



Why do external statistics matter? – A multidimensional approach in a context of macroeconomic imbalances

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The recent financial crisis highlighted the importance of an early detection and mitigation of macroeconomic vulnerabilities. In this context statistical compilers and analysts were challenged to develop enhanced methodologies and indicators, namely under the scope of external statistics. This paper proposes a multidimensional assessment of the external debt imbalances achieving a comprehensive and consistent approach by analysing not only the decomposition of the current and capital account balances but also how the economy is financed. This is possible through a deep insight of the financial account. Due to the existent interconnections one might analyse the current and capital account and whether a given deficit or surplus is explained by the component of goods and services or by the component of current income generated by the direct or portfolio investment, as an example. Simultaneously it is possible to observe in more detail the type of financial instruments; identifying if the net acquisition or disposal of financial assets is explained by the behaviour of a given institutional sector; detecting risk exposure of investment by country or identifying bilateral asymmetries that might exist with other commercial partners. It is a comprehensive and integrated approach rich of a variety of dimensions.

Keywords: external statistics, balance of payments; imbalances; direct investment; portfolio investment; income

1. Introduction

The recent financial crisis highlighted the importance of creating useful mechanisms capable to early detect and mitigate macroeconomic imbalances but that went beyond the criteria of government debt and deficit of the Stability and Growth Pact. Bearing this in mind, since 2011, a complex reform of the European governance framework has been implemented in the European Union (EU) in which is included the creation of the Macroeconomic Imbalance Procedure (MIP). Under the MIP, an alert system based on a macroeconomic scoreboard was developed in order to identify imbalances within and between individual EU countries – the Alert Mechanism Report (AMR). This scoreboard includes both stock and flow indicators which can capture shorter-term deteriorations, as well as the longer-term accumulation of imbalances. Currently it is built by 14 main indicators (along with their indicative thresholds), including some external statistics – the current account balance and the net International Investment Position (IIP). The current account balance is considered one of the most significant indicators in explaining the incidences of crises. Although surveillance under the MIP covers both current account deficits and surpluses, more attention is paid to economies with large current account deficits and competitiveness losses. A persistently high current account deficit leads to a highly negative net IIP. Besides its level, the composition of assets and liabilities in terms of maturities is also an important factor when assessing the overall vulnerability of the external position of a Member State.



This paper aims to develop a multidimensional assessment of the Portuguese external imbalances by analysing not only the decomposition of the current and capital account balances but also how the national economy has been financed during the last years.

2. The Portuguese external imbalances: an historical perspective

Portugal has historically displayed a negative current and capital account balance. Between 1963 and 1973, the current and capital account balance remained at around 1.2 per cent of GDP, declining to a deficit of nearly 5.6 per cent in the following decade (1974-1985), due to the combination of the international oil crises of the 1970s and the social and political upheavals in the aftermath of the Portuguese democratic revolution of 1974. The external imbalances accumulated during this period led to two International Monetary Fund (IMF) interventions in Portugal (1977/78 and 1983/85), which favored a rapid improvement of the goods and services balance. After 1995 and until the subprime crisis, the Portuguese current and capital account experienced substantial deterioration from - 2.5 per cent in 1996 to -11.8 percent in 2008. Since the end of 2009 a strong instability and a sovereign risk differentiation has increased markedly across the euro area, penalizing economies with larger fiscal and external imbalances and more significant structural problems, including Portugal. In the beginning of 2010 a sizeable impact on the Portuguese banks' financing capacity was installed and supplementary fiscal consolidation measures were successively adopted. In April 2011, the Portuguese government decided to give to the European Commission (EC) a request for financial assistance and on May 2011, Portugal has reached an agreement with the Troika of EC, the European Central Bank (ECB) and the IMF for a three-year 78 000 euro million bail-out.

Figure 1 tries to illustrate this reality, by presenting the evolution of Portuguese investment, national savings and the current and capital account balance. A carefully analyses of the referred chart evidences the association between the Portuguese successive current capital account deficits and the need for an intervention. Typically, these persistent deficits are mainly driven by the behaviour of the goods and primary income accounts, while services, secondary income and capital account have been contributing positively to the balance and capital account, as shown in Figure 2.

