

Bank of Albania

ANALYSIS OF DEVELOPMENTS IN THE EXTERNAL SECTOR OF THE ECONOMY

2020 Q3

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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 HIGHLIGHTS¹

The data of the Balance of Payments in 2020 Q3 reflected more moderate developments compared with the previous quarter. Although the impacts of the Covid-19 pandemic remain presents, they have been found to be milder.

The current account recorded a deficit of EUR 193.4 million², expanding by around 9.6% in annual terms. The increase of the deficit is mainly related with the contraction of the positive surplus in sub-account of services. Meanwhile, the sub-accounts of goods, primary and secondary income have had the opposite effect. The current account deficit was assessed at 5.8% of GDP, or 0.8 percentage point higher than in the same quarter a year earlier.

Trade deficit in goods and services expanded by around 17.8% in annual terms, a reverse performance compared with 2020 H1. The reason is related with the fact that the annual decline of exports remains still high, affected by the performance of services. On the other hand, the decline of imports resulted more moderated, related to the performance of goods. **Exports of goods and services decreased by 36.6%, in annual terms.** Annual growth was driven by the performance of export of services (in decline by 40.7% annually). The negative contribution is related with the contraction in annual terms of the export of tourism services by 58.7% Likewise, the export of goods decreased by 16.2% during the same period. **Imports of goods and services contracted by 24.6%, in annual terms.** The 53.0% decline in imports of services was determinant in this regard, affected by tourism services. Meanwhile, import of goods declined in annual terms by 6.4%, a rate significantly lower compared with the previous quarter (19.3%). **The performances of trade flows indicate a more rapid recovery of domestic demand (based on the performance of import of goods) compared with foreign demand, particularly that related with the export of services.**

Primary income account registered a deficit of EUR 30.4 million, which is EUR 23.1 million lower than a year ago. The contraction of the deficit was caused by the decline of investments' income outflows. **Also, the surplus of secondary income account expanded by 10.8% in annual terms,** mainly due to the increase in remittances by 6.9%. **Net inflows in the capital account** recorded EUR 36.8 million, standing around EUR 17.1 million higher than in the same quarter a year earlier.

¹ The most recent data on the balance of payments are as at 2020 Q3. As of 2008 Q1, the Bank of Albania prepares the Balance of Payments Statistics, in compliance with the BPM6 standards published by the IMF. The main differences between the actual and previous methodologies are synthesised in the following guideline:

https://www.bankofalbania.org/web/pub/01_commentary_for_changes_in_the_publication_of_external_sector_statistics_according_to_bpm6_june_2014_6689_1.pdf

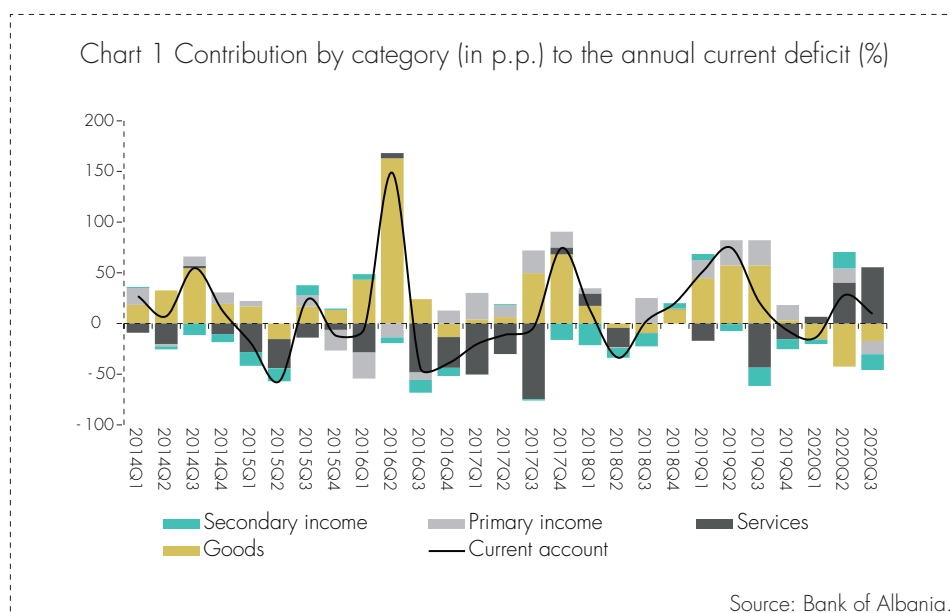
For the purposes of analyses, the Balance of Payments data from 2002 to 2007 are reclassified in line with the new methodology by the Monetary Policy Department.

