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Strategies of Albanian economy to meet EU economic policies

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Abstract

This paper aims to analyze the relevant influence that EU's economic integration policies have in strategic management of public finance, on regional economic integration. We have illustrated the effectiveness of our strategic economic policies applied by the Government for Economic Development, by using customs operation as main variable. The scope is to evaluate the foreign trade balance and risks arising of national economy from the interaction of Albania with European Community.

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1. Introduction

In order to meet requirements of the EU the Albanian public finance systems as a country that seeks to gain the accession to the European Union, goes under increased scrutiny and undergoes rapid change. At time, Customs play double role that is: 'Financial-fiscal - the creation of state revenues and for the Gross

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Domestic; Product Protection of the country (police trade) - through the Regulation of Exchange of Goods, its volume, structure of the exchange. The change of political and international economic relationships, in order to harmonize economic development among countries at risk integration, is supported by liberalization of international trade of goods and the formation of free zones (integrating) the customs^a. In the framework of the Twinning Project^b "Support to alignment of customs procedures with European standards", the customs administration is in the process for implementation the Customs Code conformed to the European Parliament Regulation No. 450/2008 "Modernized Customs Code of the Community" and it's Implementing Provisions. The New Provisions^c provide for and regulate a variety of new procedures and customs operations implementation of which requires prior knowledge of business and other partners, considering that these new procedures bring mitigating measures for the business. On the other hand, government macroeconomic objectives are complicated Cooper R. N. (1969)^d. Also we know that, gross national product is a synthetic indicator of a country's economic activity.

In the analysis of GDP Antonelli G at al. (2007)^e each item of expenditure has a direct link with the foreign trade. So, taking into account the structure of gross domestic product:

$$GDP = C + I + G + Nx \quad (1)$$

By continuing simplifications we will have:

$$S - I = Nx \quad (2)$$

It means that, savings surplus is a surplus in exports of goods. So, when the NX net exports are positive, this means that, in Albania, there are savings to be invested, and the opposite, when NX is in deficit, it means that the Albanian economy needs foreign investment, Naqellari A. (2004)^f.

Important to our analysis there are the following policy instruments used under the control of the government to regulate the above equation:

- Policies of foreign economic relations (trade policies, internal coordination of macroeconomic policies conditional on the degree of their economic dependence - economic blocs)
- Fiscal policy (government spending + taxes)

The impact of the fiscal burden on the investment process (and the economic growth of a country) is the subject of numerous studies conducted by different authors. Theoretical basis of the studies is two strands of economic thought, known as Keynesian currents and neoclassical theories.

- Monetary policy (money supply – when interest rate increases the exports decreasing, interest rate lows imports grow. Thus improves the trade balance deficit and thus the balance of payments) Dornbusch R(1976)^g;

According to the Keynesian theory of aggregate demand, reducing government spending or raising taxes, this reduces aggregate demand and indirectly the income. Thus involves a negative impact on production. In the full model of this theory, the analysis presented in the standard IS-LM curve, the negative effects

^a Albania became a member of World Trade Organization in 2000.

^b Twinning Project "Support for Harmonization of Customs Procedures with EU Standards" dt. 11.03.2010 with a 24 month times pan. From <http://www.dogana.gov.al/index.php?mid=193&art=251&info=more>

^c Mehilli T. Note that the draft laws presented in this article are in the process of updating with new provisions of the EU.

^d Cooper R. N., "Macroeconomic Policy Adjustment in Interdependent Economies", 1969, *Quarterly Journal of Economics*, Vol 83

^e Antonelli G., Cainelli G., De Liso N., Leoncini R. & Montesor S. 2007, *Economia*, Torino G. Giappichelli (ed)

^f Naqellari A. 2004, *Principles of Economics*, Tirana Dardania (ed)

^g Dornbusch R., "Exchange Rate Expectations and Monetary Policy", 1976, *Journal of International Economics*, Vol 6. pp 231-244

of multiplier are partially balanced by the effects of crowding-in as a result of lower interest rates and monetary depreciation. In Neoclassical models a lower budget deficit would reduce interest rates significantly, thus leading to positive effects of income (wealth) on aggregate demand.

