

PUBLIC FINANCE MANAGEMENT SYSTEMS IN ALBANIA: GAPS, REGIONAL COMPARISONS, AND REFORM PATHWAYS

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Abstract: *This paper evaluates Albania's public finance management (PFM) systems by examining governance frameworks, macroeconomic performance, and regional comparisons within the Western Balkans. The author has used the qualitative analysis of international governance standards, regulatory reports, and national economic data. The study highlights how principles of openness, integrity, and accountability—originally articulated in the Cadbury Report—have been adapted to the public sector through the CIPFA framework. Through the economic analysis the author has identified the key strengths, including improved fiscal balances, declining public debt ratios, and resilience to external shocks, while also revealing persistent gaps in budget execution, transparency, and public investment management. Comparative insights from neighboring countries underscore both shared regional challenges and Albania's relative progress. The paper concludes with strategic directions for strengthening PFM in Albania, emphasizing enhanced accountability mechanisms, more effective use of audits, and better alignment of fiscal policy with long-term development goals.*

Keywords: *Public sector governance, Accountability; Transparency; Integrity; Governance principles; CIPFA framework.*

1. INTRODUCTION

As more nations develop democratic, market-based economies, adopting standards based on generally accepted accounting principles (GAAP) is becoming increasingly important to the soundness of their financial systems. Sound accounting standards support efficient financial management and reporting systems that provide vital information to creditors and equity investors so that they can make profitable investments. Investors provide much need risk capital and are concerned with the risk inherent in, and return provided by, their investments. Investors and information that will help them determine if they should buy, hold, or sell an investment. Lenders, on other hand, are interested in information that permits them to determine whether their loans, and the interest attaching to them, will be paid when due. Corporate Governance Principles about the Cadbury Report set 3 foundational principles that companies listed in the stock exchange have to observe: openness, integrity and accountability. Openness of the companies, within the limits set by their competitive position, is the foundational element for the level of trust which needs to exist between the business and all those who have an interest in its success. Integrity – it means both direct practice and completeness. What is required of financial reporting is that it should be honest and that it should present a balanced picture of the state of the company's affairs. The integrity of reports depends on the integrity of those who prepare and present them. Accountability – The Boards of directors are accountable to their shareholders and both have to play their part in making that accountability effective. Boards of directors need to do so through the quality of the information which they provide to shareholders, and shareholders through their willingness to exercise their responsibilities as owners.

2. LITERATURE REVIEW

2.1. Matters of public and corporate governance

Governance is a broad term with different meanings and perceptions and is generally used in different disciplines such as political science, public administration, economics, and management (Almqvist *et al*, 2013). Corporate governance refers to the exercise of power over corporate entities (Tricker, 2012; Shleifer and Vishny, 1997), "mechanisms of steering and controlling" (Colley *et al.*, 2005), or "ways in which suppliers of finance assure themselves of getting a return on investment" (Shleifer and Vishny, 1997). Corporate governance refers to systems by which companies are directed and controlled (Tricker, 2012; European Commission, 2011, p. 2; International Federation of Accountants, 2001) and is therefore relevant for all organizational forms, such as SOEs, family business, cooperatives, and not-for-profit firms. In the public sector a debate around "governance" is related to new models and principles of steering that appear in the form of networks and hybrid organizations. Governance is not just about corporate management and marketization but also about the changing nature of government and seeks to understand such transformations (Kettl, 1993, 2000; Tricker, 1994; Rhodes, 2000). Thus, governance refers to all processes whether undertaken by a government, market, or network (Bevir, 2013), and deals with the steering and coordination of various actors, often in network-type patterns of collaboration (Rhodes, 1997).

2.2. Characteristics of the Corporate Governance of public entities in the UK

Considering the particularities of the public sector, respectively public entities not being listed in the stock exchange and not being owned by investors / shareholders, as well as the fact that they are not exclusively oriented towards profits, the characteristics of private companies' corporate governance do not entirely reflect within the corporate governance of public entities.

