FOREIGN DIRECT INVESTMENT IN BANKING SYSTEM: ALBANIAN CASE

Jonida LAMÇJA, MSc
Lecturer at the “Aleksandër Moisiu” University of Durrës, Albania
Contact: E-mail: jonidalamcja@yahoo.com

Abstract
Foreign banks can be a key element in the process of financial integration of our country in international and European financial system. This paper analyzes the importance of foreign capital in the world economy and the impact of foreign direct investment in the banking sector in Albania. Was given an overview of the situation of foreign investment in Albania and the advantages or disadvantages that the country faces in trying to attract foreign investors. Foreign direct investments in Albania have been a very important factor for economic growth; however, Albania remains one of the least developed countries of the region, marking the smallest attracting FDI during the transition. FDI to bring the most advanced technology, and modern management knowledge and contacts with foreign clients and ensures that the country's economy to benefit from this thing, but doing the retraining of the workforce in Albania.

Keywords: foreign direct investment, banking system, technological development and economic growth.

Introduction
Foreign Direct Investment (FDI) are an important factor in the economic development of a country at any stage of development. FDI provide necessary investments in growth and development of technology when domestic savings can not provide them. Foreign direct investments in Albania have been an important factor for economic growth, however, Albania remains one of the least developed countries in the region, marking the smallest attracting FDI during the transition.

The purpose of the study
The purpose of this topic is to provide a vision of foreign direct investments mainly in the banking sector. Analyzed the effects of foreign investments in Albania, barriers and reasons for investing in Albania and the role that FDI have in the banking sector.

Theoretical perspective of foreign investment
Legal framework of foreign investment
The normative framework of foreign investments in Albania is based mainly on 'Law 7764, dated 2.11.1993'. Law which shows the first step really important that Albania decides to attract foreign direct investment. Albania has a liberal legal framework regarding foreign investment in order to encourage them. The law provides guarantees to all foreigners (natural or legal persons) willing to invest in Albania.

FDI can be made in all sectors of the economy, provided they do not affect:

a) national security and defense interests of Albania;
b) regulations in force for the protection of the environment;
c) the legal and public order, health and morality rates.

Foreign investments in Albania are carried out on the basis of an authorization issued by:

a) The Council of Ministers,
b) Ministry of Trade and Foreign Economic Cooperation, for all other cases, except for investments with a value below a minimum value of 50 thousand USD in cash or in kind, or its equivalent in other currencies convertible, calculated with the average exchange rate announced by the Bank at the time of application.

On foreign investments valued under 50 thousand USD, the authorization issued by local government bodies.

On foreign investments in the Albanian state-owned enterprises, regardless of their value, Albanian state owned enterprise shall obtain approval from the relevant ministry.

The last of FDI is the 1994-er "for foreign direct investment". He has provided a favorable climate for foreign investors in Albania by offering them

---

1 AIDA
2 Law nr 7594 date 4.8.1992
investment opportunities in all sectors, participation, etc.

Promotion of FDI through improved legislation

FDI is the largest source of external finance in developing and transition. Countries of Central and Eastern Europe and Central Asia are in good position to compete for FDI if they adopt pro-development policies and laws and practices supporting investment and business development. When it comes to attracting FDI, size, just as the level of development and geographical position, plays an important role. Foreign companies encountered great difficulties in registration offices in transition economies. There are simply communication problems that slow procedures, although have plenty of time until all application forms are properly completed. Not coincidentally pioneers of FDI prefer the establishment of the joint venture with local people and companies, so that they can create access to local legal spaces. In contrast to countries in transition, in developed countries noted that foreign investors find it easier to obtain the necessary information needed to start a business. Also, in developing countries noted the prevalence of local professionals who are tasked with supporting foreign investors in various processes they face opening a new business. Usually small countries do not manage to attract multinational corporation and industries that produce for export markets to a large extent. Although this limits the degree of competition with larger host countries and low cost in attracting FDI export-oriented from a variety of sources, Albania, with its arm free and motivated workforce has a good potential to become a center/core manufacturing, and services to exports. Draft mainly focus on tax-free periods (Article 3 and 10) and the exceptions to it as the main instrument. It is interesting to mention that "free periods" tax or tax exemptions favor high-profit investments that do not need incentives and encourage tax avoidance, because it is relatively easy for firms that are not exempt from taxes which to spend their profits to firms excluded. The length of time without tax also creates opportunities for abuse and extension, and since they are related to time, they have the tendency to attract more investment with short-term than long-term. Investments by governments physical infrastructure efficiently improve the investment climate for FDI by subsidizing the cost of the total investment by foreign investors and thus increases the rate of return. Multinational enterprises are particularly sensitive to infrastructure decide where their investments designed to feed the global, regional or local, as these investments are by nature require efficiency.

