

THE ECONOMY OF ALBANIA TODAY AND THEN: THE DRIVERS TO GROWTH

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Abstract

Over the past two decades, Albania has faced many social and economic changes, since it changes its economic system from a centralized one to a democratic one in early 90s. During this transitory phase, Albania had faced difficult challenges such as of undertaking all the necessary reforms for the stabilization, liberalization, privatization and integration of its economy in the overall global and regional economic trends. The first aim of this paper is to study the Albania Economy in its democratic era. The second aim of this paper is the identification of the main drivers to economic growth in the Albanian case during past two decades and the challenges that it faces today. Furthermore, this paper deals with some of the challenges that Albanian economy faces today such as SMEs challenges that represent the 98% of the market, rail infrastructure, lack of entrepreneurship, low level of innovation spirit among the enterprises, lack of focus in R&D.

This paper finds out that Albanian Economy has performed well but yet, there exists some critical challenges that should be faced in order to achieve the desired level of economic development and competitiveness in global and regional market.

Key Word: Albanian Economy, Drivers to Growth, Challenges

1. INTRODUCTION

Over the past two decades, Albania has undergone many fundamental changes that have greatly impacted the economy of the country. Prior the year 1990, the Albanian economy was designed as a completely centralized economic system, where every economic aspect of the country was run by the state, and the principle of open market economy did not exist. The few companies that operated in the country were state administered, and as a result they were not able to fully and truly understand the needs of the market and of the Albanian people. This lack of communication and understanding slowly led to the deterioration of the economy of the country and at the end led to the collapse of communism and the beginning of the democratic era for the country.

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Following the collapse of communism in early 90s, Albania entered a transitory phase which was accompanied by a number of social and economic changes. Nonetheless, this transitory phase was not very easy for Albanian economy and Albania was faced with the difficult challenge of undertaking all the necessary reforms for the stabilization, liberalization, privatization and integration of its economy in the overall global and regional economic trends. Many reforms were undertaken regarding the shaping of the Albanian economy as an open market economy. One of the main reforms undertaken was the privatization of the previously stately run companies, which enabled the introduction of foreign investors in the internal market.

The main incomes of Albanian economy are immigrant annual remittances, services, and the agricultural sector. Albania's GDP stood at Euro 8,748 million and Euro 8,169 million in 2010 and 2009, respectively. According to preliminary data from World Bank's Poverty Assessment Program, 12% of the population lived below the poverty line in 2012, almost same as in 2010, but it marks a considerable improvement from 25.4% in 2000. The official unemployment rate for 2012 is 13%. Even though, Albanian economy, on the last two decades, has been growing and transforming into a market economy it still remains a poor country, according to Western European standards, with a Gross Domestic Product (GDP) per capita of \$4,149 in 2012 and stood at 30% of EU average in 2010. Despite the global economic crisis, foreign direct investments (FDI) in Albania increased by 23 percent during 2010 compared to 2009 reaching a level of EUR 837 million and more than double the FDI level in 2006. According to UNTAD World investment Report 2012, in 2011 the foreign investments in Albanian were almost in the same level than in 2010. FDI in Albania has mostly been in sectors such as banking, energy, and telecommunications. The rise of FDI's level in past years is a result of good investment climate and new opportunities opened from the privatization of state-own enterprises. These increases of FDI's reflect an increase of preferences of foreign investors in Albanian sectors and also risk reduction. Also being a potential candidate country, a member of NATO since 1 April 2009 and a WTO member since 2000, affects positively in FDI's Albania. Even though the privatization level in Albania has grown significantly, Albanian economy still offers numerous opportunities for domestic and foreign investment and obtains a fast-growing profit from them.

An economy growth increases the outputs produced by a country. This growth is achieved by improving the resources of the economy in quality and quantity. These resources are labor, capital, land and entrepreneurship and they can be improved through investment, exploration, education and technology innovation. Reaching a long-run economy growth is one of the three

macroeconomic goals. In this paper are analyzed the impact in the economy of geographic position of Albania, natural resources, human resources, agricultural sector and SMEs.

Albania has the advantages of a favorable geographic position benefiting from the two most important trading partners Greece and Italy – which are two large economies and in the same time neighbor countries. Also due to its geographic position, Albania inherited very rich natural resources such as metal and minerals and a good capacity for hydroelectric power. Corridor VIII that passes through Albania brought in the country important investors from the West and has launched Albania toward Eastern Europe market. These advantages have made Albanian a very attractive market for foreign investors or national companies. Nowadays in the sector of the exploration operate a significant number of nation and international companies.

