

A Look at the Trend and Features of the Romanian Current Account over the Past Years

Camelia Milea¹

Abstract: The balance of the current account provides the possibility of assessing the level of economic development of a country, its degree of foreign dependence and the international specialization of each economy. This article² aims to analyze the evolution of the Romanian current account balance and of some of its components during the period 2013-2016, showing the determinants and some of the factors influencing Romania's current account. Also, there are analysed the ways of financing the Romanian current account deficit, highlighting the advantages and disadvantages of this financing structure. The research methods used consist in comparative analysis in time, qualitative and quantitative evaluations, interpretations and correlations. The analysis shows that the services sector has developed, which increased the surplus of the services subaccount. Another result highlights that currently, the evolution of the current account deficit is sustainable in Romania. Also, the author concludes that the current account deficit of Romania has been and is still financed mainly from inflows of foreign direct investments.

Keywords: services; deficit; financing; investment; foreign credits

JEL Classification: F14; F21; F32; G01

1. Introduction

The balance of the current account, one of the main components of the balance of payments, provides the opportunity of assessing the level of economic development of a country, its degree of foreign dependence and the international specialization of the economy.

Starting with 2014, the international methodological framework used to compile the balance of payments and the international investment position has been updated, due to the requirements of the users of information, to the experience

¹ PhD, Scientific Researcher III, Center for Financial and Monetary Research Victor Slavescu, Romania, Address: 13 Calea 13 Septembrie, Academy House, B building, 5th floor, sector 5, 050711 Bucharest, Romania, Tel.: 0040213188106, int. 3510; fax: 0040213182419. Corresponding author: cami.g.milea@gmail.com.

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gathered by the theoreticians and practitioners and to the global microeconomic and macroeconomic evolutions. The new methodology is presented in IMF Balance of Payments and International Investment Position Manual, the sixth edition (BPM6), which replaces the older version, BPM5 from 1993. The new standards provided by BPM6 aim to enhance the completeness, the coherence and to harmonise the balance of payments with other sets of macroeconomic data such as the national accounts, the statistics of the governmental finances, the monetary and financial statistics, etc. (IMF, 2009, 2015)

The paper analyses the evolution and structure of the current account of Romania in the period 2013-2016 and outlines some directions of action for the management of the macroeconomic policies with impact on the foreign balance.

While before the onset of the international economic and financial crisis (particularly as of 2003) the deficit of the trade balance increased continuously on the background of higher imports than exports dynamics, this evolution slowed down after 2008, when the trade balance improved meaning that the high rate of deficit increase diminished. In 2015 and 2016, the increase rates of the trade balance deficit have been higher than in 2013 and than the year before, existing the possibility of returning to a high trade deficit.

2. Analysis of the Trend of the Current Account Balance and of Some of Its Components

In Romania, the evolution of the current account is influenced preponderantly by the trend of the goods and services subaccount. The trade balance (goods) holds the majority within this subaccount.

In 2013-2016, the exports and imports of goods and services, as well as the exports and imports of goods have increased moderately; both year to year, and compared to the year of basis, 2013. As of 2015, the annual rate of increase of the imports of goods and services was higher than the annual rate of increase of exports of goods and services. In the case of goods, the annual rate of increase of imports was higher than the annual rate of increase of exports in each year of the surveyed period (Chart 1). It can be noticed that the rate of increase of imported goods was higher than the rate of increase of imported services. (Milea, Ailincă & Bălăşescu, 2016)

The deficit of net exports decreased in 2014 on the background of an annual rate of increase of exports of goods and services higher than the annual rate of increase of the imports of goods and services, after which it increased in 2015 and 2016, when the comparative situation of the two annual rates of increase reversed.

This situation can be explained mainly by the continuous increase of the trade balance deficit in 2013-2016, on the background of an increasing surplus of the

services subaccount. This situation, if it will continue, can be regarded as an evolution of the Romanian economy towards the economic structure of the developed countries, which have a very developed services sector.



Chart 1.

Source: author calculation based on National Bank of Romania (NBR) data (National Bank of Romania, 2017)

Analysing the structure of services, it can be noticed that road transportation accounts mostly for the positive evolution of this subaccount.

An explanation is that Romania is the eastern border of the European Union and that it borders the Black Sea. As many imports of the European Union member states are done via the Black Sea, we may speak, mostly, of transit transportation through Romania.

