

# **From Reforms to Ruin: The Pyramid Schemes Crisis and its Impact on Albania's Transition**

**Adelina Nexhipi, Erjon Nexhipi**  
*"Fan S. Noli" University, Korce, Albania*

## ABSTRACT

The collapse of the communist dictatorship in Albania catalysed a series of profound transformations regarding the economic, political, institutional, legal, and social dimensions. These reforms were often rolled out haphazardly, lacking a coherent strategy, and were marred by intense political contention, pervasive corruption, inefficiencies, and deficits in transparency and accountability. The pace of change was swift and intricate, introducing phenomena that were previously unfamiliar to the Albanian populace, with legal and institutional frameworks frequently lagging behind in their responses. From the onset of Albania's political transition, informal monetary exchange markets and money lending operations thrived, with state authorities generally displaying a degree of tolerance towards these activities. While some of these lending entities were registered as legal businesses or operated under the guise of foundations, they lacked the necessary licenses for conducting banking transactions. Their operations expanded broadly and persisted until they collapsed in 1997, precipitating a crisis. The failure of these pyramid schemes was not merely an economic collapse but also precipitated institutional breakdowns, a deep political crisis, and widespread social chaos that characterized the first half of 1997. This descriptive-analytical study aims to chronicle the events that unfolded in Albania at the end of 1996 throughout the first half of 1997. It seeks to analyse and evaluate, through a synthesis of facts and examination of political and legal stances, the underlying factors and resultant consequences of pyramid scheme failures. Furthermore, the study examines the deepening political crisis and the measures undertaken by both national and international institutions to address the situation. This analysis draws upon archival documents, official re-

ports from the International Monetary Fund (IMF), the World Bank, and the Bank of Albania, as well as academic studies, memoirs, interviews, and press coverage.

## Introduction

In 1991, following the collapse of the communist dictatorship, Albania embarked on a path of multifaceted transformations encompassing the economic, political, institutional, legal, and social spheres. The population emerged from the authoritarian regime “impoverished, shattered, numbed, bewildered, disoriented, and enraged.”<sup>1</sup> The national economy was mired in a profound crisis, characterized by a decline in social product and national income, diminished labour productivity, substantial deficits in the state budget, balance of payments issues, devaluation of currency, rampant inflation, a notable scarcity of consumer goods, liquidity challenges, and escalating unemployment rates. Nonetheless, the Albanian people were euphoric about their newfound freedoms, harboured no nostalgia for the past, looked forward with anticipation, and were eager for profound reforms. As it was the case for other former communist bloc nations, “democracy was perceived as synonymous with peace and economic growth, (...) as a single cure for all societal problems, as the only right answer to a number of unrelated questions, (...) all in one big and luxury package.”<sup>2</sup>

The first pluralist elections held on March 31, 1991, reaffirmed the success of the Albanian Labor Party (PPSH). The year 1991 was marked by a disconcerting disorganization of the society and of the state apparatus. The state was exceedingly weak, public order and citizen security were severely compromised, and social indiscipline was rampant. The combined pressures from the public and the op-

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<sup>1</sup> H. Hysa, *Një tranzicion i rrezikshëm*, 2011, Tirane, p. 54.

<sup>2</sup> I. Krastev, “Democracy and dissatisfaction”, in *1989 as a political world event. Democracy, Europe and the new international system in the age of globalization*, 2014, Routledge, London-New York, p. 46.

position, governmental instability, and the inability of the PPSH to adequately address the country's dire situation led to the calling of early elections.

After securing the victory in the parliamentary elections on March 22, 1992, the Democrats appointed Aleksander Meksi to head the first non-communist Albanian government. However, Sali Berisha, who had served as the chairman of the Democratic Party (DP) and was the newly elected president, continued to be the most influential figure in Albanian politics. The Meksi government was confronted with daunting challenges. "establishing democratic institutions and structures for a market economy, alongside building a state governed by the rule of law, reforming the judicial system, and combating corruption and crime."<sup>3</sup> These endeavours were pivotal for transitioning Albania from a rigidly controlled communist regime to a more open, democratic, and market-oriented society.

The overhaul of legal and economic frameworks was critical to support the new political landscape and ensure the stability and integrity of the emerging democratic state. However, the reforms were frequently rolled out without a cohesive strategy, and were marred by intense political debates, widespread corruption, and a notable lack of efficiency, transparency, and accountability. The sociologist Kosta Barjaba describes Albania during the years 1992-1997 as "a democracy without institutions, development without production structures, chaotic freedom with no political and human rights, and a system where political, physical, and moral violence were the first and the last word."<sup>4</sup> The situation deteriorated significantly towards the end of 1996 with the onset of the pyramid schemes crisis. The incapacity of public institutions and of the Albanian political class to effectively address the financial crisis precipitated by the collapse of these pyramid firms plunged the country into a deep political and institutional crisis as well as into social chaos. This turmoil persisted throughout the first half of 1997, with lingering effects for an extended period.

<sup>3</sup> V. Duka, *Historia e Shqipërisë 1912-2000*, 2007, Kristalina-KH, Tiranë, p. 344.

<sup>4</sup> K. Barjaba, "La ribellione albanese: motivazioni regionali o politiche?", in E.C. del Re (ed.), *Albania punto a capo*, 1997, Edizione SEAM, Rome, p. 212.

The objective of this descriptive-analytical study is to describe the sequence of events that unfolded towards the end of 1996 and throughout the first half of 1997, to analyse and assess the precipitating factors and the resulting impacts of the failure of pyramid schemes, and to examine their influence on the ensuing political crisis. Additionally, this study will scrutinize the decisions and actions undertaken by public and international institutions in response to the crisis. By rigorously analysing both factual data and the political and legal responses to the crisis, the study aims to achieve several specific objectives:

1. Event chronology: identify and document the principal events before, during, and after the pyramid schemes crisis to set up a detailed chronological framework of the crisis.
2. Decision and attitude evaluation: evaluate the responses, strategies, and overall attitudes of public institutions and political parties as they confronted the crisis, assessing their efficacy and strategic coherence.
3. Causal and impact analysis: investigate the underlying causes and the broad-ranging consequences of the 1997 crisis, considering both immediate and long-term effects on the Albanian political landscape and society.

Understanding the way the Albanian political class addressed the 1997 crisis offers invaluable insights into the nature and dynamics of Albania's transition period. This analysis will not only illuminate the immediate reactions to the crisis but also elucidate the broader systemic challenges encountered during the nation's transition.

The political transition period in Albania has been extensively analysed by both Albanian and international scholars such as Elez Biberaj, Valentina Duka, Daut Gumeni, Miranda Vickers, James Petifer, and Fred C. Abrahams, among others. Memoirs of participants in the events were also published, including Bashkim Fino, Mero Baze, Prec Zogaj. Additionally, reports from the European Union, Venice Commission, Council of Europe, OSCE, World Bank, Bank of Albania and IMF are of paramount importance. These documents

not only provide a broader context for understanding the pyramid schemes activity and the 1997 crisis but also delve into specific analyses of the dimensions and factors contributing to the pyramid schemes in Albania. Noteworthy contributions to this analysis have been made by scholars such as Chris Jarvis, Dirk Bezemer, Skreb, Kraft, Smoki Musaraj.

In addition to the sources mentioned above, this study has also utilized archival documents from the Central State Archive, the Historical Archive of the Ministry of Foreign Affairs, and the Central Archive of the Armed Forces. Press articles from 1996 – 1997, including daily publications from *Rilindja Demokratike* (RD), an organ of the Democratic Party; *Zëri i Popullit* (ZP), published by the Socialist Party; and *Koha Jonë* (KJ), associated with the Democratic Alliance Party, have been instrumental. These articles reflect the official stance of the political parties during the period under review and provide an additional layer of narrative to the official documents and scholarly analyses.

The crisis of 1997 stands out as the most profound crisis faced by the Albanian populace since the fall of the dictatorship. The sequence of events, underlying factors, ensuing consequences, and the errors committed during this tumultuous period have not yet been thoroughly examined. This gap in scholarship indicates a critical need for an extensive and detailed academic inquiry to fully understand and document the complexities of this significant episode of the Albanian history.

## **1. Democratic government - reforms and problems**

### *1.1 Institutional and legislative reforms - political situation*

Albanians were entirely unprepared to confront the historic challenges associated with the sweeping transformation from one system to another, nonetheless, demonstrated patience with the costs of reforms, driven by a fervent desire to sever ties with communism. The emergent political class bore the responsibility of facing these

challenges and making pivotal decisions. From 1992 to 1996, continuous efforts were undertaken to establish a new legal framework to support the profound changes being implemented. These transformations were rapid and multifaceted, introducing phenomena previously unknown to the Albanian populace, with legal and institutional responses often lagging behind.

