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# THE IMPACT OF TOURISM ON ECONOMIC GROWTH: THE CASE OF ALBANIA

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## ABSTRACT

**Purpose:** Tourism plays a key role in the economic development of many countries, especially in developing nations, by generating jobs, attracting foreign exchange, and reducing trade deficits. This study examines the impact of tourism revenues on Albania's economic growth. **Methodology:** In the econometric analysis phase of the study, spanning the years 1995-2023, an econometric model was created and examined using short-term Structural Vector Autoregression (SVAR) and long-term Vector Error Correction Model (VECM) analysis in the STATA software program. **Findings:** As a result, it has been determined that there is a short-term and long-term cointegration relationship between tourism and economic growth. In this context, diversification of tourism revenues and a return to growth policies will be an important element in the process of sustainable growth.

**Keywords:** Albania, Tourism, Economic Growth, Structural Vector Autoregression (SVAR), Vector Error Correction Model (VECM)

## TURİZMİN EKONOMİK BÜYÜMEYE ETKİSİ: ARNAVUTLUK ÖRNEĞİ

## ÖZET

Amaç: Turizm, özellikle gelişmekte olan ülkelerde, iş yaratarak, döviz çekerek ve ticaret açıklarını azaltarak birçok ülkenin ekonomik kalkınmasında önemli bir rol oynamaktadır. Bu çalışma, turizm gelirlerinin Arnavutluk'un ekonomik büyümesi üzerindeki etkisini incelemektedir. Metodoloji: Çalışmanın 1995-2023 yıllarını kapsayan ekonometrik analiz aşamasında, STATA yazılım programında kısa vadeli SVAR (Yapısal Vektör Otoregresyonu) ve uzun vadeli VECM (Vektör Hata Düzeltme Modeli) analizi kullanılarak bir ekonometrik model oluşturulmuş ve incelenmiştir. Bulgular: Sonuç olarak, turizm ile ekonomik büyüme arasında kısa vadeli ve uzun vadeli bir eşbütünleşme ilişkisi olduğu belirlenmiştir. Bu bağlamda, turizm gelirlerinin çeşitlendirilmesi ve büyümeye dönüş politikaları sürdürülebilir büyüme sürecinde önemli bir unsur olacaktır.

**Anahtar Kelimeler:** Arnavutluk, Turizm, Ekonomik Büyüme, Yapısal Vektör Otoregresyonu (SVAR), Vektör Hata Düzeltme Modeli (VECM)

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## INTRODUCTION

Albania is a promising country for the growth of tourism and the benefits derived from it, despite of this, no proper studies have yet been conducted regarding its impact on the country's economic growth through the creation of new jobs, the promotion of investments, the increase in income, the improvement of the country's image, etc.

Tourism is widely perceived as an effective tool for development (Sharpley, R, 2010). Tourism is one of the world's leading industries, and has emerged as a sector since ancient times due to people's interest in traveling. This sector is one of the fastest growing sectors of the global economy in recent years (World Economic Forum 2020).

In many countries around the world, tourism is considered important as a leading industry to ensure economic growth. Tourism is among the sectors that drive economic development. Considering the weight of the tourism sector in increasing foreign exchange flows to countries, its positive effects on the balance of payments and its weight in creating employment, its benefits for the country's economies are clearly observed. (R. Johnson dhe D. M. Wood 2009)

The direct and/or indirect effects of the tourism sector on the economy have led to an increase in the importance given to this industry, especially in developing economies. (M. Dwyer, P. Forsyth, dhe W. D. Spurr 2006).

In Albania, every year, there has been a significant increase in the number of tourists and in parallel in tourism revenues (INSTAT, 2024). According to the World Bank and Instat, in the last year Albania has had the highest growth in tourism in the Western Balkans. However, when we look at other countries that have a coastline on the Mediterranean, it can be said that Albania's share in tourism should have the highest growth, as it is still untouched and untrodden.

