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PUBLIC INVESTMENT MANAGEMENT IN ALBANIA - THE EFFECTIVENESS ACCORDING TO KEYNESIAN MULTIPLIER

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Abstract

Since the change of the economic system in Albania and the beginning of the transition in 1992, the key word for the rise and development of the devastated Albanian economy has been investments. Under the conditions of a non-existent private sector and an ineffective public sector, the only option was the attraction of foreign investments. Up to 2002, the Albanian Government failed to finance its current public spending with its revenues. Until this year, part of the public debt went to finance current spending and only one part for financing public investment. After this year, public investments had a quantitative change, and the focus changed from the funds finding to the quality of public investment management. While the level of public investment management has often been subject to political debate, it has almost never been the subject of a dispute about its economic impact. Mostly, debates about the social strata and areas that affected investment by shadowing its impact on the economy as a whole. From most than 10 years, the Albanian economy is failing to grow at high rates, because of low levels of public investment. Restriction of investment in infrastructure and change in the process of nature of investment has maintained the level of GDP growth in the range of 1-2.5%. In this paper will be explore the impact that has in the economy the level of public investment and the quality of their management. Given that public investment produces incentive for private consumption and investment, it will be analyzed how much the additional public sector investment will influence on economic growth.

Keywords: Investment, management, financing, multiplier, public debt, GDP

INTRODUCTION

Public investment and economic development

Gittinger (1992) defines the project as a *specific activity*, with a *specific goal* and end to meet *specific objectives*. The investment project, as part of a public expenditure program, is a set of acti*vities designed to deliver certain outputs within a timeframe*.

Public investment refers to capital expenditure in physical infrastructure (e.g. roads, water supply, educational and health facilities, government buildings, etc.) and "soft infrastructure" (human capital development, innovation support, research and development costs, etc.) with a lifespan of over 1 year. Public investments include both direct investment and indirect investment (OECD, 2012).*Direct* investments are defined as the formation of gross capital and purchases, stripping off the sales of non-produced non-financial assets over a given period. *Indirect* investment is defined as capital transfers e.g. largely for investments and subsidies in cash or in kind (OECD 2015).

Also, public investment can be defined as expenditures that are made by state structures in order to meet the broad public interest and collective needs. Public investment *can also play an important role in the process of redistributing wealth and income*. As a conclusion, we can say that public investments should be characterized by the following elements:

- *Economization*: investments must be realized with the lowest possible means and achieve the highest effect.
- *General Interest*: Public investment must have at their target the exhaustion of the needs of all members of the society and not just a part of it or of an individual. Here is one of the fundamental changes between public investment and private investment.
- *Public investment productivity*: Public investment is needed to have a direct or indirect impact on the level of national income and budget revenues. Public investment directly affects productivity growth in cases where investments are intended for physical facilities and in cases where public investment is intended for "soft investment" (health, science, education, etc.) they have an indirect impact.
- *Meeting the needs according to proportionality and accessibility*: Public investments should be implemented according to needs starting from those that are most urgent. Also, their fundings should be carried out according to budgetary space and possibilities, without prejudice to the balance of fiscal indicators.
- *Legal support for the realization of public investment*: public investments, at all stages, should follow and respect legal rules so that no income is spent arbitrarily without having a legal support.

LINK BETWEEN PUBLIC INVESTMENT AND ECONOMIC PERFORMANCE – LITERATURE REVIEW

It is a general consensus that is already the fact that the level of public investment in a developing country, especially infrastructure investment, has a primary role in economic development and prosperity. This role is based on incentives that public investments have on economic growth, as in the developing countries both benefits coming from public investment in the future are considerably larger and by others side fill that gap that was created precisely from being in an inefficient economy (Dabla-Norris, Brumby, Kyobe, Mills, Papageorgiou, 2010).

