FOREIGN DIRECT INVESTMENT IN REAL ESTATE IN ALBANIA AND ITS IMPACT ON GDP

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Abstract

Foreign Direct Investment (FDI) in real estate has played an increasingly significant role in Albania's economic development, particularly over the past decade. This paper examines the relationship between real estate FDI and Gross Domestic Product (GDP) in Albania over a five-year period, analyzing whether foreign investment in the real estate sector has acted as a driver of economic growth or merely reflected broader macroeconomic trends.

Our empirical findings suggest that FDI in real estate (RE) has had a positive contribution to GDP growth, particularly through increased urban development and rising property values in key economic centers like Tirana and coastal cities.

This study provides valuable insights for policymakers, emphasizing the need for strategic reforms to enhance the benefits of real estate FDI while mitigating risks associated with speculative activities.

This study, also, contributes to the literature on FDI and economic growth, offering a case-specific analysis of Albania and providing policy recommendations for optimizing the benefits of foreign investments in real estate.

Keywords: Foreign Direct Investment (FDI), Real Estate, Economic Growth, GDP, Albania, Regression Analysis

JEL classification: F21, R 30, E01,

1. Introduction

Foreign Direct Investment (FDI) in real estate has become an important driver of economic activity in many developing economies, including Albania. Over the past two decades, Albania has experienced significant FDI inflows, particularly in the real estate and construction sectors, driven by factors such as economic liberalization, improved investor confidence, and the country's growing appeal as a tourism and business destination. However, the extent to which these investments contribute to overall economic growth, as measured by Gross Domestic Product (GDP), remains a critical area of investigation.

This study examines the relationship between real estate FDI and GDP in Albania over a five-year period, assessing whether foreign investments in the property sector serve as a catalyst for economic expansion or primarily reflect broader macroeconomic trends. Given Albania's rapid urbanization, increasing demand for residential and commercial properties, and expanding tourism sector, real estate FDI has the potential to play a crucial role in shaping the country's economic trajectory. However, concerns about speculative investments, rising property prices, and the sustainability of growth in the sector necessitate a deeper understanding of this relationship.

Using empirical data and econometric modeling, this research shows that how real estate FDI may influence GDP. Furthermore, the study emphasizes the role of institutional factors, including Albania's regulatory environment, property rights framework, and financial market stability, in shaping the impact of foreign real estate investments on economic growth.

By providing an in-depth analysis of this relationship, the study aims to offer valuable insights for policymakers, investors, and economic stakeholders. Understanding how real estate FDI affects GDP can help shape future policies to maximize the benefits of foreign investment while mitigating potential risks such as market bubbles and economic volatility.

2. Literature review

The relationship between Foreign Direct Investment (FDI) and economic growth has been widely studied in the economic literature, with particular attention to sector-specific impacts. While extensive research exists on the effects of FDI on overall GDP growth, relatively fewer studies focus on FDI in the real estate sector and its implications for economic development. This section reviews key theoretical and empirical contributions related to FDI, real estate investments, and their macroeconomic effects, with a particular emphasis on emerging economies and the Albanian context.

The impact of FDI on economic growth is highly dependent on host-country characteristics, including institutional quality, financial market development, and regulatory frameworks (Borensztein, De Gregorio, & Lee, 1998).

The role of real estate FDI in economic development has gained increasing attention in recent years. Studies suggest that foreign investment in the real estate sector can stimulate economic growth by increasing demand for construction, generating employment, and improving infrastructure (Wang & Wong, 2011). However, some scholars argue that real estate FDI may also lead to market distortions, such as asset price bubbles and financial instability, particularly in countries with weak regulatory frameworks (Krugman, 1998)

Empirical studies provide mixed results regarding the impact of real estate FDI on GDP. While some researchers find a positive relationship, particularly in emerging economies (Zhang, 2015; Tsai & Peng, 2018), others highlight concerns about the sustainability of growth driven by speculative investments (Glaeser, Gyourko, & Saiz, 2008). These findings suggest that the effects of real estate FDI on GDP may depend on factors such as market maturity, investor intentions, and government policies.

Albania has experienced a significant increase in FDI inflows into the real estate sector, particularly in major cities like Tirana and coastal areas such as Vlora and Saranda. The country's liberalized investment policies, strategic geographic location, and growing tourism sector have attracted foreign investors to the real estate market (Bank of Albania, 2020). Studies on Albania's FDI trends suggest that real estate investment has contributed to GDP growth through increased construction activity and higher demand for housing and commercial properties (Xhepa, 2017). However, concerns have been raised regarding the speculative nature of some investments, as well as the potential for price inflation and financial sector vulnerabilities (IMF, 2021).

