II. ESTONIAN BALANCE OF PAYMENTS FOR 2002

Even though the growth of the world economy accelerated in 2002 year-on-year, the economic growth in the EU and the euro area was slower than expected, reaching 1.6% and 1.0%, respectively. Although the weighted average economic growth of Estonia's major trade partners remained almost unchanged against 2001, being still a lot quicker than that of the European Union, the external demand of 2002 might be considered weak.

The economic growth of Estonia reached 6% in 2002, being almost 5 percentage points higher than the EU average. In contrast to previous years the relatively rapid growth was due to strong domestic demand and higher loan activity of the private sector. Investments increased by 17.5% in constant prices year-on-year and amounted to about 30% of the GDP. Increased investment demand was mostly caused by long-term projects, the implementation volume and speed of which do not depend on the present state of the economy. The single capital investments to technical infrastructure and export sector were evaluated to amount to 3,5–4,0% of the annual GDP. In principle, these investment plans rely on the assumption of increasing export in distant future.

The year 2002 was also exceptional, because in the conditions of increased investment demand, supply-side restrictions made the companies to import more transport and construction services, which caused the role of the services sector as the balancing mechanism for the trade balance deficit to become less important than before.

Investments were covered by external resources to a greater extent than in previous years, therefore the current account deficit, expressed as a ratio of the GDP, increased from 6.1% in 2001 to 12.3% in 2002 (see Table 2.1). In addition to the growth of investment activity, the decline in the level of savings also caused the need to use external resources and the increase of the current account deficit. The savings of households decreased most considerably, resulting in the deterioration of private persons' net position against the financial sector. Because of low loan interests, the private consumption increased by 8.2% year-on-year and the loans and leasing of private persons were up by 46.5%.

To some extent, government and business sector could offset the decline in private saving. Budget surplus was achieved two years running (the surplus in 2001 was 0.4% and in 2002 1.2% of the GDP) thanks to an expanded tax base and better tax administration and collection, all resulting from the growth in private consumption.

Weak external demand was most pronounced in the deterioration of Estonia's terms of trade (export price index fell 0.6%) and the recession in subcontracting industry. Subcontracting export volume in current prices was 22% smaller year-on-year. At the same time, increase in the volume of normal export continued at the same speed as in 2001, reaching 11%. There was substantial growth especially in the export of timber and timber products.

In 2002, a change in the structure of the domestic financing cover took place. Although the ratio of direct investment inflow to Estonia almost maintained the level of previous years, it did not cover the needs for financing increased investments. The current account deficit was more and more financed from accumulated reserves and foreign loans. Like in 2001, Estonia's external debt, expressed as a ratio of the GDP, increased (2.1 and 5.9 percentage points, respectively) and reached 65% of the GDP by the end of 2002. During 2002, the net external debt increased to 12% of the GDP. The budget surplus of the government sector and the means deposited abroad balanced the deterioration of the net position of the private sector to some extent.

Large capital inflow did not deteriorate the intrinsic balance of the economy. In 2002, the growth of consumer prices remained substantially lower than expected, reaching just 3.6%. The increase of prices in the sheltered sector reached 7%, but consumer prices were most influenced by food price decline in Europe. Therefore, food price increase amounted to just 2.7% in Estonia in 2002 (6.6% in 2001), lowering the inflation due to their large share in the consumer basket. Balanced development continued in the labour market as well, where wages increased in the same pace with productivity and labour costs per unit of production decreased.

Since investment demand probably remains high in the near future as well, the external balance may change quickly only due to increased savings of private persons and the acceleration of export growth.

Table 2.1. Internationally comparable general indicators of the balance of payments

	1995	1996	1997	1998	1999	2000	2001	2002
Foreign trade turnover (% of GDP)	113.6	106.7	123.9	124.2	112.8	144.0	133.9	124.4
Export and import ratio (%)	71.8	64.1	67.1	70.7	75.4	81.4	80.8	76.2
Nominal effective exchange rate of the kroon (% against the previous year)	125.3	100.0	97.2	108.8	117.1	97.3	101.3	102.1
Real effective exchange rate of the kroon (Q4 1992 = 100)	128.6	141.0	145.7	160.8	172.6	166.0	169.3	174.4
Terms of trade	107.4	107.7	108.8	108.8	107.9	112.6	118.4	112.2
Overall balance of the balance of payments (change of external reserves, EEK m)	1,200.4	1,228.4	2,771.3	126.4	1,797.6	2,270.5	-730.2	926.8
Ratio of the external reserves change to GDP (%)	2.9	2.3	4.3	0.2	2.4	2.6	-0.7	0.9
Current account balance (EEK m)	-1,810.6	-4,806.9	-7,810.2	-6,760.2	-3,607.7	-5,093.4	-5,889.5	-13,236.0
Current account balance deficit without government transfers (EEK m)	-2,964.4	-5,812.2	-9,143.0	-8,314.5	-5,022.8	-6,609.3	-8,072.8	-15,281.0
Current account deficit without government transfers (% of GDP)	7.4	11.1	14.3	11.3	6.6	7.6	8.2	14.1
Government transfers (net, EEK m)	1,153.8	1,005.3	1,332.8	1,554.3	1,415.1	1,515.9	2,183.3	2,045.0
Government transfers (% of GNP)	2.8	1.9	2.1	2.1	1.9	1.8	2.3	2.0
Estonia's total external debt (% of GDP)		35.8	57.4	53.3	58.7	57.9	59.3	65.0
External debt servicing (% from total exports)	1.2	3.3	1.6	1.2	1.1	1.3	1.0	1.6

CURRENT ACCOUNT

Due to the weak export demand and strong import demand, the current account deficit of Estonia's 2002 balance of payments more than doubled year-on-year, both in absolute terms as well as in relation to the GDP, amounting to 13.2 billion kroons and 12.3%, respectively (see Figure 2.1).

The sudden increase of the deficit resulted from the growth of the foreign trade deficit and the decrease of the surplus of the services balance (see Figure 2.2). The current account deficit was fully covered by the surplus of the capital and financial account. The rapid growth of the outflow of income of the previous years slowed down in 2002 and the earnings coming to Estonia from direct investments abroad increased.

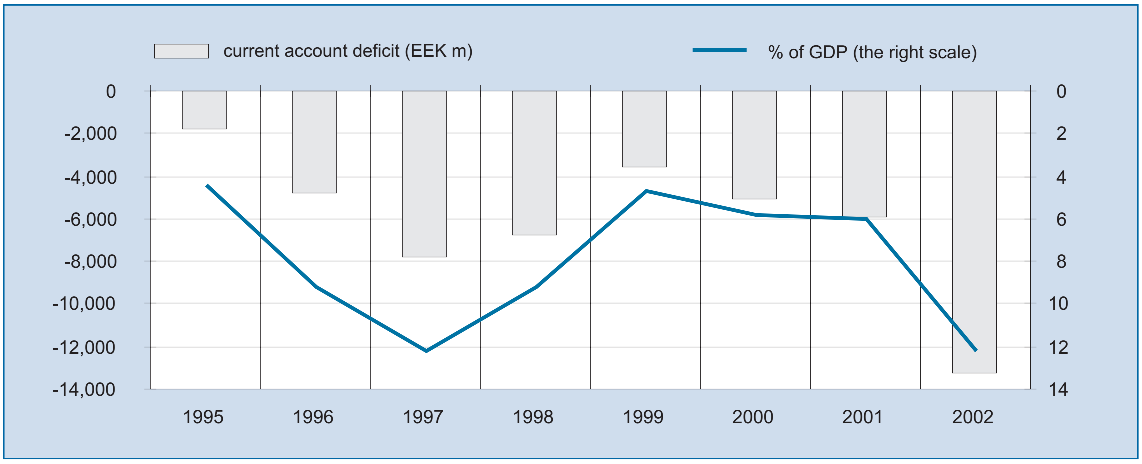

Figure 2.1. Balance of current account

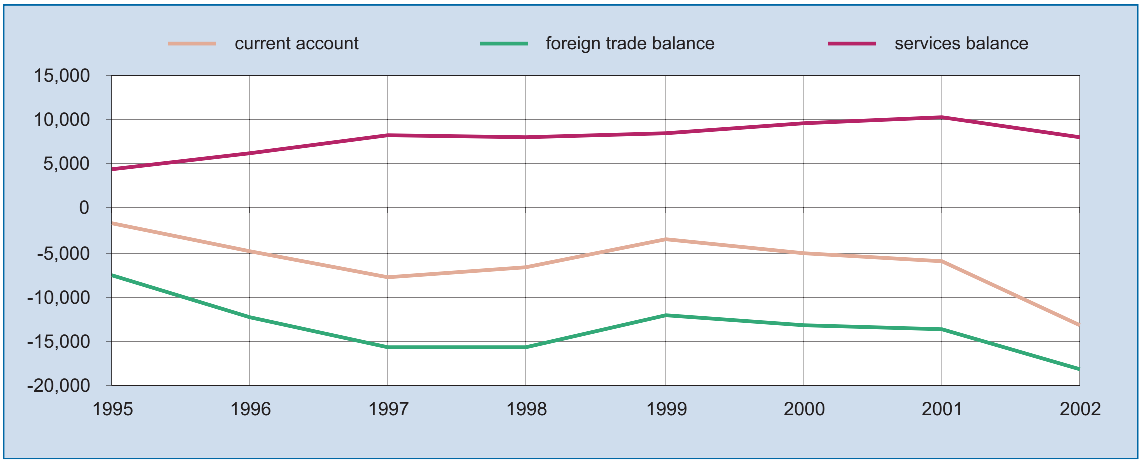

Figure 2.2. Comparison of the current account, foreign trade balance and services balance (in f.o.b prices, EEK m)