In the context of the critique brought to the Cadbury Code (which was criticized in the specialized literature because it referred solely to the private sector, and not to the public sector), starting from the three fundamental principles of corporate governance identified by the Cadbury Report, in July 1995, the Chartered Institute for Public Finance and Accounting (CIPFA) developed the first corporate governance framework for the public sector, containing a common set of principles and standards for management and control of public organizations. The corporate governance framework for the public sector, developed by the CIPFA approaches 3 key areas:

The first key area – *organizational processes and structures* – refers several aspects regarding:

(i) Responsibility towards the law; (ii) Responsibility for public money; (iii) Communication with stakeholders;

The second area of the corporate governance framework – *controls and financial reporting* – consists of the following components:

(i) Annual reporting; (ii) Internal controls; (iii) Audit committees; (iv) External audits.

The last area of the corporate governance framework – *behavioral standards of directors* – refers to:

(i) Leadership / management; (ii) Behavioral codes.

2.3. Recent developments and macroeconomic perspectives

The pace of economic growth over the last few years, until the earthquake strikes in November 2019 and the Covid-19 pandemic, has shown a positive development trend that has been reflected in a number of macroeconomic parameters in the country. So far, the country's main economic and financial fundamentals and overall macroeconomic stability have withstood these shocks relatively well. Even through the most recent external shock resulting from the war in Ukraine, it appears that so far our economy has adapted and performed relatively well.

During the first half of 2023, the Albanian economy continued to grow, showing a stabilization of economic activity. The Gross Domestic Product (GDP) for the first half of 2023 has increased by about 3.05% compared to the first half of 2022 according to the latest estimate available from INSTAT. This recovery relies on a wide range of factors and is present in almost all sectors of the economy. The increase in business confidence, especially in the services and construction sectors, as well as fiscal and monetary support policies, have brought an increase in household consumption, public and private

investments. Both the manufacturing and service sectors have benefited from these developments, providing recovery for business and employment. (INSTAT, Q1, 2023). According to the perspective of aggregate demand, in the first half of 2023, it is estimated that almost all components of aggregate demand have increased. Growth through the first half of 2023 was mainly generated by domestic demand, both private consumption and investment. Meanwhile, foreign demand is estimated to have had a negative contribution, as the high positive contribution from the increase in imports of goods and services was counterbalanced by the lower contribution from the increase in exports. In this context, total final consumption, which constitutes the largest share in the economy, for the first half of 2023 experienced an increase of 4.15%, while private consumption recorded an increase of 3.73% compared to the same period of the previous year. (Bank of Albania, 2023/II).

Total investments for the first half of 2023 recorded a stronger growth of 9.23%, compared to 6.53 percent in 2022. *Foreign trade* data suggest that exports and nominal imports of goods have contracted in annual terms. The decline is more pronounced in the case of exports and more moderate for imports. The drop in international prices remains the main factor behind the negative performance in both cases. While *exports* of goods suffered a decline in the second and third quarters, exports of services, especially those related to tourism, have registered growth rates for the same period, and will compensate for the decrease in exports of goods, making a contribution net positive in total exports in GDP growth. More specifically, exports of goods for the nine-month period 2023 recorded a decrease of -9.0% compared to the previous year. While the imports of goods for the nine-month period 2023 marked a decrease of -6.5% compared to the previous year. The trade deficit for the period January - September 2023 has improved by 3.6% compared to the same period a year ago. The coverage rate of exports to imports for this period is 51.3%.

On the aggregate supply side, positive contribution in the first half of 2023 was made by several branches, specifically: "Construction" with +0.93 percentage points, "Real estate activities" with +0.74 percentage points, "Public Administration, Education and Health " with +0.56 percentage points, "Arts, entertainment and recreation and other service activities" with 0.40 percentage points, "Trade, Transport, Accommodation and Food Service" with +0.31 percentage points", "Information and Communication" with +0.21 points percentage, "Financial and Insurance Activities" with +0.08 percentage points. The group: "Professional activities and administrative services" contributed negatively with -0.17 percentage points. (Instat, 2023) Also, the developments in the *labor market* so far have been positive. The latest data from INSTAT according to the Quarterly Labor Force Survey (LFS) in the second quarter of 2023, show that the official unemployment rate for the 15-64 age group is 11.1%, compared to 11.5% that was for the same quarter of a year ago. As for the working age group of 15 years and older, the official unemployment rate in the second quarter of 2023 was 10.7%. The number of unemployed persons of working age (15-64 years) in the second quarter of 2023 was 157,202 persons. In the second quarter of 2023, the number of employees of working age (15-64 years) was 1,255,840 people. Compared to the same quarter of the previous year (Q2-2022), the number of employed persons increased by 33,106 persons or +2.7%. (INSTAT , 2023).

