STRUCTURAL AND CYCLICAL FACTORS OF THE CURRENT ACCOUNT BALANCE AND THE CASE OF GREECE

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ABSTRACT

This paper investigates the structural and cyclical determinants of the current account balances for European economies, focusing especially on the factors underlying recent fluctuations in the Greek current account balance. Specifically, we investigate the long-run and short-run determinants of EU countries' current account balances, using panel data analysis. The long-run drivers are identified as structural, while the short-run as cyclical. Subsequently, these estimates are used to calculate the contribution of the cyclical and structural components to the changes in Greece's current account balance over the recent period. Our results indicate that the changes in the Greek current account balance recorded in recent years are associated with improvements in its structural component, while the short-term negative change of the current account balance in 2024 is attributed to cyclical factors. These findings suggest that efforts to encourage investment in critical areas, *inter alia* through the Recovery and Resilience Facility, to improve the investment environment and pursue structural reforms, are in the right direction.

Keywords: current account balance; structural component; cyclical component; panel data analysis

JEL classification: F32; F40; C23

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ΔΙΑΡΘΡΩΤΙΚΕΣ ΚΑΙ ΚΥΚΛΙΚΕΣ ΣΥΝΙΣΤΩΣΕΣ ΤΟΥ ΙΣΟΖΥΓΙΟΥ ΤΡΕΧΟΥΣΩΝ ΣΥΝΑΛΛΑΓΩΝ: Η ΠΕΡΙΠΤΩΣΗ ΤΗΣ ΕΛΛΑΔΟΣ

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ΠΕΡΙΛΗΨΗ

Η παρούσα μελέτη διερευνά κατά πόσον οι μεταβολές στο ισοζύγιο τρεχουσών συναλλαγών της Ελλάδος οφείλονται σε παροδικές κυκλικές επιδράσεις ή/και σε μόνιμους διαρθρωτικούς παράγοντες που επηρεάζουν το εξωτερικό ισοζύγιο της οικονομίας. Σε πρώτο στάδιο, εκτιμώνται οικονομετρικά υποδείγματα τύπου panel, με τα οποία εντοπίζονται οι σημαντικότεροι προσδιοριστικοί παράγοντες που επηρεάζουν το ισοζύγιο τρεχουσών συναλλαγών των χωρών της ΕΕ, τόσο σε μακροχρόνιο ορίζοντα, οπότε οι σχετικοί προσδιοριστικοί παράγοντες αξιολογούνται ως διαρθρωτικοί, όσο και σε βραχυχρόνιο ορίζοντα, στην οποία περίπτωση οι σχετικοί παράγοντες αξιολογούνται ως κυκλικοί. Σε δεύτερο στάδιο, οι συντελεστές που έχουν προκύψει από τις ως άνω εκτιμήσεις χρησιμοποιούνται προκειμένου να υπολογιστεί η συμβολή της κυκλικής και της διαρθρωτικής συνιστώσας στις μεταβολές του ισοζυγίου τρεχουσών συναλλαγών της Ελλάδος κατά την πρόσφατη περίοδο. Σύμφωνα με τα εμπειρικά ευρήματα, η συμβολή της διαρθρωτικής συνιστώσας στις μεταβολές του ισοζυγίου τρεχουσών συναλλαγών παραμένει θετική τη διετία 2023-24, αντανακλώντας τη σημαντική βελτίωση της ανταγωνιστικότητας, του επενδυτικού περιβάλλοντος και των θεμελιωδών μεγεθών της ελληνικής οικονομίας, συμπεριλαμβανομένης της αύξησης των επενδύσεων σε κρίσιμους τομείς μέσω του Μηχανισμού Ανάκαμψης και Ανθεκτικότητας. Συνεπώς, ενδείκνυται να συνεχιστεί η επίτευξη δημοσιονομικών πρωτογενών πλεονασμάτων και να υλοποιηθούν περαιτέρω διαρθρωτικές μεταρρυθμίσεις για την ενίσχυση της ανταγωνιστικότητας και του εξαγωγικού προσανατολισμού των ελληνικών επιχειρήσεων, καθώς αυτοί είναι παράγοντες που, όπως διαφαίνεται από τις εκτιμήσεις, επηρεάζουν θετικά το ισοζύγιο τρεχουσών συναλλαγών της Ελλάδος.

ΜΗ ΤΕΧΝΙΚΗ ΣΥΝΟΨΗ

Από το 2020 και έπειτα, η εξέλιξη του ισοζυγίου τρεχουσών συναλλαγών των οικονομιών της Ευρωπαϊκής Ένωσης (ΕΕ) χαρακτηρίστηκε από έντονες διακυμάνσεις, απόρροια μιας σειράς εξωγενών διαταραχών. Σε αυτό το ευμετάβλητο περιβάλλον, η Ελλάδα, μετά τη σημαντική διόρθωση του ελλείμματος του ισοζυγίου τρεχουσών συναλλαγών της την περίοδο 2013-19, κατέγραψε εκ νέου διεύρυνσή του κατά τα έτη 2020-22, ως αποτέλεσμα των περιορισμών στην οικονομική δραστηριότητα την περίοδο της πανδημίας και της ανόδου των τιμών της ενέργειας. Το 2023 καταγράφηκε διόρθωση σε -6,8% του ΑΕΠ, από -10,7% του ΑΕΠ το 2022. Ωστόσο, το 2024 το έλλειμμα του ισοζυγίου τρεχουσών συναλλαγών διευρύνθηκε κατά 0,4 της ποσοστιαίας μονάδας (ποσ. μον.) και διαμορφώθηκε σε -7,2% του ΑΕΠ. Η εξέλιξη αυτή αποδίδεται πρωτίστως στη διεύρυνση του ελλείμματος στο εμπορικό ισοζύγιο αγαθών, καθώς οι εξαγωγές αγαθών μειώθηκαν, ενώ οι αντίστοιχες εισαγωγές αυξήθηκαν, αντανακλώντας αφενός την επιβράδυνση της οικονομικής δραστηριότητας των κύριων εμπορικών εταίρων της χώρας και αφετέρου την αύξηση των εισαγωγών κεφαλαιακών αγαθών και τον χαμηλό βαθμό υποκατάστασης των εισαγόμενων αγαθών από εγχωρίως παραγόμενα.

Η παρούσα μελέτη διερευνά κατά πόσον οι μεταβολές του ισοζυγίου τρεχουσών συναλλαγών της Ελλάδος οφείλονται σε παροδικές κυκλικές επιδράσεις ή/και σε μόνιμους διαρθρωτικούς παράγοντες που επηρεάζουν το εξωτερικό ισοζύγιο της οικονομίας. Σε πρώτο στάδιο, εκτιμώνται οικονομετρικά υποδείγματα τύπου panel, με τα οποία εντοπίζονται οι σημαντικότεροι προσδιοριστικοί παράγοντες που επηρεάζουν το ισοζύγιο τρεχουσών συναλλαγών των χωρών της ΕΕ, τόσο σε μακροχρόνιο ορίζοντα, οπότε οι σχετικοί προσδιοριστικοί παράγοντες αξιολογούνται ως διαρθρωτικοί, όσο και σε βραχυχρόνιο ορίζοντα, στην οποία περίπτωση οι σχετικοί παράγοντες αξιολογούνται ως κυκλικοί. Σε δεύτερο στάδιο, οι συντελεστές που έχουν προκύψει από την εκτίμηση των βραχυχρόνιων (κυκλικών) παραγόντων για τις χώρες της ΕΕ εφαρμόζονται στα δεδομένα για την ελληνική οικονομία, προκειμένου να υπολογιστεί η συμβολή της κυκλικής συνιστώσας στις μεταβολές του ισοζυγίου τρεχουσών συναλλαγών της Ελλάδος κατά την πρόσφατη περίοδο (2023-24). Το υπολειπόμενο μέρος των μεταβολών, που προκύπτει μετά την αφαίρεση της συμβολής της κυκλικής συνιστώσας από τη μεταβολή του ισοζυγίου τρεχουσών συναλλαγών, αποδίδεται σε διαρθρωτικούς παράγοντες. Συνεπώς, η μεθοδολογία αυτή επιτρέπει την ποσοτικοποίηση της κυκλικής και της διαρθρωτικής συνιστώσας της μεταβολής του ισοζυγίου τρεχουσών συναλλαγών για την ελληνική οικονομία.

