

**Challenges and prospects of Foreign Direct Investments
In Hydropower sector in Albania**

Firalba Gjoka

**Thesis submitted for the degree of Master of Science
Department of Banking and Finance**

Epoka University

July 2016

Approval Page

Thesis Title : Challenges and prospects of Foreign Direct Investments in
Hydropower sector in Albania

Author: Firalba Gjoka

Qualification: Master of Science

Program : Banking and Finance

Department : Banking and Finance

Faculty: Faculty of Economics and Administrative Sciences

Thesis Date: 4 July 2016

I certify that this thesis satisfies all the legal requirements as a thesis for the degree of Master of Science in Banking and Finance.

(Assoc. Prof. Dr. Ugur Ergun)

Head of Department

I certify that I have read this study that is fully adequate, in scope and quality, as a thesis for of Master of Science in Banking and Finance.

(MSc. Erda Cani)

Supervisor

Exam Board of Thesis

Thesis Title: Challenges and prospects of Foreign Direct Investment in
Hydropower sector in Albania

Author: Firalba Gjoka

Qualification: Master of Science

Date: 4 July 2016

Members

Assoc. Prof. Dr. Ugur Ergun

Assoc. Prof. Dr. Eglantina Hysa

Dr. Alba Kruja

MSc. Erda Cani

Abstract

The role of foreign direct investment in the country's economic development is widely debated. Many countries have welcomed FDI as an essential contribution to the development processes. Albania is in trend in receiving huge FDI inflows in hydroelectric sector because it provides great opportunities to develop hydropower plants. During the last few years, FDIs in hydropower have contributed to the rapid growth of the state economy. Today, energy plays an important role to achieve sustainable development especially in developing countries like Albania. In general, electricity generation in Albania mainly depends on hydropower, as about 90% of electricity is generated by it.

This thesis aims to make a deep analysis of determinants of Foreign Investments in Albania, focusing in the energy sector. Also, as it was mentioned above, it is important to analyze the relationship between FDI, electricity consumption and economic growth in Albania. The thesis uses regression model to study the relationship between electricity consumption, economic growth and foreign direct investment in Albania from the period 1985 to 2014, retrieved from the World Bank and Energy Regulator Authority. This study has found that there is a long-run relationship only among electricity consumption and economic growth. Also, if three variables, (energy consumption, FDI and GDP) are taken together to see the co-integration between them it can be said that in group they are not co-integrated to each other. Further, a questionnaire will be part of this study in order to have a clear view of foreign direct investments and to analyze the potential of the hydropower sector in Albania. More specifically, there were interviewed through structured and semi-structured interviews 72 domestic and foreign investors in the field of hydropower. The survey shows that main difficulties that foreign investors face when they invest in Albania are tax rate, political risk, property issue, corruption etc.

Key words: Foreign Direct Investment, Energy Sector, GDP Growth, Hydro Power.

Abstrakt

Roli i investimeve të huaja direkte në zhvillimin ekonomik të vendit është debatuar gjerësisht. Shumë vende kanë mirëpritur IHD si një kontribut thelbësor në proceset e zhvillimit. Shqipëria është në trend në marrjen e flukseve hyrëse të mëdha të IHD-ve në sektorin hidroelektrike sepse ajo ofron mundësi të mëdha për zhvillimin e hidrocentrale. Gjatë viteve të fundit, investimet e huaja direkte në hidrocentralet kanë kontribuar në rritjen e shpejtë të ekonomisë së vendit. Sot, energjia luan një rol të rëndësishëm për të arritur zhvillim të qëndrueshëm sidomos në shtetet në zhvillim si Shqipëria. Në përgjithësi, prodhimi i energjisë elektrike në Shqipëri, kryesisht varet nga hidrocentralet, pasi rreth 90% e energjisë elektrike prodhohet nga hecet.

Kjo tezë ka për qëllim për të bërë një analizë të thellë të përcaktuesve të Investimeve të Huaja në Shqipëri, duke u përqendruar në sektorin e energjisë. Gjithashtu, siç u përmend më lart, është e rëndësishme për të analizuar marrëdhëniet në mes të IHD-ve, konsumin e energjisë elektrike dhe rritjen ekonomike në Shqipëri. Teza përdor modelin e regresionit për të studiuar marrëdhëniet ndërmjet konsumit të energjisë elektrike, rritjes ekonomike dhe investimeve të huaja direkte në Shqipëri që nga periudha 1985 në vitin 2014, marre nga banka Boterotr dhe Enti Rregullator i Energjise. Ky studim ka gjetur se ka një marrëdhënie afatgjatë në mes të konsumit të energjisë elektrike dhe rritjen ekonomike. Gjithashtu, në qoftë se tre variabla, (konsumi i energjisë, IHD dhe PBB) janë marrë së bashku për të parë bashkë-integrimin mes tyre mund të thuhet se në grup ata nuk janë bashkë-integruar me njëri-tjetrin. Më tej, një pyetësor do të jetë pjesë e këtij studimi, në mënyrë që të ketë një pamje të qartë të investimeve të huaja direkte dhe të analizuar potencialin e sektorit të hidroenergjisë në Shqipëri. Më konkretisht, janë intervistuar përmes intervistave të strukturuar dhe gjysmë të strukturuar 72 investitorët vendas dhe të huaj në fushën e hidrocentraleve. Anketa tregon se vështirësitë kryesore me të cilat përballen investitorët e huaj, kur ata investojnë në Shqipëri janë norma tatimore, rreziku politik, çështja e pronës, korrupsioni etj

Fjalet kyçe: Investimet e Huaja Direkte, Sektori i Energjise, Rritja e GDP, Hidroenergjitika.

Acknowledgements

For realization of this thesis, first I want to thank the people of my family who supported me and motivated me to complete this work.

Secondly, I thank my thesis supervisor Mrs. Erda Cani for her assistance.

Thirdly, I thank the teachers of the Department of Banking and Finance for their support, as well as my friends, who have constantly motivated and encouraged me all through this process.

Declaration Statement

1. The material included in this thesis has not been submitted wholly or in part for any academic award or qualification other than that for which it is now submitted.
2. The program of advanced study of which this thesis is part has consisted of:
 - i) Research Methods course during the undergraduate study
 - ii) Examination of several papers of particular universities both in Albania and abroad as well as a professional book on this subject.

Firalba Gjoka

4 July 2016

TABLE OF CONTENTS

Approval Page.....	ii
Exam Board of Thesis.....	.iii
Abstract.....	iv
Abstrakt.....	v
Acknowledgements.....	vi
Declaration Statement.....	vii
List of Tables.....	xi
List of Graphs.....	xi
List of Charts.....	xii
List of Abbreviations.....	xiii

CHAPTERS

1 INTRODUCTION.....	1
1.1 Research objectives.....	2
1.2 Hypothesis and research question.....	3
1.3 Foreign Direct Investment through years.....	4
1.3.1 FDIs in Albania compared to western Balkan countries.....	7
1.3.2 Advantages and disadvantages of FDI.....	9
1.4 Business climate and attraction of investment in Albania.....	10
1.4.1 Doing business in Albania.....	11
1.4.2 Key steps in attracting foreign direct investment.....	13
1.5 Hydropower Plants.....	14

1.5.1 Advantages and disadvantages of hydropower.....	15
1.5.2 Hydropower in Albania.....	16
1.5.3 Energy development inAlbania.....	19
1.6 Hydropower Concession and public -private partnership.....	23

2 LITERATURE REVIEW

2.1Literature Review.....	26
---------------------------	----

3 DATA AND METHODOLOGY

3.1 Data and methodology.....	30
3.1.1 Econometric model.....	30
3.1.2 Survey.....	31

4 EMPIRICAL RESULTS

4.1 Survey results.....	33
4.2Unit Root Test Result.....	37
4.3 Co-integration result.....	39
4.4 The error correlation model.....	40

5 CONCLUSIONS AND RECOMANDATION

5.1 Conclusions..... 41

5.2 Recommendations..... 43

REFERENCES..... 46

APENDEXES..... 52

List of Tables

- Table 1: FDI inflows, by region and major economy, 2014–2015
- Table 2: Annual inflow of foreign investments in Albania by country in million euros.
- Table 3: Annual inflow of foreign investments in Albania by economy activity, in milion euro
- Table 4: FDI inflows in million USD and in % of GDP, western Balkan countries
- Table 5: Investment value and number of projects, western Balkan countries
- Table 6: The business climate and investment environment in region, from 2013 to 2015
- Table 7: The main hydrologic characteristics of big rivers in Albania
- Table 8: Hydropower output in GWh and in LEK/\$ for 2013 and 2014
- Table 9: Hydro- power Potential in Albania
- Table 10: Main indicators of electricity (in GWh)
- Table 11: The result of Dickey-Fuller (ADF)
- Table 12: Co-integration result table
- Table 13: The error correlation model
- Table 14: Unrestricted Co-integration Rank Test (Trace)
- Table 15: Unrestricted Co-integration Rank Test (Maximum Eigenvalue)

List of Graphs

- Graph 1: Foreign direct investments inflow in Albania, for 2008 to 2014
- Graph 2: Investor’s protection indicator for 2015
- Graph 3: HPP Fierza, Koman&Vau I Dejes output vs. total output 2000-2014

List of Charts

Chart 1: Standard and poor's index for 2015

Chart 2: Type of investor interviewed and type of ownership

Chart 3: Reasons for investing in the energy sector

Chart 4: Obstacles on hydropower sector

Chart 5: Mitigating factors

Chart 6: Employment

Chart 7: Success of the investment

Chart 8: Future investment

Chart 9: Concessions in Albania

List of Abbreviations

FDI:	Foreign Direct Investment
SSE:	South Eastern Europe
EU:	European Union
UNCTAD:	United Nations Conference on Trade and Development
INSTAT:	Institute of Statistics, Republic of Albania
IMF:	International Monetary Fund
METE	Ministry of Economy, Trade and Energy
MARDWA:	Ministry of Agriculture, Rural Development and Water Administration
BoA	Bank of Albania
UNESCO:	United Nations Educational, Scientific and Cultural Organization
EBRD:	European Bank for Reconstruction and Development
OECD:	The Organization for Economic Cooperation and Development
HPP:	Hydro Power Station
GDP:	Gross Domestic Product
SHPP:	Small Hydropower Plant
MW	Megawatt
kW	Kilowatt
kWh	Kilowatt Hour
MWh	Megawatt Hour
GWh	Gigawatt Hour
TWh	Terawatt-hours

CHAPTER 1

INTRODUCTION

The role of foreign direct investment in the country's economic development is widely debated. It is noticed that FDI plays an essential contribution to the development processes of a country. Also, a lot of empirical studies acknowledge that the role of FDI in economic growth and development of host countries, especially in emerging economies.

Nowadays, developing countries are competing with each other to attract more foreign direct investments. It is clear that, FDI plays a major role in developing countries like Albania. According to the Ministry of Economic Development, Tourism, Trade and Entrepreneurship, main sectors that have made the highest contribution to the value of foreign direct investment in Albania are: energy, finance, telecommunication and manufacturing. After these years, it can be said that, foreign direct investments play a positive impact in the economic development of the country for example through the introduction of foreign capital, entry of modern technologies, reduction of unemployment, level, improvement of the balance of payments and the increase of the competition of domestic products in regional international markets.

Driven by technological change, global competition and liberalization of markets, foreign direct investments play a key role in the process of global economic integration. They create effects like in the host countries as well as investment in them. The effects in the host countries are important for the diversification of their importance as well as economic, political and social impact that they generate. The benefit of these effects does not come automatically but is affected by the implementation of some specific conditions.

The main purpose of this work is to study the development of foreign direct investment in the energy sector, especially the current environmental situation of hydropower in Albania. As it is known, energy has an important role in the economic growth, social development and human improvements, achieving a sustainable development in countries like Albania. Hydropower is a renewable energy source and known as clean energy that protects the environment and contributes to the economic growth and new jobs. This analysis is done on foreign direct investment in the energy sector because Albania has a strategic territorial location and countless

water resources. Furthermore, this thesis will explore in detail the institutional, political, legal, technology and economical factors that describe the current situation of FDI on power generation in the electricity sector. Also, the role of foreign direct investment, the main problems affecting foreign direct investment and solution to the problems on the power sector will be highlighted in this work. Another goal of this study is to create a path that will be useful for future.

The thesis employed a regression model to study the relationship between electricity consumption, economic growth and foreign direct investment in Albania from the period 1985 to 2014. Also, a survey with 72 investors interviewed will be part of this study in order to have a clear view of foreign direct investments and to analyze the potential of the hydropower sector in Albania, because as we know Albania has large potential, and so on foreign investments in this sector are very important to provide electricity to the population.

1.1 Research objectives

The main purpose of this study is to highlight the importance of foreign direct investments in Albania, especially in the hydropower sector. To achieve this we need to analyze every one of this issue:

- First of all we have to analyze the current situation of Albania economy. This is an important factor that has influenced the attraction of foreign direct investment in Albania.
- To analyze the development of foreign direct investments, concept and types of FDI, history of FDI worldwide and in Albania. So in this way we get a real picture of FDI inflows.
- To study challenges faced by foreign investors in Albania. In particular, to understand which are the reasons that push foreign investors not to invest in Albania?
- The development of foreign direct investment in the energy sector, especially the current environmental situation of hydropower in Albania.
- To explore in detail the institutional, political, legal, technology and economic factors that affect the current situation of FDI on power generation in the electricity sector.
- To examine the relationship between renewable electricity consumption and foreign direct investment and economic growth.

After being analyzed every one of the issues mentioned above, it can be reached at accurate conclusions and valuable suggestions, hoping to further improvements of the current situation.