The external position of the economy, another very important and typically vulnerable foundation in the face of such shocks, remained relatively solid, beyond the initial expectations for the impact that this foundation of the economy could have from the impact of the pandemic and the negative chain implications it could cause in other foundations. In 2022, the *balance of payments* closed with a slightly negative deficit, being calculated at around -0.4% of GDP. (Bank of Albania). Meanwhile, in the first half of 2023, the current account deficit stands at 324 million euros, narrowed in annual terms by about 121 million euros or 27% compared to the same period a year ago. Also, only for the second quarter of 2023, the current account deficit is 195 million euros, narrowed in annual terms by about 4 million euros (or 2%) against the background of the expansion of the trade surplus in services. The trade balance in services expanded significantly in the categories: travel services, transport services, construction, as well as in net income from services for the processing of physical inputs. (IMF, 2024).

In the first half of 2023, *revenues* from services generally related to Tourism increased by +37.4%, compared to the first half of 2022. Also for this period, Remittances also increased by +17.8%. These developments, together with the expansion of secondary income, positively influenced the performance of the current deficit, compensating for the deepening of the trade deficit in goods and the expansion of the negative balance of (primary) income from investments. (Bank of Albania). In the first half of 2023, *Foreign Direct Investments* recorded a value of +686 million euros or +7.2%, compared to +640 million euros in the first half of 2022. Also, only for the second quarter of 2023, FDI recorded a value of +379 million euros or +12.3%, compared to +337 million euros in the second quarter of 2022. This quarter, foreign exchange inflows in the form of foreign direct investments were mainly concentrated in real estate (to the extent of 20%), the sector of hydrocarbons (to the extent of 17%), financial intermediation (to the extent of 15%), and energy (to the extent of 9%).

The stock of *foreign exchange* reserves, at the end of June 2023, marked 5,548 million euros, enough to cover 7.3 months of average annual imports of goods and services. (Ministry of Finance and Economy, 2025). These developments in the external position of the economy and the relatively good performance of the economy as a whole have also been reflected in the other very important foundation of the exchange rate. Having a free exchange rate regime, the local currency (Leku) has remained quite stable against the main currencies (Euro, etc.) around the level of 120 Lek/Euro during the years 2019-2021, a period which coincides with the pandemic, and has significantly intensified this appreciation during the last two years with a faster strengthening trend, a period characterized by the rapid improvement of the current account deficit.

The sustainability of the financial sector, in terms of capitalization, liquidity and profitability, continues to remain another strong foundation of the economy. *Non-performing loans* (NPL) have continued to decrease, marking at the end of July the level of about 5.28% from the 8% they marked about two years ago. The total stock of bank loans in August 2023 had an increase of 1.9% compared to the same month of 2022. The stock of loans in Lek registered an increase of 8.4%, while that in foreign currency decreased by 5.0%, compared to one year before. Lending of the private sector of the economy has suffered a decrease for loans to businesses where at the end of August 2023, a decrease of 2% was recorded compared to a year ago, while loans to consumers continue to grow, where for the same period they recorded the increase of 9.0%.

Regarding *Deposits*, referring to the data so far, during the month of August 2023 the total stock of bank deposits increased by 1.7% compared to the same month of 2021. The total stock of deposits in Lek increased by 0.3%, while that in foreign currency increased by 2.8%. In August 2023, it turns out that about 42.1% of the total stock of deposits consists of deposits in Lek, while the rest of 57.9% consists of deposits in foreign currency. The total stock of deposits for the month of August 2023 only increased by 55 billion Lek compared to the previous month (July 2023). The total stock of business deposits in August 2023 increased by 17.2% compared to August 2022, while the total stock of individuals' deposits decreased by 2.6% compared to the same month a year ago. (BoA, 2023)

Inflation has reflected the recent external supply shock due to the war in Ukraine, becoming one of the main macroeconomic issues for our economy, as in many other countries around the world. However, the fact that inflation in our country has been significantly lower than in the countries of the region (at the 6.7% average annual rate for 2022), or than the average of the countries, is important and in favor of the developments and prospects of the economy. Of the European Union. Inflation in Albania recorded the highest value in October 2022, of 8.3%, mainly caused by food and transport costs. As for the latest data available, in September 2023 the annual change in the consumer price index is 4.1%, while a year ago this change was 8.1%. The average inflation for the nine months of 2023 is 5.1%. (IMF, 2024).