Τα εμπειρικά αποτελέσματα καταδεικνύουν ότι η διακύμανση του ισοζυγίου τρεχουσών συναλλαγών της Ελλάδος κατά τα έτη 2023-24 οφείλεται σε σημαντικό βαθμό σε κυκλικούς παράγοντες. Ειδικότερα, οι εκτιμήσεις των οικονομετρικών υποδειγμάτων για τις χώρες της ΕΕ αναδεικνύουν ως στατιστικά σημαντικούς διαρθρωτικούς προσδιοριστικούς παράγοντες του ισοζυγίου τρεχουσών συναλλαγών, μεταξύ άλλων, τη θέση των καθαρών απαιτήσεων έναντι του εξωτερικού, το ύψος του δημοσιονομικού πλεονάσματος/ελλείμματος, το σχετικό επίπεδο εισοδήματος και τον ρυθμό μεταβολής της μακροχρόνιας τάσης της παραγωγικότητας, τον βαθμό εξωστρέφειας της εμπορικής δραστηριότητας και την ποιότητα του ρυθμιστικού πλαισίου. Επιπροσθέτως, ως στατιστικά σημαντικοί βραχυχρόνιοι προσδιοριστικοί παράγοντες αναδεικνύονται, μεταξύ άλλων, οι κυκλικές συνιστώσες του ύψους της χρηματοπιστωτικής επέκτασης και του μοναδιαίου κόστους εργασίας.

Από την εφαρμογή των εκτιμώμενων συντελεστών για τις χώρες της ΕΕ σε δεδομένα για την ελληνική οικονομία διαπιστώνεται ότι η κατά 0,4 ποσ. μον. διεύρυνση του ελλείμματος του ισοζυγίου τρεχουσών συναλλαγών στην Ελλάδα για το έτος 2024 αποδίδεται πρωτίστως σε κυκλικούς παράγοντες. Αυτοί συνέβαλαν αρνητικά, κατά 2,5 ποσ. μον., στη μεταβολή του ισοζυγίου

τρεχουσών συναλλαγών, αντανακλώντας πιθανώς την επιβράδυνση της εξωτερικής ζήτησης και την αύξηση των εισαγωγών. Αντίθετα, η συμβολή των διαρθρωτικών παραγόντων στη μεταβολή του ισοζυγίου τρεχουσών συναλλαγών το 2024 ήταν θετική και εκτιμάται σε 2,1 ποσ. μον., δεν ήταν ωστόσο επαρκής για να αντισταθμίσει την αρνητική επίδραση της κυκλικής συνιστώσας.

Συνολικά, το ισοζύγιο τρεχουσών συναλλαγών της Ελλάδος το 2024 διαμορφώθηκε σε -7,2% του ΑΕΠ, έλλειμμα το οποίο εκτιμάται ότι οφείλεται κυρίως σε διαρθρωτικά χαρακτηριστικά της οικονομίας. Ωστόσο, η συμβολή της διαρθρωτικής συνιστώσας στις μεταβολές του ισοζυγίου τρεχουσών συναλλαγών παραμένει θετική τα τελευταία δύο έτη, αντανακλώντας τη σημαντική βελτίωση της ανταγωνιστικότητας, του επενδυτικού περιβάλλοντος και των θεμελιωδών μεγεθών της ελληνικής οικονομίας. Αξιοσημείωτη ήταν η αύξηση των επενδύσεων τα τελευταία έτη, οι οποίες, με τη συνδρομή του Μηχανισμού Ανάκαμψης και Ανθεκτικότητας, κατευθύνθηκαν σε κρίσιμους τομείς, όπως οι υποδομές, η ενέργεια και τα ψηφιακά δίκτυα, συμβάλλοντας τόσο στην άμεση αύξηση της οικονομικής δραστηριότητας και τη βελτίωση του ισοζυγίου τρεχουσών συναλλαγών όσο και στη βελτίωση των μεσοπρόθεσμων προοπτικών ανάπτυξης.

Η μελέτη καταλήγει στο συμπέρασμα ότι ενδείκνυται να συνεχιστεί η επίτευξη δημοσιονομικών πρωτογενών πλεονασμάτων και να υλοποιηθούν περαιτέρω διαρθρωτικές μεταρρυθμίσεις για την ενίσχυση της ανταγωνιστικότητας και του εξαγωγικού προσανατολισμού των ελληνικών επιχειρήσεων, καθώς αυτοί είναι παράγοντες που, όπως διαφαίνεται από τις εκτιμήσεις, επηρεάζουν θετικά το ισοζύγιο τρεχουσών συναλλαγών της Ελλάδος. Επιπροσθέτως, η βελτίωση της παραγωγικότητας και των επενδύσεων σε κεφαλαιακά αγαθά και η μείωση της εξάρτησης από τις εισαγωγές, μέσω της σταδιακής υποκατάστασης των εισαγόμενων αγαθών με εγχωρίως παραγόμενα, αναμένεται ότι θα συνέβαλλαν στη μείωση της ευαισθησίας του ισοζυγίου τρεχουσών συναλλαγών σε βραχυχρόνιες (κυκλικές) διακυμάνσεις.

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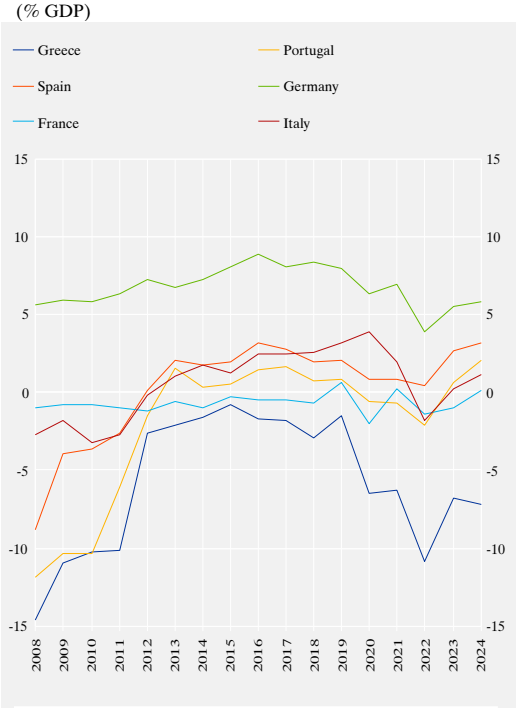
I INTRODUCTION

Over the past several years, the evolution of the current account balances (CAB) in the European Union (EU) economies has been marked by strong fluctuations, stemming from a series of exogenous shocks. Specifically, the adverse effects of the COVID-19 pandemic and the subsequent stringent restrictions imposed on economic activity, the disruptions in supply chains and the soaring energy prices, which fuelled strong broad-based inflationary pressures, adversely affected the external balances of EU countries. As depicted in Chart 1, several European economies recorded a deterioration in their current account balance during 2021-22, which is mainly attributed to the sharp rise in energy costs and import prices. However, from 2023 onwards, many economies are showing signs of a gradual normalisation of their external balances, primarily reflecting the gradual easing of inflationary pressures and more specifically the de-escalation of energy and import prices and the restoration of supply chains.