Considering the high demand for transportation through Romania, in order to capitalize on this opportunity, given the precarious quality of the road infrastructure in Romania, the author considers to be absolutely necessary to develop the road infrastructure at a rapid pace, as priority of our country.

The structure of exports has improved somehow in 2016, on the background of an higher increase of exports of goods incorporating more innovation and of higher added value (medium high-tech exports have reached 47.6% in mid 2016 in the total exports of domestic companies). (National Bank of Romania, 2016)

The surplus of the services subaccount is also largely supported by the services of goods processing, but also by telecommunications, IT and information services. The processing services bring low added value to the national economy, but the

telecommunications, IT and information services bear high added value and their development should be supported. (Milea, Ailincă & Bălăşescu, 2016)

The exports of goods accounted for less than one third of the GDP in 2013 and 2014, which shows the low capacity of the exports to capitalise on the opportunities provided by the opening of the Romanian economy towards the international markets, the insufficient level of adjustment of the industrial production to the demands of the foreign markets, as well as the absence of a macroeconomic policy which should consolidate the Romanian exports. A positive fact is, however, the slight, although discontinuous, annual increase of the indicator, which shows an improving situation of the Romanian economy as the exports increase.

The consolidation of the positive trend, qualitatively and quantitatively, of the exports should be a priority for the macroeconomic policies during the following period, by attracting investments in high added value areas, by creating the premises for a more intense foreign trade activity in branches that presume a high level of innovation and technology, by increasing the capacity of the Romanian companies to adapt to the high standards of the foreign markets and by consolidating the capacity of these companies to cope with possible unfavourable evolutions.

The slight increase of the imports of goods during the surveyed period (Chart 1) can be explained both by the slowdown of the domestic demand (for the final consumption of households and for the intermediary consumption), and by the real depreciation of the national currency. The evolution of the imports should avoid creating a dependency of the national production on imports, which might affect the sustainable development of the Romanian economy, also ensuring a balance between the demand for national products and the demand for imported goods.

Both the imports of goods and those of goods and services increased slightly between 2013 and 2016, situation which is reflected in the evolution of the proportion of goods imports within the GDP, which increased slightly each year (Chart 1).

In each year of the period 2013-2016, the proportion of goods imports within the GDP exceeded the share of exports of goods within the GDP. This evolution has negative effects on the trade balance and on the level of national debt.

A possible explanation for the high level of Romanian imports might be the dependence of the domestic consumption on imports, particularly on consumer goods. Within this context, the sustainable development of the national economy presumes the orientation of the domestic consumption towards national products, both by stimulating the Romanian producers to provide the demanded goods, at high quality standards, and by intensifying the quality inspection made by the

authorities, as well as by raising the awareness of the Romanian consumers towards the national goods.

The trade deficit increased each year, between 2013 and 2016 (Chart 2), with higher rise in 2015 and 2016. The growth of the trade balance deficit is explained by the higher dynamics of the imports than that of the exports. The domestic demand for consumer goods is one of the major factors driving this evolution.

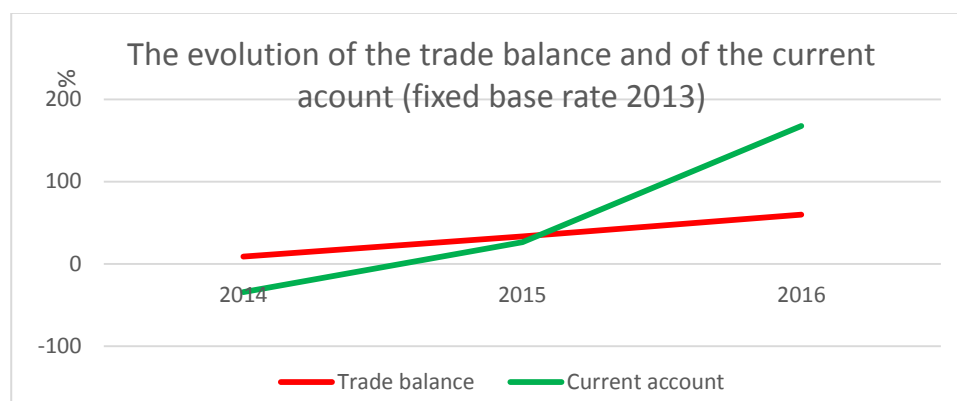


Chart 2

Source: author calculation based on NBR data (National Bank of Romania, 2017)

The increasing negative proportion of the trade balance deficit within the GDP shows a detrimental effect of the trade balance on the domestic economic process. Therefore, macroeconomic measures are required to stop the outflow of national income.