Labor force has resulted to a very skilled and low cost and education system – which is inherited form communism – is very strong and lately it been adopted according to international standards. Also an important sectors in terms of total employment in agricultural sector which began with the collapse of communism and that was considered of great importance the establishment of the legal framework for the solution of the land issues that began to arise.

Moreover, agricultural sector is the most important sector in the term of employment. According to INSTAT this sectors employs 54.9% of total employers. The development of this sector began after the collapse of communism and rapidly became an important sector in Albanian economy. Nowadays its share in nominal GDP has decreased but in 1993 it reached a share of 55%.

Small and medium-sized enterprises (SMEs) have a crucial role in the transition process. SMEs already make up the vast majority of private businesses operating in Albania and because of their size and adaptability are likely to be the main source of employment generation. Improving the business environment for SME development is a key objective of the policy framework in Albania. (Xhepa & Agolli, 2004)

Currently SMEs represents 98% of the companies in Albanian market. As Xhepa and Agolli (2004) predicted they are the main source of employment where during the past years around 95% of the total number of employees work in micro enterprises. Even though these companies play a significant role in the market, they face the most of the challenges and obstacles during their daily operation.

2. GENERAL OVERVIEW OF SME

Nowadays, the Small and Medium Enterprises (SME) are increasingly being considered as a vital part of the economy of a country, whether it is a country with a well-established

economy or a country with an emerging economy. According to the Federation of the European Accountants, as per January 2013, the SME-s constitutes 99.8% of all the European companies. While, according to the latest reports of the EU, it results that more than 99% of the companies in Europe are SMEs, employing almost 70% of the European workforce and producing close to 60% of the overall turnover from manufacturing and services.

In addition, in order to highlight that the SME-s strongly affect also the economy of the big and powerful countries in the EU, Mark Stephens, group commercial director at Aldermore, states that SMEs are the lifeblood of the UK economy and it is imperative they are given the right support for the economy to continue its recovery. Furthermore, Sir Michael Snyder, Senior Partner at Kingston Smith LLP stipulates that the performance of SMEs has a major impact on the performance of the wider economy and that in the current economic downturn; growth is most likely to come from SMEs.

Therefore, since the place occupied by the SME-s in the Albanian market resemble that of the EU market, then it is vital for Albania to give to them the same importance and pay the same attention which is given to the SME-s in the EU.

Yet, most of the reputable personalities in the economy agree that one of the main challenges faced by the SME-s is the difficulty to access finance. Regarding this challenge Mark Stephens states that the access to finance is essential for SME-s since it allows them to expand, prosper and create jobs, consequently contributing to the UK's recovery. Therefore, it can be deduced that easy access to finance is essential for the SME-s all around the world to survive and prosper and positively impact in the global economy, including the Albanian economy.

Another challenge faced by the SME-s in Europe and Albania is the administrative and regulatory burden. According to the latest reports of the EU, it results that in the European Union SME-s bear a disproportionate regulatory burden in comparison with larger businesses. Furthermore, the same reports concluded that SME-s seem to have even more difficulty with meeting the requirements of regulations, having very limited resources, particularly in terms of time and money.

In the European Union innovation is considered as an importance elements influencing the survival of the SME-s in the market. Ian Winham, CIO of the Ricoh Europe states that through the smart use of technology, SME-s can do more, in less time and for less cost. Yet, he stipulates that there exists a number of internal and external challenges, such as the lack of expertise or budget, managing regulations, and the increase of business data that are holding many SME-s back from benefiting from the transformative potential that technology can bring them.

Another important element for the SME-s is the education and training. According to the Enterprise and Industry Directorate-General of the European Union, the benefits of

entrepreneurship education are not limited to enhancing start-ups, innovative ventures and new jobs. Entrepreneurship is a competence for all, helping young people to be more creative and self-confident in whatever they undertake. Yet, in the European Union there is a shortage of entrepreneurship studies within non-business institutions and disciplines and entrepreneurship is not yet sufficiently integrated into different subjects of the curriculum.

As it can be seen, the challenges faced by the SME-s in the European Union are the same challenges faced by the SME-s in Albania. Yet, being that the Albanian economy is still an emerging economy, the severity of these challenges is higher and the measures to be undertaken should be greater. Yet, regarding the situation of the SME-s in the Albanian market, it shall be discussed more in details further in this report.

