Espe 95. Colombia's External Current Account: Performance of Exports, Progress, and Challenges

Summary

The country’s foreign revenues studied in this document include the current account component of the balance of payments, which are made up by exports of goods and services, income from investment and other Colombian assets abroad, and current transfers, which include workers' remittances. These revenues are a primary source for financing imports of capital goods required for investment and domestic production, which affect the country's growth potential themselves. Also, they are indispensable for the sustainability of the current account and the country's foreign debt.

Despite their importance to macroeconomic stability, Colombia’s foreign income has fluctuated around 20% of GDP at their best moment. This is a very low share compared with that for advanced economies (40%) or emerging Asia (50%), and it is even lower than the one observed in Chile, Mexico and Peru, whose proportions of foreign income to GDP exceed 30%. This reflects the structure of the country's economy, which focuses on the non-tradable sector, particularly on services, whose production is directed only in a minimum part to the international market.

In terms of its composition, the sources of foreign income in Colombia are highly concentrated, given that about 70% comes from exports of goods. Exports of services reach an average participation lower than 15%, while other sources of foreign income such as factor income, remittances, and other transfers contribute with close to 20%. This structure differs substantially from advanced economies, in which the service sector plays a more active role as a generator of foreign income with an average participation of 21%, while exports of goods contribute close to 56%.

On the other hand, Colombian exports are characterized by low diversification of their destinations, being the United States the main trading partner followed by nearby countries such as Ecuador, Mexico, Panama, and Peru, whose economies are prone to similar external shocks as is Colombia. Other geographical areas of greater economic dynamism such as Asia and emerging Europe are not important trading partners for the country. The concentrated structure of Colombia's foreign revenues, both in its sources as in its destinations, makes the country's economy particularly vulnerable to terms of trade and of external demand shocks, as has happened in the past.

Exports of Goods: Characteristics and Determinants

Since 1970, the participation of Colombian goods exports in world exports has barely reached 0.3% and has concentrated in commodities, which is reflected in the low contribution of its exports to GDP growth. Until late in the 1980s, agricultural exports, mainly coffee and bananas, prevailed in the Colombian export structure. Beginning the decade of the 1990s, this composition started to change in favor of oil and other mining products, creating a high dependence on natural resources for the country's foreign sales. In addition to the high exposure to unforeseen price shocks, such dependence has limited the integration of the country's economy to global trade. This is shown by various indicators that exhibit the low insertion into global value chains.

In order to provide a better understanding of the weak performance of Colombian exports, the determinants of agricultural and industrial exports (excluding coffee) were examined. In line with the literature, econometric results showed that real depreciations have positive effects through an inverse relationship with export prices, but their magnitude is marginal due to the low elasticity of sales volumes to relative prices. The poor response of exports to the exchange rate is attributed to mitigating factors of various kinds, such as low insertion in global value chains, the cost of imported raw materials, rigidity of the installed capacity, and high trading costs, among others. On the other hand, it was found that foreign demand is the most relevant variable to explain the evolution of exported volumes, mainly industrial products and some agricultural products in the long term. In this way, the low growth of the country's trading partners during the past years helps to explain the recent stagnation of Colombian exports despite the real depreciation following the oil price fall in 2014.

The paper argues that Colombia's protectionist trade policy through the intensive use of non-tariff measures—which offset the fall in tariffs during the economic liberalization process in the early 1990s—has created an anti-export bias for the country given that protection is equivalent to a tax on exports which raises their domestic costs and reduces their competitiveness. In addition, the inefficacy of logistic services for domestic transport of cargo and of port services, the excessive regulation and institutional complexity, and the lack of infrastructure increase trading costs, thus preventing enterprises from competing with prices in the external market, preferring to earmark their production to the domestic market.

Exports of Services

In the last 25 years, services exports have grown at an average annual rate of 7.3%, higher in terms of dynamics and stability *vis-à-vis* exports of goods. However, Colombia's exports of services are characterized by their high dependency and concentration in the sale of traditional services such as travel and transportation, which represented 78% of exports of services in 2018. This sets Colombia apart from countries such as the United States, Australia, and India, in which the export of services that incorporate greater knowledge and are easily integrated into global value chains have gained participation. It is a challenge for the country's economy to take advantage of the use of information technologies and the production of modern services in order to diversify its exports.

Other Current Revenue

Among other current revenues, workers' remittances and income of direct investments of Colombia abroad stand out as resources that have contributed to buffer the country's external imbalances and whose importance to the external accounts has increased over time.

Conclusions

Colombia faces the challenge of strengthening and diversifying its sources of foreign income. Revising the protectionist structure, lowering trading costs, taking advantage of new technologies, and searching for external markets with better economic performance and with different characteristics to those of the country's economy are indispensable requisites in order to reinvigorate exports of goods and boost services exports. This will result in greater economic growth as well as on reduced vulnerability of the country's economy to the ups and downs of the global economy.

Highlighted Phrase:

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