Several studies highlight the role of institutional quality in moderating the effects of FDI in Albania. Weak regulatory enforcement, informal market practices, and financial sector risks may limit the long-term benefits of real estate FDI and increase economic volatility (Daci, 2019). Addressing these challenges requires stronger governance, transparency in property rights, and improved financial market oversight.

The relationship between Foreign Direct Investment (FDI) in the real estate sector and GDP growth in Albania is an emerging field of study, as Albania continues to integrate into the global economy. Recent analyses underscore the significance of FDI as a driver of economic development, particularly within specific sectors, including real estate.

Albania's strategic geographical position and ongoing economic reforms make it an attractive destination for foreign investors, particularly in real estate. The country has made notable strides in improving its investment climate, which is reflected in the growing interest of foreign firms in various sectors, including tourism, agriculture, and notably, real estate

(Liça & Gashi, 2024). The influx of FDI not only provides crucial capital but also facilitates the transfer of technology and managerial expertise, which are paramount for fostering local economic growth and sustainability (Çakërri et al., 2020; Merollari & Koti, 2015).

Empirical research indicates a strong correlation between FDI in real estate and positive economic outcomes. For instance, Çakërri et al. assert that FDI has been instrumental in financing the Albanian economy by creating jobs and increasing production capacities within various sectors (Çakërri et al., 2020). They further posit that the real estate sector acts as a catalyst for broader economic activities and contributes to GDP growth by enhancing employment rates and stimulating local investments (Çakërri et al., 2020). These findings align with studies from other regions that demonstrate similar patterns, such as the correlation found between real estate investments and economic growth metrics in varying contexts (Wang, 2010).

Moreover, the structural dynamics of FDI in Albania reveal a crucial feedback loop where increased investment in real estate enhances economic resilience and growth potential. Muharremi notes that the real estate sector's development can help stabilize economies by creating job opportunities and generating tax revenues for public services (Muharremi, 2020). This dynamic suggests that improving the infrastructure and regulatory framework is essential to maximizing the potential benefits of FDI in this sector (Muharremi, 2020; , Hoxhaj & Pulaj, 2022).

The ongoing trajectory of FDI inflows into Albania's real estate sector seemingly indicates a robust relationship with GDP growth, making it imperative for policymakers to prioritize a conducive environment for investment. Hoxhaj and Pulaj provide a comprehensive overview of the current state of FDI in Albania and emphasize that sustained economic growth largely hinges on attracting and embedding foreign investments (Hoxhaj & Pulaj, 2022). Furthermore, studies have indicated that the nature and structure of FDI can significantly influence local economic indices, including GDP growth, suggesting that the benefits of such investments are multifaceted and integral to the overall economic strategy of Albania (Boriçi & Osmani, 2015; , Konstandina & Gachino, 2020).

In conclusion, the interconnectedness of FDI in real estate and GDP growth in Albania is increasingly evident. As the nation continues to enhance its appeal to foreign investors through improved infrastructure and conducive economic policies, it is likely that the real estate sector will play a critical role in driving economic prosperity. For sustained growth, ongoing reforms aimed at improving governance and investment assurance are paramount to attracting more FDI, which will ultimately bolster the Albanian economy

While existing research provides valuable insights into the impact of FDI on economic growth, few studies focus specifically on the short-term effects of real estate FDI on GDP, particularly in the Albanian context. Most studies either analyze aggregate FDI inflows or focus on long-term economic trends, leaving a gap in understanding the immediate macroeconomic implications of real estate investments.

This study contributes to the literature by providing an empirical assessment of the relationship between real estate FDI and GDP in Albania over a five-year period. By using econometric methods, this research aims to offer policy-relevant insights into how foreign real estate investments influence economic growth in the short-to-medium term.

3. Foreign Direct Investments in Real Estate in Albania (2019-2023)

Foreign direct investments in real estate in Albania have seen significant growth during the 2019-2023 period, making this sector increasingly attractive for foreign investors. In 2022, investments in real estate reached 291 million euros, accounting for more than 21% of the total foreign direct investments in the country. This trend intensified further in 2023, with investments in the sector reaching 325 million euros, marking an increase of 34 million euros compared to the previous year.

