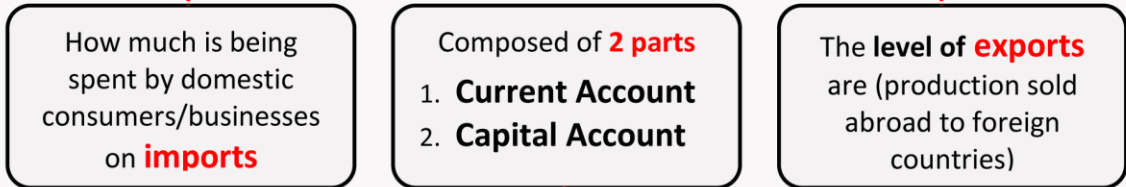


31. The Balance of Payments

The Balance of Payments (BOP) is a record of all the financial transactions that are made between all those active in the domestic economy (consumers, businesses and the government) and the rest of the world

Includes



CURRENT ACCOUNT

All flows of money received from the purchase of goods/services

$$\text{Visible Balance (of Trade)} = \text{Exports (Goods)} - \text{Imports (Goods)}$$

$$\text{Invisible Balance} = \text{Exports (Services)} - \text{Imports (Services)}$$

Exports (Services)

Examples

- Earnings of domestic airlines from foreign passengers
- Earnings of domestic hotels from foreign guests
- Earnings of domestic singers/bands from abroad
- Subsidies received domestically from the EU
- Earnings of Irish consultancies from foreign clients

Imports (Services)

Examples

- Your own citizens using foreign airlines
- Spending by your own citizens on holidays abroad
- Payments by your own citizens to foreign companies
- Earnings of foreign artists in your country
- Taxes pay by your country to the EU
- All interest pay on debt owed to those abroad

Net Investment Income

Interest payments, profits and dividends from external assets owned by nationals but sited abroad

Current Transfers

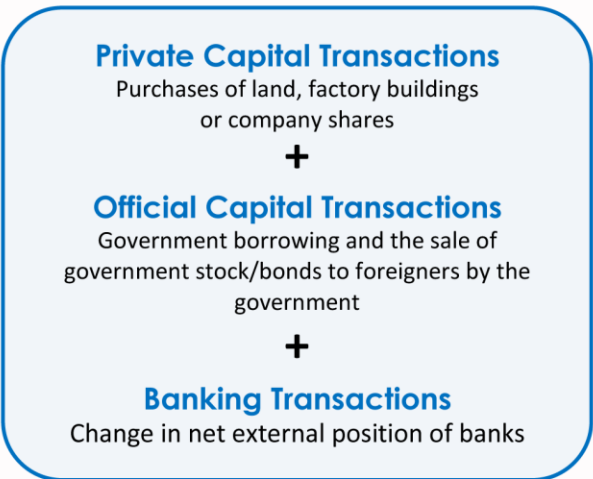
Private transfers between countries and government transfers (to EU, UN and other international bodies)

= Net Balance on **Current Account**

$$\text{Visible Balance} + \text{Invisible Balance} + \text{Net Investment Income} + \text{Current Transfers}$$

CAPITAL ACCOUNT

All flows associated with 'capital' items i.e. private capital, official capital and banking



$$= \text{Total Capital Transactions}$$

$$\text{Net Balance on Current Account} + \text{Total Capital Transactions}$$

$$= \text{BOP on Capital/Current Account}$$

Balance of Payments Explained		
Current Account (in €m)		
Visible Trade	Export of Goods	20,000
	Imports of Goods	45,000
Balance of Trade		<u>-25,000</u>
Invisible Trade	Export of Services	18,000
	Imports of Services	8,000
		<u>-10,000</u>
Net Balance on Current Account		-15,000
Capital Account (in €m)		
Private Capital		-10,000
Official Capital		+15,000
Banking Transactions		+2,000
		<u>+7,000</u>
Balance of Payments on Capital Account		-8,050

Visible trade deficit

Invisible trade deficit

BOP Deficit
Net capital outflow

The country isn't paying it way with other countries

Why is there a BOP (Trade) Deficit?

SHORT TERM FACTORS

1. **Booming home economy** means high consumer demand which can't be satisfied by domestic production. Imports grow
2. **Strong exchange rate** reduces prices of imports, switching consumer spending away from domestic production (cheaper to import)
3. **Global economic weakness** damages export growth

MEDIUM/LONG TERM FACTORS

1. **Structural problems** in the economy (long term decline of once strong exporting sectors i.e. deindustrialisation and the growth of more competitive and footloose services)
2. **Decline in comparative advantage** in the international economy
3. Low level of **capital investment**
4. **Productivity/Competitiveness problems**

Many economies in Western Europe are shifting toward **INVISIBLE** exports (services) rather than **VISIBLE** exports (goods)

- Economies are exposed to increased competition in services
- This exposes them more to investor confidence (fluctuates)
- Employment shifts to service based (most 'developed' economies = 70%)