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Philosophy International Journal
ISSN: 2641-9130

Investment Psychology in Developing Economies: Albania's Case and the Money Laundering Dynamic

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Research Article
Volume 8 Issue 4
Received Date: November 18, 2025
Published Date: December 03, 2025
DOI: 10.23880/phij-16000355

Abstract

The psychology of investment and investor behavior in financial markets presents a major challenge for developing countries, especially those transitioning from communist regimes. These emerging market economies, established after authoritarian systems, are directly affected by economic fluctuations caused by how investors and consumers perceive and react to market conditions.

Challenges in adapting to modern development models, poor economic performance, widespread corruption, legal uncertainty, and migratory flows have resulted in hybrid economic structures where neoclassical principles are combined with psychological behavior elements. Albania exemplifies this situation. Since the 1990 transition, the country has faced many difficulties in rebuilding its economic system. Domestic and foreign investments are impacted by frequent regulatory changes, unpredictable behavior of economic actors, and a lack of institutional stability. Corrupt practices, legal enforcement uncertainties, and money laundering continue to obstruct market functioning and significantly influence investment decisions. This paper aims to analyze the economic theories in Albania and demonstrate how these theories interact with an economy impacted by money laundering. The methodology combines both qualitative and quantitative empirical data gathered from theoretical literature as well as national and international statistical sources, enabling an objective comparison of the factors influencing investment behavior in the country.

Keywords: Investment Psychology; Homo Oeconomicus; Corruption; Money Laundering

Introduction

Over the years, economic theories have established the principle that humans are rational agents who, when making investment choices, act based on reasoning aimed at maximizing their personal utility and enhancing their well-being. This economic principle has evolved into the concept of Homo Oeconomicus. The term was first introduced by economist John Kells Ingram [1], who emphasized the individual's ability to reason when making investment decisions based on rational, deliberate, and information-driven thought.

In fact, following the Second World War especially during the 1950s and 1960s economists like Herbert Simon [2], Maurice Allais [3], and others laid the initial analytical groundwork challenging the concept of Homo Oeconomicus by pointing out its theoretical limitations in relation to real human cognitive processes. Even earlier, philosopher-jurist-economists such as Vilfredo Pareto, John Stuart Mill, David Hume, and Jeremy Bentham had already studied how political, intellectual, and psychological factors influence human decision-making in economic and investment contexts.

Notably, the author who later became a pioneer in reshaping economic thought through prospect theory is Daniel Kahneman [4]. This branch of behavioral economics studies human psychology and the behavior patterns individuals show when making investment decisions. It explores the human element in economic choices, which are often influenced by fleeting impulses, fear, overconfidence, poorly processed information, or even the thrill of investing without enough consideration of the possible outcomes.

Furthermore, unlike the neoclassical model of Homo Oeconomicus, this theory concentrates on examining individual and social behavior patterns within economic systems, such as financial markets. These behaviors are often characterized by emotional fluctuations that directly impact both individual investors and investment firms. The theory investigates various human emotional factors such. compassionate, pride, greed, arrogance, overconfidence, and excessive optimism which, in different forms, influence financial decisions and produce broader effects throughout the economic and financial system. These emotional types are frequently irrational and lead to the development of internalized investment beliefs that lack clear vision and long-term planning. This behavior sharply contrasts with the principles of classical finance theory, which relies on rational and analytical decision-making by individuals and the system as a whole.

Thus, the role of behavioral finance is to understand, analyze, and identify the behavioral patterns of both economic-financial systems and individual agents.

In the investment world too, the psychological factor plays a key role in shaping not only the types of investments made but also the expected benefits whether related to personal gain or the larger impact these investments have on the economy.

Likewise, external psychological factors referred to as *cognitive biases* can lead to errors with potentially devastating consequences for both individual investors and the broader financial markets.

Euristica

Consequently, financial operators and individuals often engage in an unconscious manner in a decision-making process known as heuristics [5]. This method, based on quick, intuitive thinking without thorough analysis of all available information, often results in cognitive shortcuts that, through excessive simplification, cause logical errors and faulty judgments.

In investment psychology, three main forms of heuristics are identified [6]:

a) Representativeness heuristic, which is based on forming judgments according to stereotypes and familiar patterns or scenarios.

b) Availability heuristic, which is based on retrieving information to make decisions. This heuristic reflects a tendency to estimate probabilities based on how easily certain events or situations come to mind giving higher weight to those that are simpler to understand and easier to remember.

c) Anchoring heuristic describes how individuals formulate predictions and make judgments based on an initial reference point, which then serves to adjust subsequent analytical reasoning. This anchor is often linked to previously received information or to a general estimate related to the desired element.

