

Box 1 DEVELOPMENTS IN COLOMBIA'S BALANCE OF NON-FACTOR SERVICES

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The external balance of non-factor services is a component of the balance of payments that does not receive a great deal of attention from market analysts. However, developments in the accounts that make up this balance, and the relative importance they have gained in recent years when it comes to prospects for adjusting the external imbalance in the Colombian economy, justify analyzing them in more detail.

The balance of services records the difference between what the Colombian economy earns and spends on this item with the rest of the world. Twelve cross-border activities are classified in this category. They include the services provided through different means of transport (air, maritime and others) in conjunction with foreign trade (freight) and travel services (passengers); transactions derived from the provision of travel services, such as accommodation, food and recreation, among others; business services (technical assistance, administrative services, customer service, etc.); and financial services, insurance and pensions, among others.¹

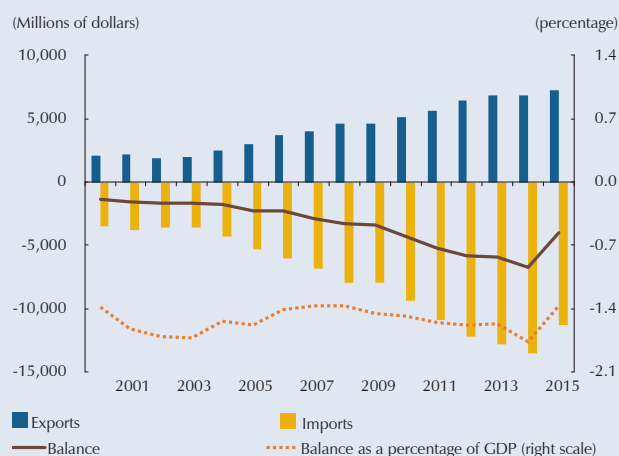
1. 2000-2014 Period

During the last decade, Colombia registered a growing deficit in dollars in its balance of non-factor services (Graph B1.1). In 2004, this deficit came to USD 1,798 b as a result of USD 2.453 b in revenue from exports of services and USD 4.251 b in expenditure on imported services. A decade later, by the end of 2014, the deficit in the balance of services had increased to USD 6.682 b, when revenue came to USD 6.876 b as opposed to USD 13.558 b in expenditure. In both cases, these amounts were triple what they had been a decade earlier. During this same period, the balance of services

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1 See “Balanza de pagos de Colombia. Metodología y fuentes de información”. Available in www.banrep.gov.co/economia/pli/Metodologia_Balanza_Pagos.pdf

Graph B1.1
Annual Balance of Non-factor Services (2000-2015)

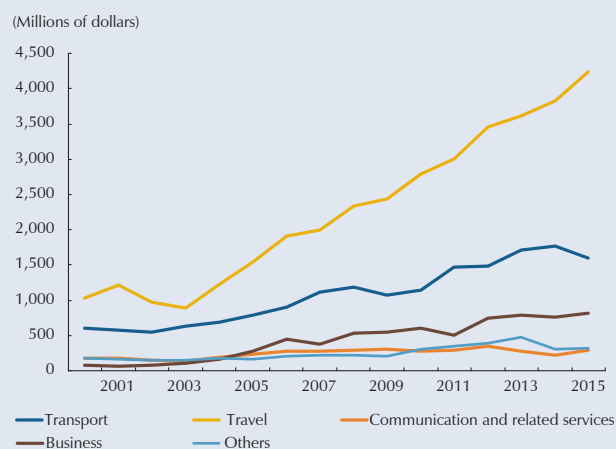


Source: Banco de la República.

as a portion of GDP did not change substantially and fluctuated at around 1.5%.

