Raffaella Barone (Italy), Donatella Porrini (Italy)

The role of foreign banks in the Albanian economic system

Abstract

The aim of this paper is to analyze the role of foreign banks in the restructuring process that has characterized the Albanian banking system in transition from the planned economy to the market economy. The backward state in which the Albanian economy was left after the fall of the communist regime made necessary a plan of reforms of the legal and financial system. The new plan of rules in the subject of regulation and banking supervision fostered the opening of new banks and new branches which increased both the demand and the supply of credits to the private sector. On the assets and deposits side, at the present, the banking system of Albania is highly characterized by the presence of foreign banks. Assuming that, on the one hand, an easier access to credit allows small enterprises to develop and contribute to the economic growth of a country and, on the other hand, that only an efficient banking system lays the basis for an easier access to credit, in this paper we will concentrate mainly on the Albanian banking system with special attention to the role of foreign banks.

Keywords: bank competition, financial stability, transition, foreign banks.
JEL Classification: G21, G28, K22, O23.

Introduction

An efficient banking system that allows for a proper credit allocation and a suitable payment system becomes a priority aim for all the Eastern European countries that have passed through a transition period from planned economy to market economy[1]. In the specific case of Albania, during the period of transition, there was also the problem of infrastructure. Albania experienced a particularly centralized and repressive communist regime which produced an entrenched backward level of production structures and living standards. The isolationist policy followed by the communist regime resulted in the country experiencing a serious economic and institutional crisis.

As other countries of Central and Eastern Europe, Albania had to start the process of building or re-building completely functional financial systems. Bases for such systems had never existed before or in the best case they had not existed for the last forty years. Facing a large number of problems with the existing banking systems, these countries embarked into a number of reforms. It is noticed that the process of reforming the financial and banking sector followed the main steps of privatization of banks and enterprises that were banks' clients, and opening the doors for the foreign banks.

Thus, one of the main steps of this process was allowing foreign capital to enter the banking system through the opening of foreign banks (i.e., branches, affiliations, joint ventures, representative offices) or through the privatization (completely or partially) of the existing state banks.

In the countries of the Balkans, the presence of foreign capital in their banking systems has intensified encouraging their development as well, even though not to an expected level. On the other hand, concerns about a total or partial dominance of foreign capital in the banking system are increasing.

Critics inside the countries against liberal policies that allow the entry of foreign banks in the market or the privatization by foreigners are becoming stronger. Also, demands on implementing the protectionist policies in this area of the economy are strongly arising.

The paper proceeds as follows: in section 1, we analyze the banking privatization process that has characterized the Albanian economy in the period of transition from communist regime to free trade; in section 2, we consider the role played by foreign banks in the credit access of small and medium-sized businesses; in section 3, which is devoted to the relation between foreign banks and credit allocation, we offer a review of the literature; in the final section there are conclusions.

1. The banking privatization process: from the growth of 1990 to the crash of 1997

The communist regime, which governed the economy of Albania until the nineties, produced with its isolationist policy a persistent backwardness of the productive structures and living conditions in the country. After the collapse of communism, the early years of the transition to a market economy were characterized by the instability of the socio-economic system.

The GDP plummeted from 1991 to 1992 because of the socio-economic chaos and of the rapidly growing inflation produced by the demand for higher wages, by the scarcity of foods and by the currency depreciation. From 1992 onwards, the

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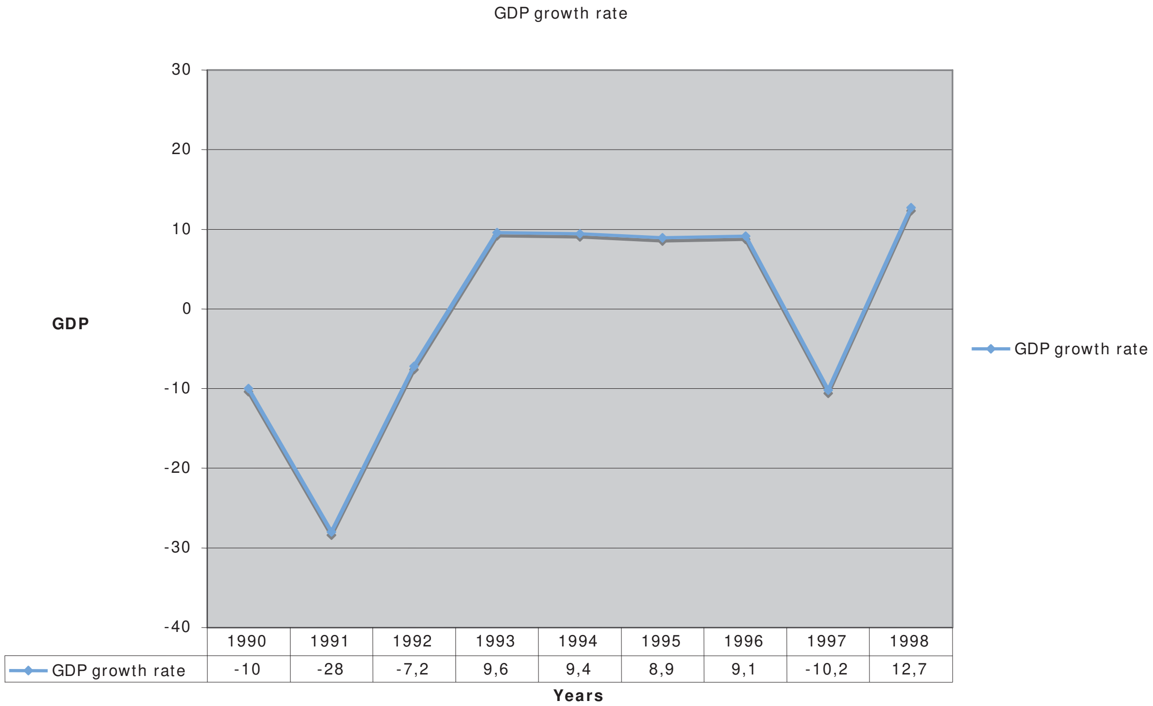
[1] See Coletti (2005).

