Beginners:Balance of payments

Statistics Explained

The balance of payments provide information on the exchanges among the different economies and records the accounts of traded goods and services, as well as the different financial transactions related to these exchanges. Why is this information important? Governments, financial institutions, international and European organisations rely on these data to make decisions and draft their policies.

This article is part of Statistics 4 beginners , a section in Statistics Explained where indicators and concepts are explained in a simple way to make the world of statistics a bit easier for pupils and students as well as for everyone else with an interest in this topic.

What is the balance of payments?

The **balance of payments** is a transactions statement commonly known by the abbreviation BoP.

It shows transactions between an economy (strictly speaking **residents** within an economy) and the rest of the world (residents in the rest of the world) during a specified period of time, in other words, international transactions. The economy for which the BoP data are compiled is called the*reporting economy* .

Balance of payments are organised into three types of accounts — **current** , **capital** and **financial** — all of which are explained below. In the BoP, the three accounts show the value of international transactions made during a period of time (such as during a month, a quarter or a year).

In its most basic form, the BoP data look at transactions with the rest of the world. However, a more detailed analysis can be made with individual countries or groups of countries. Collectively, these are referred to as '*partners* '.

For example, from the perspective of the **European Union (EU)** as a reporting economy, the partners might be other major national economies (such as the United States), other trading blocs (such as **ASEAN**), major financial centres (such as Hong Kong or other **offshore financial centres**), or simply the 'rest of the world'.

The accounts also provide information on the type of participants in the transactions: who are the residents from the reporting economy that are participating in the transaction and who from the rest of the world. The participants are organised into **institutional sectors** .

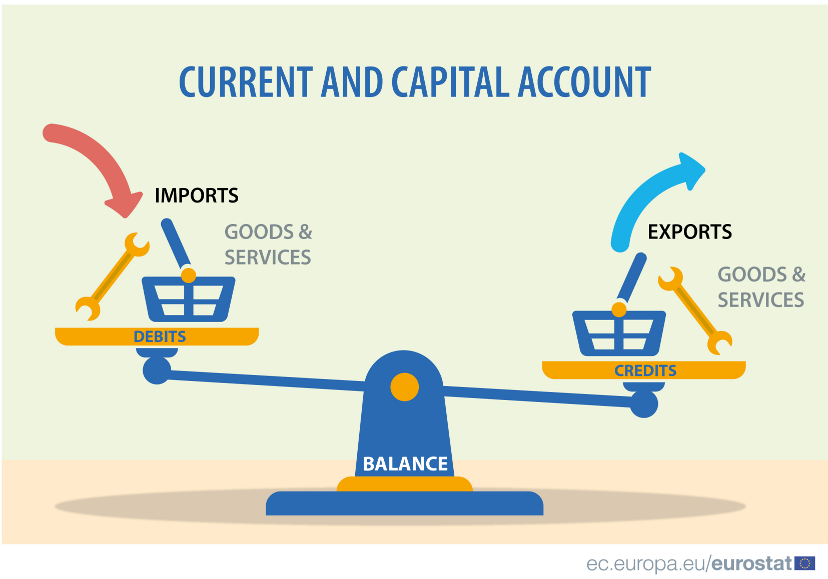
For BoP data, the types of participants of particular interest are: i) various types of **non-financial corporations** ; ii) **general government** ; and iii) the **rest of the economy** and iv/ households and non-profit institutions serving households. These sectors are described in more detail later.

Would you like to know more about BoP, about the different kinds of accounts, and for what these data can be used?

If so, read on!

What are the flows and the accounts?

For the current and the capital account, the flows during the year are called **credits** and **debits** , with the difference between these (credits minus debits) being the **balance** . A credit is recorded when goods or services flow out of an economy (so this is similar to an **export**) and a debit is recorded when goods or services flow into an economy (so this is similar to an **import**).



For the financial account, the flows are **assets** and **liabilities** , with the difference between these (the value of assets minus the value of liabilities) being the **net value** . An asset is acquired when there is a financial flow out of the economy (such as investment abroad) and a liability is acquired when there is a financial flow into the economy (investment in the reporting economy).