In addition to the legal reform, significant strides were made toward institutional reforms. The structures of the totalitarian state were dismantled, and new institutional frameworks were established. This institutional reform touched upon the legislative, executive, and judicial branches, extending even to the smallest administrative units. Albania endeavoured to establish a parliamentary democracy characterized by a balanced separation of powers, in which the Parliament was slightly more predominant over the other branches. However, the President was endowed with broad and substantial powers, and the executive was granted considerable authority over the judiciary. This configuration created ambiguities that challenged the judiciary's capacity to dispense justice effectively.<sup>5</sup>

During the period from 1992 to 1996, Albanian political life was marked by escalating conflicts among political parties. The discourse between the government and the opposition primarily revolved around issues such as corruption, authoritarianism, the politicization of public administration, marginalization of the opposition, targeting of political opponents, and the trial and sentencing of key members of the Socialist Party, (SP) including its chairman, Fatos Nano. Particularly intense debates emerged in 1994, notably concerning the referendum on the Constitution. In what was seen as an unconstitutional process, it was decided that the draft constitution, prepared by a parliamentary commission, would be subjected to a popular referendum. SP voiced strong opposition to the unconstitu-

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<sup>5</sup> Freedom House, *Nations in transit 1997 - civil society, democracy and markets in East Central Europe and the newly independent states*, Transaction Publishers, New Brunswick, USA and London, UK, p. 32.

tional procedures used to approve the draft constitution and its provisions that they argued bore an anti-democratic character. Notable among these were the chapters on presidential powers, which granted extensive authority, and on judicial powers, which lacked provisions to ensure independence and effectiveness.

The public referendum held on November 6, 1994, failed to secure approval for the adoption of the constitution. This outcome had a profound impact on the political landscape, intensifying partisan clashes and political polarization. SP interpreted the referendum result as a clear rejection of the Democratic Party's (DP) policies and continued to demand early elections. Moreover, the governing coalition was dissolved, and divisions within DP became more pronounced.

Following the referendum, President Berisha intensified efforts to organize an oppressive and authoritarian state apparatus, as noted by Italian historian, Roberto Morozzo della Rocca. Measures included increasing the number of police officers, revitalizing the secret police (SHIK), and purging the administration of individuals who were not fully aligned with government policies. State television, the only channel in the country, was transformed into the government's official mouthpiece. Furthermore, legal actions against opposition figures increased, and the judiciary was co-opted as an instrument of governmental power. These developments underscored a significant regression in democratic governance and in the rule of law in Albania.<sup>6</sup>

As the parliamentary elections of May 26, 1996, approached, the political conflict intensified significantly. It was during this period that SP felt politically marginalized due to the enactment of several laws perceived as anti-constitutional. Notably, the "Anti-Genocide Law" and the "Law on Verification of Public Figures", banning individuals who had been active during the communist era from holding public office for a defined period. These laws particularly

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<sup>6</sup> R. Morozzo Della Rocca, *Shqiperia rrenjet e krizes*, 2000, Shtepia e librit dhe komunikimit, Tirane, pp. 61-62.

impacted the opposition parties, especially SP, by declaring the ineligibility of 35 of its candidates.

Furthermore, the electoral law exacerbated and further polarized the political landscape. "The law is problematic because it restructured the electoral commissions to the government's advantage. President Berisha ordered changes in the electoral districts. The electoral law also granted the ruling party disproportionate airtime on television."<sup>7</sup> The division of electoral zones, criticized for being abusive, non-transparent, and unconstitutional,<sup>8</sup> also ignited intense political debate and controversy. These legislative actions contributed to a deepening of political divisions, setting the stage for a highly charged electoral environment.

President Berisha's decision to lead the Democratic Party's electoral campaign was perceived as a contravention of the Main Constitutional Provisions, which stipulated that the President should embody national unity, and that the presidential role was incompatible with any other function. The election campaign unfolded under challenging political conditions, which intensified on Election Day. Throughout the day, numerous legal, procedural, and administrative irregularities were observed. SP, Democratic Alliance Party (DAP), and the Social Democratic Party (SDP) collectively boycotted the elections three hours before the polls closed, citing blatant violations of the electoral law by DP and the electoral bodies. Consequently, they withdrew their candidates, commission members at all levels, and observers.

International observers publicly stated that democratic standards were not met and that there were political interventions in the electoral process. They noted that 32 out of 79 articles of the Election Law were breached.<sup>9</sup> The elections, described as a regression in the

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<sup>7</sup> International Republican Institute (IRI), *Observation Report on the Albanian Parliamentary Elections of May 26, 1996*, Washington D.C., 1996, p. 16.

<sup>8</sup> IRI, *Observation of the parliamentary elections held in the Republic of Albania*, 26 May 1996, pp. 17-18.

<sup>9</sup> OSCE/ODIHR, *Observation of the parliamentary elections held in the Republic of Albania, May 26 and June 2, 1996*, June 18, 1996, p. 2.

democratization process, exacerbated the political crisis in Albania and diverted focus from other significant issues. SP and its allies refused to acknowledge the election results, boycotted Parliament, and escalated the political conflict beyond the parliamentary framework. Consequently, the Parliament functioned essentially as a one-party system, and the new government was marked by a lack of political initiative.

### *1.2 Economic reforms and the emergence of pyramid schemes*

Similarly to many Central and Eastern European nations, Albania underwent a period of “shock therapy” of the economic sector. This approach entailed comprehensive reforms aimed at dismantling the erstwhile socialist system and rapidly transitioning to a market economy. The stabilization program was initiated promptly, which included liberalizing prices, aiming to balance the budget deficit, reforming monetary policies, liberalizing foreign trade, overhauling the privatization structure, establishing a new tax system, and introducing a modern customs system. Non-viable enterprises were closed, and the privatization and de-collectivization process in rural areas was started. The liberalization process extended to foreign trade as well, fostering opportunities for integrating the Albanian economy into the global market. The adoption of an open-door policy mandated that Albanian products adhere to international standards. However, the global market competitiveness of these products was initially low, which contributed to a negative balance in foreign trade. Within the ambit of economic reforms, the privatization process was a critical and unavoidable measure. This initiative was designed to foster conditions conducive to a market economy by divesting state-owned assets as much as possible. Privatization was regarded as an essential precursor to establishing a market democracy, predicated on the assumption that it would yield widespread benefits in the long term.

Economic reforms in Albania ushered in a series of social challenges, including elevated unemployment rates, increased prices for

consumer goods, decreased incomes, rising living costs, high poverty rates, and growing social inequality. The trajectory of economic development remained precarious; the nation continued to rely heavily on agriculture, with minimal investments directed towards the productive sectors of industry and infrastructure. These reforms were also marred by inflation and a significant budget deficit. From a fiscal perspective, a predominantly flat-rate tax system was implemented. Weak public institutions struggled to exert financial control over the private sector, leading to widespread fiscal evasion and informality.

The banking system remained predominantly under state control and was characterized by “a lack of experience and professionalism. It suffered from high employee turnover, inflexible credit policies, and delays in liquidation and payments, among other issues.”<sup>10</sup> Public banks attempted to maintain interest rates higher than the inflation rate. The escalation in non-performing loans compelled banks to impose stringent criteria on loan issuance, resulting in a supply that fell short of market demand. In the absence of developed money markets and a stable real estate sector, individuals and businesses in Albania frequently resorted to informal market transactions. This reliance on informal transactions was facilitated by a weak state banking sector, a nascent credit market, and the pressing need for funds to fuel private sector activities, initially leading to borrowing from family and relatives, which then expanded further. As a result, the Albanian economy became predominantly dependent on cash transactions.