3. DRIVERS TO GROWTH

3.1 Geographic Position and Rich Natural Resources

The very favorable geographic position of Albania and the rich natural resources possessed by the country made Albania a very attractive market for the foreign investors and for the first national companies desiring to embark in the journey of the private entrepreneurship.

The country is located in the Balkan Peninsula with a long coastline in Adriatic and Ionian Sea. It also inherited a wide range of natural resources such as metals and minerals. It also has a good capacity for hydroelectric power, due to its geographic position. The two most important trading partners of Albania are Greece and Italy – which are two large economies and the same time neighbor countries of Albania. Another benefit of this favorable position is that the Corridor VIII passes through Albania – which is one of the ten corridors that connect the Adriatic Sea with Black Sea, starting from two Italian ports, Bari and Brindisi, passing through Albanian port Durres, then to Tirana, Skopje and Sofia, to finally end in Black Sea ports of Burgas and Varna. The Corridor 8 has launched Albanian toward the Eastern European market. It also brought enormous investment for the West to develop infrastructure and subsidiary services.

Albania is rich especially in chromium, copper and nickel deposits. During the period of civil unrest in 1991-92 and 1997 mineral production was severely damaged and Albania stopped being the world's third-largest chromium producer and mining according for a substantial share of export earnings. The mineral production has generally declined during the transitory period due to the lack of investment, depreciated technology and unfavorable price movement in the international market. (Ristani, 2008)

Currently, the sector of the exploitation of the rich natural resources, which include significant hydro-electrical power potential and valuable mining deposits, represent an important sector of the Albanian economy, where they operate a significant number of national and international companies.

Geographic position of Albania offers opportunities also in investment on the tourism sector. This sector has grown significantly during the last few years, but historically the main decelerator of this growth has been the infrastructure. This increase is a result of small – mostly locally – operators, however this sector represent a promising area for further and greater investments.

Nowadays, Albania's coal and nickel mines are privatized and other important mines such as chrome and copper mines operate via concession contract. In order to increase its competitive advantage in domestic and international market, Albanian mining industry priorities are the expansion of production and processing of these minerals and application of modernized technology in mining and mineral processing.

Natural gas historically was an important source for Albanian energy market, yet its production level is very low resulting in a low contribution in economy. In June 2013, Albania has sign the agreement for the construction of Trans-Adriatic Pipeline (TAP) which passes in Albania. TAP will start from the Turkish-Greek border at Kipoi, Evros, passes thorough Greece and Albania and ends in Lecce in Italy. A report of TAP AG, this pipeline will produce an estimated additional of €106 million in GDP and 3,900 jobs (part-time and full-time) per year between 2015-18. Also this report indicate that the project will create operational benefits which over the 50-years operating horizon total estimated contribute to GDP will be €740 million and will support 450 jobs per year on average. Also, in this report has resulted that the project will create significant benefits for Albanian economy associated with the infrastructure investment, knowledge and technology spillovers to local firms, and also is expected to increase the availability of natural gas to help meet future energy demand. (Worthington, 2012)

Currently, Albanian hydropower fulfill in average the 98 of domestic energy needs. During the wet years this sector bring substantial revenue for the country. The establishment of concessional politics in the implementation of new hydropower plant by the government and also the construction of TAP will increase the possibility for Albania to be a significant exporter of energy which will increase country's GDP.

3.2 Human Resources

Another driver for the growth of the Albanian economy over the years has been the human resources. Thanks to strong educational system inherited by the previous system and

the reforms undertaken for further improvement and adapt it to the international standards, the human resources in Albania were very skilled, and at low cost and as a result the Albanian market became very competitive in the region. Even nowadays, the human resources constitute a main factor for the attraction of foreign investors in Albania.

Nowadays Albania education system has the capacity to graduate from universities in average 120,000-150,000 students from more 100 specialties. The experience of large and important companies in the Albanian market confirms that labor market in the market can fulfill the demands for employees in quantity also in quality.

Nonetheless, in order to keep up and further develop the current competitive edge, the state should invest more in the development and improvement of the human resources. Barro (1991) emphasizes that the current level of human capital development is positively related to a country growth. Also, Sach and Warner (1997) concluded that the greater the human capital development is, faster the transition growth. Romer (1990) noted that quality improvement of labor force results in new production or generates new ideas that generate higher technological progress. He also emphasizes that countries with a larger and more developed labor force are more likely to grow faster. As a result it is very important to have specialized and bespoke academic curricula introduced to the educational system, in order to train the future generations and enable them to become more competitive in the increasingly global market.