Based on the research questions, hypothesis and relevant literature review of FDI, the research objectives of this thesis are:

- 1) To detect the development of FDI in Albania, particularly in the energy sector.
- 2) To determine the main factors affecting the attraction of foreign direct investments in Albania.
- 3) To determine key sectors in attracting Foreign Direct Investments.
- 4) To examine the reasons that push foreign investors not to invest in Albania.
- 5) To examine advantages and disadvantages of FDI.
- 6) To determine the role of FDI in the country's economy, especially in hydropower.
- 7) To determine the opportunities and facilities that Albania offers to foreign investors, especially in hydropower.
- 8) Identification of the role of foreign direct investment in a developing country such as Albania.
- 9) To determine the relationship between FDI inflows, consumption of energy and GDP
- 10) Analysis of the survey findings through data from concrete FDIs in the energy sector and the realization of a questionnaire.

1.2 Hypothesis and research question

An important step for this research is the development of research questions and hypotheses. So, related to this main hypothesis of this thesis are:

Hypothesis1: Improvement of the business climate in Albania has a positive impact on the growth of direct foreign investments in Albania.

Hypothesis2: Political risk, high taxes, property issue have negative impact on the attraction of foreign direct investments in Albania.

Hypothesis 3: Electricity consumption and foreign direct investment have a long-run positive effect on economic growth.

As it can be seen these are main hypothesis of this study which are based on existing theory, and then it will be designed a research strategy to test the hypothesis. The hypothesis can be accepted or rejected, depending on the results of this research.

Also, research question raised in this thesis are:

1. Do political risk, taxes and property issue have negative impact on the attraction of foreign direct investments in Albania?
2. Does the improvement of the business climate have positive affect in attracting foreign direct investments in Albania?
3. Do Albania's general conditions affect the development of direct foreign investments in the energy sector?
4. What is the relationship between electricity consumption, foreign direct investment and economic growth in Albania?

Verification of the hypothesis and providing an answer to research questions will be the final outcome of this work.

1.3 Foreign Direct Investment through years

According to Organization for Economic Co-operation and Development, United Nations Conference on Trade and Development, International Monetary Fund, FDI is defined: “*An investment involving a long-term relationship and reflecting a lasting interest and control by a foreign direct investor or parent enterprise, in an enterprise resident in an economy other than that of the foreign direct investor*” (UNCTAD, 2006).

Generally, foreign direct investments in developing countries and in our country especially, have an strategic importance, because they secure the necessary investment for economic growth of the country. They are a key factor to increase the competition of domestic production in international trades and production in domestic trades. FDI brings advanced technology, knowledge and modern management, also more contacts with foreign customers and make possible that the domestic economy profit from abundance of human capital.

According to UNCTAD, foreign direct investment decreased from \$1.47 trillion in 2013, to \$1.23 trillion in 2014. There are three main reasons to explain this decline such as the level of geopolitical risks, global economic fragility, and at the end uncertainty created to foreign investors. Despite the fall of foreign investments in the global arena, other macroeconomic indicators (here it can be mentioned trade, GDP, and employment) increased. For 2015, global FDI flow increased by +36% (\$1.7 trillion). The main reason for this was the increase in value of cross-border mergers and acquisitions (M&As), affecting directly the increase of FDI. Also, developed economies recorded an increase of FDI inflows, accounting in their favor more than 50% of global inflow. In addition, they reached a record of \$936 billion.

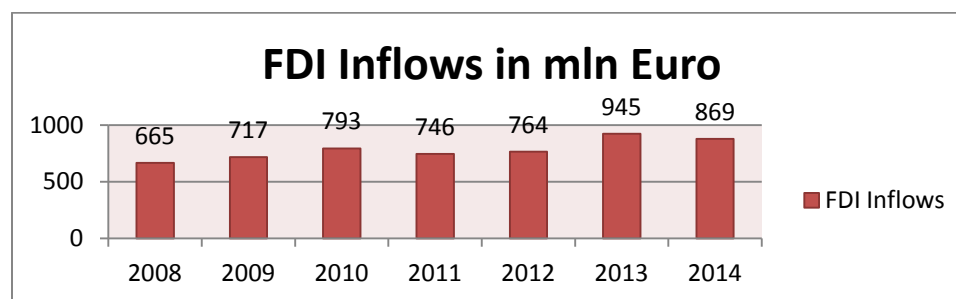
Table 1: FDI inflows, by region and major economy, 2014–2015

FDI inflows (Billions of US dollars)			
Region / economy	2014	2015	Growth rate (%)
World	1245	1699	36.5
Developed economies	493	936	89.9
Europe Union	254	426	67.6
North America	146	429	193.5
Developing economies	703	741	5.3
Africa	55	38	-31.4
Latin America and the Caribbean	170	151	-11.2
Developing Asia	475	548	15.5
Transition economies	49	22	-54.1

Source: UNCTAD.

From 2008 to 2010, foreign direct investment in Albania increased from 665 to 793million Euros, but from 2010 to 2011 FDI decreased to746 million Euro. Moreover, from 2012 to 2013FDI in Albania increased again. The following graph shows foreign direct investments inflow in Albania, for 2008 to 2014.

Graph 1: Foreign direct investments inflow in Albania, for 2008 to 2014



Source: INSTAT, Bank of Albania, Ministry of Finance

Also, it can be said that foreing direct investments from 2013-2014 have decreased. Thus, total number of FDI inflows decreased from 945 milion euro in 2013 to 869 milion euro in 2014.

Following table shows annual FDI inflows in Albania by country and they are presented in milion euro.

Table 2: Annual inflow of foreign investments in Albania by country in million euros

State	2013	2014
Austria	45	-12
Switzerland	-46	74
China	4	-2
Cyprus	-1	13
Czech CZ	40	3
Germany	8	22
France	-1	-4
United Kingdom	-1	5
Greece	13	118
Croatia	-0	6
Italy	83	38
Kuwait	-6	-8
Cayman Islands	17	19
Lebanon	3	1
Luxembourg	3	-1
Macedonia	2	3
The Netherlands	70	82
Norway	-21	1
Turkey	48	63
United States of America	16	35
International Organization	15	11

Source: Bank of Albania, 2016

As it is shown from this table, the largest annual inflow of foreign direct investments in Albania has Greece, the Netharlands, Switzerland, Turkey and Italy meanwhile the lowest annual inflow of foreign direct investments has Lebanon, Luxemburg, Norway etc. To have a clear idea on how was the annual inflow of foreign direct investments in Albania by the economic activity and by manual 6 balance of payments, following table presents a summary from 2013-2014.

Table 3: Annual inflow of foreign investments in Albania by economy activity, in milion euro

Description	2013	2014
Agriculture, hunting and forestry	0	-0
Fishing	-0	-3
Mining and quarrying	589	504
Manufacturing	-114	38
The production and distribution of electricity, gas, steam and hot water	107	75
Construction	-3	-24
Wholesale and retail trade, repair of motor vehicles, motorcycles and personal and household equipment	-9	45

Hotels and restaurants	0	-2
The transport, storage and communication	16	112
Financial intermediation	77	37
Real estate, renting, information technology, scientific research, other professional activities	238	71
Education	1	2
Health and social work	-4	-2
Other community, social and personal activities	0	4
Activities of international organizations	14	10
Total	945	869

Source: Bank of Albania, 2016

As it is shown from this table the largest inflow of foreign direct investments in Albania presents the extractive industry, transportation, telecommunication and financial intermediaries.

Meanwhile the lowest inflows of foreign direct investments present agriculture, hunting, fishing, hotels and restaurants. All in all, it can be said that main areas that which attract more foreign investors were the areas of telecommunications, banking services, energy, construction sector, agriculture, wholesale and retail sales, etc.

1.3.1 FDI in Albania compared to western Balkan countries

Most of Balkan countries are still transition economies. Part of Western Balkan region is: Albania, Bosnia and Herzegovina, Kosovo, Macedonia, Montenegro, and Serbia. All these countries have similar characteristics. In most cases they have the same culture, history, market structure, laws and other features that make them to have the same characteristics. Over the years, western Balkans region have experienced various political and social conflicts but this has changed already. In addition, to have a further development, western Balkan countries are still depended on foreign investments. Despite the economic growth in recent years, compared with European Union, Balkan countries are still known as countries with a low economic development. The main reason for this is the lack of competition and slower economic development. FDI is necessary for Western Balkan region in order to grow and to be accepted as new members of EU. Also, Western Balkan countries need to see what types of foreign investments are favorable for them in order to accelerate their economic development and to be part of the European Union. Attracting foreign direct investment is very important for Western Balkan region. Over the years, the flow of foreign direct investments in Western Balkan region has changed a lot. It can be said that the current level of foreign direct investment in Western Balkan region is still modest. According to World Bank, for 2014, in Western Balkan region the

average FDI stock per capita was €2,600 while in the European Union was €14,300. For 2014, according to World Bank, Serbia is ranked the first in the region on the amount of FDI flow, with more than 2,000 million Euros. The second is Albania with 869 million EUR, followed by Bosnia & Hercegovina, Montenegro, Kosovo and Macedonia. Moreover, Montenegro has (nearly 12%) the highest rate of flow to GDP followed by Albania (9%), Serbia, Kosovo, Bosnia & Hercegovina and Macedonia.

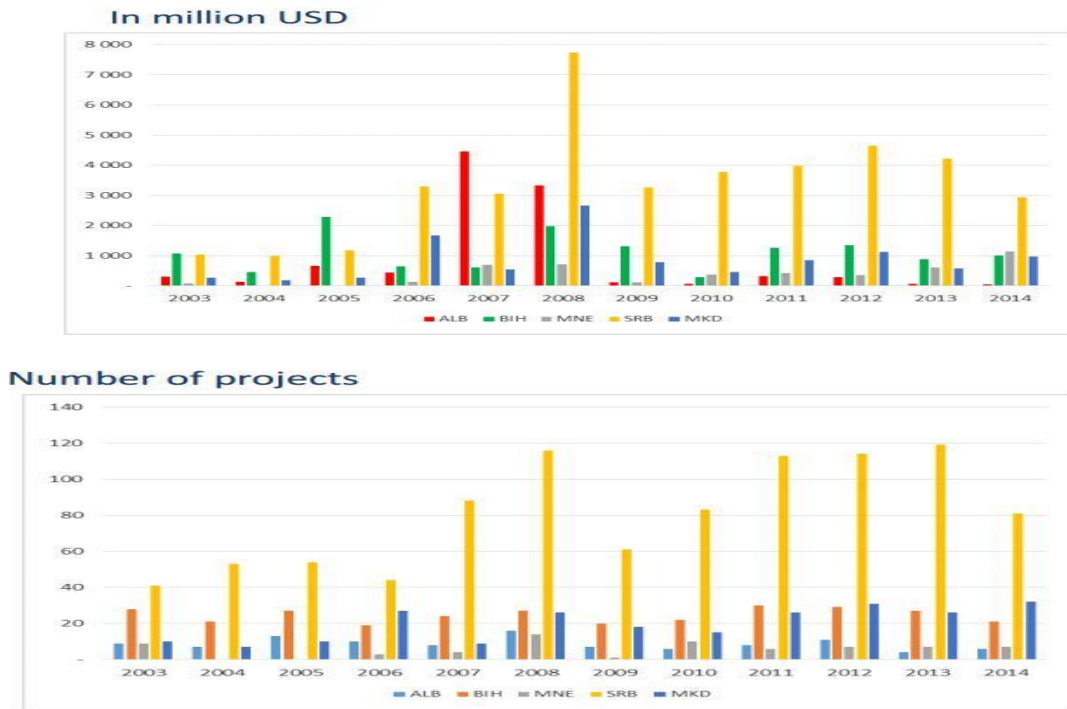
Table 4: FDI inflows in million USD and in % of GDP, western Balkan countries



Source: World Bank Data

According to UNCTAD, in 2014 Serbia was the first in the region on the investment value and number of FDI projects. Investment value was approximately USD 3,000 million and number of projects was more than 80 projects. Albania is the last in the region on the investment value and

Table 5: Investment value and number of projects, western Balkan countries



Source: UNCTAD

For the coming years, FDI flow in Albania is concentrated in Energy, Tourism, Transport and Logistics, in Macedonia, Serbia, and Bosnia & Hercegovina is focused more in Automotive Industry, while in Montenegro FDI flows are focused in Real Estate and tourism industry. It can be said that Albania, compared with the other countries of the region, has good performance relating to foreign investments value. In addition, Albania has low labor cost, competitive fiscal and non-fiscal incentives and has designed various laws on investments. During 2015- 2018, the government of Albania has estimated to have an average flow of FDI approximately 11.5 %. Despite positive advantages, there are some disadvantages affecting the attraction of foreign investments in Albania such as: fiscal burden, property problems, institutional bureaucracy, and Law enforcement.

1.3.2 Advantages and disadvantages of FDI

Advantages that FDI create are numerous. First thing that it can be said is that FDI can stimulate the country's economic development, in this way creating a more conducive environment for foreign investors and benefits for the host country. Lots of countries face import tariff, being one

of the reasons why trading abroad the country it is difficult. Also, some companies want to expense their presence in the international markets, and to ensure the sale of their products .But, through FDI, all these barriers will be easier. Another important thing to highlight is that foreign direct investment creates new jobs, because investors build new companies in the foreign country, in this way creating new opportunities.