The poor infrastructure of state institutions, a lack of structural reforms in the banking sector, the inadequacies of the formal financial system, the prevalence of large amounts of foreign currency within the country, underdeveloped legal frameworks, political in-

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<sup>10</sup> S. Llaci, “Bankat dhe financimi i biznesit”, in *Ekonomia dhe tranzicioni*, V, No. 1 (15), 1998, p. 16. Gjallica, VEFA, Populli, Demokracia Popullore-Xhaferri, Kamberi, Cenaj, Silva, Malvasia, Kambo, Grunjasi, Dypero, Bashkimi, Beno, Pogoni, B&G, Kobuzi, Arkond, A.Delon, Agi, M.Leka Company, Global Limited Co., Çashku, Sudja.

terference in financial sectors, and insufficient coordination among supervisory institutions and the government jointly facilitated the emergence and growth of pyramid schemes in Albania. From 1991 to 1997, 24 investment companies or foundations operated what would eventually be revealed as pyramid schemes, amassing deposits amounting to \$1.2 billion USD, equivalent to half of the country's GDP, with an estimated number of creditors amounting to 2 million out of a population of 3.2 million. This significant engagement highlights the profound impact and extensive reach of these schemes within the national economy.

The informal exchange market and money lending activities were largely overlooked by public authorities in Albania. "According to both national officials and international observers, including the International Monetary Fund (IMF), these informal lending companies were perceived as relatively benign and were even thought to contribute positively to economic growth, especially given the significant shortcomings of the formal banking sector."<sup>11</sup> Many of these money-lending enterprises were registered as legal entities or foundations; however, they lacked the proper licenses to conduct formal banking transactions. Despite this, the existing legal framework was insufficient to effectively regulate the lending activities of these companies operating under the provisions of the Civil Procedure Code (Civil Code 1994, Articles 1050 and 1051), which expressly envisaged money lending procedures but failed to provide any safeguards for such activities. Moreover, these companies were not subjected to financial audits and were not recognized as profit taxpayers.

In their financial reports from 1994 and 1995, the World Bank and the IMF described the money-borrowing companies in Albania that invested funds but did not issue loans as participants in an informal lending market. However, they failed to recognize the inherently pyramidal nature of these activities. Dirk Bezemer (Professor of Economics, Groningen University) has criticised both institutions

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<sup>11</sup> C. Jarvis, *IMF Survey*, IMF Volume 28, 1999, p. 7.

for their substantial role in the growth of pyramid schemes in Albania, stating, "Both institutions were actively involved in Albanian developments and lauded the most successful political reforms in Albania. They influenced economic policies and had the opportunity to express their concerns."<sup>12</sup>

On February 22, 1996, the Albanian Parliament enacted the Law on "The Banking System in the Republic of Albania," which stipulated that only banks were entitled to accept family deposits, open-ended deposits, and deposits with a maturity of 12 months or less. Following this law, the governor of the Bank of Albania declared the activities of the borrowing companies illegal, yet the General Prosecutor asserted that the law did not apply to these entities. Throughout 1996, the Governor of the Bank of Albania repeatedly informed the president and the prime minister about the potential repercussions of these companies' operations, but no institutional action was envisaged.

During the same year, the press reported the collapse of several money-borrowing companies, such as "Beci" in Gjirokastra, with deposits estimated at about 200 million drachma; "Noba," also in Gjirokastra; "Limani" in Tepelena, which owed approximately 120 million lekë (about 110 thousand US dollars); and "Arkond" located in Selice, Vlora, which had 1000 depositors and 2.6 billion lekë (about 2.4 million US dollars) in loans. Other companies like 'Grunjasi' and 'Pogoni' faced legal charges from deceived depositors, ultimately leading to the company owners fleeing the country. Despite these financial deceptions, the lending activities of borrowing companies or foundations neither ceased nor diminished.

During the second half of 1996, the World Bank and IMF frequently issued warnings about the risks threatening Albania. Carlos Elbirt, the then World Bank representative in Albania, remarked that "if any financial institution is allowed to collect and deposit money without proper authorization and close supervision by the Central

<sup>12</sup> D. Bezemer, "Post-Socialist Financial Fragility: The Case of Albania", in *Cambridge Journal of Economics*, 2001, p. 28.

<sup>13</sup> D. Kola, "Fajdet shqiptare në opinionin e ekspertëve të Bankës Botërore", in *Zëri i Popullit*, 265, November 9, 1996, p. 5.

Bank of Albania, then the public will end up being deceived.”<sup>13</sup> On October 5<sup>th</sup>, following the annual meeting with the World Bank and IMF in Washington, the Minister of Finance, Ridvan Bode, issued a warning about the risks to public deposits. However, this warning did not have the intended effect, and the Albanian public continued to invest their money in the borrowing companies as they had done before.

The IMF's warnings, despite its regular assistance to Albanian institutions, were arguably too late to avert the crisis. According to Jarvis, several objective reasons contributed to this delayed response:

- It was hard to distinguish between the legitimate informal market, which has been and continues to be beneficial for Albania, and the fraudulent schemes that masqueraded as investment funds.
- The pyramid schemes were fundamentally criminal organizations, and IMF does not engage in investigating criminal entities.
- IMF was cautious about publicly calling for investigations and the freezing of assets. While it has a responsibility to prevent significant financial crimes with macroeconomic consequences, it also has a duty to avoid unduly tarnishing the reputation of entities that might be legitimate.<sup>14</sup>

Bezemer contends that the IMF's assessments of a country's economic progress are predicated solely on macroeconomic indicators, which may present a deceptively stable view of an economy. He argues, “If economic performance is monitored exclusively through the observation of macro-economic variables, the development of fragile financial markets may go unnoticed.”<sup>15</sup>

Starting in September 1996, the domestic press, predominantly the left-wing and independent outlets, as well as foreign media, began extensively covering the issues related to the money-borrowing companies operating in Albania. These reports discussed the

<sup>14</sup> C. Jarvis, *IMF Survey*, Volume 28, No. 21, November 8, 1999, pp. 15-16.

<sup>15</sup> D. Bezemer, *Post-Socialist Financial Fragility: The Case of Albania*, p. 28.

economic effects, civic risks, and the urgent need for governmental intervention. In contrast, the right-wing press defended the government's stance and the actions of public institutions. They maintained that the lending activities were legally sanctioned and regulated by the Civil Procedure Code, asserting that Albanian citizens were free to manage their finances as they saw fit and were solely responsible for their decisions. The Minister of Finance characterized these lending activities as private transactions between lenders and borrowers, governed by the Civil Code, emphasizing that no public institutions were implicated in these dealings.<sup>16</sup> Meanwhile, the European Commission offered technical assistance to Albania to help address legal issues surrounding the regulation of pyramid schemes. However, according to Commissioner De Silguy, the Albanian authorities declined this offer.<sup>17</sup>

On November 20<sup>th</sup>, under pressure from international financial institutions, the Albanian Parliamentary Economic Commission, imposed transparency on money-borrowing companies to foster a credible environment for individuals who had invested in these entities. Subsequently, on November 21<sup>st</sup>, the Parliament enacted the law on the "Transparency of Lending Activities with Massive Participation of Albanian Citizens." This legislation established a supervisory non-parliamentary commission, functioning as an independent entity, tasked with overseeing the scope and scale of lending activities, ensuring compliance with civil legislation by the companies involved, safeguarding the rights and interests of participants, assessing the impact on the national economy, and providing recommendations to the Parliamentary Economic Commission. All entities engaged in lending activities were legally obligated to cooperate with the Supervisory Commission, which, along with the Parliamentary Economic Commission, was required to maintain confidentiality concerning the data acquired. The money-borrowing

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<sup>16</sup> S. Luku, "Në '97 nënshkruajmë marrëveshjen", in *Rilindja Demokratike*, 277, November 27, 1996, p. 2.

<sup>17</sup> Arkivi Historik i Ministrise se Puneve te Jashtme, Fondi: Bashkimi Evropian, V. 1997. D. 475, p. 8.

companies and foundations complied with the law and expressed their willingness to cooperate with the Supervisory Commission. Vehbi Alimuçaj, President of the "VEFA" Company, remarked that the Commission's oversight neither concerned nor hindered their operations.<sup>18</sup> However, the opposition criticized the law, arguing that it failed to ensure the transparency of the lending companies because the Commission was obligated to keep the data confidential.

## 2. The pyramid scheme crisis and its impact on Albania

### 2.1 *The pyramid scheme crisis*

"Sude", one of the foundations offering the highest interest rates, ceased distributing payments to depositors on November 9th, leaving them in a state of suspense and hope. Initially, this appeared to be an isolated issue concerning only the "Sude" Company, as other entities reassured the public that their deposits remained secure. However, by the end of December, similar problems emerged with "Xhaferri" and "Gjallica". The year 1997 commenced with the bankruptcy of "Malvasia", further escalating anxiety and doubt among the depositors of "Gjallica" and "Sude", as the deadlines for the return of deposits and interest to creditors were deferred once more.