The current account deficit decreased much in 2014 compared to the previous year due to the significant increase of the surplus of the services subaccount and of the important reduction of the deficit of the direct investment income subaccount, even though the trade balance worsened and the surplus of the secondary income account decreased. The current account deficit increased in 2015 and 2016 due to the higher deficits of the trade balance and of the direct investment income subaccount, despite the increasing surpluses of the services and secondary income subaccounts (in 2015 compared to 2014) (Chart 2).

Another explanation for the increase in the current account deficit refers to the internal structural changes of the economy on the background of the process of convergence.

The important decrease of the current account deficit of Romania, as a proportion of the GDP, compared to the period before 2009, is a favourable element for the overall evolution of the Romanian economy, although it is not due to the

reorganisation of the national economy on sustainable bases, rather to the effects of the financial-economic crisis, which means it doesn't have a deep, lasting character. The low proportion of the current account deficit within the GDP between 2013 and 2016 shows only a slight negative effect of the current account balance on the internal economic process, the values of this indicator being below the conventional threshold of current account deficit sustainability (5% of the GDP). One can notice, nevertheless, that the evolution of this indicator in 2013-2014 reversed in 2015-2016, the proportion of the current account balance within the GDP returning to an increasing trend that can be explained by the consistent deterioration of the trade balance within the GDP in 2015-2016 (Chart 3).

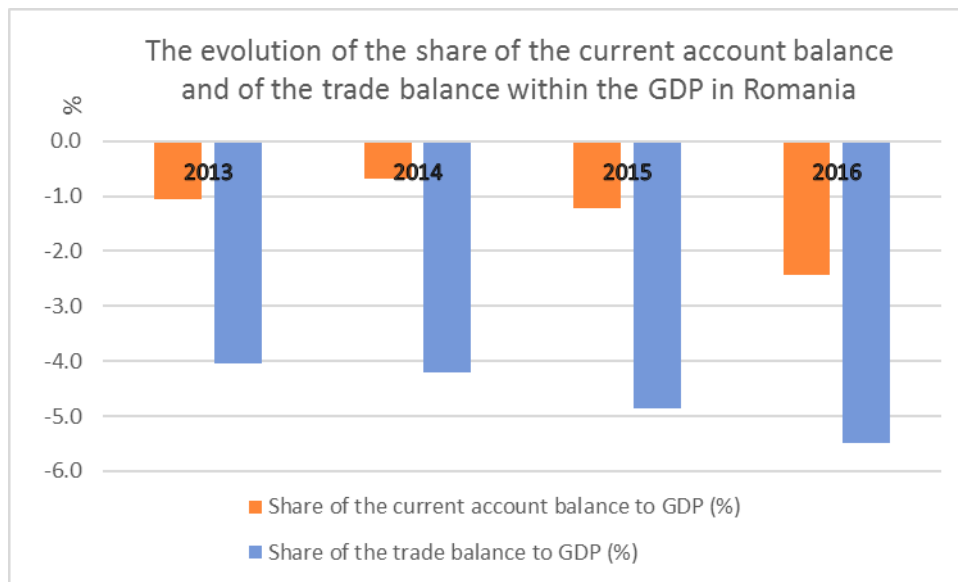


Chart 3

Source: Author calculation based on NBR data (National Bank of Romania, 2017)

We can presently speak of some degree of sustainability compared with the precrisis period (2005-2008); thus, according to RFS2016, the current account deficit in real terms was, at the end of 2016, almost 10 times lower than in 2007, and the rate of increase of the trade deficit is much smaller. However, the trend of increase of the current account deficit is expected to continue in the following period according to RFS2016; the European Commission has forecasted an increase in the current account deficit, to 2.6% of the GDP, in 2017, due to the rise in domestic consumption and demand.

Under these conditions, in order to avoid the return to high levels of current account deficit as before the occurrence of the effects of the international financial crisis, the author considers to be imperative the adoption of policies which should

ensure the current account deficit sustainability on the medium and long term, and monitoring the evolution of this indicator.