Chart 1 Current account balance of selected EU countries

(% GDP)



Sources: World Bank and Bank of Greece.

Greece recorded a significant decline of its current account deficit during 2008-19, underpinned by the sharp correction of the large macroeconomic imbalances that had built up in the run-up to the economic crisis of 2008 (see, e.g., Backinezos et al. 2020), as well as the return to a regime of fiscal discipline, with the achievement of primary surpluses. According to data from the Bank of Greece, the current account deficit recorded a remarkable reduction, from -15.3% of GDP in 2008 to -2.1% of GDP in 2019. However, it subsequently widened again in the period 2020-22, due to the negative consequences of the restrictions imposed on economic activity during the pandemic and the elevated energy prices from the end of 2021 onwards, reaching -10.7% of GDP in 2022. In 2023, another significant correction of the CAB was recorded, bringing it down to -6.8% of GDP. However, in 2024 the current account deficit widened again slightly by 0.4 percentage points, i.e. to -7.2% of GDP.[1]

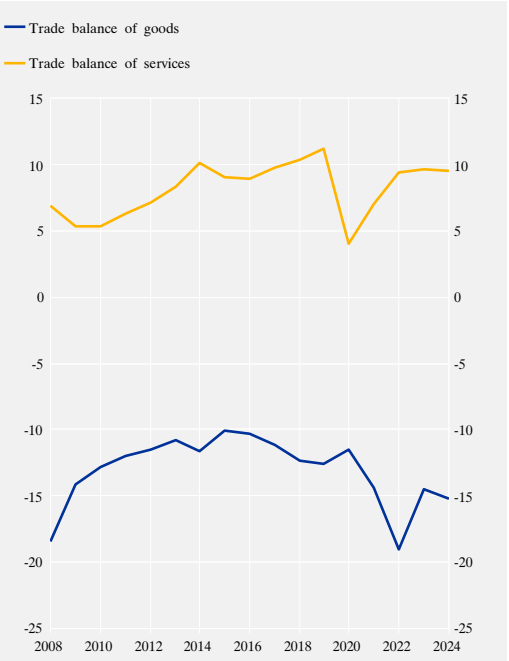
These recent developments are mainly attributed to the further widening of the deficit in the trade balance of goods. As depicted in Charts 2 and 3, exports of goods remained lower than

* The views expressed in this article are of the authors and do not necessarily reflect those of the Bank of Greece. The authors are responsible for any errors or omissions.

1 See Bragoudakis (2024) for an analysis of the evolution of the CAB in Greece during the pandemic and the recent energy crisis.

Chart 2 Trade balance of Greece

(% GDP)



Source: Eurostat.

the corresponding imports, maintaining the negative trade balance of goods, despite a positive trend in the current account balance in recent years. This reflects, on the one hand, the slowdown in the economic activity of the country's main trading partners and, on the other hand, the increase in imports of capital goods to support domestic investment, as well as the low degree of substitution of imported consumption goods by domestically-produced goods. On the contrary, exports of services remained higher than imports of services, mainly reflecting the strong tourism performance recorded in the recent years. However, they were not sufficient to mitigate the negative trade balance of goods.

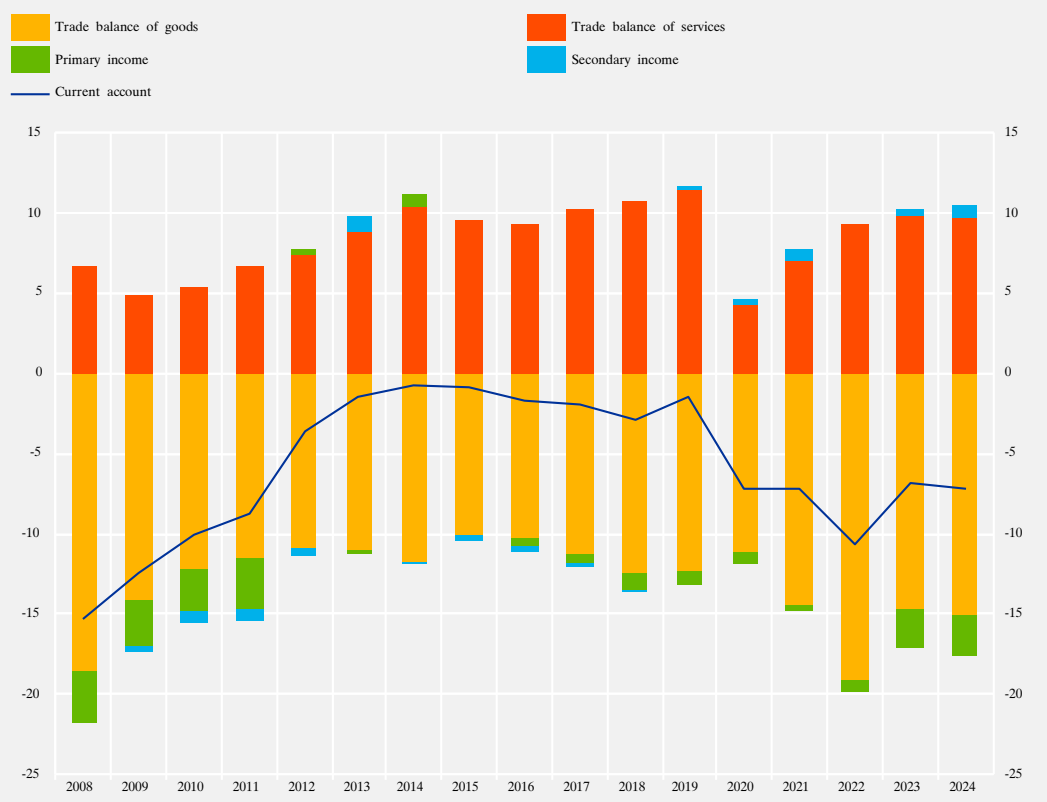
The recent fluctuations in the Greek current account balance bring to the forefront the question of whether they are attributed to transitory cyclical effects or reflect permanent structural factors that drive the external balance of the economy. Identifying whether structural or cyclical factors have driven the recent changes in the current account balance is essential in order to gauge its future trajectory and evaluate the effectiveness of alternative policies that could potentially contribute to the gradual narrowing of the current account deficit.

Against this background, the objective of this paper is, first, to investigate the structural and cyclical determinants of the current account balances for the European economies and, subsequently, to identify the structural or cyclical components of the recent changes in the Greek current account balance. To do so, we adopt the empirical methodology proposed by Cheung et al. (2010, 2013) and Chinn and Prasad (2003), in which the changes in the current account balance are decomposed into their cyclical and structural components.

The contribution of our paper is twofold. First, we investigate the long- and short-run determinants of current account balances using panel data analysis for the EU countries. The long-run drivers of the CAB, including, *inter alia*, institutional and competitiveness factors, are identified as structural, while the short-run determinants are viewed as cyclical. Our approach allows the estimation of the parameters that reflect the magnitude and direction of the impact of each individual determinant on the current account for the EU economies in our sample. Second, we focus on the case of Greece. The coefficients obtained from the estimation of the short-term (cyclical) factors for EU countries are applied to the data for the Greek economy, in order to calculate the contribution of the cyclical component to the changes in Greece's current account over the recent period. The residual obtained after subtracting the contribution of the cyclical component from the total change in the current account is attributed to structural factors. Therefore, the second stage of our empirical methodology allows for the quantification of the cyclical and structural components of the change in the current account balance for the Greek economy.

