

Bank of Albania

ANALYSIS OF DEVELOPMENTS IN THE EXTERNAL SECTOR OF THE ECONOMY

2021 Q1

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*The views expressed herein are solely of the author and do not
necessarily reflect those of the Bank of Albania.*

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I. BALANCE OF PAYMENTS HIGHLIGHTS

The data of the Balance of Payments in 2021 Q1 reflected the overall recovery of the economic activity. Nevertheless, the effects of the COVID-19 pandemic and the relevant containment measures remain present in sub-accounts, particularly in services flows.

The current account recorded a deficit of EUR 309.1 million¹, expanding by around 29.8% in annual terms. The increase of the deficit was mainly driven by the expansion of trade deficit in goods, as a result of the rapid increase of imports. Also, primary income account provided additional contributions. The current account deficit was assessed at 9.5% of GDP, or 1.7 percentage points higher than in the same quarter a year earlier.

Trade deficit in goods and services expanded by 25.3% in annual terms, determined by the expansion of the goods deficit by 15.2%. The increase in the import of goods by 19.2% was determinant in this regard. Also, the export of goods increased considerably (32.2%), by reflecting the post-pandemic recovery of the foreign demand, but the importing impact was stronger due to the high share of imports. Flows of services, differently from goods, have continued to trend downwards, compared to a year earlier, although, the falling pace was slower compared with the previous quarters. Export reduced by 10.1%, while imports by 17.6%.

Exports of services provided a stronger contribution than the exports of goods to the exporting total. As a result, overall exports reduced by 0.1%. On the other hand, the increase in the import of goods drove to a rise in the overall imports by 7.8% (despite the fall in the import of services).

The primary income account reflected a deficit of EUR 75.5 million, which is around EUR 17.7 million higher than a year earlier. The increase in the investments' income outflows drove to the expansion of deficit. On the other side, the surplus of the secondary income account expanded by 21.6% in annual terms. Annual growth of inward remittances was 10.6%.

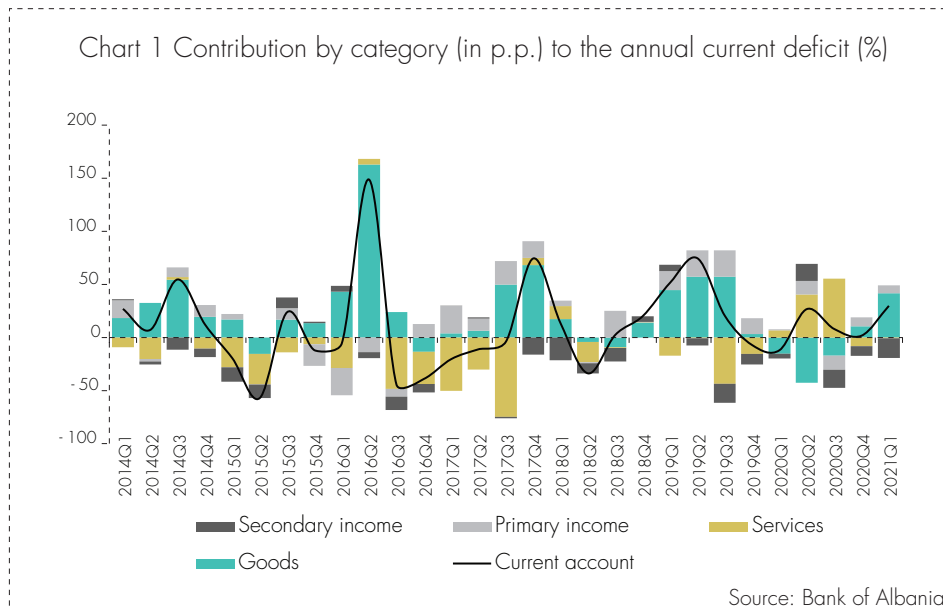
Net inflows in the capital account recorded EUR 98.0 million, standing around EUR 72.5 million higher than in the same quarter a year earlier.