The heuristic forms outlined above, commonly known as mental shortcuts, are also considered instrumental in generating cognitive biases that is, systematic errors linked to superficial analysis, emotional influences, and stereotyped environmental or familiar factors.

As previously mentioned, cognitive biases are skewed perceptions of facts and situations, leading to subjective viewpoints that distort reality. These biases stem from personal experiences, internalized concepts, and environmental stereotypes, all of which are disconnected from logic or any objective assessment of the information.

By relying on heuristics as a primary decision-making mechanism, individuals often encounter cognitive biases that result in outcomes misaligned with what was originally envisioned or intended to be achieved in practice.

Another form of cognitive bias is the so-called home bias, which is based on heuristically driven thoughts that reinforce comfort with one's own choices and prevent challenging one's psychological comfort zone. This behavior is closely linked to personal experiences, blind trust, and the emotional states individuals experience in relation to such decisions.

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This type of cognitive bias (home bias) usually appears mainly during times of economic uncertainty or in weak economies marked by significant social disparities.

Materials

To provide a more straightforward overview of the main perspectives in behavioral finance, the most prominent theories are summarized below.

Thaler [7] in The End of Behavioral Finance argues that behavioral finance, once on the fringes, has become a key part of modern economic thought. Challenging the Efficient Market Hypothesis (EMH), which assumes rational investors and efficient pricing, Thaler highlights ongoing market anomalies such as bubbles, overreactions, and excessive trading that traditional models cannot explain. Behavioral finance has advanced through strong empirical research, becoming a vital perspective for understanding financial markets.

Barberis and Thaler [8] further critique EMH by highlighting common irrational behaviors, including investors trading too frequently, selling winners too early, and holding losers too long patterns that conflict with rational maximization. These behaviors indicate emotional and psychological influences outweigh logic.

Shiller [9] investigates the psychological and social forces driving market booms and busts. He demonstrates that stock prices often diverge from fundamental values due to emotions such as fear and greed, herding behavior, and social contagion. The concept of "irrational exuberance" illustrates how collective sentiment inflates prices beyond rational expectations.

Waweru, et al. [10] note that investor behavior is greatly influenced by peer pressure, leading to herd mentality and regret. Baker and Wurgler [11] describe sentiment as a wide-ranging emotional state either optimism or fear that affects market trends regardless of fundamentals. High sentiment levels push asset prices up; low sentiment levels limit capital flow and growth.

Ritter [12] explains that cognitive biases like heuristics and framing illusions systematically distort investor judgment. Despite advances, behavioral finance has yet to establish a unified predictive model, illustrating its complexity.

Lo [13] addresses this gap with the Adaptive Markets Hypothesis (AMH), integrating principles of evolution and learning. Unlike EMH, AMH suggests that market efficiency is dynamic and context-dependent. Investor behavior changes with market conditions, influenced by competition, innovation, and environmental shifts. Under stress or when new participants join, biases emerge, leading to inefficiencies. Over time, however, adaptive behavior restores partial efficiency. AMH posits that no strategy remains optimal indefinitely; market adaptation is key. This theory accounts for sentiment-driven mispricing and return predictability based on evolving investor behavior. Emotions like overconfidence, fear, and representative bias are central to these patterns.

Together, these theories create a comprehensive framework for understanding decision-making in modern financial contexts. They highlight the importance of psychological factors in shaping both short-term market movements and long-term investment patterns. When applied to transitional economies like Albania, they offer essential tools for analyzing the interaction between formal structures and behavioral responses, especially amid systemic uncertainty and institutional weaknesses.

In the following sections, these theoretical insights will be placed within the context of the Albanian economic landscape, emphasizing how behavioral and rational mechanisms together influence investment decisions in environments affected by money laundering, corruption, and informal market dynamics.

Albania's Case and the Money Laundering Dynamic

This paper places itself within the ongoing academic and policy debate by critically assessing Albania's economic infrastructure and environment, focusing on key issues like corruption and money laundering. Using behavioral economic analysis, institutional diagnostics, and empirical data, it aims to evaluate the effectiveness of the monetary system, financial behavior, and legal issues related to money laundering, and identify structural risks that exist beneath the formal framework in investment areas.

