10.6.1986

THE CURRENT ACCOUNT OF THE GREEK BALANCE OF PAYMENTS : PROJECTIONS OF OCTOBER 1985 AND MAY 1986

1. 1985 : expectation of last October and outcome

The 1985 current deficit turned out worse than expected at USD 3276 mn (10.0% of GDP) as against last October's projection of USD 2850 mn (8.7% of GDP). Of the deterioration of USD 426 mn, USD 204 mn occurred in oil trading, due mainly to the accidents of (private) oil exports; the remaining deterioration was split approximately equally between non-oil imports and the invisibles balance, the latter being hit by unexpectedly high interest payments related to unplanned drawings on the Bank of Greece's short-term facility.

2. Comparison of projections for 1986 made in October 1985 and May 1986

The most recent projection drawn up by the Ministry of National Economy and the Council of Economic Advisers differs considerably from that presented to the Monetary Committee last October (See table 1 part A).

- The original projection implied no change in the oil balance compared to what was then foreseen for 1985 (and therefore an improvement of USD 204 mn on the actual outcome for the oil account in 1985); on the other hand the original projection supposed that non-oil imports would be reduced by USD 400 mn (-5.5%) while non-oil exports would rise by USD 350 mn (+10.1%). In comparison to the initially expected 1985 figures the non-oil trade balance in 1986 was thus to improve by USD 750 mn, and by USD 864 mn in comparison to the actual 1985 outcome; the invisibles surplus was expected to rise by USD 400 mn in comparison with the initial expectation for 1985 and by USD 508 mn in comparison with the 1985 outcome.

- The new projection for 1986 is completely different. Based on an average oil price of USD 15/barrel in 1986, with which we agree, it has an improvement of USD 950 mn in the oil blance compared to the initial expectations for 1985 and of USD 1154 mn compared to the 1985 outcome. On the other hand the new projection for non-oil imports is USD 1000 mn worse than it was in October, although non-oil exports are now put USD 250 mn higher : the non-oil merchandise trade balance is now expected to show no change from the initial expectation for 1985 and an improvement of just USD 114 mn on the 1985 outcome. The new projection for 1986 also has an invisibles surplus USD 200 mn lower than last October's projection (roughly twice the corresponding "over-run" in the 1985 outcome); this reduction is largely the result of a higher projection for invisible payments other than interest, profit and dividends, the latter being restrained in the official forecast by the fall of interest rates. The new projection for the 1986 current account deficit is the same as the old projection in spite of the greatly reduced oil deficit. **The new projection for 1986 supposes an improvement of the balance of non-oil transactions (merchandise and invisibles) from the 1985 outcome of -USD 922 mn to -USD 500 mn; i.e. by -USD 422 mn, whereas last October's projection for 1986 supposed an improvement of the balance of non-oil transactions from -USD 700 mn then expeted for 1985 to +USD 450 mn, i.e. by USD 1150 mn.**

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3. Alternative measures

3.1. In ECU

Thus when the accounts are drawn up in US dollar terms, the new projection for non-oil merchandise trade in particular is very much less ambitious than the projection presented last October. However, Greek officials argue it is wrong to look at the figures in US dollar terms, since the US dollar has fallen in value, and that therefore a target of a given number of US dollars of deficit is much more constraining now than it was at the exchange rate of last October. In particular, it is argued that the figures should be converted to ECU since the ECU represents a reference point of constant purchasing power. Part B of table 1 is a recalculation of the exercise done in Athens converting part A into ECU. Last October's estimate for 1985 and last October's projection for 1986 have been converted at the average USD/ECU rate for the first three quarters of 1985, this being the rate used by Greek officials at that time; the outcome for 1985 is converted at the 1985 average rate and the new projection for 1986 at the average for the first quarter of 1986, following the practice of Greek officials. In ECU the new projection for the non-oil merchandise balance is about as constraining as the old projection, but the new projection for the invisibles surplus is very much less ambitious than the old one. The oil balance improves by ECU 1640 mn (56%) but the current account improves by only ECU 484 mn (21%). Even in ECU terms the new projection for non-oil transactions is much less constraining than the old one. **The new projection for 1986 supposes an improvement of the balance of non-oil transactions from a 1985 outcome of -ECU 1209 mn to -ECU 541 mn, i.e. by ECU 668 mn, whereas last October's projection for 1986 supposed an improvement from -ECU 957 mn then expected for 1985 to +ECU 615 mn in 1986, i.e. an improvement of ECU 1572 mn.**

