanian population. Economic growth, structural reforms and their benefits have focused on urban areas and their elite. Albania has established a free albeit anarchic market that lacks a strong institutional framework to regulate market-based competition and compensate for social imbalances. In contrast to other transition

Socioeconomic
barriers

countries, Albania has not progressed in terms of its socioeconomic development. Its Human Development Index value has remained at 0.78 but the country dropped on the HDI ranking list from rank 65 (2005) to rank 73 (2006) within only one year. The forecasted rise in unemployment to above 20% did not occur, according to official statistics. The unofficial rate is estimated to lie much higher, though, at around 30%. Real economic growth is not reaching a significant share of the population. More than half of Albania's population, which lives in rural (hence remote) areas, is left out. Subsistence economies are still important, particularly in the mountainous areas of the country where access to adequate infrastructure and market opportunities is still missing. The population groups most vulnerable to social inequalities are the elderly, the Roma and Egyptian ethnic minorities, young people and above all women and girls. This can be seen in Albania's low GDI value of 0.780, GINI coefficient of 28.2 and Albania's Gender Empowerment Measure (GEM) of 0.306. Human rights violations are also prevalent in Albania. Domestic violence, bad working conditions, forced labor and prostitution are further expressions of violence against women, according to Human Rights Watch and Amnesty International. Child labor in privately owned factories, such as shoe factories, sewing shops or any other manufacturing firms, is another serious issue.

Economic indicators		2002	2003	2004	2005
GDP	\$ mn.	4,456	5,617	7,380	8,380
Growth of GDP	%	2.9	5.7	5.9	5.5
Inflation (CPI)	%	7.8	0.5	2.3	2.4
Unemployment	%	-	15.2	-	-
Foreign direct investment	% of GDP	3.0	3.2	4.6	3.1
Export growth	%	14.2	18.5	16.7	7.2
Import growth	%	27.4	10.8	10.1	10.1
Current account balance	\$ mn.	-407.5	-406.8	-357.9	-571.5
Public debt	\$ mn.	994.8	1,231.9	1,402.6	1,374.6
External debt	\$ mn.	1,117.9	1,484.0	1,547.2	1,839.0
External debt service	% of GNI	1.3	1	1	1
Cash surplus or deficit	% of GDP	-6.7	-2.9	-3.0	-
Tax Revenue	% of GDP	16.1	17.1	17.3	-

		2002	2003	2004	2005
Government consumption	% of GDP	10.2	10.1	9.5	9.3
Public expnd. on edu.	% of GDP	2.9	-	-	-
Public expnd. on health	% of GDP	2.4	2.6	3.0	-
R&D expenditure	% of GDP	-	-	-	-
Military expenditure	% of GDP	1.3	1.3	1.2	1.4

Sources: The World Bank, World Development Indicators 2007 | UNESCO Institute for Statistics | Stockholm International Peace Research Institute (SIPRI), Yearbook: Armaments, Disarmament and International Security

7 | Organization of the Market and Competition

Albania has succeeded in setting up all basic conditions for market-driven competition but failed to develop a strong institutional framework to safeguard free but not anarchic competition. Nevertheless, the past two years have seen progress in structural reforms, an improvement in the dialogue between the government and business community, advances in the commercialization of public utilities and significant steps to revitalize the privatization of large enterprises. At the same time, weak administrative capacities, or a lack of interest by those in power, slow down progress in market regulation, fighting corruption (often caused by close ties between politics and business) and integrating the informal subsistence economy.

Market-based competition

The risk of monopoly formation is generally not a major concern at the policy level. Nevertheless, the “intermarriage” between politics and business stimulates a system of oligarchies. Due to weak institutional structures and the bonds between politics and business, the formation of oligarchies is only inconsistently regulated. Legislation against cartels exists but lacks enforcement in practice.

Anti-monopoly policy

Albania’s privatization of industries and the banking system is nearly complete. Small-scale privatization is nearly complete, and the private sector now accounts for about 80% of employment. To support the development of small and medium-sized enterprises (SMEs), the current government has reduced taxes on small businesses and corporate profits – one important strategy for strengthening the financial sector. Moreover, it plans to reduce customs duties in line with Albania’s obligations to the World Trade Organization. Ports, railway and metropolitan bus lines are the only transport systems that have remained public. The telecommunications sector is in the process of privatization, as are other utilities (water and power supplies). Foreign trade is mostly liberalized, with uniform low tariffs and no fundamental state intervention in free trade.