Recording of assets and liabilities

Somewhat confusingly, the term 'net' is used not only as the difference between assets and liabilities but also to describe the method of*recording* the assets and liabilities themselves. These are recorded as the net acquisition of assets and the net incurrence of liabilities. The net acquisition of assets and/or the net acquisition of liabilities in a given time period can be negative in value, if disposals exceed acquisitions.

How are the accounts related?

The combined balance of the current and capital accounts records the exposure of an economy to the rest of the world, whereas the financial account explains how this balance is financed. The net financial account is interpreted as **net lending** to the rest of the world when positive, and **net borrowing** from the rest of the world when negative.

Ideally (from a statistical perspective), the combined balance of the current and capital accounts should equal the net value of the financial account. If this does not happen, then the difference is recorded as the net value of errors and omissions.

Do you want to know more about what is actually in these accounts? At a more detailed level, each account is made up of many items. These are described in the next section.

What are the detailed items within the accounts?

Current account

The current account of the balance of payments provides information on:

- international trade in goods (traditionally the largest category);
- international trade in services;
- primary income;
- secondary income.

As explained above, for all current account items a credit and a debit are recorded, as well as a balance. A positive current account balance shows that an economy is earning more from its international export transactions than its spending abroad from import transactions with other economies. It is therefore a net creditor (net exporter) towards the rest of the world.

Exports and imports of goods (international trade in goods) includes (among others):

- general merchandise trade (regular exporting and importing of goods);
- exports and imports of goods under merchanting (buying and reselling goods without the good entering the economy).

The balance for trade in goods is known as the **trade balance** (or the balance of trade). If exports exceed imports, there is a positive trade balance; if imports are higher, there is a negative trade balance.

International trade in services consists of the following items:

- manufacturing services performed on physical inputs owned by others (goods for processing); this occurs when unfinished goods are provided by one unit to another unit to process further, and then returned to the original unit or passed to another unit, without a change in ownership of the goods;
- maintenance and repair services;
- transport services (broken down by mode of transport and between freight and passenger transport);
- travel, which mainly includes the goods and services travellers acquire when abroad;
- other services

- construction services,
    - insurance and pension services,
    - financial services,
    - charges for the use of intellectual property (like copyrights) not included elsewhere,
    - telecommunications, computer and information services,
    - other business services (research and development services, professional and management consulting services, technical, trade-related, and other business services),
    - personal, cultural and recreational services,

- government services not included elsewhere;
- services not allocated.

Primary income covers international transactions for:

- the compensation of employees (such as wages and salaries) paid to non-resident workers or received from non-resident employers;
- investment income from direct, portfolio and other investments and from reserve assets; this includes income received as well as reinvested earnings;
- other primary income

- taxes on production,
  - taxes on imports, subsidies and rent.

Secondary income includes current international transfers. Transfers are payments (for which no good or service is provided directly in return). These include international transactions for:

- current taxes on income and wealth;
- social contributions and benefits;
- non-life insurance premiums and claims;
- transfers related to international cooperation;
- miscellaneous current transfers, such as personal transfers and transfers to non-profit institutions serving households (such as charities).

Capital account

The capital account of the balance of payments provides information on:

- the international acquisition of non-produced non-financial assets, for example investment in land or intangible assets (like copyrights);
- capital transfers, including capital taxes, investment grants and debt forgiveness.

Financial account

The financial account is made up of five components (of which the first three are investments):

- direct investment (also known as foreign direct investment (FDI)), where the investor gains control or a significant degree of influence on the management of a (non-resident) company;
- portfolio investment, where the investor cannot exercise significant influence over the (non-resident) companies in which they invest;
- other investment, including for example loans or trade credit;
- financial derivatives other than reserves and employee stock options

- financial instruments linked to other specific financial instruments, indicators or commodities and through which risks can be traded in financial markets,
  - employee stock options, which are options to buy the equity (shares) of a company, offered to employees of the company as a form of remuneration;

- reserve assets (such as monetary gold or currency).

Where do remittances fit in?

Remittances represent an important source of external funding for households, in particular in developing countries. In the BoP data, international remittances are classified as primary income, secondary income or as capital transfers. Remittances cover:

- compensation of (international) employees (of border, seasonal and other short-term workers, who work in an economy where they are not resident);
- acquired rights in social benefits (current transfers received as benefits from employment in another economy — for example, receiving a pension);
- personal current transfers (not just of international workers, but all personal current transfers between households);
- personal capital transfers (when assets are transferred internationally between households);
- current and capital transfers (such as private and public bilateral aid programmes) to non-profit organisations.