Goods

Under continuing global recession, Estonian export was unable to overcome the slump in 2002. Although the export of goods increased by 14% in the fourth quarter of 2002 as compared to the third quarter, the annual export slightly decreased year-on-year and amounted to 58 billion kroons (see Table 2.2). The import of goods continued to grow in the conditions of high domestic demand: import for free circulation grew by 9.7% in the fourth quarter and by 5.3% year-on-year, amounting to 76 billion kroons. Foreign trade deficit increased by 4.4 billion kroons year-on-year and reached the record level of 18.2 billion kroons.

Export under the **special trade statistics**[5] was 56.9 billion kroons, import in c.i.f. prices was 79.5 billion kroons and trade deficit 22.6 billion kroons (see Figure 2.3).

Decrease of the **goods export** by 1.7% was caused by the nearly 20% decline in the export of processed goods, which cut their share in special export by 7 percentage points, to 18 billion kroons (see Table 2.3).

[5] The analysis below does not contain the adjustment made in the foreign trade balance of the balance of payments by the Balance of Payments and Economic Statistics Department of Eesti Pank (repair of capital goods, provisions bought abroad, etc). Import is in c.i.f. prices and analysed by the trading country.
Eesti Pank uses the special trade system in its foreign trade analyses, which means that export does not contain the re-export of imported goods previously stored in customs warehouses or goods for provisioning sea vessels and aircraft. Import does not contain customs warehousing of imported goods, but reflects deliveries of goods from customs warehouses into free circulation and processing.

Table 2.2. Changes in the special export and import of goods

	Special exports			Special imports			Balance (EEK m)
	Volume[1] (EEK m)	Change compared to the previous year (%)	Share in total export of goods and services (%)	Volume[1] (EEK m)	Change compared to the previous year (%)	Share in total import of goods and services (%)	
1995	19,428.2	22.7	66.0	27,043.7	32.3	82.6	-7,615.5
1996	21,833.4	12.4	62.1	34,121.6	26.2	82.8	-12,288.2
1997	31,846.5	45.9	63.4	47,499.3	39.2	82.4	-15,652.8
1998	37,786.3	18.7	64.5	53,511.8	12.7	80.8	-15,725.5
1999	36,995.2	-2.1	62.8	49,092.1	-8.3	78.3	-12,096.9
2000	56,345.9	52.3	68.9	69,489.5	41.5	81.4	-13,143.6
2001	58,667.1	4.1	67.0	72,451.0	4.3	79.5	-13,783.9
2002	58,099.5	-1.0	63.9	76,323.7	5.3	75.5	-18,224.2

[1] Data of the balance of payments' foreign trade sub-balance.

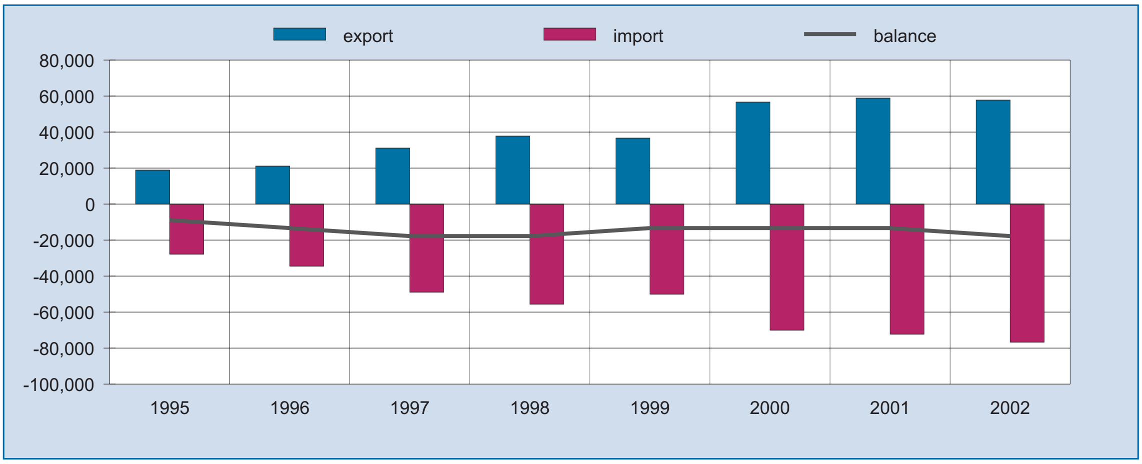

Figure 2.3. Foreign trade balance (EEK m)

Although the fourth quarter of 2002 indicated improvement of the subcontracting industry, the export of processed goods remained weak in the first three quarters of the year. The export of Estonian-assembled mobile communication equipment (capital goods) fell particularly sharply (almost by half), remaining, nevertheless, the biggest article in this group of goods. The export of capital goods also included transformers and electrical and alarm equipment. The bulk of goods of intermediate consumption was made up of mobile communication equipment parts and cables. Consumer goods processed in Estonia came from the category of textile industry products.

Table 2.3. Special export by end consumption

	Volume (EEK m)		Share (%)		Change (%)
	2001	2002	2001	2002	2002/2001
Normal export:	**35,606.6**	**38,966.1**	**61.5**	**68.5**	**9.4**
Capital goods	1,925.9	2,116.2	3.3	3.7	9.9
Goods of intermediate consumption	21,920.1	23,830.2	37.9	41.9	8.7
Consumer goods	11,124.1	12,032.6	19.2	21.2	8.2
Other	636.5	987.1	1.1	1.7	55.1
Export of proccessed goods:	**22,249.9**	**17,897.0**	**38.5**	**31.5**	**-19.6**
Capital goods	8,843.5	4,658.2	15.3	8.2	-47.3
Goods of intermediate consumption	9,674.9	9,196.1	16.7	16.2	-4.9
Consumer goods	3,730.3	3,873.8	6.4	6.8	3.8
Other	1.2	168.9	0.0	0.3	13,746.9
Total	**57,856.5**	**56,863.1**	**100.0**	**100.0**	**-1.7**

Normal export[6] increased by more than 9% year-on-year and amounted to 39 billion kroons. Biggest export articles belonged to the group of goods of intermediate consumption: unprocessed and little processed timber, wooden construction components and prefabricated buildings, car accessories (seatbelts) and metal structures. The export of consumer goods included furniture and furniture accessories, fish and dairy products, pharmaceuticals and garments. The export of capital goods covered trailers, tractors, lab equipment and various mechanisms.

Import of goods increased by nearly 6% in 2002 (see Table 2.4), although the import of processed goods fell by 16%. Deliveries of mobile communication equipment parts, which belong to the group of intermediate consumption goods, fell by more than four times year-on-year and led to the decrease of mobile phones export as well. However, the import of various parts of electrical appliances increased considerably, accounting for 35% of intermediate consumption goods. Among capital goods, mostly goods under the category of machinery and equipment were imported: alarm equipment and other electrical appliances, mobile phones, condensers, microphones. The bulk of imported consumer goods was made up of clothing and chemical products.

Table 2.4. Special import by end consumption

	Volume (EEK m)		Share (%)		Change (%)
	2001	2002	2001	2002	2002/2001
Import for free circulation (normal import):	**56,279.2**	**63,580.7**	**75.0**	**80.0**	**13.0**
Capital goods	9,801.9	11,136.1	13.1	14.0	13.6
Goods of intermediate consumption	25,278.0	29,535.8	33.7	37.2	16.8
Consumer goods	14,760.9	15,672.4	19.7	19.7	6.2
Other	6,438.3	7,236.4	8.6	9.1	12.4
Import of processed goods:	**18,797.1**	**15,886.3**	**25.0**	**20.0**	**-15.5**
Capital goods	3,046.9	3,571.0	4.1	4.5	17.2
Goods of intermediate consumption	14,592.5	11,176.5	19.4	14.1	-23.4
Consumer goods	1,154.5	1,082.5	1.5	1.4	-6.2
Other	3.2	56.3	0.0	0.1	1,641.7
Total	**75,076.3**	**79,467.0**	**100.0**	**100.0**	**5.8**

The year-on-year increase of import was caused by the 13% increase in **normal import** (import for free circulation), which grew across all groups of end consumption. Import of goods of intermediate consumption increased the most and constituted the biggest share: parts of motor vehicles and various machinery, natural gas, metal products and iron structures, plastic products, cables, raw wood and wooden sleepers, cotton, etc. Imported capital goods included mostly transport vehicles (commercial vehicles, tractors, railway engines, carriages, trailers) and machinery and equipment (computers, roadworks' machinery, machine-tools, mobile phones). Main articles among consumer goods were pharmaceuticals, furniture, food products, textile products and chemical products. Under the so-called other goods passenger cars were imported (up 25% year-on-year), as well as fuel.