In the financial account, net liabilities recorded EUR 252.1 million, around EUR 19.2 million lower from a year ago. Direct investments inflows decreased by around 1.5%. Meanwhile, liabilities of other investments expanded, due to "General Government" borrowing. Net inflows in capital and financial accounts managed to cover 113.3% of the current account deficit. The overall balance of payments resulted in an expansion of reserve assets by around EUR 74.5 million. The foreign exchange reserve stock, at the end of 2021 Q1, is sufficient to cover 9.6 months of import of goods and services, or 330% of short-term gross external debt.

¹ At the end of this material there is a summarizing table of the main developments of the Balance of Payments during the latest periods including the quarter under review.

II. CURRENT ACCOUNT

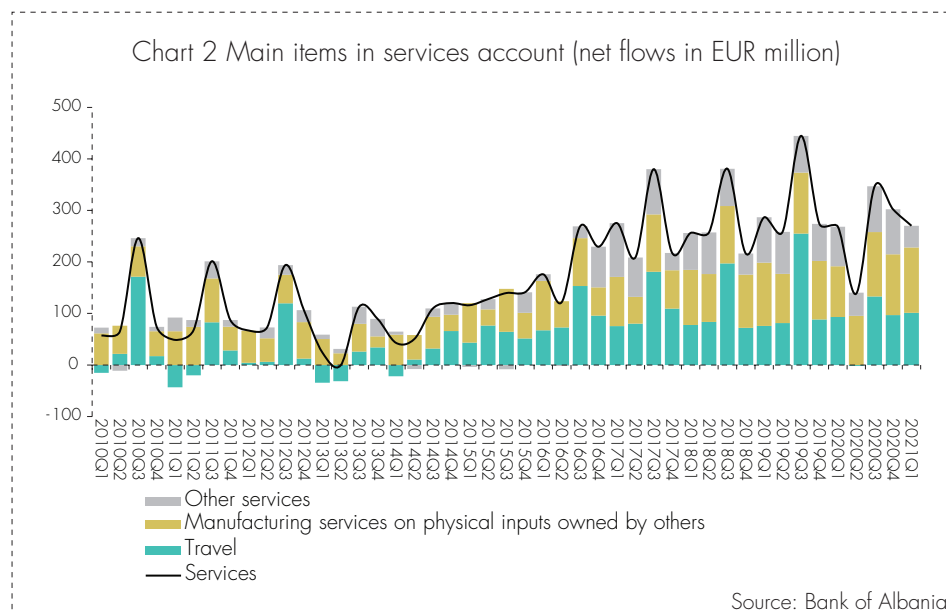
The current account recorded a deficit of EUR 309.1 million, in 2021 Q1, expanding by around 29.8% in annual terms. It was assessed at 9.5% of nominal GDP, or 1.7 percentage points higher than in the same quarter a year earlier. The performance of sub-accounts continues to show an asymmetry in terms of recovery, particularly if comparing goods flows with services flows.



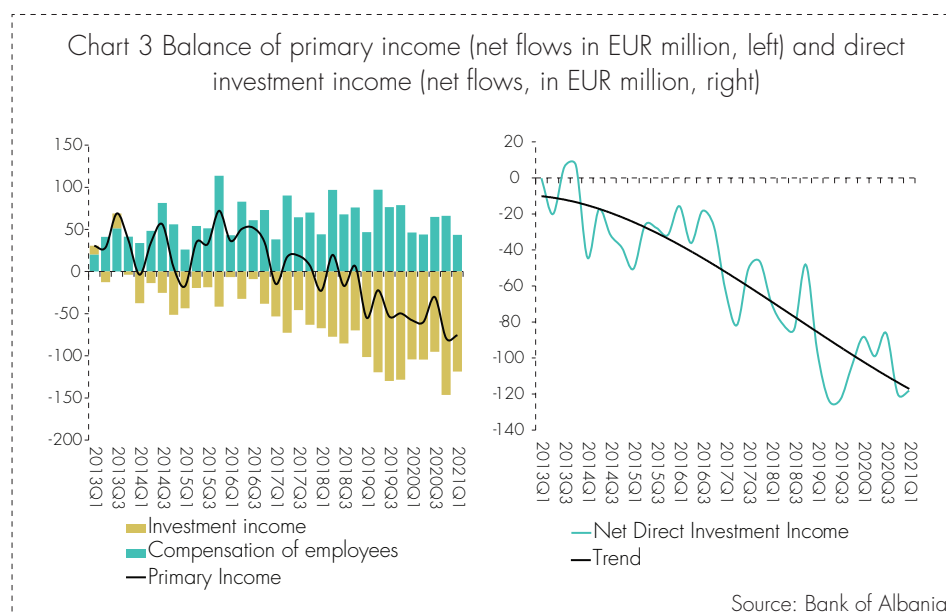
The expansion of the deficit is mainly determined by the increase in the deficit of goods by 15.2%. The latter was caused by the increase in the import of goods by 19.2%, in response to the recovery of the aggregate demand. At the same time, the export of goods rose by 32.2% in response to the recovery of the foreign demand for Albanian goods.