government, which was democratically appointed, set up a plan of reforms to promote the country's economic growth. This program gave rise to a period of growth from 1993 to 1996, when the average GDP growth rate amounted to 9%. The financial and monetary reforms were scanty.



Source: IMF, Statistics, 2008.

Fig. 1. The GDP growth rate in Albania from 1990 to 1998

Albania entered the market-economy with a rudimentary financial system, as happened to other countries that left the planned economy. There were problems of governance besides the predominance of the public universal banks, which were committed to supporting the government both in carrying out its functions and as agents engaged in production procedures. In this scenario, the bank of Albania was established with the features of a modern western central bank and an open banking system was started up with the subsequent authorization of four banks during 1992: National Bank of Albania, Savings Bank, National Commercial Bank, Agriculture and Development Bank.

These banks were founded by the decision of the institutions and all the securities which in the past had been held by the earlier state bank were transferred there. The government chose the universal bank as its organizational structure in order to offer a wide variety of banking and financial services.

The system established was marked by high concentration: the three main banks held 90% of the market[1]. The Saving Bank alone offered 75% of all the banking services supplied on the market thanks to the almost all transfers of family deposits, while the National Commercial Bank monopolized business accounts and foreign transactions.

This frame promoted the huge economic growth which characterized the early years of the transition process but at the same time the transfer of securities has increased the amount of outstanding credits.

The existing banks were not able to cope with the credit requirements driven both by the excellent results achieved by the economy till then and by the positive expectations for the future. The Bank of Albania, therefore, intervened, setting a limit to the issue of credit.

In that period the financial market was opened to foreign agents with the establishment of foreign private banks that, however, did not compete against the government banks. The first Albanian bank with foreign control was the Italian-Albanian bank, which was founded in 1994 as a joint venture between the "Banca di Roma" and the National Commercial Bank, with a minority shareholding of the European Bank for Reconstruction and Development (EBRD). The Arab-Albanian Islamic Bank was another banking joint venture which was created at the beginning by the National Commercial Bank and by Arab investors.

[1] For a deep analysis on the relationship between banking concentration and economic growth see, among others, Claessens and Laeven (2005), Deidda and Fattouh (2005), Berger et al. (2004), Beck et al. (2003), Panzar and Rosse (1987).

An informal financial market developed alongside the formal financial system[1], based on the inflow of remittances and it was managed by informal financial agencies that attracted a lot of investors by offering higher interest rates[2], which were paid using the capital invested by other investors. An insolvent pyramidal scheme arose because debts were greater than credits. The poor knowledge of the financial instruments on the consumer's side and the weakness and lack of transparency of the institutions and individual policy makers, kept investors from identifying the risk that the whole country was running: the government encouraged people to invest in the pyramidal scheme[3], in spite of the warnings of the IMF of which Albania had been a member since 1991.

At the end of November 1996, the failure of the Sude made the speculative bubble explode: the immediate collapse of confidence caused a run on the banks and the failure of other agencies. The government refused to indemnify the depositors and the population responded with actual civil war. The new government was only able to control the situation in July, thanks to the help both of the IMF and World Bank.

The collapse of the financial system and the civil war, with the breakdown of production caused a contraction of the GDP which fell to -10% as plotted in Figure 1 and a 40% rise in inflation, because of the depreciation of the Lek. The effects on the economy were recovered fortunately in a short time, thanks to the efforts of the new government whose action was favored by the price system and wage flexibility. The society paid the biggest cost: the explosion of poverty was followed by the total lack of confidence in the financial institutions that for a long time made it difficult for an efficient and transparent financial system to emerge.

