

THE INTERNATIONAL MONETARY FUND
AND THE INTERNATIONAL DEVELOPMENT ASSOCIATION

ALBANIA

Joint Staff Assessment of the Poverty Reduction Strategy Paper
Prepared by the Staffs of the International Monetary Fund
and the International Development Association

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I. OVERVIEW

1. The Growth and Poverty Reduction Strategy¹ (GPRS) of the Government of Albania builds on the Interim Poverty Reduction Strategy Paper (I-PRSP) presented to the Boards of the International Development Association (IDA) and the International Monetary Fund (IMF) in June 2000. It represents the first effort by the Government of Albania to elaborate a comprehensive development strategy in collaboration with key stakeholders. The government chose the term GPRS to signal the strong emphasis placed on inclusive economic growth. The new government, headed by Prime Minister Majko—which took office in February 2002, following a period of internal divisions within the ruling Socialist Party and the resignation of former Prime Minister Meta—has reaffirmed its commitment to the GPRS. The medium-term poverty reduction objectives and priorities remain unchanged. However, recent changes in the near-term outlook necessitated revisions in the 2002 budget and the macroeconomic framework. These have been reflected in the May 2002 GPRS supplement.

2. **The GPRS represents a significant improvement over the I-PRSP.** The Government of Albania and its civil society partners put considerable effort into producing the GPRS. The main strengths of the GPRS are: (i) strong government ownership; (ii) a broad—and unprecedented—participatory process that lays a foundation for greater civil society participation in public policy making; (iii) a close, although imperfect, link between the GPRS and the medium-term expenditure framework (MTEF), which is essential for translating strategic objectives into public expenditure allocations; (iv) an improved poverty diagnosis, albeit still limited by a paucity of reliable data; (v) the elaboration—for the first time—of a comprehensive national development strategy that focuses on results; and (vi) ambitious plans for monitoring and evaluation necessary for improving the overall effectiveness of Albania's public expenditures. The GPRS expresses Albania's long-term vision of European integration, and is

¹ *National Strategy for Socio-Economic Development (GPRS)*, Republic of Albania, Council of Ministers, November 2001, and GPRS Supplement, May 2002. The title Growth and Poverty Reduction Strategy was used during preparation of the strategy, which was then publicly launched as the National Strategy for Socio-Economic Development (GPRS). The May 2002 GPRS Supplement focuses on revisions to the 2002 budget and is not a formal progress report. The Ministry of Finance prepared the Supplement in consultation with line ministries, but it has not been subject to the usual wider consultation with all stakeholders.

intended to complement the Stabilization and Association Process (SAP).² The staffs believe that the strategy constitutes a sound basis for continued concessional assistance from IDA and the IMF.

3. There remain weaknesses to be tackled during GPRS implementation and subsequent GPRS updates. It will be important to: (i) deepen and institutionalize the participatory process; (ii) improve the poverty diagnosis as new data becomes available; (iii) strengthen the link between the poverty diagnosis, objectives, and priority actions; (iv) improve costing and prioritization of policy actions; (v) strengthen cross-sectoral linkages; (vi) improve indicators and targets; (vii) assign institutional responsibilities for monitoring and evaluation and firmly link monitoring and evaluation to the policy-making process; and (viii) strengthen capacities within the government for strategy formulation, implementation, monitoring and evaluation, and aid mobilization and coordination on the basis of the GPRS.

II. THE PARTICIPATORY PROCESS

4. The GPRS fully describes the participatory process and its impact, and candidly analyzes its shortcomings. The GPRS participatory process—involving central and local government, civil society, the private sector, and donors—exceeded the plans outlined in the I-PRSP. Notably, given Albania's history, the government was open to public participation, beginning with a well-attended national conference in November 2000 to launch GPRS preparation. Individuals from across the political spectrum participated in the GPRS, although political party leaders did not participate. The greatest impact of the participatory process was the precedent it set for civil society involvement in public policy formulation and the budget process. The government appears genuinely committed to deepening and institutionalizing public participation, and to involving civil society in implementing, monitoring, and evaluating the GPRS.