The Albanian economy exemplifies a typical developing nation transitioning from a centrally planned system to a free-market economy. Since the early 1990s, Albania has implemented a series of structural reforms to open markets, encourage private investment, and enhance competition. However, the behavior of economic agents both investors and consumers demonstrates a blend of classical rationality (utility theory) and psychological, emotional, and cultural influences, making the country more similar to a behavioral financial model (prospect theory).

With the fall of communism, the Albanian economy was restructured to create a free and competitive market. The main reforms after 1991 included privatizing state-owned enterprises, opening to foreign direct investment (FDI), and

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integrating into international markets. Officially, the system aligns with the neoclassical model of a free market; however, in practice, the behavior of economic agents has shifted it toward a hybrid model where decision-making psychology prevails.

In transitional countries overall, especially in Albania, economic decisions are greatly affected by subjective perceptions such as risk, emotions, social norms, and trust. These factors become even more important because of the instability of institutions and the lasting effects of collective behavioral patterns inherited from the previous economic system.

Investment Decisions

Making smart investment decisions can be difficult. It's not just about analyzing financial data. Traditional finance theories, such as the Efficient Market Hypothesis [14], as discussed earlier, suggest that investors always act rationally based on available information. However, behavioral finance offers a different perspective. It shows how emotions, mental shortcuts, and biases often influence people's investment choices [15]. These psychological factors can lead investors, especially in countries like Albania an emerging economy to make decisions that aren't always logical, resulting in poor financial outcomes. In such environments, investors tend to depend on advice from friends, social pressure, or simple mental rules (heuristics) when choosing where to invest [16]. Since these methods lack proper risk assessment tools, common biases such as loss aversion, herding behavior, and mental accounting become more apparent. For example, loss aversion means people care more about avoiding losses than making gains. As a result, they may hold on to losing investments longer than they should. Herding behavior [17], another common bias, occurs when people tend to follow others instead of thinking independently, often driven by the fear of missing out or the desire to fit in socially. This can lead to bubbles and substantial financial losses. Additionally, how an investment is presented can greatly influence how people perceive the risk. The same opportunity can appear either safe or risky depending on how it is displayed. Understanding how people perceive risk is crucial in financial settings because they often rely on limited or secondhand information such as stories, personal experiences, or word of mouth to assess danger. This can cause them to underestimate or overestimate risks [18], leading to poor decisions [19].

Selected Statistical Data on the Economic Climate in Albania – The Investors'

Perspective

Albania has a total area of 28,748 km². It features 316 km of coastline and 73 km of shoreline along inland lakes. The country is rich in natural resources. The southwestern region is abundant in oil and natural gas. In contrast, the northeastern region holds significant mineral reserves, including chromium, copper, and iron-nickel, as well as substantial bitumen deposits and notable potential for renewable energy, primarily hydropower [20]. As of January 1, 2025, Albania's population was 2,363,314, with a GDP per capita of USD 11,389.7, placing the country in the upper-middle-income category [21].

According to the World Bank's Doing Business indicators, Albania ranked 82nd out of 190 countries, with a DB score of 67.7 [21].

Based on empirical data collected by the Foreign Investors Association of Albania (FIAA) [22] regarding the business environment in Albania for 2025, the following findings emerged: Foreign investors rate Albania's current Doing Business climate at 45/100 (down 4 points from 2024). Expectations for the future stand at 50/100 (down 2 points). Currency depreciation and inflation remain major concerns, though less severe than in 2024. Corruption has increased significantly (+6 to 57/100), while informality has decreased (−5 to 61/100). Order & Security shows the highest improvement (+25 to 36/100). Market competitiveness improved by 13 points. The political climate has improved to 43/100 (+6). The judiciary has slightly increased to 56/100 (+1). Energy supply shows overall improvement. The tax system remains problematic, especially regarding tax liability calculations (38/100) and VAT reimbursement (44/100). Institutional relations have weakened overall, despite two areas remaining above the midline: institutional capacity at 56/100 and the procurement system at 52/100. The labor market continues to underperform, with wage pressure at 62/100 (down 3 points) and skilled labor availability at 72/100 (down 2 points). Economic expectations for 2026 stay steady at 56/100, while turnover expectations are moderately positive at 60/100. Awareness of EU integration is exceptionally high: 79% know the reform agenda, 77% are familiar with the EU Growth Plan, and 98% want more information. Additionally, 66% rate the EU Delegation positively.

An analytical assessment based on the theories mentioned above clearly shows that investment structures in Albania are directly affected by behavioral factors, especially those aligned with prospect theory. However, some elements mainly those related to the European Union integration process demonstrate a more rational analysis and comparative expectations compared to countries that are already members of the EU.

The following Table 1 summarizes these findings.