On January 10<sup>th</sup>, the Central Bank of Albania mandated that banks facilitate daily disbursements of up to 30 million Leke (approximately 27 thousand US dollars) to their clients to help maintain inflation under control. This regulation hampered the ability of borrowing companies and foundations, which had their funds deposited in public banks, to fulfil interest payments. "Gjallica" and "Sude" continued to struggle with repaying depositors' interests, and initial difficulties also began to surface for "VEFA". These com-

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<sup>18</sup> D. Kola, "Ligji është i pranueshëm për kompanitë private", in *Zëri i Popullit*, 277, November 23, 1996, p. 7.

panies attributed their repayment challenges to the public banks, citing the imposed limitations as problematic.

As the initial issues with the money-borrowing companies surfaced, opposition parties laid the blame squarely at the feet of the Government. Neritan Ceka, President of DAP, sharply criticized the administration: "Sude, in reality, is the Albanian Government. We are witnessing an economy devoid of law, guarantees, and mercy, one that thrives on deception. Undoubtedly, the Government is responsible for the existence and operation of such institutions."<sup>19</sup> SP regarded these companies as byproducts of reckless governance by the ineptest individuals within DP, who cultivated a conducive environment for these "ghost companies". Under the Government's tacit protection, marked by its inactivity, these entities systematically deceived and defrauded citizens, who were lured by the "miracles" they were promised.<sup>20</sup> From the perspective of DP, the Government could not bear any responsibility, either legally or morally, for these issues. According to DP, governmental intervention was only justifiable when financial fraud was formally reported by the aggrieved parties to judicial authorities. The Government had never offered guarantees to the public, who entrusted their money to others in the form of loans, and it could not meddle in the civil relationships between private individuals.<sup>21</sup>

On January 15<sup>th</sup>, the bankruptcy of "Sude" was declared, revealing its incapacity to repay its creditors. Maksude Kadëna, the president of "Sude", admitted to having established a pyramid scheme that was no longer sustainable. This revelation triggered widespread protests by citizens who had lost their deposited funds. Demonstrations quickly spread to the cities of Tirana and Vlora, with protestors vocalizing their demands under chants of "We want our money" and

<sup>19</sup> N.Z., "Sudja realisht është vetë shteti shqiptar", in *Zëri i Popullit*, 300, December 21, 1996, p. 4.

<sup>20</sup> Editorial, "Qeveria sponsorizon pasigurinë e fajdeve", in *Zëri i Popullit*, 316, January 14, 1997, p. 1.

<sup>21</sup> E. Paloka, "Fajdet, shteti dhe opozita", in *Rilindja Demokratike*, 320, January 18, 1997, p. 3.

“Government of thieves.”<sup>22</sup> The public’s frustration escalated into confrontations with police forces in the streets. In the immediate aftermath, the Court of Justice of Tirana took swift action by arresting Maksude Kadëna, charging her with “cooperative theft by fraud.” At the time of her arrest, Kadëna possessed no bank accounts, and no cash had been seized by the police. The issue of reimbursing the creditors remained a formidable challenge.

Following the collapse of “Sude” on January 16<sup>th</sup>, 1997, the Council of Ministers made the decision to freeze the bank accounts of the foundations “Xhaferri” and “Populli”. According to the Minister of Finance, Ridvan Bode, this measure was taken in the interests of the depositors, who were given full guarantees that the funds seized by the state would be returned to them.<sup>23</sup> The deposits of both foundations held in public banks, which were frozen in favour of the citizens, were estimated to amount to 25.5 billion Lekë [approximately 225 million US dollars].<sup>24</sup> However, this figure did not fully capture the true scale of the amounts borrowed from the public, as a significant portion of the financial transactions had been conducted through informal channels, bypassing the banking system.

The response of public institutions to the imminent collapse of pyramid schemes in Albania was notably delayed, materializing only after the initial signs of failure became evident. According to Nikos Ziogas (who, at the time, served as the Director of the World Bank in Tirana), “the government, for political reasons, avoided informing the Albanian populace about the potential consequences of their ‘investment’ activities, while simultaneously allowing the ‘companies’ to continue operations. Additionally, the rest of the political forces in the country share a portion of the blame as they failed to adequately enlighten the ordinary citizen about the inherent risks associated with these ‘Pyramids’.”<sup>25</sup> The government did not initiate any measures,

<sup>22</sup> “Nga Tirana në Vlorë, revoltë e shqiptarëve”, in *Zëri i Popullit*, 318, January 16, 1997, p. 3.

<sup>23</sup> “Paratë e ngrira në Bankë janë të sigurta”, in *Rilindja Demokratike*, 320, January 18, 1997, p. 1.

<sup>24</sup> S.N., “Qeveria siguron paratë e qytetarëve”, in *Rilindja Demokratike*, 319, January 17, 1997, p. 1.

<sup>25</sup> N. Ziogas, *Albanian Crisis*, 3, [http://www.hri.org/MFA/thesis/spring97/albanian\\_crisis.html](http://www.hri.org/MFA/thesis/spring97/albanian_crisis.html), retrieved: 12. 07. 2017.

even after receiving warnings from IMF and the World Bank regarding the true nature of these lending companies. The scholar Miranda Vickers suggests that this inaction stemmed from President Berisha's reluctance to cause public frustration prior to the local elections in October 1996.<sup>26</sup> Dirk Bezemer argues that the government and DP actually benefitted from the pyramidal schemes: "The evidence clearly points to government involvement and officials' profiting from Ponzi schemes' growth. Probably, they recognized the destructive impact of Ponzi schemes but at the same time in the name of their vested interests they were not keen to discourage their further growth."<sup>27</sup>

Preç Zogaj, at that time one of the leading figures of the DAP, posits that the activity of the pyramid schemes was indirectly allied with the government, which "was unable to fulfil the people's demands for jobs and minimal wages, and hence was satisfied that part of them were trying to find solutions of their own."<sup>28</sup> For Skreb and Kraft, "The late reaction of the authorities was not only caused by an inadequate legal framework but broadly speaking it was a problem of governance i.e., of crisis management. The authorities reacted slowly and weakly. Links with the highest levels of government and corruption postponed an adequate reaction for some time. This delay not only allowed the schemes to grow but also delayed the seizure of remaining assets, which facilitated asset stripping."<sup>29</sup> An IMF survey indicated that "Controlling and closing down pyramids can be politically difficult – especially if politicians or other important people are subscribers to the scheme. Once they grow, the authorities may be increasingly reluctant to trigger their collapse,"<sup>30</sup> a scenario that appears to have unfolded in the Albanian context.

<sup>26</sup> J. Pettifer, M. Vickers, *Çështja shqiptare, riformësimi i Ballkanit*, 2007, Bota shqiptare, Tirane, p. 8.

<sup>27</sup> D. Bezemer, *Post-Socialist Financial Fragility: The Case of Albania*, p. 24.

<sup>28</sup> P. Zogaj, *Intuicionet e tranzicionit*, 1, 2009, UET Press, Tiranë, p. 274.

<sup>29</sup> M. Skreb, E. Kraft, *Financial crises in South East Europe causes, features and lessons learned*, 10, <https://www.researchgate.net/publication/2549551>, retrieved: July 12, 2017.

<sup>30</sup> IMF Survey, *IMF Advice Helps Fight Financial Fraud as Schemes Multiply*, 4, <http://www.imf.org/en/news/articles/2015/09/28/04/53/sopol021209a>, retrieved: 11. 08. 2017.

## 2.2 Political crisis, social anarchy

Due to the indifference of public institutions, the collapse of the pyramid schemes prompted widespread public blame towards the government. Citizens sought accountability within governing structures, as these are typically seen as representations of social compromise, responsible for addressing the issues faced by various groups and society at large. This sentiment was echoed even by the Bank of Albania, which stated, "It is known that economic regulatory policies are crafted and implemented by the authorities, and in this respect, it is fair to say that no effective action was taken."<sup>31</sup>

By January 1997, public protests had erupted, accusing the government of causing financial losses for many citizens. On January 16th, the closure of "Gjallica" Company's offices sparked a violent protest in Vlora, marked by anti-government sentiments. The unrest quickly spread to other cities including Tirana, Berat, Krujë, Shkodër, Kurbin, Korçë, Fier, and Gjirokastër, leading to clashes with police forces and injuries on both sides. Amidst this turmoil, the opposition recognized the protection of citizens' rights as a fundamental responsibility and organized a rally at Skanderbeg Square in Tirana on January 19<sup>th</sup>. This gathering was a call to action against the political and economic downfall, as exemplified by the pyramid scheme crisis. The opposition's demands were not only focused on addressing the fraud and police brutality associated with these schemes but also called for new parliamentary elections and the establishment of new democratic and legal institutions to extricate the country from its multifaceted crisis.<sup>32</sup> However, this protest by the opposition was deemed illegal by the police, leading to its prohibition and the subsequent use of physical force. The confrontations resulted in casualties, including the death of a protester. DP described the opposition's protest as an attempt by "leftist extremists to politically exploit people's suffering and misfortune."<sup>33</sup>

<sup>31</sup> Banka e Shqipërisë, *Buletini Ekonomik*, Volume 1, No. 3, 1998, p. 3.