5. Government ownership was strong despite capacity constraints. The Minister of Finance, who was the National Coordinator for the GPRS, provided leadership throughout the process. Recognizing its limited capacity to manage consultations and draft the final document, the government involved local consultants and private experts, which proved essential for producing a good GPRS paper while maintaining Albanian ownership. An interministerial working group met regularly during the preparation phase and helped establish a close link between the GPRS and MTEF, although imperfect synchronization resulted in the finalization of the MTEF before the GPRS. As preparation progressed, ministries and agencies not represented in the interministerial working group asked to contribute to the GPRS, reflecting a building momentum for participation within the government and a growing awareness of the importance of the GPRS. Still, there is need for continuing work to ensure that all key government officials fully understand the GPRS and its implications.

6. Broad civil society participation signaled a new emphasis on transparency and inclusiveness, a basis for greater future participation. At government request, The Carter Center facilitated the participation of civil society in the GPRS. Civil society advisory groups

² Negotiations for the Stabilization and Association Agreement are expected to begin in 2002.

worked with four of the ministries involved in the MTEF: the Ministries of Agriculture and Food, Education and Science, Health, and Labor and Social Affairs. Despite problems at some ministries, joint declarations emerged for all four sectors. In addition, a new National Civil Society Advisory Group commented on each GPRS draft. Public consultations designed to reach the poor also took place at twelve sites in four districts. Civil society generally welcomed the participatory process and seized the opportunity for dialogue—even if short timeframes and inexperience limited the opportunity for substantive discussions—with the expectation that the process would improve in the future.

7. Local governments, the private sector, and members of parliament participated in the GPRS to various degrees. The government hired local consultants to facilitate the discussions. Consultations with local governments about decentralization proved rewarding. Consultations with the private sector were not well attended, but the government is exploring ways to institutionalize a dialogue with the private sector. Members of parliament were briefed on the GPRS, but no subsequent consultations took place because parliament was dissolved in April 2001 in preparation for national elections. The Government of Albania intends to fully involve parliament—particularly the relevant parliamentary commissions—during GPRS implementation.

8. Albania requested—and received—the involvement and support of its development partners. At a March 2001 Consultative Group (CG) meeting, the government presented its I-PRSP and its progress in preparing the GPRS. A number of donors provided financial resources for the participatory process and analytical work. A dozen donors³ created a GPRS Core Donors Group, which met regularly to keep abreast of GPRS progress and determine how to best support the process. GPRS drafts were shared with development partners, including IDA and IMF, which provided detailed feedback. The GPRS Core Donors Group, recognizing Albania's inexperience with this type of initiative, has expressed overall satisfaction with the final GPRS paper, which it views as a solid framework for an improved policy dialogue. The GPRS Core Donors Group is now engaging the government in a constructive dialogue about GPRS implementation, pledging support for building institutional capacity and implementing GPRS priority actions. It is expected that the government will also present the GPRS at the next CG meeting in 2002 or early 2003.

9. A public awareness campaign accompanied the preparation of the GPRS, and the strategy itself will be widely disseminated. Posters, brochures, television and radio spots, and a nationally televised talk show were used to publicize GPRS preparation. Both print and electronic media provided wide coverage of GPRS-related events. The government intends similar efforts to publicize the final GPRS paper and implementation progress. The GPRS was presented at a national conference on November 1, 2001. The GPRS is posted on the Ministry of Finance website; copies of the GPRS executive summary were distributed in Albanian and

³ The group includes the Canada International Development Agency, Greece, European Union, IMF, Italian Cooperation, Netherlands, Organization for Security and Co-operation in Europe, UK Department for International Development, UNDP, UNICEF, US Agency for International Development, and World Bank. Germany joined the group in December 2001.

English to all stakeholders; and a concise summary of the GPRS was published in major newspapers.

III. POVERTY DIAGNOSIS

10. The GPRS poverty diagnosis improves on the I-PRSP diagnosis and makes good use of available data. The diagnosis is based on a Living Conditions Survey (1998), Multiple Indicators Cluster Survey (2000), Qualitative Poverty Assessment (2001), pilot poverty mapping exercise drawing on administrative data (2001), and several stand-alone studies. Given the absence of a regular and nationally representative household survey, the available quantitative data have serious limitations, some key data are of limited reliability, and poverty trends cannot yet be identified. For this reason, a qualitative study of poverty was conducted in ten regions to strengthen the poverty diagnosis. Also, the government is initiating a comprehensive plan to improve the statistical base on poverty. A census was completed in 2001 that sets the stage for fully representative living standard measurement surveys (LSMSs) to be conducted on a regular basis starting in 2002.