Among the first economists who articulated the importance of public investment was Adam Smith, who has dealt with the idea that the government should finance public investment in infrastructure and institutional assets in order to support production and trade exchanges. In his publication, "The Wealth of Nations," Smith states that:"*Governance has three main tasks, tasks that are of the utmost importance: the first task is to protect the society from violence or occupation by other countries, the second task is to protect each individual of the society from the injustices that can be committed by the members of the society, by establishing and respecting the maximum levels of the legal state. And the third concerns the provision and maintenance of public works, which are not merely the individual interests of the members of the society, or a small group of public works that cannot be carried out or benefit only a small part of society, but a whole society* "

In the following, Smith thinks that the implementation of public investment by the government, especially infrastructure investments, would be facilitated and would be support and development of markets and sustainable long-term economic growth. Also, given that the private sector would not be able or interested in conducting public investment, due to the high costs needed to implement them, there is still a growing need to get the power from Government itself for these investments, without which would be significantly affected economic growth.

Keynes (1936) argues that public investment during Great Depression was an instrument in government's hand to stimulate aggregate demand by catalyzing income and employment multipliers in order to increase it. Since then, governments have justified financing public investment projects, such as providing a corrective response, in order to increase the growth of private sector development and long-term growth.

Also, Aschauer (1989) states that the stock of public investment (roads, railways, airports, etc.) was of particular importance to the level of productivity of the US economy, and concluded that the decline in productivity in the 1970s and 1980s could be attributed Low level of public investment.

Further studies (Glomm and Ravikumar, 1997) show that the impact of infrastructure investments was somewhat lower than those set by Aschauer (1989), they still have a direct impact on the level of productivity and economic growth. Rodrigue (2009) said that for every dollar invested in the road network in America in the period 19454 - 2001, it contributed to a productivity increase of $ 6.

Over the past few years, under the negative effects caused by the global crisis (beginning in 2007), many countries have been forced to show a lot of prudence and cut their spending. This has attracted even more attention to the governments of the various countries that, in the conditions of uncertainty and insecurity of economic performance and the tightening budgetary reforms undertaken, are even more focused on better management of projects of public investment, in order to make the return on investment as high as possible and their impact on the economy to be as sensitive. Already in many countries, one of the policy focus pursued by governments is precisely the very high attention to maximizing public investment efficiency by performing a better selection process and project management that will be implemented.

Infrastructure investments do not only affect the growth of the production of physical and human capital, but indirectly also affects the reduction of transport costs, enabling, among other things, for a subject to increase its profits (Straub, 2008).

Calderon and Serven (2008) argue that in developing countries, lack of infrastructure development, especially in the streets, telecommunications and energy, significantly reduces productivity. It is thought that this reduction is considered as much as the reductions caused by other structural factors such as corruption, excessive administrative bureaucracies or lack of funding.

Keefer and Knack (2015), concluded that spending on implementation of public investment projects in developing countries has little impact on the country's economic development as a result of high levels of abuse and corruption.

Studies have shown that emerging economies that conceive and implement projects in their country's infrastructure, halving the deficit of the previous state and reaching the level of medium-income infrastructure, then the economy will be positively affected and the annual real growth rate of gross domestic product will rise by 2 percent (Calderon and Serven, 2008).

In developing countries, the impact of public investment on economic performance is affected by the low efficiency of these investments. Appropriate investment positively contributes to long-term positive growth, increasing the return on a number of factors of production (Barro, 2009).

The importance of public investment, especially in infrastructure, is quite high. Many studies and economic facts have shown that an improvement and / or extension of the road infrastructure network has created the necessary space for greater economic growth and development, especially in the various rural areas, where it can be said that the reduction of transport costs is verified on the costs of consumption and production of goods and services, the increase of farm production through the encouragement of greater access and use of modern inputs, improved access to markets and the reduction of agricultural input prices. Also, the improvement and expansion of the road network provides important links to national, regional and international markets. Investing in rural roads improves access to and access to public and social services such as schools and hospitals (Khandker, Bakht, & Koolwal, 2009).

Over the last two decades, there has been a noticeable shift from donors or governments themselves to focus and fund largely the major infrastructure projects, thus increasing the focus on local investment. According to Deichmann (2008) this may have been caused because large investments bring about changes in the improvement of the industrial sector or specific areas, it is difficult for these benefits to be felt even in local areas if there is a lack of infrastructure development Local roads.

