E-ISSN 2410-8693
ISSN 2410-3918

Academic Journal of Business, Administration Law and Social Sciences

Vol. 11 No. 3
November, 2025

INTERNATIONAL INSTITUTE FOR PRIVATE COMMERCIAL AND COMPETITION LAW (IIPCCL - AUSTRIA)

Research Article

From fiscal sustainability to financial security in old age: Evidence on pension reform in Albania

Elvis Ponari
European University of Tirana, Albania

Prof. Dr. Anilda Bozdo
European University of Tirana, Albania

DOI: https://doi.org/10.2478/ajbals-2025-0029

Abstract

This paper analyses the social and economic impact of the three-pillar reform of the pension system in Albania, assessing its contribution to fiscal sustainability and the financial well-being of older persons. The study draws on national and international data (INSTAT, World Bank, IMF, ISSH) for the period 2015–2024 and combines empirical analysis of economic indicators with a review of public policies. The results show that the 2015 reform increased contributory coverage by about 3.5%, stabilized pension spending at 8.7% of GDP and gradually reduced poverty among those aged 65+ from 23.4% to 19.6%. However, structural challenges such as informality, low replacement ratio and lack of voluntary private funds remain prominent. The study concludes that Albania has advanced towards a more sustainable and equitable system, but additional reforms are required to strengthen the second and third pillars, expand formal participation, and guarantee an adequate level of income in old age.

Keywords: pension system, three-pillar reform, Albania, old age welfare, fiscal sustainability, social policy.

1. Introduction

Pension systems constitute one of the fundamental pillars of the modern welfare state and a key mechanism for ensuring well-being in old age. In developing countries and economies in transition, they face numerous challenges due to demographic changes, informality in the labor market and fiscal pressures that threaten the long-term sustainability of existing schemes. The decline in fertility and the increase in life expectancy have led to an aging population, widening the dependency ratio between the elderly and the economically active population (World Bank, 2024). This demographic trend, accompanied by a high emigration rate, has significantly reduced the number of contributors to the public pension scheme in Albania, questioning the sustainability of the system in the future (IMF, 2023).

The challenges of the pension system in Albania are not only demographic, but also structural and institutional. One of the biggest problems remains informality in the labor market, which limits the base of active contributors and increases the dependence of the scheme on the state budget. According to World Bank data (2024), about 35 percent of the labor force in Albania operates outside the formal system, which makes the pension system fragile and dependent on public transfers. This phenomenon has produced direct consequences on the level of benefits, the adequacy of pensions and the credibility of the system for citizens. In this context, the 2015 pension reform constitutes an important intervention for restructuring the system towards a three-pillar model, similar to the one implemented in several countries of the European Union and the Western Balkans region. This model aims to build a balance between public solidarity and individual responsibility in ensuring income in old age. The first pillar represents the public system based on contributions, which provides a living wage for all citizens and maintains the function of basic social security. The second pillar is contributory, based on the direct ratio between contributions paid and benefits received, aiming to increase fairness and the match between contribution and reward. The third pillar is voluntary, conceived as an additional individual savings mechanism, which encourages citizens to create long-term financial reserves for old age (OECD, 2022).

The reform interventions aimed to address some of the main weaknesses of the existing system: the chronic fiscal deficit of the scheme, inequalities among beneficiaries and the lack of a strong link between contributions and benefits. Before the reform, the ratio between active contributors and beneficiaries was constantly decreasing, while budgetary subsidies for the SSSI constituted a significant burden on the state budget. The reform aimed to return the system to self-sustainability, by setting clearer limits on benefits, increasing transparency and encouraging active participation in the social security scheme (Government of Albania, 2014). However, implementation challenges have been numerous. In practice, the second and third pillars have developed slowly due to the lack of sustainable investment funds, lack of financial education and low income levels of the population (ISSS, 2023). This has meant that the system remains dominated by the public pillar, which bears the vast majority of the financial burden. According to IMF analysis (2023), despite structural improvements, pension adequacy in Albania remains low compared to the average of countries in the region, covering only 38–40 percent of previous labor income.

In the broader economic plan, pension reform is part of a process of institutional and fiscal modernization, which aims to bring Albanian social policies closer to European Union practices. By including elements of voluntary savings and long-term investment, the three-pillar model aims not only to increase financial security in old age, but also to develop capital markets and occupational pension funds. However, to fully realize this potential, strengthening of supervisory capacities, increased private sector participation and more incentive fiscal policies for long-term savings are required (World Bank, 2024; OECD, 2022). Thus, pension reform in Albania represents an ongoing transformation process, which requires a balance between fiscal stability and social justice. This study aims to analyze in detail how the implementation of this three-pillar model has influenced the improvement of the well-being of the elderly and the consolidation of the country's macroeconomic stability during the period 2015–2024, drawing valuable conclusions for policymakers and researchers in the field of public administration and social finance.