One big advantage of FDI is the development of human capital. In this case human capital is the knowledge and competence of those who are able to perform labor, known as the workforce. The attributes that human capital gain by training and sharing experience, increase the education and overall human capital of the host country. Human capital is not a tangible asset of a country. With this in mind, a country with FDI can benefit more by developing its human resources. As we know foreign direct investment can transfer resource and other exchanges of knowledge, technologies and skills. Also the disparity between revenues and costs can be reduced. Another advantage of foreign investment is the increase of the country's income. That's because more jobs and higher wages means higher country's income. As a result, we have an economic growth. Despite these advantages, there are a lot of disadvantages of Foreign Direct Investment.

One of the disadvantages is the negligence of investments made to domestic investors. This is because all resources are focused to foreign investors. Political risk also has a great impact on foreign investment, this is because political power is not the same, and it can change at any electoral choice. The risk of impact on the exchange rate by foreign direct investment is high because it has a direct impact on the value of the domestic currency.

Also, to perform a direct investment in a foreign country means an expense many times higher than the import of products. In this way can we say that foreign investment from the point of view of the investor can be risky or sometimes non- viable. At the end but the most important is that sometimes foreign investment may have negative impact on the country's economy. Investment may be banned in some foreign markets, which means that it is impossible to pursue an inviting opportunity.

1.4 Business climate in Albania and attraction of investments

Albania is upper middle income country with a sustainable economic development. Through years, different economic models are designed with a basic aim on increasing exports,

production and foreign investments. Despite the transition process in the past 24 years, Albania's potential is not fully used. Main purpose of Albania government is to create favorable conditions for business climate and investment environment for foreign and domestic investors. Moreover, the Albania Government has designed new legal framework. These legal frameworks consist on strategic investments, public-private partnership, free economic zones and tourism. In this way, Albania's economy will grow because the foreign investment inflow increases. Foreign direct investments play an important role for the economy of a country because they ensure development, employment and liquidity; in special foreign investments increase the performance level of each sector. Always, the Albanian Government has tried to create a free and competitive market for foreign investors. Nowadays, Albania is more open to foreign investors, creating more investment opportunities because it is a country rich in resources with huge potential.

1.4.1 Doing Business in Albania

According to World Bank Doing Business Report 2015, Albania has better business environment and economic freedom. In 2015, Albania was ranked 68th out of 189 countries. Key indicators that show this progress are: paying taxes, registering property and investor's protection. Moreover, in 2014 the EBRD listed Albania as the top reformer country compared to other countries in the region. Also, The Heritage Foundation's 2015 Index of Economic Freedom shows that Albania is one of the most favorable countries in the region for doing business because it has the highest score in trade, investment and fiscal indicators. Furthermore, Standards & Poor's says that Albania has done improvements since 2014 by climbing from B to B + for 2015. Standard and poor's improved twice the outlook for the country, from B (stable) to B (+).

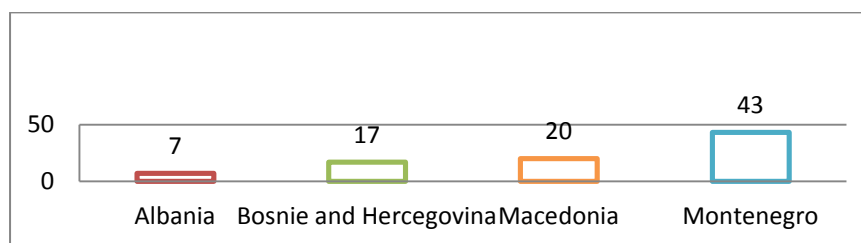
Chart 1: Standard and poor's index for 2015



Source: Standard & Poor's Rating Services, 2015

Related to investor's protection indicator, Albania shows the highest scores because it is ranked 7th from 189 countries listed in this report. This indicator will increase the interest of foreign investors to invest in Albania.

Graph 2: Investor's protection indicator for 2015



Source: Doing Business Report 2015, World Bank

The business climate and investment environment in Albania, has improved a lot. According to the World Bank Report, from 2013 to 2015 Albania shows the highest score in the region. The following table presents Albania compared with regional country.

Table 6: The business climate and investment environment in region, from 2013 to 2015

State	2013	2014	2015
Albania	1.4	2.1	3.0
Bosnia & Herzegovina	2.5	0.4	1.5
Kosovo	3.4	2.5	3.0
FYR Macedonia	2.7	3.3	3.5
Montenegro	3.3	1.5	3.4
Serbia	2.6	-2.0	-0.5
SEE6	2.5	0.2	1.3

Source: National Statistical Offices and World Bank Projections. Note: SEE6 is a weighted average.

As stated above, Albania is very attractive country, with a stable economic, legal and political environment. Also, it has free economic framework and good business conditions for domestic and foreign investors. The Albanian Government has designed a variety of reforms such as territory reform, law reform etc. in this way creating more competitive environment. The focus of all these reforms is to increase production, exports and foreign investment. According to the Ministry of Economic Development, Tourism, Trade and Entrepreneurship, key sectors where foreign investors can invest in Albania are: renewable energy, manufacturing, agriculture, tourism, mining industry, ICT services, transport and logistics.

1.4.2 Key steps in attracting foreign direct investment

According to UNCTAD, globalization has brought change in how international enterprises pursue their objectives in seeking new markets, resources and efficiency. The openness of markets, FDI and technology have provided to international enterprises a wide range of choices on how they want to serve in the international market, how to gain access to the resources and how to improve the efficiency of the production system. FDI is important in developing countries like Albania. There are several factors that affect FDI, and countries are scrambling to adapt as best as they can. Factors influencing FDI inflows are divided into political and economic factors. Some of these factors are:

- Economic, political and social stability
- International agreements on FDI
- Privatization policy, concessions
- Cheap work force
- Size of the market
- Infrastructure
- Institutional and legal environment etc.

The government of Albania has made huge steps in creating favorable conditions to attract foreign investments in Albania. Some of these reforms include:

- Free Economic Zones
- Strategic investments law
- Tourism law
- Territorial and Justice reform

Albania has a favorable location, with huge energy potential. The energy potential on hydro, solar and wind resources is amazing. Also, Albania has signed trade agreements with EU, Central Europe (through CEFTA), Europe (through EFTA), Turkey and USA. Moreover, Albania is a member of World Trade Organization (WTO) and applies WTO rules to all import licensing. Human resources in Albania are very competitive. Workforce is young and very motivated. Workforce is very dynamic and competitive because more than 57% of the population is under 35 years, English & Italian are widely spoken and more than 116,000 students are registered in university. According to Ministry of Economic Development, Tourism, Trade and

Entrepreneurship, the minimum wage is 157 Euro and average monthly payment is 266 Euro. The government has designed new fiscal package in consultation with the International Monetary Fund and World Bank. The main purpose of this package is to keep macroeconomic stability, in this way creating favorable condition for further development and growth. The new fiscal policy includes: Corporate tax rate 15% and Personal Income Tax rate from 0% - 23%. The new fiscal policy is the same for both domestic and foreign investors.

In Albania, the registration of a new business takes 24 hours. The cost of this registration is less than 1\$. Also, licensing of a new business is a quick and transparent process. Business licensing is done through National Licensing Centre. Moreover, most of the services are offered on line, here it can be mentioned: online tax system, tendering procedures and customs services. Albania has designed new legal framework on FDI, in this way creating more favorable business climate. Also, the government is implementing some economic reforms to support foreign investors in Albania. Foreign investors are not limited in operation and they have full openness in the market. Furthermore, they do not need prior government authorization to invest in Albania and no sector restriction is set to them. Moreover, foreign investors are not limited on the percentage of share that they can have in an investment, in most cases they can have 100% of ownership.

Foreign investors are protected by the government. They have all rights to invest in Albania and their investment is equal and unbiased compared with domestic investments. In any case, foreign investments are not restricted on capital movement and on the repatriation of profit. Also, tax procedures are simplified, with competitive tax rate. In general, Albania has shown stable macroeconomic indicators with low inflation, fixed exchange rates and stable prices. It can be said that the average annual inflation from 2009 to 2014 has been stable, nearly 1.9 %. Also, the domestic currency is stable; €1 is equivalent to 140.0 ALL for 2014.

1.5 Hydro Power Plants

Through years, water has played an important role in human history, becoming a vital resource. Water has been used for different purposes, this starting from the use of water as a source of human life further more water is used as a source of energy. Hydropower is a renewable, reliable, nonpolluting source of energy that comes from the natural flow of water. This type of energy supply approximately one-fifth of the world's electricity, but compared with other

renewable sources, hydropower is one of the most important sources of energy. It can be said that hydropower has been used in many ways. An example of early use of hydropower is water wheels. Greeks used it to grind wheat into flour. Also, American and European factories used it to power their machines. This type of machine is very simple in use because the water in buckets that is attached to the wheel causes the wheels to function and its location is below a source of flowing water. Through wheels the potential energy of the water is converted into motion. Then, in the late 19th century, water was used to generate power or electricity. In 1879 at Niagara Falls was built the first hydroelectric power and later many more hydroelectric were built. Firstly plants burned oil and coal because it was cheaper compared with hydro plants but the oil shocked in 1970 increased interest in hydro power plant. As stated above, hydropower is a renewable source of energy. One of the largest producers of hydroelectricity is China. China operates two of the ten biggest hydro power plants in the world.

This thesis aims at providing the benefits of investing in hydropower. For this reason, Albania has an attractive location for such an investment. Albania is dependent on hydropower in the production of electric energy; approximately 100 % of the country's electricity comes from hydropower but there is still place for further development of this sector. Private investment in the hydropower sector can take place in several methods. The first one can take place through the rehabilitation of existing projects and the second through the construction of new projects.

The main focuses of this thesis is on attracting private investment to new projects in Albania. Nowadays, Albania targets the development of small hydropower plants.

1.5.1 Advantages and disadvantages of hydropower

Compared with the other renewable energy sources, hydroelectric power has several advantages. Hydropower energy is a renewable energy source and it will be available as long as the water flows. Furthermore, hydroelectric power does not depend upon the price of other types of fuel for example oil, uranium etc. In this way costs stable and low. This is the most important advantages of hydropower plants. Also, hydroelectric station does not require a large number of employees. Moreover, this is the main advantages why the cost of hydroelectricity is low. One of the most important advantages of hydroelectric power is that it does not produce greenhouse gases. Hydropower plant does not pollute the environment like the other plants that burn fossil

fuels. An important thing to note is that hydropower is a domestic source of energy. In this case, electricity is produced near the place where it is needed. Hydroelectric power is flexible and high efficiency power of energy. That is because conventional hydropower efficiency is approximately 80% compared with other power plants. Also, depending upon the river that is used to operate, hydropower stations can be built in any size and the operation of these stations works for many years after they are built. By the time that electricity is not needed, the station gates can be shut, stopping the production of electricity. In this way, the water can be saved or stored and can be used at another moment when electricity is needed. Thus, hydropower can be available where is needed and the flow of water can be controlled by engineers through turbines to produce electricity. Further, hydropower station can be used for other functions, for example flood control, irrigation, urban rural life, aquaculture, tourism, energy etc.

Nevertheless, building a new hydropower station has some disadvantages that have to be taken into consideration. Firstly, building new hydropower is very expensive this due to high cost of construction. In this way, hydropower stations must operate for many years to become profitable. Another disadvantage is that in most cases hydropower stations can create serious problems between countries or localities by blocking the progress of a river in one country affecting the following country. Therefore, in the case of flood, people who live near the plants must move out because they may lose their houses, farms or businesses. As stated before, hydropower is a renewable energy that produces electricity without using fossil fuels. Additionally, it does not produce greenhouse emission. However, in most cases generating hydropower energy causes some environmental issues. That is because damming areas are rich with biodiversity of flora; this means that its effect on biodiversity is very huge. Also, hydropower has a negative impact on the climate due to large amount of carbon. Moreover, this creates high concentration of methane. Another important thing to highlight is that in most cases hydropower effect watercourse. At the end but the most important is the impact on the fish population.

1.5.2 Hydropower in Albania

Hydropower resource in Albania occupies an important role and position, that's because Albania is one of countries which have the most abundant water resources in Europe. It can be said that Albania is almost dependent on hydropower in the production of electricity that is because

approximately 100 per cent of electricity comes from hydropower. Albania is rich in rivers and it has eight important rivers. One of them is Drin River that is located in northern Albania. The Drin river is one of the largest rivers in the country and on this river are build three hydropower stations: Komani (600 MW), Fierzë (500 MW), and Vau I Dejës (250 MW). According to the Ministry of Economy, Trade and Energy in Albania, the capacity of this cascade is 1,350 MW and represents three-quarters (3/4) of total electricity or in other words 90% of domestic electricity production.

Graph 3: HPP Fierza, Koman&Vau I Dejes output vs. total output 2000-2014



Source: The Ministry of Economy, Trade and Energy in Albania, ERE, KESH

Albania exports and import electricity but in most cases import energy due to high demand. An example of this was in 2011, when the country suffered electricity shortages because of long dry periods and blackouts during prolonged droughts. Moreover, in 2020 energy demand is forecasted to increase by 60 per cent, and so on is very important for Albania to strengthen its electricity market. Through this, Albania can increase its impact in the regional market. Despite the development of other energy resources like thermal, solar or wind, still hydropower is one of the most important and largest energy resources in Albania. Also, it is estimated that only 35 % of hydropower potential in Albania has been developed and there is still place for further development. Most of hydropower projects are delayed because of environment or social issue. Despite this, Albania government is focused more on constructing smaller hydropower plants with a capacity less than 100 MW. Additionally, the government offers passing fiscal barriers for these hydropower plants. Moreover, investments in renewable energy sources have favorable legal and regulatory environment. These are some reasons why Albania’s hydropower sector is still attractive to foreign investors. As stated before, Albania is almost dependent on hydropower plants and so it relies totally on hydrological conditions. Also, the National Energy Strategy has estimated that the annual production of energy from hydropower plants is 10,000 GWh. That is because installed capacity on hydropower plants is 3,000 MW. Before 2015, the Albanian energy

sector was governed by the Law No.9072, dated 22.05.2003 “On power sector”. This law defines everything about the development of this sector such as the production, transmission and distribution of electricity. Moreover, this law defines how investors can obtain a license to operate in this sector. But after 2015, the Government of Albania approved a new law, the law No.43/2015 “On power sector”, reflecting the EU Directives on power sector.