In a country as Albania, which suffers from severe imbalance of the budget deficit, the reduction of budget deficit would affect the reduction of price interest rate risk. However, it would increase the market value of private property and therefore would increase the aggregate demand. On the other hand, reducing the government deficit would provide for the private sector and consumers in the future as a signal of decreasing tax burden and increase of their income, which should boost their consumption and the economic activity.

2. Objectives and hypothesis of the study

The main objective of this paper research is to illustrate our strategic management of public finance according to Stabilization and Association Agreement (SAA) to evaluate the impact of EU political – economic situation' related to Albanian economic public strategies. Through the policies instruments and statistics data we will explain the important role of SSA reforms versus the respective challenges of customs service, strategies of international business and reforms of the public finance. The specific hypotheses in this paper research are:

- What are the efficient economic tools of Albanian Government, in response to the new challenges of international political - economic situation?
- What is the role of the public finance strategies on public debt and gross domestic product?

For this purpose, we have used data available from the Customs of Albania, Ministry of Finance, Bank of Albania, as well as by other competent authorities that supervise the strategic economic development.

3. Methodology

At this paper, we have comparing statistical data of different indicators and macroeconomic aggregates. Customs integration is evaluated on performance and risks arising from the interaction of Albania in European Community. We evaluated the performance of the Albanian economy comparing qualitative and quantitative variables Pastorello S. (2001)^h as below: Foreign trade Dornbusch R.(1976)ⁱ, expectations of economic growth, fiscal policy strategies, the benefits of EU Integration maintaining as main variable, the Customs.

4. Albanian customs towards the EU

EU is created as a single economic market across the territory of all its members. Two of the main objectives of the European Economic Community were to develop a common market and customs union between the states member. The single market implies the free movement of capital, people, goods and services within the EU states which cannot become the subject of discriminatory customs duties or import quotas Zajmi I. (2010)^j. Consequence of this policy is the customs union that includes applying a single external tariff on all goods entering the market. For the realization of the above two objectives

^hPastorello S. 2001, *Rischio e rendimento: Teoria finanziaria e applicazioni econometriche*, Il Mulino, Bologna,

ⁱDornbusch R., "Expectations and Exchange Rate Dynamics", 1976, *Journal of Political Economy*, Vol 84. pp 1161-1176

^jZajmi Iva, 2010, *European Common Market*, OMBRA GVG, Tirana

were established common currency-the Euro-purpose use of a single exchange rate, eliminating the problems of foreign exchange through transparent price and creating a single financial market where monetary policy in the EU member states are under the control of the ECB.

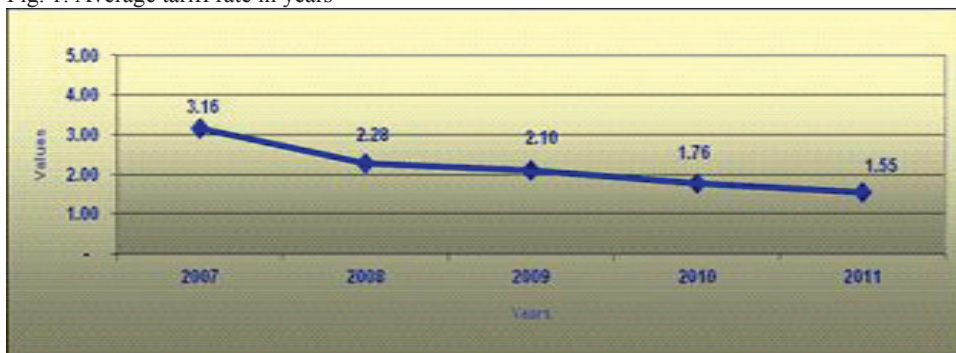
The aspiration to join Europe begins with the establishment of diplomatic relations between Albania and the European Union in 1990 and the signing of the Agreement on Trade and Cooperation in 1992. Following this agreement, Albania was able to benefit from preferential trade regimes for the European Union offered to developing countries. Since 1992 the European Union became the main donor to Albania, offering free support to its development through the aid allocated by the EU to Eastern European countries and from the PHARE program. Stabilization and Association Agreement is an international legal agreement between signatory country and the EU, whose function is to establish a legal framework for cooperation and gradual adoption of European standards. It offers the possibility for bilateral cooperation and the free entry of goods duty free state signatory to the EU markets.