Chart 3 Components of the Greek current account

(% GDP)



Source: Eurostat.

Our findings can be summarised as follows: First, the estimation results from the panel regressions for EU countries highlight as statistically significant a number of structural determinants of the current account balance, *inter alia*, the position of net foreign assets, the fiscal balance over GDP, relative income and the rate of long-term economic growth, the degree of trade openness and the quality of the regulatory framework. In addition, the cyclical components of private credit to GDP and unit labour costs are identified as statistically significant short-term determinants of EU current accounts. In a second step, by applying the cyclical coefficients estimated for the EU countries to Greek data, we show that the fluctuation of Greece's current account deficit over the years 2023-24 is due, to a significant extent, to cyclical factors. On the contrary, the contribution of the structural component to changes in the Greek current account balance has remained positive over the last two years of the sample, arguably reflecting the significant improvements in competitiveness, the investment environment and the fundamentals of the Greek economy achieved in recent years.

The rest of the paper is organised as follows: Section 2 provides a brief literature review. Section 3 discusses our data sample and presents our empirical strategy, while Section 4 introduces our main findings. Finally, Section 5 concludes.

2 LITERATURE REVIEW

The determinants of current account balances have been extensively examined in interna-

tional macroeconomics, particularly in the context of research on global imbalances, external sustainability and macroeconomic adjustment within monetary unions. The literature distinguishes between cyclical determinants, associated with temporary fluctuations in economic activity and financial conditions, and structural determinants, which influence saving, investment and competitiveness, and, through these, the CAB over the medium to long term. In this vein, emphasis has been placed on the role of structural reforms and improvements in the investment environment in fostering sustainable current account adjustment.

Early empirical contributions include Debelle and Faruqee (1996), who analyse current account balances using cross-sectional and panel-data techniques for industrial and developing economies. Their findings suggest that demographic factors, fiscal balances, stages of development and terms-of-trade movements significantly affect external balances. This paper was among the first to distinguish between short- and long-run determinants of the CAB. Chinn and Prasad (2003) later investigated medium-term determinants of current account balances across industrial and developing countries, using panel regressions. They show that government budget balances, net foreign asset positions, demographic variables and relative income levels are key determinants of external positions. Their results support the "twin deficits" hypothesis for advanced economies and underline the importance of institutional and financial development in shaping saving-investment balances. Importantly, their benchmark reduced-form framework was widely adopted in the literature.

Building on their approach, Cheung et al. (2010, 2013) explicitly distinguish between cyclical and structural factors behind current account balances. Using a panel of 94 countries spanning the period from 1973 to 2008, they demonstrate that output gaps, commodity price fluctuations and temporary demand shocks explain short-run movements in current accounts, whereas structural characteristics exert more persistent effects. In particular, labour market flexibility, product market regulation and institutional quality are found to influence competitiveness, productivity and resource allocation between tradable and non-tradable sectors. Their findings notably suggest that better financial regulation as well as structural reforms aimed at strengthening the business climate can improve current account balances over the medium term, by bolstering export performance and enhancing productive efficiency.

Beyond the aforementioned seminal papers, several studies in this strand of the literature focus on the role of structural policies and institutional reforms. Kennedy and Sløk (2005) examine how such structural reforms in labour markets, product markets and financial markets affect current accounts and find that, while many do have a significant impact on current account developments, the size of their contribution is quite limited. Ju and Wei (2007) show that labour market rigidities influence the speed and persistence of current account adjustment. Chinn and Ito (2007) update and extend the research by Chinn and Prasad (2003) by additionally incorporating the effects of the legal environment and the level of institutional development and exploring their interplay with fiscal balances and financial development as regards their impact on the current account. Kerdrain et al. (2010) examine how labour market reforms, financial liberalisation and product market deregulation affect saving and investment dynamics and find that structural reforms influence current accounts both directly and indirectly through productivity growth and investment responses. Gruber and Kamin (2007) additionally explore the impact of financial crises on current accounts.

The literature on Greek current account imbalances also emphasises the interaction between structural weaknesses, macroeconomic policy distortions and cyclical developments, particularly in the period preceding the

sovereign debt crisis.[2] A broad consensus has emerged that the substantial widening of the Greek current account deficit after euro area accession reflected not only strong domestic demand and credit expansion, but also persistent competitiveness losses and structural weaknesses in the productive base of the economy. Brissimis et al. (2010) identify declining external competitiveness, financial liberalisation and increased capital inflows following participation in the Economic and Monetary Union (EMU) as central determinants of the deterioration in Greece's external position. Their analysis, based on co-integration techniques, suggests that the Greek current account deficit became increasingly unsustainable due to weak export performance and excessive reliance on non-tradable sectors. Similarly, the Bank of Greece repeatedly stressed in its publications that low export diversification, rigid product and labour markets, limited technological intensity and chronic investment inefficiencies constrained the adjustment capacity of the Greek economy (Athanasoglou et al. 2010; Bank of Greece 2020a). Arghyrou and Chortareas (2008) further argued that EMU participation reduced borrowing costs and relaxed external financing constraints, thereby facilitating persistent external deficits without corresponding productivity gains. In addition, Gibson et al. (2012) emphasised the role of fiscal imbalances and institutional weaknesses in amplifying external vulnerabilities during the pre-crisis period. More recent studies underline that the subsequent correction of the Greek current account deficit after 2010 resulted partly from cyclical compression in domestic demand during the recession, but also from structural reforms that improved labour cost competitiveness and export performance (Backinezos et al. 2020; Bank of Greece 2020b; IMF 2019). The literature generally concludes that durable external adjustment in Greece depends on sustained productivity growth, stronger tradable sectors, improvements in the investment environment and higher-quality institutions rather than solely on demand-side contraction.

In sum, the literature suggests that current account balances are shaped by the interaction between cyclical conditions and structural characteristics. While temporary fluctuations in output and financial conditions explain short-run developments, medium- and long-run outcomes depend critically on productivity, competitiveness, institutional quality and the investment environment. Academic research and institutional analyses converge on the conclusion that structural reforms enhancing productivity, export capacity and business conditions are essential for sustainable external adjustment, particularly in euro area economies where nominal exchange rate adjustment is limited.

3 DATA AND EMPIRICAL METHODOLOGY

3.1 DATA DESCRIPTION

Our sample covers the EU27 member countries for the period 1970-2024. The panel dataset is unbalanced; thus, there are differences in the length of the series for some variables by country, due to missing data (especially during the 1970s). Also, for the institutional variables the dataset starts from the 1990s, so the sample is reduced accordingly. The sources of our data include the World Bank, the European Commission, the Energy Institute Statistical Review of World Energy, the BIS and the 2024 update of the external wealth of nations database by Lane and Milesi-Ferretti (2018).

As our dependent variable, we use the current account balance over GDP drawn from the World Bank. Moreover, we control for a series of explanatory variables that are widely used in the relevant empirical literature (see, e.g.,

2 Following the sovereign debt crisis, European institutions increasingly linked persistent current account deficits to weak competitiveness and insufficient structural adjustment. Notably, the European Commission, within the framework of the Macroeconomic Imbalance Procedure, emphasises the importance of labour market flexibility, productivity growth and efficient resource allocation in correcting external imbalances (European Commission 2016).