<sup>32</sup> "Deklaratë e Kryesisë së PSSH", in *Zëri i Popullit*, 319, January 17, 1997, p. 2.

<sup>33</sup> "PS, parti e fatqeqwsisw", in *Rilindja Demokratike*, 320, January 18, 1997, p. 1.

On January 20<sup>th</sup>, a parliamentary session was convened to deliberate on the legal measures necessary to address the ongoing financial crisis and to support citizens who had lost their savings. President Berisha suggested social support initiatives including employment opportunities in the public or private sectors, provision of agricultural credits, and facilitation of investments. On January 21<sup>st</sup>, the heads of “Populli” and “Xhaferri” foundations, along with 118 clerks from these organizations, were detained on charges of “cooperative fraud.” Preliminary investigations conducted by the Transparency Commission revealed that both foundations operated as quintessential pyramid schemes, initiating activities without any foundational capital. The investigations further uncovered that both entities had contravened the laws and statutes under which they were registered, essentially transforming into organizations that extensively pursued material profit through fraudulent means. A couple of days later, Fitim Gërxhali, one of the presidents of “Gjallica”, was arrested following an analysis of the company’s documentation that indicated a clear pyramid scheme.

The collapse of “Gjallica” and the ensuing crisis of other similar enterprises showed the public that even those money-borrowing companies purporting to make investments were either completely or partially structured as pyramid schemes. Amid the chaos of these companies’ documentation, discerning their financial solvency was challenging; it was uncertain whether their operational profits could cover their debts. For certain entities, such as “Sude”, “Xhaferri”, or “Populli”, which possessed no tangible assets or investments, it became apparent that they were outright pyramid schemes.

The crisis triggered by the pyramid schemes underscored the prevailing political instability in Albania, which had been exacerbated by a lack of political dialogue since the 1996 elections and a parliamentary boycott by the opposition. The opposition parties capitalized on the financial crisis to advance their political demands. According to SP, the Meksi government was incapable of resolving the usury crisis as it was both responsible for and implicated in its escalation. Consequently, SP reiterated calls for the resignation of

the government, the establishment of a new technical government comprising experts, and the consensus of all political parties. The opposition proclaimed its intent to lead the legitimate popular protests "to fulfil its duty in service of the country and as a beacon of hope for the future."<sup>34</sup>

The popular protests escalated into violent riots, beginning in Lushnja on January 24<sup>th</sup>, where citizens clashed with police forces, attacked and set ablaze local institutional buildings, obstructed national roads, and briefly took Tritan Shehu, the Chairman of DP, hostage. In the days that followed, the violence spread to other towns including Berat, Vlorë, Tirana, Gramsh, Belsh, Fier, Korçë, Kavajë, Skrapar, Poliçan, and Memaliaj. The aftermath of these protests included 84 police officers wounded, 30 individuals detained by protesters, and material damages estimated at approximately 5 billion lekë (around 4.5 million US dollars)<sup>35</sup> President Berisha called the violence the "acts of manipulators who exploit the despair and misfortune of the citizens."<sup>36</sup> He urged the populace to remain calm and requested more time to resolve the crisis, assuring that the return of their money was guaranteed. The Parliament resolved that limited units of the Armed Forces of the Republic of Albania would support the Ministry of Interior Affairs in managing the situation, protecting public and governmental institutions, and ensuring the free movement on national roads.<sup>37</sup> President Berisha declined the Prime Minister's suggestion to impose a state of emergency.

DP and the government persisted in their endeavours to maintain control over the escalating situation. Zef Preçi, a prominent Albanian

<sup>34</sup> "Fajdet i solli në skenë politika e partise në pushtet", in *Zëri i Popullit*, 330, January 29, 1997, p. 4.

<sup>35</sup> A. Baçi, "Shqiptarë largohuni nga bandat", in *Rilindja Demokratike*, 328, January 28, 1997, p. 3.

<sup>36</sup> "Apel i Presidentit të Republikës, Sali Berisha", in *Rilindja Demokratike*, 327, January 26, 1997, p. 1.

<sup>37</sup> Vendim i Kuvendit të Shqipërisë, No. 294, dated 26.1.1997, Fletore Zyrtare nr.: 1, 11/02/1997.

expert in economic research, criticised the governing bodies, including the political opposition, noting that they “were unable to immediately reflect the popular demands. They demonstrated considerable lack of flexibility and responded late to the political changes that were required.”<sup>38</sup> On January 30<sup>th</sup>, the Albanian Parliament enacted the Law “On distribution of the wealth of foundations operating their lending activities on pyramidal schemes.” This legislation established procedures, rules, criteria, and designated the institutions responsible for the distribution of assets accrued through pyramid schemes. According to the law, each creditor’s claim would be validated based on the provided documentation; the distribution coefficient for each foundation would be calculated based on the amount of frozen funds and their obligations to depositors; and the disbursement of funds would be conducted either in cash or through savings books.<sup>39</sup>

On the same day, opposition parties and the “Organization of Former Political Prisoners” founded the “Forum for Democracy,” an anti-government alliance aimed at steering the popular movement through institutional means. Within its political platform, the Forum for Democracy characterized the current state of affairs as the most severe political and economic crisis since the beginning of the post-communist era. It attributed the primary cause of the crisis to the manipulation of the parliamentary elections held on May 26, viewing the pyramid scheme debacle as a result of erroneous economic policies underpinned by corruption, illicit trafficking, and the misappropriation of properties. The platform also condemned violations of human rights, and the police-judicial-administrative pressures exerted on the opposition, asserting that the Meksi government lacked the necessary moral and political authority and held it accountable for the ongoing crisis.<sup>40</sup>

<sup>38</sup> Z. Preçi, *Fillimet e vendosjes së ekonomisë së tregut në Shqipëri - një vështrim retrospektiv*, p. 8.

<sup>39</sup> Law No. 8190, dated January 30, 1997, “Për shpërndarjen e pasurisë së fondacioneve që kanë ushtruar veprimtarinë e tyre të huamarrjes mbi bazën e skemave piramidale mashtruese”, in *Fletore zyrtare*, no. 1, 11/02/1997.

<sup>40</sup> “Projekt - platformë”, in *Zëri i Popullit*, 336, February 5, 1997, p. 2.

The President of the Republic convened a meeting with political entities and syndicates to deliberate on the issue of usury and explore strategies to substantially mitigate the hardships it induced. However, SP and the opposition parties opted for not participating in this dialogue. This absence was perceived as an attempt to undermine the majority's commitment to political dialogue. In response, SP articulated its conditions for engagement in discussions: it stipulated that peaceful demonstrations should be permitted, all arrested opposition leaders and protesters should be released, the Meksi government should resign, a government of experts should be instituted, a date for new parliamentary elections should be set, and a commission should be established to monitor the wealth of government executives.