11. The poverty diagnosis stresses the multidimensional nature of poverty in Albania. The diagnosis outlines the high incidence and depth of income poverty; rural/urban and regional poverty disparities; employment and unemployment levels; ownership of assets; risk determinants; and the role of remittances in supporting many households, particularly female-headed households. Some female-headed households—widows with children and women living alone—have a higher incidence of poverty, and unemployment is higher among women. The diagnosis discusses Albania's weak and deteriorating infrastructure and services and the lack of access for many families to basic necessities such as water, sanitation, basic education, and heating. The diagnosis further outlines the national and rural/urban health and education status, including the relationship between poverty and low education and the imperiled health of children. The Qualitative Poverty Assessment confirmed that Albanians see poverty as a multidimensional phenomenon, with poor infrastructure, weak institutions, and insufficient security as major contributing factors.

12. The GPRS analyzes the growth and distributional impacts of past policies and programs and correctly identifies the main constraints to poverty reduction. It candidly mentions shortcomings of existing policies, such as abuse and poor targeting of economic assistance and unemployment benefits. The GPRS presents evidence of growing inequality—although the data are of limited reliability—that underscores the importance of distributional and equity issues. The GPRS identifies several major constraints to poverty reduction: institutional weaknesses, corruption, and a large informal economy, including illegal activities. However, the GPRS would have benefited from an explicit discussion of how the strategy addresses these constraints.

13. Overall, the GPRS poverty diagnosis provides a sufficient, if incomplete, basis for developing a growth and poverty reduction program. The GPRS largely focuses on growth-related measures to enhance income opportunities within Albania, as well as on actions to improve access to health, education, and infrastructure. These directions are consistent with both the quantitative work and the priorities identified by the poor in the Qualitative Poverty Assessment. The forthcoming LSMS and monitoring program will permit a more sophisticated

analysis, such as identifying trends in asset distribution and consumption, and they will help focus the overall strategy on specific policy interventions with a high impact on poverty reduction. However, the broad GPRS priorities are unlikely to change.

IV. THE POVERTY REDUCTION STRATEGY

14. The GPRS is a successful first attempt to formulate a comprehensive national development strategy. The GPRS presents a long-term vision—EU integration—and a medium-term strategy for 2002 to 2004. The strategy rests on two pillars—improved governance and strong economic growth. It also identifies health care, education, and infrastructure as priorities. The staffs agree with the overall strategy, which is broadly consistent with the poverty diagnosis. The government recognizes the GPRS as the start of a process requiring further work. The GPRS includes a policy matrix that will facilitate implementation, which will require improved coordination between government agencies and between donors.

Targets, indicators, and monitoring

15. The GPRS presents indicators and targets that require additional work. Setting indicators and targets proved challenging for the government, given its lack of experience and capacity in policy monitoring. The final monitoring plan is a step forward but does not fully link GPRS objectives to priority actions and related targets and indicators. Some indicators, such as the poverty reduction target, can only be measured reliably after the first LSMS in 2002. Other indicators lack a current baseline and a plan for establishing a baseline within the program period. Data sources are not identified for several indicators, such as the infant mortality rate. A few targets, including those for infant mortality and secondary school enrollment, may be overly ambitious within the envisioned timeframe. Intermediate and final targets are not identified for many indicators. Although not explicitly linked to the Millennium Development Goals (MDGs), several indicators (such as reductions in infant and maternal mortality) are consistent with the MDGs. The IDA team has had a productive dialogue with the government on the importance of improving indicators and targets, establishing better linkages with the MDGs, and building institutional capacity for monitoring and evaluation. IDA will provide support to the government in these areas.

16. GPRS plans for strengthening national capacity in monitoring and evaluation are promising. The plan specifies organizational roles and responsibilities for policy monitoring and evaluation, although responsibilities still need to be formally assigned. Supported by IDA and the UK Department for International Development, the government is implementing a 5-year program to build capacity for regular household surveys, including two LSMSs. The first LSMS is underway and on schedule. The government created a Data Users Group, consisting of ten public and private agencies, which provided information on data demand and helped design the LSMS questionnaire. Quantitative work will be complemented by periodic qualitative studies; and there are plans to directly involve civil society in monitoring and evaluation. The government is developing capacity to geographically map data and indicators. There are also efforts underway to improve policy and program monitoring, initially in the Ministry of Finance and six pilot MTEF sectors. For this purpose, an IDA and government workshop in February 2002 began to lay out a monitoring strategy and implementation plan. The Bank's Multi-Sectoral Team Learning Initiative is providing training to key counterparts and the proposed IDA-

financed Poverty Reduction Support Credits would help the government develop a comprehensive monitoring plan with explicit linkage to the MDGs. These efforts will enhance the government's ability to set more appropriate baselines, better monitor trends, and thereby formulate more effective policies.