Classifications of foreign direct investment

"One of the main causes of the diversity of definitions of FDI comes from changes in the importance attributed to the characteristics of companies operating in the international arena".

According to the International Monetary Fund, foreign direct investment known as FDI refers to an investment made to acquire lasting interest or long-term economic enterprises operating outside investor. Direct investment is because the investor, who can be a foreigner, company or group of entities, is seeking to control, manage or have a significant control on foreign entrepreneurship. Nuances of FDI have taken various forms, being classified into five types.

- The first type of FDI is concerned with FDI used to gain access to specific factors of production, such as resources, technological knowledge or goodwill that is owned by a company in the host country.
- The second type includes FDI which are performed to gain access to cheaper factors of production such as labor force. The study on this type of FDI is attributed to Raymond Vernon in his theory of the product cycle.
- The third type of FDI relates to firms that compete internationally by undertaking a series of investments in the competing countries. This is realized through the organizational form joint venture.
- The fourth type is related to FDI aimed at consumers access host country. In this type of FDI is to ensure that efforts are all products and services for customers receiving the same as offer them for domestic consumers and investors.
- Type of fifth and last of FDI related to diversify trade aspect of regional integration. This type occurs when the local host country presents advantages for foreign companies wishing to invest to gain access to the investment market.

Some economists, such as Caves, Kojima and Narula gave their ways of sharing of FDI from the perspective of the investor (country of origin of FDI). Caves divides FDI in horizontal, vertical and conglomerate. Horizontal FDI aimed at producing the same or similar to those produced in the country of origin. Vertical FDI consists of geographical separation of the different phases of the product life cycle, hence stimulate commerce across borders and increase the chance of branches to export. Conglomerate FDI can be a mixture of horizontal and vertical investments which include investment in an industry of a different

---

3 Article 3 Law nr 7594 date 4.8.1992
4 Eliona GREMI, Elona ILJAZI, Selda XHUPI, IHD
5 Report of foreign direct investment in Albania, 2010
6 Eliona GREMI, Elona ILJAZI, Selda XHUPI, IHD
8 Hood and Young, 1979.
9 Millar, Clegg and Chryssochooidis, 1997
10 Caves 1971
nature. Kojima\textsuperscript{11} classifies FDI as oriented toward trade or anti-trade oriented. Kojima says that for developing host countries, FDI in industries ranging intensive use of labor are 'creative trade'. While FDI going to use capital intensive called 'trade substitute. "Promotion of trade 'aimed at supplying other markets. Narula FDI classifies as' substitutes trade " that go towards activities that replace imports to supply domestic markets. "Promotion of trade 'aimed at supplying other markets. 'Complementary trade' when directed to rationalize production of auxiliary equipment in export markets, and to 'avoid trade' if they intend to use the unused part of the market, with preferential trade agreements. In general we can say that: FDI is a term used for the purchase of physical assets outside the limits as systems and equipment under the control of the parent company.'

The situation of foreign direct investment

Reasons for investing in Albania

- A place where life take swift reforms, and focuses on doing business ease, a strategic location, access to free markets, low taxes and economic incentives, and a motivated work force, educated and competitive, all this make the country an excellent destination for investment.
- Strong Economic Performance. Positive economic growth recorded by indicators of GDP in 2010 grew by 3.9% and 3% in 2011, making Albania be ranked alongside strong economies of South-Eastern Europe.
- Its location in the center of a natural crossroads between the major corridors of transit as well as the connection with European transport network provides Albania a strategic position and favorable foreign exchange trade.
- Registration of new business done in 24 hours with an amount of 100 ALL. Business licensing is done through a simple and transparent procedure by the National Licensing Center, and easily verified via the Internet, with a total of 100 ALL. Online tax system for documentation and payments. Business legal framework is in line with EU legislation.
- High potential for investment. The Albanian economy has untapped potential in terms of renewable energy, tourism, agribusiness, infrastructure and services. Natural sources include hydro, solar, wind, farmland and about 400 km coastline. The country is rich in oil and gas and valuable mineral deposits such as copper, iron chrome.
- Lower taxes. Fiscal regime in Albania taxation imposes a more liberal than many countries in the region.