As violent protests escalated throughout Albania, the southern region witnessed chronic violence, resulting in casualties among both police forces and protesters. Victor Ruffy, in his report to the Committee on Political Affairs of the Council of Europe, noted, "If such a collapse were to occur in any of our countries, undoubtedly there would be a popular uprising." He further elaborated that it was unclear to what extent the financial collapse-induced popular uprising had been manipulated by specific political factions. The report characterized the uprising as predominantly spontaneous rather than orchestrated and underscored the armed forces' lack of determination in defending their positions and in preventing the looting of weapons depots. This, according to the report, was indicative of "deep demoralization among troops who were unconvinced of the necessity to defend the regime against the populace."<sup>41</sup>

The situation was particularly dire in Vlora, where chaos was pervasive. On February 20<sup>th</sup>, forty students from Vlora University commenced a hunger strike, articulating several demands: the resignation of the government, reimbursement for those impacted by

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<sup>41</sup> Arkivi Historik i Ministrise se Puneve te Jashtme, Fondi: Keshilli i Evropes, V. 1997, D. 476, Political Affairs Committee, Report on the state of emergency in Albania, Doc. 7780 (18 March 1997), p. 59.

the pyramid schemes, the resignation of the public television director, and an end to military activities. The authorities deemed the strike illegal and attempts by the National Information Service (SHIK) to resolve the hunger strike escalated into severe violence. This tension reached a climax when infuriated citizens set the SHIK building in Vlora ablaze, resulting in the tragic death of three employees who were burned alive; three additional employees were mercilessly killed in the ensuing melee. The violence intensified on the night of February 28<sup>th</sup>, when protesters detonated a weapons depot, seizing numerous Kalashnikovs and other firearms. The aftermath of these clashes was grim: six SHIK employees and three citizens were killed, and thirty individuals were injured.<sup>42</sup>

Following the severe disturbances in Vlora, President Berisha convened a meeting with various political parties, including SP. This meeting initiated a political dialogue that led to the decision for Prime Minister Meksi's government to resign and for discussions to begin among the political parties regarding the formation of a new government. Subsequently, on March 1<sup>st</sup>, Prime Minister Meksi presented his resignation. On March 2<sup>nd</sup>, in response to the escalating crisis, the Albanian Parliament enacted several laws and resolutions aimed at managing the situation. These included the Law on "The State of Emergency", the Law on "Declaring the State of Emergency in Albania", the Law on "Integrating the National Information Service with the Ministry of Interior Affairs" – which placed SHIK (State Intelligence Service) and the Ministry of Interior Affairs in charge of suppressing armed gangs – and the Law on "Certain Measures in Terms of the State of Emergency."

The Law on "The State of Emergency" temporarily suspended some constitutional rights and freedoms; public gatherings, as well as political, sporting, cultural, and trade union activities, were prohibited. The enforcement of these emergency measures was overseen by the Defence Council, while the operational aspect was

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<sup>42</sup> Arkivi Historik i Ministrise se Puneve te Jashtme, Fondi: Keshilli i Evropes, V. 1997, D. 476, p. 59.

managed by the Defence Headquarters, established on a district-based (prefecture) level and led by the Prefect.<sup>43</sup> The Law on “Declaring the State of Emergency” was to remain in effect until the constitutional and public order was restored. It was also decided that SHIK would be integrated into the Ministry of Internal Affairs. The Armed Forces of the Ministry of Internal Affairs and SHIK were tasked with suppressing the armed rebellion during the state of emergency and reestablishing public order. The defence Council was assigned the responsibility of partially mobilizing the population and deploying it at the disposal of the law enforcement structures and SHIK.<sup>44</sup> The Council of Europe underscored that “Albania, as a Member State of the Council of Europe, must demonstrate full respect for human rights in any use of force to restore order. The measures taken (...) must not exceed ‘the extent strictly required by the exigencies of the situation.’”<sup>45</sup>

In such conditions of political and social turmoil, on March 3rd, Sali Berisha was reconfirmed president by the Parliament, a decision that intensified political discontent and popular unrest, fuelling calls for Berisha to resign. The revolts escalated in violence, and their rapid expansion was alarming. Control over southern Albania rapidly deteriorated as the nation began to fragment within a matter of days. The agitated populace set public buildings ablaze, obstructed national thoroughfares, and raided food supply and armament depots. State responses were similarly forceful. A pervasive atmosphere of apathy dominated in Tirana, reflecting the deepening crisis. The government’s popularity plummeted as public institutions found themselves paralyzed, unable to perform actions necessary to mollify the escalating public discontent.

<sup>43</sup> Law No. 8194, dated 2.3.1997, “Për gjendjen e jashtëzakonshme në rastet e cenimit të rënde të rendit kushtetues e të rendit publik”, Fletore zyrtare no. 2, 07/03/1997.

<sup>44</sup> Law No. 8195, dated 3.3.1997, “Për disa masa në kuadrin e gjendjes së jashtëzakonshme”, Fletore zyrtare no. 2, 07/03/1997.

<sup>45</sup> Arkivi Historik i Ministrise se Puneve te Jashtme, Fondi: Keshilli i Evropes, V. 1997, D. 476, Political Affairs Committee, Report on the state of emergency in Albania, Doc. 7780 (18 March 1997), p. 50.

### 2.3 *The commitment of the international community to help Albania cope with the crisis*

In response to the unfolding crisis, international institutions urged political parties in Albania to collaborate and demonstrate maturity to forge a better future for the nation and its citizens. In March, the Organization for Security and Co-operation in Europe (OSCE) took an active role in Albania, aiming to assist the country – as an OSCE member – in regaining stability and reinforcing its commitment to democratic processes, human rights, and the rule of law. OSCE Chairman Helveg Petersen appointed Franz Vranitzky as a special representative in Albania to facilitate this mission.

During his inaugural visit, Vranitzky focused on fostering dialogue among the Albanian political factions. His mediation proved instrumental, and on March 9<sup>th</sup>, through his efforts, ten Albanian political parties reached a consensus and signed an agreement. The agreement aimed to stabilize the political landscape by ensuring cooperation across the political spectrum and laid the groundwork for the establishment of the Government of National Reconciliation. This agreement consisted of nine items:

- General amnesty: the Albanian Parliament is urged to declare a general amnesty for all civilians and military personnel implicated in the rebellion.
- Formation of a Government of National Reconciliation: this government should be inclusive, representing all political forces to ensure broad-based support and legitimacy.
- Disarmament of civilians: all citizens possessing weapons and ammunition are required to surrender them within a week in every Albanian town.
- National mourning: March 16<sup>th</sup> should be designated as a day of national mourning to honour the lives lost during the period of turmoil.
- Parliamentary elections: elections should be held no later than June 1997.
- International observers for the elections: the forthcoming parlia-

mentary elections should be conducted with the presence of observers from international bodies to ensure transparency and fairness.

- Aid for damaged areas: in cooperation with national and international institutions, the government is tasked with implementing all necessary measures to aid primarily the areas most affected by the crisis, ensuring rapid and effective recovery and rehabilitation.
- Phased removal of the state of emergency: initiatives should be undertaken to attenuate and eventually lift the state of emergency, reinstating normalcy and civil liberties.
- Continued political dialogue: dialogue among political parties should persist to facilitate ongoing cooperation and to collectively address emerging challenges.<sup>46</sup>

The accord was reached belatedly, given the scope of the crisis and the violence within the country. Under the terms of the agreement, Bashkim Fino was appointed to lead the Government for National Reconciliation. The primary responsibilities assigned to this government included reestablishing public order and peace, stabilizing the economic landscape, taking control of the financial situation, and preparing for free and fair elections. The new government assumed leadership amid extraordinarily challenging circumstances. The national army was severely depleted, with only 4,163 soldiers in active service out of the 29,796 officially listed.<sup>47</sup> The situation in southern Albania was particularly dire, where insurgents had looted weapons from military depots and orchestrated jailbreaks, releasing both criminal and dangerous individuals who roamed the country armed. Crime rates soared to alarming levels, with violence becoming rampant and the fear for personal safety becoming a pervasive nightmare for the populace. According to data

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<sup>46</sup> *Përpyjekja*, IV, no. 11-12, Tiranë, September-December 1997, p. 63.

<sup>47</sup> Arkivi Qendror i Forcave te Armatosura, Fondi: Kabineti i Ministrise se Mbrojtjes, V. 1997, D. 16, Relacion per demtimet e shkaktuara kohet e fundit ne Ushtri, 19.04.1997, p. 1.

from the Ministry of the Interior, from January 24 to April 8, 291 civilians and 9 police officers were killed, and 469 civilians and 137 police officers were injured.<sup>48</sup> The exodus of Albanians, primarily to Italy, escalated daily, with estimates reaching 13,000 by mid-March<sup>49</sup>. Public institutions had collapsed; police departments were abandoned. In many towns, local government structures were effectively non-existent as prefects and mayors had either fled the country or abandoned their posts due to fear.