The way trade in services performed during the last decade is explained by several phenomena, which are described in this section. As for income, the largest increases were in the area of travel services. This item includes sales of tourist and business services in Colombia to non-residents (other than tickets for transportation) (Graph B1.2). The value of these exports averaged around USD 1 b in the early years of the previous decade, reaching USD 3.825 b by the end of 2014. This amounts to more than 12.0%

Graph B1.2
Annual Exports by Type of Services (2000-2015)



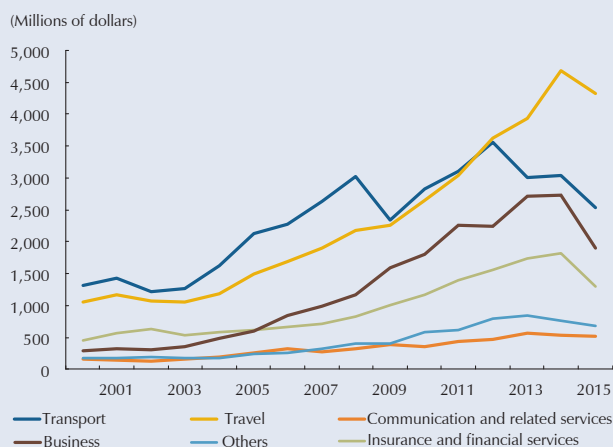
Source: Banco de la República.

average annual growth during the last decade. A portion of this performance is explained by aspects such as the significant improvement in the perception of security in Colombia during that period, which stimulated a larger influx of tourists, business people and investors, and the migratory wave of the late nineties, which led a significant number of Colombians to settle abroad and then visit the country as non-residents.

Another highlight is the evolution of revenue from transport services and other business services. The respective average annual increases in these services during the last decade came to 10.4% and 19.8% at the close of 2014. In the case of transport, this development is linked closely to the performance of travel services (as described above), which bolstered revenue from air transport passenger services. At the same time, business services were propelled, in part, by the increase in demand for consulting services (mainly tax and legal) on the part of non-resident users who were attracted by business opportunities in the country.

In the group of imports, the most significant increases were also in foreign purchases of travel services, transportation and business services (Graph B1.3). In the first case, the outlays for these services went from slightly over USD 1 b in 2004 to USD 4.678 b at the end of 2014. This rise was associated mainly with the effect of appreciation on the peso value of tourist packages purchased by Colombians abroad. In other words, the wealth effect that caused Colombian income to appreciate in dollars (32.7% cumulative appreciation between 2004 and 2014) made foreign destinations more attractive and boosted these imports as a result. Added to this was the expansionary phase of the economic cycle (4.8% average annual growth between 2004 and 2014); coupled with the

Graph B1.3
Annual Imports by Type of Services (2000-2015)



Source: Banco de la República.

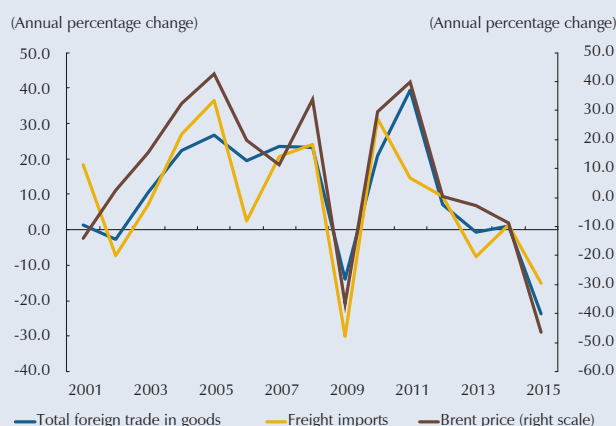
effect of appreciation, it stimulated Colombian purchases of tourism services and business travel abroad.

Transport services were bolstered not only by the performance of foreign trade in the last decade, which raised the demand for freight services, but also by the increase in purchases of air passenger transport services associated with the travel services phenomenon mentioned earlier. The rising cost of transport services was another element, linked closely to the price of oil, which meant the value of these services rose during the boom in oil prices. All these factors combined led to 7.6 % annual average growth in transport services between 2005 and 2014 (Graph B1.4).

In the case of business services, foreign purchases increased at an average annual rate of 19.6% during the period in question, going from nearly USD 600 m in 2005 to USD 2.725 b by the end of 2014. This performance was associated with the rise in demand for imported technical services to develop oil and mining activities, amidst the mining-energy boom in the Colombian economy during that time. The demand for management consulting services increased as well (accounting, tax and legal services, mainly) and stemmed from companies with foreign direct investment (FDI) that have come to Colombia. Colombian branches of an important number of companies belonging to major multinational groups carry out consulting contracts they establish with their parent companies abroad, generating an outflow for such services in Colombia.