4.1. Legal characteristics of stabilization and association agreement (SAA)

SAA Zajmi I. (2010)^k provides the creation of a free trade area between the two countries for a transitional period of 10 years. Also, it provides the opening stages of the domestic market for EU exports. Both sides was engage to implementing gradual reduction customs duties to their complete disappearance during a five year transitional period provided for in the agreement and other measures with equivalent effect as is provided in the agreement. This excludes only the goods included in the list of sensitive products, customs fees which will not change and, therefore, they are left out of this Agreement.

SAA or Transitional Agreement as its integral part, allows certain restrictive measures in free trade between the parties with the aim of protecting the domestic product and making it competitive in the market community, allows its implementation and then to membership Albania in the community, something that would bring the mandatory implementation by Albania of the principles established by the treaties (EU) and European Community *acquis communautaire* (the whole set of norms of the European Community). Trade liberalization provided in the Transitional Agreement in addition to liberalization offered by the parties with legal instruments it takes into account the unilateral international agreements in which the parties adhere.

Fig. 1. Average tariff rate in years^l



Source: Fiscal bulletin 2011

^k Zajmi Iva, 2010, *European Law*, OMBRA GVG, Tirana

^l Average Tariff Rate from http://www.dogana.gov.al/doc/BULETINI%20FISKAL%20JanarTetor%202011_files/image017.gif

The creating a free trade area^m in principle means the removal of barriers and restrictions on trade relationships between the parties as customs tariffs, quantitative restrictions or other measures with equivalent effect. The purpose of this principle is to eliminate trade barriers between the parties bringing the promotion of national products. Thus Agreement provides that, in case of economies with similar or equal levels of development, applicant country's accession can pass through an expedited procedure.

At the other hand, *when the economic development of the countries is different, the immediate opening of the immature market to a more competitive market would have negative consequences for the first.*

The level of economic development of the countries as Albania, which have signed a Stabilization and Association Agreement with European Union *makes that in the agreement would be provided a relatively long preliminary phase, characterized by unilateral trade of relationships (from European Union). Since 2000 the European Commission operates a preferential trade regime to the Western Balkan countries.*

European Union has reduced to 0% of all customs duties on industrial products and agricultural products with the exception of three products: lamb, eggs and some fish products. Transitional Agreement specifically its Title II (Free movement of goods) has been developed in full respect of principles and provisions of the World Trade Organization (WTO), especially Article XXIV of GATT (1994). Other provisions relating to the application of SSA to the free movement of goods specified in the last chapter (III) of Title II of the Transitional Agreement. Articles 19 to 32 contain specific provisions as follows, for all products subject to the SSA. Suspension (Article 20 TA) - Under this clause the parties agree not to impose new customs tariff or measures with equivalent effect on imports, exports or increase existing fees after the entry into force of the TA. Also, the parties undertake not to apply new quantitative restrictions and other measures with equivalent effect or further restrict existing quotas.