In his memoir, "Abyss '97," Bashkim Fino reflects on his initial days as Prime Minister, describing his role as "a mediator between the angel and the demon,"<sup>50</sup> capturing the tumultuous nature of those times. Reports from daily briefings sent by the General Headquarters of the Army to Prime Minister Fino during this period provide further insight into the severity of the situation: "At the depots in Mirake, Librazhd, armed crowds overpowered the guards' resistance, broke into the infantry ammunition depot and, according to rough estimates, approximately 1,700,000 rounds were taken;" "In the Tresh tunnels in Lezhe, (...) three children were injured;" "In the ammunition tunnels at Qafe-Shtame, Burrel, local villagers blew open the tunnel entrances and began to take artillery ammunition. Meanwhile, a fire erupted causing massive explosions of shells, resulting in the deaths of 22 people."<sup>51</sup>

Confronted with a dire situation, the newly formed government sought assistance from the international community. OSCE adopted a dual approach to aid Albania: providing political counsel and technical support to prepare for the upcoming parliamentary elections. The Permanent Council of OSCE decided to establish a permanent mission in Tirana, creating a coordinating framework within which other international organizations could contribute their expertise to

<sup>48</sup> Arkivi Qendror Shteteror, Fondi 490, V. 1997. D. 661, Drejtoria e Policise Kriminale, Te dhena per numrin e te vrareve dhe te plagosurve per periudhen 24 janar deri ne 8 prill 1997, pp. 272-273.

<sup>49</sup> *Përpyjekja*, IV, no- 11-12, Tiranë, September-December 1997, p. 197.

<sup>50</sup> B- Fino, *Humnerë '97*, 2007, Edisud, Tiranë, p. 35.

<sup>51</sup> Arkivi Qendror Shteteror, Fondi 490, V. 1997. D. 661, p. 53.

help alleviate the crisis. OSCE posited that the organization of free and fair elections was essential for restoring a normal democratic environment and rekindling the public's trust in the political system and state institutions.<sup>52</sup> In the lead-up to the elections, OSCE concentrated on its role in coordinating international assistance and activities or programs related to the electoral process.

International institutions recognized that their support to Albania should extend beyond the political agreement. They expressed a commitment to assist the Government of National Reconciliation in achieving political reconciliation, peacefully resolving the rebellion, implementing the nine-point agreement, and making every effort to restore the confidence of the Albanian people. Their objectives included promoting tolerance, democracy, and the rule of law, assisting Albania in achieving a comprehensive assessment of the assets and losses incurred by the pyramid schemes, and providing guidance on managing a market-based economy. To ensure that the forthcoming elections were conducted freely and fairly, there was a call for extensive international observation to reassure the populace of their integrity. Furthermore, these entities urged those who had taken up arms to support Prime Minister Fino's governance efforts by laying down their weapons. A meeting of potential donor nations was convened to assist Albania in recovering from its economic downturn and to maintain ongoing diplomatic efforts to support Albania's emergence from the crisis.<sup>53</sup>

The government expedited measures to mobilize state institutions at both central and local levels and initiated a campaign to foster dialogue with the citizenry. A decision was made to replace certain prefects who were unable to effectively fulfil their duties. Additionally, four members of the Steering Committee of the Radio-Television and the Governor of the Central Bank were replaced. The Parliament was requested to amend the Law on the state of emer-

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<sup>52</sup> OSCE, 105<sup>th</sup> Congress, 1<sup>st</sup> Session, *"The present situation in Albania"*, May 23, 1997, p. 7.

<sup>53</sup> *Ibid.*, p. 25.

gency to moderate its provisions. Efforts were made to stabilize public order and peace. The Ministry of Internal Affairs outlined a strategic platform with key objectives to ensure public safety.

On March 28<sup>th</sup>, the UN Security Council unanimously passed Resolution 1101, authorizing “the establishment of a protective, multinational, temporary and limited force to facilitate the safe and immediate provision of the humanitarian assistance and help establishing a safe setting for the international missions in Albania.”<sup>54</sup> The resolution explicitly stated that the authorized mission, based on Chapter VII of the UN Charter, was to be conducted neutrally and impartially, adhering to the principles of impartiality and neutrality that underpin UN peacekeeping operations. However, the resolution did not include provisions for financial support from the UN. Instead, financial emergency support amounting to approximately US\$180 million was provided by the European Union and the World Bank.<sup>55</sup> The operation, dubbed “Alba”, reflecting its multinational composition, was primarily managed by the contributing countries, which coordinated the operations and cooperation among their troops. Each contributing nation bore the financial costs associated with their participation in the operation. The multinational security force comprised approximately 6,000 troops from 11 different countries, working collectively to stabilize the situation in Albania.

Notably, “Alba” was the first operation led by the Italian Armed Forces. Italy and Greece, in particular, expressed significant concern about the situation in Albania. Since the end of the Cold War, the Italian government had provided clear political and economic support to the Albanian government. Moreover, Italy had been directly impacted by the influx of Albanian refugees since the onset of the crisis, with thousands reaching its shores in 1991. Both Greece and Italy had a vested interest in encouraging Albania to establish acceptable social and legal conditions and to secure its territory to mit-

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<sup>54</sup> United Nations, Security Council, S/RES/1101 (1997) 28 March 1997, p. 2.

<sup>55</sup> R. Marchio, “Operation Alba”: A European approach to the peace support operations in the Balkans, U.S. Army War College, April 10, 2000, p. 7.

igate the flow of migrants. As part of these efforts, Italian troops patrolled Albanian territorial waters up to the Albanian shores, encapsulated by the policy aimed to “keep Albanians in Albania.”<sup>56</sup>

Officially, Operation “Alba” commenced on April 15<sup>th</sup>. The presence of international forces significantly improved the local population’s living conditions. They provided a safe environment for civil and humanitarian support and the activities of international agencies. They also ensured order during the elections of June 1997 and contributed to the restoration of peace in the country.

By the end of April and beginning of May, the measures implemented by the Government and the international peacekeeping forces began to show results in restoring order: newspapers resumed publication, schools reopened across most of the country, and the curfew was reduced by two hours. Subsequently, operations at Rinas Airport were restarted, and control was reestablished at the port of Durres, among other improvements. Under civic and international pressure, transparency measures were enforced upon the lending companies that continued to operate, to assess their capability to repay citizens. Presidents of these companies were restricted from traveling abroad, and the government proposed legislation to enhance transparency.

The date for the elections was established by the President for June 29<sup>th</sup>. A few days prior to the elections, on June 23<sup>rd</sup>, a pivotal meeting was held in Rome, where representatives of the political parties, in response to the challenging conditions facing the country and mediated by international actors, signed an understanding and conciliation agreement. This agreement aimed to ensure a fair and honest electoral process, the development of an election campaign grounded in proper political dialogue and devoid of violence, and the unequivocal acceptance of the election results by all parties, as validated by international observers. Additionally, it underscored a commitment to form a government that would include contributions

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<sup>56</sup> T. Perlmutter, “The Politics of Proximity: The Italian Response to the Albanian Crisis”, in *International Migration Review*, Vol. 32, No. 1, Spring 1998, p. 208.

from all political parties, encompassing those from the opposition.<sup>57</sup>

Early elections were perceived as a crucial opportunity to guide Albania out of its pervasive crisis. However, there was a common understanding among stakeholders that conducting free and democratic elections would be challenging given that much of the population remained armed. In preparation for the elections, the OSCE Office for Democratic Institutions and Human Rights (ODIHR) deployed approximately 100 officers to Albania. These officers were divided into two teams and covered the entire country to assist in the electoral preparations. An international coordinator was appointed by OSCE to observe and assess the elections, ensuring an external oversight mechanism was in place.

Despite these preparations, the electoral campaign unfolded within a hostile political climate, marred by mutual accusations between parties regarding the ongoing crisis. Election day itself was generally calm with a high voter turnout of 73%, indicating robust participation. Nevertheless, the atmosphere was tense, and there were numerous reports of delays and procedural infractions. Despite these challenges, OSCE-ODIHR deemed the elections to be acceptable under the prevailing conditions. "We can say that the elections can be deemed as acceptable, given the prevailing circumstances, because of:

- the large participation of voters;
- voters were generally able to cast their ballot without fear or intimidation;
- the conduct of the electoral commissions appears to have been, apart from a relatively small number of incidents, correct and impartial;
- domestic and international observers were, for the most part, granted access to all stages of the voting and counting without interference or intimidation."<sup>58</sup>

<sup>57</sup> "Një pakt për të ardhmen e Shqipërisë", in *Zëri i Popullit*, 430, June 24, 1997, p. 1.

<sup>58</sup> OSCE, *Parliamentary election in Albania 29 June-6 July 1997*, final report, OSCE, 1997, p. 6.

The election results represented a significant setback for the Democratic Party, which experienced a substantial decline in support, securing only 25.82% of the national vote – a sharp decrease from the 55.5% garnered in the previous year's election. The party secured merely 24 seats in Parliament. Conversely, the Socialist Party obtained 52.71% of the votes and, together with its coalition allies, took 110 out of 155 parliamentary seats. This outcome was largely attributed to a protest vote against the Democratic Party, which was held responsible for the collapse of the pyramid schemes.