The other factors that boosted imported services in the last decade deal with rising expenses for the use of intellectual and industrial property, and royalties for the use of brands. This expansion is associated with the rise in FDI registered during the period, as well as the increase foreign payments for insurance, specifically in

Graph B1.4
Freight Imports, Foreign Trade and Oil Prices



Source: Bloomberg, DANE and Banco de la República

terms of reinsurance for the large investments made in Colombia during the economic boom.

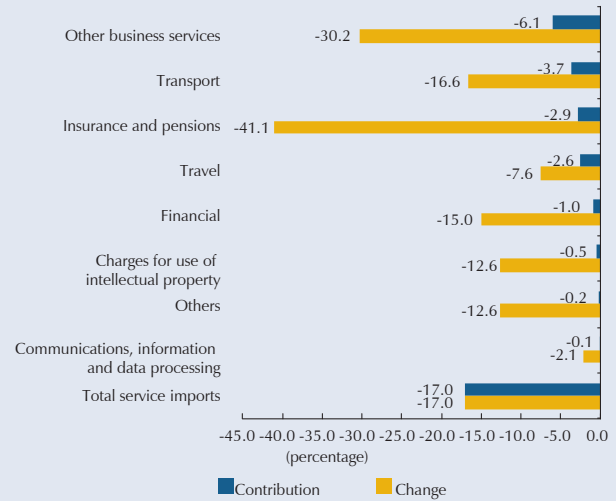
2. The Outcome in 2015 and Forecasts for 2016

Most of the factors that explain the evolution in the country's external balance of services during the last decade have reversed as of late 2014, thereby changing the trend in the services deficit observed since 2004. The sharp drop in prices for oil and other commodities, as of mid-2014, and the impact this had on variables such as the exchange rate, foreign trade, economic growth and investment, had an important effect, mainly on imported services and, to a lesser extent, on exports. As a result, the deficit in the balance of services fell by USD 2.701 b between 2014 and 2015. This is explained by 5.7% annual growth of exports (USD 390 m) and, above all, by an annual contraction of 17.0% in imports (USD 2.312 b).

Given their share, the services that contributed the most to the drop in imports were those related to business (-30.2%), transport (-16.6%) and travel (-7.6%) (Graph B1.5). On the export side (Graph B1.6), the major contribution came from foreign sales of travel services (11.0% annually). Exports of other services, such as those associated with business and communications, also grew during 2015, but made a smaller contribution. Given the 33.0% annual decline in exports of goods over the last year and the growth in exports of services, the latter increased from less than 11.0% of total exports in 2014 to 16.0% by the end of 2015, raising the relative importance of this source of foreign exchange for the country.

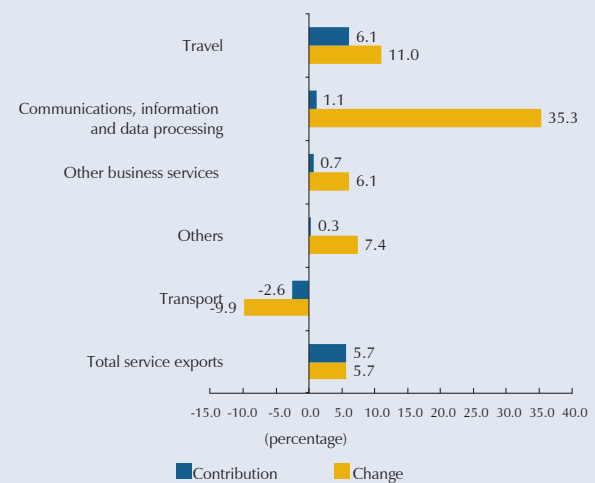
In the central scenario for the balance of payments outlined in Chapter I of this report, the deficit is expected to continue to decline during 2016 and possibly in the years thereafter. This would be due to the delayed effect depreciation can have on decisions regarding consumption, particularly those related to tourism services. Also, the improvements in Colombia's external competitiveness, due to the adjustment in relative prices, build interest in investment in sectors with good potential for being service exporters, which means an increase in revenue associated with these sectors. This is particularly relevant, not only in activities related to tourism, but also in those associated with other business services, such as health and customer service platforms.

Graph B1.5
Performance of Service Imports in 2015



Source: Banco de la República.

Graph B1.6
Performance of Service Exports in 2015



Source: Banco de la República.