- **Albania hydro graphic territory**

Albanian hydrographical territory is 44, 000 m² and it is quite rich in rivers. Moreover, Albania has more than 152 rivers but eight main rivers are: Drin, Buna, Vjosa, Mati, Semani, Shkumbini, Ishmi and Erzeni. The average altitude of the country is about 700 m above the sea and the total average flow of the rivers is about 1245 m³ /sec. Furthermore, it can be said that these rivers play an important role in the development of hydropower sector in Albania.

Table 7: The main hydrologic characteristics of big rivers in Albania

Rivers	Length km	Catchments area, km ²	Average flow m ³ /s	Module of flow l/S/km ²	Ratio Max/Min flow
Buna	41	5.187	320	-	5,3
Drin	285	14.173	352	24,8	5,1
Mat	115	2.441	103	42,6	9,3
Ishmi	74	673	20,9	31,0	5,9
Erzen	108	760	18.1	24,0	11,2
Shkumbin	181	2.441	61.5	25,2	13,2
Seman	281	5.649	95,7	16,9	13,7
Vjora	272	6.706	195	29,1	7,2

Source: Albania Energy Association

- **Albania hydropower potential**

Albania has huge hydropower potential and only 35.4% of this potential is used. But there is still place for further development. The total hydropower reserves allow the installation of 4500MW.

Starting from 1997 until 2014, 171 concession agreements have been signed for the construction of 502 HPP across the country, with an Installed capacity of 2,113 MWh, expected annual output of 9,121 GWh, and with contracted investment value 314,059 (Lek million) which:

101 In the production phase

Installed capacity 447 MW; expected annual output 1,413,709 MWh; contracted investment value 26,473 million Lek

84 In the construction phase

Installed capacity 666 MWh; expected annual output 2,489 GWh; contracted investment value 134,757 million Lek

317 Pre-construction phases

Installed capacity 1,152 MWh; expected annual output 5,359 GWh; contracted investment value 152,829 million Lek

1.5.3 Energy development in Albania

Through years the history of the energy development has changed a lot. According to Agency of Natural Resources, the Energy and resources sector is mainly dominated by:

- Petroleum sector,
- Hydro-energy sector,
- Mining and quarry sector.

Starting from the Ottoman occupation, even during King Zog period, Albania has not known any signs of energy development. From 1945 – 1951, the average amount of energy per capita was 10 KWh. But after 1952, the sector started to develop. During that time, Selita hydro-power plant started to operate and its installed capacity was 5 MW. After Selita hydropower, other hydropower plants were built. Some of them are Ulza, Shkopet, Bistrice 1 and Bistrice 2. Their total installed capacity was 78 MW. Furthermore, about 90 other small HPPs were built and their installed capacity was 1 MW, this varying between 5-1,200 MW. In this way, some of the nation's needs for energy were met. Also, the average life of these HPP was 25 years and their power generation in normal years was 200 GWh.

Three main hydropower in Albania are Fierza, Koman and Vau i Dejes. They are built on the Drin River from year 1971 to 1985. Also, their installed capacity is 1,350 MW. From 1985 up to 2001, the energy sector in Albania did not recognize further development. As stated before, one of the largest rivers is Drin River, followed by Vjosa and Devoll which are the second and third largest rivers in Albania. Based on numerous studies, these rivers enable numerous opportunities for construction of small and medium HPPs.

In Albania, public sector dominates more than 80% of energy produced by hydropower. Hydropower sector is dominated by The Albanian State. It can be said that the production, transmission and distribution of electricity is controlled 100% by the Albanian State because state owns and operate the Albanian energy system through:

- Albanian Electrical Power Corporation (KESH),
- Transmission System operator (OST)
- Electricity Power Distribution Operator (OSHEE)

The Albanian Electrical Power Corporation is the biggest producer of energy in Albania. Installed capacity of KESH is 1,448 MW and is built in a cascade over Drini River. In 2013, the contribution of KESH was 87% of total energy produced. But in 2014, this percentage dropped to 72%. This decrease occurred due to increased production from private HPPs and HPP under concession in this sector. According to ERE, in 2013 hydro-power output was 6,956 GWh and in 2014 was 4,726 GWh. In other words, the domestic production was estimated Lek 25.5 billion (USD 243 million) in 2013 and Lek 24.1 billion (USD 229 million) in 2014. As the price of energy in Albania is Lek 1 per KWh (or USD 0.01 per KWh), so it can be said that sales from the sector in 2013 were Lek 11 billion (USD 106 million) and Lek 9.6 billion (USD 91.5 million) in 2014. The table below summarizes hydropower output in GWh and in LEK/\$ for 2013 and 2014.

Table 8: Hydropower output in GWh and in LEK/\$ for 2013 and 2014

	2013	2014
Hydropower output in GWh	6,956 GWh	4,726 GWh.
Hydropower output in Lek / \$	Lek 25.5 billion (USD 243 million)	Lek 24.1 billion (USD 229 million)

Source: The Ministry of Economy, Trade and Energy in Albania

The Albanian State regulates power sector. This starts from the price of energy that is generate, transmission and at the end distribution of this energy. This is the main reason why the contribution of this sector to GDP is 2%. It can be said that not all energy is transmitted, most of power is lost. That is because the distribution system in Albania has bad technical condition and high informal connection. Additionally, in 2013 more than 45% of power transmitted was lost, but in 2014, the losses decreased to 37.81%. The main reasons why the losses dropped to this level were the Government's and OSHEE efforts. Moreover, estimated foregone contribution of energy losses for 2013 were Lek 22.3 billion in 2013 (USD 212 million) and Lek 19.9 billion in 2014(USD 190 million).

Due to the increase of production from private HPPs, the cost of domestic energy output has changed a lot through years and is forecasted to change more in the future because a huge number of medium and small HPP are expected to be built. In 2013, the contribution of this sector in the state budget is estimated 0.2% of total income but this value dropped to 0.1% for 2014. Furthermore, the government has collected more than Lek 15,439 billion from the privatization of Shkopet, Bistrice 1& 2 and Ulza. These HPPs were under the management of KESH until 2013. Additionally, it can be said that contribution of this sector to the National budget for 2013 increased by 4.9%. According to AKBN more than 502 HPPs are under concession. About 308 of them with an installed capacity of 1,152 MW and estimated energy 5,359 GWh have not been built yet. Also, 84 hydro power plants are in the construction stage. An important thing to highlight is that all HPPs in Albania are under concession and the concession fee in 2013 was Lek 1.78 billion and Lek 1.9 billion in 2014. It can be said that mostly Albania depends on hydropower to fulfill its electricity needs. The main goal of the Albanian government is to be self-sufficient with energy. In this way Albania can be able to meet all of its energy demand and to be the main player in the regional energy market. Moreover, the Albanian government will continue to prioritize the use and utilization of energy resources this with a low impact on the environment and society. This can be able through promoting the use of renewable energy sources such as water, solar, wind and biomass energy.

In addition to this, Albania has created several fiscal facilities to encourage the development of hydro power plants. As stated before, Albania is one of the most dynamic countries in Europe

with a great potential in the energy sector. Furthermore, the main priority of The Albania government is the development of renewable energy. This is done through a serious commitment and concrete strategy of the Albanian government. In this way, Albania can become a leading renewable energy-driven economy.

Table 9: Hydro- power Potential in Albania

Total installed capacity	1,878 MW
Potential installed capacity	4,500 MW
Average power production	4.2 TWh
Potential annual power production	16-18 TWh
Hydroelectric energy potential utilized	35%

Source: The Ministry of Economy, Trade and Energy in Albania, ERE

From 2010 to 2014 the electricity production in Albania has changed a lot. The table below shows this change:

Table 10: Main Indicators of electricity in Albania, from 2010 to 2014

Main Indicators of electricity	2010	2011	2012	2013	2014
Energy(MWh)	6.772.750	7.210.731	7.619.409	7.857.033	7.793.736
Production (MWh)	7.673.728	4.036.309	4.724.800	6.959.326	4.726.246
HHPs(MWh)	7.673.728	4.036.309	4.724.800	6.959.326	4.726.246
Import gross(MWh)	1.004.571	3.474.966	3.230.144	2.322.528	3.355.987
Export gross(MWh)	1.905.549	300.544	335.535	1.424.821	288.497
Consumption by consumers(MWh)	4.605.551	5.031.574	4.369.370	4.551.411	5.010.554

Source: The Ministry of Economy, Trade and Energy in Albania

To have a clear idea about investments on hydropower sector in Albania a real case study is taken in consideration. In this section it is presented Lapaj HPP, which is one of the biggest hydropower that operates in Albania.

- **Gjo-Spa project**

The Lapaj hydropower plant is located in the north of Albania, on the Bushtrica River in Bushtrice, Kukes. Hydropower Lapaj uses the waters of the river Bushtrica and has an installed

capacity of 13.62 MW, with an average annual energy production estimated at 49,865 MWh. The type of this HPP is run off power plant. This project is an investment worth about 14 million euro realized from the concessionary company "Gjo-Spa Power" sh. p. k., part of the Italian group ETEA. Construction of this hydropower plant started in 2008. Lapaj hydropower plant was built with maximum utilization of water flow but at the same time leaving opportunities for irrigation to local residents. Since 2012, Lapaj hydropower plant has started work and produces enough energy to cover the needs of more than 22,000 families. From its construction till now are employed 2500 employees, engineers and specialists. HPP Lapaj has created new jobs and providing a positive impact to the country and the region. It can be said that the construction of this HPP guarantees the reliable supply of electricity, reduces energy imports and does not produce any gas emission, in this way minimizing the environment affects. In future, this power plant will be producing more than 55 million kilowatt-hours of electrical power. At the end of the 35-year which is the concession period, the HPP Lapaj will be handed over to the Republic of Albania. This hydropower plant has these economic and technical parameters:

1.6 Hydropower Concession and public -private partnership

The Ministry of Economy, Trade and Energy in Albania is the main authority that has responsibility for all concessions given in hydropower sector. The Albanian legislation on concessions defines all procedures that investors should follow in obtaining a concession contract in the hydropower sector. The Government of Albania has approved a concession law which states that all concessions are granted up to 35 years. Before 2013, all investments that are constructed and operated in hydropower sector were regulated by law The Law No. 9663, dated 18 December 2006 "On Concessions" and regulation "On the evaluation and granting of concession", approved with CMD. No. 1701, dated December 17, 2012. This law recognized the hydropower concessions as Build-Operate-Transfer, where the investor finances the construction of the project and then benefits from its. Energy produced for sale is regulated by the Power Purchase Agreements, between the investor and Wholesale Public Suppliers with tariffs that is regulated by ERE. But in 2013, the government of Albania approved new law. The Law No. 123/2013 "On Concessions and Public-Private Partnership" ("Law on Concessions and PPP") and additional regulations "For the evaluation and granting of concessions and public-private

partnership” approved by decision. No. 575 dated July 10, 2013 ("New Concessions Regulation"). The law on Concessions and Public-Private Partnership defines "Public Private Partnership" as a long-term contractual cooperation between the public partner which is the contracting authority and private partner which is the economic operator. Within the competence established by the public partner, the private partner is obliged to provide this service to the public. Moreover, the private partner should present to the public partner the necessary preconditions in providing this public service. Prerequisites may consist in the renovation, operation, maintenance or construction of public infrastructure. Payments to the private partner can be done in two ways, either by the public partner or service users which is arranged by the public partner.

Concessions granting and contracting of Public Private Partnership

1. Identification of concession opportunities

The Ministry of Economy, Trade and Energy in Albania receives project proposal for the construction of hydropower. These project proposals may come from government institution, different organizations or private investors. Before granting the concession contract, The Ministry of Economy, Trade and Energy analyzes all the impacts that this concession may have on the economy, environment and society, all this in accordance with Albanian laws. Moreover, investors should also carry out a study on their project proposal in accordance with applicable laws in Albania. Then, the project is subject to a technical assessment in accordance with the government decision No. 191, dated March 22, 2007 "For the establishment of state technical opposition to construction projects of HPP under concession". After, the project is appointed by METE and approved by KBN; experts of hydro-energy, environmental and geology perform this evaluation in accordance with the law No. 8093, dated March 1, 1996, "On water reserves" and the Law No. 8402, dated September 10, 1998 "On the control and regulation of construction works”.

2. Procurement procedures

After the ministry approves the project and enables the concession, all potential investors are invited to participate in a tender procedure, in accordance with Law The Law No. 9643 November 20, 2006 "On Public Procurement" ("The law on public procurement"). Moreover, the allocation of concessions is done in accordance with the provisions of the law No. 9643, dated 20

November 2006, and amended “On Public procurement”. The concession law and regulation defines that all applicants should be treated equally and fair. According the law on concession, if the concession is changed from the initial proposer to another investor, the initial investor is compensated from 0.5% to 2% of the concession value. Also, this value varies from the study carried out in the initial project proposal. The concession price depends on the technical and economic advantages of the project and highest concession fee that is offered. Moreover, the investor must pay a guarantee, which is estimated to be 10% of the investment, in cases where the contract is violated or conditions are not respected.