3.2. In percentages of GDP

It is not obvious that the ECU is the best unit of measurement. In the context of a dollar falling rapidly against the ECU, the drachma has, in order to maintain its real exchange rate unchanged, to undergo a real appreciation against the dollar and a real depreciation against the ECU. Neither the US dollar nor the ECU alone can give a measure of the adjustment represented by a change of balance of payments target in terms of the balance between domestic absorption and domestic output : this can only be given by percentages of GDP. Part C of table 1 therefore converts part A to GDP percentages using the annual average DR/USD rate for both expectation and outcome in 1985; using for last October's 1986 projection the DR/USD rate assumed at that time; and using for the new projection the rate of the first quarter which is used by Greek forecasters for the whole of 1986. An extra column gives the results of using the DG II forecast for the 1986 average DR/USD rate to convert the new projection. As was to be expected, this method of evaluation makes much less of a change to the picture presented by the US dollar figures than does the ECU conversion. In terms of GDP percentages the new current account projection is more ambitious than the October projection to the extent of 0.6% of GDP (-12%) if one takes the official Greek view of the 1986 DR/USD exchange rate (but only to the extent of 0.3% of GDP if one takes the DG II view of the exchange rate). Keeping to the Greek view of the exchange rate, one notes that the 0.6% overall improvement results from a 3.3 point improvement in the oil account and a 2.7 point deterioration in the balance on non-oil transactions, and of the latter deterioration only 0.7 points could be attributed to the deterioration of the 1985 position from what was expected in October.

Last October, an improvement equal to 3.5% of GDP was expected in the balance of non-oil transactions compared to the 1985 outcome then expected. In the new official projection for 1986 non-oil transactions show only an improvement equal to 1.5% of GDP compared to the actual 1985 outcome.

3.3. A more discriminating approach

However, the two preceding methods of adjusting the USD figures are gross over-simplifications. They both involve applying the same exchange rate correction (ECU/USD in the first case and DR/USD in the second) to all the current account categories, whereas these categories in fact differ greatly in currency structure, i.e. the currencies in which suppliers and competitors incur their costs and in which customers form their spending plans. One important step towards a correct adjustment of the USD figures is to leave unchanged elements which are dollar-based in this sense and adjust only the remaining elements, at this level of simplification, by the ECU/USD rate. We consider that 22.1% of merchandise exports and 45.7% of merchandise imports are dollar-based; and that 28% of invisible receipts but 61% of invisible payments are dollar based. Thus Greece's current account payments have a much larger dollar element, because of the predominance of oil imports and interest payments, than do Greece's current account receipts. A rise of the ECU against the dollar was thus found (ceteris paribus and by its direct effects) to reduce the 1986 current account deficit as it was projected last October. In one example we have taken, a rise of 10.5% of the ECU against the USD was found to cut the current account deficit by 9.4%.

4. Justification of the initial projection for 1986

4.1. Was the initial projection for the 1986 current account, which was built into the adjustment programme and the Community loan process, completely unrealistic? Table 2 represents as far as possible a line-by-line re-working of the forecast for 1986 as it is seen in DG II. The starting point which, it is believed, would be accepted in Athens is the belief (a) that Greece will have "normal" net oil imports of 10.5 mn tons at an average cost of USD 15 per barrel and (b) that non-oil imports on a cash basis in 1985 had a leads and lags element of about USD 500 mn which will be neither repeated nor reversed in the current year. Leads and lags affecting other current account items are assumed to have been reversed within 1985.

