Balance of Payments

Fourth quarter 2008

Statistiska centralbyrån Statistics Sweden

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Statistics Sweden
2009

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Foreword

The balance of payments have been compiled and published by Statistics Sweden behalf of Sweden's Riksbank since September 2007.

The balance of payments is a compilation of Sweden's real and financial transactions with the rest of the world, and can be divided into the current account, the capital account and the financial account.

This report includes the results of the fourth quarter of 2008.

Statistics Sweden February 2009

Lars Melin

Christina Ekblom

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Balance of payments

The balance of payments for the fourth quarter of 2008 produced a surplus in the current account of SEK 63.6 billion, a negative capital account and a deficit of SEK 21.4 billion in the financial account.

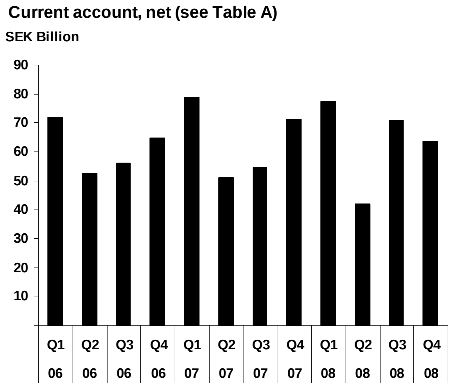
The final quarter of 2008 was marked by considerable turbulence on the financial market. The ongoing financial worry and economic decline has weakened the krona significantly. The balance of payments measures real and financial transactions with the rest of the world and is sharply affected by the exchange rate of the Swedish krona. The krona has become weaker against all of the currencies of Sweden's important trading partners, except the British pound.

Both imports and exports of goods were down during the fourth quarter due to the declining market. However, trade in services is still strong, with increased exports and imports compared to the previous quarter and the same period in 2007. Trade in services improved by SEK 8.7 billion in 2008 compared to 2007 and amounted to SEK 115.6 billion.

Direct investment show the large gross flows during the quarter, which among other things are due to increased internal corporate transactions. During the fourth quarter, direct investment generated a net outflow of SEK 48.2 billion.

Portfolio investments resulted in a net outflow of 170.9 SEK billion. Most of the large capital outflow came from trade in Swedish debt securities. Banks and housing finance institutions had difficulties with borrowing abroad, and this has resulted in huge outflows since the existing loans became due and were not able to be renewed. The weak exchange rate of the krona has a significant affect on the item of financial derivatives since a considerable amount consists of currency contracts. The net inflow during the quarter amounted to SEK 29.3 billion.

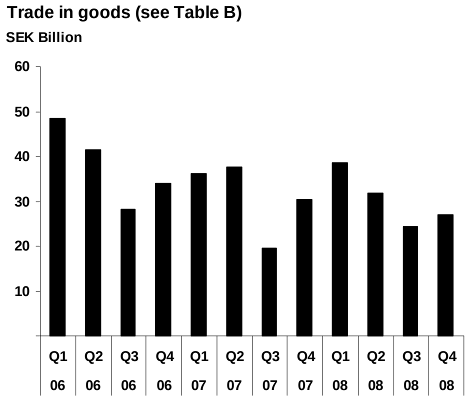
Current account



The current account generated a surplus of SEK 63.6 billion for the fourth quarter of 2008, which is SEK 7.3 billion less than the amount for the third quarter. This worsening is significant compared to the fourth quarter of 2007 when the current account resulted in a surplus of SEK 75.0 billion. Trade in goods is the main contributor to the decline, since a considerable downturn was seen during the quarter. However, trade in services continues to be strong and improved compared to both the previous quarter and the fourth quarter of 2007. The item *current transfers* showed a large deficit during the quarter, mainly as a result of payments for EU membership.

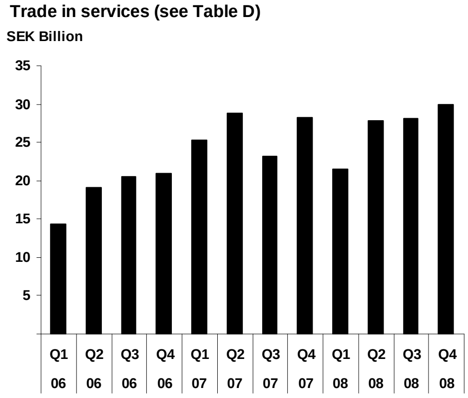
The current account for all of 2008 resulted in a surplus of SEK 263.5 billion, which can be compared to a surplus of SEK 264.0 billion in 2007.