Chinn and Ito 2007; Chinn and Prasad 2003; Gruber and Kamin 2007; Altayligil and Çetrez 2020). These include macroeconomic, demographic, financial and institutional factors. As macroeconomic factors, we include, among others, the per capita GDP growth rate (used as a proxy for productivity growth), the stage of economic development (the variable used to proxy for the stage of economic development is the relative (to the EU) income per capita), the net foreign assets-to-GDP ratio, the government primary budget balance over GDP, trade openness (defined as exports plus imports over GDP), oil prices and oil consumption. As demographic factors, we use the youth and old age dependency ratios, and as financial indicators, the credit-to-GDP ratio and financial development indices. We also use real effective exchange rates (REER) and unit labour costs as measures of a country's competitiveness. Regarding the institutional determinants, we use the World Governance Indicators from the World Bank.

Following Cheung et al. (2010, 2013) and Gruber and Kamin (2007), we express all the explanatory variables as deviations from their GDP-weighted EU mean (except for net foreign assets), since current account balances are relative measures depending on the developments in other countries.[3]

3.2 EMPIRICAL STRATEGY

To assess the structural and cyclical factors that determine current account balances in the EU, we work in two stages. First, we estimate the medium-term or structural factors that drive current accounts. Second, we focus on their short-term or cyclical determinants.

3.2.1 ESTIMATION OF STRUCTURAL DETERMINANTS

To examine the structural factors that shape the movements of current account balances in the EU, we estimate the medium-term trends of our explanatory variables. To do so, we estimate the following general specification, using ordinary least squares (OLS):

$$\overline{CA}_{i,t} = \bar{\alpha} + \bar{\beta}_1 \bar{X}_{i,t} + \bar{\beta}_2 \bar{I}_{i,t} + \bar{\beta}_3 \bar{Z}_{i,t} + c_i + \tau_t + \varepsilon_{i,t} \quad (1)$$

where $\overline{CA}_{i,t}$ is the medium-term trend value of the CAB in country i at time t and $\bar{X}_{i,t}$ is the vector of the medium-term trend values of macroeconomic, demographic and financial variables. This serves as our benchmark specification. Moreover, we examine the role of institutional and competitiveness factors, augmenting our regression equation with these factors, where $\bar{I}_{i,t}$ is the vector of the medium-term trend values of institutional variables and $\bar{Z}_{i,t}$ is the vector of the medium-term trend values of competitiveness variables. We calculate the medium-term trend values as the non-overlapping four-year averages of all variables. As a result, we rule out any cyclical fluctuations and reduce the possibility of measurement errors.[4] Finally, equation (1) includes country fixed effects, c_i, time effects, τ_t, and $\varepsilon_{i,t}$ which is a zero-mean error term. Variations in the set of variables included give rise to different models examined.[5]

3.2.2 ESTIMATION OF CYCLICAL DETERMINANTS

Following the relevant literature (see, e.g., Cheung et al. 2010, 2013), the cyclical component of each variable is constructed as the annual deviation from its four-year overlapping (moving) average. This filtering method smooths out temporary shifts, while maintaining the slower-

3 It is worth noting that Cheung et al. (2010, 2013) convert their explanatory variables into deviations from their GDP-weighted world mean; in contrast, we use the EU GDP-weighted mean as our baseline, since we want to explain differences between EU member states relative to the EU average. For robustness, we could examine the same relationship using the GDP-weighted world mean, since several EU countries direct the bulk of their exports towards non-EU countries. We leave this approach for future work.

4 It is worth noting that Cheung et al. (2010, 2013) use the non-overlapping five-year averages of all variables to approximate their medium-term trend values; however, we use the four-year averages to gain observations mainly due to the fact that we focus our analysis only on the EU economies, in contrast to the corresponding literature where larger samples of countries are used (e.g. developing vs developed).

5 Moreover, as a robustness check, we perform instrumental variable two-stage least squares estimations (IV–2SLS) to address any reverse causality issues driven by the potential endogeneity between fiscal balances and current account balances. Following the related literature (Cheung et al. 2013), we use government effectiveness as an instrument in the IV estimation. The resulting estimates corroborate the robustness of our main OLS estimates. Results are available upon request.

moving structural path of the data. The cyclical components therefore capture only temporary movements of the factors examined in the structural estimations, away from their corresponding medium-term trajectories. For instance, these transitory changes could capture short-lived changes in income, competitiveness, credit conditions or trade dynamics.

Next, we estimate a dynamic version of equation (1), in order to identify the short-term determinants of the current account balances, using as regressors the cyclical components of each variable. The specification for the short-term or cyclical estimations is:

$$\widetilde{CA}_{i,t} = \tilde{\alpha} + \rho\widetilde{CA}_{i,t-1} + \tilde{\beta}_1\tilde{X}_{i,t} + \tilde{\beta}_2\tilde{I}_{i,t} + \tilde{\beta}_3\tilde{Z}_{i,t} + c_i + \tau_t + \varepsilon_{i,t} \quad (2)$$

where $CA_{i,t}$ denotes the cyclical component of the current account balance of country i at time t, and so on for the other variables with a tilde.

Thus, except for the cyclical components of the various variables, the short-term equation also includes the lagged value of the cyclical component of the current account balance. Estimating equation (2) by least squares would provide biased estimates, due to the presence of the lagged dependent variable as an additional regressor, in addition to the endogeneity caused by the reverse causality between fiscal and current account balances. To this end, we adopt the generalized method of moments (GMM) estimators by Arellano and Bover (1995) which produce consistent estimates of the parameters in the presence of unobserved heterogeneity and simultaneity caused by correlation between the regressors and the error term. The consistency of the estimates depends on the validity of the instrumental variables set, which are tested using the Hansen test for the validity of orthogonality conditions (over-identifying restrictions).

3.2.3 CALCULATION OF THE IMPLIED CYCLICAL CONTRIBUTIONS

Finally, we calculate the fraction of the change in Greece's current account during the years 2023-24 that can be attributed to cyclical and structural drivers. To decompose the change in the current account balance (CAB) into its cyclical and structural components, we follow the approach by Cheung et al. (2010). Specifically, the changes in the current account balance can be split into changes in its cyclical and its structural components, i.e.:

$$\Delta CA_t = \Delta CA_t^{cyc} + \Delta CA_t^{str} \quad (3)$$

We multiply the constructed cyclical components of our explanatory variables by the corresponding estimated coefficients obtained from our baseline panel GMM estimation for the EU27 countries, i.e. a version of equation (2), in which we exclude institutional and demographics variables.[6] This provides a measure of each variable's short-run (cyclical) contribution to the year-on-year change in the Greek current account balance. Summing up these contributions, we obtain the total estimated cyclical component of the change in the Greek current account balance for each year. Specifically, the change in the total cyclical component is determined using the coefficients derived from the estimation of the cyclical CA and the changes in the cyclical components of each of the explanatory variables, as follows:

$$\Delta CA_{GR,t}^{cyc} = \rho\Delta\widetilde{CA}_{GR,t-1} + \tilde{\beta}_1\Delta\tilde{X}_{GR,t} + \tilde{\beta}_2\Delta\tilde{I}_{GR,t} + \tilde{\beta}_3\Delta\tilde{Z}_{GR,t} \quad (4)$$

The structural contribution is then obtained residually, as the difference between the observed change in the current account and the estimated cyclical component, i.e.:

$$\Delta CA_{GR,t}^{str} = \Delta CA_{GR,t} - \Delta CA_{GR,t}^{cyc} \quad (5)$$

This residual measure represents the underlying and persistent forces influencing Greece's external balance, i.e. those not driven by short-

6 These variables move slowly and are not expected to exhibit significant cyclical variation. However, we have also estimated the cyclical specification including some of these variables and our results remain qualitatively robust. Results are available upon request.

term fluctuations. These can be attributed to slow-moving changes in the fundamental characteristics of the Greek economy.