- Labour force is educated and competitive. In Albania counted over 1,071,948 young, educated professionals. Over 57% of the population is under the age of 35. English, Italian, French and German are widely used.
- Net inflows of foreign investment on the rise. In the last decade there has been a withdrawal of foreign investment in progressive growth. Liberal legal framework governing foreign investment guarantees equal treatment and fair for foreign investors. There is no limit on the percentage of foreign participation in the company - 100% foreign ownership is possible. Foreign investors have the right to remove all funds and their contributions to the type of investment. The Albanian government has adopted and applies special protection for foreign investors in the event of litigation in which they are parties.
- Rapid improvement of infrastructure. Improved infrastructure has been a priority and is concretized through the implementation of infrastructure works mainly in the road network
- Quality of life. Assessed among the highest in the region based on Quality of Life indicators provided by International Living Magazine. Albania offers a safe environment to live, with great potential fun and entertainment.

Barriers of FDI in Albania

Barriers faced by FDI in Albania are:
- Problems in cooperation with local officials
- Lack of raw materials
- Preferences locals to buy from locals
- Repatriation of profits
- Domestic currency undervalued / overvalued / black market
- Technology backward
- Business mentality to the local population
- Low labor productivity
- Barriers due to cultural considerations
- The banking system unstable
- Lack of managerial abilities
- Property rights are not clearly defined
- High Risk Investment
- Volatility of exchange rates
- Underdeveloped infrastructure business

Elements determinants of FDI

1. Terms of factors
A country creates its own important factors as resources and technology base. The position of the factors in a given time is less important than the fact that they are improving. Disadvantages local production factors cause newness. Opposite conditions as deficiencies in labor or raw materials force firms to

\textsuperscript{11} Kojima 1987
develop new methods, and this innovation leads to a national comparative advantage.

2. Terms of the request
When the market for a particular product is locally wider than in foreign countries, local firms should pay more attention to the product than foreign firms, resulting in a competitive advantage to local firms at the time of exporting this product. A local market with higher demand leads to a national advantage. A strong local market, trend setters helps local firms to accelerate global trends.

3. Supporting and related industries
When local supporting industries are competitive, the firm enjoys more cost effective and innovative inputs. This effect is enhanced when the suppliers themselves are strong global competitive.

4. Strategy, structure and competition of firms
Local conditions affect in the strategy of firms. For example, German firms tend to be hierarchical, while Italian firms tend to be small and are run more like extended families. This structure and strategy helps to determine which type of industry in a national firm will be known.

5. Government
The government’s role is to:
- Encourage companies to increase their performance, reinforcing e.x strict standards for products.
- To stimulate early demand for advanced products.
- Focus on specialized factors of creation.
- To stimulate local rivalry by limiting direct cooperation and reinvigorate antitrust rules.

6. Chances
Another element are the chances that might exist for the firm itself or from which it benefits by being part of a particular environment.
In the Porter Diamond, low rivalry makes an attractive industry. Meanwhile, in a given time a firm prefers less rivalry, in the long-term local rivalry is more preferable since it puts pressure on firms to bring innovation and improvement. In fact, a higher local rivalry results in a higher global rivalry. Local rivalry forces firms to move beyond basic advantages that the country of origin provides and as the lowest cost. The diamond should be seen as a system. The effect of a point depends on others.

Banking system and foreign direct investment
Role of FDI in banking
While time passes, the concept of foreign direct investment and the role and importance of FDI for host countries has changed. In the past, the prevailing views are presented in Marxist economic doctrine, a doctrine which states that foreign direct investment not only have a positive impact on economic growth of the host country, but in fact it is the opposite by foreign direct investment are a user element that is used by developed countries to developing countries. Studies have shown that foreign direct investment have brought unquestionable benefits primarily for the least developed countries and those in transition. Usually foreign capital, part of FDI transfers to the place that he goes not only capital but also temporary agreements, advanced management and experience in technology and offers opportunities in transition countries placed in foreign markets. Many empirical studies show that the economic development of a country is a positive feature of the development of the financial system and in particular the banking system. Some studies have shown that countries with developed financial system live through the accelerating pace of real GDP growth per capita. In transition economies banking system meets most of the functions of a financial system because of other financial intermediaries. Studies have argued the necessity of the presence of foreign banks in transition countries. The favorable or negative impact of the presence of foreign banks should be watched closely linked to overall levels of a country’s economy, given that this effect is different for developed countries, developing countries or in transition. Development of the banking system is coupled with the stability of the financial system and strengthening internal and entry of foreign banks usually associated with the development of the financial market of the host country. Banking stability refers to a better supervision and a safe placement in the host country. These studies showing a positive relationship between foreign banks and banking stability have shown that influence the improvement of accounting practices and financial reporting in accordance with international standards. Local banks can benefit from the presence of foreign banks in more than one way. The entry of foreign banks Interbank market develops and attracts as their clients businesses that are customers of other foreign banks. However it is necessary to note that generally the transition countries foreign banks are more profitable than local banks. Generally we can say that the assumption that exists shows that foreign banks constitute a stable source of credit if international banks with regard to their affiliates may have the possibility of attracting additional funds. Foreign direct investment in the banking sector can also be accompanied by some disadvantages. Foreign banks may have different objectives and methods of local banks and these investments do not comply with the economic policies of the host country. In case the