Macroeconomic and fiscal framework and financing

17. The medium-term macroeconomic framework in the GPRS, developed in consultation with the staffs, aims to achieve both macroeconomic stability and poverty reduction through inclusive growth. The GPRS notes GDP growth of about 6 to 7 percent per annum is essential to improve living standards, alleviate poverty, and advance toward the long-term goal of European integration. However, macroeconomic stability and viable fiscal and external positions are necessary for sustainable high growth. Under the GPRS, expenditures will increase in the areas of education, health, and infrastructure, consistent with the priorities that emerged from the poverty diagnosis and consultation process. (As described in the GPRS supplement, the spending cuts in the revised 2002 budget resulting from the shortfall in privatization revenue, attempt to maintain the priorities of the overall strategy). Government revenues are projected to increase significantly as a share of GDP, allowing the overall fiscal deficit to decline by 2 percentage points of GDP and the trade deficit to decline by $3\frac{3}{4}$ percentage points over 3 years. Monetary policy will continue to be guided by the Bank of Albania's (BoA) commitment to an inflation target range of 2 to 4 percent, in the context of a flexible exchange rate regime. The staffs consider this a reasonable target, consistent with the BoA's monetary program, the proposed fiscal path, and the ability to finance an external current account deficit on concessional terms. The discussion of the macroeconomic framework in the GPRS could have been better supported by the inclusion of a more comprehensive set of tables (to include the fiscal and external accounts), rather the single summary table. The staffs would encourage the inclusion of such tables in subsequent GPRSs.

18. Growth projections are realistic in light of recent experience. The staffs agree that private sector development—particularly foreign direct investment—will be a key contributor to economic growth. The GPRS accurately identifies an agenda to promote private sector growth through strengthening governance and the rule of law; addressing urgent infrastructure needs and energy shortages; and further privatization. While ambitious and not without risk (see Section V), the growth target is feasible, especially considering Albania's history of high growth enabled by its commitment to reform. Future GPRS updates would benefit, however, from a better analysis of the sources of future growth and the relationship between growth and poverty reduction.

19. The staffs welcome the more cautious fiscal path in the GPRS compared with that in the July 2001 MTEF, given debt sustainability considerations and heightened global uncertainties. Under the GPRS, the overall deficit is set to decline relatively rapidly from 8 $\frac{1}{2}$ percent of GDP in 2001 to 6 $\frac{1}{2}$ percent of GDP in 2004, revised from 8 percent of GDP under the MTEF. Fiscal consolidation is justified by the temporary nature of two important sources of financing in recent years—privatization receipts and concessional foreign assistance. Domestic borrowing is projected to fall from 3 percent of GDP in 2001 to 1 $\frac{3}{4}$ percent of GDP in 2004, despite a decline in receipts from privatization.

20. **Given the importance of poverty-reducing expenditures, deficit reduction hinges on improved revenue mobilization.** Total revenues are projected to increase to almost 26 percent of GDP in 2004, from 23 percent of GDP in 2001. This ambitious increase will come largely through improved tax and customs administration. The staffs view the revenue projection as feasible in light of the experience of the past three years, which has demonstrated the authorities' strong commitment to agreed targets, and given the currently still low level of tax receipts, reflecting fiscal evasion. However, recent performance has demonstrated the underlying risks to the revenue outlook and the government will need to persevere with their policies of broadening the tax base and modernizing tax and customs administration. Future GPRS updates should further elaborate and extend the revenue framework.

21. **The GPRS's assessment of the availability of domestic and external financing is reasonable.** The required domestic borrowing is consistent with a cautious path for growth in monetary aggregates and sufficient room for increases in private sector credit. On the external side, projected financing needs are supported by indications that generous donor support will continue. Several key donors have negotiated or are in process of negotiating new multi-year foreign assistance packages and, importantly, a number of donors are working toward aligning their support with priorities and objectives of the GPRS. While the fiscal program assumes a relatively cautious path for projected privatization receipts, these remain subject to risks (as illustrated by the recent delay in privatizing Albtelekom).

