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Green Finance Development in Albania

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Abstract: Green finance has emerged as a critical tool in addressing climate change and promoting sustainable economic growth. Albania, has started to explore the potential of green finance to support its transition to a low-carbon and resilient economy. This paper aims to provide an overview of the current state of green finance in Albania, gives an insight of the main developments in the banking and energy sector as two of the main sectors contributing in the greening process the green pathway and furthermore lists the challenges and opportunities for further development. The paper builds on existing literature, which is mainly in the form of reports. There is a number of promising initiatives and projects underway, but academic researches for Albania are missing. In order to achieve the main objective, a desk research and semi structured interviews with stakeholders of the main financial institutions have been conducted. The results obtained from analyzing the quantitative and qualitative data indicate the early stage of green finance development in Albania, the problems and challenges of this transition. The study contributes in developing additional theoretical basis related to green finance in Albania and gives proper recommendations for further development.

Keywords: sustainable finance; green transition; green products; banks; energy

JEL Classification: Q01; Q40; Q54; G18

1. Introduction

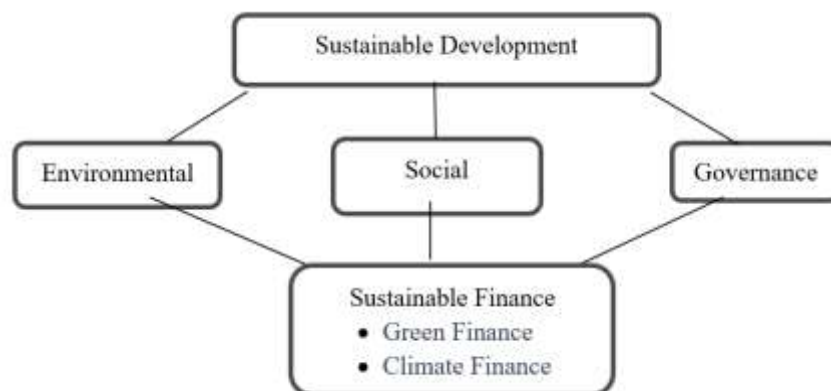
The urgent need to combat climate change and promote sustainable development has spurred increased global interest in green finance. With its potential to mobilize financial resources for environmentally friendly projects and incentivize the transition towards a low-carbon economy, green finance has emerged as a key driver of sustainable growth. In recent years, Albania, a country known for its rich natural resources and diverse ecosystems, has been actively pursuing initiatives to foster green finance development.

It is inevitable to understand green finance without looking it from a broader perspective; that of sustainable finance. Sustainable finance plays a crucial role in advancing our understanding and implementation of green finance. By embracing sustainable finance principles, we gain a deeper understanding of the wider implications and impacts of green finance initiatives. Sustainable Finance has become a top priority in Europe's political agenda due to growing awareness of its importance. Sustainable Finance refers to the integration of sustainability aspects in the decision-making processes of financial market actors, financial market policy and related institutional and market arrangements that contribute to the achievement of strong, sustainable and inclusive growth. The current international debate on sustainability focuses on environment, particularly climate change related aspects. However,

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the term of Sustainable Finance is conceptually broader, including the narrower term of green finance, but also social and governance-related aspects.

The concept of Sustainable Finance



Source: Illustration of the author

As Albania pursues its goal of EU accession, the country has demonstrated a strong commitment to sustainable finance, recognizing its importance in achieving long-term economic and environmental sustainability. The government has introduced a series of reforms to strengthen the regulatory framework, promote responsible investment, and encourage the integration of environmental, social, and governance (ESG) factors into financial decision-making. Furthermore, Albania has actively participated in regional and international initiatives, such as the Western Balkans Sustainable Finance Initiative and the European Union's Sustainable Finance Action Plan. These efforts show Albania's dedication and commitment to harmonizing its financial practices with EU standards, fostering a sustainable financial system and advancing its integration into the European Union.

The first initiatives to address environmental challenges, regarding sustainability date back from the Earth Summit in Rio de Janeiro in 1992, where the United Nations Framework Convention on Climate Change and the Convention on Biological Diversity were adopted. The summit also led to the adoption of Agenda 21, a plan to promote sustainable development globally, which included recommendations for both developed and developing countries to achieve sustainable development. Agenda 21 aimed to address issues such as poverty, environmental degradation, and unsustainable consumption patterns by promoting sustainable development practices. The summit recognized that economic development needed to be balanced with social and environmental concerns, and that global cooperation was necessary to achieve this goal. Later initiatives have continued to develop further and two of the most important next events are The Paris Agreement and UN 2030 Agenda. The Paris Agreement provides a culmination in the political discussions regarding the climate change problem. This international treaty was agreed by 196 countries at the UN Climate Change Conference, held in Paris, in 2015. Alongside this, the "Agenda 2030" was set up and adopted by all United Nations Member States in 2015. The 2030 Agenda for Sustainable Development seeks to end poverty and hunger, protect the human rights, achieve gender equality and the empowerment of all women and girls, and ensure protection of the planet and its natural resources.