The **foreign trade deficit** increased by 31% year-on-year and reached 22.6 billion kroons (see Table 2.5). The surplus of processed goods fell by 1.5 billion kroons, while the negative balance of normal export and import increased by 4 billion kroons, mostly due to the growing import of capital goods and goods of intermediate consumption.

Across the groups of countries, export of goods to the European Union decreased by 4%, but increased to the Central and Eastern European countries and the CIS countries (see Table 2.6). Nevertheless, export to the EU countries accounted for 68% of the total export and even 82% if we include accession countries.

[6] Normal export – export of goods manufactured in Estonia and belonging to Estonian legal entities; does not include the export of goods brought to Estonia for processing. Normal import – import of goods into Estonia for internal consumption; does not include import of goods for processing.

Table 2.5. Foreign trade balance by end consumption

	2001	2002
Balance of normal export and normal import:	**-20,672.7**	**-24,614.6**
Capital goods	-7,876.0	-9,019.9
Goods of intermediate consumption	-3,358.0	-5,705.6
Consumer goods	-3,636.8	-3,639.8
Other	-5,801.8	-6,249.3
Balance of export and import of processed goods:	**3,452.9**	**2,010.8**
Capital goods	5,796.6	1,087.3
Goods of intermediate consumption	-4,917.6	-1,980.3
Consumer goods	2,575.8	2,791.3
Other	-2.0	112.5
Total	**-17,219.8**	**-22,603.9**

Table 2.6. Special export by groups of countries

	Volume (EEK m)		Share (%)		Change (%)
	2001	2002	2001	2002	2002/2001
EU countries	40,181.6	38,625.3	69.5	67.9	-3.9
Central and Eastern European countries	6,842.9	7,732.8	11.8	13.6	13.0
CIS countries	2,586.2	2,882.0	4.5	5.1	11.4
Other	5,955.1	6,344.7	10.3	11.2	6.5
Customs-free zone	2,290.6	1,278.3	4.0	2.2	-44.2
Total	**57,856.5**	**56,863.1**	**100.0**	**100.0**	**-1.7**

Finland, Sweden and Germany were still Estonia's top three export partners, accounting for 74% of the export to the EU and half of the total export. Export to Finland decreased by 28% year-on-year (mostly due to the drop in processing of mobile communication equipment), but export to Sweden was up by 7% and to Germany even by 40%. Latvia and Lithuania dominated among the Central and Eastern European countries, with export to these two neighbouring countries growing by 6% and 15%, respectively. Among the CIS countries, the leading position belonged to Russia (up 21%) and the Ukraine (down 6%). Major partners among other countries included Norway and the USA with a 20% growth in exports. 1.3 billion kroons worth of goods was placed into free trade zones to wait for export.

Import of goods across all groups of countries increased in 2002, with the exception of import from the CIS countries, which remained unchanged against 2001 (see Table 2.7). The top three partners in the EU were again Finland, Germany and Sweden, and the growth trend was similar to that of export: import from Finland decreased by 18%, import from Germany and Sweden increased by 14% and 11%, respectively. Among the Central and Eastern European countries, import from Latvia increased by 7% and from Lithuania by 33%. Estonia's trade balance with Latvia had a surplus of nearly 1 billion kroons, while trade with Lithuania showed a deficit of almost the same size. Leaders among the CIS countries were Russia, the Ukraine and Belarus. Major import partners among other countries included Japan, Hong Kong, China and the USA.

The **foreign trade balance** was negative for all groups of countries (see Table 2.8).

Table 2.7. Special import by groups of countries

	Volume (EEK m)		Share (%)		Change (%)
	2001	2002	2001	2002	2002/2001
EU countries	52,471.3	53,331.6	69.9	67.1	1.6
Central and Eastern European countries	8,879.2	9,956.4	11.8	12.5	12.1
CIS countries	7,518.9	7,517.6	10.0	9.5	0.0
Other	6,206.9	8,661.4	8.3	10.9	39.5
Total	**75,076.3**	**79,467.0**	**100.0**	**100.0**	**5.8**

Table 2.8. Foreign trade balance by groups of countries

	2001	2002
EU countries	-12,289.7	-14,706.3
Central and Eastern European countries	-2,036.3	-2,223.6
CIS countries	-4,932.7	-4,635.6
Other	-251.8	-2,316.7
Customs-free zone	2,290.6	1,278.3
Total	**-17,219.8**	**-22,603.9**

Services

The surplus of the **services balance** amounted to 8.1 billion kroons in 2002, down 20% year-on-year (see Figure 2.4 and Table 2.9). While in previous years the surplus of the services balance compensated for 50–75% of the foreign trade deficit, then in 2002 the surplus of the services balance covered only 44% of the foreign trade deficit.

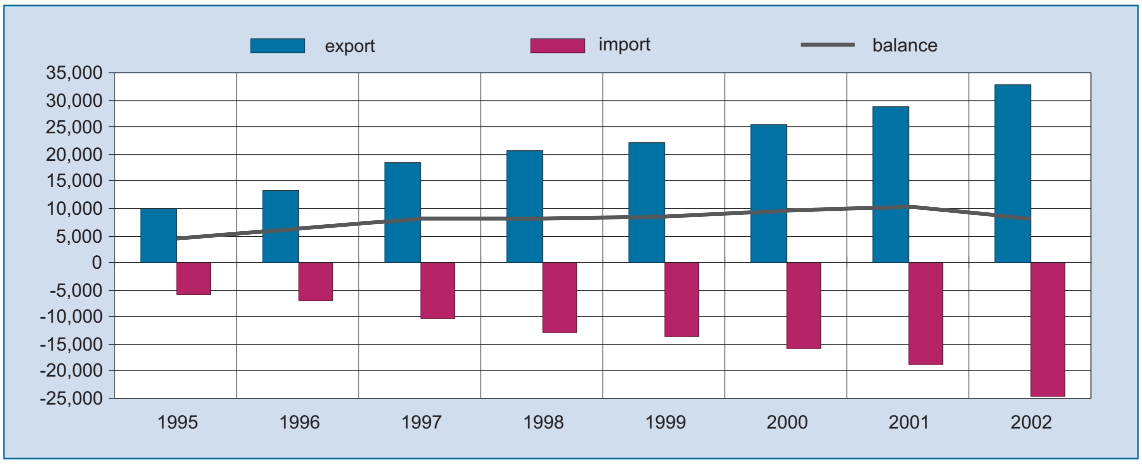

Figure 2.4. Services balance (EEK m)

Table 2.9. Services export and import

	Export		Import		Balance	
	Volume (EEK m)	Change compared to the previous year (%)	Volume (EEK m)	Change compared to the previous year (%)	Volume (EEK m)	Change compared to the previous year (%)
1993	4,434.3	81.7	3,437.2	78.2	997.1	95.0
1994	6,657.0	50.1	5,301.3	54.2	1,355.7	36.0
1995	10,022.9	50.6	5,692.6	7.4	4,330.3	219.4
1996	13,352.8	33.2	7,107.8	24.9	6,245.0	44.2
1997	18,366.7	37.5	10,134.0	42.6	8,232.7	31.8
1998	20,804.0	13.3	12,754.8	25.9	8,049.2	-2.2
1999	21,951.9	5.5	13,610.4	6.7	8,341.5	3.6
2000	25,485.8	16.1	15,911.2	16.9	9,574.6	14.8
2001	28,866.5	13.3	18,706.3	17.6	10,160.2	6.1
2002	32,830.9	13.7	24,736.9	32.2	8,094.0	-20.3

The main change in the structure of the services balance in 2002 concerned the 0.9 billion kroons deficit of construction services, which replaced the 0.8 billion kroons surplus of 2001 (see Table 2.10). Balances of other major categories of services changed little, yet surpluses decreased and the share of deficits in the balance of payments increased.