4 RESULTS

4.1 STRUCTURAL (MEDIUM-TERM) CURRENT ACCOUNT BALANCE DETERMINANTS IN EU COUNTRIES

Table 1 reports the estimation results of our baseline structural specification, i.e. the specification which does not incorporate institutional and competitiveness factors. The first five columns present the results obtained when we allow for country fixed effects, while columns 6-10 report the results with both country and time fixed effects.[7]

The estimates obtained from our baseline specification, i.e. equation (1) without the terms $\bar{\beta}_2 \bar{I}_{i,t} + \bar{\beta}_3 \bar{Z}_{i,t}$, are broadly in line with the existing empirical literature on the determinants of current account balances. Our findings corroborate a statistically significant positive relationship between fiscal and current account balances, supporting the "twin deficits" hypothesis. In general, the magnitude of this coefficient is broadly similar to the values suggested by the literature (see, e.g., Gruber and Kamin 2007; Cheung et al. 2013; Altayligil and Çetrez 2020). The coefficient is very close to 0.3 across all the reported specifications, implying that a 1 percentage point increase in the government deficit (surplus) is associated with a 0.3 percentage points increase in the current account deficit (surplus).

Moreover, we find positive and statistically significant coefficients for the net foreign assets (NFA) to GDP ratio, implying that a country's net foreign asset position affects the current account through the accumulation of past CABs or through direct changes in the net primary income. Also, we observe a negative statistically significant relationship between the current account balance and economic growth across 5 of the 10 specifications examined. This result can be attributed to the fact that, on the one hand, higher economic growth increases import demand to support investment and consumption and, on the other hand, a higher medium-term trend per capita GDP growth is translated into higher productivity growth, which in turn could attract foreign capital flows since they are expected to provide higher rates of return. We also detect a positive and statistically significant relationship between trade openness and the CAB, across all the specifications, which might suggest that, over the long run, trade openness is associated with more export-led growth, as the absence of barriers to trade allows domestic industries to tap into larger global markets. In a similar vein, we get significant positive coefficients (with only one exception) for the stage of economic development, which is proxied by the relative (to the EU) income per capita and negative coefficients for the squared relative income per capita. This result is consistent with the stage-of-development hypothesis advanced by Chinn and Prasad (2003) and Cheung et al. (2010, 2013). Within the EU, countries at a more advanced stage of development tend to exhibit higher saving relative to investment and stronger external positions, while relatively less developed economies often rely more heavily on external financing to support capital accumulation and economic growth. However, the negative coefficient of the squared term confirms the U-shaped relationship documented in the related literature (e.g. Cheung et al. 2013), i.e. the CAB improves with income up to a point, then declines.

Finally, we find a negative coefficient for the oil consumption value, reflecting the high energy import dependency of the EU economies as well as the fact that countries with higher oil consumption are more vulnerable to oil price shocks, worsening their terms of trade. Both effects put downward pressure on CABs. Additionally, we get a positive coefficient for the

7 We have also examined the case with time effects only and our results remain qualitatively the same. We do not report them due to space limitations. These results are available upon request.

Table 1 Structural determinants of the CAB (OLS)

Dependent variable (CAB/GDP)	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)
Net Foreign Assets/GDP	0.022**	0.015	0.015	0.022**	0.015	0.032***	0.027**	0.026**	0.021	0.021*
	(0.010)	(0.010)	(0.011)	(0.010)	(0.012)	(0.011)	(0.010)	(0.011)	(0.015)	(0.011)
Primary balance/GDP	0.324**	0.360**	0.358***	0.317**	0.345**	0.306***	0.341***	0.343***	0.218**	0.309***
	(0.121)	(0.131)	(0.111)	(0.120)	(0.139)	(0.092)	(0.108)	(0.096)	(0.101)	(0.106)
Relative income	0.090***	0.036	0.119***	0.090***	0.112**	0.029	-0.011	0.056	-0.073**	0.036
	(0.029)	(0.039)	(0.029)	(0.028)	(0.043)	(0.039)	(0.047)	(0.039)	(0.028)	(0.044)
Relative income squared	-0.031***	-0.019*	-0.033***	-0.031***	-0.050***	-0.014	-0.005	-0.016	0.007	-0.031***
	(0.010)	(0.011)	(0.008)	(0.010)	(0.013)	(0.012)	(0.014)	(0.011)	(0.007)	(0.010)
Growth (per capita GDP)	-0.187	-0.269*	-0.140	-0.191	-0.301**	-0.188*	-0.229*	-0.141	-0.029	-0.245*
	(0.117)	(0.143)	(0.124)	(0.138)	(0.124)	(0.109)	(0.130)	(0.123)	(0.198)	(0.120)
Trade openness	0.075***	0.065**	0.071***	0.075***	0.113***	0.065**	0.056*	0.061**	0.106***	0.090***
	(0.024)	(0.026)	(0.023)	(0.024)	(0.022)	(0.030)	(0.031)	(0.028)	(0.031)	(0.028)
Oil consumption per capita		-0.988*					-0.724			
		(0.496)					(0.449)			
Youth dependency ratio			0.303**					0.277**		
			(0.118)					(0.105)		
Private credit to GDP				-0.002					-0.029**	
				(0.014)					(0.012)	
Financial development index					-0.050					-0.075**
					(0.048)					(0.031)
Country effects	YES	YES	YES	YES	YES	YES	YES	YES	YES	YES
Time effects	NO	NO	NO	NO	NO	YES	YES	YES	YES	YES
Observations	261	254	261	260	219	261	254	261	260	219
R-squared	0.228	0.204	0.260	0.226	0.292	0.480	0.458	0.505	0.481	0.541
Number of countries	27	26	27	27	27	27	26	27	27	27

Note: The dependent variable is the current account balance over GDP. Robust standard errors in parentheses, *** p<0.01, ** p<0.05 and * p<0.1.

youth dependency ratio[8] and negative coefficients for the private credit to GDP as well as the financial development index. Deeper financial markets reduce the need for precautionary savings through easier access to credit for households and firms, lowering current account balances.

Table 2 presents the estimation results after incorporating institutional and competitiveness factors in our baseline specification (i.e. including $\bar{\beta}_2\ \bar{I}_{i,t}+\bar{\beta}_3\ \bar{Z}_{i,t}$ to the regression equation). The coefficients of the main macroeconomic control variables remain qualitatively similar to those from the baseline estimations (see Table 1). Regarding the institutional variables examined, we report only the estimated coefficients for regulatory quality and the voice and accountability variables which are found to be negative and statistically significant (increases in these indices are associated with improved specific aspects of institutional quality).[9] This result is also evident in the studies by Gruber and Kamin (2007) and Cheung et al. (2013). Improved institutional quality reduces uncertainty around future economic conditions, leading to lower precautionary savings. Furthermore, a more business-friendly institutional environment increases the inflows of foreign capital, reducing the current account balance. Also, we get negative coefficients for

8 We obtain similar positive coefficients for the old age dependency ratio (but statistically significant only for one regime). The positive relationship may reflect the fact that, within the EU economies and in a relative and medium-term context, a higher age dependency ratio may boost national savings and improve the CAB for the euro area, in line with the extended life-cycle hypothesis (see Bank of Greece (2026), *Annual Report 2025*, Box IV.6).