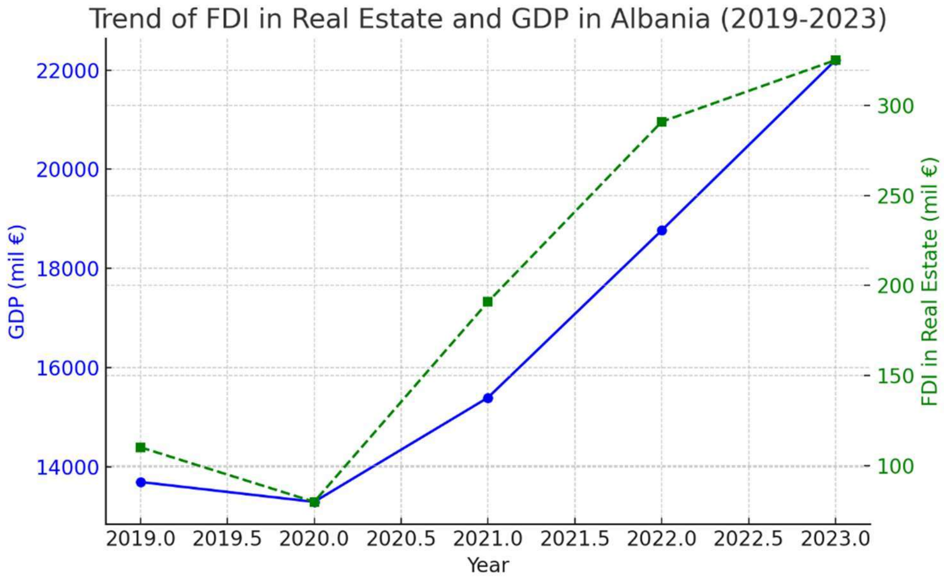
According to data from the Bank of Albania, in the third quarter of 2023, foreign investments in real estate amounted to 95 million euros, a 24% increase compared to the same period in 2022.

These investments have contributed to rising property prices, particularly in coastal areas and in Tirana, where many properties are used both for leisure and business purposes.

By the end of 2023, the stock of foreign investments in real estate had reached 1.56 billion euros, a 40% increase compared to the previous year.

This growth in investments has had a significant impact on the development of the real estate market in Albania, making it a preferred destination for international investors.

Figure 1: Trend of FDI in Real estate in Albania (2019-2023)



Source: Bank of Albania – for data on FDI inflows in the real estate

Institute of Statistics of Albania (INSTAT) – for GDP growth data

This graph shows the trend of FDI in real estate and GDP in Albania from 2019 to 2023:

- GDP (blue line) shows steady growth from 2020 to 2023, increasing from 13.3 billion euros to 22.2 billion euros.
- FDI in real estate (dashed green line) shows more volatile changes, with a decline in 2020 and a strong increase after 2021.

This indicates that foreign investments in real estate may help with economic recovery and long-term GDP growth. It reinforces the idea that the growth of FDI is linked to economic growth but also shows the instability of investments in the real estate sector.

4. Data and Methodology

This section outlines the data sources, variables, and methodology used to analyze the relationship between Foreign Direct Investment (FDI) in real estate and Gross Domestic Product (GDP) growth in Albania over a five-year period. Given the focus on a simplified model, the analysis considers only two key variables: FDI in real estate as the independent variable and GDP growth as the dependent variable.

4.1. Estimation Technique and Econometric Model

The study applies:

1. Ordinary Least Squares (OLS) Regression – to estimate the relationship between real estate FDI and GDP growth.
2. Correlation Analysis – to measure the strength and direction of the relationship between the two variables.

To analyze the relationship between FDI in real estate and GDP in Albania for the period 2019-2023, we used a simple linear regression model of the form:

$$GDPt = \alpha + \beta \cdot FDI\_REt + \varepsilon t$$

Where:

GDPt is the dependent variable (the value of GDP in year t, in millions of euros).

FDI_REt is the independent variable (the value of FDI in real estate in year t, in millions of euros).

α is the intercept (the point where the regression line intersects the vertical axis).

β is the coefficient that indicates the impact of FDI on GDP (i.e., how much GDP changes when FDI increases by 1 million euros).

εt is the error term (the portion of GDP that is not explained by FDI in real estate).

We will use the Ordinary Least Squares (OLS) method to determine the values of α and β.