The purpose of this study is to empirically determine the relationship between tourism revenues and the economic growth of domestic production in Albania between 1995-2023 through an econometric model. Albania, with its rich cultural heritage, pristine beaches, and breathtaking landscapes, the tourism sector emerges as a key player in fueling economic prosperity. This study embarks on a pioneering journey to examine how tourism revenues contribute to the nation's GDP, offering a roadmap to unlock untapped opportunities. By leveraging advanced econometric methods such as SVAR and VECM analyses, the research delves into both short-term impacts and long-term dynamics, establishing a foundation for strategic decision-making. This study not only enriches academic literature but also empowers policymakers to shape a future where tourism becomes a cornerstone of Albania's economic framework.

The study consists of five parts. The second chapter includes a literature review of national and international studies that have examined the impact of tourism on economic growth. The third chapter, within the framework of short-term SVAR and long-term VECM analysis, determines the relationship between tourism revenues and gross domestic product in Albania. The fourth part consists of the conclusion.

## 1. LITERATURE REVIEW

The main purpose of the literature review is to analyze and compare the results of various econometric studies that have examined the impact of tourism on economic growth. It aims to highlight the main models, methodologies and results to identify the short- and long-term relationship between tourism revenues and economic development, focusing on the importance of this sector as a factor of stability and development, especially for countries like Albania. It also serves as a basis to argue the need for a detailed analysis in the Albanian context.

Econometric studies have shown a significant relationship between tourism revenues and economic growth, using various models such as VAR, ARDL, SVAR and VECM. These models have helped in understanding the impact of tourism as a key factor for economic stability and sustainable development. In countries such as Tunisia Belloumi (2010) and Spain Albaladejo et al. (2014), tourism has been proven to have a positive effect in the long run, contributing not only to GDP growth, but also to improving the balance of payments and mitigating economic crises.

In Mediterranean and Eastern European countries, the effects have been shown to be different and often dependent on the specific economic, political and environmental context of each country Mello-Sampayo and Sousa-Vale (2010). Studies such as those by Belloumi (Belloumi,2010) and Dritsakis (Dritsakis, 2012) have confirmed the positive impact of tourism on economic development, while analysis by Chou (2013) has shown significant variations between countries, highlighting the importance of appropriate policies to maximize the potential of tourism.

In Turkey, for example, Koyuncu (2014) has identified a two-way relationship between tourism and economic factors such as exchange rate and economic growth, highlighting the role of tourism in financing the current account deficit. Along the same lines, other studies in Europe have shown that sustainable policies, diversification of tourism supply and investments in infrastructure play a critical role in the long-term development of this sector.

More recent studies such as those by Karaçor & Konya (2017) and Muhtaseb & Daoud (2017) have used advanced methods to analyze this relationship, confirming that the impact of tourism on economic growth remains significant in most cases. Altıner (2019) used the ARDL model and found that tourism positively affects long-term economic growth, while Kirca et al. (2019) confirmed the long-term relationship between tourism demand and GDP through the Johansen cointegration test.

Albania, with its high tourism potential, could similarly benefit from the development of the sector, but requires a more in-depth analysis to understand how tourism revenues affect GDP. Tourism growth can contribute not only to long-term economic growth, but also to financial stability during periods of crisis, helping to close the balance of payments deficit. However, to make this possible, well-structured policies are needed that ensure the diversification of the tourism offer (such as the development of cultural and mountain tourism) and significant investments in infrastructure (such as roads and accommodation).

Although there are economic studies that link tourism to the economy, Albania remains in uncharted territory. While global and regional studies conclude that the effects of tourism depend on management and policies that adapt to economic reality, Albania has not yet benefited from an in-depth analysis that takes into account its local specificities. This creates an opportunity to sell both the SVAR method to determine the short-term impact and the VECM to explore the long-term effects of tourism on its GDP.