Although large according to the international standards, the current account deficit of Romania, as proportion within the GDP, has not been worrying, as long as its financing has been ensured, particularly by inflows of foreign direct investments. The Romanian economy seems to have opened abroad faster than it has restructured. (Milea, Ailincă & Bălăşescu, 2016)

Consistent, coherent and deep measures of reorganisation of the national economy should be taken, as soon as possible, in order to temper the increase of the current account deficit within the GDP.

If analysing the proportion of trade balance within the current account balance during the surveyed period 2013-2016, one can notice that the main cause of the current account deficit has been the situation and evolution of the trade balance (Chart 4), the other subaccounts of the current account having a reduced activity compared to the trade balance. Therefore, one can state that the trade deficit might decrease and could support the decrease of the current account deficit only if the implemented macroeconomic policies support the decrease of the imports (or of their value) (both those for the production and, particularly, those for consumption) and the increase of the exports, particularly by improving the quality and the added value of the exported goods.

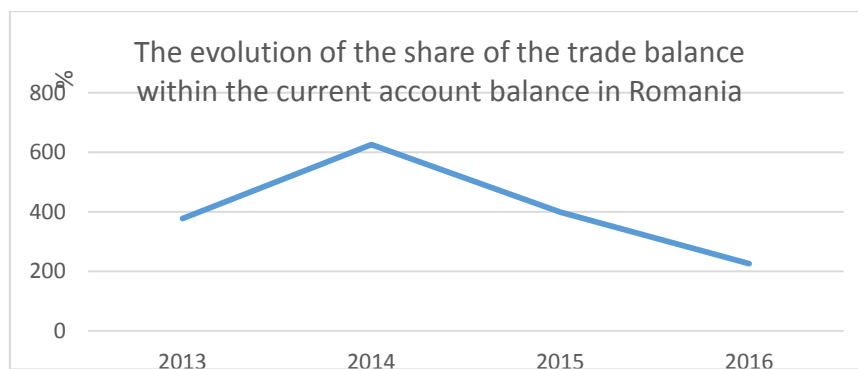


Chart 4

Source: author calculation based on NBR data (National Bank of Romania, 2017)

When we analyse the extent to which the imports are covered by exports (of goods and services) we notice that the indicator nears 100%, which shows that the trade balance deficit is offset in a certain degree by the surplus of the services subaccount (Chart 5).

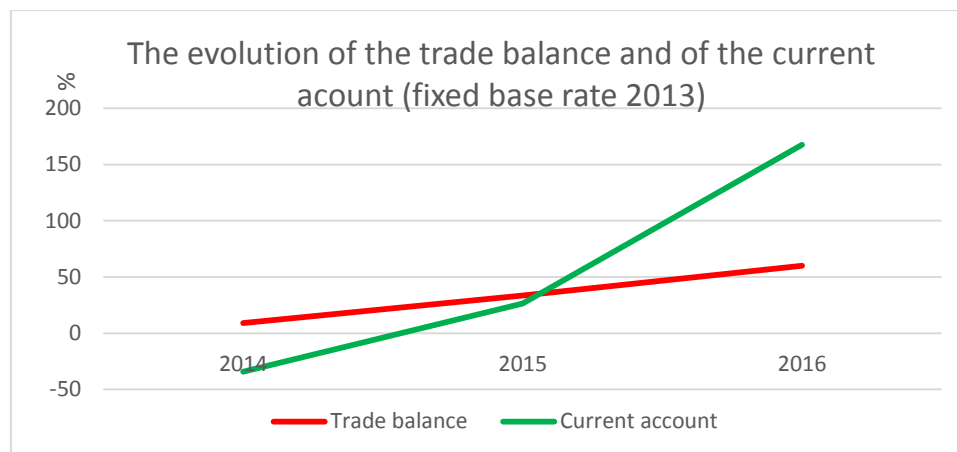


Chart 5

Source: Author calculation based on NBR data (National Bank of Romania, 2015, 2016)

Although the compensation for employees contributed little to the reduction of the current account deficit during the surveyed period, they influenced positively the evolution of the current account balance.

