Informality effects in the economy of Albania in light of world’s economic crisis

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Abstract. Recently, academicians and economists have expressed a great interest about the informal economy of Albania. This is mainly due to the size of informal economy in absolute and relative terms and to the emphasis economists have placed on the increasing evidence that the size of informal economy, calculated as a percentage of GDP has increased, and grown over the past two decades in many countries of the world. In light of the international economic crisis that was evidenced in 2008, the article will discuss problems of informality in economy as a condition for decreasing the dimensions of impact of the recent economic crises. Informality was and continues to be a concern to the economic circles regarding the theoretical definition, measuring its size and ways to reduce its dimensions. Informality in Albania, according to CIA World Factbook, may be as large as 50 per cent of the official GDP during 2007, 2008, 2009, 2010, and 2011. The aim of this paper focuses in the reduction of informal economy as an anti-crisis factor.

Keywords: informality, non-official economy, economic crises, farms

JEL Codes: E26, Q13

1. Introduction

In the beginning of the 21st century the economies of many countries were impacted by the economic crises and given the length and size of the crisis it turned into a global crisis. Under these conditions, this calls for a larger number of researcher papers, including scientific and public debate, which aims to take into consideration the factors that lead to it, including ways out of it and the tools to reduce its consequences in the economic and social life of various countries. Therefore it is clear that different countries have used different courses and specific ways in reducing the consequences of the global crisis.

2. Materials and methodology

Various theoretical studies of renowned researchers of the field, including Cohen, B., Kindleberger, Ch. P., etc, as well as the experience of Albania in light of the current crisis can be used as an important reference point. This study uses several official data gathered through various means, including made available public data. The objective of this paper is to highlight the informal sector in the Albanian economy and the possibilities of reducing it as an anti-crisis factor.

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3. **Research results**

The global financial crisis, though in effect for a while, started to show tangible effects in the midst of 2007 and into 2008, the aftermath of Wall Street in 2008, constitutes a financial phenomena that the world faced during the previous period as well. In the recent four hundred years of world development economics counts hundreds of crisis, of different size and scope, most prominent the one after WWII, the great depression, the collapse of international markets, etc. Given that these crises are of different sizes, the financial blow and the aftermath make them an important subject of research.

Some common denominators of crises include: an increase of money available in the markets, known as the development before the collapse stage, which brings about economic development of the countries; the crisis starts after a trigger of the economic-financial phenomena, and then it is spread publically; as well as despite circumstances the crisis is related to economic decline. Human Minsky, a theoretician, studied and reported about an uncommon increase and decrease of the bonds markets.

Albania emerged as a market economy after the collapse of communism, as early as 1991. During these years the country’s economy has undergone rapid development. However, an economic crisis and consequences it brings about constitute a preoccupying problem. The recent economic crisis disaggregates countries in two categories, those affected by the crisis and those suffering its consequences. Albania could be bundled with the second group. The fact that Albania is a country that has not been directly affected by the crises is evident, however it has been impacted by its consequences.

The non-inclusion of the Albanian economy in the swirl of the global economic crisis should be found in the economic policies and practices that have been implemented in the country. The fact is that during the pre-crisis period economic ‘blooming’ credit expanded which directly expanded the money supply. Also it expanded debt, purchase in instalments, etc. Albania has been characterized as undertaking of careful crediting policies, which constitutes an important fact in support of economy from the global economic crises. It is important to note that the agriculture sector plays an important role in the Albanian economy, as it provides almost 25 percent of its Gross Domestic Product and given that half of the country’s population lives in rural areas. Recent data indicate that rural population in Albania carries on activities in 368,997 agricultural economic units, also known as farms. The area of these units ranges between 0.52 to 1.13 hectares. Despite farms being small, the agricultural sector plays an important role in the economy of the country. Due to the limited developments of these sites, they are considered as survival economies. According to Schneider and Enste (2000) this type of economic activity is considered as first level of informal businesses. Back in 1990 and onward farms have been charged neither for their economic activity, nor the land they own. Measuring informality in this sector would be difficult, as the government itself has allowed for circumventing obligations so that inhabitants would be able to fulfil their survival needs. However, figuring the informality level of the sectors remains of theoretic and practical importance to the country. Presently about 320 farmers have paid their duties and taxes.

The agricultural economy units (farms) are relatively small and as such most of them are survival or self consumer economies. Schneider and Einste have characterized the informal economy classification (2003) according to the following:

a) **Official Economy**
Most of the farms in the country are included under the ‘self-sufficient economy’ structure, and these compose fragile economic units. The state aims to improve the economy and to increase the well-being of the people living by and supplied by it, thus it circumvents their economic obligations.