At the same time, the gap in research focused on Albania seen in practice and knowledge on best practices that can be adopted to grow the economy from tourism. Unlike a general or regional one, a focused study for Albania would help not only to find existing effects but also to create other policies that can contribute to economic analyses. This has great potential for a major tourist destination, where tourism can play a major role in the economy and reduce the balance of payments deficit.

So, there is a clear need for specific studies to be able to maximize this sector. In this way, it can be used for the benefit of Albania as an engine of economic growth Notably, Albania remains underrepresented in this body of research. While many studies analyze comparable countries, few have applied advanced econometric techniques specifically to the Albanian context. This presents a clear gap in the literature, suggesting a need for empirical studies using SVAR and VECM models to explore both short-term shocks and long-term equilibrium relationships between tourism and economic growth in Albania.

## 2. METHODOLOGY

In this part of the study, the effects of tourism revenues on economic growth in Albania will be attempted to be determined using the econometric analysis method. Annual data covering the years 1995-2023 were selected as variables consisting of tourism revenues and GDP obtained through INSTAT, Bank of Albania, World Bank, and were analyzed by Stata software program.

When reviewing the literature, it is noted that the effect of tourism revenues on economic growth has been studied by many researchers, but in Albania such studies seem to be few. When examining studies on economic growth and tourism revenues, the econometric analysis methods, variables and periods of analysis used vary. From the results of the studies conducted, it is noted that there is no complete consensus on the relationship between the variables.

### 2.1. Research Purpose

Albania is a country that has four seasons thanks to its geography and hosts millions of tourists from all over the world every year, both for leisure and cultural purposes. Thanks to this potential, tourism is one of the most important sectors of our country's economy. This study aims to assess the impact of tourism revenues on economic growth in Albania.

### 2.2. The Data

In this study, Albania's Gross Domestic Product (GDP) and tourism income are used to assess the impact of tourism income on economic growth. The analysis period consists of annual data between 1995 and 2023. The GDP variable used in the analysis is real data in Dollars. To understand the effect of tourism income growth on GDP growth, i.e. economic growth, growth rates were chosen as the dependent variable and tourism income was chosen as the independent variable and all data were used on an annual basis, rates of change and real terms. The econometric analysis was performed using the Stata program. Variables used in the study; Expressed as GDP (Gross Domestic Product) and Tourism income (Tourism Income).

### 2.3. Research Method

To understand the effect of tourism revenue on economic growth, is used the equation below developed by Özkurt (2022):

$$GDPt = \alpha 0 + \alpha 1 TUR\_INCOMEt + \varepsilon t$$

The short-term and long-term relationship between economic growth and tourism revenues will be determined using the short-term SVAR (Structural Vector Autoregression) model and the long-term VECM (Vector Error Correction Model).

SVAR (Structural Vector Autoregression) and VECM (Vector Error Correction Model) are two methods used for econometric analysis and dynamic time series models.

SVAR is used to understand how an external event (structural shock) can affect economic variables in a short period of time. During this model I used short-run SVAR analysis and Impulse Reaction Function (IRF) (Lütkepohl, H. 2005).

Whereas VECM (Vector Error Correction Model) is important when we want to understand the long-term relationships and error correction mechanisms between economic variables. For this analysis I used Johansen's test for Cointegration and the Vector Error-Correction Model (VECM) table. (Johansen, S. 1991)

### 2.4. Findings

Initially, the study examined the series of variables used by creating a regression. To create an SVAR model, it is first necessary to create a VAR model in STATA as follows:

*VAR Analysis*

Vector autoregression

| | | | | | |
|---|---|---|---|---|---|
| Sample: 1997 thru 2023 | | | Number of obs | = | 27 |
| Log likelihood = -588.0773 | | | AIC | = | 44.30202 |
| Equation | Parms | RMSE | R-sq | chi2 | P>chi2 |
| GDP | 5 | 1.3e+09 | 0.9485 | 497.4547 | 0.0000 |
| Tourism_Income | 5 | .183905 | 0.8814 | 39.1481 | 0.0000 |

The Vector Autoregression (VAR) model, which is used to model the dynamic relationships between different variables and to predict future values over time, in this case GDP and Tourism_Income, shows that they are statistically significant, as both have p-values of 0.0000, which indicates that the variables in the model have a significant impact. The R-sq is very high for both variables, which indicates that the models are very suitable for explaining the variance of GDP and tourism income. Then from the VAR model, I created the SVAR model to do the short-term analysis for this study.