² 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.

In the financial account, net liabilities recorded a value of EUR 92.2 million, around EUR 85.8 million higher compared with the previous year. Direct investments inflows decreased by around 6.8%. Net inflows in the capital and financial account managed to cover 66.7% of the current account deficit. The overall balance of payments resulted in an increase of reserve assets by around EUR 0.3 million. The foreign exchange reserve stock at the end of 2020 Q3 is able to cover 9.7 months of import of goods and services or 384% of short-term gross foreign debt.

II. CURRENT ACCOUNT

The current account recorded a deficit of EUR 193.4 million, in 2020 Q3, expanding by around 9.6% in annual terms. The expansion has been moderated compared with the previous quarter. It was assessed at 5.8% of nominal GDP, or 0.8 percentage points higher than in the same quarter a year earlier.

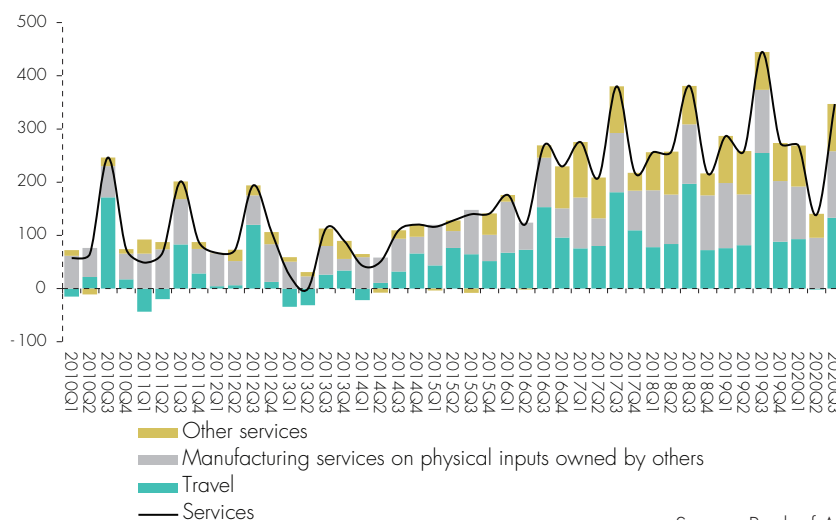


The expansion of the deficit is defined mainly by the decline in services' surplus, which contracted by 22.0% in annual terms. The decline of exports by 40.7% remains the reason for this development. Export of travel services decreased by 58.7%. Although the annual decline is lower compared with the previous quarter (87.6%), due to the higher comparative base of the third quarter, the annual decline in absolute terms is higher (EUR 459.0 million against EUR 443.7 million in 2020 Q2). In the case of imports the annual decline resulted 53.0%, also caused by travel services.

³ External debt statistics are reviewed in terms of maturity (publication of 2020 Q3). Total debt remained unchanged, but the share of short-term debt decreased and that of long-term debt increased. For this reason, the share of the reserve to short-term debt has increased significantly. For more details see: https://www.bankofalbania.org/rc/doc/Deklarata_BJB_Q3_2020_18025.pdf

The deficit of “goods” sub-account narrowed by 3.7% in annual terms. The main impact comes from the decline of imports by 6.4%. In parallel, the decline of export of goods registered 16.2%. Trade data indicate a more rapid recovery of goods flows compared with services. This suggests a faster recovery of domestic demand compared to the foreign one. For this reason, differently from the previous quarters, **the overall trade deficit in goods and services expanded by around 17.8%**. The trade deficit was assessed at 13.5% of GDP, around 2.7 percentage points higher than on year ago.