Trade in goods



The financial crisis is reflected in trade in goods by a reduced international demand which hits Swedish exports. During the quarter the value of foreign trade of goods has fallen. Trade in goods for the fourth quarter amounted to SEK 26.9 billion, which is 3.9 billion less than the same quarter of 2007. The value of exports amounted to SEK 286.9, which is SEK 6.3 billion less than the previous quarter, and SEK 18.6 billion less than the fourth quarter of 2007. The drop in imports of goods is not as comprehensive, but is still large at SEK 8.9 billion less than the previous quarter and SEK 14.7 billion less than the fourth quarter of 2007.

Trade in services



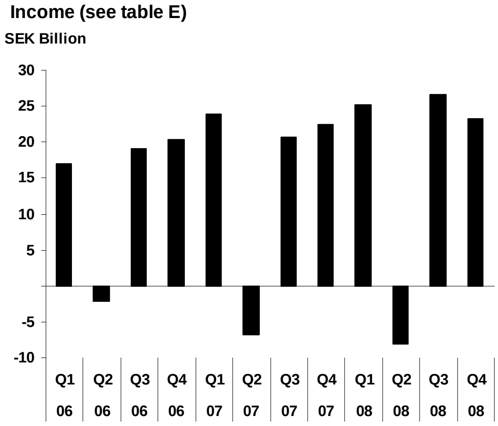
The trade in services for the fourth quarter of 2008 resulted in a surplus of SEK 29.9 billion, which is an improvement of nearly SEK 2 billion, compared to both the quarter before and the fourth quarter of 2007. Trade in services improved by SEK 8.7 billion in 2008, compared to 2007.

Total trade in services for the quarter amounted to SEK 127.5 billion. However, exports were SEK 10.0 billion higher than for the third quarter and even the same quarter of 2007. The item *other business services* is the main contributing factor to increased exports. Among other things, the item includes the sub-items *research and development* and *business and technical services.* Total imports of services rose by about SEK 8 billion, both compared to the previous quarter and the same quarter of 2007.

The item *transport* generated a net outflow of SEK 6.2 billion. Exports increased by SEK 0.3 billion compared to the same quarter of 2007, and imports increased by SEK 2.2 billion in the same comparison. The sub-item *sea transport* contributed the most to total exports and imports of transport.

The item *travel*, that includes goods and services used by travellers when travelling to other countries, generated a net outflow of SEK 3.5 billion, a considerably lower figure than the net outflow in the same quarter of 2007. Because of sharp seasonal variations for this item, comparisons are best made with the same period the year before. The inflow consists of consumption by foreign travellers in Sweden, and amounted to SEK 19.8 billion in the fourth quarter. The amount for the same quarter in 2007 was SEK 17.9 billion. At the same time, the outflow of travellers was down somewhat. That is to say, Swedes spent less on foreign travel. However, an increase of net outflow was noted for the entire year. In other words, expenses of Swedes abroad increased more than expenses for foreigners travelling to Sweden. The net outflow for all of 2008 was 4.9 billion higher than in 2007.

Income

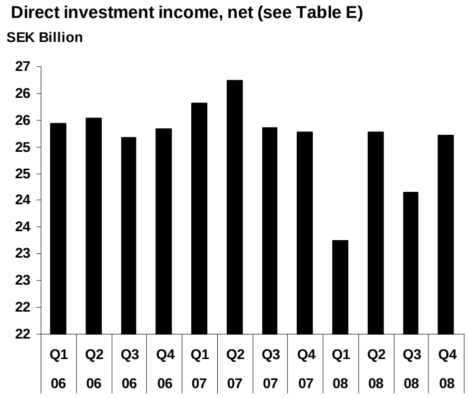


Income, consisting of salaries and capital income, showed a surplus of SEK 23.3 billion during the fourth quarter, which is SEK 3.3 billion lower than the quarter before. The item was SEK 2.6 billion less compared to the same period last year. Returns from direct investment resulted in a large net inflow and accounted for almost the entire surplus of this quarter. Returns from portfolio investments resulted in a net outflow of 2.0 SEK billion.

Returns on capital from other investment resulted in a net outflow of SEK 0.8 billion, which can be compared to a net outflow of SEK 0.5 billion in the previous quarter.

The item *compensation of employees* generated a net outflow of SEK 0.7 billion, in line with previous periods.