3.3 Agricultural Sector

Being a former communist country where the principle of private property or land did not exist for a very long period and since after the communism, most of the population of Albania lived in the rural area, it was considered of great importance the establishment of the legal framework for the solution of the land issues that began to arise after the collapse of communism. The solution of the land ownership issues made it possible for the beginning of the development of the agricultural sector, which rapidly became an important sector in the Albanian market, providing employment and revenues for many families living in the rural areas. Nowadays, agriculture is one of the most important sectors of the Albanian economy in terms of total employment. In table 1, is shown the number of employees according to the economic activity. Accordingly, the companies with activity in agriculture, forestry and fishing employs the greater number of the total employees. In 2011, it employs 54.6% of the total number of employees. Before the transitory period, the industry sector used to outperform agriculture sector in terms of GDP. In 1993, the share of GDP reached 55%. Since then it has grown continuously but with a lower rate than other main sectors of the economy. Therefore, this sector lost its importance, mainly in favor of services. According to INSTAT (2013), the share of agriculture in nominal GDP declined from 30% in 2000 to 19% in 2011.

Table 1: Number of employees according to the economic activity (in thousands)

Economic Activity	2009	2010	2011
Total	899	917	928
Agriculture, forestry, fishing	496	507	507
Extractive Industries	5	6	8
Processing Industries	53	53	63
Energy and water Industries	26	26	21
Construction	40	39	35
Trade	58	58	65
Hotel and Restaurant	12	13	22
Transport and Communication	23	24	26
Education	40	42	41
Health	26	27	28
Other	120	122	112

Source: INSTAT (2013)

Agricultural sector offer opportunities for good investment because of the favorable Mediterranean climate and low cost rural work-force. Yet, the number of enterprises operating in this sector has not changes significantly in the past year. This lack of investments in agriculture is generally a result of bad infrastructure, but the latest improvements in the energy and road infrastructure, this section is expected to benefit from new and profitable investment. Agricultural sector is a promising important producer and exporter of quality good because generally agricultural products are free of artificial additives or pesticides.

3.4 Small And Medium Enterprises

3.4.1 SMEs in Albania Market.

An important aspect of the development of Albanian economy is the size of the companies operating in the market. As it has been shown by the past and current studies, the main percentage of the companies operating in the Albanian market are small and medium enterprises, with only a number of companies, which can be categorized as large companies. Still, it is important to emphasize that the group of large companies is constituted of the well-known foreign companies, which only in the last previous years have entered the internal market.

Table 2: Active enterprises by year of creation and size, 2012

Year of creation	Total	Group by the number of employed			
		1-4	5-9	10-49	50+
	104,275	94,025	5,396	3,898	956
Total	12,681	12,071	418	162	30
	11,772	11,218	374	154	26
	13,169	12,407	543	195	24

Source: INSTAT (2013)

In the framework of the Stabilization - Association Process undertaken by Albania and with the change of the criteria used for the division of the companies in accordance with their size, it has resulted that 98% of the companies currently operating in the Albanian market are small and micro enterprises. Article IV of the law nr. 8957, date 17th October 2002 “On Small and Medium Enterprises” states the definition of SMEs. The enterprises that have 5 or fewer employees are classified as micro enterprises. The small enterprises all classified all the companies that have 6-20 employees and an annual turnover smaller than 40 million ALL. Medium enterprises are all the companies that employ 21-80 people and have a turnover lower than 80 million.

SME’s definition in EU classifies all the companies that employ less than 250 people and have a turnover smaller than EUR 50 million. Although criteria differ, Albanian definition of SMEs is consistent with the definition of EU because the size of economies and its preference also differ.

In table 2 is shown the number of people employed by companies in Albania during 2010-

2012. All these years, around 95% of these employees work in micro enterprises.

According to INSTAT, the companies that produce services employ 87% of the total number of employees in companies. (Figure 1) Their services include:

- Hotels, Coffee, Restaurants
- Transport, Storage and Communication
- Financial Intermediation

- Real estate, renting and business activities
- Education
- Health and Social Work
- Other community, social and personal service activities & Activities of households

While the 13% of companies produce goods such as:

- Products of agriculture, hunting, forestry
- Fishing
- Mining & quarrying industry
- Manufactured Industry
- Electricity, gas and water supply
- Construction

According to figure 2, the service providing companies with a number of employees lower than 5 – which classify as micro enterprises – represent 93% of the total number of service providing companies. Also according to figure 3, the goods providing companies that classify as micro enterprises represent 76% of all goods providing companies.