For which partners are data available?

In theory, like for international trade , BoP data can be compiled for transactions between a particular economy (the reporting economy) and every individual country in the rest of the world (the partner economies).

In practice, in terms of reporting economies Eurostat publishes data for the **EU-27** , the **euro area** , each of the individual **EU Member States** and some non-member countries (such as **EFTA** and **enlargement** countries).

For partners, Eurostat publishes data for three large aggregates:

- the rest of the world (in other words, all countries of the world other than the reporting economy)

- **intra-EU** (or intra-euro area),
  - **extra-EU** (or extra-euro area).

Intra-EU means transactions with other EU Member States, while extra-EU means transactions with all countries of the world who are not members of the EU.

In addition, Eurostat publishes data for some individual countries as partners:

- each of the individual EU Member States;
- Argentina;
- Australia;
- Brazil;
- Canada;
- China except Hong Kong;
- Hong Kong;
- India;
- Indonesia;
- Japan;
- Mexico;
- Russia;
- Saudi Arabia;
- South Africa;
- South Korea;
- the United Kingdom;
- the United States.

Finally, Eurostat publishes data for one special grouping of countries as a partner:

- offshore financial centres (countries or jurisdictions that provide financial services to non-residents on a scale that is incommensurate with the size and the financing of its domestic economy; definition proposed by the International Monetary Fund).

What are the sectors?

While many analyses of BoP data focus on the items and the partners, the data published by Eurostat also provide an analysis of the type of participants in international transactions. These distinguish both sides of a transaction, such as who is acquiring an asset and who is disposing of it.

The list below indicates the relatively detailed list of financial corporations, as well as general government and an aggregate of all other institutional sectors.

- Total economy
- Financial corporations
- Central banks
- Monetary financial institutions (MFIs) other than central banks
- Deposit taking corporations other than the central bank
- Money market funds
- Financial corporations other than monetary financial institutions, such as insurance corporations and pension funds
- General government
- Non-financial corporations, households and non-profit institutions serving households
- Other sectors

Who are the main users of BoP?

BoP statistics form the only available accounting framework which measures all types of international economic transactions.

The data they provide may be used to study the international exposure of different parts of an economy, indicating comparative advantages and disadvantages with the rest of the world.

These data have traditionally been a fundamental macroeconomic tool for a wide range of users, such as governments, international organisations, financial and non-financial enterprises and researchers. These statistics are used by the **European Central Bank** for monetary policy, by the **European Commission** for economic policy and trade negotiations, and by national governments for analyses of various kinds.

What are the methods and sources?

International methodological guidelines

Compiling and disseminating consistent and timely balance of payments is possible only by using internationally agreed methodological standards. The main methodological reference used for the production of balance of payment statistics is the sixth edition of the International Monetary Fund's (IMF's) Balance of Payments and International Investment Position Manual (BPM6) (click here for a link to the PDF). BPM6 was released in 2009 and in 2014 a compilation guide was released to assist compilers further. BPM6 is being reviewed and the release of BPM7 is targeted for March 2025.

The main sources of data

Each country compiles its BoP data from a combination of surveys and administrative sources. Methods used to collect and compile statistics differ from one item to another within a country and from one country to another.

Data for*goods* are generally based on international trade in goods statistics , which are often collected by customs administrations. Data for*services* come from a variety of surveys, with data reported either by banks or directly by enterprises or households. Data for*primary income* are generally estimated using information from the banking sector and other financial institutions. Data for *secondary income* generally come from administrative sources. Data for the *financial account* generally come from banks and from other financial and non-financial institutions.

Frequency / time coverage, timeliness and presentation of data

Eurostat publishes monthly, quarterly and annual BoP data. The most detailed data, with the largest number of items and the largest number of partners, are published annually, while less detailed data are available on a monthly and quarterly basis.

In terms of timeliness, the first estimates of annual data are normally available in April of the year following the year to which they refer. For example, in April 2020 the first estimates for 2019 were released.

Data are presented in national currencies and in euros.

What makes BoP difficult to compile?