22. **Continued improvement in public expenditure policy is essential for translating priorities into expenditure allocations.** Expenditure management has improved in recent years with the preparation of an internal audit law, measures taken to increase transparency of the procurement process and to strengthen management and control of Treasury operations, and the introduction of the MTEF. However, cost estimates for GPRS programs are rudimentary and/or missing, making it difficult to judge whether the priorities are sufficiently funded. For 2002, differences exist between the MTEF sectoral resource ceilings and the proposed budget allocations in the GPRS. Over time, better synchronization of the GPRS and MTEF should strengthen the role of the MTEF in translating GPRS priorities into expenditure allocations. Efforts are also needed to improve coordination with donors to enhance control over foreign-financed investment, which constitutes a major bulk of increased expenditures in priority areas. In addition, the capacities of local governments to manage budgets and expenditures need to be strengthened so that fiscal decentralization does not weaken control over total allocations to priority sectors.

Structural and sectoral policies

23. **The GPRS confirms the government's commitment to ongoing structural reforms, but it could have better prioritized measures and targeted vulnerable groups.** Since 1998, the government has successfully implemented a broad structural reform program, including privatization of strategic enterprises, financial sector reform, civil service reform, and anti-corruption initiatives. Building on these structural reforms, the GPRS presents sectoral strategies that reflect an increased focus on poverty reduction. However, future strategies should strengthen cross-sectoral linkages, although the GPRS did make a notable effort to address the cross-cutting issues of environment and rural and urban development. In addition, the GPRS would have benefited from better costing—to identify policies that most efficiently reduce poverty—and

better prioritization of priority actions based on the poverty diagnosis. Plans to improve the quality of data and to build government capacity for policy analysis are expected to sharpen the strategy's focus on poverty in the future.

24. The staffs welcome the GPRS emphasis on governance. The GPRS discusses all important areas of governance, including legal and judicial reform, law enforcement, public order, anti-corruption, public administration reform, public resource management, and decentralization. It also recognizes the role of the civil society in overseeing governance. However, the GPRS would have benefited from a more operational treatment of these issues, including short-term actions to demonstrate the government's commitment and build up needed grassroots support. In the staffs' view, there is need for a clearer definition of priorities in these areas, and for a realistic appraisal of the technical and financial feasibility of the proposed measures. Implementation of the proposed program necessitates closer coordination of the various government agencies involved.

25. The GPRS recognizes the private sector as the driving force behind growth and poverty reduction. It acknowledges the need for improving the business environment, in particular for reducing administrative barriers to private investment; facilitating business through new legislation and initiatives, such as credit information, collateral for bank credit, insolvency law, and commercial conflict resolution; enhancing competitiveness; and addressing business concerns regarding tax and customs administration. Additional efforts are needed, however, to enhance the partnership with the business community and articulate specific actions and programs. In early December 2001, the government organized a round table discussion with the assistance of the International Finance Corporation and Southeast Europe Enterprise Development (SEED). Government and business representatives confirmed their intent to prepare a more comprehensive action program, including a study on administrative barriers, and organize a private sector development conference in mid-2002.

26. Continued implementation of the government's financial sector strategy is an important cornerstone of private sector development. GPRS priority measures include: Strengthening bank regulation and supervision; and privatizing the Savings Bank, Albania's dominant bank, and INSIG, the state-owned insurance company, marking the final exit of the state from any major ownership role in the financial sector. IDA is providing support for these actions. The GPRS also acknowledges the importance of expanding the coverage of microfinance programs given the vital role of micro and small enterprises in Albania's economy.