Table 2.10. Balance of services by major categories

	Balance (EEK m)		Share (%)	
	2001	2002	2001	2002
Transport services	5,328.6	5,183.0	52.4	64.0
Travel services	5,544.7	5,340.7	54.6	66.0
Construction services	822.1	-917.8	8.1	-11.3
Business services	-128.3	-146.0	-1.3	-1.8
Government services	-1,469.9	-1,418.7	-14.5	-17.5
Other	63.0	52.8	0.6	0.7
Services: net	**10,160.2**	**8,094.0**	**100.0**	**100.0**

Similarly to 2001, **export of services** increased by 14% in 2002 (see Table 2.11). The only category that indicated above-average growth of export was transport, the most important of services, which increased by 29%. Export of construction**,** business and government services has decreased year-on-year.

Import of services increased by 32% in 2002, import of construction services increased four times and import of transport services was up 48% (see Table 2.12).

Table 2.11. Export of services by major categories

	Volume (EEK m)		Share (%)		Change (%)
	2001	2002	2001	2002	2002/2001
Transport services	13,877.1	17,841.5	48.1	54.3	28.6
o/w freight	6,828.0	10,778.1	23.7	32.8	57.9
passenger	2,700.3	2,979.5	9.4	9.1	10.3
other transport services	4,348.9	4,083.9	15.1	12.4	-6.1
Travel services	8,897.7	9,148.8	30.8	27.9	2.8
Construction services	1,369.1	1,289.4	4.7	3.9	-5.8
Business services	3,390.0	3,236.8	11.7	9.9	-4.5
Government services	155.3	126.8	0.5	0.4	-18.4
Other	1,177.2	1,187.6	4.1	3.6	0.9
Total	**28,866.5**	**32,830.9**	**100.0**	**100.0**	**13.7**

Table 2.12. Import of services by major categories

	Volume (EEK m)		Share (%)		Change (%)
	2001	2002	2001	2002	2002/2001
Transport services	8,548.5	12,658.5	45.7	51.2	48.1
o/w freight	6,365.9	10,103.4	34.0	40.8	58.7
passenger	1,073.7	1,223.1	5.7	4.9	13.9
other transport services	1,108.9	1,332.0	5.9	5.4	20.1
Travel services	3,353.0	3,808.1	17.9	15.4	13.6
Construction services	547.0	2,207.2	2.9	8.9	303.5
Business services	3,518.3	3,382.8	18.8	13.7	-3.9
Government services	1,625.2	1,545.5	8.7	6.2	-4.9
Other	1,114.3	1,134.8	6.0	4.6	1.8
Total	**18,706.3**	**24,736.9**	**100.0**	**100.0**	**32.2**

In 2002, export and import of **transport services** increased faster than the total export and import of services (see Figure 2.5), with the volume of cargo transport growing at a particularly rapid rate (export was up 58% and import 59%). The export of cargo transport by rail increased 5.8 times, import climbed 3.7 times. Road transport, however, has decreased.

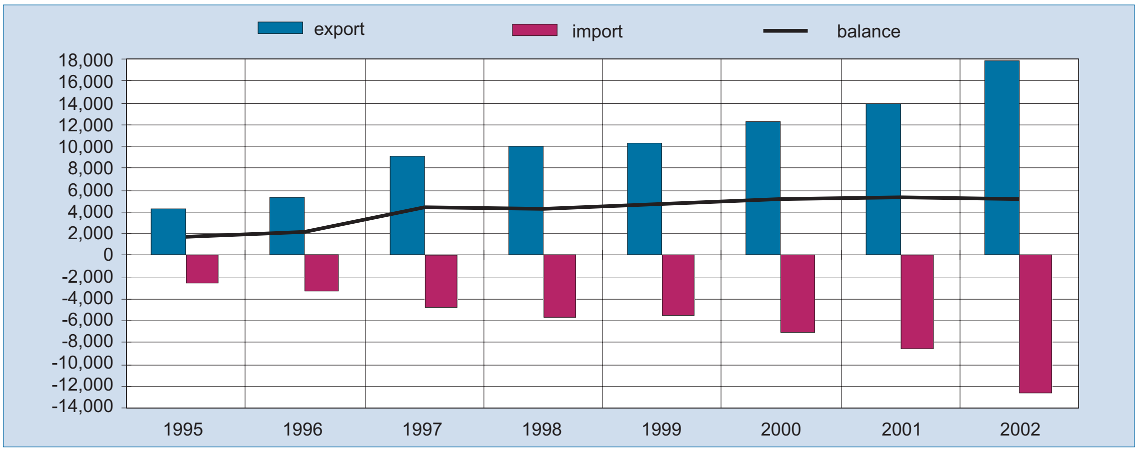

Figure 2.5. Transport services balance (EEK m)

The growth of **travel services** export was very small in 2002 (3%). The number of foreign tourists visiting Estonia decreased by 1%, whereas the length of visits increased by 9% (see Figure 2.6). The cross section of tourists has changed – fewer visitors came from Finland, the CIS countries and the USA while the number of visitors from Scandinavia and the EU increased. Given the numerous discounts related to the 2002 slump in the tourism industry and increasing purchasing power of Estonian residents, the import of travel services increased by 14%. Discount offers by airlines took more Estonians to far-away destinations that involved higher expenses. The number of visits to such far-away countries that have never been in the statistics of travel destinations on their own before, increased at a particularly rapid rate. The most popular destinations besides the neighbouring countries included Spain, Italy, Great Britain and the USA.

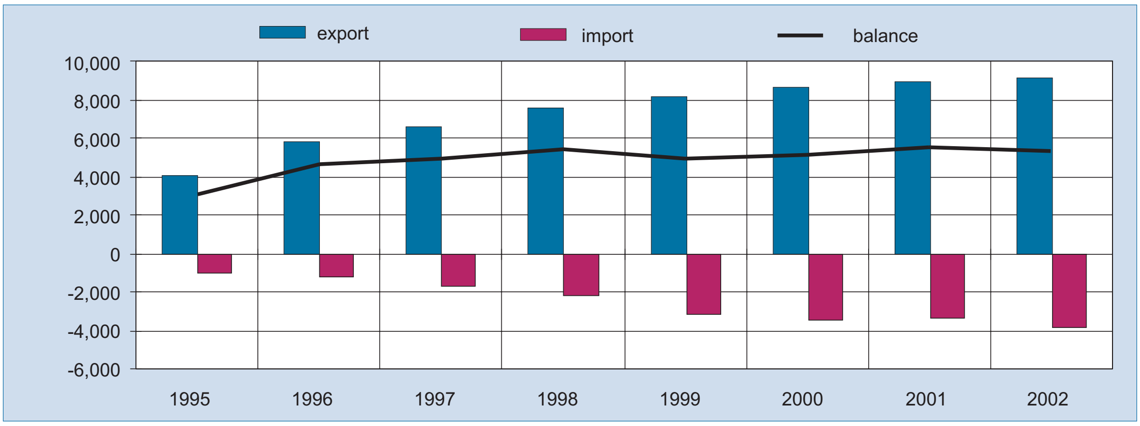

Figure 2.6. Travel services balance (EEK m)

Income

The **deficit of the income balance** was 5.5 billion kroons in 2002, up 11% year-on-year (see Table 2.13 and Figure 2.7). The bulk of the increase resulted from the net outflow of direct investment income, which grew by 15%. The growth of income outflow was slowed down by the decrease in the outflow of other investment income (loan and deposit interests, etc) and increase in the net inflow of employee compensation income.

Inflow of income to Estonia increased by 0.3 billion kroons in 2002 (10%). Inflow of income from direct investments made into foreign countries increased by 84%, making up 26% of the total inflow of income (see Table 2.14). Income from compensations paid to Estonians working abroad increased rapidly as well (75%).

Table 2.13. Income balance (EEK m)

	Volume (EEK m)		Share (%)		Change (%)
	2001	2002	2001	2002	2002/2001
Income from direct investments	-4,965.0	-5,714.3	100.8	104.2	15.1
o/w income from equity	-4,751.0	-5,478.3	96.4	99.9	15.3
income from debt (interests)	-214.0	-236.0	4.3	4.3	10.3
Income from portfolio investments	458.7	485.6	-9.3	-8.9	5.9
Income from other investments	-512.3	-418.5	10.4	7.6	-18.3
Other income	92.5	164.1	-1.9	-3.0	77.4
Income: net	**-4,926.1**	**-5,483.1**	**100.0**	**100.0**	**11.3**