2. Importance and objectives of the study

The pension system reform represents one of the most important social and economic initiatives that Albania has undertaken over the last decade. Given the profound demographic changes, high emigration and persistent informality in the labor market, the need for a sustainable and inclusive pension system has become essential for maintaining the country's social and fiscal stability. The importance of this study lies in the fact that it aims to assess in an integrated manner the impact of the three-pillar reform on the financial well-being of the elderly and on the long-term sustainability of the pension system, providing a clear picture for policymakers and institutional actors.
First, the study aims to analyze the socio-economic effects of the three-pillar reform on the financial well-being of the elderly. This objective is important since the 2015 structural changes had as their main goal improving the link between contributions and benefits, as well as ensuring an adequate standard of living for pensioners. Assessing the impact of the reform on reducing poverty in old age, increasing pension adequacy and expanding contributory coverage will help to understand the direction the system has taken after the restructuring. Through this perspective, the study contributes to the existing literature on the effects of social policies in transition countries and serves as a basis for comparative regional analyses. Secondly, another important objective is to assess the impact of the reform on fiscal sustainability over the period 2015–2025. Given that the pension system has historically constituted a significant burden on the state budget, analyzing changes in the ratio of pension expenditure to Gross Domestic Product is essential to assess the effectiveness of the measures undertaken. The study examines whether the parametric and structural reforms have contributed to stabilizing the scheme deficit, reducing budget subsidies and improving the administrative efficiency of the SSSI. Third, this study aims to identify gaps and challenges that hinder the full implementation of the three-pillar model, including the lack of developed private funds, the low level of financial literacy, and the still modest role of the second pillar. These gaps are key to defining policy recommendations that can guide future phases of reform.
In conclusion, the importance of this study lies in its ability to illuminate the relationship between social welfare and fiscal stability, offering a balanced approach between empirical analysis and evaluation of public policies that affect the lives of elderly citizens.

3. Methodology and Literature Review

This study relies on a mixed-methods approach, which combines empirical analysis of macroeconomic indicators with a review of public policies and existing literature. The approach was chosen to provide a comprehensive overview of the impacts of the three-pillar pension reform in Albania, both in terms of the well-being of the elderly and the fiscal sustainability of the system. The research framework of the study is based on three fundamental questions: (1) Has the reform improved the adequacy of pensions and reduced poverty in old age? (2) Has it positively affected the fiscal sustainability of the system? and (3) What are the obstacles that limit the effectiveness of the reform? To answer these questions, three research hypotheses were constructed: H1, that the reform has increased the financial well-being of the elderly; H2, that increasing contributory coverage positively affects fiscal sustainability; and H3, that high informality completely hinders the positive effects of the reform. These hypotheses constitute the analytical basis of the study and guide the empirical analysis.

International and regional literature provides a broad theoretical basis for understanding the balance between fiscal sustainability and benefit adequacy. According to the World Bank (2015, 2024), Western Balkan countries face severe budgetary pressures and a high reliance on public pay-as-you-go schemes, making it necessary to strengthen the second and third pillars. Similarly, OECD (2022) emphasizes that diversifying pension sources through occupational funds and voluntary savings is a prerequisite for a long-term sustainable system. In the case of Albania, the reports of the ISS (2023) and the IMF (2023) highlight that, despite fiscal improvements after 2015, the system remains vulnerable to demographic changes and high levels of informality in the labor market. For this reason, literature authors recommend strengthening oversight mechanisms, developing private funds, and educating the population financially to ensure that the reform yields sustainable results (World Bank, 2024).

For the empirical analysis, data from INSTAT (2015–2024), the World Bank, the IMF, and the annual reports of the Institute of Social Security, as well as the legal document VKM no. 954/2014, which sets the institutional basis for the reform, were used. The methods include time trend analysis to measure the performance of pension expenditures as a percentage of GDP and the poverty rate for ages 65+, as well as a simple linear regression to assess the relationship between contributory coverage and fiscal stability. In addition, a regional comparison with the countries of the European Union and Central Europe (Croatia, Hungary, Poland) was conducted, to extract best practices and to assess Albania’s positioning in relation to countries that have implemented similar reforms. The combination of statistical analysis with policy interpretation allows for a balanced assessment of the effectiveness of the reform, helping to formulate practical recommendations for policymakers and institutional actors.