“Services” flows continued trending downwards (although at lower rates compared with the previous quarters), by reflecting a slower recovery compared with goods. Exports were reduced by 10.1%, while imports by 17.6%. In both cases, the fall of flows is related to the performance of the export of travel services (tourism). The presence of restrictive measures on the movement of citizens (both foreign citizens to Albania, and Albanian citizens to abroad) continues to be a strong obstacle for the recovery of these flows.

As a result of the stronger impact of “goods” sub-account, the overall trade deficit, in goods and services, expanded by around 25.3%. This effects best reflects the differences in terms of trade structure for exports and imports. In the case of imports, the higher share of goods against services has driven to an overall increase of imports by 7.8%. On the other side, the higher share of services against goods, in the case of exports, has driven to an overall fall of exports by 0.1%. The faster recovery of domestic aggregate demand and the slow recovery pace of foreign demand (particularly for services), is reflected in an expansion of trade deficit, consequently, of current deficit as well.



The net balance in the **primary income account**, registered a deficit of EUR 75.5 million, up by EUR 17.7 million compared with a year earlier. The increase in **direct investments outflow income** continues to be determinant in this regard. On the other hand, employee compensation income inflows continue to show a falling trend, although at lower rates compared with the previous quarters.



The surplus of the sub-account of **secondary income** expanded by around 21.6% in annual terms. Annual growth of **remittance inflows** was 10.6%, similar to the rate in the previous quarter.

Net cumulative inflows from services, primary income and secondary income accounts financed around 59.8% of the trade deficit in goods. This ratio is 4.6 percentage points lower compared with a year earlier, driven by the fast expansion in the deficit of goods due to the importing impact.

Chart 4 Remittances (net flows, in EUR million, left) and financing of trade deficit from net primary and secondary income and from services (right)



Source: Bank of Albania.

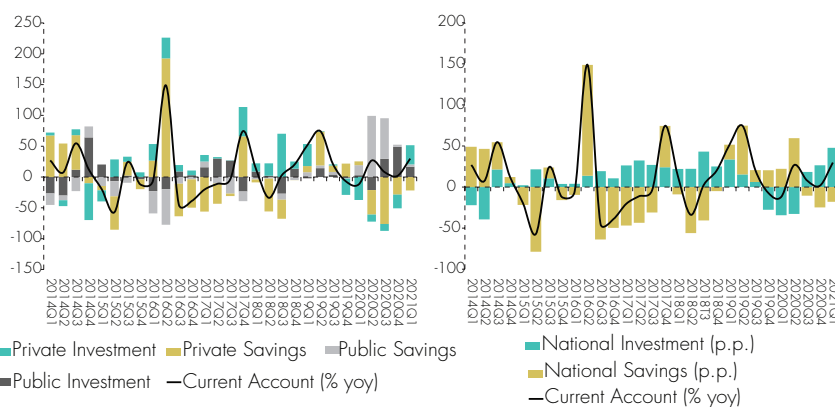
BOX 1 DEVELOPMENTS IN THE SAVING-INVESTMENT GAP

The saving-investment gap of the private sector was assessed at -7.3% of nominal GDP for 2021 Q1, around 0.3 percentage point deeper compared with a year ago. The ratio of private investments to nominal GDP was assessed at 15.0%, around 1.5 percentage points higher than a year earlier. Private savings to nominal GDP were assessed at 7.7%, around 1.2 percentage points higher than a year earlier. The increase in investments drove to the expansion of the gap of private sector.