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Category	2025 Score	Change vs 2024	Analytical Note
Doing Business Climate	45/100	-4	Slight deterioration
Future Expectations	50/100	-2	Weak optimism
Euro Depreciation	Major issue	Less severe	Still impactful
Inflation	Major issue	Less severe	Stabilizing
Corruption	57/100	6	Worsening
Informality	61/100	-5	Moderate improvement
Order & Security	36/100	25	Strongest improvement
Market Competitiveness		13	Fairer competition
Political Climate	43/100	6	Mild improvement
Judiciary	56/100	1	Stable, minimal progress
Energy Supply	Improved		Positive trend
Tax Liability Calculation	38/100		Critical issue
VAT Reimbursement	44/100		High concern
Tax Law Changes	60/100		Serious obstacle
Tax Interpretations	57/100		Persistent problem
Institutional Capacity	56/100		Above midline
Public Procurement	52/100		Above midline
Wage Increase Pressure	62/100	-3	Rising costs
Skilled Labor Availability	72/100	-2	Workforce shortages
Economic Expectations 2026	56/100		Stable outlook
Turnover Expectations	60/100		Moderate optimism
EU Reform Awareness	79%		Very high
EU Growth Plan Awareness	77%		Very high
Desire for More EU Info	98%		Nearly unanimous
EU Delegation Evaluation	~66% positive		Favorable

Table 1: Summary of key categories assessing the economic climate in Albania for 2025.

It is observed that phenomena such as corruption, fear related to exchange rate volatility, political uncertainty, judicial insecurity (*prospect theory*), legal ambiguity in taxation, lack of workforce qualification, and an unstable labor market (*utility theory*) create significant barriers to investment and foster a climate of moderate pessimism.

Although there has been some progress in measurable factors affecting investment willingness from 2024 to 2025, financial behavior remains heavily shaped by external environmental influences. Consequently, Albania still faces fluctuations in economic stability related to investments. Albania remains a moderate-yield market burdened by high structural costs, including various forms of money laundering and the inflationary pressures they generate factors that weaken competitive balance and disrupt financial stability.

To further reinforce the data related to the business climate in Albania, as well as to clarify the connection between economic theories and their application to the Albanian economic and financial system, it is necessary to examine specific empirical evidence, such as:

a) – According to Albania's ranking in "Doing Business," it fluctuates, with recent reports indicating a decline. A 2020 assessment ranked Albania 63rd out of 190 countries in the World Bank's "Ease of Doing Business" report, while a 2025 survey of foreign investors gave it a score of 45/100 for the current situation. Key challenges include a high tax burden, complex administrative procedures, and issues in areas such as construction permits, energy, and property registration.

b) - 2025 Investor Survey: According to a FIAA Albania survey (November 2025), foreign investors gave Albania a score of 45 out of 100 for the current business environment,

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a decrease from 49 in 2024.

c) - Albania was ranked 81st out of 141 countries in the 2023 report, which is the most recent data available through the WEF's Global Competitiveness Index (GCI). Key challenges and areas for improvement include: Taxation A high administrative burden from complex tax procedures is a major concern, with Albania ranking 123rd in the World Bank's 2025 Global Economic Prospects report [24]. Bureaucracy and procedures The country performs poorly in areas like handling construction permits, energy, fiscal procedures, and property registration. It was ranked 122nd out of 131 countries for transparency, with issues in the judicial system and nepotism in administration. Challenges remain in the judicial system, securing property rights, and the lack of transparency in administrative policies. Infrastructure It remains a significant challenge. Innovation Albania lags behind, with low rankings in innovation sophistication, research, human capital, and creative production.

Areas of relative strength: Trade: Albania is more competitive than the region in cross-border trade, requiring fewer documents for export, incurring lower export/import costs, and experiencing shorter import times. Financial system: The financial system has improved, with strong capitalization and a high monetary freedom score (80.4%). The economic system is considered resilient, although the banking sector is small and mostly owned by foreign banks. Business sophistication: The country performs well in this area, and its infrastructure and institutions are also strengths.

Interpreted through the lens of the two theoretical frameworks discussed **utility theory** and **prospect theory** and applied to the identification of investor profiles in Albania, it may be concluded that:

According to *Prospect Theory*, investors react more strongly to losses than to equivalent gains. Their expectations toward empirical data related to the overall investment environment are often perceived as negative.