Figure 1: Current and capital account, investment and national saving

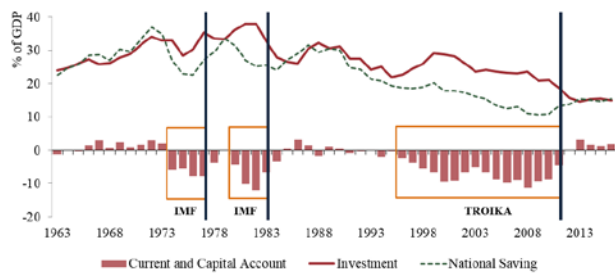
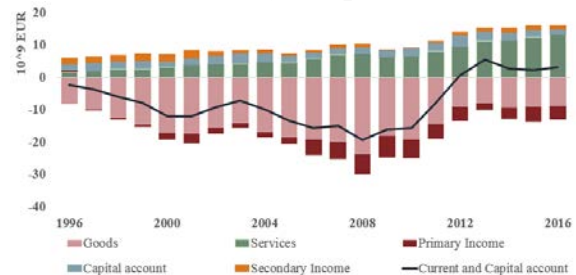


Figure 2: Portuguese current and capital account by component



3. Current and capital account in detail

Since 2012, the Portuguese economy has been registering a surplus on the current and capital account. This reversal was attributable to a combined improvement in the goods account deficit and an increase in the services account surplus.

The decrease in the goods account deficit started in 2009, with a significant boost in the performance of consumer, intermediate and investment goods exports. These transactions are mostly directed to other



UE countries. Assessing the bilateral trade and dependency to partner countries, in 2016, the main trading partners were Spain, France and Germany, which together represented about 50 per cent of total Portuguese exports of goods.

Figure 3: Portuguese goods exports (X) and imports (M)

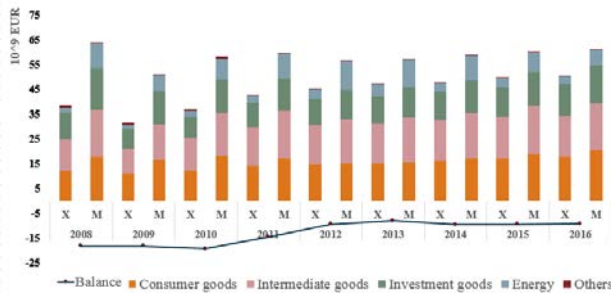
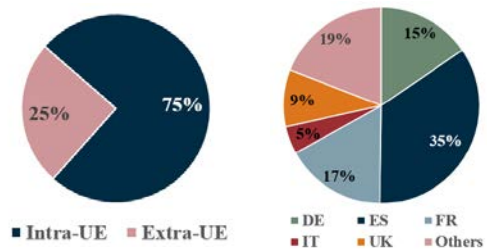
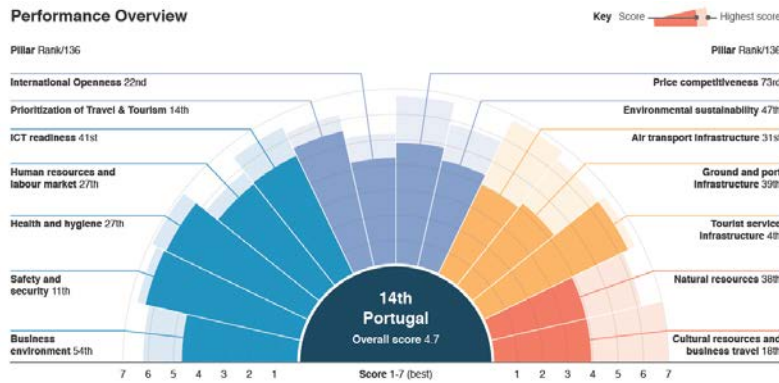


Figure 4: Portuguese exports of goods, broken down by geographical area, 2016



The travel sector is the most prominent sector of Portuguese exports of services, representing around 45 per cent of total in the 2008-2016 period. In the last years, it has been the major factor behind the increase of the services account surplus. The main four country visitors are from France, United Kingdom, Spain and Germany. In 2017, Portugal attained the 14th position in the Global Travel & Tourism Competitiveness Index. Besides its appealing weather, tourism services infrastructure, safety and security concerns and cultural resource helped driving tourism toward Portugal, as shown in Figure 5.