In regard to the public sector, the gap is -2.2% of GDP, deepening by 1.4 percentage points, compared to the previous year. Public savings were estimated at 2.5% of nominal GDP, down by 0.5 percentage point in annual terms. Public investments were estimated at 4.7% of nominal GDP, around 1.0 percentage point higher compared with a year earlier. The high increase in public investments was determinant in the deepening of the public gap.

The ratio of national investments to GDP increased by 2.5 percentage points in annual terms. The ratio of national savings to nominal GDP increased by 0.7 percentage point. The slightly higher contribution of national investments was determinant in expanding by 1.7 percentage points the ratio of the current deficit to GDP, compared with the previous year.

Chart 5 Contribution of investments and savings indicators in the deficit dynamic (left) and their contribution to current account annual performance (right)



Source: Bank of Albania, Ministry of Finance and Economy, INSTAT and author's estimations.

III. CAPITAL ACCOUNT

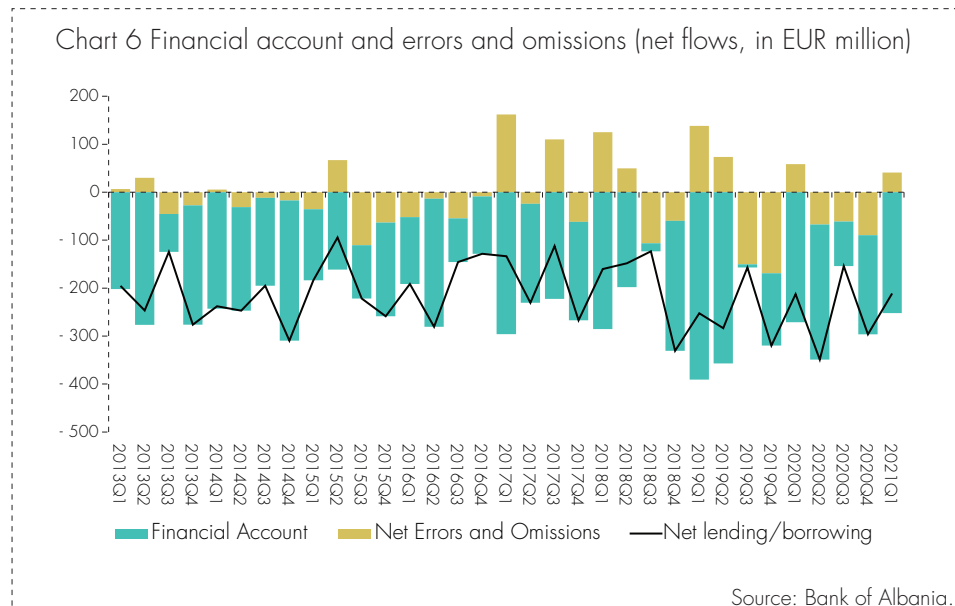
The capital account's surplus was around EUR 98.0 million, around EUR 72.5 million higher compared with a year ago. Net capital flows in this account are estimated at 3.0% of nominal GDP. The main impact is related to the "General Government" flows, due to the grants for reconstruction.

The combination of net transactions of the current and capital accounts provides the net position of the domestic economy, as net lender (surplus), or net borrower (deficit) against non-resident economies. In 2021 Q1, our economy reflects a net borrowing position of EUR 221.1 million. This ratio is 0.7% lower than in the same period a year earlier.