4.2. Our forecast for non-oil import prices and export volumes is based on the DG II "consistency exercise" of May 1986, behind which lies the DG II forecast for the import volumes and export prices of the industrial countries individually; and an exchange rate and competitiveness hypothesis for Greece based on maintenance of that country's competitive position in terms of unit labour costs. Our forecast for Greece's import volumes and export prices results from our general forecast in which domestic demand falls 2.4% and the GDP deflator rises 21.8%; some allowance is made for the impact of the import deposit scheme on import volumes.

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4.3. We also take a more optimistic view of invisible receipts than Greek officials do : we believe that there will be a modest rise in travel receipts in volume terms and that the strong increase of world trade this year, and particularly the increase of world trade in oil, will be reflected in an increase in the volume of goods carried by sea, and that the devaluation will enable Greek shipping to have a larger share of this growing market. We also consider that the Greek officials' view of emigrants' remittances does not make full allowance for the exchange rate effect on the USD value of remittances from Europe; and that there should by some modest allowance for a rise of those remittances in ECU terms in view of the expected rise of wages in the EC (+6% in ECU terms).

4.4. Our own broad view is therefore that the coherence of the recovery programme can be defended, and the more favourable international environment now means that it is possible to move much more quickly to the point at which no net official borrowing will be necessary. Two features of the situation must however be noted :

- the adverse J-curve effects which would otherwise have been expected this year have been partly offset by the volume effects of the import deposit scheme; this scheme must be assumed to dissappear next year, when the favourable volume effets of the devaluation will have their full effect;

- the recovery programme and the present forecast rely heavily on the belief that there was a large element of adverse leads andd lags last year, and that this will not be repeated in 1986. This supposition rests to some extent on the workings of the regulations on international payments, but it also presupposes a certain minimal return of confidence. This return of confidence is probably also necessary for a satisfactory performance of emigrants' remittances and private capital flows. Our forecast for imports also depends in a more general sense on full implementation of the recovery programme.

5. Interpreting the outcome of the first quarter of 1986

5.1 Drawing conclusions for the whole year 1986 from the results of the first quarter is subject to high uncertainty : account should be taken of the falling dollar, the gains from oil prices, extraordinary invisible receipts, a strong seasonality and also the fact that projections based on that quarterly result have to compare to an 1985 base heavily distorted by speculative behaviour.

5.2 Table 3 shows that merchandise trade of the first quarter left a deficit of about 1,5 mio dollars, a slight improvement compared to the same quater of the previous year, and the invisibles surplus increased by more than 130 mio or 30%. In total, an improvement of 260 mio $ appears on the current account, compared to the same quarter of 1985, but the deficit seems, at first sight, too high compared to the expected outcome. However, a number of considerations based on closer examination of each item suggest that an improvement should be expected in the following months.

5.3 The oil trade, in the first place, has contributed an improvement of less than a hundred million $ whereas a total improvement of more that one billion can be reasonably expected for the year as a whole : the large improvement is still to come. Non-oil trade shows an improvement of 32 million $ in the first quarter, but it is difficult to analyse as the break-down between volume and price changes is not possible with the Bank of Greece data. Besides, both exports and imports expressed in dollars are subject to unnaturally high changes. Non-oil exports, however, seem to be developing in line with both the Greek and the DG II forecast in value terms. They also seem to be compatible with the DG II forecast for 7% volume increase in 1986 as a whole. Moreover, seasonally adjusted data for non-oil exports confirm both the quarterly and the monthly upward trend.