Today, the financial sector should understand the SDGs (Sustainable Development Goals) and adopt the idea of long-term investments, which necessitates directing capital towards sustainable activities, to build a more resilient and sustainable future for all. The financial system can play a catalyst role in the sustainable transition process through sustainable finance, green finance, and climate finance.

2. Literature Review

Sustainable finance refers to financial activities that promote sustainable development in three main interconnected dimensions: economic, environmental, and social (Ryszawska, 2016). Essentially, any financial practices adopted by institutions that support and facilitate sustainable development can be classified as sustainable finance, as per the UNEP in 2015 (UNEP, 2015).

The literature does not provide a universally accepted definition of green finance. The term “green finance” defines a wide range of financial activities that support sustainable development objectives, encourage environmentally friendly products and policies, and promote the growth of a sustainable economy. It involves investments aimed at achieving sustainable development goals, mitigating climate change risks, and preserving natural resources (Höhne, Khosla, Fekete, & Gilbert, 2012). According to (Wang & Zhi, 2016) green finance is a new financial model that focuses on protecting the environment and promoting the sustainable use of resources. If the principles of green finance are applied soundly, it can direct the movement of funds and ensure efficient management of environmental risks and the appropriate distribution of both environmental and social resources. Sustainable finance, green finance and climate finance all contribute to ease the transition towards a sustainable financial system.

According to UNEP, a sustainable financial system:

- Identifies the cost of high carbon and resource intensive assets
- Allocates capital towards low carbon, resource efficient assets
- Achieves resilience of financial institutions and individuals towards shocks.

The existing economic models we have today were created in a world that had an abundance of goods and services produced by nature, without considering the finite nature of natural resources and the impact of economic activities on the environment (Schoemaker & Schramade, 2019). These economic models are still widely used, but are no longer viable. The world is now in the process of adjusting its production and consumption practices and is looking for alternatives to support the transition to a more sustainable and low-carbon economy. The main financial system’s objective is to channel the savings to their most efficient and fruitful applications. According to Sachs, Woo, Yoshino, & Taghizadeh-Hesary, 2019, when the financial system functions effectively, the savings are directed towards investments that enhance living standards. However, when the financial system fails to operate correctly, such as in recent times, savings are directed towards environmentally harmful projects that worsen climate changes effect.

It is widely argued that the financial development of a country significantly impacts environmental degradation (Haseeb, Xia, Baloch, Abbas, & Danish, 2018). This relationship between financial development and environmental quality is also consistent with the theory expressed in the Environmental Kuznets curve.

Fumitaka, 2015 examined the relationship between financial development and energy consumption in Asia for the period of 1980–2012. The findings of their analysis stated a long run equilibrium relationship between finance and energy consumption in the region, indicating that energy usage could be a driving force behind financial development.

Green finance can have a positive impact in the environmental and societal issues, but faces many challenges such as: the lack of awareness, inconsistent definitions, inconsistent policies, lack of coordination, and lack of incentives to investors and financial institutions. Therefore, it is necessary to

identify the important points for green finance development and plan the strategies of green financing, so that it will also be profitable (Ozili, 2022).

3. Methodology

This paper aims to provide a comprehensive analysis of the current state of green finance in Albania, exploring the challenges, opportunities, and potential pathways for further growth. By examining the regulatory frameworks, financial instruments, and stakeholders involved, this study aims to shed light on the progress made, as well as identify areas for improvement in Albania's green finance ecosystem. Through this exploration, valuable insights can be gained to inform policy-making, financial industry practices, and future research in the field of green finance in Albania. The country is still in its early steps towards the greening process, so the focus of the research will be to identify the key issues and challenges and draw conclusions for the availability of financing green projects, the role of policymakers and involvement of key stakeholders.

To achieve the main goal, the methodology of this paper will combine both primary and secondary data. The first part of the paper presents the literature review, which was conducted by searching articles, reports and publications using the key words "sustainable finance", "green finance", "green transition". The statistics used have been collected using databases of European Union, EBRD, UNEP and information from the websites of Albanian banks.