IV. FINANCIAL ACCOUNT

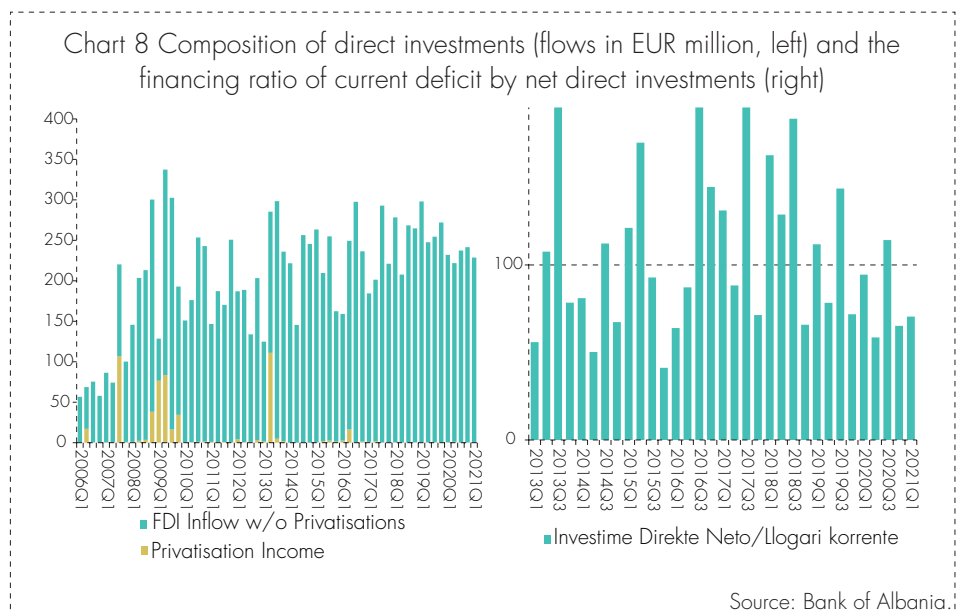
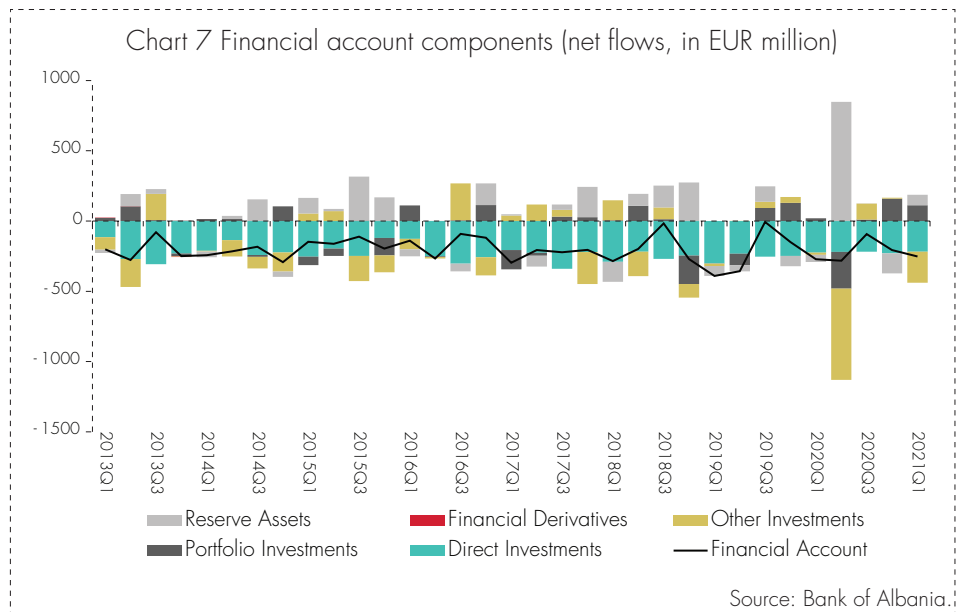
The financial account recorded net liabilities amounting to EUR 252.1 million, around 19.2% lower than a year earlier. Net liabilities of this account were estimated at about 7.7% of nominal GDP and financed 81.6% of current account deficit during this period.

Direct investment inflows decreased by 1.5%, by pursuing the trend of the previous year, but at lower rates. The driving impacts came from the "Mining" sector and "Energy" sector. On the other hand, the "Financial sector", "Real Estate", and "Professional, scientific and technical activities" provided increasing contributions.