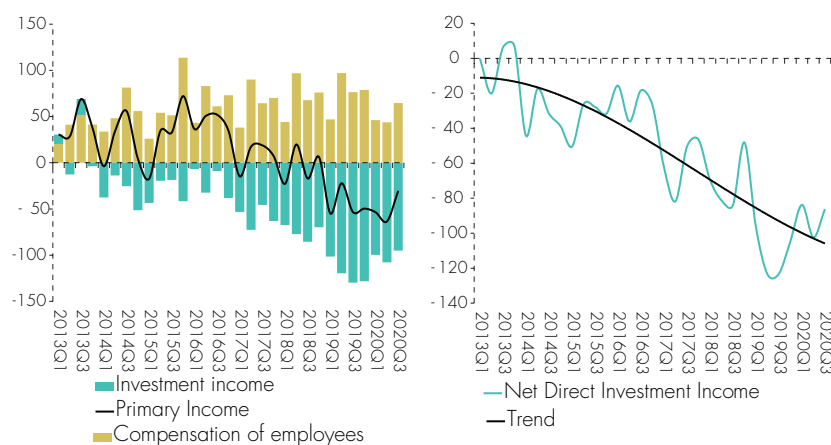
Chart 2 Main items in services account (net flows in EUR million)



Source: Bank of Albania.

The net balance in the primary income account, registered a deficit of EUR 30.4 million, from EUR 53.4 million in the previous year. The decline of the deficit was defined by the contraction of direct investments outflow income, and this as well is a development different from the previous quarters. During 2020 H1, the dynamic of the sub-account was defined by the decline of compensation of employees income inflows, as a component more sensitive to the impact of the pandemic (closing borders and the restriction of the movement of seasonal workers).

Grafik 3. Balance of primary income (net flows in EUR mln, left) and direct investment income (net flows, in EUR mln, right)

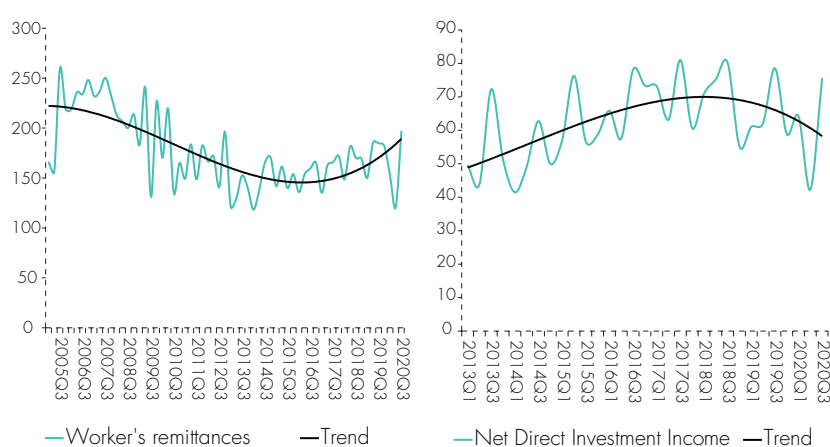


Source: Bank of Albania.

Investment income outflows resulted more stable due to the fact that foreign companies have repatriated profits generated in previous periods. The decline of these flows in 2020 Q3 indicates the impact of the pandemic in this sector of the economic activity.

The surplus of the sub-account of secondary income, expanded by around 19.1% in annual terms. This is related with the expansion of **remittance inflows by 6.9%**, another reversed dynamic compared with the previous quarter. Net cumulative inflows from services, primary income and secondary income accounts financed around 75.7% of the trade deficit in goods. This ratio is 2.9 percentage points lower compared to a year ago.

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



Source: Bank of Albania.

