

*Tauno Tyllinen**

Estonia: the current account deficit remains high

Estonia was affected by the slowdown in the global economy in 2003. The GDP growth rate dropped from 7.2% in 2002 to 5.1% in 2003: mainly the outcome of impaired export opportunities. In the first quarter of 2004, however, the country's GDP rose by 6.8%.

Domestic demand rose by 7.3% in 2003. Both private and public consumption increased some 5-6%. The increase in private consumption expenditure was supported by attendant strong growth in lending (38.4%) and palpable increases in real wages (8.5%); this was further reflected in the rise in imports of goods (13%) and retail sales (10%). The growth rate of gross fixed capital formation declined somewhat, yet remained high (11.5%).

Broken down according to the main branches of the economy, value-added increased most in mining and quarrying (10%) and manufacturing (over 8%), followed by financial intermediation (close to 8%) and construction (7%). Value-added decreased in both forestry (10%) and fishing (7%). Manufacturing accounted for 19%, transport, storage and communications for 16% and wholesale and retail trade for 14% of total value-added. New manufacturing capacity is mostly export-oriented, while outsourcing and subcontracting account for a large share in manufacturing output.

In 2003, Estonia recorded its lowest inflation rate since the onset of transition, thanks to favourable import prices and a drop in food prices. After slowing down in the first quarter of 2004 to 0.4% year-on-year, inflation increased again in May as higher excise taxes were levied on fuel, sugar and certain other products following Estonia's accession to the EU.

The foreign trade deficit (EUR 1.7 billion) increased to 23% of GDP in 2003. Imports of goods grew last year by 13%; exports by less than 10% (customs statistics). Estonia's current account deficit remained high in 2003, amounting to 12.6% of GDP; this was mainly the outcome of a pronounced increase in the volume of imports. Last year FDI net inflow funded 61% of the current account deficit. At the end of December 2003, FDI stock amounted to EUR 5.1 billion and the country's central government external debt was only 3.2% of GDP.

The GDP growth forecast for 2004 ranges between 5.1% and 6.0%. Recovery of export demand in the EU and the CIS countries will facilitate growth. With export revenues rising and domestic demand declining, it is expected that the current account deficit will drop from 12.6% of GDP in 2003 to below 10% in 2005. Given the price and tax adjustments necessitated by the country's accession to the EU, consumer prices in 2004 are expected

* The author is special editor at the *Economic Trends Magazine*, Statistics Finland, Helsinki.

to rise on average by nearly 3%. A balanced budget is expected for this year; it is most likely to turn into a minor deficit in 2005 on account of the ongoing tax reforms. Given budgetary discipline to date, the low rate of inflation and a public debt of 5.8% of GDP, the announcement that Estonia entered the ERM II on June 28 came as no surprise. The central rate of the kroon to the euro was set at 15.6466.