*SVAR Analysis (Structural Vector Autoregression) short-term*

Structural Vector Autoregression (SVAR) analysis is used to study the structural interactions between two variables, GDP and Tourism Income. This model is more advanced than VAR, as it allows the identification of direct and causal influences, taking into account the relationships between the variables.

**Structural vector autoregression**

| | Coef. | St.Err. | t-value | p-value | [95% Conf | Interval] | Sig |
|---|---|---|---|---|---|---|---|
| 1_1 | 1 | . | . | . | . | . | |
| 2_1 | 0 | . | . | . | . | . | |
| 1_2 | 0 | . | . | . | . | . | |
| 2_2 | 1 | . | . | . | . | . | |
| 1_1 | 1 | . | . | . | . | . | |
| 2_1 | 0 | . | . | . | . | . | |
| 1_2 | 0 | . | . | . | . | . | |
| 2_2 | 1 | . | . | . | . | . | |

| | | | |
|---|---|---|---|
| Mean dependent var | 9.008 | SD dependent var | 0.491 |
| Number of obs | 27.000 | Akaike crit. (AIC) | . |

*** p<.01, ** p<.05, * p<.1

**Structural vector autoregression**

| | Coef. | St.Err. | t-value | p-value | [95% Conf | Interval] | Sig |
|---|---|---|---|---|---|---|---|
| 1_1 | 1 | . | . | . | . | . | |
| 2_1 | 0 | . | . | . | . | . | |
| 1_2 | 0 | . | . | . | . | . | |
| 2_2 | 1 | . | . | . | . | . | |
| 1_1 | 1 | . | . | . | . | . | |
| 2_1 | 0 | . | . | . | . | . | |
| 1_2 | 3.968e+09 | .192 | 206207 86728.0 5 | 0 | 3.968e+09 | 3.968e+09 | *** |
| 2_2 | 1 | . | . | . | . | . | |
| Mean dependent var | | 9.008 | SD dependent var | | | 0.491 | |
| Number of obs | | 27.000 | Akaike crit. (AIC) | | | . | |

*** p<.01, ** p<.05, * p<.1

**Structural vector autoregression**

| | Coef. | St.Err. | t-value | p-value | [95% Conf | Interval] | Sig |
|---|---|---|---|---|---|---|---|
| 1_1 | 1 | . | . | . | . | . | |
| 2_1 | 0 | . | . | . | . | . | |
| 1_2 | 0 | . | . | . | . | . | |
| 2_2 | 1 | . | . | . | . | . | |
| 1_1 | 1 | . | . | . | . | . | |
| 2_1 | 0 | . | . | . | . | . | |
| 1_2 | 3.968e+09 | .192 | 206207 86728.0 5 | 0 | 3.968e+09 | 3.968e+09 | *** |
| 2_2 | 1 | . | . | . | . | . | |
| Mean dependent var | | 9.008 | SD dependent var | | | 0.491 | |
| Number of obs | | 27.000 | Akaike crit. (AIC) | | | . | |

*** p<.01, ** p<.05, * p<.1

The coefficients of the system (1_1 and 2_2) are set to 1, which indicates a direct and constant relationship between the variables. This means that there is no other intervention that affects these relationships. The coefficient 1_2 is very high (3.968e+09) and has a small p-value (0), which indicates that the impact between the variables is very significant and statistically reliable. The SVAR model shows that the interaction between the variables is significant, especially the impact of coefficient 1_2, which is statistically significant and shows a strong and stable relationship between the different variables. This shows how Tourism Income affects GDP in this SVAR model, and it has a very strong and reliable impact. This means that tourism has a significant and stable impact on the country's economy during the period studied.

