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THE PROBLEM OF THE CURRENT ACCOUNT DEFICIT IN BULGARIA

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Abstract: The present paper illustrates the views of the author about the cause for the current account deficit in Bulgaria. The usual public explanation of the problem here is that the current account deficit is a result of the low competitiveness of the country's export. The author's analyses shows that the main factor for the deficit is the inflow of the foreign investment and the growth of the foreign debts of the private non banking sector in Bulgaria. This conclusion could be of very high importance for a revision of the fiscal policy in the country of the last years, because it gives valuable arguments against the practice of the budget surpluses.

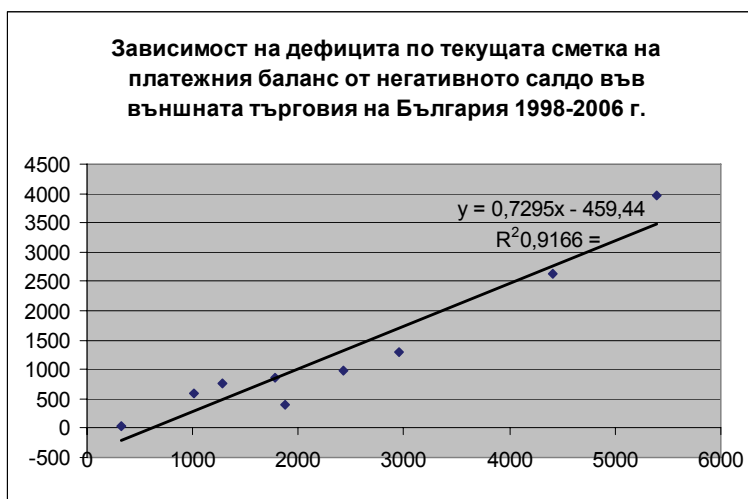
Key words: interdependence between passive in the current account and the inflow of FDI in Bulgaria

The usual explanation for the practice of budget surpluses of Bulgaria in the last years is that this could be the only instrument to set some limits or to stop the growth of the current account deficit. Which deficit, on its side, is a result of the passive

in the foreign trade of the country. Our studies based on the statistics of the Bulgarian National bank shows that the correlation between the current account deficit and the international trade deficit is 0.96.¹ See Graph N 1.

¹ www.bnb.bg – statistics, balance of payments

Graph N 1



This fact provides many domestic economists with the argumentation in favor of the low competitiveness of the Bulgarian

economy as a whole, because of the impact of the currency board and especially because of the fixed exchange rate of the

national currency, the Bulgarian leva, to the euro since 1997.

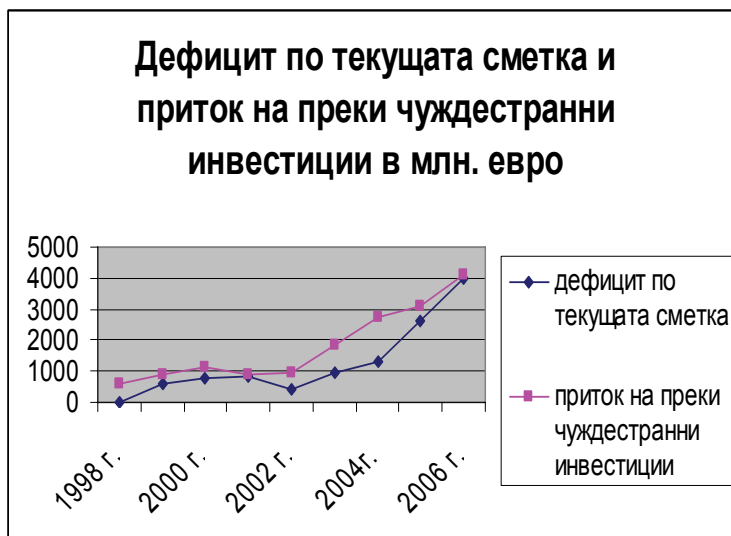
In the same time the comparative price level in Bulgaria in the end of 2007 is about 40-43% of the comparative price level in the Euro zone.² The Bulgarian joining of the European Union has practically doubled the inflationary rate and in 2007 it has reached 12%. For the year 2008 the most prognoses shows not less than 7-8% inflation. That means that any revision of the fixed exchange rate of the Bulgarian leva would cause only acceleration of the inflation and so would not obligatory contribute for the growth of the competitiveness of the economy and for the continuation of the 6-

7% economic growth. The consequences for the standard of living in the country so would be also negative.