Liberalization of foreign trade

Since the sale of the Savings Bank of Albania to the Austrian Raiffeisenbank four years ago, the national banking system and the capital market can be considered thoroughly differentiated. The bank held approximately 60% of all deposits in Albania. The institutional foundations have been laid for a solid banking system oriented toward international standards with functional banking supervision, minimum capital requirements and market discipline.

Banking system

8 | Currency and Price Stability

Thanks to recent monetary and financial policies, the Albanian government managed to curb inflation, foster confidence in the national currency (lek), and spurred credit to the private sector. The annual inflation rate could be maintained within the 2-4 percent target range since 2002.

Anti-inflation /
forex policy

Over the past years, Albania has maintained macroeconomic stability. The Stabilization and Association Agreement acknowledged Albania's effort to embrace a culture of policy stability. However, the country still lacks institutional safeguards for the future – such as managerial integrity, reliable law-abiding institutions and thoroughly improved public infrastructure. This makes the economic environment vulnerable to populist policy changes – perceived by foreign investors as a likely risk.

Macrostability

9 | Private Property

Overall, legislation for local and foreign private capital is in place and undergoes constant reform to create a favorable legal framework for private capital. Setting up a private business in Albania takes roughly 41 days. Although property rights and the regulation of the acquisition of property are defined in principle, problems remain with their legal implementation. A key problem area remains the settlement of ownership disputes related to different phases of post-communist land reform and nationalization (pre-communist owners, post-communist owners of real estate privatized after communism, buyers in good faith of real estate with unclarified ownership). In some cases, up to three parties claim ownership of one piece of real estate. The unsolved problem of land ownership is among the more serious obstacles to the country's social and economic development and, in particular, the main cause for a lack of investment.

Property rights

Small-scale privatization is virtually complete and the private sector accounts for nearly 80% of employment. Priorities in privatizing strategic, formerly state-run industries include the telecommunications company (Albtelecom), the Albanian Savings Bank and the Albanian power corporation (KESH). An important foreign direct investment (FDI) law has been passed, allowing foreigners to purchase real estate if they invest in local businesses. Nevertheless, legal uncertainties in combination with a weak administration and judiciary increase the risk to investors.

Private
enterprise

10 | Welfare Regime

A public welfare system is in place, constituted by social policy regulations and public institutions, but it is insufficiently equipped to give adequate support to people in need. There are three basic schemes of social protection: unemployment benefits, pensions and social assistance to families suffering from abject poverty. Unemployment benefits are paid for a maximum of one year. The health care system is still undergoing reconstruction. Recent reforms have not led to a clear improvement in the availability and affordability of health care for the poorest in society, most of whom live in rural areas. Expenditure on health has increased to 2.7% of GDP from public and 3.8% from private sources (2003). The formal social support system for poor families is insufficient, with payments of around ALL 2,170 – 3,188 per month per family, too little to escape the income poverty trap.

Social safety nets

Public institutions exist to compensate for gross social differences, but they lack resources. Economic insecurity in Albania has a detrimental impact on the equal opportunity to participate. In secondary education, the number of children attending school has dropped noticeably since 1990. There is an alarming decline in school attendance in rural areas and an equally disturbing reappearance of illiteracy, especially among girls. Children of Roma and Egyptians are the most vulnerable in terms of education. The average number of years in education for Roma children is approximately 4.2, whereas for Egyptian children it is about 5.05. University enrollment documents the country's rural – urban divide. Young people, both girls and boys, drop out of secondary and university education due to economic pressure. Women are underrepresented in politics.

Equal opportunity

11 | Economic Performance

Albania's economic performance is a success story with many shadows. While it has made impressive progress over the past 15 years with respect to many macroeconomic factors, the growing rural-urban divide that cuts across the country as well as persisting corruption show that Albania's economic achievements have not been without side effects. Also, whereas economic growth rates have been steady and reported to be relatively high, this is only in comparison to prior rates; they are still low in comparison to other transition countries. While a concerted series of structural reforms and a strong commitment to macroeconomic stability has led to sufficient employment levels and rapid growth, more than doubling Albania's per capita income, economic growth has not reached many parts of society, particularly not the poorest, remote areas. While the income gap with its neighboring countries could be steadily reduced, the country's urban-rural divide deepened. Moreover, Albania's informal