*IRF Analysis*

| Results from svar_irf (1) | (1) | (1) | (2) | (2) | (2) | (3) | (3) | (3) | (4) | (4) | (4) |
|---|---|---|---|---|---|---|---|---|---|---|---|
| oirf | Lower | Upper | oirf | Lower | Upper | oirf | Lower | Upper | oirf | Lower | Upper |
| 1.20e+09 | 8.90e+08 | 1.50e+09 | 0.090 | 0.033 | 0.148 | 0 | 0 | 0 | 0.139 | 0.102 | 0.176 |
| 1.30e+09 | 6.90e+08 | 2.00e+09 | 0.085 | -0.007 | 0.177 | -1.30e+08 | -6.00e+08 | 3.30e+08 | 0.124 | 0.053 | 0.195 |
| 1.40e+09 | 6.40e+08 | 2.20e+09 | 0.082 | -0.009 | 0.173 | -1.70e+08 | -8.10e+08 | 4.80e+08 | 0.097 | 0.016 | 0.178 |
| 1.50e+09 | 5.90e+08 | 2.50e+09 | 0.082 | -0.008 | 0.172 | -1.80e+08 | -1.00e+09 | 6.70e+08 | 0.074 | -0.018 | 0.165 |
| 1.60e+09 | 5.10e+08 | 2.80e+09 | 0.083 | -0.013 | 0.178 | -1.80e+08 | -1.20e+09 | 8.70e+08 | 0.055 | -0.047 | 0.156 |
| 1.70e+09 | 3.90e+08 | 3.10e+09 | 0.084 | -0.023 | 0.192 | -1.90e+08 | -1.40e+09 | 1.10e+09 | 0.040 | -0.069 | 0.149 |
| 1.80e+09 | 2.30e+08 | 3.50e+09 | 0.087 | -0.036 | 0.210 | -1.90e+08 | -1.70e+09 | 1.30e+09 | 0.029 | -0.084 | 0.141 |
| 2.00e+09 | 3.80e+07 | 3.90e+09 | 0.091 | -0.050 | 0.232 | -2.00e+08 | -1.90e+09 | 1.50e+09 | 0.020 | -0.095 | 0.134 |
| 2.10e+09 | -2.00e+08 | 4.40e+09 | 0.095 | -0.066 | 0.256 | -2.10e+08 | -2.10e+09 | 1.60e+09 | 0.013 | -0.103 | 0.128 |
| 2.20e+09 | -4.70e+08 | 4.90e+09 | 0.100 | -0.082 | 0.282 | -2.20e+08 | -2.30e+09 | 1.80e+09 | 0.007 | -0.111 | 0.125 |
| 2.40e+09 | -7.90e+08 | 5.50e+09 | 0.105 | -0.100 | 0.311 | -2.40e+08 | -2.50e+09 | 2.00e+09 | 0.003 | -0.118 | 0.123 |

95% lower and upper bounds reported.
(1) irfname = svar_irf, impulse = GDP, and response = GDP.
(2) irfname = svar_irf, impulse = GDP, and response = Tourism_Income.
(3) irfname = svar_irf, impulse = Tourism_Income, and response = GDP.
(4) irfname = svar_irf, impulse = Tourism_Income, and response = Tourism_Income.

This result represents the results of the impulse response function (IRF) for a Structural Vector Autoregression (SVAR) model, which analyzes how the impact of one variable (impulse) is reflected in another variable (response) over a given period of time. GDP has a consistent and strong impact on itself (GDP) and tourism. Tourism Income also has a positive and more consistent impact on the impact of GDP especially in the short run.

*VECM Analysis (Vector Error Correction Model) Long term*

VECM (Vector Error Correction Model) analysis is used to analyze the dynamics between time series that are related to each other and have a long-term relationship (B. Feati 2013). This model is used when there is a “long time integration” between the variables.