The Albanian events seem to be different from those of its neighbors. Actually, although it shares with them the experience of the financial crisis in the mid-nineties, it differs for its characteristics: in Bosnia, Serbia and Montenegro, the crash of the financial system happened inside the banking sector because of the existence of too many banks[4] that were created as a result of the market liberalization and privatization process. This procedure took place in an inadequate normative system, due to institutions' lack of ability to manage the change.

The result was an uncontrollable increase in credits, in particular non-receivable credits[5], which then produced the collapse of the financial system developed until that moment.

In Albania, where only four banks operated with the permission of the government, the crisis affected the banking institutions indirectly, while the direct protagonists were financing companies and agencies belonged to the informal financial system that had grown since 1993. The scanty use of the credit market due, on the one hand, to lack of expertise and to the banks' reluctance to extend credit to private individuals, above all small and medium sized enterprises (SME), and, on the other hand, to the low demand for credit, replaced with the availability of equity capital in the form of remittances, were to Albania's advantage.

Even if the cost of the crisis was very high, because of the increased poverty and the lack of confidence in the financial and banking system on the people's part, the existence of a banking system exempt from the crisis enabled stability to be recovered more quickly, which fostered the opening of new banks during 1999.

2. Banking system and the presence of foreign banks

2.1. The characteristics of the Albanian banking system. In consequence of the pyramidal scheme breakdown, it was necessary to introduce a strict policy in the matter of financial intermediation. This started a period of great reforms that affected both the legal and the financial systems. The Albanian institutions invested many resources in supervision and control activities, with the aim of avoiding the instability and the inflationary phenomena that had characterized the previous expansionist period. One of the first steps in this direction was the approval of act n. 8269 of December 23, 1997, which made official the existence of the Bank of Albania[6]. In reality, act n. 7559 of April 22, 1991 put an end to the experience of the Albanian State Bank, a legacy of the communist dictatorship, and built the basis for the establishment of a poly-functional central bank, "responsible for the internal and external national money defence by the implementation of a monetary policy"[7]. Nevertheless, the Bank of Albania still didn't have a clear role: although it was supposed to

[1] While some agencies (Vefa, Gjallica, Kamberi), which took part to the pyramid, held a few real investments, the Xhafferi, Populli and Sude held none. Almost all the agencies were involved in criminal activities, specifically the smuggling of consumer goods into Yugoslavia.

[2] A vicious circle has been created because the agencies steadily had to increase the rates in order to attract the new investors. The interest rates raised from 4-5% to 12-19% monthly, during the top of speculative period.

[3] In Albania, 2 out of 3.5 millions of the residents invested in the pyramidal scheme, that in November 1996, achieved the nominal value of US$ 1.2 billion.

[4] In Bosnia, in 1999, there were 61 banks, reduced to 33 in 2004. In Serbia, in 2000, 81 banks operated, reduced to 43 in 2004.

[5] In 1995 it amounted to 75% on the total.

[6] The presence of an Albanian Central Bank, free in its implementation of monetary policy, has been confirmed in section 161 of the Albanian constitutional act, approved on 10-21-1998.

[7] Section 3, act n. 7491 04-29-1991.

control the operability of the system, it was not able to contain the explosion of formal deposits, also because it was lacking the support of the government, which it opposed with the watchdog role operated by the new-born central bank.

It was only with the act of '97 that the Bank of Albania gained independent legal status and an operating autonomy that made it free from any other Albanian institutions, in order to let it execute its tasks and pursue its purposes[1], among which the achievement and the preservation of price stability had great priority. To the extent that this is compatible with its fundamental purpose, the Bank of Albania should promote and support the definitive moving towards a market-based model of the international trade system, the internal financial market and the payment system. It should also encourage the establishment of monetary and credit conditions that could support a sustained and balanced economic growth of the country[2].

The powers assigned to the Bank of Albania cover a large spectrum of functions that could be summarized as the definition of banking system liquidity and creditworthiness conditions, the operability of the payment system, the issue of legal money, the management of official reserves, the employment of direct and indirect monetary policy instruments, the action as a lender of last resort, the issue of government securities, the financing of public deficit and the management of the State Treasury[3].

The Central Bank has also the task of supervising the operability and the stability of the banking system. The constitution of the new bank, both local and foreign, is subordinate to the approval of the Bank of Albania[4].

Due to the preceding experience of the Albanian economic system, it seems important to stress that, during the constitutional phases, some prohibitions have been explicitly introduced that help to define the degree of freedom in which the Bank of Albania operates; this has been done in order to prevent a direct central bank intervention from producing a misleading effect for the new-born Albanian market[5].