Output strength

economy still plays an important role, with an activity rate of 34.1% of GNI. Inflation rates were relatively stable at around 2.2% from 2003 to 2005 and are expected to stay at low levels, whereas the state's high internal debt remains worrying, amounting to 38% of GNI. Improvements in Albania's external position notwithstanding and despite the high growth in exports at an annual real growth rate of 14% from 2000 to 2005, its trade deficit remains relatively large at 23% of GDP. Remittances, around 14% of GDP, still constitute the main source of trade deficit financing, with FDI playing only a limited role. At less than 3% of GDP, FDI in Albania remains among the lowest in the. While financial intermediation through investment is rising, confidence is steadily increasing, and in the virtual absence of capital controls, the freely floating exchange rate continues its trend of appreciation. Both foreign investment and exports remain very low as percentages of GDP. In sum, in the absence of a strong institutional framework and respect for the law, Albania's market economy is free but anarchic. A small corrupt political and business elite, tied together in a strong network of self-interest, does not invest money in a visible way.

12 | Sustainability

In recent years, both the government and international bilateral and multilateral development institutions have paid more attention to environmentally friendly policies. The Ministry of the Environment identified all hot spots in the country and started a successful fundraising campaign for a clean up. At the political level, however, the advocacy of environmentally friendly policies is not backed up by a commitment to increase environmental awareness issues and to implement environmentally friendly policies. Environmental protection remains a marginal issue for the Albanian public.

Environmental
policy

Overall, the country possesses a good educational infrastructure but does not invest enough in education and R&D. The United Nations Development Program's 2006 Human Development Report contains no data on public and/or private R&D expenditures in Albania. Recent figures for state expenditure on education show a clear decrease from 3.3% to 2.8% of GDP in 2004. Consequently, the university system will continue to suffer, especially in remote areas where proper schools and teachers are lacking. Overall, Albania's low investment in human capital (education and R&D) correlates with its low rates in socioeconomic and human development.

Education policy
/ R&D

Transformation Management

I. Level of Difficulty

Structural constraints on governance date back to the long period of isolation and poverty during the communist era. The Kosovo war, ethnic conflicts in Macedonia and periodic tensions with Greece prevented infrastructure deficits from being overcome in the 1990s. The problems faced by Albania's neighbors have also been serious obstacles to Albania's development because, in one way or another, they have affected investment, regional cooperation, etc. Despite tensions with Greece, the fact that about 600,000 Albanians work there has been an important factor for Albania's development. Albania could only begin to integrate into the region fully with the installation of the stability pact following the Kosovo war. Apart from infrastructure constraints, poverty in remote areas is still a serious problem. In addition, erosion makes it difficult to make full use of natural resources. Last but not least, the process of democratization has been accompanied by serious political conflicts. Corruption has sabotaged many investments in the review period. The current government is faced with structural constraints in many respects, and these cannot be overcome swiftly.

Structural
constraints

There is no organic development of civil society from within Albanian society. There has always been a strict division between the public and the private sphere. The presence of NGOs and other civil society organizations (CSOs) started only after the breakdown of communism, but it was massive from the very beginning, supported and financed by international organizations in the social, media and other civic sectors. International observation of the political process in Albania is relatively intense and, in this way, protects civil society players. CSOs depend on external financial sources to a large extent, such as aid programs and the like. When outside organizations retreat, the gap can rarely be filled by Albanian organizations, resources or manpower; most native NGOs cannot provide a financially viable domestically focused concept. Establishing a sustainable civil society will remain an ongoing task and a field of international financial engagement in Albania.

Civil society
traditions

There are no irreconcilable ethnic, religious or social cleavages. Nevertheless, the society is deeply split along clan structures and interest groups, as well as political parties. Although to some extent, some parties have a more urban or a

Conflict intensity

more rural, a more southern or a more northern profile, the ethnic, religious or social question is never decisive. Since its founding, the Albanian state has been a nation based on a common language with a population of Christians, Muslims and people of other faiths. This concept of the nation has helped to avoid societal splits along ethnic or religious lines. Most Albanians are proud of their religious tolerance. In January 2007, the American Anti-Defamation League honored Albanians who had protected Jews during the Second World War. One Jewish survivor praised Albania as the only occupied country where no Jews died at the hands of the Nazis.

II. Management Performance

14 | Steering Capability

The political leadership pursues long-term goals, but it often postpones them in favor of short-term political benefits. The fight against corruption was declared the government's main priority in 2005. Due to political conflicts with the opposition parties, however, especially in the run-up to local elections, this topic has been postponed. Populist agendas are becoming increasingly prevalent in Albania's political agenda. While the population shows no resistance to reforms, the political elite is losing more momentum in reform implementation every day.