3. Approval of concessions

The Ministry of Economy, Trade and Energy sign the concession contract and the Council of Ministers approves them. After this, the investor develops in detail the construction plan. Moreover, the project is subject to numerous permits and licenses, such as: permits for construction, the use of water resources, the transmission, power generation, environmental etc. Terms of the concession contact and public-private partnerships are confidential.

The terms of a concession contract for the construction of hydropower are:

- a. Object of contact.
- b. Duration of the Concession.
- c. The Concessionary Company.
- d. Features of the hydropower plant.
- e. Investment Value.
- f. Fee and re-investment value.
- g. Contract guarantee.
- h. Concession benefits
- i. The projects risks

CHAPTER 2

LITERATURE REVIEW

2.1 Literature Review

The World Bank defines FDI as “*the net inflows of investment to acquire a lasting management interest (10 percent or more of voting stock) in an enterprise operating in an economy other than that of the investor. It is the sum of equity capital, reinvestment of earnings, other long-term capital, and short-term capital as shown in the balance of payments.*”(The World Bank, 2016)

Based on their motivation, there are three main types of foreign direct investment (Chrysochoidis G., Millar C. and Clegg J. , 1997). First, market seeking FDI: This type of FDI is based on market size and market growth in the host country. Second, resource seeking FDI: In this case, foreign investor wants to have access to the resources in the host country such as natural resources, raw materials etc. Third, efficiency seeking FDI: In this case the investor will profit from the common governance of geographically activities.

According to Farrell (2008), through foreign direct investment a firm is allowed to operate in foreign market, providing various goods and services. Moreover, Farrell states that a foreign direct investment is a package of some main indicators such as management, technology, and capital etc., which can help foreign investors to enter in the global market (Farrell, 2008). Direct foreign investments are seen as a way through which the host country can increase its economic (L. Alfaro, A. Chanda, S. Kalemlı-Ozcan, and S. Sayek, 2010); (Mencinger J. , 2003), moreover foreign investment may be more effective for a country because in most cases they provide more economic growth compared with domestic investment (J. De Gregorio, J. W. Lee. and Borensztein, E., 1998).

Also, ODI (1997) analysis foreign direct investment flows in countries with low-income and he states that foreign direct investment has an important role for economic growth in developing countries (Overseas Development Institute, 1997). According to Mottaleb (2007) foreign direct investment are essential for rapid economic growth generally for developing countries. It can be

said that developed countries attract more foreign direct investments compared to developing countries. Thus, Mottaleb reached the conclusion that countries with a high GDP growth, a developed infrastructure and an attractive business environment, can attract more FDI flows, thus affecting economic growth of a country (Mottaleb, 2007). Moreover, Khan investigated the role of FDI in this age of globalization (Rahman, 2008). According to him, FDIs have increased greatly in recent years, thus playing an important role in the economic growth of many countries. Also, the distribution of FDI inflows is unequal because rich countries attract more FDI than poor countries.

According to OECD, there are five positive effects that a foreign investment has on economic growth in the host country (OECD, 2002): transfers advanced technology, develop human resources; integrates the economy towards development; improves competition; and at the end creates development opportunities for firms. Overall, it can be said that in most cases FDI have positive impact on economic growth (Moura, R., and Forte, R., 2009). Beside positive effects, FDI may have negative impact on economic growth of a country (Moura, R., and Forte, R., 2009). Furthermore, some studies indicate that FDI does not have a positive effect on economic growth. In their studies, Ocaya, Ruranga and Kaberuka tested the correlation between FDI inflows and economic growth, concluding that these variables are independent from each other (Bruno Ocaya, Charles Ruranga, and William Kaberuka, 2013.). Also, Mencinger conducted a study of the relationship between FDI and economic growth, focusing on Central and East European, came to the conclusion that a negative correlation exist between them (Mencinger J. , 2003).

According to Eller, Haiss and Steiner foreign direct investment does not have always positive effect on the economy of a country, but in some cases they show negative impact on economic growth (Eller, M., Haiss, P. and Steiner, K., 2005). It can be said that foreign direct investment does not always bring the expected impact on economy. Smeets et al. concluded that countries that benefit most from foreign investment are rich countries (Beugelsdijk S., Smeets R., Zwinkels, R., 2008) (Magnus Blomstrom, Robert E. Lipsey and Mario Zejan, 1992). According to Gallagher and Zarsky, in most cases foreign direct investments have a negative impact on poor countries (Kevin P.Gallagher and Lyuba Zarsky, 2006). There are too many factors that affect the attraction of foreign direct investment. Borensztein et al. states that there is a link between

foreign investment and human capital; economies with low level of human capital have negative impact from FDI (J. De Gregorio, J. W. Lee. and Borensztein, E., 1998).

Moreover, Borensztein et al, show that foreign investments have positive impact on economy if the level of human capital insufficient trained and educated (J. De Gregorio, J. W. Lee. and Borensztein, E., 1998). To continue, another factor that affect FDI are institutions (here it can be mentioned property rights), because if a country has problems with property rights then the country will not be attractive for foreign direct investment (Ali F., Fiess N. and MACDonald R., 2011). Another important thing is that forms of foreign investment (i.e. mergers & acquisitions and “Greenfield” investment) affect the impact that they will have on economic growth. In this case, M&A provide low economic growth compared to Greenfield. According to Wang and Wong, M&A activity depends more on human capital compared to Greefield Investment, that’s the main reason why M&A provide low economic growth. Furthermore, Wang and Wong state the effect that foreign investments have on economic growth does not depend much on their form for example Greenfield or M&A (Miao Wang and M. C. Sunny Wong, 2009).

Nowadays, many studies explain the role of foreign direct investment in developing countries, focusing more on the factors affecting the attraction of foreign direct investments. According to UNCTAD, there are two main determinants of FDI: Business facilitation and Policy framework for FDI (United Nations Conference on Trade and Development, 1998). According to EkremTatoglu, there are some factors, such as economy openness, market size, and developed infrastructure etc., that have positive impact on attracting foreign investors. Moreover, Tatoglu stated that other factors such as economy instability, political instability etc., have negative impact on attracting foreign investors. International investors have concluded through their studies that factors such as institutional framework investment policy, market size, human capital, and infrastructure, political and economic stability play an important role on attracting foreign investors (Tatoglu, 2002). Overall, It can be said that main factors that affect the attractiveness of FDI are: political, economic and social conditions; institutional framework, protection and treatment of foreign investors; investment incentives; market size, natural resources, market growth, structure and accessibility; raw materials, human capital, infrastructure and telecommunication.

In general, foreign direct investments bring development and growth in a country. Furthermore, FDI is a key indicator for economic development, especially in developing countries, because developing countries have huge potential in natural resources and human capital. Thus, FDI in hydropower sector play a significant contribution in transferring new technology, creating new jobs, increasing income etc. Investing in hydropower sector may create numerous advantages such as economic, social and environmental one. According to Kaygusuz, hydropower is that type of energy sources that is growing very fast all over the world, especially in the developing countries(Kaygusuz, 2004), in this way being a key indicator for economic development in many developing countries.

Pao and Fu's (2013) studied the importance of hydropower. According to them there is a long term positive relationship between GDP and hydropower. In this way, it can be said that limiting the use hydroelectric would prevent economic growth of a country. Pao and Fu stated that limiting factors may be different unfavorable policy that would directly affect the use of hydropower (Pao, H-T. and Fu, H-C., 2013). In recent years, Albania has attracted numerous foreign direct investments mainly in hydropower sector because Albania offers great opportunities to develop hydropower plants.

Moreover, Sari et al. studied the relationship between energy consumption, industrial output and employment. They found that there was a presence of co-integration between the variables (R. Sari, B.T. Ewing and U. Soytas, 2008). In addition, Shahbaz et al. examine the relationship between renewable energy consumption, capital, labor and economic growth and concluded that renewable energy consumption, labor and capital increase economic growth (M. Shahbaz, N. Loganathan, M. Zeshan and K. Zaman, 2015).

Albania is rich in natural resources, the use of which will have significant contribute to economic growth. One of the forms of use of natural resources is hydropower, which has been growing from year to year. Thus, the government of Albania has undertaken numerous initiatives in order to attracting FDI mainly hydropower sector. Despite the development of other energy resources like thermal, solar or wind, still hydropower is one of the most important and largest energy resources in Albania. Also, it is estimated that only 35 % of hydropower potential in Albania has been developed and there is still place for further development.

CHAPTER 3

DATA AND METHODOLOGY

3.1 Data and methodology

The methodology used is a function of the goals set out in this study. This type of methodology is based on the alternation of the primary and secondary data.

- ✓ Primary data

3.1.1 Econometric model

As Albania is dependent on hydropower in the production of electric energy; approximately 100 % of the country's electricity comes from hydropower and for 2020 the demand for energy will increase to 60%, it is important to analyze the relationship between FDI, energy conception and GDP in developing countries such as Albania. Main focus of this thesis is to analyze to relationship that exist between electricity consumption, foreign direct investment and economic growth in Albania. The thesis uses Autoregressive Distributed Lag model to study the relationship between electricity consumption, economic growth and foreign direct investment in Albania from the period 1985 to 2014, retrieved from the World Bank and Energy Regulator Authority. Numerous studies have found that there is a long-run relationship among them; foreign direct investment and electricity consumption have a long-run positive effect on economic growth.

- ♣ Model specification and data

The data in this thesis include foreign direct investment (net inflows), real GDP per capita and net consumption of total electricity. The sample period is from 1985 to 2014. As it was mentioned above, in order to examine the relationship between economic growth, electricity consumption and foreign direct investment, a linear natural logarithm equation is specified as following:

$$GDP_t = B_0 + B_1 E_t + B_2 FDI_t + e_t$$

- (1) GDP_t - real GDP per capita (US\$),
- (2) E_t - E is net consumption of total electricity (MWh),

- (3) FDI_t - FDI is net inflows of foreign direct investment (BOP, current US\$),
- (4) e_t - is the error term,

Data from 1985 to 2014 for foreign direct investment (net inflows) and real GDP per capita and were obtained from the World Bank, while that of net consumption of total electricity were obtained from Energy Regulator Authority, annual reports from 1985 to 2014.

3.1.2 Survey

This survey is used as another way of collecting primary data. The purpose of the survey was to gather the views and judgments of foreign investors and domestic investors in the energy sector. Through this questionnaire it will be analyzed the current situation in Albania's hydropower sector, role and development of FDI in Albania, difficulties and opportunities that they face, number of people employed in this sector and at the end but the most important the absorption of foreign direct investment.

Focus group- The choice of each category is based on the search patterns of foreign authors as well as specific issues that the author has identified as valuable for the construction of this study. More specifically there were interviewed through structured and semi-structured interviews 72 domestic and foreign investors in the field of hydropower. As mentioned above part of this focus group besides foreign investors were domestic investors too, because the main goal is to see if domestic and foreign investors face the same difficulties or challenges in hydropower sector in Albania.

To answer the research question and hypothesis are used data collected from questionnaires. The survey was conducted by representatives of foreign investors and domestic investors in Albania. To determine the number of completed questionnaires for this study was used Taro Yamane formula. Under this formula, the number of sample can be calculated as follows:

$$n = \frac{N}{1 + N * e^2}$$

Where:

- N population size
- n sample size
- e the level of significance

In the case 5% is the significance level

Knowing that hydropower sector has 101 hydropower plants in operation, based on the above formula, the number of elements of the sample would be:

$$n = \frac{101}{1+101*0.05^2} = 80.6$$

From questionnaires 85 completed, 13 proved to be invalid. Thus the data of 72 questionnaires were processed in this analysis. A copy of the questionnaire used in the survey is presented in the appendixes of this thesis.

The questionnaire covered the following issues (elements):

- reasons for investing in hydro power sector
- challenges that these companies face when they invest in Albania
- opportunities and facilities
- their interest for the future
- main factors that a foreign company should take into consideration when they start an investment

✓ Secondary data

Secondary data are provided by the literature, such as the National Library, the library of Epoka University. Also here we can mention annual reports from Bank of Albania (BoA), The World Bank, IMF, INSTAT, Ministry of Economy, METE, government institutions, books, business, as well as various academic books. Another source of information were also various electronic addresses, as well as academic research works, works conferences, journals, business associations, and lectures on the field or research papers.

Both types of information, like the primary and secondary, have served on the analysis performed in this study, and helped the methodology used to see which are the problems and challenges of FDI in Albania and how we can improve the situation in which we are.

CHAPTER 4

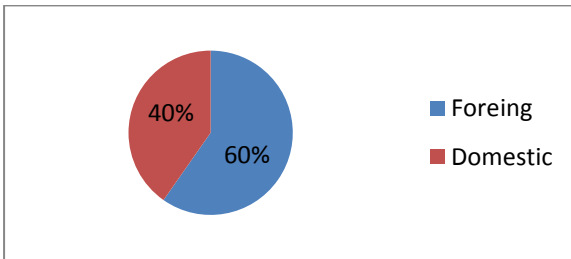
EMPIRICAL RESULTS

This section represents the results of the thesis based on the methodology employed above. It includes survey results, unit root test results, co-integration results and the error correlation model

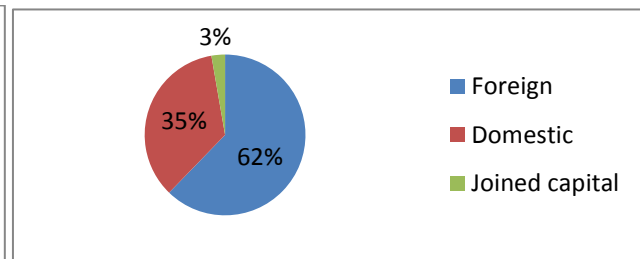
4.1 Survey results

There were interviewed through structured and semi-structured interviews 72 domestic and foreign investors in the field of hydropower. The total group of interviewed investors is divided into two groups: Foreign investors 63% and domestic investors 37%.