As a result, investors often hesitate to commit capital, which diminishes the amount of evaluative analysis of Albania's investment potential. Psychologically, they are more influenced by risk-related factors especially those tied to institutional instability, corruption, and legal uncertainty particularly in taxation, which is frequently viewed as an unmanageable risk than by the prospect of medium- or long-term returns. According to Prospect Theory, based on the reviewed data, it is clear that positive factors such as trade facilitation and financial stability have less impact on investment decisions than negative perceptions linked to taxation, judicial inefficiency, and bureaucratic barriers. Therefore, although Albania offers a favorable business environment due to its strategic location between East and West, access to the Adriatic and Ionian Seas, a stable financial system, and relatively simple procedures for starting a business these factors alone are not sufficient to generate strong investor confidence.

This is mainly caused by the psychological overestimation of potential losses, which are seen as twice as severe as they actually are.

From the perspective of *Utility Theory*, the foregoing can be analyzed under the assumption that investors are rational, detached, and analytical agents who consistently choose the option that maximizes their expected utility.

In this context, Albania is considered a low-utility country mainly due to uncertainties surrounding property rights enforcement, limited access to justice, lengthy judicial processes, administrative corruption, the lack of a competitive system to support market dynamics, an inefficient tax system, and slow VAT reimbursement procedures. Additionally, shortages of human capital and low levels of innovation decrease the likelihood of generating high returns. Conversely, a stable financial system and low export costs are positive aspects in the overall assessment. Based on Utility Theory, it can be argued that rationally Albania continues to involve higher costs and risks than the potential benefits it provides.

Understanding Consumer Investment Perceptions: Rational Utility vs. Behavioral Prospect

Framework

As previously analyzed, based on the referenced data, the implementation of the two fundamental theories Utility Theory and Prospect Theory has been studied in relation to investor behavior in the commercial domain.

To further deepen the understanding of the interconnected structure between these two theoretical frameworks, the focus now shifts toward analyzing the behavior of the Albanian consumer.

Due to the intellectual formation shaped by the communist era which was centered around a centrally planned economy the contemporary Albanian consumer now faces a free market system, driven by competition and capital circulation.

However, when analyzing the consumer's ability to engage in investment behavior, it becomes clear that, in Albania, several problematic profiles appear. These are closely connected to Prospect Theory, as shown through heuristics and cognitive biases.

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Thus, the perception of Albanian consumers regarding the economic climate is shaped by an interplay between objective economic factors such as taxation, wages, prices, investments, cost of living, fluctuations in foreign currencies, and access to credit and subjective psychological elements, including uncertainty, fear of loss, expectations about the future, and environmentally induced mentalities and stereotypes (e.g., greed, vanity, low education and the willingness to pay any price for social appearance).

- Examining the Albanian economy through the lens of Prospect Theory, several conclusions can be drawn about the behavior of Albanian consumers.

The economic climate is often viewed through an emotional lens, where even small changes in economic indicators tend to lead consumers to see investment opportunities negatively.

Specifically, any increase in prices typically caused by inflation along with systemic uncertainties, especially concerning property rights, a corrupt government bureaucracy, labor migration, low wages, and widespread insecurity about the future and the ability to improve income contribute to an environment seen as economically declining.

Furthermore, the lack of domestic production in key sectors, an agro-economic system based on subsistence family farming rather than coordinated state-supported structures, and the disconnect between wages and actual living costs (including service prices, essential goods, and fuel costs) all contribute to a situation where even when macroeconomic indicators show positive trends the economy is still viewed negatively. As a result, consumers often feel poorer and psychologically register losses, even in the presence of objective growth.

All these factors lead to the development of conservative behavioral patterns among consumers regarding investment decisions [25].

Specifically, the observed tendency includes a rise in cash savings kept outside the formal banking system; avoiding high-risk or long-term investments such as government bonds with maturity periods of 5 to 15 years; keeping remittances sent by emigrant family members as savings rather than spending them; and cutting back on non-essential consumption, especially in categories like clothing.

In this context, it can be stated that the Albanian consumer exhibits a behavioral model best classified as *defensive, in which the weighting of negative evaluations is approximately two to three times greater than that of* positive assessments.

- According to Utility Theory, Albanian consumers are seen as rational agents who aim to maximize their personal utility.

The supporting indicators for this approach include the assumption that financial assessment mainly depends on the cost of living, wage levels, financial stability, access to essential services, and the efficiency of institutions.