Actually, the banking system is controlled according to act n. 9662 of June 01, 2007; this act defines the conditions to access and operate in the Albanian banking system. In order to obtain the necessary authorization from the Bank of Albania, banks should be set up as a joint venture, while there is no restriction on the participants and on the capital formation (the minimum initial capital required cannot be less than one million Lek). As regards personal requisites, the bank managers should have at least three years' experience in the same sector and every bank should have at least two executive directors.

The last few years have been characterized by a great dynamism deriving from a set of elements such as the remarkable increase of the credit footing, the opening of new banks and branches and also the reforms of banking supervision amended in order to conform the banking system to Basle standards[6]. Moreover, the Albanian banking system has recently been characterized by some important institutional developments: the restructuring and privatization process of public banks, the establishment of banks with domestic capital and the existence of foreign banks has changed the Albanian banking system into a dynamic environment where more and more efforts are made by the banks to improve their market position. The financial system in particular has undergone a quantitative development; with regard to the qualitative dimension, at the moment it is important to encourage the diversification of the products and services supplied in order to improve the relationship with customers and to establish a long-term relation between firms and banks.

As a result of the start of the liberalization process, the Albanian banking market was characterized until 2000, by a steady growth of the concentration level because of the dominating position of the Savings Bank which, in 2000, held 63.3% of the credits and 71.3% of all deposits. Since 1999, the establishment of new commercial banks has fostered the distribution of the market shares and the reduction of the concentration level.

At present, the Albanian banking market is dominated by the National Commercial Bank and the Raiffeisen Bank (which benefited from the Savings Bank's privatization), the biggest Albanian bank with regard to both the presence in the country and the allocated sums[7]. A lot of private commercial banks, local and foreign, have opened branches in the most important cities. Four banks among these are controlled by Greek commercial banking companies (Alpha Bank, Emporiki Bank, National Bank of Greece, Tirana Bank); the German ProCredit Bank; two Italian banks: since January 1, 2008, the Italian-Albanian Bank of the Intesa Sanpaolo Group (in joint-venture with SIMEST "Società Italiana per le Imprese all'Estero" and the European Bank for Reconstructon and Development,

[1] Section 1, sub-section 3, act n. 8269 12-23-1997.
[2] Section 3, act n. 8269 12-23-1997.
[3] Section 3, sub-section 4, act n. 8269 12-23-1997.
[4] See section 5 and 6, act n. 9662 on 12-18-2006.
[5] See art. 4, act n. 8269 on 23/12/1997.

[6] For this purpose, at the end of 2006, the Albanian Parliament passed the new act "On banks of the Albanian Republic" to regulate the activities of banks operating in the country. It was the result of many years of Albanian and other European countries' joint experience in banking system development.
[7] The Raiffeisen Bank and the National Commercial Bank held 31.94% and 13.40% of the credit market, respectively.

EBRD) merged with the American Bank of Albania, founded by the AAEF (Albanian American Enterprise Fund) and founded the brand American Bank of Albania, under the control of Intesa San Paolo. The "Banca Popolare Pugliese" is a member of the Italian Development Bank (IDB), 95% of whose capital is held by individual investors, with a share of 5%. The United States can count one bank: Union Bank – Western Union. As a result of the transfer, in 2007, of 75% of Popular Bank capital to the French Societé General and of the selling in February 2008 of 22.17% of Credins Bank to the Dutch group BFSE Holding BV, only one banking institute remains Albanian property: the Union Bank which began its activity in early 2006.

In July 2007, a licence was granted to another foreign bank, the First Investment Bank. Jnt. Stk. which is a branch office of the Bulgarian First Investment Bank.

Observing the market shares of the same banks listed in Tables 1 and 2, from 2006 to 2007, we see that the concentration of the banking market is still high, especially because of the lack of dynamism of the small banks whose growth could enable the market share of big international banking group to decrease further.

Table 1. Banking operators in Albania as of March 31, 2008

	Foundation year	Number of branches in Albania			Number of agencies	Number of employees		
		2006	2008	Δ%		2006	2008	Δ%
Raiffeisen Bank	1999	37	98	62.2	46	1263	1402	9.9
National Commercial Bank	1999	21	39	46.1	20	439	555	20.9
Italian Development Bank	1999	1	5	80.0	7	18	43	58.1
Tirana Bank	1996	32	42	23.8	4	377	467	19.3
National Bank of Greece (Tirana Branch)	1996	4	25	84.0	19	154	276	44.2
International Commercial Bank	1997	5	5	0.0		52	56	7.1
Alfa Bank (Tirana Branch)	1998	9	20	55.0	1	105	205	48.8
American Bank of Albania	1998	10	39	74.4	15	367	496	26.0
ProCredit Bank	1999	21	27	22.2	1	567	824	31.2
First Investment Bank (Tirana Branch)	1999	1	7	85.7	3	48	94	48.9
Emporiki Bank	1999	3	17	82.3	7	92	182	49.5
Credit Bank of Albania	2002	2	2	0.0	1	35	35	0.0
Credins Bank	2003	11	27	59.3	4	169	301	43.9
Popular Bank	2004	29	33	12.1		284	384	26.0
Union Bank	2006	3	22	86.4	12	73	179	59.2
TOTAL		190	408	53.4	141	4189	5568	24.8

Source: Bank of Albania, Economic Bulletin, vol. 11, n. 1, 2008, p. 78; Albanian Association of Banks, Annual Report (2007).