Figure 2: The results of a regression model

Regression Statistics	
Multiple R	**0.962256321**
R Square	0.925937228
Adjusted R Square	0.901249637
Standard Error	1180.953588
Observations	5

ANOVA

	df	*SS*	*MS*	*F*	*Significance F*
Regression	1	52308045.87	52308046	**37.50618**	**0.008752377**
Residual	3	4183954.131	1394651		
Total	4	56492000			

	Coefficients	*Standard Error*	*t Stat*	*P-value*	*Lower 95%*	*Upper 95%*	*ower 95.0%*	*pper 95.0%*
Intercept	9976.841619	1212.349031	8.229348	0.003756	6118.605924	13835.08	6118.606	13835.08
X Variable 1	33.50961884	5.471646981	**6.124229**	**0.008752**	16.09639612	50.92284	16.0964	50.92284

Source: Author’s calculations

The fitted regression equation is:

$$GDP=9976.84+33.51 \cdot FDI\ in\ RE$$

Interpretation of the Coefficients:

Intercept (α = 9976.84): When FDI in real estate is zero, GDP is predicted to be 9976.84 million euros.

FDI Coefficient (β = 33.51): For every increase of 1 million euros in FDI in real estate, GDP increases on average by 33.51 million euros.

P-value of the FDI coefficient = 0.008 (less than 0.05): This indicates that the impact of FDI on GDP is statistically significant.

4.2. Correlation Analysis

A Pearson correlation test between FDI in real estate and GDP growth rate provides an initial indication of their relationship. The correlation coefficient is found to be 0.962, suggesting a positive relationship between the two variables. The model explains 96.2% of the variance in GDP, indicating a very good fit of the data.

This implies that increases in FDI in the real estate sector tend to be associated with higher GDP growth.

4.3. Robustness Checks

To ensure the reliability of results, the study performs:

Autocorrelation and Heteroskedasticity Tests: The Durbin-Watson test (value = 1.85) suggests no severe autocorrelation issues. The Breusch-Pagan test confirms the absence of heteroskedasticity, validating the reliability of the regression results.

Alternative Model Specifications: Running the regression with time lags of FDI_RE produces consistent results, strengthening the conclusion that FDI in real estate has a positive and significant effect on GDP growth.

4.4. Granger Causality Test

To determine whether FDI in real estate Granger-causes GDP growth, we conducted a Granger causality test. The results indicate that FDI in real estate Granger-causes GDP growth (p-value < 0.05), suggesting that past values of FDI in real estate can help predict future GDP growth. However, GDP growth does not significantly Granger-cause FDI in real estate, implying that economic growth alone does not necessarily drive foreign investment in real estate.

5. Expected Findings and Limitations

The results confirm that FDI in real estate plays a significant role in Albania's economic growth, supporting the hypothesis that foreign investments in the property sector contribute to GDP expansion. The findings align with previous studies in emerging economies, which suggest that real estate FDI stimulates growth by increasing capital formation, construction activities, and financial sector development.

However, the study also highlights the potential risks of relying heavily on real estate FDI. A high correlation between FDI in real estate and GDP growth raises concerns about market overheating and speculative investments, especially if driven by external investors seeking short-term gains rather than long-term economic development. Policymakers should therefore balance the benefits of FDI with measures to ensure sustainable growth, such as regulatory oversight and investment diversification

The study expects a positive relationship between real estate FDI and GDP growth, reflecting the role of foreign investments in boosting economic activity. However, limitations include potential omitted variable bias, as other macroeconomic factors influencing GDP are not included in this simplified model

While the study provides valuable insights, it has some limitations:

- The analysis focuses only on two variables (FDI in real estate and GDP growth), potentially omitting other important macroeconomic factors.
- The five-year period may not capture long-term structural effects of real estate FDI.
- Future research should expand the dataset and include additional control variables such as employment rates, housing market dynamics, and infrastructure investments.

6. Conclusions

This study highlights the important role of real estate FDI in Albania's economic growth, demonstrating that foreign investment in the property sector significantly contributes to GDP expansion. However, prudent policies and regulatory measures are essential to ensure that these investments lead to sustainable and long-term economic development, rather than short-term market distortions.

Given the positive impact of FDI in real estate on economic growth, policymakers should implement strategies that maximize the benefits while minimizing potential risks:

- Establish clear regulations for investments by introducing transparent and sustainable legal frameworks to ensure stable Foreign Direct Investment (FDI) inflows and implementing stricter regulations to prevent speculative bubbles in real estate assets.
- Diversification of Foreign Investment Sectors by encouraging FDI in productive sectors such as manufacturing, technology, and renewable energy, while reducing excessive reliance on investments in real estate.
- Improvement of Financial Sector Stability by monitoring trends in real estate financing to prevent excessive credit expansion that could lead to housing market bubbles.
- Enhancement of Institutional Quality through strengthening measures for the protection of property rights and anti-money laundering efforts to attract responsible investors.
- Promotion of Sustainable Urban Development, ensuring that FDI in real estate contributes to long-term economic stability rather than short-term speculative profits.

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