According to Albanian Ministry of Economy during the period of 2008-2020 the contribution of SME sector **73%** of GDP. As a result, it can be said that the SME (Small and Medium Enterprises) sector continues to play an important role in the economy of the country. Yet unfortunately, the companies operating in this sector are the ones that face the most challenges and obstacles during their daily operation.

Figure 1: Companies in Albania according to their activities

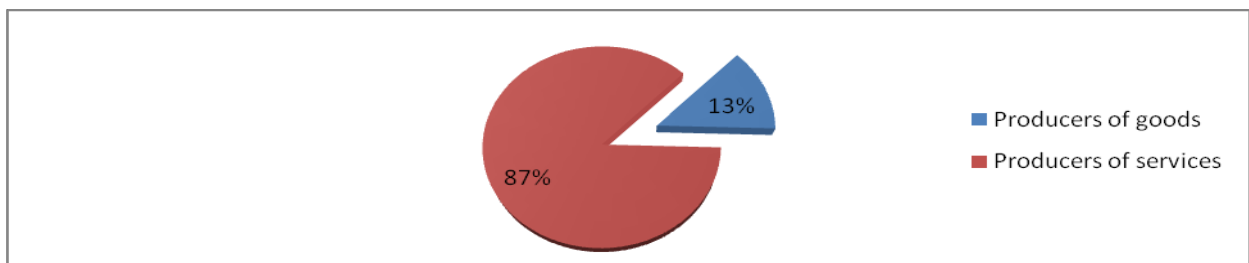


Figure 2: Producers of Services groups by their number of employees

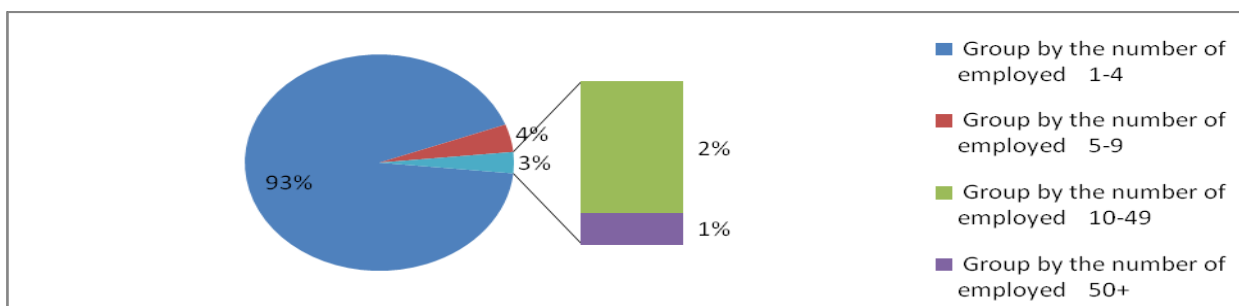
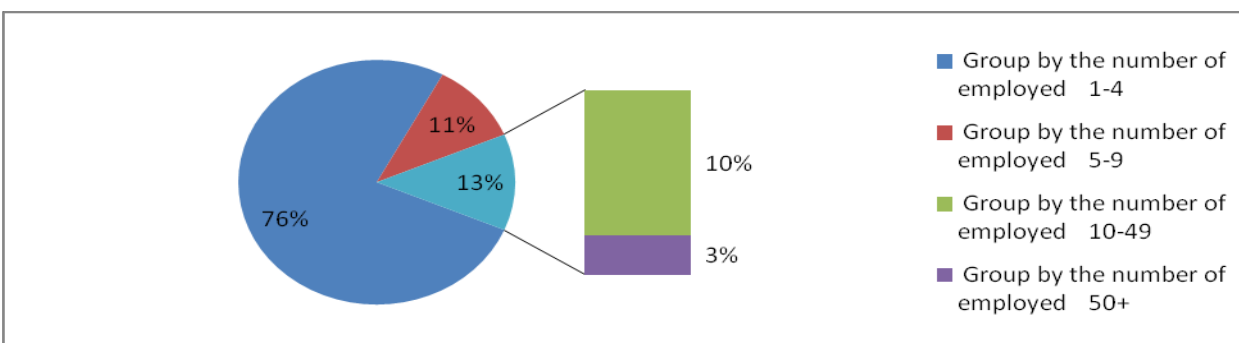


Figure 3 : Producers of Goods groups by the number of their number of employees



Source: INSTAT (2013)