On the other hand, primary data for the study has been collected through semi-structured interviews with key stakeholders in the financial system in Albania. 10 interviews have been conducted with a diverse group of stakeholders; including representatives from government, regulators and financial institutions. They mainly included policymakers and financial industry professionals the questions asked during the interviews were as follows:

1. How would you define green finance, and what role do you believe it plays in addressing environmental challenges?
2. How do you assess the current level of awareness and understanding of green finance within the financial industry?
3. Can you provide examples of successful green finance projects or investments that your organization has been involved in? What were the key factors contributing to their success?
4. What steps has your organization taken to promote and support green finance initiatives?
5. How do you collaborate with other stakeholders, such as NGOs, or international organizations, to advance the development of green finance?
6. How do you see the future of green finance evolving, and what trends or developments do you anticipate in the coming years?
7. What policy or regulatory changes do you believe would further accelerate the growth and adoption of green finance practices?

There are several limitations to this study that should be acknowledged. Firstly, the study will focus on the Albanian financial system and may not be generalized for other countries. Secondly, the study does not capture the perspectives of all relevant stakeholders.

4. Green Finance in the Context of Albania Energy Sector

Albania's energy sector holds significant potential in contributing to green finance and promoting sustainable development. The country has diverse renewable energy resources, including hydropower, solar, wind, and biomass. With its vast river systems and mountainous terrain, hydropower has been a traditional source of electricity generation in Albania. According to (Ciuta & Gallop, 2022), in 2020, 70% of the electricity generated in Albania was from hydro powers, 30% was imported and only 0.4 per cent of electricity was generated by solar photovoltaics. The country is entirely dependent on hydropower. This is considered as an advantage in the aspect of decarbonization of the energy sector, but it also means that the energy sector is strongly reliable on climate changes. So, there has been a growing emphasis on diversifying the energy mix and expanding renewable energy sources, followed by changes in legislation which now allow and incentivize solar and wind energy.

The Albanian government has implemented policies and incentives to attract private investments in renewable energy projects, creating opportunities for green finance. These initiatives have led to increased capacity in solar and wind power, with several large-scale projects underway. Moreover, the development of small-scale hydropower plants has gained momentum, promoting decentralized and community-driven energy solutions. The energy sector's commitment to renewable energy not only contributes to reducing carbon emissions but also fosters the growth of green finance by attracting investments in sustainable infrastructure and promoting the adoption of clean technologies.

5. Green Finance in the Context of Albania Banking Sector

One of the major actors driving the development of green finance include banking sector. Despite the unique country-based challenges and opportunities, the Albanian banking sector is facing today similar challenges to those faced by the banking sector globally. With the increasing focus on environmental sustainability, many countries are introducing regulations that require banks to integrate environmental and social factors into their lending and investment decisions. The urgent need for digital transformation, challenges posed by climate change, and offering of new ESG products have all become critical issues of the banking industry today.

Green banking is an emerging area of creating competitive advantages and new business opportunities, in the frame of Sustainable Development Goals. Bank are now embracing ESG principles and developing green products in the context of achieving SDG objectives. Albanian`s banks have started to pay special attention to green banking, by putting environmental and corporate social responsibility as very important points of their missions. On one hand, banks, in the role of entities operating within a community, have a direct impact on the environment (carbon footprints, water consumption, energy consumption, paper consumption, etc.) but also an indirect impact through the products and services they offer to their clients. That is why banks are incorporating environmental goals in their development mission.

Green banking has affected the external performance of banks. It has provided the opportunity for banks, to create new products and services for clients and achieving a competitive advantage inside the industry. (Lee & Baral, 2017) define a "green" product, service or instrument when used to raise funds which will be spent on environmentally friendly projects. Typically, banks provide loans for green projects such as renewable energy, energy efficiency, and sustainable agriculture. These loans tend to have lower interest rates than traditional loans, which incentivizes borrowers to invest in environmentally friendly activities.

In the household segment, the main segment of green loans is related to loans for increasing energy efficiency. These types of loans are typically aimed at financing energy-efficient home upgrades, such as installing solar panels, improving insulation, or upgrading heating and cooling systems to reduce energy consumption and environmental impact.

Some of the most important financial institutions that operate in the field of green finance in Albania, and the respective products and services offered have been summarized in the table below.