Without prejudice to the concessions granted under Article 13 (mutual abolition of quantitative restrictions on agricultural products and fisheries), the afore mentioned provisions do not restrict the exercise of the respective agricultural policies and the Community, or taking any measures under such policies as long that these actions do not affect the import regime. The creating a free trade area (Article 21 of the 22 TA) implies not only the removal of customs tariffs but also avoidance measures or practices of the tax, which directly or indirectly, discrimination between the products contracting parties. Abolition of customs duties on imports is applied for customs duties of a fiscal nature. Dumping and Subsidy (Section 24 of TA) - The parties are free to take action to protect the trade if it detects that the trade with the other party is dumping occurs and / or countervailing subsidies. However, these measures must be in accordance with Article 25 of the TA (general clause for protective measures), with the WTO Agreement on Implementation of Article VI of the General Agreement on Tariffs and Trade 1994, WTO Agreement on Subsidies and Countervailing Measures and with its internal legislation related to it.

5. Custom's role, as part of financial strategy

Special studies on the relationship between tax burden and economic growth (i.e., promoting the investment process) examining the impact of customs tariffs on growth Philip G. (1998)ⁿ, Knight et al. (1993)^o have shown that: the level of tariffs on capital and intermediate goods has a significant effect on

^m Regulation no. 2000/2007 of the European Commission. Section 2 and 3/1 of the Transitional Agreement.

ⁿ Philip Garson. "The Impact of Fiscal Policy Variables on Output Growth" IMF Working Paper WP/98/1. www.imf.org

^o Knight et al., 1993, "Testing the Neoclassical Theory of Economic Growth: A Panel Data Approach", *Staff Papers, International Monetary Fund*, Vol. 40, pp 512-41

economic growth, countries which with lower rates grow faster than the others. Ministry of Finance is responsible for developing a sector strategy for Public Finance Management Bundo Sh. (2012)^p covering customs revenue. Based on Articles 85 and 98 of the SAA to strengthen further reforms in the fiscal system and the restructuring of tax administration, strategy of Public Finance, through macroeconomic analysis covers four basic functions of central government: the forecast of revenue, public expenditure, policy fiscal and public debt.

The main purpose of the financial strategy is to increase the customs standards, data exchange with the European Union in order to implement preventive measures for fiscal evasion, prevention of smuggling, corruption, creation of monopolies, and the correction of market distortions and ensure competition for business.

For this purpose, based on the *acquis communautaire*, the most important reforms in the field of taxation consists on the application of the flat tax^q and increasing the level of excise. Simplification of the VAT refunding^r and no exemptions and incentives applied on profit tax and VAT.

Two Cases of specific application of the tax on the import and export are: *For imports* - Apart from the wholesalers, the persons, whose taxable turnover is less than 8 million AL for each calendar year, are not obliged to register for VAT. These taxable persons conducting imports and exports take NIPT (Tax ID Number), but they declare and pay the local tax on small business and simplified tax on Profits. VAT is applied with 0% for exports, in relation to:

- Goods exported from the Republic of Albania.
- Supplies and Services outside the territory of the Albanian Republic operated by a taxable person, whose place of business or residence is in Albania;
- Supply of Goods and services related to International Transport of Goods and Passengers, except Air Navigational Services in the territory of the Albanian Republic.
- Supplies of Goods and services related to Commercial or Industrial Activities in the sea.

The customs is the only economic observer that directs the strategies of government and other economic operators, as the only data manager and processing of foreign trade statistics.

6. Conclusion

In this paper, we have shown how the function of protecting the economic development of the customs system, given the state of balance of payments, the adjustment of the structure required for imports, the impact on the importation of new technology, affects the economic development of the state. So the revenue from customs influences the growth of GDP and revenue of the state budget. In Developing Nations such as Albania, customs revenues included 20% of total revenues. While in the European Union, customs revenues are very small, ranging from 0.1% to 4.5% due to the common provisions on free movement of goods.