3.4.2 SMEs Challenges

One of the main challenges faced by the Albanian SME is the financing. Even though in the last years the burden of obtaining external financing, mainly bank/financial institution loan, has been reduced, yet the Albanian SME continue to be very concerned by the long, difficult and very bureaucratic administrative aspect of the lending procedures. The main problem that concerns SMEs is the collateral since the conditions required to be met by the collateral to be considered as good and acceptable collateral are heavy for SMEs. Usually, banks require that collateral is either in the form of a real estate property, or collateral may be in the form of a bank deposit. Therefore, being that most of the Albanian SMEs can hardly reach reasonable profit margin, let alone make enough profit to own various properties and bank deposits to act as collateral for a bank loan, in most of the cases many excellent business ideas do not become true due to the lack of collateral. Moreover, The Albanian SMEs find the amount of forms required to be filled in by them very excessive and time wasting. Nevertheless, in contrast to the European SMEs, the Albanian SMEs do not have any external assistance while filling them in or to make these procedures easier for them. Additionally, the

high interest rates offered by the banks are another problem encountered by the Albanian SMEs. Even though, the degree of competitiveness between the banks operating in the banking sector have increased in the last few years, yet the interest rates have not experienced a substantially decrease

Infrastructure has always been, and it continues to be a big problem for the normal development of the Albanian economy. Even though, in the last years, the infrastructure has undergone major improvements, still there are many problems with it. One of the main problems of the infrastructure worth to be mentioned is that, nowadays the rail system in Albania is badly damaged and its usage level is very small due to the lack of necessary investments. Usually, railway network is used for people transportation and not for goods transportation and as a result, nowadays the only method of transporting the commercial goods is by using the road system making the transportation process very long and expensive for SMEs.

Albania as the rest of Europe has understood the importance of the entrepreneurship in the further development of the national economy. Nevertheless, Albania in contrast to other countries in the region of Western Balkans has done little to develop the entrepreneurial attitude. Over the last years, the Albanian state has introduced entrepreneurship as a module in various educational levels with a more an academic approach of it where its basic concepts are explained. Nonetheless, the module is not taught continuously and following a logical increasing level of knowledge throughout an educational level, but it experiences gaps and the taught things may be repeated at various levels. As a result, the Albanian youngsters are not ready yet to face the challenges that comprise being an entrepreneur when they finish studies.

Even though, Albania has undertaken various measures to develop the innovation spirit among the enterprises, innovation still is not at the desired levels. Online services such as e-business and e-signature, which are commonly used in EU, in Albania exist merely as a concept and are not widely used by Albanians. The main reason for this lack of usage is that Albania does not have a proper developed infrastructure for online services. Another problem related to innovation is that Albanian enterprises do not focus as much as they should on R&D. Usually, the Albanian enterprises focus more on increasing their profit forgetting that successful R&D ideas will help them generate more profit.

4. CONCLUSIONS

To sum up, even though as a former communist country with no experience of open market economy, Albania has performed well, and it has been able to create an attractive market for national and international investor. The good performance has to be credited to the wise and forward thinking measures taken by the Albanian state over the year. Despite

the global economic crisis FDI in Albania has increased reflecting an improvement in investment climate and an increase in preferences of foreign investors for the Albanian market.

Albania is a very attractive market for foreign investors because of the country's very favorable geographic position, rich natural resources, and very skilled and low-cost human resources. Also, after the collapse of communism, the agricultural sector, which was the beginning of the sector that nowadays is one of the most important sectors in terms of total production, offers great investment opportunities in different sectors such as tourism, agriculture, energy, etc.

Yet, there exist many important challenges to be faced by Albania in order to achieve the desired levels of economic development and become very competitive in the regional and global market. The major part of the Albanian market that bears the most difficult challenges has resulted to be SMEs. Some of the SMEs' challenges are financing, very excessive and time-wasting amounts of forms required to be filled, and the high interest rates offered by the banks. Infrastructure is another challenge due to the badly damaged rail system, which would have resulted to be a cheaper way of transportation for SMEs.

Albania has introduced entrepreneurship as a module with a more academic approach, where its basic concepts are explained, as a result Albanian youngsters are not ready yet to face the challenges of young entrepreneurs when they finish studies. Also, in Albania the innovation spirit among enterprises, innovation still is not at the desired levels and online services merely exist due to the lack of properly developed online services infrastructure. Moreover, Albanian enterprises that have successful R&D ideas generate more profit and focus very little on them.

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