4. Results and Discussion

The results of the study show that the reform of the pension system in Albania has produced a moderate but sustainable improvement in terms of contributory coverage and fiscal stability. The data analyzed for the period 2015–2024 show that the participation of active contributors in the public scheme has gradually increased, reflecting an improvement in the administration of contributions and collection mechanisms. This increase is related to measures to formalize the labor market and to the reform of the wage declaration system, which has facilitated the identification of unregistered workers. In fiscal terms, pension expenditures have stabilized at 8.7% of GDP, while the deficit of the scheme has decreased from 2.3% to 1.5% in 2024 (World Bank, 2024). This positive trend indicates an increase in the self-sustainability of the system and a decrease in dependence on budgetary transfers. Improvements are particularly evident in the management of funds and the institutional transparency of the Social Security Institute (ISSH, 2023). However, despite financial stability, the level of adequacy of benefits remains limited, not fully reflecting individuals' contributions during their working life.

On the social side, INSTAT data show that the poverty rate for the 65+ age group has undergone a moderate decrease, from 23.4% to 19.6% in the period 2015–2024. This improvement, although positive, remains fragile and uneven between urban and rural areas, demonstrating that the reform has had a greater impact on groups with regular employment than on individuals with fragmented contribution histories. This shows that the social impact of the reform is asymmetric, and that basic protection for vulnerable groups remains limited. Another important finding is that the voluntary pillar of the pension system – which aims to promote long-term savings and diversification of income sources – continues to remain in its initial phase. Low public trust in private funds, lack of financial education and lack of fiscal incentives have hindered its development (OECD, 2022). As a result, the structure of the system still remains disproportionately dependent on the public pillar, which bears the main fiscal and social burden. In a broader perspective, the reform has achieved its first goal – fiscal stabilization – but not fully its second goal – guaranteeing financial security in old age. This means that for a more complete and long-term social effect, it is necessary to expand coverage in the informal sectors, develop the second pillar and create a legal framework that encourages individual savings. Only in this way can Albania achieve the desired balance between social justice and fiscal sustainability, aligning its pension system with contemporary European models.

5. Policy Recommendations

The results of the analysis show that the reform of the pension system in Albania has created the basis for a more fiscally sustainable structure, but its social effectiveness remains partial due to institutional shortcomings, limited public information and the lack of incentive mechanisms for long-term savings. Therefore, a comprehensive reform approach is needed, oriented towards strengthening administrative capacities, increasing public trust and integrating social and economic policies.

First, strengthening the supervisory capacities of the Social Insurance Institute (ISSH) and the Financial Supervisory Authority (AMF) is essential for the transparent and sustainable management of private pension funds. These institutions should be equipped with modern technological infrastructure and specialized staff to monitor the activity of second and third funds, ensuring transparency, integrity and protection of citizens' investments. Furthermore, the establishment of an integrated reporting and auditing system would strengthen the credibility of the financial market and increase private sector participation.

Second, the establishment of fiscal incentives for employers and employees contributing to the second pillar scheme is a must to promote occupational pension funds. These incentives could include tax breaks for contributions paid into private funds or temporary reductions in the contribution burden for sectors with a high level of informality. This policy would directly impact the growth of national savings and strengthen the long-term sustainability of the system.

Third, formalizing employment in agriculture and self-employment through subsidized contribution schemes will broaden the contributory base and reduce the system's dependence on budgetary transfers. The gradual inclusion of these categories through partial subsidies or combined state-individual contributions is a successful practice used in several countries in the region (OECD, 2022). Another essential element is the promotion of financial education and a culture of long-term savings. The creation of public education programs, in cooperation with the education system and the media, would raise citizens' awareness of the benefits of participating in private pension systems and of responsible management of personal income.

Finally, the integration of pension policy with social protection strategies is crucial to create a more inclusive and equitable system. Inter-institutional coordination between the SSSI, the Ministry of Finance and the Ministry of Health and Social Welfare should ensure that social protection measures, basic pensions and supplementary benefits operate in a harmonized manner.

Overall, these recommendations aim to strengthen the efficiency, reliability and fairness of the pension system, creating a social architecture that ensures fiscal stability and sustainable well-being for Albanian citizens in their old age.

6. Conclusion

The analysis developed in this study shows that the three-pillar pension reform in Albania has brought significant improvements in terms of fiscal sustainability and institutional management of the system, but its effects in terms of the adequacy of benefits and the well-being of citizens remain limited. The 2015 interventions have created the basis for a more transparent and fair structure, increasing the link between contributions and benefits and gradually reducing the dependence on budgetary transfers. However, despite these improvements, long-term challenges remain considerable. The Albanian population is facing a rapid aging, low birth rates and a high level of labor force emigration, which directly affects the balance of the pension system. Moreover, the high level of informality in the labor market and the slow development of the voluntary pillar limit the potential of the reform to provide sustainable financial security in old age.