Figure 5: Portuguese tourism performance overview, 2017



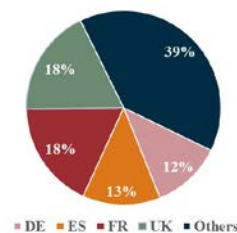
Source: World Economic Forum

The second most relevant sector in Portuguese exports of services is the transportation sector, with a share of around 25 per cent of the total of services during the same period.

Figure 6: Portuguese BoP Services account



Figure 7: Portuguese exports of tourism broken down by geographical area, 2016





4. Primary and secondary income balance

In Portugal, primary income is mainly determined by investment income – interests, reinvested earnings and income on equity among other (Figure 8). For the time-series considered, compensation of employees, income on reserve assets and the remaining primary income represent, on average, 40% of the primary income. On the basis of the available data it is also possible to analyse the income associated to each functional category like direct investment, portfolio investment, reserve assets and other investment and making possible to establish a link with the international investment position (IIP) performance.

On the other hand, the evolution of secondary income is largely driven by the migrant’s remittances. While in 2010 the emigrants’ remittances were mainly from France, Switzerland and Angola; in 2016 the emigrants’ remittances continue to be mainly from France and Switzerland but the United Kingdom swapped with Angola. Identifying the main host countries helps in delineating in a more accurate way policies targeted to specific groups (as an example, aiming to increase migrants’ savings).

Figure 8: Investment income

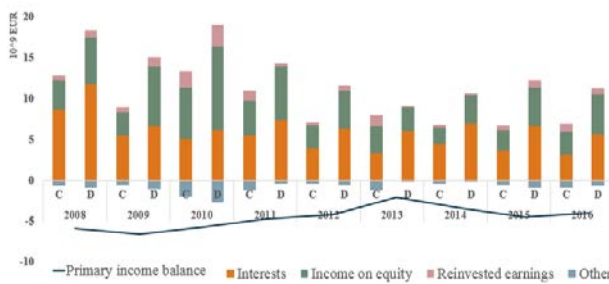
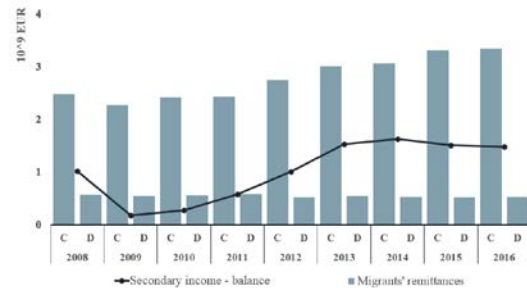


Figure 9: Secondary income: migrants’ remittances



In the case of Portugal, the capital account it is mostly composed by capital transfers and, in particular, by investment grants received from the European Union (EU). It is to be referred that the funds received from the EU are also recorded as subsidies in the primary income and as current transfers in the secondary income. Nonetheless, the evolution of the capital account illustrates an overall decrease of the EU funds in the most recent years. Links could be established with the time-series of gross fixed capital formation of the sector of non-financial corporations noting that the time of recording of these amounts in balance of payments corresponds to the moment amounts are received by the final beneficiaries.

Figure 10: Capital account





5. International Investment Position

A net lending of the current and capital account corresponds to a rise in net foreign assets (via redemption of liabilities or via an increase of assets). This was what happened in 2016, in Portugal, because the financial account recorded a rise in net foreign assets of €3142 million (Figure 11). These developments were partially due to the redemption of Treasury bills held by nonresidents (category portfolio investment) and an early repayment of loans granted by the IMF under the Economic and Financial Assistance Programme (category other investment).