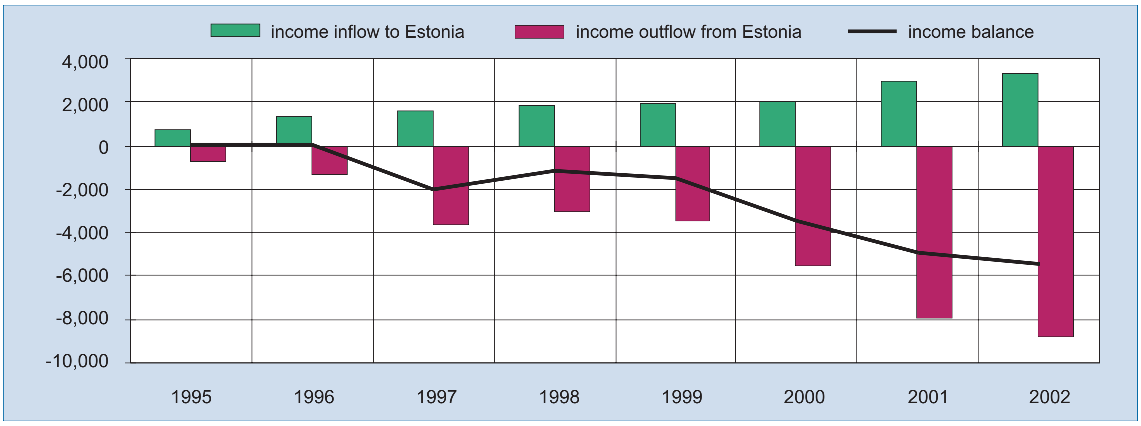

Figure 2.7. Income balance (EEK m)

Table 2.14. Income inflow to Estonia

	Volume (EEK m)		Share (%)		Change (%)
	2001	2002	2001	2002	2002/2001
Income from direct investments	456.4	840.8	15.2	25.6	84.2
o/w income from equity	349.1	732.7	11.7	22.3	109.9
income from debt (interests)	107.3	108.1	3.6	3.3	0.7
Income from portfolio investments	1,621.4	1,435.3	54.1	43.8	-11.5
Income from other investments	808.2	812.4	27.0	24.8	0.5
Other income	108.7	190.8	3.6	5.8	75.5
Total	**2,994.7**	**3,279.3**	**100.0**	**100.0**	**9.5**

Outflow of income from Estonia increased by 11% and amounted to 8.8 billion kroons (see Table 2.15). The only category that saw the growth of outflow of income was direct investments made into Estonia (21%). In 2002, dividend and undistributed profit payments to non-residents increased 2.3 times year-on-year, supposedly resulting from the amendment of the Income Tax Act concerning taxation of dividends.

Table 2.15. Income outflow from Estonia

	Volume (EEK m)		Share (%)		Change (%)
	2001	2002	2001	2002	2002/2001
Income from direct investments	-5,421.4	-6,555.1	68.4	74.8	20.9
o/w income from equity	-5,100.1	-6,211.0	64.4	70.9	21.8
income from debt (interests)	-321.3	-344.1	4.1	3.9	7.1
Income from portfolio investments	-1,162.7	-949.7	14.7	10.8	-18.3
Income from other investments	-1,320.5	-1,230.9	16.7	14.0	-6.8
Other income	-16.2	-26.7	0.2	0.3	64.8
Total	**-7,920.8**	**-8,762.4**	**100.0**	**100.0**	**10.6**

Transfers

The surplus of the transfer balance stood at 2.4 billion kroons in 2002, decreasing by 0.3 billion kroons year-on-year. The bulk of transfers were government transfers to get ready for the EU accession. The surplus of the government transfers decreased due to the debit growth. The debit and credit of private transfers have increased considerably over the year (by 24% and 79%, respectively), but the surplus decreased only by 145 million kroons year-on-year.

CAPITAL AND FINANCIAL ACCOUNT

The surplus of the capital and financial account reached the record level with 13.6 billion kroons, standing at almost 2.8 times higher than in 2001. There were changes in the financing structure of the current account deficit in 2002. While in previous years it was mostly covered by direct investments, then in 2002 the share of direct investments decreased and the share of portfolio and other investments increased. A survey of the financial account is given in Figures 2.8 and 2.9.

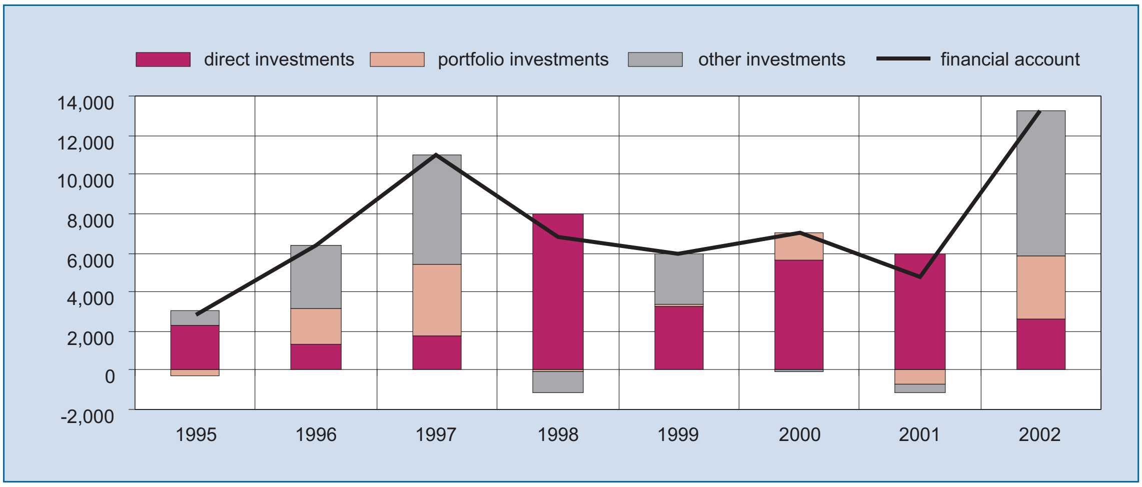

Figure 2.8. Changes in the structure of foreign investment capital flows (EEK m)

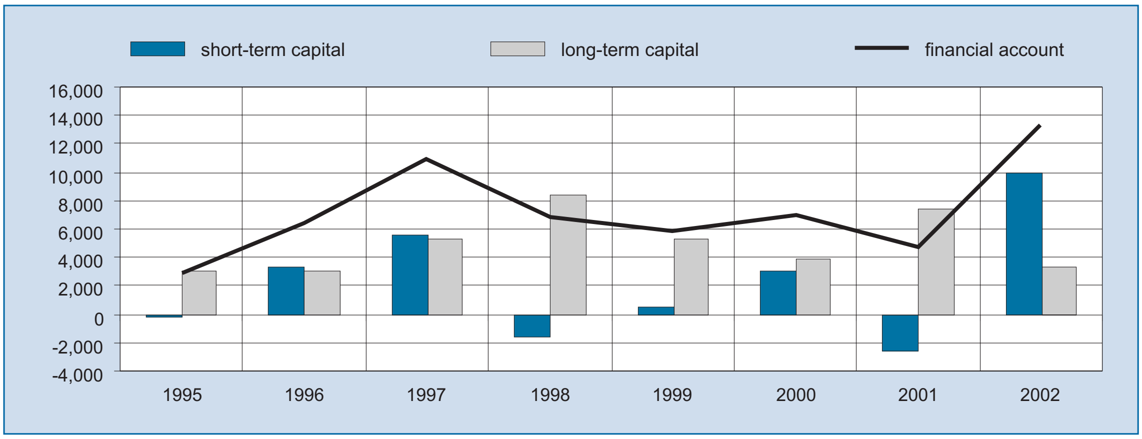

Figure 2.9. The maturity structure of financial sources (EEK m)

Direct Investments

The **balance of direct investments** had a surplus of 2.6 billion kroons in 2002, amounting to 44% of the net inflow of direct investments in 2001. Non-residents invested 4.8 billion kroons into Estonia and Estonian residents' direct investments in foreign countries increased by 2.2 billion kroons (see Table 2.16 and Figure 2.10). One fifth of the current account deficit was covered by the net inflow of direct investments.

The **inflow of direct investments into Estonia** fell by more than a half year-on-year. However, we have to keep in mind that the year 2001 was a record one as far as inflow of direct investments was concerned. In 2002, non-residents invested almost 90% of long-term financial investments into equity capital, of which 70% consisted of undistributed profits belonging to non-residents. At the same time, an extensive withdrawal of owner's earnings took place, testifying to Estonia's favourable investment climate. Dividend payments were affected also by the expected amendment of the Income Tax Act concerning taxation of dividends (took effect in 2003). Income was mostly reinvested to the manufacturing, while transport, storage and communication firms preferred dividend payments. Compared to equity capital investments, transfers of loan capital were small, because short-term loans were repaid and new long-term loan liabilities were taken in approximately the same amount (see Figure 2.11).