THE KEYNESIAN MULTIPLIER

The Keynesian multiplier was introduced by Richard Kahn in 1930. It shows that any government spending incurs a successive cycle of spending. This increase of expenditures in the economy, regardless of their form, directly affects the growth of employment and prosperity in the economy. For example, the investment projects of the Albanian Government through public investments realized by themselves or by the concessionaires will have to increase the cash flows thrown into the economy. This will be distributed as labor costs, purchase of materials, various expenses, taxes and taxes etc. This money thrown into the economy will increase as consumption thereby increasing the revenues of companies from sales of goods and services. At the same time, this money thrown into the economy will increase savings by simultaneously increasing funding sources for company investments. In both cases, both the increase in consumption and savings will increase funding for business investment by increasing their investment. In short, a government cash flow into public investment is expected to trigger an increase of private investment in a multiplied chain. This logic is the main argument for expectations for increased investment, employment, output and the economy as a whole driven by additional public investment flows.

If in a hypothetical situation we would assume that people would not spare, but all of the additional income would go for consumption then the economy would turn into an unstoppable engine that would aim for a full employment. According to Keynes, it would be beneficial to increase consumption by reducing savings by setting a savings tax in order to encourage people to consume more and more. The Keynes model arbitrarily divides private savings and investments into two distinct functions by showing savings as a depleted economy and private investment dependant on spending cuts.

One element that ignores the Keynesian multiplier is how public investment is funded. If the add-on to public investment is financed through increased taxes then we have to consider the fact that some of the money is withdrawn from the economy, causing a multiplier effect of falling spending and investment in the economy. Likewise, domestic debt financing has the same effect by increasing competition for private investment. Only the increase of external debt investment gives the full effect of the multiplier of investments because the funds come from outside the economy and do not affect the current level of investments and expenditures of economic operators in the country.

EFFECTIVENESS OF PUBLIC INVESTMENT IN ALBANIA - INVESTMENT MULTIPLIER

Public investments in Albania have been an important driving force for the Albanian economy during its recovery after 2000. Apart from the difficulties in finding the right projects and funding for their realization, one of the difficulties has been their effectiveness as projects in particular and their economic impact. Unnecessary involvement in public and political debates has often created an adequate ground for abuse and concealment of investment failures. Among the many parameters will be analyzed the two factors and the relationship they have and how they are affected by each other: GDP and public investment levels.

Initially, it will be analyzed the level of public investment funded partly with the additional public debt. According to records for the period 2005-2016 we have this data regarding the level of public investment.

Table 1: Public Investment in the Republic of Albania, 2005-2016

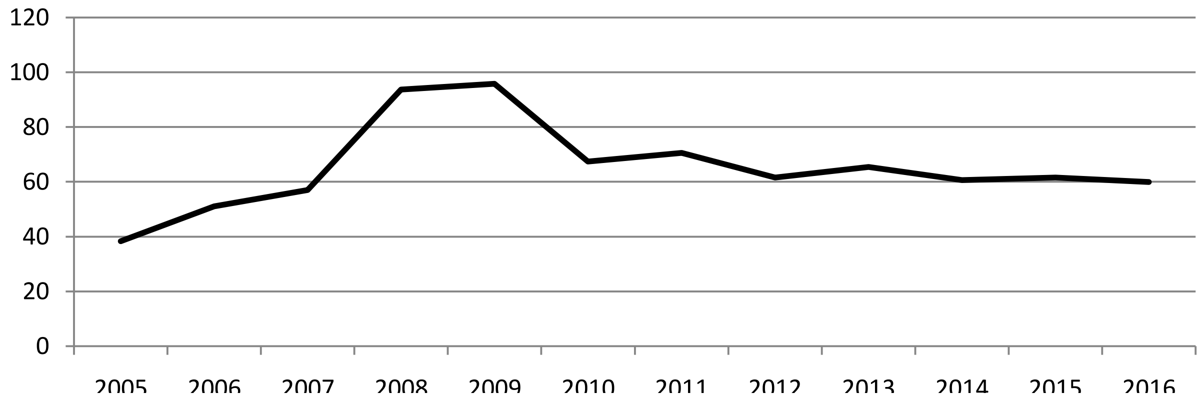
Years	**2005**	**2006**	**2007**	**2008**	**2009**	**2010**
Total Public Investment (in billion Lek)	38.375	51.108	57.040	93.783	95.881	67.492
Annual growth rate (in%)	0,28	33,18	11,61	64,42	2,24	-29,61
Years	**2011**	**2012**	**2013**	**2014**	**2015**	**2016***
Total Public Investment (in billion Lek)	70.679	61.655	65.477	60.749	61.622	59.988
Annual growth rate (in%)	4,72	-12,77	6,20	-7,22	1,44	-2,65