Chart 2: Type of investor interviewed



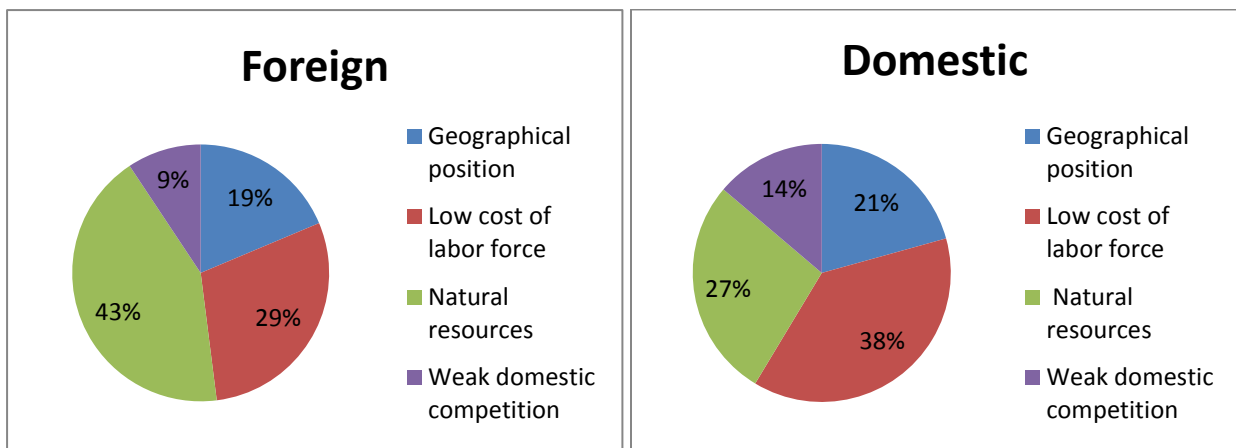
Type of ownership



Source: The conducted survey

Replying to question about the type of ownership, it can be said that 62% of investors were foreign investment, 35% domestic investment and 3% joined capital (foreign and domestic).

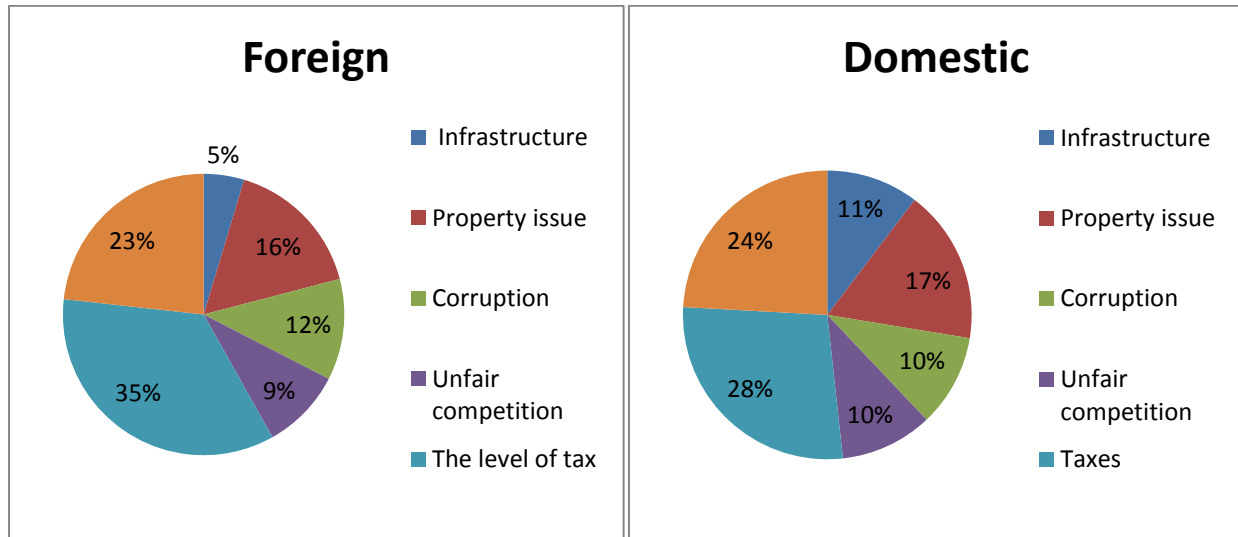
Chart 3: Reasons for investing in the energy sector



Source: The conducted survey

Than about question that which were the reasons for investing in the energy sector, foreign investors' highlighted natural resources and labor cost. Also domestic investors said that main reasons for investing in this sector were natural resources, labor cost and geographic position.

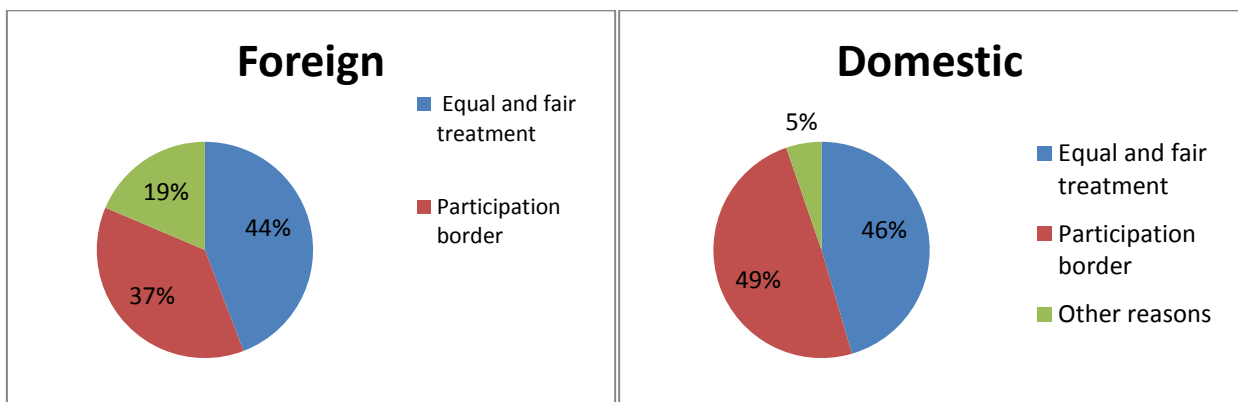
Chart 4: Obstacles on hydropower sector



Source: The conducted survey

Abut obstacles on hydropower sector, for foreign investors main obstacles are taxes, political risk and property issue. The same thing can be said about domestic investors. They highlighted as first taxes, property issue and political risk. It can be said that both type of investor face the same obstacles when they invest in this sector.

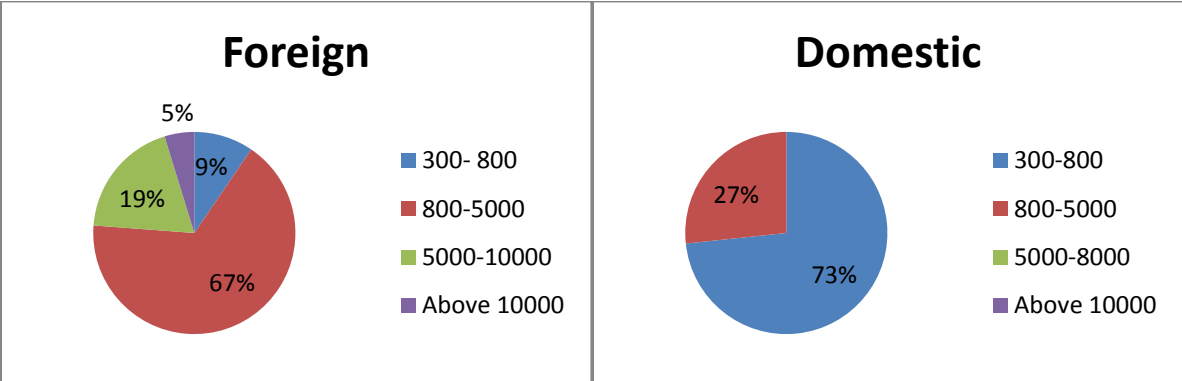
Chart 5: Mitigating factors



Source: The conducted survey

Replying to question about mitigating factors, both type of investors, domestic and foreign, stated that treatments and participation borders were main factors that attract them to invest in this sector. Moreover, foreign investor added the agreement on avoidance of double taxation.

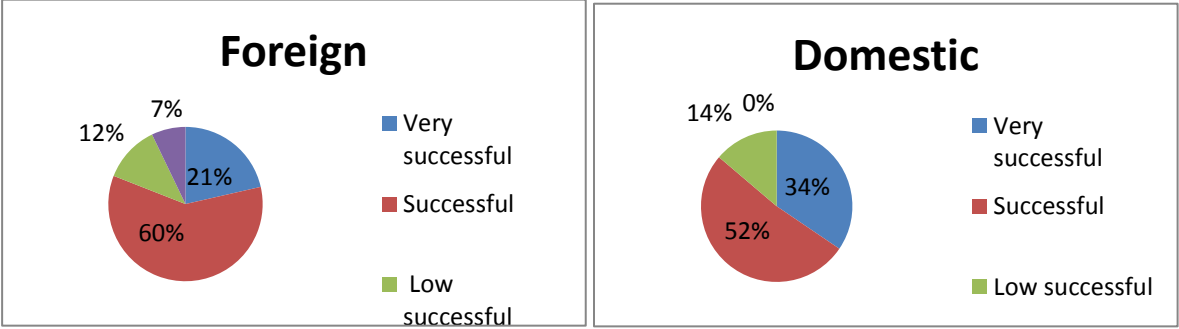
Chart 6: Employment



Source: The conducted survey

About employment, for foreign investments, 67% of them employed from 800 to 5000 employees, 19% from 50000 to 10000, 9% 300 to 500 employees and 5 % more than 10000 employs. For domestic investments, 73% of them employed 300 to 800 employees and 27% from 800 to 5000 employees. This difference between domestic and foreign investments can be explained because most of domestic investor have invested on hydropower with an installed capacity of 2 or lower than 2 MWh. This means that their investment is not huge compared to foreign investors that can invest on hydropower with an installed capacity of 20.000 MWh.

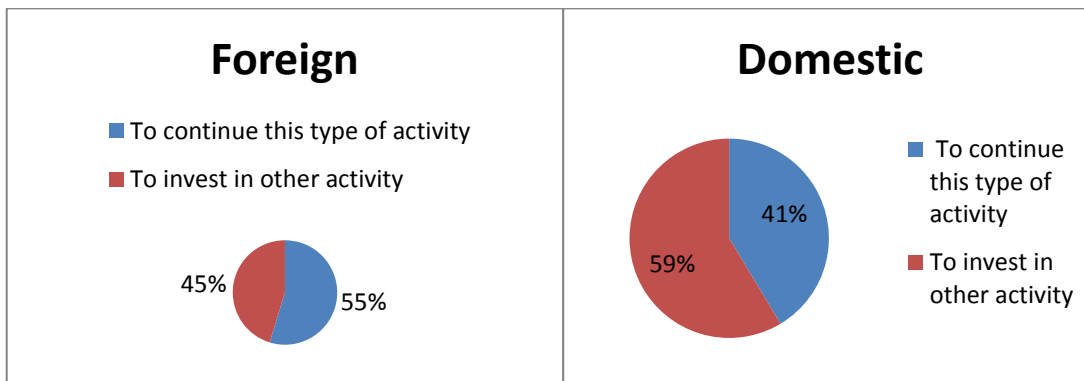
Chart 7: Success of the investment



Source: The conducted survey

Then, about the success of their investment, for foreign investor, 60% said that it was successful, 21% very successful, 7% low successful and 12% not successful. About domestic investors, 52% said that their investment were successful, 34 % very successful and 14 % low successful. These results indicate that despite difficulties in this sector, foreign and domestic investors still consider their investment to be successful.

Chart 8: Future investment

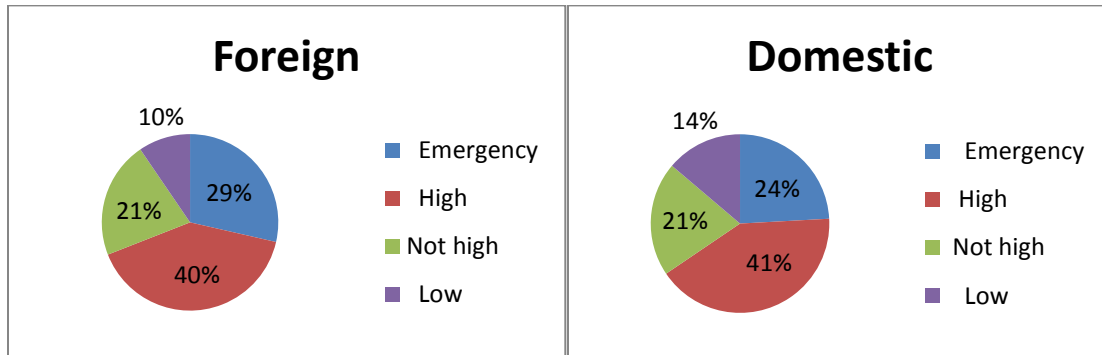


Source: The conducted survey

Then, about future investment, for foreign investors, 55% of them said that they would invest in this sector and 45% said that they would invest in other activities. For domestic investors, 59 % of them would invest in other activity and 41% would continue this type of activity. Main reasons why some of investors said that would continue this type of activity is that it is very profitable sector and the market of electricity is secure. As it can be seen, a high % of investor would not invest in this sector because of difficulties mentioned above and because Albania has other attractive and profit sectors when they can invest in the future.