Table EE

Estonia: Selected Economic Indicators

	1999	2000	2001	2002	2003 ¹⁾	2003 1st quarter	2004	2004 forecast	2005
Population, th pers., mid-year ²⁾	1375.7	1369.5	1364.1	1358.6	1353.8	.	.	.	.
Gross domestic product, EEK mn, nom.	81639.7	92717.1	104337.7	116869.0	125832.1	29002.2	.	137000	149000
annual change in % (real)	-0.1	7.8	6.4	7.2	5.1	5.8	6.8	5.5	5.7
GDP/capita (EUR at exchange rate)	3793	4327	4888	5498	5940	.	.	.	.
GDP/capita (EUR at PPP - wiiw)	8040	9010	9610	10450	10860	.	.	.	.
Gross industrial production ²⁾									
annual change in % (real)	-3.4	14.6	8.9	8.2	9.8	12.8	7.7	8	8
Construction industry ²⁾									
annual change in % (real)	-13.4	18.7	5.5	21.8	5.0	1.4	28.1	.	.
Consumption of households, EEK mn, nom.	45832.9	51036.5	57351.9	65135.3	69201.7	16060.5	.	.	.
annual change in % (real)	-2.7	8.5	5.9	9.9	5.4	5.8	.	5.3	5.2
Gross fixed capital form., EEK mn, nom.	20238.6	23769.4	28134.3	33554.7	35749.7	8131.4	.	.	.
annual change in % (real)	-15.6	14.3	13.0	17.2	5.4	22.3	.	6	5.5
LFS - employed persons, th, avg. ³⁾	579.3	572.5	577.7	585.5	594.3	576.8	589.3	595	596
annual change in % ³⁾	-4.5	-1.2	0.9	1.4	1.5	0.3	2.2	.	.
LFS - employed pers. in industry, th, avg. ³⁾	147.2	151.1	151.3	144.4	150.0	152.5	152.1	.	.
annual change in % ³⁾	-5.9	2.6	0.1	-4.6	3.9	2.3	-0.3	.	.
LFS - unemployed persons, average ³⁾	80.5	89.9	83.1	67.2	66.2	68.7	66.3	.	.
LFS - unemployment rate in %, average ³⁾	12.2	13.6	12.6	10.3	10.0	10.6	10.1	9.8	9.5
Reg. unemployment rate in %, end of period	5.2	5.9	6.1	5.4	4.9	5.8	5.2	4.5	4.3
Average gross monthly wages, EEK ⁴⁾	4440	4907	5510	6144	6723	6333	6748	.	.
annual change in % (real, gross)	6.9	6.3	6.1	7.6	8.0	8.1	6.1	.	.
Consumer prices, % p.a.	3.3	4.0	5.8	3.6	1.3	2.4	0.4	2.9	3.1
Producer prices in industry, % p.a.	-1.2	4.9	4.4	0.4	0.2	0.8	0.8	1	1.5
General governm. budget, EU-def., % GDP ⁴⁾									
Revenues	.	50.3	46.1	39.6	41.2	.	.	.	.
Expenditures	.	50.6	45.8	37.9	38.6	.	.	.	.
Deficit (-) / surplus (+)	-2.8	-0.3	0.3	1.8	2.6	.	.	0	-1
Public debt in % of GDP ⁴⁾	6.5	5.0	4.7	5.7	5.8	.	.	5.5	6
Money market rate, % p.a., end of period ⁵⁾	4.4	5.8	3.7	3.4	2.6	3.1	2.6	.	.
Current account, EUR mn	-231	-326	-376	-847	-1015	-281.6	-258.2	-920	-860
Current account in % of GDP	-4.4	-5.5	-5.6	-11.3	-12.6	-15.2	.	-10.5	-9.0
Total reserves minus gold, EUR mn	850	990	927	964	1089	996	1063	.	.
Gross external debt, EUR mn	2864	3233	3707	4490	5553	4893	.	6000	6500
FDI inflow, EUR mn	284	425	603	307	756	284	152	500	550
FDI outflow, EUR mn	79	67	226	140	137	18	43	150	170
Exports of goods, BOP, EUR mn	2364.4	3600.9	3749.4	3712.9	4052.7	913.5	1076.1	4480	4930
annual growth rate in %	.	52.3	4.1	-1.0	9.2	8.7	17.8	10.5	10
Imports of goods, BOP, EUR mn	3137.7	4441.1	4630.1	4877.9	5441.3	1260.3	1373.3	5900	6400
annual growth rate in %	.	41.5	4.3	5.4	11.6	15.6	9.0	8.5	8.5
Exports of services, BOP, EUR mn	1403.0	1628.7	1845.1	1807.5	1974.0	385.3	430.4	.	.
annual growth rate in %	.	16.1	13.3	-2.0	9.2	-12.5	11.7	.	.
Imports of services, BOP, EUR mn	869.9	1017.3	1195.4	1288.9	1219.1	247.7	271.7	.	.
annual growth rate in %	.	16.9	17.5	7.8	-5.4	-29.2	9.7	.	.
Average exchange rate EEK/USD	14.69	16.98	17.48	16.61	13.86	14.65	12.53	.	.
Average exchange rate EEK/EUR (ECU)	15.65	15.65	15.65	15.65	15.65	15.65	15.65	15.65	15.65
Purchasing power parity EEK/USD, wiiw	6.76	6.97	7.35	7.67	7.85	.	.	.	.
Purchasing power parity EEK/EUR, wiiw	7.38	7.51	7.96	8.23	8.56	.	.	.	.

Notes: 1) Preliminary. - 2) Enterprises with 20 employees and more. - 3) Persons aged 15-74. - 4) According to ESA 95, excessive deficit procedure. - 5) TALIBOR 1 month interbank rate.

Source: wiiw Database incorporating national statistics; AMECO; wiiw forecasts.