9 We also examined the following variables from the World Bank Governance Indicators: political stability, government effectiveness, rule of law and control of corruption. However, we do not report them, since we obtained statistically insignificant coefficients.

Table 2 Structural determinants of the CAB (OLS, including institutional and competitiveness factors)

Dependent variable (CAB/GDP)	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)
Net Foreign Assets/GDP	0.019** (0.009)	0.017* (0.009)	0.018 (0.012)	0.016 (0.010)	0.024** (0.010)	0.021 (0.012)	0.020 (0.012)	0.027** (0.012)	0.019 (0.012)	0.033*** (0.011)
Primary balance/GDP	0.501*** (0.162)	0.539*** (0.157)	0.322** (0.124)	0.446** (0.168)	0.264** (0.122)	0.477*** (0.152)	0.507*** (0.149)	0.304*** (0.108)	0.422** (0.163)	0.262** (0.099)
Relative income	0.088** (0.032)	0.075** (0.030)	0.118** (0.056)	0.122** (0.051)	0.094*** (0.032)	0.072 (0.045)	0.061 (0.044)	0.052 (0.058)	0.095* (0.049)	0.031 (0.039)
Relative income squared	-0.026*** (0.009)	-0.023*** (0.008)	-0.035** (0.014)	-0.035*** (0.012)	-0.037*** (0.010)	-0.020 (0.013)	-0.017 (0.012)	-0.019 (0.014)	-0.027** (0.011)	-0.018* (0.010)
Growth (per capita GDP)	-0.303*** (0.085)	-0.333*** (0.094)	-0.202 (0.125)	-0.377*** (0.092)	-0.325*** (0.108)	-0.247** (0.098)	-0.275** (0.101)	-0.166 (0.125)	-0.317*** (0.112)	-0.299** (0.116)
Trade openness	0.064** (0.027)	0.061** (0.028)	0.073** (0.027)	0.066** (0.027)	0.078*** (0.023)	0.041 (0.026)	0.038 (0.027)	0.066* (0.033)	0.043 (0.027)	0.068** (0.029)
Regulatory quality	-0.034* (0.018)					-0.025* (0.015)				
Voice and Accountability		-0.040* (0.021)					-0.034* (0.017)			
REER_CPI			-0.005 (0.004)					-0.005 (0.003)		
REER_ULC				-0.004 (0.004)					-0.004 (0.003)	
Real Unit Labour Cost					-0.010** (0.004)					-0.007** (0.004)
Country effects	YES	YES	YES	YES	YES	YES	YES	YES	YES	YES
Time effects	NO	NO	NO	NO	NO	YES	YES	YES	YES	YES
Observations	206	206	224	206	261	206	206	224	206	261
R-squared	0.292	0.285	0.211	0.281	0.259	0.484	0.483	0.439	0.479	0.495
Number of countries	27	27	24	27	27	27	27	24	27	27

Note: The dependent variable is the current account balance over GDP. Robust standard errors in parentheses, *** p<0.01, ** p<0.05 and * p<0.1.

some competitiveness indicators, i.e. the real effective exchange rate (REER) based on the consumer price index (CPI) and the unit labour cost (ULC) as well as for the real unit labour cost; however, we get statistically significant estimates only for the latter and their magnitude seems smaller compared to the remaining structural determinants. This may indicate that the competitiveness indices are in fact related mainly to the short-run fluctuations of the CAB, as discussed in the next subsection.

4.2 CYCLICAL (SHORT-TERM) CURRENT ACCOUNT BALANCE DETERMINANTS IN EU COUNTRIES

To assess the short-run drivers of the current account balances in the EU, we estimate equation (2) using the cyclical components of our explanatory variables, i.e. the variables after removing their medium-term trend component. It is worth noting that we do not include in our short-run estimations the cyclical components of variables relating to e.g. institutional quality and demographics, since they are not expected to exhibit cyclical variation.[10] Therefore, we focus only on the cyclical components of the macroeconomic variables examined in the baseline specification of the structural estimations (i.e. net foreign assets, government balance, relative income and its squared term, trade openness and economic

10 We have also experimented with alternative specifications including these variables and our results do not alter qualitatively.

growth). In addition, we augment our baseline specification with competitiveness and financial factors (specifically, with credit to GDP and real unit labour cost) that exhibit short-term fluctuations and are expected to affect the cyclical component of the CAB.

We estimate the cyclical specification using the system generalized method of moments (GMM) estimator (Arellano and Bover 1995), including a lagged dependent variable to capture persistence.[11] The potentially endogenous variables – net foreign assets and the government primary balance – are instrumented using their own lagged values (lags 2-3), while the remaining controls are treated as predetermined or weakly exogenous and included as standard instruments in the level equation. Also, following Cheung et al. (2013), we estimate an augmented version of our specification that includes per capita oil consumption volume as well as a variable that captures oil price shocks. This latter variable is defined as the Brent crude oil price multiplied by a weight, which is computed as the trend share of oil consumption volume in GDP, relative to the EU average and allows oil price shocks to affect countries asymmetrically, depending on their structural oil dependence. Hence, in this way, both volume and price can affect the short-run fluctuations of the current account. Table 3 presents the resulting estimates.

Table 3 Cyclical determinants (IV-GMM estimations)

Variables	(1)	(2)
$(CAB/GDP)_{t-1}$	-0.519***	-0.527***
	(0.149)	(0.144)
Primary balance/GDP	0.175	0.176
	(0.256)	(0.205)
Growth (per capita GDP)	-0.036	-0.032
	(0.056)	(0.053)
Trade openness	-0.089	-0.087
	(0.078)	(0.085)
NFA/GDP	0.021	0.020
	(0.024)	(0.027)
Real Unit Labour Cost	-0.030***	-0.029**
	(0.010)	(0.011)
Credit to GDP	-0.037*	-0.039**
	(0.018)	(0.018)
Oil consumption per capita		-0.016
		(0.019)
Oil shock[1]		-0.005*
		(0.002)
Constant	-0.001	0.001
	(0.000)	(0.001)
Hansen's test p-value	0.329	0.362
Observations	664	664
Number of countries	17	17

Note: Standard errors in parentheses, *** p<0.01, ** p<0.05 and * p<0.1.
1 Oil shock is defined as the oil price multiplied by a weight, which is defined as the trend share of oil consumption volume in GDP, relative to the EU average. This variable allows oil price shocks to affect countries asymmetrically depending on their structural oil dependence.

Our empirical estimations provide statistically significant coefficients for the lagged value of the current account balance, indicating a significant degree of persistence. Moreover, we get a negative statistically significant coefficient for the oil price shock variable, implying intuitively that a short-run rise in oil prices worsens the current account balances. Finally, and most interestingly, we get negative and statistically significant coefficients for the real unit labour cost and the private credit to GDP ratio. Regarding the former, a short-term increase in the real unit labour cost is associated with a deterioration in a country's competitiveness, hurting exports and leading to a decrease in the current account balance. Also, temporary increases in the supply of credit are associated with lower saving and higher consumption and investment, i.e. higher aggregate demand. As a result, the rise in imports of capital and consumption goods leads to a deterioration in current account balances over the short run. We find a negative coefficient of trade openness in the cyclical estimation, in contrast to the corresponding structural estimate. This could perhaps be attributed to its definition as the sum of exports and imports over GDP. In this case, it could likely reflect the procyclicality of imports. During economic expansions, open economies experience stronger increases in

11 We also performed several OLS estimations using the same set of control variables and our results are similar to those obtained in GMM estimations. However, we only report GMM estimation results, since we also control for endogeneity issues. Results are available upon request.

their demand for imports – particularly for intermediate and capital goods – which temporarily deteriorates their current account balance. In contrast, the positive effect found in the structural estimation arguably reflects the long-run benefits of trade openness through improved competitiveness and export capacity. The coefficients of the rest of the explanatory variables are of the same sign as in the structural estimations; however, they are not statistically significant. This could suggest that their effects are more relevant at medium-term horizons rather than in driving short-run fluctuations. Thus, they should be interpreted with caution.