3. Countries of region

Based on reports and analyzes of international institutions, the performance of economic growth in the Western Balkans region was different among countries in the second quarter of 2023.

*PUBLIC FINANCE MANAGEMENT SYSTEMS IN ALBANIA: GAPS, REGIONAL COMPARISONS,
AND REFORM PATHWAYS*

In Serbia, Albania and Montenegro, higher rates of expansion were recorded than in the quarter the previous one, while in Kosovo, Bosnia-Herzegovina and North Macedonia, GDP growth slowed down. On average, the region's real GDP growth accelerated marginally to 2% on an annual basis from 1.9% in the first quarter. The unemployment rate fell compared to the previous quarter in some countries and in most of them it was the same or lower than in the same period a year ago.

The four-quarter moving average current account deficit in the region fell to 4% of GDP in June, the lowest level since the third quarter of 2021. This improvement was mainly driven by strong growth in services exports, higher remittance inflows and narrowing merchandise trade deficits helped by softening import prices.

Driven by the slowdown in energy and food prices, average annual consumer price inflation in the Western Balkan countries slowed further to 10.2% in the second quarter of 2023. The rate of inflation continued to decline through August in most economies, at levels ranging from 3.2% in Kosovo and 11.5% in Serbia. In countries with monetary autonomy, the pace of tightening slowed: in Albania, the base rate of monetary policy has remained unchanged since March and in Serbia since July. Continued economic expansion and high inflation supported the growth of budget revenues and fiscal balances have improved in almost all Western Balkan economies in the first eight months of 2023, with the exception of North Macedonia.

Economic growth was generally driven by private consumption and in some countries by the recovery of investments. However, consumer spending showed a mixed performance across the region; where they turned positive in Bosnia-Herzegovina and even accelerated in Kosovo and Albania, while they slowed down in North Macedonia and Montenegro and continued to fall in Serbia.

Table 1: Gross Domestic Product (annual growth in %, in real terms)

	2018	2019	2020	2021	2022	2023*
<i>Real economic growth, in %</i>						
Albania	4.0	2.1	-3.3	8.9	4.9	3.7
Bosnia and Herzegovina	4.6	2.3	-2.9	7.3	3.8	1.5
Chuang	3.4	4.8	-5.3	10.7	5.2	us
Macedonia	2.8	3.9	-4.7	4.5	0.9	2.0
Black Mountain	5.1	4.1	-15.3	13.0	6.4	3.0
Serbia	4.5	4.3	-0.9	7.5	2.3	1.9
The average of the region	4.1	3.6	-5.4	8.7	3.9	2.4

Source: European Commission (DG-ECFIN), MFE

The reduction in the current account deficit was particularly pronounced in North Macedonia and Serbia, which saw the biggest deterioration in its external balance when the energy crisis hit in 2022. Foreign direct investment inflows remained broadly stable in the four quarters to June and covered most or all of the current account deficit in some countries.

Table 2: Current Balance (% of GDP)

	2018	2019	2020	2021	2022	2023*
<i>Current account balance, (in % of GDP)</i>						
Albania	-6.8	-7.9	-8.7	-7.7	-6.0	-4.7
Bosnia and Herzegovina	-3.3	-2.6	-2.8	-1.8	-4.3	-3.8
Chuang	-7.6	-5.7	-7.0	-8.7	-10.5	us

Macedonia	0.2	-3.0	-2.9	-2.8	-6.2	-4.1
Black Mountain	-17.0	-14.3	-26.1	-9.2	-13.2	-10.3
Serbia	-4.8	-6.9	-4.1	-4.2	-6.9	-5.5
The average of the region	-6.6	-6.7	-8.6	-5.7	-7.9	us

Source: European Commission (DG-ECFIN), MFE

Trade dynamics were generally dampened by weak and often contracting exports of goods, which were however offset by a steady increase in services exports, particularly in countries dependent on tourism. Import growth was slow overall.