Prioritization

The leadership is committed to building democracy and a market economy, especially with regard to the process of integration into European structures. The government tries to do its European integration homework but nevertheless shows a lack of ability to follow a policy of integration and compromise with other political forces. A compromise between the governing and opposition parties intended to make local elections possible in early 2007 was successful only due to strong international intervention in early January 2007. Success stories include the reform of the banking sector, economic reforms, privatization and the implementation of generally favorable investment conditions.

Implementation

Policy learning in Albania can be best evaluated by analyzing the behavior of the major political players. Albanian Prime Minister Sali Berisha (Democratic Party) might be seen as an example of selective policy learning, adapting policy to international standards only if it will stabilize his existing position of power. After being the first president to be democratically elected in 1992, he became increasingly autocratic until he was removed from power through early elections brought on by public demonstrations and an international diplomatic intervention in 1997. In 2005, his party came back to power and Berisha became prime

Policy learning

minister. His policies are now regarded as being moderate and democratic and geared toward meeting the standards required by the international community. The political leadership responds to the former government's mistakes and failed policies by implementing changes, but its policy often remains stuck in the same routines. Learning processes occur, but rarely affect the knowledge base or cognitive framework on which policies are based.

15 | Resource Efficiency

The government uses only some of the available resources efficiently. Administrative and governmental structures have undergone many changes since the beginning of the transformation process, but these have not always been effective reforms. The administration has been visibly improving since 1997, as it gains political independence. After the Democratic Party took power in 2005, the independence of administrative bodies was respected more than in the past, and no general replacement of management staff took place. But the administrative body lacks sufficient funds and infrastructure to act efficiently. Clientelism and nepotism are still strong, although there have been some efforts to reduce their reach. Strong political pressure is exerted on public administration, especially during election campaigns, causing insecurity and conformism among civil servants. The recent crisis concerning identity certificates for the voter registration process showed again that not even the most basic population data needed to plan elections is available. Deficiencies in the state administration lead to ongoing waste of resources, for example when it comes to tax collection. Albania has relatively weak local self-government, but localities are able to implement their own agendas efficiently and independently of the central government, so long as the elected officials take responsibility and develop their own strategies. Responsible decentralization and financial district autonomy has not been efficiently implemented.

Efficient use of assets

Intragovernmental friction is limited. Even the various political parties represented in the government rarely present programs format odds with that of the dominant Democratic Party. Although clearly divided into ministries and offices, the governmental structure is strictly ruled by the prime minister. Prime Minister Sali Berisha has the final say on all major political issues; he dominates the government. This hierarchical structure helps to avoid letting frictions become publicly visible. There is also little overlap between different government branches. Consequently, overall policy is presented coherently. The messages conveying strategy and political goals are also coherent and clear.

Policy coordination

In July 2006, the World Bank published a comparative study on corruption in transformation countries. It noted a drop in corruption in many countries due to reversed and simplified tax systems and other factors that established transparency and hindered corruption. Albania was one of the exceptions to this

Anti-corruption policy

positive trend, however, and firms actually reported increases in the frequency of bribery. As in 2002, Albania and the Kyrgyz Republic continued to have the worst corruption indicators of the 33 countries surveyed in 2005. After the report was published, the Albanian government defended itself, arguing that it was too early to see the effects of the new anti-corruption policy, which had been proclaimed a priority. Some integrity mechanisms have indeed been implemented, but they often remain ineffective; private interests impede their functioning. The government's motivation is high, but the capacity to implement reforms is mixed. There is an increasing will to implement transparency and monitoring mechanisms. A regional conference on fighting corruption by the "Stability Pact Anti-Corruption Initiative" on 3 and 4 April 2007 highlighted considerable success by the Albanian administration in reforming legislation and procedures in accordance with the 2005 UN Convention Against Corruption in recent years.