Table 2. The market share variations in the Albanian banks

	Assets	Deposits
	Percent variation from IV/2006 and IV/2007	Percent variation from IV/2006 and IV/2007
Raiffeisen Bank – Albania	-13.95%	-14.48%
National Commercial Bank	0.10%	1.22%
American Bank of Albania	-24.59%	-24.71%
Tirana Bank	9.34%	6.71%
Alpha Bank – Albania	14.31%	16.70%
Popular Bank	5.46%	7.18%
Credins Bank	5.89%	3.41%
National Bank of Greece	30.55%	34.50%
ProCredit Bank	-12.77%	-11.49%
Italian-Albanian Bank	0.73%	2.33%
Emporiki Bank – Albania	--	--
Union Bank	--	--
United Bank of Albania	-9.04%	-0.71%
International Commercial Bank	10.54%	15.02%
Italian Development Bank	12.95%	22.09%
First Investment Bank– Albania	-31.67%	-46.44%
Credit Bank of Albania	1.68%	-9.46%

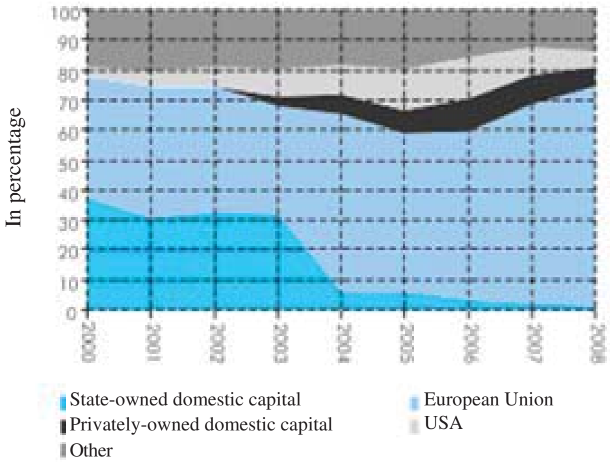
Source: Elaboration of the Albanian banking association on quarterly data.

2.2. Ownership structure. Recently, the banking system's capital has incurred important structural changes, which brought about the increase of foreign capital domination in the system. During 2008, with regard to Credins Bank, the sale of common shares, owned by a private Albanian shareholder, to two foreign investors (BFSE Holding BV, The Netherlands, and SECO through SIFEM, Switzerland) raised the share of foreign capital in this bank to 33.34%, as compared to 5% in 2007. Regarding proCredit Bank, two of its shareholders, FEFAD (domestic capital) and IFC (capital from the USA), sold all their shares, 25% and 11.25%, respectively, to Procredit Holding, thus, turning this bank into a bank entirely owned by foreign capital originating from the European Union.

At Union Bank, during 2008 the European Bank for Reconstruction and Development purchased 12.5% of the shareholders' capital. This development marks the entry of foreign capital to the last bank of the system that was entirely owned by domestic capital, thus, decreasing the share of domestic capital in our banking system.

The structural changes, and the increase of paid-in capital[1] during 2008, have resulted in 12.5 billion Lek (33%) more foreign capital, and 266 million Lek (5.6%) less Albanian capital. At the end of December 2008, foreign capital in the system was 50.3 billion Lek, or 91.8% (versus 88.8% in 2007), while domestic capital was 4.5 billion Lek, or 8.2% of the total capital.

As shown in Figure 2, capital originating from the European Union has the highest share to foreign capital, whereas capital originating from the United States has gradually lost its importance for the Albanian banking system. Domestic state-owned capital represents 40% of shares owned by the Albanian Government in the United Bank of Albania.



Source: Bank of Albania, Supervision Annual Report (2008).

Fig. 2. Paid-in capital of the banking system by country origin

In Table 3, comparing and contrasting Albanian banking system with those of the region, it can be noticed that foreign capital in the system has a higher share to total capital, than in any other country of the region, except for Croatia.