Table 1. Green Products Offered by Albania`s Banking Institutions

Financial Institution	Green Product Offered
BKT	GEFF Green Loan that supports investments in energy efficiency projects.
OTP Bank Albania	GEFF Green Loan dedicated to private individuals for energy efficiency investments in houses (non-collateral consumer loans, mortgage loans including reconstructions, as well as mortgage loans).
Intesa SanPaolo Bank	Loans for green residential buildings, leasing for electric vehicles, different alternatives for financing photovoltaic systems for self-production, targeting all business segments from Large Corporate, SME, Small Business and Individuals.
ProCredit Bank	“Eco loans”; special credit services available to both business and private clients for investments in energy efficiency, renewable energies, photovoltaic systems, and e-vehicles.
Union Bank	GEFF Green Loan for investing in insulation, solar panels, efficient boilers, and other green technologies to improve energy efficiency in houses.
BESA Fund	GEFF Green Loan for promoting investments in the green economy in apartments.

International donors and development banks have played an important role on national banks by providing technical and financial assistance and the GEEF is an example of this assistance. The Green Economy Financing Facility (GEFF) is a programme designed by the EBRD and supported by grants from the European Union, which supports sustainable investments, which help to build a more resilient and sustainable future for everyone. The finance provided by GEFF in Western Balkans supports green investments in the residential sector and businesses who provide energy efficiency and renewable energy products and services to households. Albania has attracted a total of €1.2 billion invested in 84 projects, all towards investments that promote environmentally sustainable alternatives of investment.

6. Challenges of Green Finance Development in the View of Main Stakeholders

The challenges of green finance development in Albania, mentioned in this section, are a summary of the opinions gathered from the semi-structured interviews. Processing the answers received from the interviews, the following conclusions were reached regarding the development of green finance and current issues:

- Lack of standardized definitions and frameworks makes it difficult to assess and compare the environmental impact of different financial products;
- Data availability and quality. There is often a lack of consistent, reliable, and standardized data on environmental factors and about the environmental performance of potential investments;
- The introduction of new risks that financial institutions need to evaluate and manage (policy and regulatory changes, technological uncertainties, and reputational risks). Financial institutions and regulatory bodies must develop appropriate risk assessment methodologies and tools to effectively evaluate the risks associated with green finance;

- Lack of financial education and awareness of individuals and businesses about green economy.

The majority of population may not be aware of the concept of green finance, its benefits, and how it works.

- Limited financial resources: Albania may not have sufficient financial resources to invest in green technologies and projects. Additionally, green technologies are often more expensive than traditional technologies, making it difficult to switch to green alternative.
- Weak financial infrastructure: Albania lacks the financial infrastructure required to support green finance, such as credit rating agencies, green bond markets, and specialized financial institutions.
- Individuals take an unwilling approach towards environmental investments. Usually, individuals in developing countries prioritize immediate needs over long-term environmental concerns.
- Lack of expertise of the people and institutions which promote these activities because green finance is still a new concept for the country.

In order to better analyze the challenges, it is necessary to understand the views of two of the main stakeholders involved; on one hand the financial institutions and on the other hand companies and individuals that will make green investments. The fact that the participants in the interviews consist of representatives from regulatory bodies and financial institution, the frame of green finance is not complete.

7. Recommendations for Green Finance Development in the View of Main Stakeholders

The development of green finance in Albania requires a coordinated effort between the government, private sector, and society as a whole. These recommendations have been formulated based on the analysis of Albania green financial development with a focus on the view of the interviewees. Given the challenges and barriers that the country encounters, these specific recommendations for the country can be developed:

- Raising awareness among market participants of the financial sector for environmental risks.

This should involve a coordinated effort of all relevant stakeholders is necessary to bring about a fundamental cultural shift in financial markets and to integrate sustainability into financing and investment practices.

- Developing a regulatory framework for green investments. The Albanian government should establish fiscal, economic, climate and environmental policies. Financial authorities need to set incentives for firms and private investors, to enhance green finance and provide support to encourage such investment, such as tax incentives or subsidies for sustainable projects.
- Stimulate green products issuance and promote the use and development of new blended finance products for green finance purposes.
- There is need for more training and capacity-building initiatives, to help institutions build the necessary expertise for green finance. This will require collaboration between governments, financial institutions, and other stakeholders to create a supportive environment for building expertise in green finance.

8. Conclusions

Green finance is currently still a new market in Albanian financial system, but it has the potential to rapidly grow because of the increasing interest from both the public and the private sector. European Union is promoting widely the concept of green finance, considering it as a vital component of the transition towards a sustainable and competitive economic system. Considering Albania's aspiration to join the EU, the country is making efforts to address environmental challenges and pursue sustainable development. The government has taken steps to create a supportive regulatory framework for green finance, and the private sector has responded with the development of new financial products and services. However, there is still room for further growth and development in the field, particularly in terms of raising awareness among the public, encouraging the adoption of green finance practices and developing new green financial products. Overall, the development of green finance in Albania has the potential to create a more sustainable future for the country, while also contributing to global efforts to address climate change and other environmental issues.

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