

### Box 3 Financing of the current account deficit and other currency outflows since 1998

The accompanying table presents an overview of funding of the current account deficit and other currency outflows since 1998. Initial estimates for 2002 are also given, but should be taken with great reservations.

The table shows the basic balance which comprises currency outflow for the current account deficit, net direct investment and net portfolio investment in foreign securities. It then shows how the basic balance is financed respectively by the private sector and by the public sector and Central Bank. The difference is the net currency outflow. By way of comparison, the Central Bank's net sale of currency in the interbank market and changes in foreign assets of pension funds are also quoted.

Figures for 2001 and 2002 are based on the Central Bank's rough update of the National Economic Institute forecast for the current account deficit, incorporating new data which have become available since the forecast was made. It is also based on a survey of plans for foreign borrowing by the main financial institutions, the largest power company (Landsvirkjun) and municipal authorities. It is assumed that the outflow to

meet direct investment and investment in foreign securities more or less halted during the second half of the year and that broadly the same pattern will be followed in 2002.

The main finding that the table produces is as follows: A substantial public sector foreign financing requirement emerged in 2000. It was similar last year, but started to decrease as the year progressed and will be below zero this year if the assumptions made in the survey hold good. A sharp turnaround has taken place in the basic balance. In 2000 an exceptionally wide current account deficit was accompanied by a massive outflow on portfolio investments abroad, financed by a credit inflow which was equivalent to one-fifth of GDP yet was not sufficient to keep the exchange rate stable. Last year, when the current account deficit shrank and the outflow of venture capital dropped at the same time, the ratio of basic balance to GDP is estimated to have diminished to 8%, from 20% in 2000. If the estimates outlined above are realised, this year's basic balance will be equivalent to 5.7% of GDP.

## Financing of the current account deficit and other currency outflows 1998-2002

<i>B.kr.</i>	1998	1999	2000	<i>Oct.-Dec.</i> 2000	<i>Jan.-Sept.</i> 2001	<i>Oct.-Dec.</i> 2001	2001 <sup>1</sup>	2002 <sup>1</sup>
<i>Borrowing requirement</i>								
Current account balance (1) .....	-40.1	-42.7	-67.1	-23.0	-37.1	-6.5	-43.6	-33.0
Net direct investment (2).....	5.4	-2.9	-18.0	-7.6	-12.2	0.0	-12.2	-8.8
Net portfolio investment (3) <sup>2</sup> .....	-21.5	-28.1	-49.2	-0.5	-5.9	0.0	-5.9	-2.8
Net venture capital .....	-16.2	-31.1	-67.2	-8.1	-18.1	0.0	-18.1	-11.5
Basic balance (4)=(1)+(2)+(3) .....	-56.2	-73.8	-134.3	-31.1	-55.2	-6.5	-61.7	-44.5
<i>Borrowing</i>								
Credit institutions (5) .....	35.0	46.7	70.0	11.2	9.1	13.9	23.0	40.7
Other private borrowers (6) <sup>3</sup> .....	24.8	39.2	40.3	15.2	20.7	-2.7	18.0	12.8
Private sector, total (7)=(5)+(6) .....	59.8	85.9	110.3	26.4	29.8	11.2	41.0	53.5
<i>Public sector foreign financing requirement (8)=- (4)-(7)</i>								
Public sector borrowing (9).....	-3.6	-12.1	24.0	4.7	25.4	-4.7	20.7	-9.0
Central Bank (10).....	-3.5	5.6	16.0	3.8	12.5	27.0	39.5	...
Central Bank (10).....	1.6	-5.4	15.9	0.7	7.4	-11.1	-3.7	...
<i>Net currency outflow (11) = (8)-(9)-(10).....</i>	-1.6	-12.3	-7.8	0.2	5.5	-20.6	-15.1	...
Central Bank's net sale of currency in the interbank market .....	-17.0	-12.0	13.9	4.9	15.6	13.9	29.5	...
Change in foreign assets of pension funds <sup>4</sup> ....	50.7	19.5	20.8	-7.9	-16.7	...	...	...
Gross domestic product .....	577.4	622.7	671.9	503.9	558.7	186.2	745.0	786.5
<i>Percent of GDP</i>								
Basic balance (4)=(1)+(2)+(3) .....	-9.7	-11.9	-20.0	-6.2	-9.9	-3.5	-8.3	-5.7
Public sector borrowing requirement (8)=(4)-(7) .....	-0.6	-1.9	3.6	0.9	4.5	-2.5	2.8	-1.1
Net currency outflow (11)=(8)-(9)-(10).....	-0.3	-2.0	-1.2	0.0	1.0	-11.1	-2.0	...
Central Bank's net sale of currency in the interbank market .....	-2.9	-1.9	2.1	1.0	2.8	7.5	4.0	...
Change in foreign assets of pension funds .	8.8	3.1	3.1	-1.6	-3.0	...	...	...

1. Estimate/forecast. Update of NEI forecast incorporating most recent data on merchandise trade balance. 2. Net purchases of foreign securities. 3. In 2002, estimated borrowing by municipal authorities is included with the private sector. Thus the public sector foreign financing requirement then refers only to the central government. 4. At average exchange rates at each time.