Figure 11: Breakdown of the financial account by functional categories

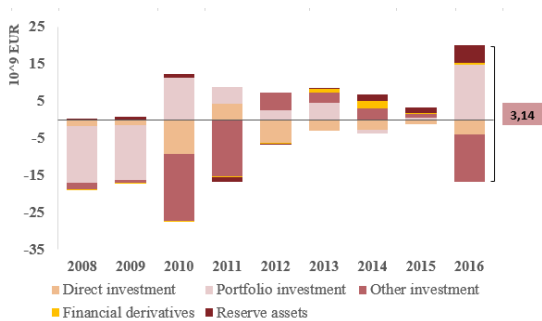
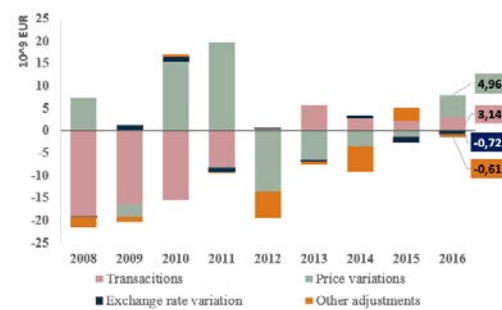


Figure 12: International investment position by component



Besides analysing the transactions, it is important to have into account the stocks. One of the most meaningful aggregated measure of the external accounts is the IIP. The composition of the IIP illustrates the vulnerability of the economy to changes in external market conditions. The implications for vulnerability differ among functional categories and instruments. The IIP shows how the transactions recorded in the financial account plus the price changes, the exchange rate changes and other adjustments contribute to explain the change of the financial assets or liabilities of a given country (Figure 12). For example, in 2016, Portugal’s IIP stood at €194.4 billion, corresponding to -105.2 per cent of GDP. The referred rise of €3142 million in net foreign assets (transactions) explained to some extent the change in the IIP because the change was, however, primarily explained by price changes due to the devaluation of Treasury bonds held by non-residents (category portfolio investment).

In addition, the breakdown of the international investment position by institutional sector illustrates the main contributors to a given evolution of the IIP. Referring to Portugal (Figure 13), it is possible to observe that in most recent years, general government (GG) has had an important role when explaining the change of IIP.

Figure 13: Breakdown of the International Investment Position by institutional sector

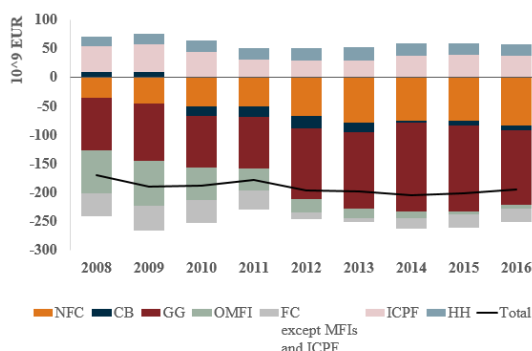
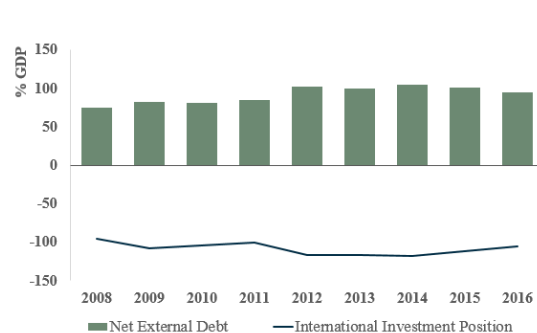


Figure 14: Net external debt and international investment position





Together with the IIP, external debt statistics is undoubtedly considered an indicator allowing external creditors to assess countries financial vulnerabilities.

Gross external debt corresponds to the sum of the non-equity liabilities components in the IIP statement of the economy, while the net debt is the difference between gross debt and the related financial assets that the country holds vis-à-vis the rest of the world (Matos (2013)). The net debt can be seen as an appropriate measure of external indebtedness, if one considers a country with a significant amount of assets which need to be considered when thinking about the solvency of its external accounts.

At the end of 2016, the net external debt of Portugal reached €174.6 billion, which represented a fall of €7.6 billion from 2015 and corresponded to a decrease from 101.5 to 94.5 per cent of GDP, the lowest value since March 2012 (Figure 14).

Final Remarks

External sector accounts are a rich data source for analysing risks based on: maturity mismatches that can put in hazard debt payments; currency mismatches; structure problems of a financial nature; solvency problems or dependence from a partner economy.

The level of data desegregation on this statistical domain disseminated by Banco de Portugal allow economists, analysis and policy makers to develop their own tailor made analysis. When correctly managed and understood, external statistics can be considered a powerful tool in the monitoring of economic developments.

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