Source: Ministry of Finance

*Comments and Analysis: Open Data Albania   * Note: Values for 2016 are a plan*

Placed on a coordinate axle system, the data in the table above represent a level of public investment rising by 2009 and a steady decline after this year.

Figure 1: Performance of Public Investment in the Republic of Albania, 2005-2016



In fact, due to the impact of the economic crisis, the level of public investment should have been declining since 2007. But this has not happened because the Albanian Government has been engaged in high value investment projects in infrastructure where the largest project was the construction of the Durrës-Morinë highway project, which has continued with high investment levels until 2009. To illustrate, below we have a reflection of budget spending over the years of the national road network program.

Table 2: Budget Expenditures of the National Road Network Program (Million Lek)

Years	**2006**	**2007**	**2008**	**2009**	**2010**	**2011**	**2012**	**2013**	**2014**	**2015**	**2016***
Domestic Financing	19,342	28,582	27,390	54,350	26,254	19,552	8,849	20,708	21,842	9,214	5,753
Foreign Financing	17	2,823	34,075	7,486	6,758	11,145	17,126	12,224	5,129	11,271	15,650
Total	**19,359**	**31,405**	**61,465**	**61,836**	**33,012**	**30,697**	**25,975**	**32,932**	**26,971**	**20,485**	**21,403**

*Source: Ministry of Finance * The value 2016 is budgeted*

As noted, the best years in the financing of road infrastructure have been the first years of the financial crisis, 2008 - 2009, with a high rate of economic growth during this period.

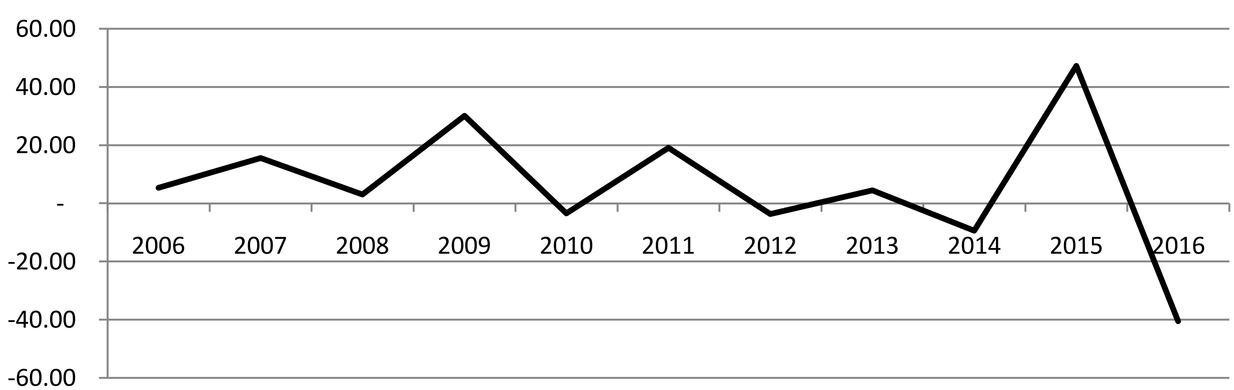
Of course, public investments carried out in large part in infrastructure investments have a direct impact on the country's economic growth. From the interlacing of data on economic growth and public investment for the period 2005-2016, the parameter of the *effectiveness of public investments* was issued. This parameter is calculated *as a ratio of GDP change with the* *change of public investment*. The goal is to calculate how much the GDP has been increased by the increase of 1 ALL of public investment. The data related to this parameter is presented in the table below.