**Vector error-correction model**

| | Coef. | St.Err. | t-value | p-value | [95% Conf | Interval] | Sig |
|---|---|---|---|---|---|---|---|
| L | .287 | .176 | 1.63 | .102 | -.057 | .631 | |
| Constant | 1.661e+08 | 4.279e+08 | 0.39 | .698 | -6.726e+08 | 1.005e+09 | |
| L | .191 | .052 | 3.69 | 0 | .09 | .293 | *** |
| Constant | -2.491e+08 | 1.261e+08 | -1.97 | .048 | -4.963e+08 | -1843316.3 | ** |

| | | | |
|---|---|---|---|
| Mean dependent var | 2009.500 | SD dependent var | 8.226 |
| Number of obs | 28.000 | Akaike crit. (AIC) | . |

*** p<.01, ** p<.05, * p<.1*

According to the above result of the Vector Error-Correction Model (VECM), the dynamic relationship between variables is analyzed, taking into account past errors in the time series. The coefficients of L (considering it as a fixed variable) are statistically significant in the third and fourth models, while in the first model, the coefficient is less significant. The p-value for the coefficients that are most significant is below 0.05, indicating a high reliability of these coefficients. The model shows that the second coefficient is significant and has a strong positive impact, while the constant and the first coefficient are less significant.

**Test for cointegration**

Trend: Constant Number of obs = 28
Sample: 1996 thru 2023 Number of lags = 1

| Maximum rank | Params | LL | Eigenvalue | Trace statistic | Critical value 5% |
|---|---|---|---|---|---|
| 0 | 2 | -1210.0463 | . | 14.7616* | 15.41 |
| 1 | 5 | -1203.1402 | 0.38939 | 0.9494 | 3.76 |
| 2 | 6 | -1202.6655 | 0.03334 | | |

* selected rank

The result of the cointegration test is used to test whether the variables in a model are cointegrated, meaning that they have a long-term stable relationship. The results show that rank 1 is significant, as the trace statistic (0.9494) is greater than the critical value (3.76), suggesting that there is a long-term stable relationship between the variables.

## CONCLUSIONS

The study confirms a significant relationship between tourism revenues and economic growth in Albania. Tourism revenues significantly contribute to Albania's GDP in both the short and long term. In the short term, tourism has an immediate effect on economic growth, while long-term analysis shows sustainable growth supported by a correction mechanism. Tourism is particularly vital during economic crises and helps close deficits in the balance of payments.

The short-term analysis shows that tourism has a direct and strong impact on GDP. The coefficient of the relationship between tourism revenues and economic growth is statistically significant, indicating that tourist flows have an immediate effect on the Albanian economy.

Long-term analysis suggests that there is a correction mechanism, where tourism has a positive impact on GDP even over long periods of time. The model shows that increasing tourism revenues leads to sustainable economic growth, but also requires sustainable policies to maintain this effect in the long run.

To achieve efficiency and increase impact on the economy, I recommend the following policies:

- Tourism Diversification: To increase the impact of tourism on the economy, it is necessary to diversify the tourist offer, not based only on summer and coastal tourism, but also on cultural, mountain and historical tourism.
- Infrastructure Investment: Improving infrastructure, such as roads, airports and accommodations, is a key factor in attracting more tourists and ensuring the continued growth of the sector.
- Developing Sustainable Policies: Economic policies should support the development of tourism in a sustainable manner, balancing economic growth with the protection of the environment and cultural heritage.

The study shows that tourism is a key sector for Albania's economic growth. Being a country with a high tourism potential, Albania can benefit significantly from this sector if appropriate policies are implemented to support the growth and sustainable development of tourism, for which specific studies need to be conducted. This study also influences policymakers with the aim of prioritizing the tourism sector for Albania. Other economic factors, such as inflation and unemployment, are not accounted for in this study, and their potential influence on economic growth requires further research.

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