27. The GPRS correctly identifies the need for major reforms in education and health, but additional work is needed. The GPRS and MTEF outline a 3-year program of increased health and education expenditures to address underfunding, target rural areas, and improve service delivery. However, long-term interventions will be needed to close gaps in service delivery, infrastructure, management capacity, transparency, and accountability. GPRS education objectives appropriately focus on increasing basic and secondary enrollment. However, the proposed measures (scholarships, school buses, free textbooks) are unlikely to increase enrollment unless parents perceive better school quality. Furthermore, the proposed development of vocational boarding schools should focus on rural areas, where needs are greatest. The GPRS health strategy addresses inadequacies and inequities in resource allocation and service distribution by improving regional planning and introduces specific interventions for emerging

public health problems, including HIV/AIDS and tuberculosis, the rising incidence in smoking, and drug and alcohol abuse. It includes specific measures to address the country's persistent maternal and child health problems, particularly in rural areas. The government will address the need for health financing reforms by introducing health insurance contracts with regional providers to improve the incentives for health providers while ensuring financial protection for poor and vulnerable groups.

28. The GPRS recognizes the need for a social protection strategy that is targeted and inclusive, encourages employment, and meets individual needs. Currently, social assistance is not well targeted, and further decentralization will not necessarily improve targeting. With the support of the Bank, the government intends to study social protection effectiveness to develop measures that improve targeting. The GPRS focuses appropriately on developing community social care services to assist vulnerable groups, such as women in abusive situations, children in need of foster care, and substance abusers. The GPRS also envisages a broad, active labor market policy. The staffs urge the government to reconsider government-run active labor market programs, such as public works schemes, which are probably not the most efficient method to promote employment given Albania's institutional capacity constraints. The GPRS identifies critical fiscal and social issues related to social insurance reform. In recent months, the government adopted or implemented a number of parametric reforms to the current system, including a further round of increases in the retirement age for pension eligibility, an increase in the ceiling on earnings subject to social insurance contributions, and a reduction in the social insurance contribution rate. The staffs are working with the government to define an ongoing program of robust short- and medium-term pension reforms to be supported by Bank and IMF operations. In light of international experience, however, the government should undertake an economic analysis of various policy options before committing to fully merge the rural and urban pension schemes for self-employed workers.

29. The staffs urge vigorous and sustained implementation of priority actions in the energy sector. Since mid-2000, Albania has experienced a severe electricity shortage, necessitating extensive load-shedding (power outages) despite large government subsidies for imports of electricity. The crisis results from several factors: excessive demand caused by chronic failure to curb illegal use and nonpayment; impact of a dry hydrological cycle on the largely hydropower-based system; and transmission capacity constraints limiting electricity imports. Recognizing the magnitude of the crisis and its wide-ranging macroeconomic and social implications, the government developed in late 2000 a power sector action plan to tackle the underlying issues. Implementation of the action plan has proceeded well. Nevertheless, the situation in the sector had deteriorated to such an extent that sustained efforts over an extended period of time will be required to improve sector performance and eliminate the electricity shortage. The action plan has been updated for 2002 and 2003 and the government has developed and adopted a Policy Statement setting out a power sector reform program and a viable schedule for its implementation. The GPRS adequately describes the key problems in the electricity sector and summarizes the measures to redress these problems. Future GPRS updates should fully incorporate the government's comprehensive strategy for the sector.

30. The rural development, environment, and infrastructure aspects of the GPRS are well developed. Consistent with the poverty diagnosis, the GPRS includes an especially comprehensive discussion of rural development. The government should now focus on

elaborating a time-bound action plan that clearly describes the roles of the government and private sector. The staffs also welcome the emphasis on the environment: environmental issues are correctly identified, and the GPRS proposes a reasonable action plan and timeframe to address them. In the transport sector, future GPRS updates should address the ongoing restructuring of the port sector and required next steps, as well as the need to restructure the railways. The GPRS strategy on water and sanitation adequately addresses the main sector issues, especially the central government's changing role from service provider to service regulator, and the need for greater cost recovery. The latter issue is of considerable importance, as nonpayment by water supply companies has aggravated problems in the electricity sector.