We have evaluated the importance of customs procedures for the success of the domestically market, creating an economic climate characterized by credibility and ability to plan long term strategies. We

^p Bundo SH.2012, *Fiskalitete*, Tirana albPAPER (ed)

^q Mehilli T. Flat tax in reality corresponds at a proportional tax (10%)

^r Instruction No. 17 of the Minister of Finance for VAT was adopted, dated 13.05.2008 www.tatime.gov.al

have pointed out the fact that, the EU is investing to improve the customs system with the prospect that, Albania will be part of a wider market, in which the rules of the game are well known.

a. Implementation of Albanian Customs service strategies:

On the basis of customs legislation⁵, the Directorate General of Customs of Albania has developed policies for the approximation of the standard strategies of the customs with those of the EU as follows:

- Policies to indirect taxes are still applied in part to European standards.
- Tax laws and regulations have been amended to simplify the procedures.
- Significant improvements have been made of an administrative nature. The bureaucratic obstacles have been reduced through the application of electronic system for the taxpayers.
- The structures of the customs and tax have increased the ability to successfully implement the reforms mentioned above.

The SA process involves a number of activities and relationships between the interested country and the European Union, the gradual application of EU legislation by signatory country. Essentially, this process establishes a series of bilateral agreements between signatory country and the EU, concerning customs duties for industry and agriculture, intellectual property rights and standardization and certification procedures.

b. The benefits from Stabilization and Association Agreement:

- Increases availability of local products to be exported to the European common market.
- With the improvement of exports, increases the potential for the development of local companies and national economy in general.
- On the other hand, the Stabilization and Association Agreement allows a better access to European goods, to buyers and local consumers, through administrative procedures shorter, faster and at lower prices.
- Signing of the Stabilization and Association Agreement creates the possibility of obtaining financial resources from various structural funds, as well as development assistance and participation in several EU projects, such as exchange programs for professors and students, collaboration between research centres in the country with the EU.
- The SAA with the EU regarding exports is asymmetrical, which means that export tariffs will decrease, faster than those for imports.

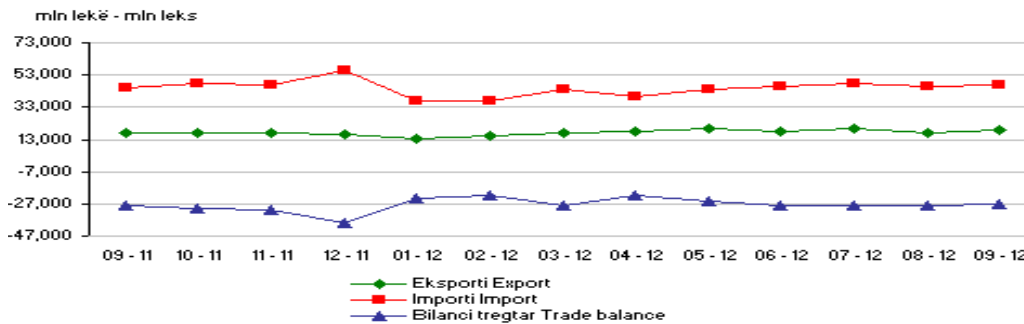
c. Relation between international business and effectiveness of fiscal policy

When we emphasize the exports role, it should be noted that, this activity is an integral part of the overall process of globalization and fundamental changes that have suffered economic and political relations in the international arena.

⁵ Consists on the Customs Code, which was drafted on the basis of European Council Regulation EECNr. 2913/92, date October 12, 1992. Law no. 8449, approved by Parliament dt.27.01.1999, come into force on 15.05.1999. Decision of Council of Ministers no. 205, dt. 13.04.1999 "On the Customs Code Implementing Provisions" designed on the basis of the European Commission Regulation EC no. 2454/1993 as well as other legal acts related to customs operations.

The application of fiscal and monetary policies by the Albanian government to promote exports was intended to: creating comparative superiority of domestic goods in international business and an objective perception of the process of globalization by companies.