Table 3: Effectiveness of Public Investment in to GDP 2005-2016 (billion ALL)

Viti	**2005**	**2006**	**2007**	**2008**	**2009**	**2010**
GDP	804,16	872,74	965,53	1.080,68	1.143,94	1.239,64
Change of GDP		68,57	92,79	115,15	63,26	95,71
Public investment (Domestic + Foreign Financing)	38,375	51,108	57,04	93,783	95,881	67,492
Change of public investment		12,733	5,932	36,743	2,098	-28,389
Effectiveness of public investment (Investment Multipliers)	20,96	17,08	16,93	11,52	11,93	18,37
Viti	**2011**	**2012**	**2013**	**2014**	**2015**	**2016**
GDP	1.300,62	1.332,81	1.350,05	1.394,42	1.435,75	1.501,89
Change of GDP	60,98	32,19	17,24	44,37	41,33	66,14
Public investment (Domestic + Foreign Financing)	70,679	61,655	65,477	60,749	61,622	59,988
Change of public investment	3,187	-9,024	3,822	-4,728	0,873	-1,634
Effectiveness of public investment (Investment Multipliers)	18,40	21,62	20,62	22,95	23,30	25,04

Cast in a coordinate axis system the data from the table above for the effectiveness of public investment, represent a line with almost sinusoidal fluctuations. This fluctuation has been due to the variation in public investment from one year to another.

Figure 2: Effectiveness of Public Investment in the Republic of Albania, 2006-2016



Throughout the 2009-2016 period, public investment has had a one year growth and a one-year decline, causing a positive year and a negative year by year change. This has also made the parameter of public investment efficiency the same fluctuation.

CONCLUSIONS

Based on the logic of Keynesian Public Investment Framework and the need for better management of not only investment but also public debt withdrawal plans intertwined with the quantitative data analysis for the Albanian economy over the period 2005-2016, we have reached some conclusions and recommendations. We think that these conclusions and recommendations can be useful if implemented in the form presented in this study but may also serve as a basis for further study of these phenomena. Below are the conclusions of the analysis of public investments, their type and their impact on GDP.

First, public investment in Albania has had a steady growth trend. It has been the economic-financial crisis of 2007-2008 *the most influential factor that has caused their repression*. This crisis has also affected private investment by bringing about a halt to economic growth.

Secondly, the *high level of public investment especially in the national road network has kept Albania's economic growth at high levels*. Although the economic crisis hit the neighboring countries and the Albanian economy, GDP continued to grow due to the incentives came from the high public investment in road construction and especially the construction project of the Durrës Morine road, which closed the financing with high rates precisely in 2009.

Third, after 2010, the decline and fluctuation of public investment *has been followed by a low GDP growth but relatively stable level*. This demonstrates *a weakening of the link between the level of public investment and GDP*. An influential factor in this regard may be the change in the nature of public investment. The decline in infrastructure investment may have been an influencing factor in reducing the impact of public investment on GDP.

Fourthly, the economic crisis has been a powerful factor in the economic growth rate in Albania especially after 2009. This crisis has impacted on curbing economic growth while simultaneously reducing the effectiveness of public investment. The impact of this regional crisis on the Albanian economy has come mainly through the reduction of remittances which have served as an important source of development for the Albanian economy.

RECOMMENDATIONS

Based on the above conclusions and those that can be accomplished to improve economic growth, are made two *recommendations* which are mainly addressed to the Albanian Government. These recommendations are a source of analysis and are feasible and believe necessary for the development stage and the prospect of a developing economy such as the Albanian economy.

First, the Albanian Government in harmony with the international financial institutions to which has contractual obligations, such as the IMF, need to un*dertake high-level public investment in those directions which have a multiplier impact on GDP*. As history has shown and economic theories suggest, the increase in public investment, especially in *construction and infrastructure*, has a strong impact on the growth of consumption and private investment, thus bringing the economy back to high growth rates.

Secondly, *it's an urgent need a short-term replacement plan for remittances*. Looking at the potential of the country's development, it is necessary to focus primarily on public investments and through incentives and private investments. The goal is *to find an alternative source of development that will replace remittances*. The financial crisis that hit the European Union countries damaged the Albanian economy through remittances. In fact, the crisis is not the only cause of their collapse. Even if the crisis did not happen it is expected that their level will fall. The crisis only proves how sensitive the Albanian economy is from the fluctuation of the level of remittances.

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