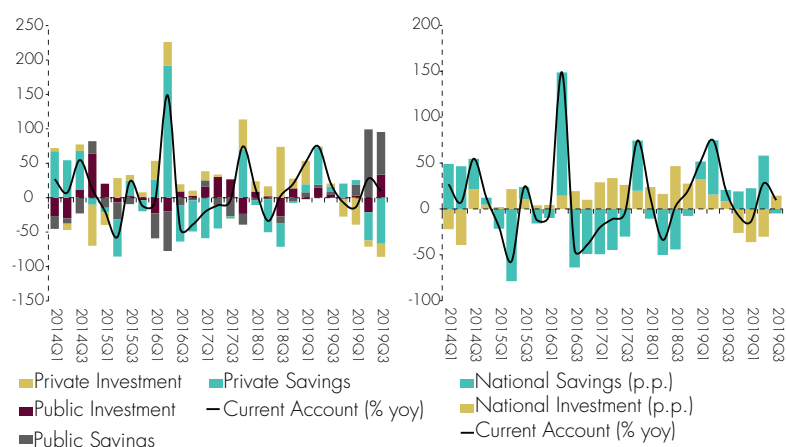
BOX 1 DEVELOPMENTS IN THE SAVING-INVESTMENT GAP

The saving-investment gap of the private sector was assessed at -0.8% of nominal GDP (negative value of the gap means that investments were higher than savings) for 2020 Q3, narrowing by 4.3 percentage points compared with a year ago. The ratio of private investments to nominal GDP was assessed at 17.6%, almost the same as a year ago. On the other hand, private savings to nominal GDP were assessed at 16.8%, or 4.3 percentage points higher than a year earlier.

In regard to the public sector, the gap is -5.1% of GDP, deepening by 5.1 percentage points, compared to the previous year. Public savings were estimated at 1.0% of nominal GDP, down by 3.1 percentage points in annual terms. Public investments were estimated at 6.1% of nominal GDP, around 2.0 percentage point higher compared to a year ago. The decline of savings was the main factor of the deepening of the public gap, also affected by the increase of investment.

The ratio of national investments to GDP increased by 2.1 percentage point in annual terms. On the other hand, the ratio of national savings to nominal GDP increased by 1.3 percentage points. The increase in national savings was determinant in expanding the ratio of current deficit to GDP.

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



III. CAPITAL ACCOUNT

The capital account's surplus was around EUR 36.8 million, around EUR 17.1 million higher compared with a year ago. Net capital flows in this account are estimated at 1.1% of nominal GDP. Net capital transfers for the account of "general government" resulted with a surplus of EUR 12.6 million, while those in "financial and non-financial corporations, households and non-profit institutions serving household", were EUR 24.2 million.

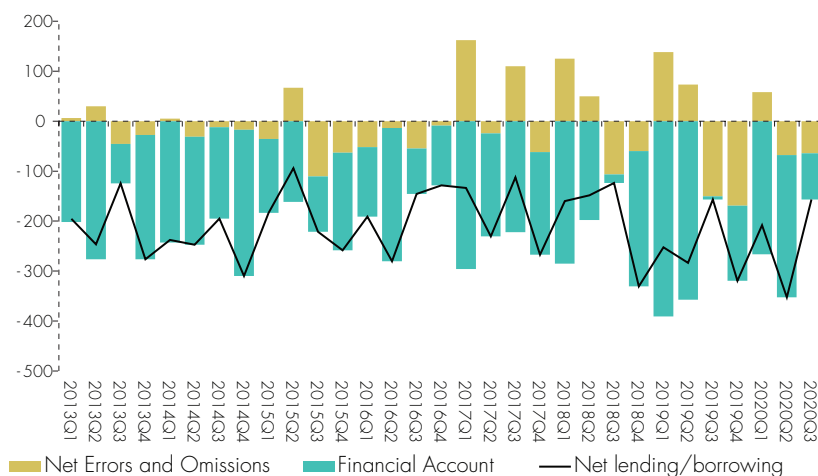
The combination of net transactions of the current and capital accounts provides the net position of the domestic economy, as net lender (surplus), or net borrower (deficit) against non-resident economies. In 2020 Q3, our economy reflects a net borrowing position of EUR 156.5 million. This ratio is about 0.2% lower than in the same period a year earlier.