13 Papi and Revolta 2000
14 Caprio dhe Honahan 2000
local banks are not developed they will not be able to react properly in international competition, risking in the company's activity or gaining in significant amounts or could go into bankruptcy. Also the presence of foreign banks in periods of economic crisis can be dangerous. Extern Control in the distribution of credit can translate into additional power for each of the economies of the host countries. For example, foreign banks may have a strong relationship with foreign companies operating in the host country. It may be that foreign activities abroad to be financed by local capital, while local projects do not receive funding, and this usually happens when foreign banks have no knowledge about the local market. This approach also prevents the development of the local economy.

**Foreign direct investment in Albanian banks**

Banks, in their role as financial intermediaries establish the balance between subjects with a surplus and those running trade deficit. No bank intervention would have been difficult if not impossible process of collecting and channeling a large number of small investments of individuals and the movement of capital. Their role in private business can be explained in two ways:

First, private companies do not have sufficient funds to finance all investment needs. Secondly, although direct financing can replace bank loans, many authors have the principle that the market can not be a convincing solution for transition countries. This argument becomes important especially in circumstances in which the market coupons are not yet operational. Banking reform in our country as well as throughout the rest of the countries in transition aimed at achieving the following objectives associated.

1. Enhancing the role and autonomy of the Bank of Albania in the highest monetary authority.
2. The liberalization of the banking sector through privatization that did the state-owned bank and encouraging private banks.
3. Improve the quality and competition in the banking sector
4. Introduction of an efficient control banking.

During 2006 many banks opened their branches and have a grouping them as follows:

Group 1: Emporiki Bank, First Investment Bank, Tirana Bank etc.
Group 2: Alpha Bank, Credins bank, NBG ETC.
Group 3: Raiffeisen Bank, American Bank of Albania etc.

In 2008 the finances were the main beneficiaries of foreign direct investment, accounting for 32% of the reserve's investments are directed from within the region.

**Conclusions**

1) Different states take a certain number of tax incentives to encourage investment in order to develop an area or a particular region, given the scope of its development.
2) Foreign direct investment is increasing dramatically in the age of globalization. They have played an important role in economic raising during the process of globalization.
3) Studies have argued the necessity of the presence of foreign banks in transition countries.
4) The banking system still has room for other foreign investors, powerful, reliable consolidated.
5) Advantages of FDI in the banking sector are still unearned how and properly
6) According to an OECD report carried on FDI in Eastern Europe based in 11 developing countries, including Albania, the main determinants of FDI are: political stability, fiscal system, infrastructure, economic stability, corruption, legal and other determinants of FDI.

**Recommendations**

1) Elimination of unnecessary regulations in order to reduce corruption.
2) Improvement of the legal framework not only in terms of legislation but also to its implementation.
3) All the countries of Eastern Europe, each in different measure, they need to make further efforts to simplify the tax system and law and consumer protection rules, facilitation of permits for land acquisition and construction license, acceleration of trade disagreements solutions and elimination of discriminatory conditions to foreign investors.
4) One other important area is the expansion of the number of bilateral agreements with other countries, which will result in improvement of its image in the eyes of investors.
5) Further improvements are needed and infrastructure. It plays a very important role in attracting foreign investors. Can be implemented various projects that would outcome.
6) Also, can develop specific geographical areas in the country.

---

16 Schnitzer, 1999
18 UNCTAD, WIR 10, page 52.
References
5. Nagesh Kumar, Availability of infrastructure, of foreign direct investment and their export orientation: an exploration of suburban areas (System for Scientific Research and Information in Developing Countries 2001) http://www.gdnet.org/pdf/pdf
6. OSCE guide best practices for a positive climate for business and investment, report of foreign direct investment in Albania,
9. Schnitzer, 1999