Table 3: Trade balance of goods (% of GDP)

	2018	2019	2020	2021	2022	2023*
<i>Trade balance (in % of GDP)</i>						
Albania	-22.4	-22.9	-22.4	-25.3	-23.8	-22.4
Bosnia and Herzegovina	-22.5	-22.3	-18.0	-18.3	-22.4	us
Chuang	-41.0	-40.3	-38.0	-44.8	-48.0	us
Macedonia	-16.2	-17.3	-16.6	-19.7	-27.0	-25.5
Black Mountain	-43.9	-41.7	-39.2	-38.7	-46.1	-45.3
Serbia	-11.9	-12.2	-11.1	-11.3	-15.5	-13.9
The average of the region	-26.3	-26.1	-24.2	-26.4	-30.5	us

Source: European Commission (DG-ECFIN), MFE

Average employment growth slowed to 0.9% on an annual basis in the Western Balkans in the second quarter of 2023, while labor force participation increased in some countries, notably in Albania where it climbed to a record high of 75.8%. Overall, unemployment rates in the region remained high compared to the EU, ranging from 9.6% in Serbia to 13.5% in Montenegro.

Table 4: Unemployment rate (in %)

	2018	2019	2020	2021	2022	2023*
Albania	12.8	12.0	12.2	12.0	11.3	10.7
Bosnia and Herzegovina	18.4	15.7	15.9	17.4	15.4	14.5
Chuang	29.6	25.7	25.9	20.7	12.6	us
North Macedonia	21.0	17.5	16.6	15.6	14.5	14.2
Black Mountain	15.5	15.4	18.4	16.9	15.1	14.1
Serbia	13.7	11.2	9.7	11.0	9.4	9.3
The average of the region	18.5	16.3	16.5	15.6	us	us

Source: European Commission (DG-ECFIN), MFE

The January-August budget balance recorded surpluses in Albania, Montenegro, Kosovo and Serbia, which however was often partly due to under-executed capital expenditure, sometimes by a significant margin.

Table 5: General government balance (Fiscal deficit in % of GDP)

	2018	2019	2020	2021	2022	2023*
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Fiscal balance, (in % of GDP)

*PUBLIC FINANCE MANAGEMENT SYSTEMS IN ALBANIA: GAPS, REGIONAL COMPARISONS,
AND REFORM PATHWAYS*

Albania	-1.6	-1.9	-6.7	-4.6	-3.7	-2.4
Bosnia and Herzegovina	2.2	1.9	-5.2	-0.3	-0.4	-0.3
Chuang	-2.9	-2.9	-7.6	-1.2	-0.5	us
Macedonia	-1.8	-2.0	-8.0	-5.3	-4.5	-3.9
Black Mountain	-3.9	-2.0	-11.1	-1.9	5.2	-4.7
Serbia	0.6	-0.2	-8.0	-4.1	-3.1	-2.8
The average of the region	-1.2	-1.2	-7.8	-2.9	us	us

Source: European Commission (DG-ECFIN), MFE

The ratio of public debt to GDP decreased in most countries in the second quarter of 2023 compared to the end of 2022, partly due to strong nominal GDP growth. The public debt ratio remained the highest in Albania and Montenegro, with 64.8% and 62.4% of GDP, respectively.

Table 6: Total public debt (% of GDP)

	2018	2019	2020	2021	2022	2023*
<i>Public and guaranteed debt (in % of GDP)</i>						
Albania	67.7	65.8	74.3	74.5	64.5	61.5
Bosnia and Herzegovina	34.1	32.3	36.1	33.9	29.4	29.5
Chuang	17.0	17.6	22.4	21.5	19.9	us
Macedonia	40.4	40.5	50.8	52.0	51.0	51.5
Black Mountain	70.1	76.5	105.3	82.5	69.5	71.0
Serbia	53.7	52.0	57.0	56.5	55.2	52.1
The average of the region	47.2	47.5	57.7	53.5	48.3	us

Source: European Commission (DG-ECFIN), MFE

The economic performance of the Western Balkans in 2023 reflects a region navigating post-pandemic recovery while adjusting to global price shocks and domestic structural constraints. Although growth remained positive, it was uneven across countries, with Albania, Serbia, and Montenegro experiencing accelerated expansion, while North Macedonia, Kosovo, and Bosnia and Herzegovina recorded slower momentum. On average, regional GDP growth improved marginally to 2%, supported primarily by private consumption and, in several cases, by recovering investments.