Table 3. Share of foreign capital in some regional countries

Country	No. of banks			Foreign capital share (in %)		
	2005	2006	2007	2005	2006	2007
Albania	16	17	17	86.3	85.7	88.8
Bosnia-Herzegovina	24	23	22	70.2	75.5	74.2
Bulgaria	34	32	29	74.9	72.8	72.8
Croatia	38	38	38	81.7	86.6	90.8
Slovenia	25	25	27	34.9	37.7	37.7
Serbia	40	37	35	53.8	73.1	77.2
Moldova	16	15	16	50.6	62.7	71.9
Romania	40	39	42	68.9	78.8	79.4

Source: Bank of Albania, Supervision Annual Report (2008).

2.3. Foreign bank presence and credit allocation. The Albanian experience is a common one among those of other economies in transition that in the middle of the 90's were interested in instances of foreign bank penetration, often resulting in the acquisition of the local institutes of which they are creditors. This phenomenon of penetration has been generally driven by a criterion of territorial proximity. Actually, it can be seen that Italian, Greek, Austrian and German banks, encouraged by the profitable investments, higher than that of their home markets, chose South-East Europe as a privileged target. The availability of foreign banks in local markets assumes great importance if we consider the benefits and negative effects that could arise from this process. Derviz (1997), analyzing the Czech Republic case, attributes a positive role to the presence of foreign banks, especially in the early phases of the transition process, because these figures can lead the process. Bonin and Wachtel (2003) argued that this positive effect is appreciable only in small countries, while no influence has been observed for big ones, like Russia or China.

[1] Paid-in capital includes capital donation to foreign banks' branches and issue premiums.

While the absence of systematic data on the composition of banking portfolios, on technologies used and on financing instruments doesn't allow us to have empirical studies on the effects of foreign bank penetration, the experience of other emerging countries constitutes an important source of information.

As for the analysis of credit portfolios, the literature available reveals a sort of dichotomy between foreign and local banks that has the effect of distorting the opportunities in credit access. Foreign banks, especiallly in the early periods, have partial and limited information about markets and their operators. So, having high transaction costs, these banks tend to reduce credit risks by offering their financing only to big multinational corporations, considered much more creditworthy than small local companies. On the other hand, local banks have a real knowledge of the market and they can also select their customers on the basis of direct relations with them; in this way, they can offer their financing to small local companies, because their limited size does not allow them to take the high risk of granting financing to big companies. Recent studies on transitional economies show that this phenomenon is limited to the short term; in the middle-long term, foreign banks tend to take over local ones, thus, reducing transaction costs; this leads to a system consolidation that produces a reorganization of the credit supply.

Creditor assessment has been improved thanks to the introduction of scoring systems and better collaboration from local companies, which try to operate more clearly when offering information to banks.

Clarke et al. (2001) think that foreign bank penetration leads to an improvement of financial conditions for all companies, while bigger ones have far more benefits from this process. In their study, however, it is unclear whether this generalized benefit arises from an increment of credit supply by bigger banks or by local banks which increase their financing in order to be more competitive. Certainly, this behavior has a limit in the requisites imposed by regulation systems. Berger, Demirgüç-Kunt, Levine and Haubrich (2004), in their analysis of the situation of developing countries, say that the access of foreign banks introduces an increased credit supply for small and medium-sized companies.

Tables 4 and 5 show, respectively, the credit volume supplied on the whole from 2000 to 2007, divided into fields, and the share of credit supplied by foreign and local banks. In 2007, foreign banks represented 89% of Albanian bank assets (about 67% of the local GPD), collected 90% of deposits and supplied credit to the private sector for about 26% of the local GDP.

Table 4. Credits in the Albanian economic system (in millions of Lek)

	2000	2001	2002	2003	2004	2005	2006	2007
Total credits	23242	27941	38652	50683	69973	121939	191211	287555
Credits in the public sector	1053	0.547	0.033	-	0.116	0.068	0.172	3915
To families	8422	3990	7085	12289	21428	38437	64470	102587
To companies	13767	23404	31533	38296	47879	82760	126512	180955

Source: Bank of Albania, Statistics.

Table 5. Structure of the banking sector (shares of total assets at the end of 2007)

	Assets		Deposits		Private sector loans		Net government credits	
	2003	2007	2003	2007	2003	2007	2003	2007
Share of the total								
All banks	100	100	100	100	100	100	100	100
Foreign banks	47	89	41	89	97	90	24	91
Local banks	53	11	59	11	3	10	76	9
GDP share								
All banks	55	75	47	62	7	29	29	26
Foreign banks	26	67	19	55	7	26	7	24
Local banks	29	8	28	7	0	3	22	2

Source: IMF 2008 (based on data from Bank of Albania).

While the number of foreign banks rose, those of home banks fell. They passed from a share of 53% in 2003 to 11% in 2007, with assets in 2003 worth about 29% of the GDP and in 2007 fell to 8%.