The left-wing coalition, led by SP, subsequently assumed power and formed a government under the leadership of Fatos Nano. The new administration was confronted with a myriad of challenges that needed urgent attention to stabilize the country. The government's primary objectives included rebuilding state institutions, restoring public trust and authority, reestablishing order, and disarming the populace. Additionally, a key task was to provide transparency concerning the operations of pyramid schemes.

#### *2.4 The consequences of pyramid schemes*

The proliferation of pyramid schemes in Albania, as highlighted by the prestigious "Daily Finance," was recognized as one of the top ten financial scandals globally<sup>59</sup>. This phenomenon surpassed global analogues in its duration, for the extent of the population involvement, and for the severe repercussions it inflicted on the country. The pyramid schemes had multifaceted impacts across social, economic, and financial dimensions.

**Social Consequences:** On a social level, the schemes fostered passivity among the population. The allure of easy money diminished the willingness to engage in productive work, with the labour force participation seeing a notable decline. During a period when aver-

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<sup>59</sup> B. Lund, "10 financial scandals of all the time", in *Daily Finance*, April 18, 2014, <https://www.aol.com/article/finance/2014/04/18/top-10-financial-scandals/20871664/>, retrived: May 17, 2017.

age monthly wages were no higher than 70 US dollars, the promise of higher returns offered by these firms was irresistibly attractive to many. They exacerbated housing issues, with homelessness involving approximately 3,000 more families<sup>60</sup> which having sold their homes and invested the proceeds in these ill-fated schemes, found themselves without shelter.

Economic consequences: economically, the schemes inhibited genuine investment in the economy. The high interest rates promised by these firms led people to deposit their savings with them rather than investing in more productive economic activities. These schemes immobilized capital that could have been utilized more productively. As stated, "They immobilized money that could have been used more productively. In the extreme, capital inflows in a Ponzi-dominated economy have no effect on welfare but merely increase the amount of money in circulation, driving up nominal wages and prices at constant real incomes."<sup>61</sup> The investment activities of these pyramid firms were negligible, which substantially paralyzed economic activity, diminishing productive outputs across Albania. This misallocation of resources stalled economic growth and development.

Financial consequences: pyramid schemes activity severely strained the banking sector due to a deficit of deposits. Concurrently, such operations complicated the control of the Albanian currency by the Central Bank of Albania, facilitating significant flows and movements of money outside formal banking channels. This contributed to an escalation in consumer goods prices due to heightened money circulation, despite the absence of growth in macroeconomic indicators.

The crisis precipitated by these pyramid schemes "rapidly nullified the modest economic advancements achieved during the first six years of Albania's transition. [...] The collapse of these schemes

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<sup>60</sup> A. Malaj, F. Mema, "Tipare dhe pasoja të tregut joformal financiar", in *Ekonomia dhe tranzicioni*, V, No. 1 (15), January-March 1998, p. 8.

<sup>61</sup> D. Bezemer, *Post-Socialist Financial Fragility: The Case of Albania*, p. 15.

not only jeopardized individual financial security and the anticipated freedoms associated with market reforms but also challenged a broader set of universal values."<sup>62</sup> Moreover, the fallout from this crisis tangibly eroded national wealth.

The Albanian crisis of 1997, characterized by rampant violence, thefts, and widespread destruction, left indelible marks on the nation's infrastructure, including public utilities and social infrastructure such as hospitals and schools. The financial toll of the damages and losses incurred from January to June 1997 surpassed one million dollars.<sup>63</sup> During this tumultuous period, a staggering total of 6,394 criminal acts were recorded, of which 1,542 were murders.<sup>64</sup> Tragically, the violence claimed the lives of 30 children, and approximately 1,200 more were injured.<sup>65</sup> The wave of destruction also extensively damaged military units, departments, institutions, and enterprises. According to damage assessments conducted by the General Headquarters of the Army in October 1997, it is estimated that the damages in the military sector alone amounted to 61 billion and 465.5 million lekë (approximately 412.52 million US dollars). The evaluations revealed that around 600,000 infantry weapons, about 1.5 billion infantry bullets and hand grenades, and 3,500 tons of explosive ordnance and explosive materials were taken. Furthermore, approximately 30% of the artillery munitions were destroyed; their fuzes were removed, and the gunpowder was left exposed, posing a significant risk to human life.<sup>66</sup>

The collapse of pyramid schemes not only precipitated social chaos and a political and institutional crisis in Albania but also had dire consequences for the economy. According to a report from the Bank of Albania, the economic impacts were profound and multifaceted:

<sup>62</sup> Z. Preçi, *Fillimet e vendosjes së ekonomisë së tregut në Shqipëri - një vështrim retrospektiv*, p. 11.

<sup>63</sup> P. Zogaj, *Intuicionet e tranzicionit*, 1, 2009, UET Press, Tiranë, p. 253.

<sup>64</sup> B. Hoxha, *Krimi dhe antikrimi*, 2008, Ombra GVG, Tiranë, pp. 61-62.

<sup>65</sup> *Përpyekja*, IV, no 11-12, Tiranë, September-December 1997, p. 207.

<sup>66</sup> Arkivi Qendror i Forcave të Armatosura, Fondi 100/1, Viti 1997, Dosja 25, Shtabi i Përgjithshëm i Ushtrisë, Analizë për shkaqet e shkatërrimit të Ushtrisë, pp. 24-25.

- Restriction of economic activities;
- Savings retention;
- Inflation surge: the economic instability triggered a considerable increase in prices, with inflation soaring to 42.1 percent;
- Escalation of budget deficit;
- Worsening trade deficits;
- Currency depreciation: the domestic currency depreciated by 44.6 percent;
- Erosion of public trust in financial institutions: this lack of confidence led to a significant withdrawal of deposits from the banking system, resulting in a pronounced liquidity shortfall among commercial banks.<sup>67</sup>

## Conclusions

The crisis of 1997, marked by the collapse of some pyramid schemes, stands as a pivotal event in Albania's post-communist history. The collapse of the pyramid schemes in Albania not only precipitated a profound social and political crisis but also inflicted severe damage on the nation's economy. The multifaceted impacts of the pyramid scheme crisis illustrate the interconnected nature of economic stability, political governance, and social trust.

This period of profound instability not only inflicted severe physical and economic damage but also deeply impacted the societal structure, exacerbating issues of safety and security across the country. The 1997 crisis underscored the fragility of Albania's post-communist transition and systemic vulnerabilities within Albania's nascent market economy. It not only destabilized the nation's burgeoning market economy but also eroded public trust in the political and financial institutions. The breakdown of these schemes revealed profound vulnerabilities within the Albanian legal and regulatory frameworks, which failed to keep pace with the complex dynamics of a transitioning economy.

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<sup>67</sup> Banka e Shqipërisë, *Raporti vjetor 1997*, Tiranë, 1998, pp. 7-8.

This study has demonstrated that the Albanian government's delayed and often ineffective responses to the warning signs of the financial crisis exacerbated the situation. The lack of timely and decisive intervention allowed the pyramid schemes to expand unchecked, culminating in a catastrophic economic and social fallout. This period marked a significant low in the efficacy and legitimacy of the government, illustrating the profound disconnection between state mechanisms and the populace during a critical juncture of Albania's political history. The crisis highlighted the intense political tension, the deep political divisions and the charged atmosphere that shaped the responses to Albania's profound crisis during this period. Series of events underscored the extreme tensions and the volatile environment in Albania, illustrating the depth of the crisis, the complex dynamics of negotiation and the profound discontent among the populace. The political turmoil and social unrest that followed were symptomatic of a broader institutional failure, which underscored the urgent need for comprehensive reforms in governance, financial regulation, and public accountability.

The international community's involvement, spearheaded by organizations such as OSCE, UN and IMF, although critical, came at a stage when the crisis had already reached a peak. This underscores the importance of proactive international engagement in monitoring and advising emerging markets on sustainable economic practices and crisis prevention.

The enduring impact of these schemes deeply scarred Albania's socio-economic landscape, demonstrating the dangers of such financial activities and underscoring the need for stringent regulatory oversight to prevent similar crises. While the Albanian crisis of 1997 was a result of specific historical, political, and economic conditions, it offers universal insights into the risks of transitional economies. The lessons from Albania's experience are also valuable for other post-communist nations navigating the complex path from planned to market economies.

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