Schneider and Einste (2003) also studied the connection between taxes and economy size, by using a modified form of the Laffer’s curve to show the relationship between tax rate and the size of the various economic sectors, such as public sector, official sector, and informal sector. When taxes are introduced there seems to be a positive incentive to move out of the informal economy into the formal economy, because the benefits that result from the public sector outweigh the costs, and this process reaches an optimal level. Looking into the future, any rise in taxes results in negative incentives to work in the formal economy, and this poses the risk of units going back to the informal economy.

According to CIA Factbook informal economy during 2007, 2008, 2009, 2010, and 2011 informal economy in Albania is calculated to approximately 50% of the official GDP. Due to the high level of informality and the fact that the country develops its economic relationships mainly with Greece and Italy, whose informal sector reaches 20 percent, this also influences the high level of informality in Albania.

When focusing on the informal sector, another factor that supports it, is an increase in regulations. Lawmakers and enforcers should pay great importance to enforcement and regulations, rather than simply increasing the number of regulations. In practice it seems that as laws and regulations increase in number, informal economy increases in response to this.

Those operating in the informal economy are of the opinion that there are benefits for operating in this sector, not being mindful that the informal economy has its costs. Some of the penalties for operating in the informal economy include not making use of or taking advantage of the services provided by the government.
to formal economies. And the pivotal service is access to the legal system, which means ensuring property rights and trade law. Businesses operating illegally might not receive any legal support or lack documents, as they operate in an environment of uncertainty. Therefore, this would increase the cost of capital, which means lower level of investments.

4. Conclusions

As displayed thus far in the paper, the presence of informal economy, while considering the macro and economic costs it entails for the country, reducing the size of the informal sector becomes of utmost importance. Several ways could be followed to reduce the size of the informal sector in Albania, and the working group of this paper proposes the following:

There are several factors that incentivize the development of an informal economy in Albania, to name widespread corruption, legal and sublegal framework at times arbitrary and inconsistent, bureaucracies within the administration, higher level of taxes, lack of information on how economies can be formalized, including other factors related to the economic structure such as the existence of a family-economy, which makes up for ninety percent of small businesses in Albania.

Several methods can be used to calculate the size of the informal economy in Albania. When macroeconomic data are available, a suitable method could be the indirect approach. Economists presently use five indirect measures to track informal economy, including the discrepancy approach used to compare discrepancies in statistics about national expenditures as compared to income statistics; surveys which when used can help calculate participation of the active labour force in the informal economy, this is also known as official and actual labour force indicator, the method of currency demand, the method of transactions, and method of calculating consumed electricity.

Measuring the informal economy through estimated participation of an active labour force in the formal economy, according to the working group a decline of the active labour force in the official economy could be seen as an indicator of its participation in the informal economy. Over the years, if this number remains constant, a decrease in the rate of official participation can be seen as an indicator of increased activity in informal economy. In this calculation the weaknesses remain the fact that individuals can be employed both in the formal and in the informal sector. Therefore, we might not be able to draw an accurate size of the informal economy. To quote the example of Albania, the current country’s employed active labour force is estimated to be 10 percent.

If for estimating the size of informal economy, we were to use the transaction method, it states that there is a constant relation between transactions and total monetary unregistered income. However in order to receive reliable estimates, accurate figures are needed. Albania lacks these data, and there is no base year during the transaction period where there was no informal economy. Therefore variables which need to be calculated are influenced by the informal economy. We would be unable to accurately calculate its size, given the country lack these data.

During the transition years, it is noteworthy that the demographic map of Albania has changed a lot due to inner migration. This has helped the creation of approximately 800 informal zones, where some 150,000 illegal settlements were established, and whose cost is calculated to range $3 to $4 billion. As long as these settlements are not legalized, this capital will remain “dead” capital, as it cannot be put to use.

In Albania, informal economy is displayed in various forms, including:

- Rural families conducted economic activity;
• Businesses considered as micro or family businesses, are generally temporary and always almost unofficial;
• SMEs (small, medium) and large enterprises which operate in different informal levels and forms;
• Certain criminal and illegal activities, including money-laundering, smuggling, are covered as legal businesses;
• Some informality elements can be noted in companies of foreign capital, irrespective of their size;
• Generally, informal activities in the country either generate small revenues or larger profits.

Most prominent forms of informal economy include non-adherence to the fiscal legislation and fiscal evasion. Businesses that have not registered with tax authorities, or that avoid some fiscal obligations, are those businesses where fiscal informality is most prominently encountered. It has been reported officially that some fifteen percent of taxes are not paid, however reality in the country shows that some thirty percent of taxes are not paid, and that at least one third of businesses operate as unregistered.

Informality touches several aspects of the society, including the effects it brings over the social development of the country. Education and health sectors are reportedly touched by this phenomenon as well.

Fighting informality remains a daunting task, and designing some policies that fight informality could bring positive changes in the registration and administration of taxes, administration of customs, increasing the social insurance contribution scheme, as well as drafting support policies on the organization of cooperative farms.

5. References
[2] Data from Ministry of Agriculture Food and Consumer Protection and General Tax Directorate