Moreover, foreign and domestic investors were asked on how they judge the need of the Albanian economy for the concession contract, because this sector is characterized by high number of concessionary contact. In both cases, they said the need of the country for concession contract is high because Albania is a developing country and concessionary contract would be key indicator for further development.

Chart 9: Concessions in Albania



Source: The conducted survey

Also, all the energy that is produced by these hydropower plants is sold in Albania, in order to fulfill the county needs. At the end but the most important, according to foreign and domestic investors, the Albania Government should remove barriers in obtaining development permits; cut taxes and should create its own energy markets, where investors can trade the electricity.

All in all, it can be said that based on the existing literature and survey, there are lots of factors that affect the attraction of FDI such as market size, labor costs, infrastructure, legal environment, privatization policy, economic political and social stability.

4.2 Unit Root Test Result

The thesis uses Autoregressive Distributed Lag model to study the relationship between electricity consumption, economic growth and foreign direct investment in Albania from the period 1985 to 2014, retrieved from the World Bank and Energy Regulator Authority. Unit root test is employed and the result is reported in the following tables.

It can be seen that GDP stationary in the first difference because P- value is 0.006 lower than 0.05, electricity is stationary in the first difference because P- value is 0.0034 lower than 0.05 and FDI is stationary in the first difference because P- value is 0.003 lower than 0.05.

Table 11: The result of Dickey-Fuller (ADF)

variables	ADF statistics	Critical value (5%)	Probability P	conclusion
GDP	0.894235	-2.96777	0.994	not stationary
D(GDP)	3.90253	-2.97185	0.006	stationary
ELECTRICITY	-0.328809	-2.967767	0.9087	not stationary
D(ELECTRICITY)	-4.1362	-2.97185	0.0034	stationary
FDI	-0.22112	-2.96777	0.9249	not stationary
D(FDI)	-4.17856	-2.97185	0.003	stationary

All in all, it can be said that the result shows that all variables used in this study are non-stationary in level and stationary in first difference. According to p-values that obtained from the regression model, FDI, GDP and Energy are stationary in their first difference, because their p-values are smaller than 0.05 which means they fit to the rule that $p \leq 0.05$.

4.3 Co-integration result

To see the co-integration between Electricity and GDP, run a regression of GDP and electricity and save residuals, if residual is stationary in level, there is co-integration.

Table 12: Co-integration result tables

Variables	ADF statistics	critical value(5%)	Probability P	Conclusion
D(RESID01)	-3.421783	-3.004861	0.0212	stationary

It can be seen that residuals are stationary in level because P- value is 0.0212 lower than 0.05.

Dependent Variable: D(RESID01)				
Variable	Coefficient	Std. Error	t-Statistic	Prob.
RESID01(-1)	-0.579765	0.169434	-3.42178	0.0045
D(RESID01(-1))	0.551144	0.203289	2.711136	0.0178
D(RESID01(-2))	0.341178	0.244177	1.397254	0.1857
D(RESID01(-3))	0.481108	0.202854	2.371696	0.0338
D(RESID01(-4))	0.3219	0.228142	1.41096	0.1817
D(RESID01(-5))	-0.105396	0.230974	-0.45631	0.6557
D(RESID01(-6))	0.681953	0.259702	2.625902	0.0209
D(RESID01(-7))	0.475016	0.28181	1.685594	0.1157
C	-118.8939	65.40673	-1.81776	0.0922

It can be seen that GDP and Electricity are co-integrated to each other and they have a long run relationship among them.

4.4 The error correlation model

To see the short run between them it is used error correlation model. This model indicates that these variables do not have short run correlation.

Table 13: The error correlation model

Dependent variable: GDP				
Variable	Coefficient	Std. Error	t-Statistic	Prob.
DELECTRICITY	0.208476	0.16563	1.258684	0.2193
RESID01(-1)	-0.063456	0.066634	-0.95231	0.3497
C	96.19128	56.11143	1.71429	0.0984

But if all three variables are taken in group and tested if they are co-integrated to each other it can be said no. In group they are no co-integrated. That is because FDI it is not co-integrated with GDP and there are lots of factors that affect the trend of FDI such as taxes, political risk, property issue etc.

Table 14: Unrestricted Co-integration Rank Test (Trace)

Hypothesized	Trace		0.05	
No. of CE(s)	Eigenvalue	Statistic	Critical Value	Prob.**
None	0.548523	28.675	29.79707	0.0669
At most 1	0.468922	12.77037	15.49471	0.1235
At most 2	0.005656	0.113451	3.841466	0.7362

Trace test indicates no co-integration at the 0.05 level

* denotes rejection of the hypothesis at the 0.05 level

**MacKinnon-Haug-Michelis (1999) p-values

Table 15: Unrestricted Co-integration Rank Test (Maximum Eigenvalue)

Hypothesized	Max-Eigen		0.05	
No. of CE(s)	Eigenvalue	Statistic	Critical Value	Prob.**
None	0.548523	15.90463	21.13162	0.2305
At most 1	0.468922	12.65692	14.2646	0.0883
At most 2	0.005656	0.113451	3.841466	0.7362

Max-eigenvalue test indicates no co-integration at the 0.05 level

* denotes rejection of the hypothesis at the 0.05 level

**MacKinnon-Haug-Michelis (1999) p-values

CHAPTER 5

CONCLUSSION AND RECOMANDATION

5.1 Conclusions

FDI brings benefits to the economy, by making contribution to GDP and total investment in a host economy. As it was said above, FDI is an important indicator in the economy because it allows transfer of advance technology, increases the efficiency in production, increase employment and has it positive impact on the balance of payments through export growth. Now, FDI has become one of the largest sources of external finance for a country.

Moreover, FDI provides various opportunities for a country because investors can have access to global market, human capital and natural resources are used in optimal way, markets are more competitive and efficient. There are lots of factors that affect the attraction of FDI such as market size, labor costs and productivity, political risk, infrastructure, legal environment, and privatization policy etc.

Hydropower is a renewable source of energy, being one of the clearest and cheapest sources of energy. There are many advantages of investing in hydropower plants. First, hydropower does not cause greenhouse gasses or other harmless emissions and it does not cause global warning or climate changes. Second, hydropower plants can be used for irrigation, energy production, tourism etc.

Moreover, hydropower is a reliable source of energy, with a regular production of electricity. Also, they generate the largest share of electricity worldwide, compared with other sources of energy such as wind, solar or thermal. The use of hydropower plants as a form of generating electricity means faster, sustainable and consistent production of electricity for the future. Hydropower energy is a renewable energy source and it will be available as long as the water flows.

However, using hydropower plants has many disadvantages too. In many cases it can be very dangerous because it causes negative effects on the environment. Hydropower plants can destroy agriculture land, small animals and other habitats.

Albania has huge dependence on hydropower plants. The results show that FDI has played a very strategic and critical role in the economic growth of Albania. Albania is dependent on

hydropower in the production of electric energy; approximately 100 % of the country's electricity comes from hydropower.

Moreover, in 2020 energy demand is forecasted to increase by 60 per cent, and so on is very important for Albania to strengthen its electricity market. Also, it is estimated that only 35 % of hydropower potential in Albania has been developed and there is still place for further development.

Energy has an important role in development, mainly in developing countries like Albania. Electricity consumption is caused by economic growth, so it can be said that economic growth play a critical role in the development of renewable electricity in Albania.

Further, as economic growth depends on electricity consumption because energy consumption causes economic growth, so it is important to design different policies that can attract foreign and domestic investors to invest in renewable energy such as hydropower.

This study has found that there is a long-run relationship among electricity consumption and economic growth. Electricity consumption has a long-run positive effect on economic growth. But in short run they do not have short run correlation. Also, is three variables, (energy consumption, FDI and GDP) are taken together to see the co-integration between them it can be said that in group they are not co-integrated to each other. That is because factors that can affect FDI in a country are different such as political risk, high taxes, property issues etc.

Also, through the survey main difficulties that foreign investors face when they invest in Albania are tax rate, political risk, property issue, corruption etc. Improvement of the business climate and general conditions in Albania has a positive impact on the growth of direct foreign investments in Albania.

Also, it is known that foreign direct investments have positive effect on economic growth and electricity consumption is caused by economic growth, it can be said that foreign direct investments have an important impact on economic growth and electricity. This indicates that the government must do great efforts in this field, for further development.

In final conclusion, it can be said that Albania has an enormous opportunity for foreign investor on hydro power sector. Albania lacks some major requirements to facilitate foreign investor such as property issues, high taxes, infrastructure, corruption, informal competition, changes in legislation, political instability, but it can be said that progress is visible.

5.2 Recommendations

This study shows that Albania has huge potential on hydropower plants, but the foreign and private players in this sector are still low in numbers. The FDI in energy sector is improved by last one decade but the contribution of this sector to GDP is low.

This study has found that lot of steps taken by the government of Albania, such as strategic investments law, tourism reform, territorial and justice reform, in this way increasing the confidence of foreign investors for investment especially in energy sector. Recognizing FDI contribution to economy growth, all governments want to attract more FDI in their countries.

Therefore, Albania government needs to take important reforms in order to increase FDI inflows. The difficulties that foreign investors are facing include corruption, property issue, unfair competition, policy instability and financial package etc. Further, Albania needs to offer more competitive investment environment to attract more FDI flows into hydropower sector, meaning more competitive investment policies and laws. It can be said that there is still much work that needs to be done in order to create a favorable business environment for foreign investors that invest in Albania.

Based on the findings of the thesis, it can be said that the contribution of FDI to economy growth is estimated to be positive in Albania. Care should be taken when attracting FDI because each sector should analyzed in specific way to decide where foreign investment is needed most. In addition, knowing the impact of foreign investment for each sector would increase the knowledge about FDI and sectors that need more foreign direct investment. Further, FDI in the energy sector can has positive effect in the economy growth and society as whole. Also, investing in the Albanian electricity market contains on several risks such as exchange risk, interest rate risk, and so foreign investors should be able to manage these risks. If investors are able to do this, the opportunity to invest in the hydropower sector in Albania is highly recommendable.

However, compared with other developing countries, it can be said that Albanian hydro- power resources development is still low and utilization level of water is not very high. Therefore, the potential for development of Albania hydropower resources it can be enormous profitable. It can

say that developing hydro-power in the long-term is a strategic policy for Albania economy and social development, but also protecting the natural environment of Albania.

Moreover, studying the impact and role of foreign investment in Albania, especially on hydropower plants, can be very useful in making policies or other reform and laws to attract more FDI. This area is worth studying and is recommended for further research.

REFERENCES

- Abdullah Alam. (2013). Electric power consumption, foreign direct investment and economic growth. *World Journal of Science, Technology and Sustainable Development*, 10 (1) , pp. 55–65.
- Addison, T., & Heshmati, A. (2003). *The new global determinants of FDI flows to developing countries: The importance of ICT and democratization*. United Nations University, Helsinki: Discussion Paper No. 2003/45. World Institute for Development Economics Research.
- Albania Investment council. (27 April, 2016). Initiatives for Promotion of Investments: Albania and Western Balkans countries. *Meeting on Investment Council*. Tirana.
- Ali F., Fiess N., MACDonald R. (2011). CLIMBING TO THE TOP? FOREIGN DIRECT INVESTMENT AND PROPERTY RIGHTS. *Western Economic Association International, Issue Economic Inquiry*, pg.289-320.
- Bank of Albania . (2016). *Stock of FDI in Albania, Time Series Database of the Bank of Albania*. Retrieved from official page.
- Bank of Albania. (2014, March 31). *International Investment Position*. Retrieved from http://www.bankofalbania.org/web/Time_series_22_2.php?evn=agregate_detaje&evb=agreg
- Bank of Albania. (2016). *Flow of foreign direct investments in Albania - by country*. Retrieved from www.bankofalbania.org
- Bank of Albania. (2016). *Flow of foreign direct investments in Albania - by economic activity, Time Series Database of the Bank of Albania*. Retrieved from official page: www.bankofalbania.al
- Beugelsdijk S., Smeets R., Zwinkels, R. (2008). The impact of horizontal and vertical FDI on host's country economic growth. *International Business Review*, 17 (2008).
- Beugelsdijk, S., Smeets, R., & Zwinkels, R. (2005). The impact of horizontal and vertical FDI on host's country economic growth. *International Business Review*, 17(4), pp. 452-472.
- Bevan, A. A., & Estrin, S. (2004). The determinants of foreign direct investment into European transition economies. *Journal of Comparative Economics*, 32(4), pp. 775-787.

