

RESEARCH BRIEF

DIVERSIFICATION IN THE INDUSTRIAL SECTOR OF ALBANIA: IDENTIFYING STRATEGIC AREAS

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Background

Albania's economy has grown considerably in the past 20 years: its exports in 1996 totaled US\$260 million, while in 2016 exports brought in US\$2.11 billion. But while this expansion is significant, there was **little diversification in the portfolio of goods** that Albania exports.

Three main sectors account for around two-thirds of Albania's total exports: Textiles, Hides, and Clothing; Agriculture and Foodstuffs; and Metals. Most of these products are easy to produce and of low complexity. In order for Albania to grow faster and catch up to its European Union and Western Balkans neighbors, it needs to **expand into new areas of production and increase the variety and complexity of products** it is able to export.

Towards this purpose, CID used information available in the Atlas of Economic Complexity (www.atlas.cid.harvard.edu) to determine which products are most feasible for Albania to expand into given its current production.

Research Methodology

Diversification, by definition, requires a country to learn to produce new things it currently does not know how to produce. CID's research finds the key element of success to diversification, and therefore sustained economic growth to be **knowhow**. Products vary in the amount and type of know-how they require, and local economies vary in the amount and type of knowhow they possess. By understanding what capabilities exist locally, one can analyze what additional products could be manufactured by adding relatively few new capabilities to existing knowhow. Products differ in their degree of shared capabilities - for example, producing a shirt and a suit require similar knowhow as compared to producing coffee and TV sets.

High potential products for diversification in Albania will balance two characteristics:

- **Distance to existing capabilities:** Promising products will be "nearby" existing in order to leverage knowhow. Nearby distance is treated as a proxy for lower risk or fewer missing capabilities in moving into a new product.
- **Complexity:** Promising products will also be more complex than those existing exports, and therefore will tend to be able to support higher productivity and wages.

Distance is considered a crucial determining factor in whether a country can feasibly export a product. Complexity, on the other hand, matters greatly for improving value creation, wages, and productivity – the key factors that lead to a wealthier economy.

Other dimensions that are traditionally contemplated in the economic complexity analysis but are not immediately relevant to Albania are opportunity gain and global market size. Given Albania's relatively small population and economy, a minimum global market size for each product does not need to be considered because even small global markets will generate sizeable new demand, growth, and contribution to job creation in Albania.

By taking the Complexity and Distance variables, normalizing them, and weighing them equally, a “Strategic Value” measure was obtained for each product that Albania does not yet export significantly. Products were then ranked by this value, and their overarching sectors were compared.

Research Insights

- The **Plastics and Rubbers** sector ranks first in feasibility, with a high average complexity of its products.
- The **Agriculture and Foodstuffs** sector comes second in the ranking, with a lower average complexity but a higher proximity to current exports. Albania already produces many products in this sector; for example, it already exports different types of fruits, vegetables, and seafood in significant quantities. However, it does not produce many prepared or processed foods, which ranked highly for their potential to Albania and lower risk in diversification.

It is important to note that this ranking does not guarantee success of any one individual product, as more detailed analysis is needed to assess the requirements of each. However, it suggests that these sectors as a whole offer less risky opportunities while increasing the level of economic complexity.

Download the full report

<https://albania.growthlab.cid.harvard.edu/publications/diversification-industrial-sector-albania-identifying-strategic-areas>

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