From an analytical perspective, these factors lead Albanian consumers to take a cautious approach to investing. Factors like low wages, limited institutional efficiency closely associated with a high perception of corruption legal uncertainty around conflict resolution (especially relating to property rights), and lengthy dispute resolution and utility recovery times all impede rational decision-making. As a result, consumers become more skeptical and prioritize preserving existing economic capital over making new investments. The logic is straightforward: if property isn't protected and justice is difficult to access, then investment holds little value making any expenditure aimed at generating returns seem excessive.

Albanian consumers operate within an economy marked by a high level of institutional corruption risk, an inefficient and clientelistic public administration, and a market structure prone to significant distortions, including the destabilizing effects of illicit financial flows such as money laundering.

Within this framework, Prospect Theory highlights consumers' increased sensitivity to risk and their aversion to losses, while Utility Theory provides a rational explanation for reduced consumption, higher savings, and the avoidance of investments. Despite their theoretical differences, both approaches ultimately agree on the same empirical fact: Albanian consumers view the economic environment as uncertain and see investment utility as limited. In this context, psychological insecurity amplifies the actual economic costs.

The Money Laundering Dynamic in Albania

Albania operates within a multidimensional, complex economic and institutional landscape where money laundering (ML), corruption, and structural weaknesses affect not only macroeconomic stability but also consumer and investor perceptions.

According to international monitoring agencies for 2025, Albania remains highly vulnerable to money laundering, with illegal funds primarily passing through sectors like real estate, construction, cash-based businesses, and trade-related financial activities [GI TOC 2025].

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Based on specialized reports addressing money laundering issues, Albania is identified as a jurisdiction where illicit funds are funneled through the domestic economy to be integrated and laundered. Key sectors impacted include construction, real estate, cash-heavy businesses, money transfer channels, and complex corporate structures [Agnesa].

This also includes using commercial companies as front organizations to hide illegal activities, issuing fake invoices, and conducting trade-based operations meant to disguise the origin of funds. These practices cause significant economic instability by manipulating prices and encouraging unfair competition.

The two most common methods of money laundering in Albania are centred around the real estate sector especially through property overpricing and the misuse of the financial system by issuing large loans that are later repaid with illicit funds. These practices establish Albania as a "privileged" destination for systemic money laundering, where the phenomenon is not just sporadic but deeply embedded and integrated into the operational structure of key markets impacting both consumers and investors.

Albania is a country with high exposure to money laundering, as evidenced by the wide range of sectors infiltrated by this criminal activity [26].

In addition to the areas previously mentioned, money laundering has extended into services provided by non-profit organizations, notaries, legal professionals, certified accountants, public procurement procedures (particularly for infrastructure projects), car rental services, and small-scale commercial activities such as gold trading shops.

The origin of money laundering comes from criminal activities such as tax evasion, corruption, arms and drug trafficking, and fraudulent schemes.

From the perspectives of both Prospect Theory and Utility Theory, these activities serve as major obstacles to investment because they increase perceived risks, undermine trust in institutions, and reduce expected utility in the Albanian economy.

Despite demonstrating more coordinated and institutionalized efforts by prosecutorial bodies during 2024, statistical data reveal that the amount of illicit funds being laundered within Albania's economy continues to raise serious concerns [27]. According to estimates, between 2015 and 2024, Albania's money laundering activities totaled approximately €1.079 billion [28].

Economically, in 2024 alone, the informal sector is projected to have made up about 20–25% of the national GDP, roughly equivalent to $4–5 billion [29].

In 2024, Albania's Special Structure Against Corruption and Organized Crime (S.P.A.K.) seized and confiscated assets worth €65.5 million including €28.7 million in provisional seizures and €36.8 million in confirmed confiscations. The recovered assets consisted of real estate, bank deposits, vehicles, cryptocurrencies, and luxury items.

Additionally, S.P.A.K. launched investigations against 33 former senior public officials, with 19 (52.9%) officially indicted, and dismantled 16 high-risk criminal organizations, referring 10 for judicial proceedings [27].

These data collectively provide a thorough overview of how money laundering distorts the Albanian economy, influences economic perceptions, and erodes investor confidence in the local business environment.