External sector indicators showed notable improvement. The regional current account deficit fell to its lowest level since 2021, driven by strong services exports—particularly tourism—higher remittances, and easing import prices. Countries such as North Macedonia and Serbia experienced the most significant adjustment, reversing part of the deterioration caused by the 2022 energy crisis. Despite weak goods exports, the resilience of services exports and moderate import growth helped strengthen overall trade balances. Inflationary pressures eased considerably in response to declining global energy and food prices, with average inflation dropping to 10.2%. Monetary tightening slowed across economies with independent monetary policy frameworks, most notably in Albania and Serbia, where policy rates remained unchanged for several months. The moderation in inflation, combined with continued—though modest—economic expansion, contributed to higher budget revenues and improved fiscal balances in most countries.

Labor market conditions continued to strengthen gradually. Employment growth remained positive, labor force participation increased in several economies, and unemployment rates either declined or stabilized. Nevertheless, unemployment remains significantly higher than in EU member states, reflecting persistent structural challenges in regional labor markets. Public finances showed overall improvement, with budget surpluses recorded in Albania, Montenegro, Kosovo, and Serbia for the January–August period. However, these surpluses were often influenced by under-execution of

capital spending, highlighting ongoing weaknesses in public investment management. Public debt ratios also declined in most countries, supported by strong nominal GDP growth, though levels remain comparatively high in Albania and Montenegro.

4. Conclusion

The analysis of Albania's public finance management (PFM) system shows that substantial progress has been made in strengthening macroeconomic stability, modernizing fiscal governance, and improving institutional performance. Albania has demonstrated resilience in the face of major shocks—including the 2019 earthquake, the COVID-19 pandemic, and recent external price shocks—supported by prudent fiscal policies, sustained reforms, and a gradual alignment with European governance standards. Key macroeconomic indicators, such as GDP growth, employment, the current account balance, and public debt, have generally moved toward more sustainable trajectories, despite persistent structural vulnerabilities. At the core of these developments lies the increasing importance of sound governance frameworks. The evolution of public-sector corporate governance, inspired by international standards such as CIPFA and the Cadbury principles, has contributed to greater transparency, accountability, and integrity in public financial decision-making. Nonetheless, gaps remain in areas such as internal control systems, the effectiveness of audit institutions, fiscal risk management, and the integration of performance-based budgeting.

Comparative analysis with Western Balkan economies shows that Albania performs relatively well in terms of economic resilience, labor force participation, tourism-related service exports, and foreign direct investment inflows. However, the country continues to face challenges related to external sector vulnerabilities, fluctuating trade balances, and public debt levels that remain among the highest in the region. Overall, the findings underscore that continued modernization of PFM systems is essential for ensuring fiscal sustainability, strengthening public trust, and supporting long-term economic development. Effective governance will remain a decisive factor in Albania's ability to maintain macroeconomic stability and progress toward EU integration.

5. Recommendations

Strengthening public financial management should begin with reinforcing internal control and audit mechanisms across government institutions. This requires enhancing the capacity, independence, and accountability of internal audit units, while improving coordination with external audit bodies to ensure coherent and effective oversight. Expanding fiscal transparency is also essential, including broader and timelier publication of fiscal reports, better-quality data, and improvements in performance-based budgeting that link resource allocation to measurable outputs and outcomes.

A more resilient fiscal framework further depends on improved management of fiscal risks and public assets. Governments should implement systematic monitoring of contingent liabilities, state-owned enterprises (SOEs), and public-private partnerships, supported by medium-term risk assessments integrated into the annual budget cycle. Strengthening SOE governance in line with OECD standards—through transparent oversight, professional and depoliticized boards, standardized reporting, and regular external audits—is critical. In parallel, sustainable public debt management should be promoted through prudent borrowing, diversified financing sources, and growth-enhancing reforms. Finally, enhancing the efficiency of public expenditures requires substantial improvements in public investment management, digital transformation, and institutional capacity. Better project appraisal systems, cost-benefit analysis, and procurement planning are essential to reduce persistent under-execution of capital expenditures. Expanding digital tools for budgeting, accounting, tax administration, and financial reporting—alongside improved interoperability of government information systems—will support more efficient service delivery. These efforts must be complemented by continuous professional training, knowledge exchange with EU institutions, and alignment with the EU's *acquis communautaire*, particularly in procurement, financial control, and anti-corruption, to advance Albania's broader integration and governance reform agenda.

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