IV. FINANCIAL ACCOUNT

The financial account registered net liabilities of EUR 92.2 million, around EUR 85.8 million higher compared to a year ago. Net liabilities of this account were estimated at about 2.8% of nominal GDP and financed 47.7% of current account deficit during this period.

Direct investments inflows decreased by 6.8%. The driving impacts came from the "Mining " sector. The annual rate of decline is lower compared with 2020 H1.

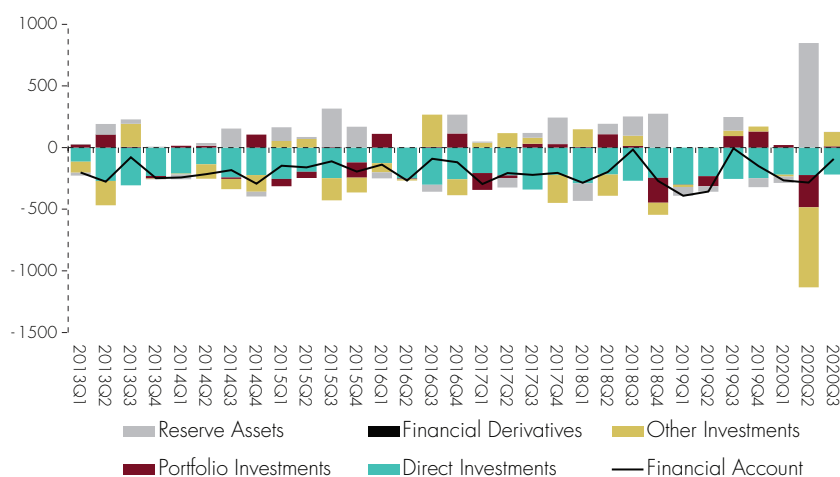
Chart 6 Financial account and errors and omissions (net flows, in EUR million)



Source: Bank of Albania.

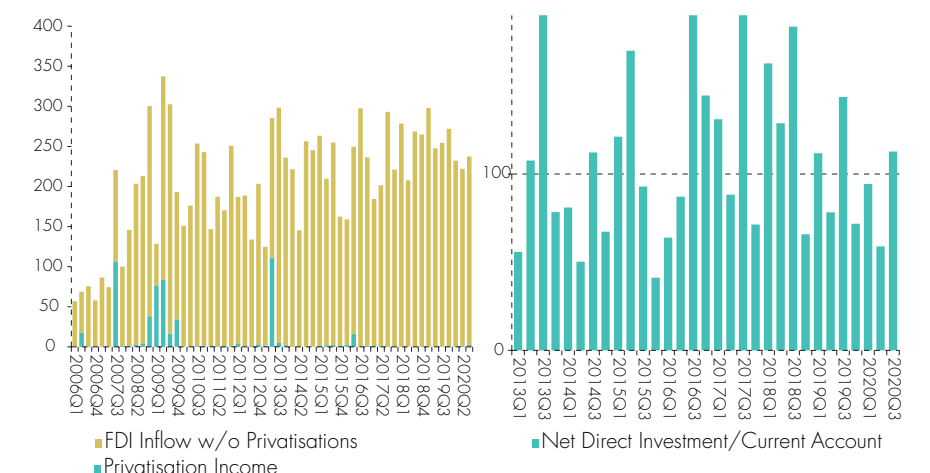
Net portfolio investments reflected net assets of EUR 10.6 million, from EUR 93.4 a year ago. The contraction of assets is related with the debt instruments of depository-corporations. Meanwhile, other investments registered net assets of EUR 115.1 million, related with assets in the form of currency and deposits.

Chart 7 Financial account components (net flows, in EUR mln)



Source: Bank of Albania.