Table 2.16. Structure of direct investments

	Into Estonia				Abroad			
	Volume (EEK m)		Share (%)		Volume (EEK m)		Share (%)	
	2001	2002	2001	2002	2001	2002	2001	2002
Share capital	**3,641.2**	**821.0**	**38.6**	**17.1**	**-1,897.1**	**-903.9**	**53.8**	**41.3**
Inflow	4,955.5	3,361.2	52.6	70.0	288.5	126.1	-8.2	-5.8
Outflow	-1,314.3	-2,540.2	-13.9	-52.9	-2,185.6	-1,030.0	61.9	47.1
Reinvested earnings	**3,878.9**	**3,370.3**	**41.1**	**70.2**	**-305.2**	**-665.5**	**8.7**	**30.4**
Claims	-4,095.4	-5,009.0	-43.4	-53.1	-522.1	-837.6	-5.5	-8.9
Liabilities	7,974.3	8,379.3	84.6	88.9	216.9	172.1	2.3	1.8
Loan capital (net)	**1,892.3**	**171.5**	**20.1**	**3.6**	**-1,322.4**	**-583.7**	**37.5**	**26.7**
Trade credit	-474.1	-549.4	-5.0	-11.4	-164.7	-146.9	4.7	6.7
Short-term loans	1,215.9	-1,257.9	12.9	-26.2	-569.4	558.3	16.1	-25.5
Long-term loans	1,150.5	1,978.8	12.2	41.2	-588.3	-995.1	16.7	45.5
Other capital	**17.2**	**437.4**	**0.2**	**9.1**	**-3.6**	**-35.3**	**0.1**	**1.6**
Total	**9,429.6**	**4,800.2**	**100.0**	**100.0**	**-3,528.3**	**-2,188.4**	**100.0**	**100.0**

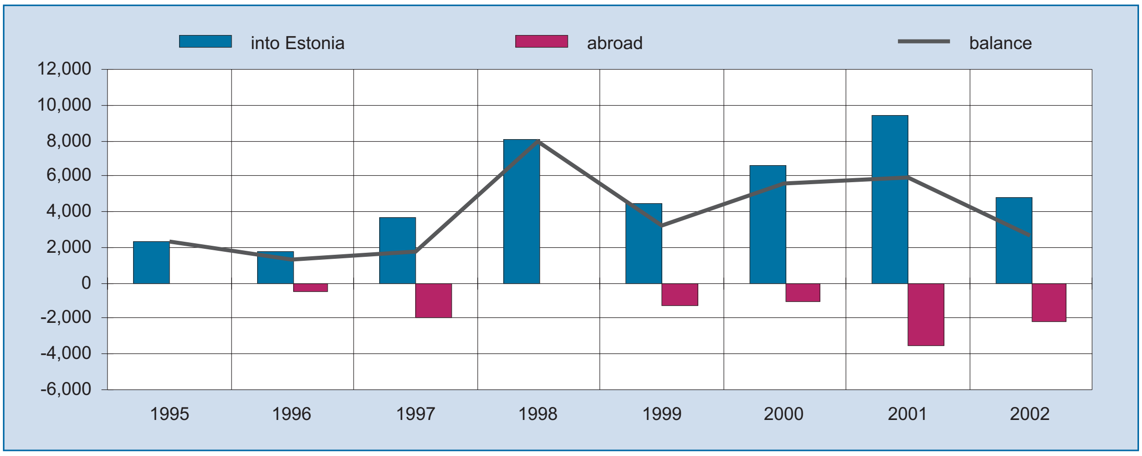

Figure 2.10. Direct investments (EEK m)

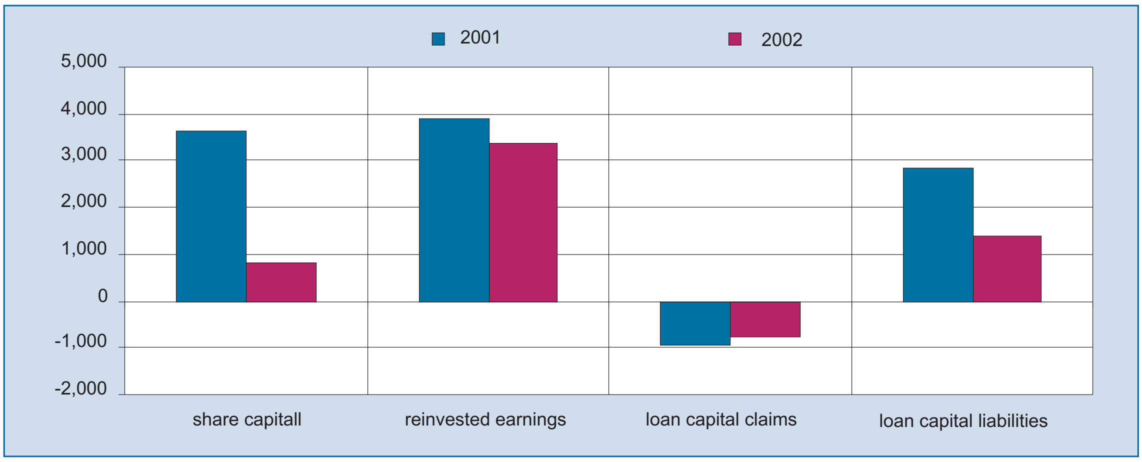

Figure 2.11. Structure of direct investments made into Estonia (EEK m)

82% of direct investment inflow came from Finland and Sweden; in case of Dutch investments a considerable flow-back occurred (see Figure 2.12). 85% of the net inflow of direct investments originated from the EU member countries and 44% from the Monetary Union. The share of investments from countries invited to join the EU in 2004 amounted to just 2%. Finance and wholesale and retail trade were the most preferred sectors, whereas direct investments into electric energy, gas and water supply companies decreased considerably (see Figure 2.13).

Direct investments abroad by Estonian businesses dropped by one third year-on-year. Three fourths of the outflow of direct investments increased the equity capital of companies abroad with Estonia's majority holding. The value of investments calculated under the equity method (reinvested earnings) increased by 30%. Similarly to direct investments made into Estonia, an extensive return of short-term loan capital took place in the fourth quarter (0.6 billion kroons) and the positions of long-term loan capital in foreign countries increased by almost 1 billion kroons (see Figure 2.14).

In 2002, the most preferred investment target was still Lithuania (44% of the total outflow). While previously the second place belonged to affiliated/associated companies in Latvia, then in the given period Cyprus occupied this place (see Figure 2.15). A change of places has also occurred in spheres of activity – investments

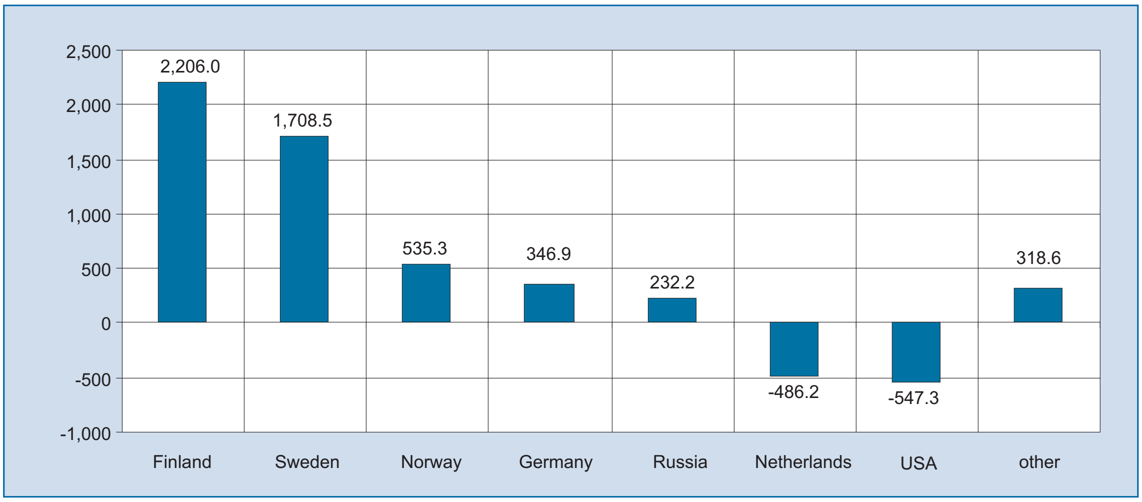

Figure 2.12. Structure of direct investments made into Estonia by countries in 2002 (EEK m)