The increase in the credit supply also corresponds to an increase of demand for credit, particularly on the part of families. This phenomenon originates from the improvement of the regulations concerning creditor protection and property rights, associated to a monetary policy oriented to the stability of interest rates that encouraged the property market. The increase in the supply was both quantitative (credits supplied grew at an average rate of 56.7% per year) and qualitative, thanks to the diversification of available financial instruments. On the other hand, something similar has happened to medium and small sized companies, which were traditionally not inclined to apply to banks for financing, preferring to use their own funds. This tendency and the peculiarity of the Albanian business system, mainly based on commerce and the construction industry, prevented small firms from accessing the local credit market[1] for many years[2]. Thanks to the development of the banking sector and to entrepreneurs' increased trust, business credit in 2007 reached a share of 63% of the total, 80% of which was granted to constructions, industry and commerce.

Moreover, the innovations introduced in the process of creditor assessment were fundamental in the development of the Albanian credit system: the use of standardized procedures and of the ICT instruments, imported from foreign banks, helped to simplify the elaboration and sharing of information about custommers and operators in the financial market, lowering any asymmetric information and the likelihood of any moral hazard or any adverse selection, which discourage institutes from granting credit.

3. The presence of foreign banks: advantages, disadvantages and withdrawal risk

Theoretical reasons for and against the entry of foreign banks in a given country are clearly listed in Bonin et al. (1998). Within the arguments supporting the entry of foreign banks, the products and services innovation means that foreign banks tend to offer a larger variety of products and services as they possess the necessary experience and know-how transferred from their home markets. Meanwhile, the domestic banks lack the proper knowledge on how to launch new products or services or are unable to invest on those due to their present situation.

So, the main contribution made by big banking groups is their capital resources and their know-how: experiences, management skills and technical instruments allowed local financial systems to make great progress in the modernization process without paying high costs. Moreover, the close relation between primary and secondary offices leads these banks to maintain a constant credit level, also during crisis periods in which local banks had to reduce their credit offer. At the same time, these relations can have a negative influence on the performance of the branch, which may suffer for the downward trend in the country of origin: the more concentrated the bank market is, the higher this risk becomes. This is essentially due to the fact that possible financial shocks may be exported into the economies of the emerging countries.

Undoubtedly, foreign bank presence leads local markets to a higher degree of stability and can reduce the impact of financial crisis. The IMF, in fact, stresses the fact that concerns in this field are reduced because of the credit growth generated by foreign banks. To achieve this purpose, local authorities should take action to set up a regular information exchange and a close collaboration with their foreign counterparts: "A high degree of foreign ownership puts a premium on close and effective collaboration with home-country supervisors" (IMF, 2008, pp. 14-15).

Another argument is the presence of economies of scale and scope. On the one hand, foreign bank could offer new technology, which is very necessary for the main domestic banks to generate profit from economy of scales. However, foreign banks are willing to offer it only if they manage to purchase the majority of shares in a domestic bank. On the other hand, foreign bank can encourage the consolidation of banking system by participating in joint ventures of acquisitions with small domestic banks. Also, foreign banks take the advantages provided by the economy of scope through their knowledge of other financial operations such as insurance, portfolio management and commissions.

Furthermore, competition is increasing because foreign banks that enter the market naturally lead to an increase in the number of banks, thus, increasing competition. However, this is not always the case given the market segmentation. Also, financial markets development comes from the fact that foreign banks help the expansion of inter-banking market and can attract clients who in other circumstances would either seek off-shore banks or would not approach the banking system at all.

Finally, the argument of the attraction of foreign direct investments, given that the presence of foreign banks itself is a form of foreign direct investments. Also, their presence increases the credibility and safety for foreign investments and can help to attract other direct foreign investments especially from the respective countries.

For what concerns the arguments against the entry of foreign banks, the fear of foreign control comes from the fact that banks are involved in deposit and lending activities, which directly affect the economy of a country and the quality of life of its citizens, it is natural that a sense of fear starts to develop when these activities are in the hands of foreigners.

Furthermore, banks represent a special activity. Banks are subject to special protections from government due to their important role in the economy. Thus, it is argued that it is not appropriate that foreign investors enjoy these "privileges" as well.

[1] In 2000, only 10% of the total credit was supplied to firms.
[2] Until the early 2000s, Albanian companies preferred to deposit their assets in foreign banks, outside national boundaries.

Foreign banks might be interested in the economy of their home country rather than the development of the economy where they have invested. For example, they might be interested in promoting exports from their home country or in supporting projects undertaken by home country firms. Furthermore, it might happen that foreign banks gather deposits in one country to make loans to their home countries.

And there could be regulatory differences because under European Union law, the branches of foreign banks are supervised by home country supervising authorities. However, it might happen that the quality of this process varies from one country to another and in the worst case the home countries lack a consolidated supervising authority resulting into a poor monitoring process of a part of the banking system and consequently leading to unsound banking policies. In the case of Albania, foreign banks are under the supervision of the sole supervising authority, Bank of Albania.