V. RISKS TO THE STRATEGY

- 31. GPRS implementation is subject to a number of risks, especially the fragility of domestic and regional political stability.** Although Albania's political stability and domestic security have improved since 1997, its politics remain relatively divisive and confrontational. Both major political parties have serious internal divisions. Regionally, the prospect of closer ties with European structures are major incentives for reform and political consolidation. But the 2001 outbreak of ethnic conflict in Macedonia underscores the region's continued instability.
- 32. The precarious electricity situation poses a principal risk to growth and stability if not addressed in a timely fashion.** Reliable electricity is essential for private sector development and sustainable growth. Continued load shedding could make it difficult to achieve annual growth rates of around 7 percent. Continued reliance on government-subsidized energy imports threatens to undermine further fiscal consolidation—as illustrated by the pressures exerted on the 2002 budget by the shortfall in domestic electricity production resulting from low river flows—and the government's ability to fully finance GPRS priority actions. Continued energy shortages could also contribute to social unrest and political instability.
- 33. Institutional weaknesses are likely to hamper GPRS implementation.** The GPRS preparation process itself revealed capacity constraints within the government. The GPRS correctly identifies governance and institutional capacity as key to achieving sustained growth and reduced poverty. Strengthening institutional capacity is critical for translating higher public expenditures into results, especially because new monitoring and evaluation functions will further strain government capacity. Albania will require substantial and well-coordinated external support to meet the challenge of implementing and monitoring the GPRS.
- 34. Decentralization needs to proceed judiciously.** Given weak local government capacities, rapid decentralization could jeopardize GPRS targets. Local governments could effectively target poverty, provided they have adequate resources and capacity. Local government transparency and accountability also need improvement. Decentralization should be guided by successful examples of community-driven development.
- 35. As evidenced by this year's budget amendment, the GPRS is subject to external economic risks.** Although Albania's external vulnerability is limited by low exports and lack of dependence on private capital markets, global shocks could adversely affect privatization receipts, official transfers, and remittances. The mid-year changes to the 2002 budget underscore

the importance of including well-defined, medium-term fiscal contingency plans in future GPRS updates in order to best protect the government's poverty-reducing expenditures.

36. Medium-term debt sustainability is contingent on favorable economic growth, low interest rates, and ongoing improvements in revenue collection. In recent years, large primary fiscal deficits have been financed without triggering adverse debt dynamics, because GDP growth rates have exceeded the interest cost of government borrowing, owing to favorable conditions: concessional external financing, an appreciating exchange rate, and declining domestic interest rates. Albania's public sector debt is not high by international standards, and primary deficits are projected to decline in future years. Nevertheless, a reversal of these favorable conditions, or fiscal slippage, in particular on the revenue side, could place debt sustainability at risk.

VI. CONCLUSIONS

37. Albania's GPRS marks a major achievement, although elements of the strategy will need improvement in coming years. The Government of Albania welcomed the GPRS initiative and worked hard to produce the GPRS. The GPRS's main strengths include the government's ownership, the participatory process, and the efforts to link it with the MTEF. Albania has already benefited from the process of preparing the GPRS: it set a precedent for civil society participation in formulating public expenditure strategies; reinforced a long-term results-oriented vision of development; and sparked increased press coverage and public discussion of poverty. As the first document of this kind produced by the Government of Albania, the GPRS is an impressive effort.

38. The Government of Albania is already working to address the weaknesses of the GPRS. Most notably, the government recognized the weaknesses of existing data, and has initiated an ambitious program to improve data collection and analysis. The government is also committed to further develop civil society participation during GPRS implementation and monitoring. It is especially important to strengthen the government's capacity to formulate, implement, and monitor policies. The government—with the assistance of the World Bank, the European Union, and other donors—is planning numerous initiatives to build capacity and strengthen institutions.

39. The staffs of the World Bank and IMF consider that the GPRS presents a credible poverty reduction strategy and provides a sound basis for Bank and Fund concessional assistance. The staffs recommend that the respective Executive Directors of the World Bank and the IMF reach the same conclusion.

**Albania: Tentative Schedule of Key World Bank and IMF Events
Related to the GPRS in 2002-03**

Institution	Event	Expected Date
IMF/World Bank	Boards consideration of the Joint Staff Assessment of the GPRS	June 19, 2002/June 20, 2002
IMF	Board consideration of the PRGF	June 19, 2002, 2002
World Bank	Board consideration of the CAS	June 20, 2002
World Bank	Board consideration of the Financial Sector Adjustment Credit, Poverty Reduction Support Credit, Power Sector Rehabilitation and Restructuring Project, and Road Maintenance Project	June 20, 2002
IMF	Staff visit	July 2002
IMF	Mission for Article IV/First Review of the PRGF	October 2002
IMF	Board consideration of the Article IV/First Review of the PRGF	January 2003
IMF	Mission for Second Review of the PRGF	April 2003
World Bank/Development Partners	Consultative Group Meeting	2002/early 2003 (unscheduled)