5.4 Non-oil imports are surrounded by the largest uncertainty. They rose by 5,7% in the first quarter but that rate should not normally continue through the year : the first quarter of 1985 was, according to the recent speech of the Minister of National Economy, free of speculation, it is then a good comparison for the first quarter of 1986; however, the remaining three quarters of 1986 will have to be compared to 1985 imports higher than normal by the non repeated amount of speculation. Therefore negative rates of change should normally appear on non-oil imports in the remaining months of 1986 if the austerity package works and if speculation has effectively ceased. In that sense the national forecast of 6,5% increase of non-oil imports in the whole year 1986 seems to be pessimistic. The development in March (1,5% on March 1985) would seem to support the idea of a slow-down in imports but if the data is seasonally adjusted the March figure depicts rather on acceleration. On the other hand, internal indicators (rush for housing and consumer durables, low bank deposits) do not readily suggest a turnaround in import behaviour; imports would, in that case, continue to increase.

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5.5 First quarter non-oil imports could also be interpreted to indicate a large fall in the volume of imports if converted in drachmas and deflated by import prices as included in the wholesale price index or by the two-month unit value of non-oil imports as observed in customs statistics. This result would be in line with the idea that the import deposit scheme has had its full effect on that quarter : nevertheless such an outcome should be interpreted with caution as that data is not directly comparable to settlements statistics and also because unit values often show large unexplained changes from one month to another.

5.6 It is, therefore, difficult to draw a conclusion from the data of the first quarter for non-oil imports. It could generally be said on the basis of those data that a moderate development is probable in the rest of the year for non-oil imports. Non-oil trade should therefore show a much larger improvement in the next months.

5.7 In total, the trade deficit of the first quarter could not and should not continue in the same rythme and, if policy is working, a large improvement is to take place in the subsequent months.

5.8 Among the invisible receipts, transportation is flattening out for the first time in the recent years, which seems to confirm both DG II and national forecasts. Emigrants remittances, on the other hand, are increasing and are in line with forecasts and so are EC transfers even if account is taken of the new MCA accounting and an exceptional transfer that took place in the beginning of the year. In total, the balance of invisibles seems to be on course to both the national and the DG II forecasts.

5.9 The balance on current account in the first quarter left a deficit of 874 mio \$. The above analysis shows that a strong improvement should be expected in the rest of the year if the government's policy succeeds and also because of the expected gains from oil. Therefore, the total current account deficit for the year should not be determined as the product of the quarterly result multiplied by the normally observed ratio of yearly deficit to deficit of first quarter, for in 1986 exceptional factors are at work which point to a much smaller deficit. The problem is the extent of the improvement which depends mainly on the effectiveness of the government policy on which there is no positive evidence as yet.

5.10 The private capital inflow improved slightly during the first quarter, which is in line with the modest improvement expected for the year as a whole.

Table 1 GREECE - BALANCE OF PAYMENTS CURRENT ACCOUNT

in 1984, 1985 (expectation and outcome) and 1986 (first and second official projections) - alternative measures -

	1984	1985: October estimate	1985: Outcome	1986: official projection: October 1985	1986: official projection: May 1986
A) USD mn.					
Merchandise trade					
Oil: exports	893	950	834	950	450
imports	3080	3100	3188	3100	1650
balance	-2187	-2150	-2354	-2150	-1200
Non-oil: exports	3501	3450	3459	3800	4050
imports	6665	7250	7373	6850	7850
balance	-3164	-3800	-3914	-3050	-3800
Total: balance	-5351	-5950	-6268	-5200	-5000
Invisibles					
receipts	5289	5150	5260	5650	5750
payments	2068	2050	2268	2150	2450
balance	3221	3100	2992	3500	3300
Current account					
balance	-2130	-2850	-3276	-1700	-1700
B) ECU mn.					
Merchandise trade					
Oil: exports	1132	1298	1094	1298	487
imports	3904	4236	4182	4236	1785
balance	-2772	-2938	-3088	-2938	-1298
Non-oil: exports	4437	4715	4537	5193	4382
imports	8447	9907	9672	9361	8494
balance	-4010	-5193	-5134	-4168	-4112
Total: balance	-6782	-8131	-8222	-7106	-5410
Invisibles:					
receipts	6703	7038	6900	7721	6233
payments	2621	2801	2975	2938	2662
balance	4082	4236	3925	4783	3571
Current account					
balance	-2700	-3895	-4297	-2323	-1839

Table 1 (ctd.)