Figure 2 Foreign Trade 2012¹



Source: INSTAT

Law no. 9920, date 19.05.2008 "On tax procedures in Republic of Albania"^u has adopted international best practices, tax procedures with the terms and conditions of our country, aiming to reduce informality and improve the climate for business. Basic goal of fiscal policy has been the development of tax system supported by the formulation of *fiscal policies and incentives right for economic and business development*. Parallel to this end, another important feature of this fiscal reform has been *the distribution of tax burden more evenly and less distorting*.

Table 1. Values of Import – Export by years in mln Euro;

Year	Total Export	Total Import	Trade Balance/ Difference	% of coverage
2008	620.65	2,267.38	-1,646.73	27%
2009	498.59	2,100.02	-1,601.43	24%
2010	763.96	2,218.86	-1,454.90	34%
2011	924.30	2,479.06	-1,554.76	37%

Source: Fiscal Bulletin 2012 Foreign Trade Customs^w

¹ Mehilli T. The date of Foreign Trade November 2012 are significant for our conclusions, in reference to the trade balance and its problems. www.instat.gov.al

^u Directorate General of Taxation - Tax legislation in force from - http://www.tatime.gov.al/gdt/Tax_legislation_in_Force.aspx

^v Mehilli T. I want to remember that the concept of comparative superiority of goods destined for international business is based on the follow principle price - cost - quality and therefore the two main political instrument of a government: fiscal and monetary policy.

^w Taken from: <http://www.dogana.gov.al/doc/Buletini%20%20Treg%20Jashtme%20Janar%20Gusht%202012%20publikim.htm>

From the statistical data on trade balance' difference, we note that, our economy is based mostly on imports and the policy instruments used by our government hadn't the desired results Mehilli T. at al. (2012)^x.

Referred to the above results, we can concluded that: government economic policies were such that the savings of Albanians are oriented towards improving the budget deficit and confirms that the fiscal burden supported by taxpayer has been elevated.

So, the trade deficit problems and the state budget problems, in reference to the the impact of EU political – economical situation', are deeper than trade barriers (customs). They relate closely to the internal economic structure of the country and the lack of development strategies.

Some of the problems in a summary are:

- The progress of legislative reform and the business climate (such as uncertainty of property rights, fragmentation of agricultural land, administrative burdens and subjectivity of administration, low quality of public services, lending problems etc.) Dumi A., Mehilli T., (2012)^y;
- The underutilization of modern technology, poor infrastructure.
- Inability of firms on competing and exporting Albanian products.
- Absence of Institutional bodies for verification and quality standards of the goods and the services.
- Marketing of products "Made in Albania" for export almost does not exist.
- Low percentage of employees in the export sector.
- Lack of partnership schemes between local companies and international ones.
- A weak role of the Albanian Competition Authority, which must support export production.
- Lack of an export centre of export products near the most important ports. The centre will process products but also offer a range of additional services such as standardization, packaging, etc., giving the product an added value against international standards.

Although, the problem of the use of fiscal incentives is a controversial issue in the literature and empirical analysis of current studies show that, levels of taxes have a significant influence in establishing the right balance between savings and investment, thus the economic growth.

The removal of customs tariffs as a result of SSA shows that, competition from EU countries has increased pressure for investment in technology, research, development, or clearly defined strategy of domestic business. These investments in the long term should lead to increased competitiveness of products "Made in Albania".

The factors cited above and the situation of the international business, the new strategies of customs as part of financial strategy show that should be implemented new development strategies and a better coordination between institutions responsible^z

^x Mehilli T., Xhafa K., Naqellari A., Demo E., "The Influence of Financial System in Albanian Economy" 2002, *Mediterranean Journal of Social Sciences*, vol 3,no.6, pp 11-20

^y Dumi A., Mehilli T., "The Institutional Progress and Strategic Reforms in Albania, Require Active Role of Government Policies",2012, *Acta Universitatis Danubius. (Economica)* Vol 8, No.1, pp 82-94

^z Mehilli T. I am referred to a better correlation to the monetary policies of Central Bank of Albania and fiscal policies implementing by Ministry of Finance.

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