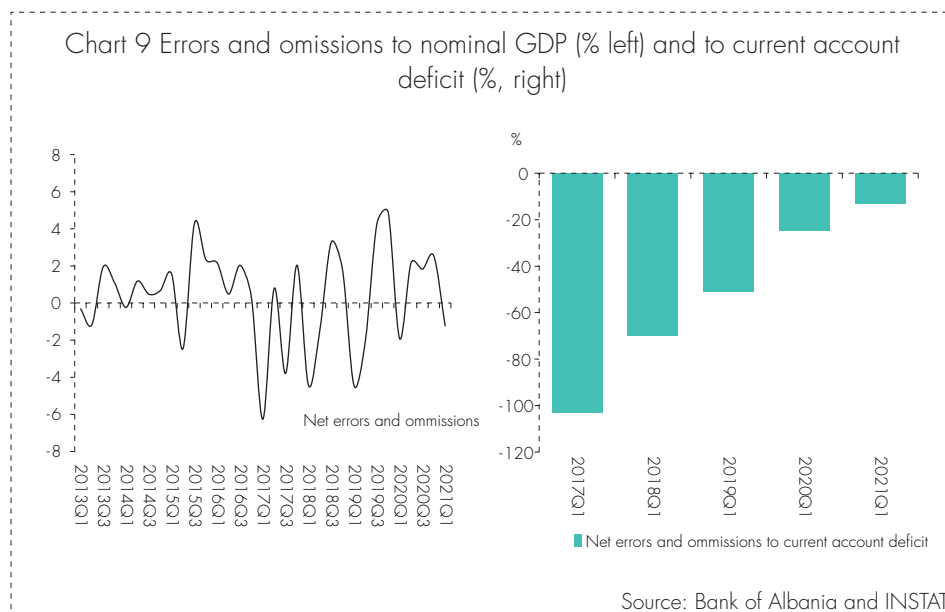


Portfolio investments reported net assets amounting to EUR 111.8 million, from EUR 20.1 million a year ago. "Deposit-taking corporations" have reflected increase of assets in the form of "securities"; meanwhile liabilities for this sub-account have been reduced. **Other investments** reported net liabilities

amounting to EUR 220.5 million, mainly due to the increase of “General Government” borrowing.

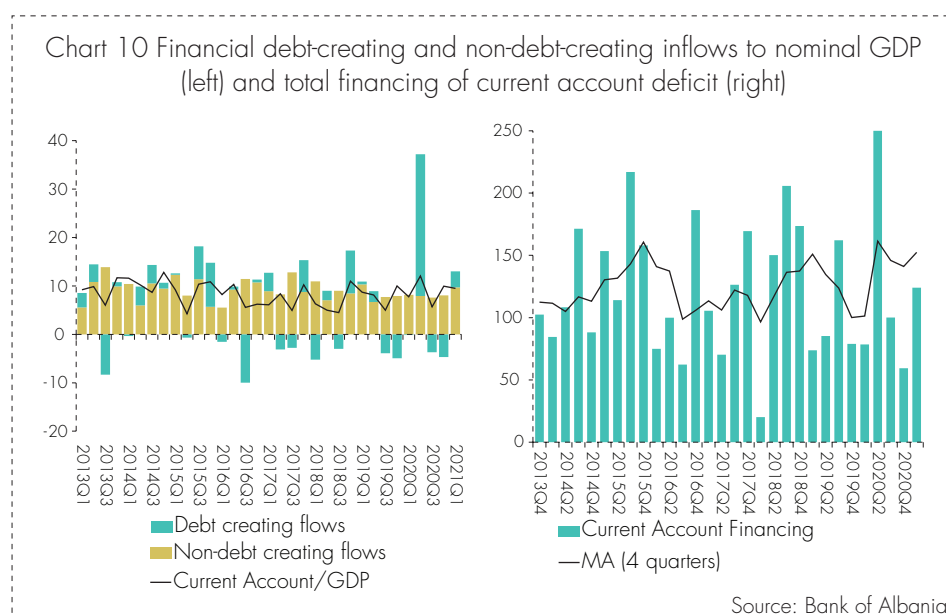


The overall balance of payments resulted in an expansion of reserve assets by EUR 74.5 million. At the end of March 2021, the foreign exchange reserve stock was considered sufficient to cover 9.6 months of import of goods and services or 330% of short-term gross external debt. Finally, “net errors and omissions” account resulted in an outflow of EUR 41.0 million which is assessed at 1.3% of nominal GDP.