3. The Analysis of the Funding the Current Account Deficit

If until the start of the global economic and financial crisis there was an important level of foreign direct investments inflows to Romania, confirming the high level of trust of the foreign investors in our country, once the crisis began, the possibilities of attracting foreign direct investments decreased both at the international level, by an almost generalized risk aversion, and especially at the local and regional level, on the background of the regional tensions, such as the war from Ukraine, but also because of the characteristics of our country. Thus, the depletion of objectives that could be privatized, the precarious transportation infrastructure, the lack of fiscal facilities, of viable strategies to draw strategic investors, among others, resulted in a modest rate of attraction and capitalization of direct foreign investments in Romania.

The current account deficit of Romania has been and is still funded mainly from inflows of foreign direct investments which amounted from 2930 million euro in 2013 to 4804 million euro in 2016. In 2016, the balance of foreign direct investments was by 30.7% higher than in 2013.

In 2014 there was the highest level of current account deficit funding by the foreign direct investments, on the background of a strong decrease of the external deficit. In 2016, the level of current account deficit covering by the foreign direct

investments was lower than in 2014 and 2015, as the current account deficit has increased strongly (Chart 6).

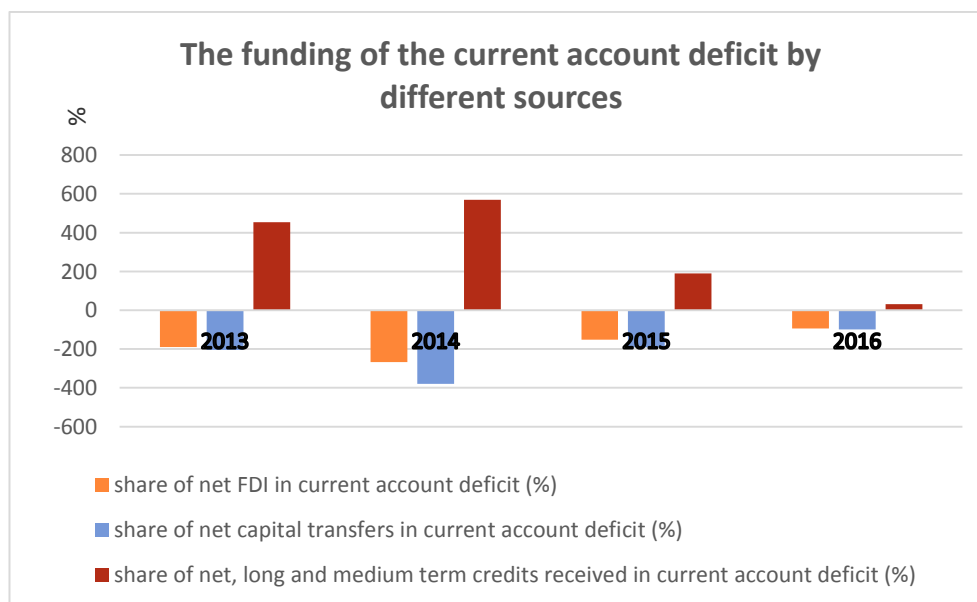


Chart 6.

Source: author calculation based on NBR data (National Bank of Romania, 2017)

Note: the negative sign shows the counter-balance of the current account deficit, while the positive sign signifies the contribution to the formation of the current account deficit

In Romania, the foreign direct investments are mainly investments of non-residents for 2013-2016, fact reflected by the balance of the direct investments subaccount. The inflows of foreign direct investments of non-residents have increased during the surveyed period, which reflects an improved perception of the foreigners about our country. Between 2013 and 2016 the direct investments of the Romanian abroad have increased also. In terms of the net balance, the direct investments decreased slightly in 2014 compared to 2013, followed by increase in 2015 and 2016, which signifies higher engagements of our country towards non-residents, therefore a negative influence on the international investment position.

According to Financial Stability Report [FSR] 2016, the advance payment of the equity and investment funds shares was the main element determining the increase of net inflows of direct investments. This reflects the improvement of capital inflows quality since 2015 and the reduction of instruments such as the debt. On the background of a higher confidence of the investors in the Romanian economy, the reinvestment of earnings remained positive and increased in 2016, after having negative values in 2008-2014. (National Bank of Romania, 2016)

Given the surveyed period (2013-2016), in 2014, the surplus of capital transfers contributed mostly to offsetting the current account deficit on the background of an important decrease of the current account deficit and of the high positive balance of the capital transfers compared to the other years of the surveyed period. The surplus of the capital transfers account signifies that Romania continues to receive funds from the European Union and from other international organisms, under different forms.