- Blonigen, B. A. (2005). A Review of the Empirical Literature on FDI Determinants. *Atlantic Economic Journal*, 33(4), pp. 383-403.
- Bobrowicz, W. (2006). *Small Hydro Power – Investor Guide*. *Koncern Energetyczny SA*. Retrieved 11 November, 2010. Retrieved from http://www.leonardoenergy.org/webfm_send/467
- Brevan, A. and Estrin, S. (2000). The determinants of foreign direct investment in transition economies.
- Bruno Ocaya, Charles Ruranga, and William Kaberuka. (2013.). Foreign Direct Investment and Economic Growth in Rwanda: A Time Series Analysis. *Online Journal of Business and Marketing Management*, Volume 2 Issue 1, Pages 11-18; .
- Cai, J. (2009, September). Hydropower in China.
- Chrysochoidis G., Millar C. and Clegg J. . (1997). *Internationalisation Strategies*. *NewYork: MacMillan Press*, 3-17.
- E. Borenszteina, , J. De Gregoriob, J-W. Leec. (1998). How does foreign direct investment affect economic growth?1. *Journal of International Economics*, Pg.115–135.
- Eller, M., Haiss, P., Steiner, K. (2005). Foreign Direct Investment in the Financial Sector: The Engine of Growth for Central and Eastern Europe? EI Working Paper, vol. 69. Europainstitut, Vienna University of Economics and Business Administration.
- Estrin, S., & Uvalic, M. (2013). Foreign direct investment into transition economies: Are the Balkans different? . LEQS Paper No. 64, European Institute, LSE.
- Explained, E. S. (2016, February). *Energy from renewable sources, Electricity generation from renewable sources*. Retrieved from official website
- Farrell, R. (2008). *Japanese Investment in the World Economy: A Study of Strategic Themes in the Internationalisation of Japanese Industry*. Britain: Edward Elgar.
- Foreign Investor Association in Albania. (2015). *Business Environment, Survey 2015*. Retrieved from <http://fiaalbania.al/>
- Foreign Investor Association in Albania, FIAA. (2011). *Albanian FDI Report 2011*.
- Foreign Investor Association in Albania, FIAA. (2013). *Recommendations for improvement of the business climate in Albania, White Book* .

- Gonzalez, David; Kilinc, Aygün; Weidmann, Nicole. (n.d.). Renewable Energy, Hydropower in Norway. Norway, Seminar Paper 1/2011, ISSN 2191-4850 .
- H.A. Bekhet, N.S. Othman. (2011). Causality analysis among electricity consumption, consumer expenditure, gross domestic product (GDP) and foreign direct investment (FDI): Case study of Malaysia. *Journal of Economics and International Finance*, pp. 228–235.
- INSTAT. (2016). *Production and consumption of primary energy*. Retrieved from www.instat.gov.al
- INSTAT. (2016). *Energy. Overall Energy Balance*. Retrieved from www.instat.gov.al
- International Energy Agency. (2010, November 19). *Renewable Energy Essentials: Hydropower*. Retrieved from www.iea.org/papers/2010/Hydropower_Essentials.pdf
- Invest-in-Albania.org. (2014, June 1). *Invest in Albania*. Retrieved from <http://invest-in-albania.org/energypower-generation/>, Energy/power generation
- J. De Gregorio, J. W. Lee. and Borensztein, E. (1998). "How Does Foreign Direct Investment Affect Economic Growth?". *Journal of International Economics*, v45, 115-135.
- Juliussen, E. (2007). *Small hydro – Possibilities and experiences for remote communities*. Retrieved from Norwegian Water Resources and Energy Directorate: [http://www.nordicenergy.net/_upl/small_hydro_in_remote_areasshetland,_erik_juliusen_\(norwegian_wa](http://www.nordicenergy.net/_upl/small_hydro_in_remote_areasshetland,_erik_juliusen_(norwegian_wa)
- Karki, B. (2013). Opportunities for finish firms in Nepal’s Energy sector, Research on Hydropower.
- Kaygusuz, K. (2004). The Role of Renewables in Future Energy Directions of Turkey. *Energy Sources*, 26, 1131–1140.
- Kevin P.Gallagher and Lyuba Zarsky. (2006). Rethinking Foreign Investment for Development. *Post-autistic economics review*.
- L Alfaro, A Chanda, S Kalemli-Ozcan, S Sayek. (2010). Does foreign direct investment promote growth? Exploring the role of financial markets on linkages. *Journal of Development Economics*.
- L. Alfaro, A. Chanda, S.K. Ozcan, S. Sayek. (2004). FDI and economic growth: The role of local financial markets. *Journal of International Economics*, 64 (1), pp. 89–112.
- Llameli, J. (2011). Foreign Direct Investment in Nepal Patterns and its future prospects.

- M. Shahbaz, N. Loganathan, M. Zeshan, K. Zaman. (2015). Does renewable energy consumption add in economic growth?. An application of auto-regressive distributed lag model in Pakistan. *Renewable and Sustainable Energy Reviews*, pp. 576–585.
- Magnus Blomstrom, Robert E. Lipsey, Mario Zejan. (1992). What Explains Developing Country Growth?
- Mallampally, P., & Sauvart, K. P. (1999). Foreign Direct Investment in Developing Countries. *Finance & Development, A quarterly magazine of the IMF*, 36(1).
- Mencinger, J. (2003). Does foreign direct investment always enhance economic growth? *Kyklos*, 56(4), 491-508.
- Mencinger, J. (2003). Does Foreign Direct Investment Always Enhance Economic Growth? *Kyklos, Volume 56, Issue 4*, pages 491–508.
- Miao Wang and M. C. Sunny Wong. (2009). FOREIGN DIRECT INVESTMENT AND ECONOMIC GROWTH: THE GROWTH ACCOUNTING PERSPECTIVE. *Western Economic Association International, Volume 47, Issue 4*, pg. 701-710.
- Ministry of Economic Development, Trade and Entrepreneurship. (2015). *ALBANIA CALLS, publication 2015*. Official Page, www.mete.org.
- Mottaleb, K. (2007). *Determinants of Foreign Direct Investment and Its Impact on Economic Growth in Developing Countries*. Retrieved from <https://mpira.ub.uni-muenchen.de/9457/>
- Moura, R., & Forte, R. (2009). The Effects of Foreign Direct Investment on the Host Country Economic Growth- Theory and Empirical Evidence. FEP Working Papers, No. 390.
- National Agency of Natural Resources (AKBN). (2014). *Hydro-energetic Potential*. Retrieved from www.akbn.gov.al
- Neupane, A. (2013). FDI and Hydropower projects in Nepal. Nepal.
- OECD. (2002). *Foreign Direct Investment for Development; MAXIMISING BENEFITS, MINIMISING COSTS*. France: OECD Publications Service.
- Organisation for Economic Co-operation and Development . (2009). Definition of Foreign Direct Investment 2008. *OECD Publishing*.
- Organisation for Economic Co-operation and Development. (2002). Foreign direct investment for development: Maximising benefits, minimising costs. *Paris: OECD*.

- Overseas Development Institute. (1997). FOREIGN DIRECT INVESTMENT FLOWS TO LOW-INCOME. *ISSN 0140-8682*.
- Pao, H-T. & Fu, H-C. . (2013). The Causal Relationship Between Energy Resources and Economic Growth in Brazil. *Energy Policy*. Vol. 61, pp. 793-801.
- Philipp Harms, Pierre-Guillaume Méon. (2013). *Good and bad FDI: The growth effects of greenfield investment and mergers and acquisitions in developing countries*. Retrieved from <http://www.etsg.org/ETSG2012/Programme/Papers/204.pdf>
- R. Sari, B.T. Ewing, U. Soytaş. (2008). The relationship between disaggregate energy consumption and industrial production in the United States: An ARDL approach. *Energy Economics*, pp. 2302–2313.
- Rahman, K. M. (2008). “*Globalization and the Climate of Foreign Direct Investment: A Case for Bangladesh*”.
- Shrestha, Ratna Sansar. (2007). *Investment in Hydropower Sector: Opportunities and Risks*. Retrieved from www.nepjol.info/index.php/HN/article/download/891/978
- Tatoglu, E. (2002). Locational Determinants of Foreign Direct Investment in an Emerging Market Economy: Evidence from Turkey’. *Multinational Business Review; 10, 1; ABI/INFORM Globa*, pg.21.
- The Extractive Industries Transparency Initiative in Albania, EITI. (2014). *Annual report for 2014*. Retrieved from <http://www.albeiti.org/en/>.
- The Global Issue Blog. (2007). *Advantages and Disadvantages of Foreign Direct, Renewables in Global Energy Supply*. Retrieved from International Energy Agency
- The World Bank. (2015). *World Bank Report 2015*. World Bank Publications.
- The World Bank. (2016). *Doing Business in Albania*. Annual Report for 2015.
- The World Bank. (2016). *Foreign direct investment, net inflows (% of GDP)*. Retrieved from <http://data.worldbank.org/indicator/BX.KLT.DINV.WD.GD.ZS/countries?display=graph>
- United Nation Conference on Trade and Development, UNCTAD. (20 JANUARY 2016). *Global Investment Trends Monitor*. Report No.22 .
- United Nations. (2014). *INVESTING IN THE SDGS: AN ACTION PLAN*. World Investment Raport for 2014.

- United Nations. (2015). *Reforming International Investment Governance*. World Investment Report for 2015.
- United Nations Conference on Trade and Development. (1998). *World Investment Report 1998, Trends and Determinants*. New York and Geneva: United Nations.
- United Nations Conference on Trade and Development. (2013). Global value chains: Investment and trade for development. *United Nations World Investment report 2013, Geneva: United Nations*.
- Vesaite, R. (2014). FDI from European Union to Western Balkan Countries: is the economic development being intensified in the region? Universitat Autònoma de Barcelona.
- Walsh, J. P., & Jiangyan, Y. (2010). Determinants of foreign direct investment: A sectorial and institutional approach (10/187). Washington, D.C.: International Monetary Fund.

Appendixes

✓ Survey

There were interviewed through structured and semi-structured interviews 72 domestic and foreign investors in the field of hydropower. As mentioned above part of this focus group besides foreign investors were domestic investors too, because the main goal is to see if domestic and foreign investors face the same difficulties or challenges in hydropower sector in Albania. A copy of the questionnaire used in the survey is presented in this section.

- *Questionnaire 1 aims to collect data and opinions for the study, specifically for monitoring the situation of domestic investment in hydropower sector in Albania.*

Questionnaire 1

The information provided in this questionnaire is completely confidential.

1. How do you rate you opportunity in hydropower sector in Albania?

- Not attractive
- Little attractive
- Attractive
- Very attractive

2. Reasons for investing in the energy sector:

- Geographical position
- Low cost of labor force
- Natural resources
- Weak domestic competition

3. Obstacles you've encountered in your business:

- Infrastructure
- Property issue
- Corruption

- Unfair competition
- High taxes
- Political Risk

4. Mitigating factors that have affected your business:

- Equal and fair treatment
- Not having participation border
- Other reasons

5. Your products are sold:

- In Albania
- Abroad

6. The number of employees in your business:

- 300- 800
- 800-5000
- 5000-10000
- Above 10000

7. How do you consider your investment in this area?

- Very successful
- Successful
- Low successful
- Not successful

8. What do you think about the future?

- To continue this type of activity
- To invest in other activity

9. Which are the reasons for judgment of the above?

10. How do you judge the need of the Albanian economy for the concession contract?

- Emergency
- High
- Not high

- Low

11. What do you think the government should do to attract more foreign investment in energy sector?

- *Questionnaire 2 aims to collect data and opinions for the study, specifically for monitoring the situation of foreign investment in hydropower sector in Albania.*

Questionnaire 2

The information provided in this questionnaire is completely confidential.

1. Form of ownership:

- Joint venture capital
- Foreign capital

2. Reasons for investing in the energy sector:

- Geographical position
- Low cost of labor force
- Natural resources
- Weak domestic competition

3. Obstacles you've encountered in business:

- Infrastructure
- Property issue
- Corruption
- Unfair competition
- The level of tax
- Political Risk

4. Mitigating factors that have affected your business:

- Equal and fair treatment
- Not having participation border
- Agreement on avoidance of double taxation

5. Your products are sold:

- In Albania
- Abroad

6. The number of employees in your business:

- 300- 800
- 800-5000
- 5000-10000
- Above 10000

7. How do you consider your investment in this area?

- Very successful
- Successful
- Low successful
- Not successful

8. What do you think about the future?

- To continue this type of activity
- To invest in other activity

9. Which are the reasons for judgment of the above?

10. How do you judge the need of the Albanian economy for the concession contract?

- Emergency
- High
- Not high
- Low

11. What do you think the government should do to attract more foreign investment in energy sector?

✓ **Econometric model**

Data from 2005 to 2014 for foreign direct investment (net inflows) and real GDP per capita and were obtained from the World Bank, while that of net consumption of total renewable electricity were obtained from Energy Regulator Authority, annual reports from 2005 to 2014.

Year	GDP per capita (current US\$)	Foreign direct investment, net inflows (BoP, current US\$)	Net consumption of total renewable electricity Kilowatt
1985	662.9	0	2,575
1986	719.2	0	2,949
1987	699.4	0	3,072
1988	676.6	0	3,304
1989	723.4	0	3,475
1990	639.5	0	3,377
1991	348.7	0	2,910
1992	218.5	20,000,000	2,790
1993	380.5	58,000,000	3,316
1994	619.1	53,000,000	3,719
1995	760.6	70,000,000	4,317
1996	1,046.40	90,100,000	4,872
1997	749.6	47,500,000	5,054
1998	865.3	45,010,000	5,067
1999	1,098.40	41,200,000	5,742
2000	1,175.80	143,000,000	5,739
2001	1,327.00	207,300,000	5,431
2002	1,453.60	135,000,000	5,430
2003	1,890.70	178,036,401	5,900
2004	2,416.60	341,285,113	5,945
2005	2,709.10	262,479,013	5,933
2006	3,005.00	325,138,317	6,121

2007	3,603.00	652,275,604	5,767
2008	4,370.50	1,240,972,849	6,260
2009	4,114.10	1,343,091,150	6,592
2010	4,094.40	1,089,416,366	6,924
2011	4,437.80	1,049,425,306	7,342
2012	4,247.50	920,080,650	7,617
2013	4,411.30	1,253,783,309	7,958
2014	4,564.40	1,149,384,241	7,793

Data from 1985 to 1991 for FDI are zero, because before 1991 there were no foreign direct investments in Albania. Main reason for this is that before 1991 Albania was a communist country with a closed economy.