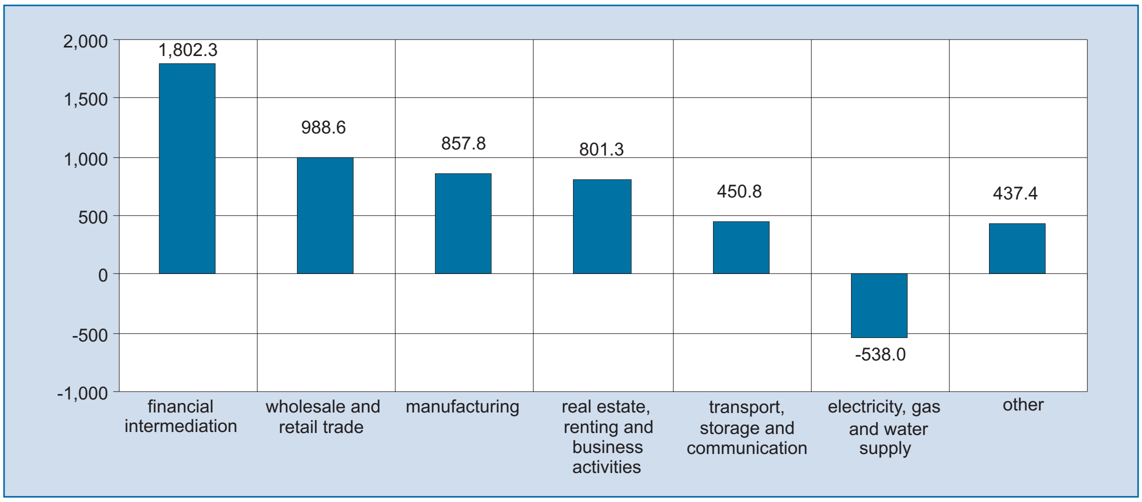

Figure 2.13. Structure of direct investments made into Estonia by spheres of activity in 2002 (EEK m)

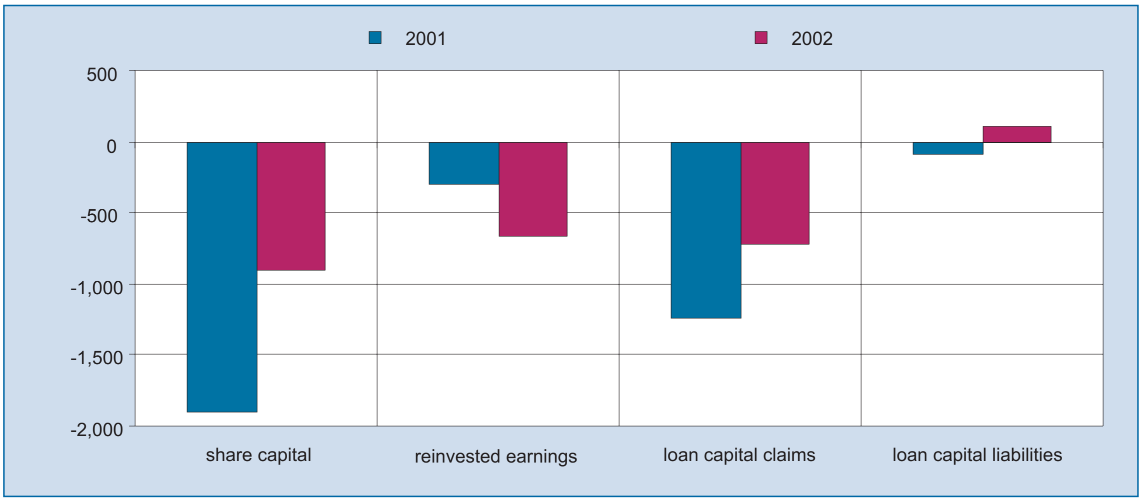

Figure 2.14. Structure of direct investments made abroad (EEK m)

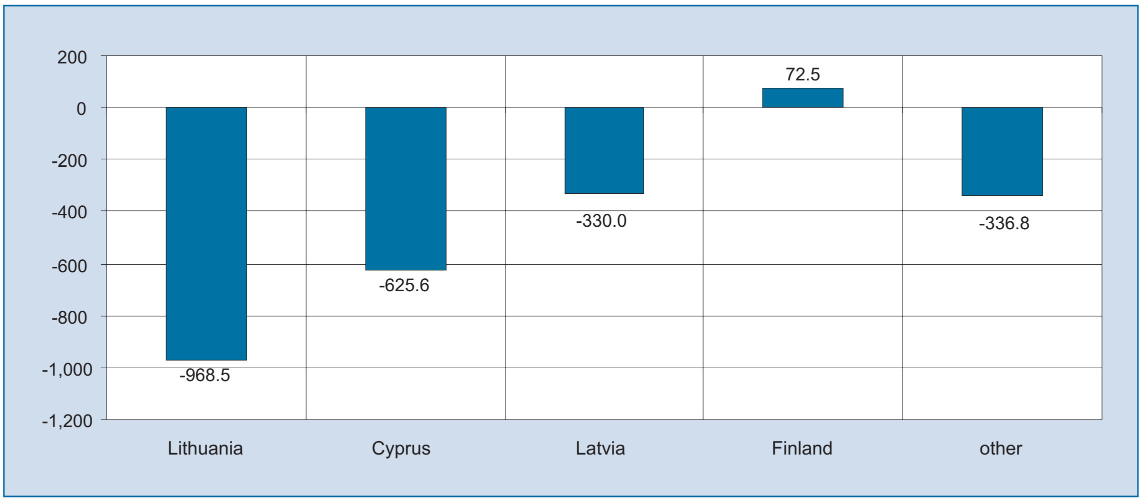

Figure 2.15. Structure of direct investments made abroad by countries in 2002 (EEK m)

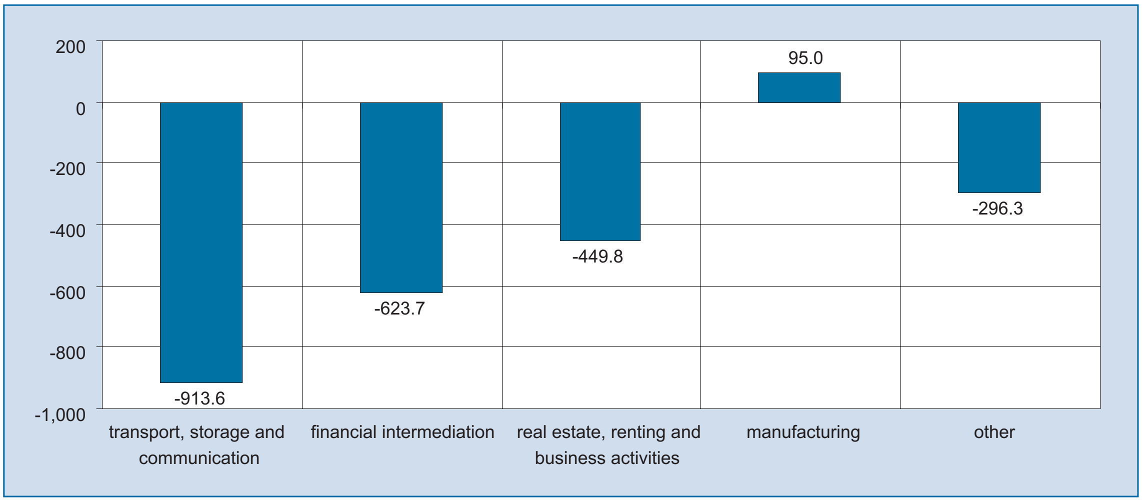

Figure 2.16. Structure of direct investments made abroad by spheres of activity in 2002 (EEK m)

into transport, storage and communication have risen to the top and the former leader financial intermediation has dropped to the second place (see Figure 2.16). The share of direct investments placed into EU member countries was 2%, whereas 88% of direct investments were made into countries joining the EU in 2004.

Portfolio Investments

The **net inflow of portfolio investments** amounted to 3.2 billion kroons in 2002, surpassing the figure of 2001 more than four times (see Figure 2.17 and Table 2.17). This form of investment inflow was an important source of finance for the Estonian economy in 2002 and can be compared in size to direct investments.

Portfolio investments abroad increased by 2.4 billion kroons last year, resulting mostly from free resources of government sector being invested into debt instruments issued by non-residents. No major changes took place in investments into equity securities.

Portfolio investments into Estonia increased by 5.6 billion kroons year-on-year, with approximately 1 billion kroons invested into equity securities and 4.6 billion kroons into debt securities. 0.1 billion kroons worth of investments into equity securities were made into credit institutions and 0.8 billion kroons worth into companies of the other sector. Successful bond issues of the government sector and the other sector attracted, respectively, 3.0 billion and 1.5 billion kroons of additional capital to Estonia.

