

# Lecture 2

- What is balance of payments (BOP)?
  - ◆ Informal: a country's cash ins/outs in a year
  - ◆ Formal:
    - To systematically record the money values of all economic transactions between a nation's **own residents** and residents in the ROW during a specific time period, usually a year.
- Categorizing balance of payments
  - ◆ Type: goods & services, financial assets
  - ◆ Direction: import/export, inflow/outflow
  - ◆ Time: short-term/long-term
  - ◆ Holder: private/official

## Item Classification (1)

- Current Account (Category I):
  - ◆ Balance of Trade (BOT) or Merchandise Trade Balance (MTB):  
$$\text{BOT} = (X - M)_{\text{goods}}$$
  - ◆ Balance on Goods & Services:  
$$\text{BTGS} = \text{BOT}_{\text{goods}} + \text{BOT}_{\text{services}}$$
  - ◆ Balance on Goods, Services & Investment Income:  
$$\text{BOT}_{\text{goods}} + \text{BOT}_{\text{services}} + \text{Net investment income receipts}$$
  - ◆ Current Account (Table 5):  
$$\text{C/A} = \text{BOT}_{\text{goods}} + \text{BOT}_{\text{services}} + \text{Net investment income receipts} + \text{Net transfers received}$$

## Item Classification (2)

- Capital Account (Category II to IV):
  - ◆ Direct investment and other long-term capital flows (II):  
Examples: FDI, government bonds
  - ◆ Short-term nonofficial capital flows (III):  
Examples: check deposits and withdraws
  - ◆ Changes in reserve assets of central banks (IV):  
Role of central banks  
Examples: Fed buys/sells US\$
  - ◆ Capital Account:  
K/A = sum of category II to IV

## Balance of Payments Summary Statement

	Debit/Credit
I.	
Exports of goods	
Imports of goods	
Balance of trade	
Exports of services	
Imports of services	
Balance on goods and services	
Investment income receipts from abroad	
Investment income payments abroad	
Balance on goods, services, and investment income	
Unilateral transfers received	
Unilateral transfers made	
Balance on current account	
II.	
Net increase in foreign long-term private assets in US	
Net increase in long-term private assets abroad	
III.	
Net increase in foreign short-term private assets in US	
Net increase in short-term private assets abroad	
Official reserve transactions balance	
IV.	
Net increase in short-term official assets in US	
Net increase in official reserve assets or official assets abroad	
Balance on capital account	