16 | Consensus-Building

The ability to build consensus varies according to the issue. There is a high consensus among all major political actors concerning the aim of establishing a market-based democracy, as well as integrating into the EU and NATO. The level of consensus-building is low among interest groups, the political parties competing for dominance and within these parties. The most recent political crisis took place in the winter of 2006/07 when local elections scheduled for January 2007 had to be postponed because a consensus on voter identification certificates could not be reached. Within a climate of distrust that has dominated Albania for 15 years, the opposition voiced doubts that the proposed regulations could prevent abuse and election manipulation. The breakthrough finally came when all parties agreed on a compromise that required a voter to present a birth certificate and a second document to prove his or her identity. This consensus was reached only after strong international warnings that failure to ensure free and fair elections could harm Albania's EU and NATO membership prospects. The Council of Europe criticized the "poor" political climate in the country in December 2006. In addition, the European Union appealed to Albania's political forces to take responsibility for the local polls. Following these interventions, President Alfred Moisiu took on the role of mediator and invited the main political players, Sali Berisha and Fatos Nano. These two rivals have dominated Albania for the last 15 years and made the country a synonym for political chaos. Their handshake at the presidential palace was seen as a "national compromise" to enable a consensus on the local elections. But it was also seen as a deal between the two politicians in which Berisha's influence on the local elections would be enhanced in terms of ushering in his candidate for Tirana, and Nano would win Berisha's support for his presidential ambitions. Reaching compromises via international mediation and round tables has become part of the

Consensus on goals

political culture. The role of the president – who himself was elected as a result of international mediation and political compromise – increases in this process. Moisiu has become the major consensus-building factor.

All main political actors are committed to democratic and market-oriented reforms. Nevertheless, the political reality has often been one of counteraction on the part of either the Democratic or the Socialist Party. The inability to accept majority decisions or to achieve political compromises has therefore often led to boycotts of parliamentary proceedings, an effective veto of reforms. However, taking into account the general consensus on market-oriented reforms, progress has been achieved in many fields. Boycotting the parliament often seems to be more of a tool to gain public awareness for party interests than a substantial protest against the ongoing reform process. The ability to limit the power of veto actors outside the political landscape is limited, particularly when it comes to organized crime and corruption.

Anti-democratic veto actors

Ethnic and religious differences are of low significance in political life. More significant are regional differences more related to the societal aspects of modern life. Even today, northern Albania suffers from economic deficiencies and infrastructure problems, even though the government is full of high-ranking political leaders from the North. Apart from Prime Minister Sali Berisha, Josefina Topalli (Democratic Party) comes from the North. She is the head of parliament, has a Catholic background and hails from the northern city of Shkodra. The planned highway linking the city of Durrës with the northern area of Kukes and Kosovo is an important project to minimize regional clashes. Apart from the North – South –differences, there is regional differentiation between the capital and the rural areas. Albania's elite is concentrated in Tirana for the most part. In many cases, regional politicians and other high-ranking representatives of regional projects spend most of their time in the capital, the only center with modern cultural and social life. Decentralization should be supported more actively. Albania needs confident and capable local governance that takes charge of its own affairs.

Cleavage / conflict management

Over the years, the NGO sector has gradually become involved in policy-making. The government has taken some steps to improve transparency and create opportunities for NGO participation. This has mostly taken place under pressure from international organizations and civil society, but the government also wants to demonstrate intention to implement advanced good governance standards. Analyses written by NGO activists are taken seriously. They belong to the elite and political class. Over the past few years and specifically since Berisha came back to power in 2005, many analysts have become more and more independent and have kept their political distance. This is a new development and follows a long period in which most NGO actors had been closely linked to either one or the other political party. Nowadays, there are NGOs engaged in policy dialogue with the government and others that play a

Civil society participation

watchdog role by monitoring government performance regarding human rights standards, minority rights, election law requirements, etc. The political leadership is thus often confronted with a public debate and has to accommodate the interests of civil society actors. The government has taken initiatives to establish a dialogue with the business community. The business community is also developing institutions to increase its interaction with the government.

The political leadership recognizes the need to deal with historical acts of injustice, but the process of reconciliation is still difficult. The main political leaders of all parties are members of a generation that was part of the political elite in communist times as well. Sali Berisha was an active party member and highly respected doctor of the “nomenclatura.” Fatos Nano was part of the socialist leadership even before political changes began and prime minister in the time of transition. Albania is one of the few countries where former sigurimi (security service) files are still classified. A serious reappraisal of the past has not started yet. However, the highest-ranking members of the former communist regime have been sentenced. Some hundred thousand people (out of a population of 3 million) suffered serious injustices during the communist period. Due to the high degree of expropriation, banishment and other political crimes during the communist period, compensation is difficult. The reconciliation process nevertheless continues in a peaceful way. The democratic political leadership unanimously condemns the historical injustices but sometimes manipulates history to use it as a weapon against political opponents.