GREECE - BALANCE OF PAYMENTS CURRENT ACCOUNT

in 1984, 1985 (expectation and outcome) and 1986 (first and second official projections) - alternative measures -

		1985		1986 official projection		
	1984	October estimate	Outcome	October 1985	May 1986 1)	May 1986 2)
C) % GDP						
Merchandise trade						
Oil: exports	2,6	2,9	2,6	2,9	1,2	1,3
imports	9,1	9,5	9,8	9,4	4,4	4,7
balance	-6,5	-6,6	-7,2	-6,5	-3,2	-3,4
Non-oil: exports	10,4	10,6	10,6	11,5	10,7	11,4
imports	19,7	22,2	22,6	20,7	20,7	22,2
balance	-9,3	-11,6	-12,0	-9,2	-10,0	-10,7
Total: balance	-15,8	-18,2	-19,2	-15,7	-13,2	-14,1
Invisibles:						
receipts	15,6	15,8	16,1	17,1	15,2	16,2
payments	6,1	6,3	6,9	6,5	6,5	6,9
balance	9,5	9,5	9,2	10,6	8,7	9,3
Current account:						
balance	-6,3	-8,7	-10,0	-5,1	-4,5	-4,8

1) official DR/USD rate
2) DG II DR/USD rate

Table 2

GREECE - ALTERNATIVE PROJECTIONS FOR 1986 BALANCE OF PAYMENTS

	1985 Base	DG II projection			Ministry projection
		volume (%)	price (%)	new value	
oil balance	-2354			-1165	-1200
non-oil imports	7373				
less leads and lage	513				
	6860	-8.5	+18.2	7419	7850
non-oil exports	3549	+7.2	+ 8.4	4019(1)	4050
merchandise balance	-6268			-4565	-5000
travel credits	1428	+2.5	+13.0	1654	1600
transport credits	1039	+6.0	- 1.0	1091	1030
migrants' remittances	801	+0.8	+11.5(3)	900	850
EC transfers	869			1050	1050
withdrawals(2)	451	+2.9	+ 8.4	503	500
other invisible receipts	673			720	720
total invisible receipts	5261			5918	5750
interest, profits and dividends	1237			1317	1250
other invisible payments	1037			1200	1200
total invisible payments	2269			2517	2450
invisible balance	2992			3401	3300
current account balance	-3276			-1164	-1700
balance on current non-oil transactions	- 922			1	- 500

(1) including USD 80 mn. extra olive oil exports.
(2) withdrawals from convertible drachma deposits.
(3) exchange rate effect only.

BANK OF GREECE
ECONOMIC RESEARCH DEPARTMENT
BALANCE OF PAYMENTS SECTION

Table 3

BALANCE OF PAYMENTS

(Millions US dollars)