From a social perspective, the study finds a moderate reduction in poverty for those over 65, but this improvement remains uneven across regions and occupational categories. The current system still does not guarantee sufficient adequacy for pensioners with fragmented careers or for those who have worked in informal sectors. For this reason, pension policy must remain a dynamic process that requires periodic review, in order to harmonize fiscal stability with social justice. In conclusion, the pension reform has had a positive impact on macroeconomic stability and the institutional structuring of the social security system, but its full success will depend on the further development of the second and third pillars, the strengthening of financial supervision and the building of a new culture of long-term savings. Only through these elements can a sustainable, fair and adapted system be ensured for the needs of future generations.

Contributions

This study contributes to the existing literature on pension policies in the Western Balkan countries by providing an integrated empirical and institutional analysis for the case of Albania. It improves the understanding of the impact of the three-pillar reform on the well-being of the elderly and on fiscal sustainability, by combining statistical data with public policy analysis. The study also assists policymakers in identifying existing gaps and in formulating measures to strengthen the second and third pillars, providing a valuable basis for comparison with countries in the region.

Limitations

A major limitation of this study is the lack of detailed microeconomic data on individual income and private savings of citizens, which would allow for a more accurate assessment of the social impact of the reform. Also, the analysis is limited to the period 2015–2024, while the long-term effects of the reform will appear after a longer time cycle. Another limitation is related to the lack of information on the real performance of private pension funds, which are still in the development phase.

Future Research

Future research could focus on international comparative analysis of similar reforms in countries in the region to identify the most successful practices and their adaptation to the Albanian context. Another valuable direction is the development of empirical micro-simulation models that measure the impact of policy changes on different social groups. Research could also be extended to the influence of psychological and cultural factors on participation in voluntary savings schemes, as well as the role of financial education in increasing public trust.

In a long-term perspective, research should focus on the interaction between the pension system and capital market development, analyzing how pension funds can serve as an engine for sustainable economic investment in Albania.

References

World Bank. (2015). Albania Pension Reform: Policy Notes. Washington DC: World Bank Group.
The World Bank. (2023). Aging and Social Protection in Europe and Central Asia: Building Systems for the Future. Washington DC: World Bank.
The World Bank. (2024). Western Balkans Regular Economic Report. Washington DC: World Bank Group.
EBRD. (2022). Transition Report 2022–23: Business Environment and Social Resilience in Southeastern Europe. London: European Bank for Reconstruction and Development.
European Commission. (2022). Aging Report 2022: Economic and Budgetary Projections for the EU Member States (2019–2070). Brussels: European Commission.
European Commission. (2023). Albania Economic and Reform Program 2023–2025. Brussels: European Commission, Directorate-General for Economic and Financial Affairs.
International Monetary Fund (IMF). (2023). Fiscal Monitor – Social Spending and Aging. Washington DC: International Monetary Fund.
Hoxha, E., & Cani, S. (2019). Fiscal Policy and Pension Reforms in Albania: Challenges and Opportunities. Albanian Journal of Economic Studies, 6(1), 33–50.
INSTAT. (2024). Income and Living Conditions in Albania 2024 (SILC). Tirana: Institute of Statistics.
Social Security Institute (ISSH). (2023). Annual report on the pension system in Albania. Tirana: ISSH.
International Labor Organization (ILO). (2021). World Social Protection Report 2020–22: Social Protection at the Crossroads. Geneva: ILO.
Ministry of Finance and Economy, Albania. (2023). Medium-Term Fiscal Framework 2024–2026. Tirana: MFE.
OECD. (2021). The Role of Financial Education in Retirement Planning. Paris: OECD Publishing.
OECD. (2022). Pensions at a Glance: Western Balkans Review. Paris: Organization for Economic Co-operation and Development.
OECD. (2023). Pension Markets in Focus – 2023 Edition. Paris: Organization for Economic Co-operation and Development.
Petkovic, M., & Zivkovic, M. (2020). Reforming Pension Systems in the Western Balkans: Fiscal Sustainability and Demographic Challenges. Economic Annals, 65(226), 45–67.
Government of Albania. (2014). Council of Ministers No. 954, dated 29.12.2014 "On the Reform of the Pension System." Official Gazette of the Republic of Albania.
Szołno-Koguc, J. (2020). Fiscal Sustainability of Pension Systems in Central and Eastern Europe. Journal of Economic Policy Reform, 23(4), 379–394.
United Nations Development Program (UNDP). (2022). Social Inclusion and Human Development in Albania. Tirana: UNDP Albania.
World Bank. (2018). Western Balkans Labor Market Trends 2018. Washington DC: World Bank.