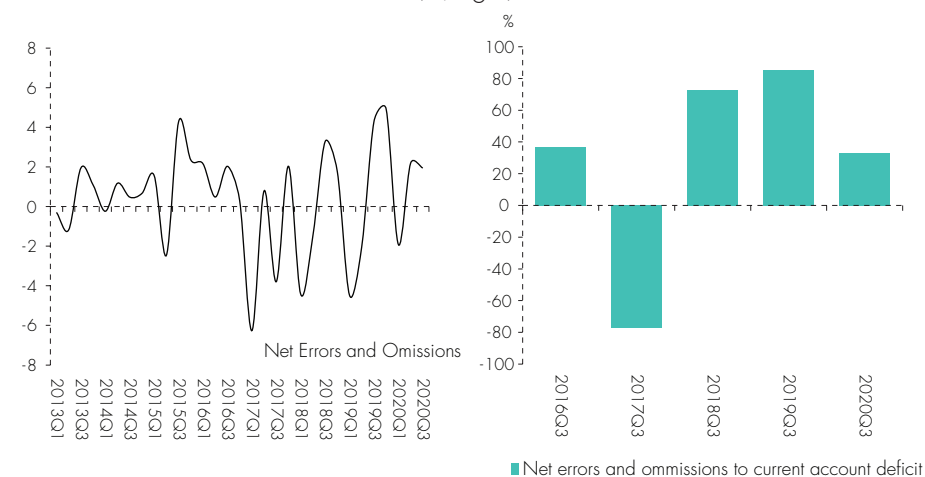
Chart 8 Composition of direct investments (flows in EUR mln, left) and the financing ratio of current deficit by net direct investments (right)



Source: Bank of Albania.

The overall balance of payments resulted in an increase of reserve assets by EUR 0.3 million. At end-September 2020, the foreign exchange reserve stock was around EUR 4.13 billion. This level is considered sufficient to cover 9.7 months of import of goods and services or 384%⁴ of short-term gross external debt. Finally, "net errors and omissions" account resulted in an inflow of EUR 64.4 million which is assessed at 1.9% of nominal GDP.

Chart 9 Errors and omissions to nominal GDP (% left) and to current account deficit (% right)



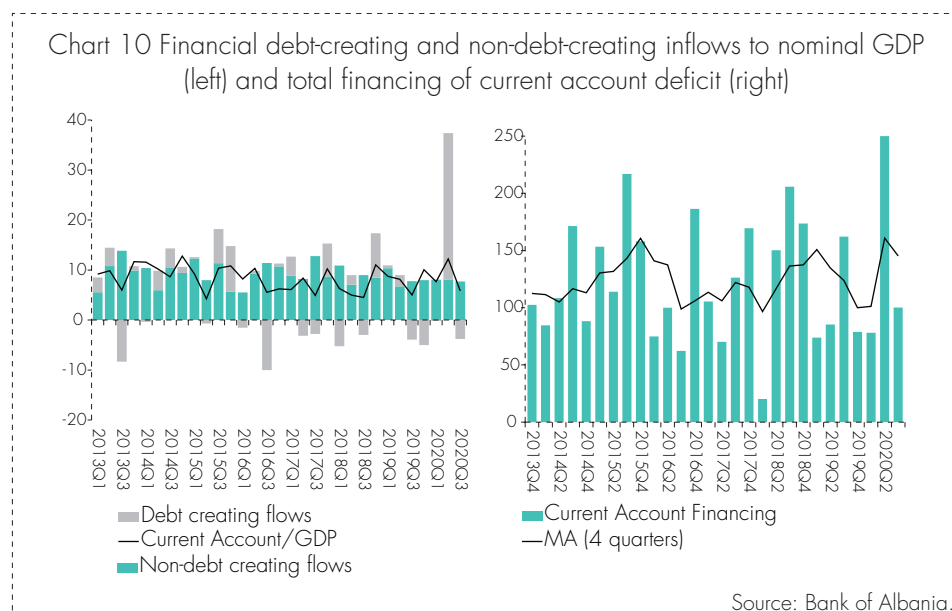
Source: Bank of Albania, INSTAT.