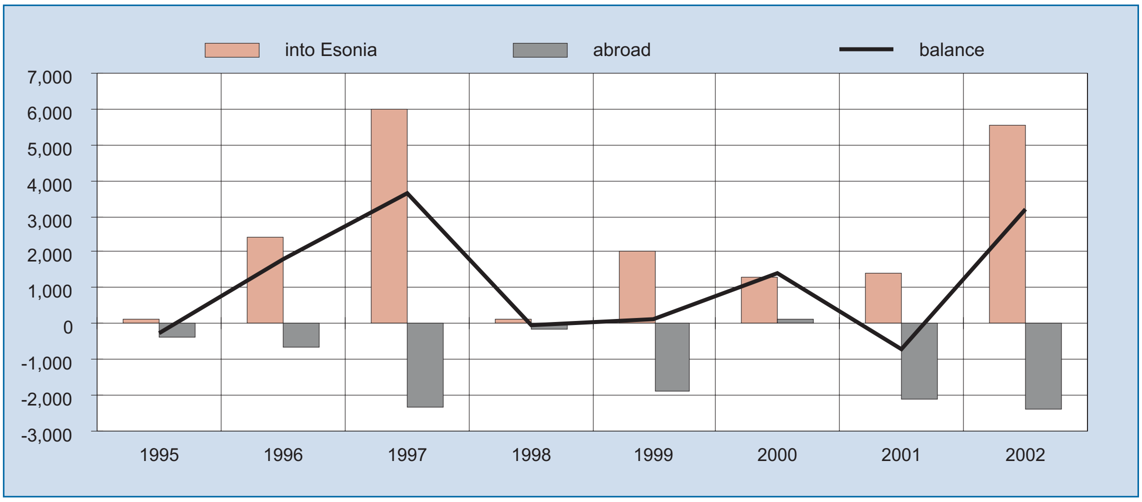

Figure 2.17. Portfolio investments (EEK m)

Table 2.17. Portfolio investments by types of securities and sectors of economy (EEK m)

	Claims		Liabilities		Balance	
	2001	2002	2001	2002	2001	2002
Total portfolio investments	**-2,100.2**	**-2,358.0**	**1,400.5**	**5,561.6**	**-699.7**	**3,203.6**
o/w equity securities	236.5	9.1	568.4	912.2	804.9	921.3
credit institutions	399.1	13.0	429.1	105.7	828.2	118.7
other sectors	-162.6	-3.9	139.3	806.5	-23.3	802.6
debt securities	-2,336.7	-2,367.1	832.1	4,649.4	-1,504.6	2,282.3
central bank	81.8				81.8	0.0
government sector	-2,479.1	-2,464.0	-115.6	1,448.6	-2,594.7	-1,015.4
credit institutions	437.0	-56.0	543.0	189.4	980.0	133.4
other sectors	-376.4	152.9	404.7	3,011.4	28.3	3,164.3

Other Investments

The **balance of other investments** showed a surplus of approximately 7.5 billion kroons in 2002 (see Figure 2.18 and Table 2.18), differing considerably from the year 2001 when a capital outflow of 0.4 billion kroons took place. The 2002 capital inflow of 7.5 billion kroons can be attributed to the remarkable increase of liabilities in the form of growing loan liabilities and larger deposits of non-residents in domestic credit institutions. The inflow of investments mostly took the form of short-term capital (see Table 2.19).

Other investments abroad increased by 0.7 billion kroons year-on-year. The biggest changes concerned loans granted by the other sector, which resulted in the outflow of capital worth 1.4 billion kroons, and the decrease of trade credit claims, which caused the inflow of capital worth 1 billion kroons. Other claims decreased by 0.2 billion kroons year-on-year.

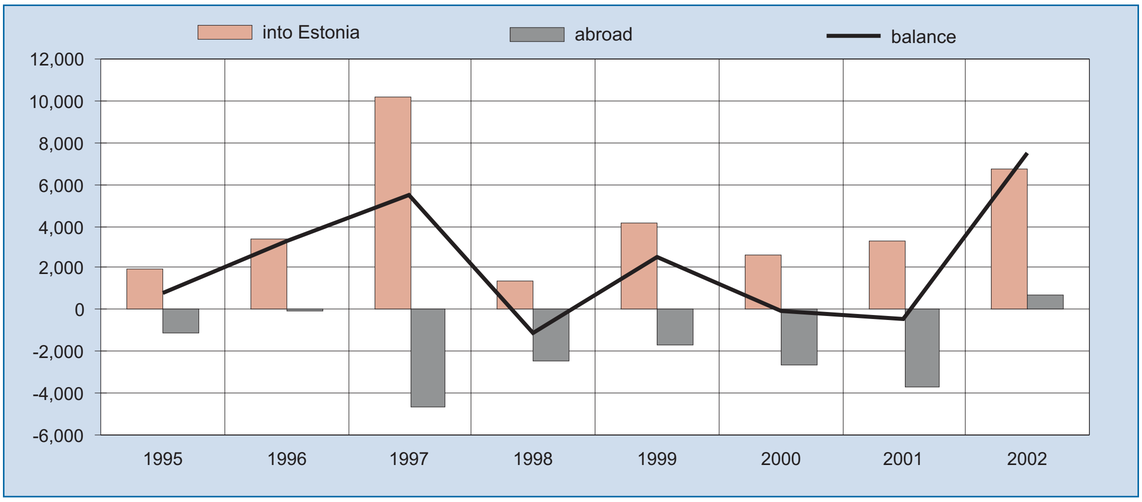

Figure 2.18. Other investments (EEK m)

Table 2.18. Other investments by type of capital (EEK m)

	Claims		Liabilities		Balance	
	2001	2002	2001	2002	2001	2002
Total	**-3,716.7**	**723.6**	**3,288.2**	**6,733.3**	**-428.5**	**7,456.9**
o/w trade credit	-584.8	1,089.5	102.9	781.1	-481.9	1,870.6
loans	-2,278.9	-1,324.5	2,570.4	1,963.3	291.5	638.8
deposits	-738.0	729.2	81.4	3,763.5	-656.6	4,492.7
other	-115.0	229.4	533.5	225.4	418.5	454.8

Table 2.19. Other investments by maturity (EEK m)

	Claims		Liabilities		Balance	
	2001	2002	2001	2002	2001	2002
Total	**-3,716.7**	**723.6**	**3,288.2**	**6,733.3**	**-428.5**	**7,456.9**
Long-term capital	**-322.7**	**-1,083.0**	**1,814.4**	**1,829.0**	**1,491.7**	**746.0**
central bank	3.0	4.8	-2.9		0.1	4.8
government sector			-128.2	-883.9	-128.2	-883.9
credit institutions	-130.0	-156.8	183.5	1,638.3	53.5	1,481.5
other sectors	-195.7	-931.0	1,762.0	1,074.6	1,566.3	143.6
Short-term capital	**-3,394.0**	**1,806.6**	**1,473.8**	**4,904.3**	**-1,920.2**	**6,710.9**
central bank	-202.7	-53.3	-89.2	646.1	-291.9	592.8
government sector	637.6	-324.6			637.6	-324.6
credit institutions	-3,574.7	-345.3	908.2	4,045.4	-2,666.5	3,700.1
other sectors	-254.2	2,529.8	654.8	212.8	400.6	2,742.6

Other investments into Estonia increased by 6.7 billion kroons in 2002. In order to meet higher domestic demand, credit institutions have increased their loan liabilities to non-residents by 2 billion kroons; loan liabilities of the other sector grew by 0.5 billion kroons. Deposits of non-residents in Estonian credit institutions have increased by 3.8 billion kroons, which has also contributed to the growth of liabilities. Only the government sector has reduced its loan liabilities – by 0.9 billion kroons.

RESERVES

Reserves of the balance of payments increased by 927 billion kroons in 2002. Coverage of imports with the reserves is illustrated in Figure 2.19.

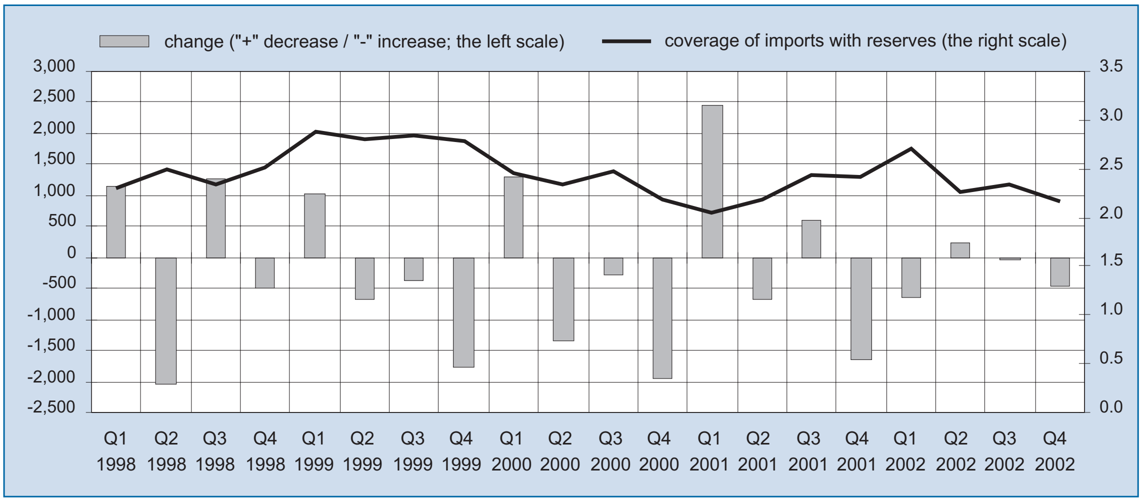

Figure 2.19. Change of Estonian gold and foreign currency reserves (EEK m) and the coverage of imports with reserves (by quarters)