Reconciliation

17 | International Cooperation

The political leadership works with bilateral or multilateral international donors and tries to make use of international assistance. Albania receives continual support for the political and structural reform process. It cooperates with international anti-crime –structures, especially the Italian carabinieri and coast guard, to reduce drug trafficking, prostitution and illegal migrations from and through Albania. Albania actively cooperates with all main international institutions and receives training and technical support from institutions such as the GTZ, KfW, EBRD. Many reforms, laws and even the constitution have been prepared and drawn up with the help of international experts, who generally enjoy a high reputation.

Effective use of support

The government tries to act as a credible and reliable partner – for its citizens as well as its international partners. Image problems make it hard to achieve this goal, however. Within the country, people tend to doubt politicians’ assertions. Statistics show that trust in the political class is low. Internationally, the government faces a similar situation. Major international actors still express doubts regarding its reliability due to the experiences of the 1990s.

Credibility

The political leadership cooperates actively with neighboring states and complies with the rules set by regional and international organizations. The Albanian government calls for the protection of the rights of ethnic Albanians in neighboring countries and the peaceful resolution of interethnic disputes. Albanian Prime Minister Sali Berisha, who had been President of Albania in the 1990s, acknowledged in November 2006 that his country had broken the UN embargo on the former Yugoslavia during the early 1990s. Berisha said that he had disagreed with the UN embargo because it was negatively affecting Kosovo's ethnic Albanian majority as well as Montenegro. Nevertheless, Albania is highly valued for its moderate role during the conflicts of neighboring countries. The emigration of thousands of unemployed Albanians to nearby Italy and Greece is of great economic importance for Albania and has a positive impact on its bilateral relations.

Regional cooperation

Strategic Outlook

Albania has come a long way in the transition to democracy and a market economy. Its economy is expected to continue growing by 5 to 7% a year in the medium term. The peaceful transfer of power in 2005 was a display of increasing political maturity. Due to these developments, Albania has finally achieved the first important step toward integration into the European Union, the signing of the Stabilization and Association Agreement with the European Union.

More efforts are needed to overcome poverty and traditional structures and to stabilize democratic institutions. The country must also focus on consolidating its development by strengthening the rule of law more convincingly. The independence of the legislative, judiciary and executive branches must be implemented as guaranteed by constitution. This is an important prerequisite for good governance, economic growth and legal certainty. In order to attract more external investors, Albania will also need to improve the reliability of the legal system and increase security. Albania must decisively combat corruption, nepotism and crime, and continue its efforts to undermine the profitability of drug plantations and trafficking.

Economically speaking, Albania's main transition challenges are to encourage private sector development, particularly small and medium enterprises, and to bring the large informal sector into the formal economy. The country should continue to pursue commercialization and privatization in utilities and in the financial sector in order to increase competition, which will help improve services and introduce new management skills. The improvement of the country's dilapidated infrastructure is a key development task. This means resolving the energy crisis, which is a recurring and serious problem during the winter months due to a dilapidated infrastructure. Albania must also improve its provision of municipal services and strengthen local and international transportation networks. Long-term investment is needed to improve the country's infrastructure, streets, airports, electricity and telecommunication infrastructures must be built and expanded. Although important steps have already been taken with companies such as Hochtief or Vodafone, much more needs to be done, as there are other areas of potential interest to foreign investment, such as large-scale tourism that does not lose sight of environmental considerations. Albania should also increase its own productivity in terms of industrial and agricultural production, which remains low due to delayed privatization and a lack of technology that would enable the country to use its resources in a modern and efficient manner.

As a small country with a young, dynamic population of only 3.2 million, reforms and change can be applied relatively easily. Therefore, Albania must improve opportunities for the higher education of its youth. Investment in human capital is urgent. As private economic activity increases, the role of civic initiatives increases, both in the economic and education arenas. In order to achieve these tasks, Albania still needs long-term prospects for direct international support. Transformation will be sluggish if not all aspects of political, economic, social and cultural developments are integrated holistically. External financial support and monitoring, combined with a policy of discipline and reward from donors and European politicians, will remain indispensable to Euro-Atlantic integration. Maintaining political stability and deepening the relationship with the European Union will be very important for future macroeconomic performance. The resolution of Kosovo's final status will have a positive effect in Albania, since it will consolidate regional stability and expand the opportunities for foreign investment and regional cooperation.