⁴ External debt statistics are reviewed in terms of maturity (publication of 2020 Q3). Total debt remained unchanged, but the share of short-term debt decreased and that of long-term debt increased. For this reason, the share of the reserve to short-term debt has increased significantly. For more details see: https://www.bankofalbania.org/rc/doc/Deklarata_BJB_Q3_2020_18025.pdf

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 inflows⁵. Non-debt-creating financial flows from net direct investments and from the capital account were assessed at 7.7% of nominal GDP. These were around 0.1 percentage point lower than a year earlier. The debt-creating financial flows were estimated at -3.8% of nominal GDP, around 0.1 percentage points higher compared to a year ago.

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 100.1%, translating into a slight increase in reserves. The financing ratio was around 2.5 percentage points lower compared with the previous year.



⁵ 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

Table 1 Balance of payments indicators (in EUR mln)

	2019 Q1	2019 Q2	2019 Q3	2019 Q4	2020 Q1	2020 Q2	2020 Q3
Current account (in EUR million)	-270.4	-296.0	-176.5	-345.8	-233.6	-378.6	-193.4
y-o-y (%)	51.6	74.7	20.6	-7.1	-13.6	27.9	9.6
/GDP (%)	-8.8	-8.2	-5.0	-10.1	-7.7	-12.2	-5.8
Goods and services	-407.7	-523.0	-379.9	-569.3	-384.2	-516.8	-447.5
y-o-y (%)	13.8	22.4	5.6	-7.4	-5.8	-1.2	17.8
Exports, f.o.b.	886.8	1059.2	1346.0	1019.1	847.5	488.4	853.5
y-o-y (%)	5.4	3.4	8.5	7.0	-4.4	-53.9	-36.6
Imports, f.o.b.	1294.5	1582.2	1725.8	1588.5	1231.7	1005.2	1300.9
y-o-y (%)	7.9	9.0	7.9	1.3	-4.9	-36.5	-24.6
Net Travel	75.9	81.5	254.9	88.2	93.0	-1.9	133.1
Primary income	-54.9	-22.2	-53.4	-49.6	-53.6	-63.5	-30.4
Credit	76.0	129.7	106.0	108.5	73.9	77.2	96.4
Debit	130.9	151.9	159.4	158.1	127.5	140.7	126.8
Net income from Direct Investments	-96.4	-123.4	-123.1	-104.5	-83.8	-102.4	-86.2
Secondary income	192.1	249.3	256.7	273.1	204.2	201.7	284.4
Credit	225.6	281.0	288.4	310.4	244.1	241.9	331.9
Debit	33.5	31.7	31.7	37.3	39.9	40.2	47.4
Net Remittances	150.2	185.2	184.6	181.9	152.4	120.9	197.4
y-o-y (%)	1.0	1.9	8.6	7.5	1.5	-34.7	6.9
Capital account	17.9	12.3	19.7	26.2	25.4	26.1	36.8
Net borrowing/net lending	-252.6	-283.6	-156.8	-319.6	-208.1	-352.5	-156.5
Financial account	-390.8	-357.1	-6.3	-150.5	-266.3	-284.8	-92.2
y-o-y (%)	37.0	80.4	-62.5	-44.5	-31.9	-20.3	1352.1
/GDP (%)	-12.7	-9.8	-0.2	-4.4	-8.8	-9.2	-2.8
Direct investments	-302.3	-231.9	-253.6	-248.5	-220.4	-223.3	-218.1
y-o-y (%)	4.1	6.3	-5.6	1.4	-27.1	-3.7	-14.0
Portfolio investments	-0.2	-82.4	93.4	129.8	20.1	-260.5	10.6
Financial derivatives	0.0	0.0	0.0	0.0	0.0	1.0	0.7
Other investments	-17.6	0.8	44.2	41.2	-14.8	-649.1	115.1
Reserve assets	-70.7	-43.6	109.7	-73.0	-51.1	848.2	0.3
Errors and omissions	-138.2	-73.5	150.5	169.1	-58.1	67.7	64.4

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