- According to Prospect Theory, when investors or consumers process economic decisions through an emotional lens, they tend to think: "There is a high circulation of illicit money, widespread presence of criminal groups, and significant insecurity regarding life and property. Corruption is rampant at the highest levels therefore, the risk of losing my capital or becoming involuntarily entangled with criminal networks is very high." In this context, the dominant frame is that of loss, not gain. A foreign investor, for example, may hesitate to enter the Albanian real estate market because they perceive that property prices and ownership structures are tainted by money laundering and clientelistic ties between organized crime groups and the political elite.
- Meanwhile, domestic consumers see the rise in real estate prices not as a sign of healthy economic growth but as a sign of systemic money laundering.
- This perception breeds fear and a feeling of being excluded from a market that appears distorted and disconnected from real economic fundamentals. Prospect Theory demonstrates that even when sector growth presents clearly high return opportunities people tend to avoid risk. Concerns about losing capital, damaging reputation, and legal issues lead to behaviors focused on avoiding risk and becoming overly sensitive to it. So, individuals shift their attention from potential opportunities to existing risks.
- Continuing the analysis from the perspective of Utility Theory, it is worth noting that a similar conclusion emerges when the situation is evaluated by a rational investor one who considers expected return relative to costs and risk.

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Under Utility Theory, the rational investor compares expected returns with systemic risks. In the Albanian context, the widespread issue of money laundering driven by predicate crimes such as drug trafficking, corruption, tax evasion, and fraud creates a high level of institutional uncertainty. Structural flaws in enforcing anti-money laundering laws, loopholes in asset confiscation, and limited capacity to track offshore assets [30] all contribute to a risky environment. As a result, even though high short-term returns are possible, the overall net utility of investment is greatly reduced by the chance of exposure to criminal activity, legal disputes, and asset insecurity. From a *Utility Theory* perspective, markets dominated by actors using illicit capital create a competitive imbalance that undermines fair business practices.

These actors often prioritize money laundering over profitability, accepting minimal margins in exchange for transactional cleansing.

Therefore, legitimate investors face an uneven playing field, marked by distorted pricing, unregulated market forces, and high barriers to entry. In this setting, the expected utility of legal investment drops significantly, as returns no longer match risk, cost, or economic sense.

Integration of Utility Theory and Prospect Theory in the Context of Money

Laundering

In sum, both theories agree that uncertainty whether rationally assessed or psychologically perceived significantly reduces the attractiveness and expected utility of investing in high-risk environments such as Albania.

- Within the psychological framework of Prospect Theory, both investors and consumers in Albania primarily operate within a “loss frame”: they focus on risk, anticipate potential losses, and lack credible long-term security guarantees. Every new report of a criminal group being dismantled or a senior official being investigated for money laundering or corruption only reinforces the belief that the system is controlled and influenced by a parallel economy fueled by illicit funds. This environment encourages a mindset of avoidance, distrust, and disengagement from formal investment opportunities, since the perceived risk of loss consistently outweighs any potential gains.
- Under Utility Theory, rational actors react not only to the expected profit of a specific investment but also to the hidden and systemic costs caused by criminal infiltration.
- When shadow capital distorts the market, legitimate investors face greater compliance burdens and higher reputational risks, which ultimately reduce expected utility. The gap between law in theory and law in practice further erodes institutional trust and long-term investment prospects.

Even as anti-corruption and anti-money laundering institutions demonstrate operational progress, both rational analysis (*Utility Theory*) and behavioral perception (*Prospect Theory*) converge on a shared outcome: a low-utility, high-risk investment environment that continues to deter formal economic engagement.

Methodology

This paper offers a multidisciplinary, comparative, and deductive analysis of the investment climate in Albania by combining classical economic theories with modern behavioral finance approaches. The study uses a mixed-methods research design, integrating qualitative insights into investor and consumer behavior with quantitative statistical data to examine the duality of rational and psychological decision-making processes based on Utility Theory and Prospect Theory, respectively.

Using a comparative approach, the research examines how economic actors in a developing market like Albania operate amid institutional fragility, widespread informality, and high levels of money laundering. Illicit financial flows are seen as key distortive forces that cause inflated real costs (such as compliance, risk premiums, and reputational damage), decrease net utility, and hinder market transparency.

The findings indicate that economic decision-making in Albania is influenced by the interaction between limited rationality and emotionally driven heuristics, which strengthens investor risk aversion and long-term disengagement. The paper provides an original contribution by connecting systemic vulnerabilities such as weak law enforcement and criminal infiltration to reduced investment performance. It emphasizes the need to address both structural and perceptual barriers to unlock sustainable economic growth in transitional economies.

Results and Discussions

The empirical and theoretical analysis describes Albania as a small transition economy with hidden growth potential, influenced by favorable geography, resource supplies, and increasing global integration. However, these strengths are significantly challenged by structural issues long-standing institutional weaknesses, widespread corruption, deep-rooted money laundering, and ongoing legal uncertainties. While macroeconomic indicators classify Albania as an “upper middle income” country, comparative measures

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show a decline in its investment profile. The 2025 FIAA Business Confidence Survey highlights this gap: the current investment climate scores 45 out of 100, with only slight improvement in future outlooks (50/100). Major obstacles include systemic informality, fiscal instability, bureaucratic hurdles, and a shortage of skilled workers. Limited improvements are seen in energy access, public safety, and competition regulation, which are not enough to restore investor confidence.