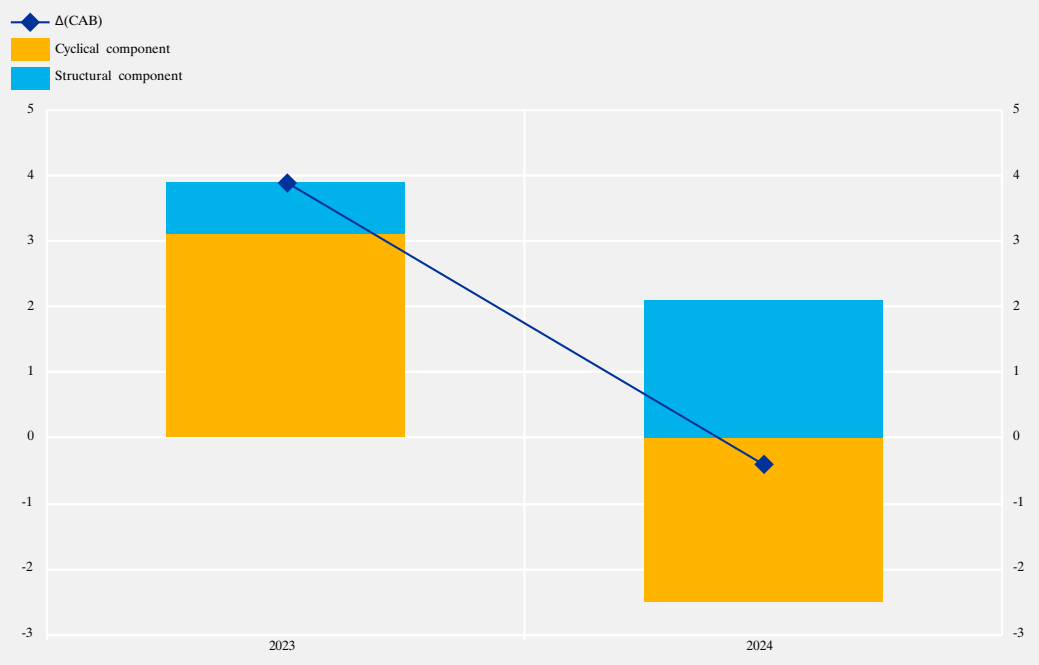
4.3 CONTRIBUTION OF CYCLICAL FACTORS TO CHANGES IN THE GREEK CURRENT ACCOUNT BALANCE

In this section, we apply the estimated cyclical coefficients to the actual change in the Greek current account balance observed in the data, so as to compute the cyclical component of the recent fluctuations. Specifically, we multiply the estimated coefficients obtained from our baseline panel GMM estimation (column (1) in Table 3) by the constructed cyclical components of our explanatory variables. These calculated values provide an estimate of each variable's short-run (cyclical) contribution to the year-on-year change in the current account balance. Summing up these contributions, we obtain the total estimated cyclical component for each year. The structural contribution is then obtained residually, as the difference between the change in the current account balance and its estimated cyclical component. This residual is interpreted as capturing the underlying and persistent forces influencing Greece's external balance, i.e. those not driven by short-term demand fluctuations.

Chart 4 presents the structural and cyclical contributions to the change of the current account balance for Greece during 2023-24. Despite the fact that the level of the current account deficit is mainly due to structural

Chart 4 Change in the current account balance of Greece, structural and cyclical components

(percentage points over GDP)



Source: Bank of Greece calculations.

characteristics of the Greek economy (see Bank of Greece (2026), *Annual Report* 2025, Box IV.4), the recent changes in the CAB indicate a gradual improvement in its structural component, with the short-term negative fluctuation of the CAB in 2024 being attributable to cyclical factors.

Our analysis reveals that the 0.4 percentage points widening of the current account deficit in Greece for 2024 (from -6.8% to -7.2%) was primarily driven by cyclical factors. Specifically, the cyclical component made a negative contribution of 2.5 percentage points to the change in the current account balance, reflecting weaker external demand and higher demand for imports. On the contrary, the contribution of structural factors to the change in the current account balance in 2024 was positive, estimated at 2.1 percentage points, but not sufficient to offset the negative impact of the cyclical component. It is worth noting that the contribution of the structural component to the change in the CAB over the last two years remains positive, arguably reflecting the significant structural reforms and improvement in competitiveness of the Greek economy, as well as the gradual establishment of an investment-friendly environment. Moreover, the significant increase in investment recorded in recent years, supported by the funds from the Recovery and Resilience Facility, has been directed to critical sectors such as infrastructure, energy and digital networks. Although the rise in investment may initially increase imports of capital goods and weigh on the current account balance, it is expected to strengthen the productive base of the economy, improve competitiveness and support a more sustainable external position over the medium term.

5 CONCLUSION

This paper examines the structural and cyclical determinants of the current account balances for the European economies in general and Greece in particular and explores to what extent the recent fluctuations in the Greek current account balance can be attributed to cyclical or structural components. Applying a two-stage empirical approach, we first decompose the possible determinants of the CAB into their structural and cyclical components, where the structural component is defined as the non-overlapping four-year average, while the cyclical component is defined as the annual deviation from the corresponding overlapping four-year average. Next, we identify the statistically significant structural and cyclical determinants of the current account balances for the European economies. Our empirical findings suggest that medium-term trends of the government budget balance, the net foreign assets position, the degree of trade openness, the stage of economic development and the regulatory quality are significant structural determinants of the CABs. By contrast, the short-term fluctuations in the CAB are primary related to the cyclical component of credit supply and labour costs.

Furthermore, we apply the estimated cyclical coefficients to the actual change in the Greek current account balance observed in the data during 2023-24, so as to derive its total cyclical component. Then, the structural contribution is derived residually, as the difference between the change in the current account balance and the estimated cyclical component. Our analysis indicates that the recent changes in the Greek CAB are associated with an improvement of its structural component, with the short-term negative change of the CAB in 2024 being attributed to cyclical factors. Additionally, we observe a positive contribution of the structural component to the change in the CAB over the last two years (2023-24), implying that the fundamental characteristics and competitiveness of the Greek economy have gradually improved, affecting economic growth and current account balances.

Our findings have significant policy implications. First, maintaining fiscal prudency so as to continue achieving fiscal primary surpluses could be beneficial for the continued improvement of the structural component of

the current account balance. Second, accelerating structural reforms to boost productivity and strengthen the competitiveness and export orientation of Greek businesses can also underpin the narrowing of the persistent current account deficit in Greece. Third, improving productivity and investment in capital goods and reducing dependence on imports, through the gradual substitution of imported goods with domestically produced goods, should contribute to reducing the sensitivity of the current account balance to short-term (cyclical) fluctuations. Finally, preventing increases in labour costs could contribute to partially offsetting short-term pressures on external balances.

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