The current account of the Bulgarian balance of payments is steady negative in the last ten years, but the balance of payments ends with steady positive results. So it occurs the question, if there is an other explanation of the deficit in the current account. Our calculations are proving that the growing of passive in the current account of Bulgaria could be a result of the growing of the inflow of the foreign investment. The both curves 1998-2006 are illustrated in the following graph.

² Calculated on the base of the statistics of the World bank, www.worldbank.org, research & data, key statistics, GDP and GDP PPP

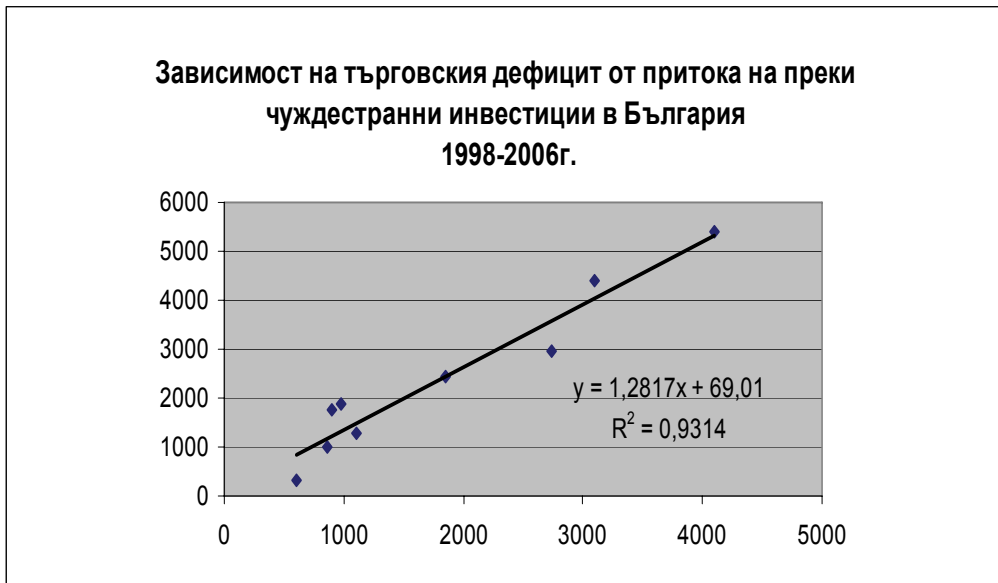
Graph N 2



Our further calculations show that the correlation between the foreign investment and the current account deficit 1998-2006 is

0,97. The interdependence between the both is illustrated on the **Graph N 3** below.

Graph N 3



The theoretical explanation of the result, calculated above, could lay also on macroeconomic level. One of the popular equation describing the macroeconomic equilibrium is as follows:³

$$I + G + E = S + T + M$$

Where :

I – is the investment in the economy

G – are the government purchases

E – is the export

S – are the savings

T – are the taxes

M – is the import

If we assume, that **G** and **E** on the left and **S** и **T** on the right are constant, we could see that the growth of the investment

activity– **I** (in our case - the growth of the FDI) is leading to the growth of the import - **M** (in the Bulgarian case - of the passive in the current account).

This conclusion is of very significant importance, because it illustrates what could be the real cause for the deficit in the current account in the Bulgarian balance of payments. On this sight of view the government policy of budget surpluses looks counter productive, because it means “savings” in the field of infrastructure. Which is really a bad choice, because the signals of overheating of the Bulgarian economy are coming most from the side of the old, undeveloped and ruined infrastructure in the country, infrastructure decapitalized in the years of transition with about 48%.⁴

³ Look. Hyman D., *Economics*, IRWIN, Boston 1989, P.674

⁴ Look Nikolov Ch., *The Economic Development of Bulgaria in the Beginning of its EU- membership*, Edition of the Southwest University Neofit Rilski, Bulgaria 2008, p 164