The informal economy continues to be a major part of the economy estimated at 20–25% of GDP in 2024 with real estate, construction, cash-heavy businesses, and trade-based schemes serving as main channels for money laundering. Despite significant actions by SPAK, including asset seizures and prosecutions, enforcement remains insufficient compared to the amount of illegal money flows.

Behavioral patterns reflect this reality. Under Prospect Theory, investors and consumers act from a loss-averse frame amplifying risks related to legal instability, reputational exposure, and accidental entanglement in criminal circuits. Even modest improvements are dismissed as fragile.

Utility Theory confirms this defensiveness: legitimate market actors face distorted competition, reduced profit margins, and inflated entry barriers. Consumers, facing high living costs and weak institutional guarantees, rationally prefer capital preservation over risky commitments. Both theories converge Albania is perceived and calculated as a high-risk, low-utility investment ecosystem.

Conclusion

The combined assessment of economic theory and Albania's empirical context shows that the country's investment climate is influenced by a complex interaction between rational evaluation and behavioral perception. Although Albania has notable structural and geostrategic potential based on its natural resources, geographic location, and gradual integration with European markets this potential is still limited by deep-rooted institutional weaknesses, systemic corruption, ongoing informality, and the widespread influence of money-laundering networks. These factors both distort investors' rational decision-making, as explained by Utility Theory, and heighten loss-avoidance psychological responses, as outlined in Prospect Theory.

From a behavioral perspective, Prospect Theory explains why investors and consumers in uncertain environments tend to overemphasize potential losses compared to equivalent gains. In Albania, signals such as corruption scandals, legal instability, fiscal unpredictability, and rising structural costs create a persistent "loss frame" that encourages defensive strategies: less willingness to take risks, withdrawal from long-term investments, and a stronger preference for short-term capital preservation. Even when some economic indicators show slight improvements, people see these gains as fragile and not enough to offset ongoing uncertainty. As a result, conservative behavior becomes standard, slowing market activity and weakening the conditions needed for sustainable growth.

From a rationalist perspective, Utility Theory leads to the same conclusion. The costs of doing business such as administrative inefficiencies, bribery, tax ambiguities, reputational risks, and distorted competition from illegal capital often outweigh the expected benefits of formal investment. The dominance of informal and criminal capital in key sectors like construction, real estate, trade, and cash-intensive businesses creates artificial pricing structures that do not reflect true economic value. This distortion reduces profit margins, raises barriers to market entry, and logically causes economic actors to believe that the net utility is not enough to justify large investment commitments.

Together, these theoretical perspectives reveal a clear diagnosis: the Albanian market is seen as and truly functions as a high-risk, low-benefit environment where both emotional resistance and rational calculation discourage productive investment.

To break this dual cycle of mistrust and diminished utility, Albania must undertake a deep institutional and economic transformation. Key priorities include strengthening the rule of law, ensuring legal certainty in commercial transactions, improving judicial effectiveness, and establishing strong, irreversible mechanisms for asset confiscation and preventing criminal capital infiltration. Equally important are stabilizing fiscal policy, simplifying administrative procedures, and increasing tax transparency, all of which would reduce systemic uncertainty and lower operational costs for legitimate businesses. Restoring fair competition through close monitoring of sectors prone to money laundering is vital for re-establishing market integrity.

Beyond structural reforms, Albania must also address the psychological aspects of economic decision-making. Only through credible communication, measurable institutional performance, and a clear long-term reform vision can collective loss aversion be lessened and investor confidence shifted toward opportunity rather than risk. Strengthening institutional stability and public trust together is the only viable way to transform Albania's investment climate and realize its true economic potential.

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Disclosure Statement

The authors have no conflict of interest.

Authors Contributions

Bozheku E contributed to the development and integration of the Money Laundering concept in Albania within the framework of Utility and Prospect Theory, compiling existing documentation in this field. She proposed and explored extending behavioral finance to economic realities marked by high informality, money laundering, and corruption.

Profkola K contributed to the analysis and interpretation of economic and investment data and theories for the work.

Cucllari I drafted the results and conclusions in collaboration with the coauthors and critically revised it. All gave final approval and agreed to be accountable for all aspects of the work, ensuring integrity and accuracy.

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