V. PROFILE OF CURRENT DEFICIT FINANCING

The sustainability of current deficit financing is determined by the performance of debt-creating inflows against the most desirable non-debt-creating inflows². Non-debt-creating financial flows from net direct investments and from the capital account were assessed at 9.7% of nominal GDP. These were around 1.5 percentage points higher than a year earlier. The debt-creating financial flows were estimated at 3.3% of nominal GDP, around 3.5 percentage points higher than a year earlier.



² This breakdown serves to monitor the impact of financial and capital flows on Albanian's external debt. Non-debt creating flows include Direct Investments and net inflows of the capital account, whilst debt-creating flows include portfolio investments and other net investment.

By adding to foreign currency net debt-creating and non-debt-creating flows also the net errors and omissions, we obtain the overall financing of the current deficit. During the quarter under review, the current account financing ratio stood at 124.1%, translating into an increase in reserves. The financing ratio was around 45.6 percentage points higher compared with a year earlier.

Table 1 Balance of payments indicators (in EUR million)

	2019 Q3	2019 Q4	2020 Q1	2020 Q2	2020 Q3	2020 Q4	2021 Q1
Current account (in EUR million)	-176.5	-345.8	-238.0	-375.2	-190.7	-351.8	-309.1
y-o-y (%)	20.6	-7.1	-12.0	26.8	8.0	1.7	29.8
/GDP (%)	-5.0	-10.0	-7.8	-12.1	-5.7	-9.9	-9.5
Goods and services	-379.9	-569.3	-384.4	-517.0	-447.4	-577.5	-481.8
y-o-y (%)	5.6	-7.4	-5.7	-1.2	17.8	1.4	25.3
Exports, f.o.b.	1346.0	1019.1	847.3	488.2	852.6	836.3	846.4
y-o-y (%)	8.5	7.0	-4.5	-53.9	-36.7	-17.9	-0.1
Imports, f.o.b.	1725.8	1588.5	1231.7	1005.2	1299.9	1413.8	1328.2
y-o-y (%)	7.9	1.3	-4.9	-36.5	-24.7	-11.0	7.8
Net Travel	254.9	88.2	93.0	-1.9	133.1	96.9	101.4
Primary income	-53.4	-49.6	-57.8	-59.9	-30.2	-79.1	-75.5
Credit	106.0	108.5	69.7	80.8	96.6	90.0	69.8
Debit	159.4	158.1	127.5	140.7	126.8	169.0	145.4
Net income from Direct Investments	-123.1	-104.5	-88.2	-99.0	-86.2	-120.0	-118.2
Secondary income	256.7	273.1	204.2	201.7	286.9	304.7	248.3
Credit	288.4	310.4	244.1	241.9	333.5	350.3	286.5
Debit	31.7	37.3	39.9	40.2	46.6	45.5	38.2
Net Remittances	184.6	181.9	152.4	120.9	197.4	202.7	168.5
y-o-y (%)	8.6	7.5	1.5	-34.7	6.9	11.4	10.6
Capital account	19.7	26.2	25.4	26.1	36.6	55.4	98.0
Net borrowing/net lending	-156.8	-319.6	-212.6	-349.0	-154.1	-296.4	-211.1
Financial account	-6.3	-150.5	-271.2	-281.6	-93.0	-206.7	-252.1
y-o-y (%)	-62.5	-44.5	-30.6	-21.1	1365.4	37.4	-7.1
/GDP (%)	-0.2	-4.3	-8.8	-9.1	-2.8	-5.8	-7.7
Direct investments	-253.6	-248.5	-224.9	-219.9	-217.8	-229.4	-217.8
y-o-y (%)	-5.6	1.4	-25.6	-5.2	-14.1	-7.7	-3.2
Portfolio investments	93.4	129.8	20.1	-260.5	10.6	159.5	111.8
Financial derivatives	0.0	0.0	0.0	1.0	0.7	1.7	2.7
Other investments	44.2	41.2	-15.3	-649.4	114.0	5.8	-220.5
Reserve assets	109.7	-73.0	-51.1	848.2	0.3	-142.7	74.5
Errors and omissions	150.5	169.1	-58.6	67.4	61.1	89.7	-41.0

Source: Bank of Albania, INSTAT and author's estimations