Increased globalisation of production and distribution has brought new challenges to the compilation of high-quality balance of payments data. The lifting of foreign exchange restrictions, the increasing number and complexity of cross-border financial transactions, and the integrated management of payments made by multinational firms have produced more and more complex flows, making it particularly difficult to compile the financial account and the related investment income.

For instance, an increasing number of individuals and businesses have connections to two or more economies, and economies themselves are increasingly involved in economic arrangements, which makes it harder to determine accurately the related financial flows.

In addition, more and more often, complex, multi-economy corporate structures have built special legal structures that are used to hold assets but with little or no physical presence in an economy. This phenomenon often makes it challenging to establish the residence of the owners of goods, services and assets.

And as globalised production processes have become more important, there is a need to retrace every step of the production process, to provide a fuller and more coherent picture of outsourced processes (in other words, goods sent abroad for processing), as well as sales and management of manufacturing that do not involve physical possession (in other words, merchanting).

Eventually, financial innovation led to the emergence and growth of new financial instruments and arrangements among different institutions. An example of this are financial derivatives, which are financial packages linked to other financial packages, indicators or commodities and tools to trade risk over the financial market.

Can BoP statistics be compared with other statistics?

Many types of statistics have links to BoP data or appear to overlap in some way. Two are mentioned below.

National accounts

The introduction of the **European System of Accounts 2010 (ESA2010)** and the sixth edition of the BPM contributed to the harmonisation of methodological standards among the EU Member States. Consequently, since 2014, National accounts have been increasingly comparable and consistent.

Discrepancies can still occur, for example from using different data sources in compilation, through a lack of coordination, or resulting from different interpretations of (harmonised) methodological standards. The more complex the item, the greater is the possibility of discrepancies. However, some countries may be more subject to discrepancies than others. Nonetheless, Eurostat systematically analyses these inconsistencies to improve the quality of data.

International trade in goods

Like BoP statistics, international trade statistics cover an economy's exports and imports of goods and services. Whereas BoP data are based on the BPM6, the compilation of statistics on the trade in goods is based on the United Nations manual of International Merchandise Trade Statistics (IMTS 2010).

For the BPM6, the fundamental principles for international transactions are residence and change of ownership. In other words, the change of ownership between a resident and a non-resident is the major prerequisite of recording a transaction.

The IMTS 2010 methodology is based on physical movements as a sufficient criterion to record cross-border transactions in goods, although the change of ownership criterion is recommended in exceptional cases. Furthermore, this methodology records an international transaction at the time point when the goods enter or leave an economic territory, rather than when ownership changes.

In a standard trade situation, the physical movement of goods could be related to a change of economic ownership, but the two events may occur at different times. These differences between BPM6 and IMTS 2010 can lead to differences in the data, and they can arise from transactions in goods that:

- do not physically cross borders of the reporting economy, despite a change in economic ownership;
- do not involve a change of economic ownership, but are transported across the reporting economy's borders.

A further difference is how exports and imports are valued. While the cost (value) of the underlying goods being transported may be the same for BoP and statistics on trade in goods, related costs, such as transport and insurance charges are treated differently in these two statistics. This impacts the overall value of imports.

What is the legal basis for BoP statistics?

The transmission of balance of payments data to Eurostat is covered by Regulation (EC) No 184/2005 on Community statistics concerning balance of payments, international trade in services and foreign direct investment. New data requirements according to BPM6 are included in Commission Regulation (EU) No 555/2012 and Commission Regulation (EU) No 1013/2016 as amendments to the above.

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Other articles

Related articles in Statistics 4 beginners :

- International trade in goods

Related articles in Statistics Explained :

- All articles on balance of payments

Glossary items in Statistics Explained :

- Balance of payments
- Residents
- Current account
- Capital account
- Financial account
- European Union (EU)

- ASEAN
- Offshore financial centres
- Institutional sectors
- Financial corporations
- General government
- Credits
- Debits
- Export
- Import
- Assets
- Liabilities
- Trade balance
- Remittances
- Compensation of (international) employees
- Non-profit organisations
- EU-27
- Euro area
- EU Member States
- EFTA
- Enlargement countries
- Intra-EU
- Extra EU
- Institutions and bodies of the EU
- Non-financial corporations
- Households
- Non-profit institutions serving households
- European Central Bank
- European Commission
- Enterprises
- European System of Accounts 2010 (ESA2010)
- Eurostat
- United Nations