

Institutional Quality and Sustainable Economic Convergence

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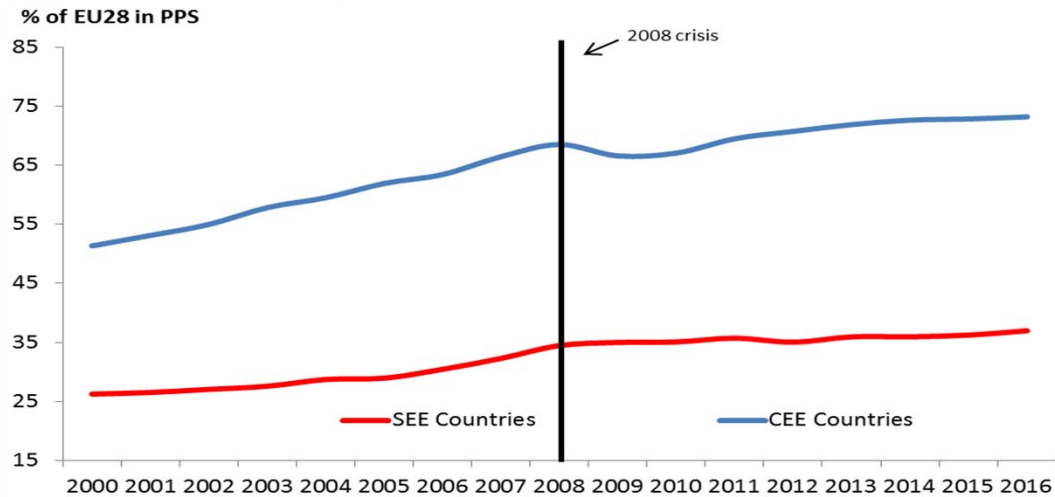
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1. SEE Convergence Process - Challenges

The economic convergence has slowed down...



Source: Eurostat

- Economic convergence firmly tied to the EU integration process in the SEE region.
- SEE countries benefited from rapid efficiency gains due to large-scale liberalization reforms during the transition period.
- The economic and financial crisis induced a stall in convergence dynamics for the region.

1. SEE Convergence Process - Challenges



- Convergence slowdown due to diminishing returns from capital and labour, as well as fading efficiency gains.
- Risks of falling into a ‘middle-income trap’ because of low level of innovation, poor quality of institutions and unfavourable demographics in the future.
- Imperative to prepare our economies for a gradual transition, from efficiency-gains-driven systems onto innovation-driven ones.
- Quality of institutions paramount in facilitating the move to the next development stage.
- Necessity for intelligent and targeted structural reforms:
 - Objectives: to promote business environment, rule of law, innovation capacity and overall competitiveness.
 - Targeted policy outcomes: improvement of the human capital stock, facilitation of innovation in production processes, advancement of domestically-generated technology and expansion of high value-added exports.

2. Convergence Process in Albania



- Institutional setup in Albania has been largely contributory to the convergence process, and macroeconomic policymaking has improved considerably in the past years.
- Independent central bank with an inflation targeting regime and a free floating exchange rate.
- Fiscal policy is on a steady consolidation path and a debt-reducing fiscal rule adopted.
- Range of structural policy initiatives to strengthen financial stability:
 - A banking sector de-euroization strategy
 - Removal of legal impediments to collateral execution and NPL resolution
 - Bank Resolution Law recently passed
 - Independence and efficiency of the FSA and the DIA strengthened further
- However, certain structural imbalances remain.

2. Convergence Process in Albania



- For a steadfast economic convergence to EU countries, Albanian needs to engage in continuous structural reforms aiming at improving:
 - institutional development
 - business sophistication
 - innovation capacity
 - technological readiness
 - financial market development
 - rule of law and quality of the judiciary.
- Various have been carried out:
 - Growth enhancing reforms:
 - a) Education reform, aimed at reducing skills mismatch in the labour market
 - b) Active labour market policies, aimed at increasing labor participation
 - c) Judicial system reform, aimed at improving law enforcement and increasing contract compliance
 - d) Energy sector reform, aimed at increasing efficiency and alleviating bottlenecks in supply
 - Sustainability enhancing reforms:
 - a) Pension system reform, aimed at ensuring sustainability of public finances
 - b) Administrative and territorial reform, aimed at reducing waste and increasing efficiency
- However, more is needed to smooth Albania's EU integration process and ensure that convergence is successfully achieved.

3. Concluding Remarks



- Economic systems in the SEE countries need to be transformed to avoid falling into ‘a middle-income trap’.
- Domestic ownership of structural reforms is crucial for the advancement of institutional quality and for achieving a sustainable long-term and inclusive economic growth.
- Targeted policy needs to promote innovation, cushion the effects of adverse demographics and facilitate the overall convergence process.
- The EU institutions can contribute further by:
 - providing transparent and objective EU integration guidelines;
 - emphasising the need of institutional convergence throughout the process;
 - continuing to monitoring and reporting on the progress of individual countries.



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THANK YOU!

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