The evolution of the medium and long-term credits marked a turning point in 2011. Thus, in 2005-2010, the medium and long-term credits offset the current account deficit. As of 2011, however, within the context of paying back part of the credits received previously, this indicator contributed to the formation of the balance of payments (Chart 6), with decreasing absolute values in 2015-2016.

We may say that Romania pays, starting with 2011, for the massive foreign loans taken during the previous period. Thus, the increase of the foreign debt generates microeconomic risks (higher exposure to a possible external shock and stronger effects on the Romanian banking system), but also has macroeconomic implications in terms of the foreign debt sustainability. The increase of the medium and long-term foreign debt might bring about problems through the exchange rate channel (the sudden depreciation of the national currency would increase significantly the cost of foreign funding), through the confidence channel (the alteration of the feeling and perception of the investors would increase the risk premium, therefore the cost of foreign funding), through contagion (through a regional economic, political or social shock), or even through a shock within the national economy, of conjunctural or structural nature. We are currently facing some of these consequences (unfavourable perception of the investors, high cost of foreign funding). Chart 6 shows that both foreign direct investments and the transfers of capital contribute to covering the current account deficit. As of 2011, the net medium and long-term credits have increased the current account deficit.

The correlation of the current account deficit with its sources of financing should be the object of an in-depth analysis, considering that the inflows of foreign direct investments have been and still are a very important factor to offset the current account deficit in Romania, but with a decreasing share.

4. Conclusions

The exports and imports of goods and services increased moderately between 2013 and 2016, as well as the exports and imports of goods. Between 2014 and 2016, the rate of growth of the imports of goods was higher than that of the exports, which worsened the trade balance and the current account balance.

The structure of the exports of goods improved somehow in 2016, in the context of a faster increase of the exports of goods incorporating more innovation and higher added value.

One can also notice the development of the services sector, which increased the surplus of the services subaccount. Among the services, the road transportation accounts for most of the positive evolution of this subaccount.

In the context of the high demand for transport through Romania, given the precarious state of the road infrastructure in Romania, the author considers to be absolutely necessary to develop the road infrastructure at a faster rate as a priority of our country, in order to capitalise on this opportunity.

The low proportion of exports of goods within the GDP should generate the turn of the macroeconomic policies towards drawing investments in sectors with high added value, by creating the premises for a more intense foreign trade activity in branches which presume a high level of innovation and technology; respectively by increasing the capacity of the Romanian companies to adapt to the high standards of the foreign markets and to consolidate their capacity to cope with possible unfavourable conditions.

The evolution of the imports should avoid creating a dependency of the national production on imports, which might affect the sustainable development of Romania's economy, ensuring a balance between the demand for national products and the demand for imported products.

Currently, the evolution of the current account deficit is sustainable in Romania. The considerable decrease of the current account deficit, as proportion of the GDP, compared with the period before 2009, is not due to the reorganization of the Romanian economy on sustainable bases, but mostly to the effects of the economic-financial crisis, which means that its character is not long-lasting. The share of the current account deficit within the GDP between 2013 and 2016 is below the conventional threshold of sustainability (5% of the GDP). However, the evolution of this indicator in 2013-2014, reversed in 2015-2016, the share of the current account deficit within the GDP increasing. This might also be explained by the considerable deterioration of the trade balance, as proportion of the GDP, in 2015-2016, the evolution of the trade balance being the main cause of the current account deficit in Romania. Thus, one might say that the economy needs rather a moderation the commercial openness and a more efficient reorganisation.

Under these conditions, in order to avoid returning to the high levels of current account deficit in Romania from the period before the display of the effects of the international financial crisis, policies must be adopted in order to ensure the medium and long-term sustainability of the current account deficit and to monitor the evolution of this indicator.

The current account deficit of Romania has been and is still financed mainly from inflows of foreign direct investments, which decreased after the crisis has started due to an almost generalized risk aversion, to the regional tensions and to the characteristics of our country.

It can be noticed that both foreign direct investments and the transfers of capital contribute to offsetting the current account deficit. On the other hand, as of 2011, when Romania started to pay back partly the foreign loans received before, the medium and long-term credits exacerbate the current account deficit.

The correlation of the current account deficit with its sources of financing should be analysed in-depth, considering that the inflows of foreign direct investments have been and still are a very important factor in financing the current account deficit in Romania, but with a decreasing contribution (share).

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