Apart from the concerns about the entry of foreign banks, it is necessary to consider another major point in this analysis, i.e., the diversification of foreign capital, which flows into the Albanian banking system. Foreign capital diversification has theoretically two main advantages: first, it introduces new banking cultures interested in various areas of the economy or market segments; second, it decreases the level of exposure of the host country banking system to the development of a sole economy and, thus, it lowers the possibility of this sole economy affecting the banking system if the former is in financial difficulties.

While foreign banks own the high share of the total assets of the national banking systems in several countries, there are several factors that led a parent bank to shut down a foreign subsidiary. In the period of 1999-2006 and particularly during 2001-2002, nine banks were closed in Argentina, seven in Indonesia and five in Romania.

The motivations that led a parent bank to close or sell a foreign subsidiary to a domestic or foreign investor may be due to financial problems in the home country or to bad performance of the subsidiary.

With regard to the second reason, we observe that a foreign bank decides to enter in a host country if there is “money on the table” of the banking system. The probability that it happens is higher in developing countries. The entry of a foreign bank in a host country unavoidably fuddles the environment and forces the local banks to be more competitive and more efficient, it slowly produces an erosion of markets opportunities. The result is a decrease in the profitability of the foreign bank that may lead the parent bank to close the foreign subsidiary. As Tschoegl (2005) pointed out, another reason is the rise of political, financial and economics problems in the home country of the parent bank. It was the case of Asia in 1997 and Latin America in 1999 where the effects of financial crisis were more pervasive.

Nevertheless, as Tschoegl (2004) himself, Peek and Rosengren (2000) and Hryckiewicz and Oskar Kowalewski (2009) stressed, it is more likely that the decision of a parent bank to close or sell a foreign bank is affected by financial problems in the home country. The analysis of the Japanese banks after the financial crisis that hit Japan in 1990 showed that their position in the US banking sector declined and some banks leaved California. Today three banks of the eight subsidiaries that were established in California between 1952 and 1978 are still operative. The choice to sell foreign banks is a consequence of the need of the parent bank to reduce costs and increase capital when there are economic and financial problems in home country.

Nothing excludes the possibility that, once the problems in the home country are overcome, the foreign operations may be recovered. As Hryckiewicz and Oskar Kowalewski (2009) recalled, in the period of 2001-2004 the Chief Executive Officer of Banca Intesa, Corrado Passera, decided to sell its subsidiaries in Europe, North and South America, focusing its operations on the domestic market. This choice was due to an increase in costs and bad loans. This strategy improved the profits of Banca Intesa and, as a consequence, since 2004 Intesa began to look again to international market and acquired new subsidiaries abroad.

Conclusions

In this paper we analyzed the reforming process that characterized the financial and banking Albanian sector in the period of transition from planned economy to the market economy. In particular, we focus on the role of foreign bank in the restructuring process. Like all the Eastern European countries that passed through a transition period, the Albanian economy needed for an efficient credit allocation and a suitable payment system. In order to reach this objective, two main steps should be pursued, i.e., the privatization of the existing state banks and the opening of foreign banks. The Albanian system took its steps in this direction during 1992 with the authorization of four banks: National Bank of Albania, Savings Bank, National Commercial Bank, and Agriculture and Development Bank. The system established was characterized by high concentration: the three main banks held 90% of the market. The Saving Bank alone offered 75% of all the banking services supplied on the market, thanks to transfers of almost all family deposits, while the National Commercial Bank monopolized business accounts and foreign transactions.

Soon after, the financial market was opened to foreign banks and in 1994 the first Albanian bank with foreign control was established, it was the Italian-Albania Bank which was the result of a joint venture between the "Banca di Roma" and the National Commercial Bank, with a minority shareholding of the European Bank for Reconstruction and Development. Another banking joint venture was the Arab-Albanian Islamic Bank, which was founded by the National Commercial Bank and by Arab investors.

Today the higher share of foreign capital originates from European Union while United States are slowly losing importance.

The Albanian banking market is dominated by the National Commercial Bank and the Raiffeisen Bank.

Since January 2008, the Italian-Albanian Bank of Intesa Sanpaolo Group (in joint-venture with SIMEST and EBRD) merged with the American Bank of Albania and founded the brand American Bank of Albania, under the control of Intesa San Paolo. The "Banca Popolare Pugliese" is a member of the Italian Development Bank (IDB), 95% of whose capital is held by individual investors, with a share of 5%. The United States can count one bank: Union Bank – Western Union.

The decrease in US banks presence in Albania may be the consequence of a drop in market opportunities offered by the local banks. Nevertheless, another reasons could be the rise of financial problems in the home country of parent banks. Focusing on this second motivation a further research could be the analysis of the risks that foreign banks leave the host countries as a consequence of the actual global financial crisis.

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