	JANUARY-MARCH			CHANGE %		MARCH			CHANGE %	
	1984	1985	1986 *	1985	1986	1984	1985	1986	1985	1986
Imports	2.565	2.566	2.453	0,4	-4,4	841	840	795	-0.1	-5,4
Petroleum	675	823	611	21,9	-25,8	172	240	186	39,5	-22,5
Non-Petroleum	1.890	1.743	1.842	-7,8	5,7	669	600	609	-10,3	1,5
Exports	1.168	986	1.000	-15,6	1,4	421	325	300	-22,8	-7,7
Petroleum	285	245	128	-14,0	-47,8	113	64	36	-43,4	-43,8
Non-Petroleum	883	741	872	-16,1	17,7	308	261	264	-15,3	1,1
TRADE BALANCE	-1.397	-1.580	-1.453	13,1	-8,0	-420	-515	-495	22,6	-3,9
Invisible receipts	935	923	1.109	-1,3	20,2	290	299	324	3.1	8,4
Foreign travel	115	114	121	-0,9	6,1	44	42	42	-4,5	
Transportation	254	218	218	-14,2	..	82	71	79	-13,4	11,3
Emigrant remittances	205	162	176	-21,0	8,6	75	58	53	-22,7	-8,6
Interest-Dividents-Profits	29	32	24	10,3	-25,0	11	12	13	9,1	8,3
Withdrawals in drs. out of convertible deposits	52	117	107	125,0	-8,5	19	39	40	105,3	2,6
Miscellaneous	175	114	131	-34,9	6,1	59	41	35	-30,5	-14,6
EEC transfers	105	166	342	58,1	106.0	–	36	62		72,2
Invisible payments	464	477	530	2,8	11,1	169	181	199	7,1	9,9
Foreign travel	81	71	97	-12,3	36,6	27	26	31	-3,7	19,2
Government services	35	37	37	5,7		15	16	13	6,7	-18,8
Interest-Dividents-Profits	206	243	241	18,0	-0,8	86	101	106	17,4	5,0
Transportation	42	43	54	2,4	25,6	14	13	19	-7,1	46,2
Miscellaneous	100	83	101	-17,0	21,7	27	25	30	-7,4	20,0
BALANCE OF INVISIBLES	471	446	579	-5,3	29,8	121	118	125	-2,5	5,9
BALANCE OF CURRENT ACCOUNT	-926	-1.134	-874	22,5	-22,9	-299	-397	-370	32,8	-6,8
MOVEMENT OF CAPITAL (net)	944	1.044	911	10,6	-12,7	260	318	245	22,3	-22,6
Private Sector	361	356	247	-1,4	-30,6	112	53	117	-52,7	120,8
Entrepreneurial capital	66	52	56	-21,2	7,7	28	16	16	-42,9	
Real estate investment	99	94	81	-5,1	-13,8	37	31	27	-16,2	-12,9
Commercial bank loans	2	104	24		-76,9	–	11	27		145,5
Deposits in foreign exchange	66	24	37	-63,6	54,2	12	-17	27		
(Deposits in foreign exchange by individuals)	(63)	(34)	(67)	(-46,0)	(97,1)	(8)	(-13)	(26)		
Suppliers' credits	164	104	74	-36,6	-28,8	50	23	30	-54,0	30,4
Other	9	-3	-5		66,7	5	–	1		
Amortization	-45	-19	-20	-57,8	5,3	-20	-11	-11	-45,0	
Public Sector	583	688	664			148	265	129		
Central Bank (1)	500	526	-104			184	184	-28		
Government	18	11	876			8	8	198		
Public enterprises	177	218	-13			36	111	-9		
Suppliers' credit	-2	15	–			–	1	–		
Allocation of SDR's	–	–	–			–	–	–		
Amortization	-110	-82	-95			-80	-39	-32		
ERRORS AND OMISSIONS	-117	41	-50			-40	89	-76		
Difference resulting from a revaluation of gold holdings	–	–	110			–	–	-8		
OVERALL BALANCE	-99	-49	97			-79	10	-206		
IMF Credits	–	–	–			–	–	–		
Official reserves	-88	-48	101			-67	10	-207		
Clearings	-11	-1	-4			-12	–	-1		
Official reserves (end of period)	954	1.055	1.835 **			954	1.055	1.835		
Clearings	112	95	60			112	87	60		

(1) Central Bank: - Long-term	15	519	86	-1	20	–
-Short-term (net)	485	7	-190	185	164	-28

* Provisional data

** On December 31st 1985 gold holdings have been revalued on the basis of the 65 per cent of the average market price of gold during December 1985. This price will be applicable during 1986 (up to 30.12.86).
Beginning January 1986 data on gold and foreign exchange holdings exclude the deposits made with the European Monetary Cooperation Fund of the gold and gross U.S. dollar holdings. On the other hand, holdings of European Currency Units [illegible]