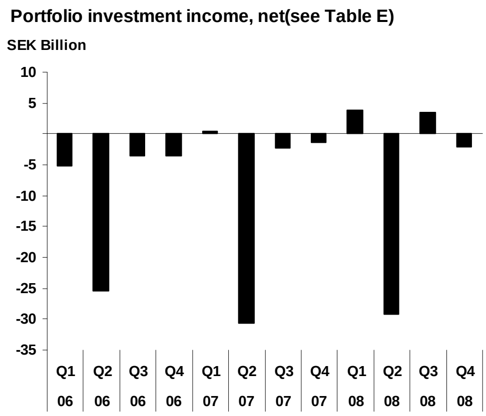
Returns on direct investment, net



Returns on direct investment showed large flows for the fourth quarter of 2008 and resulted in a net inflow of SEK 25.2 billion. Returns on direct investment abroad amounted to SEK 73.8 billion, while returns on corresponding foreign direct investment in Sweden totalled SEK 48.6 billion. The net flow of the dividends taken home was unusually large for the fourth quarter and amounted to SEK 35.8 billion. This indicates that Swedish parent company takes home more in dividends from foreign subsidiaries than the Swedish subsidiaries give to their foreign owners. Net flows of dividends for all of 2008 were considerably higher than the previous year.

Returns on direct investment are estimated for 2008. These estimations are made every year before the final values are available for companies who have a direct investment relationship.

Returns on portfolio investment, net



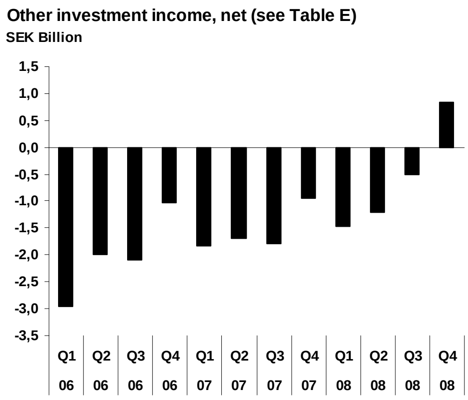
Returns on portfolio investments resulted in a capital outflow of SEK 2.0 billion net during the fourth quarter of 2008. This is a decrease of SEK 0.7 billion compared to the same period last year.

Interests from bonds and money market instruments accounted for most the outflow. Interest costs for foreign holdings of Swedish debt securities amounted to SEK 23.2 billion. The corresponding amount for the same period last year was SEK 20.3 billion.

Dividends on Swedish shares were insignificant during the year's last quarter, while dividends on foreign shares resulted in an inflow of SEK 8.0 billion.

Returns on foreign portfolio investments during all of 2008 increased to nearly SEK 20 billion compared to 2007. This is partly due to the weak krona during the year which has raised the value of foreign currency which is converted to Swedish kronor.

Returns on other investments, net

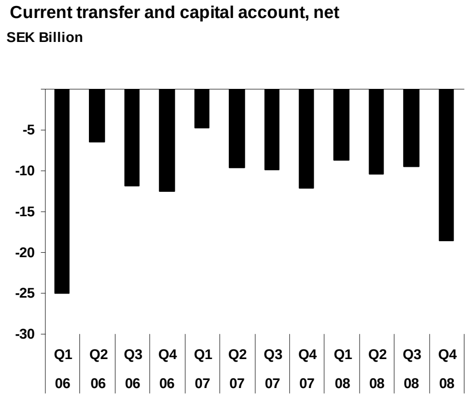


Returns on other capital produced a net inflow of SEK 0.8 billion during the fourth quarter of 2008. This post usually shows outflow, and the inflow for the fourth quarter is due to high returns on the Swedish reserve assets.

During the fourth quarter of 2008, returns on other capital abroad resulted in an inflow of SEK 22.4 billion, while other capital in Sweden resulted in an outflow of SEK 21.5 billion. During the entire year of 2008, returns on other capital abroad resulted in an inflow of SEK 74.7 billion, while other capital in Sweden resulted in an outflow of SEK 76.3 billion.

Returns from other capital consists of returns on loans and bank deposits etc. The largest contributions to this item come from Swedish banks' income on their assets and liabilities towards counterparts abroad.

Current transfers and capital account, net

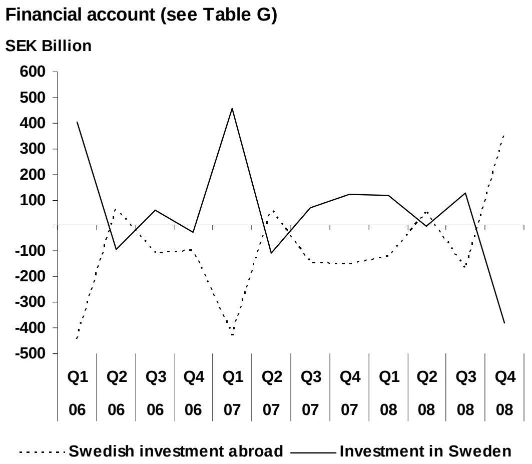


Current transfers and capital account produced a deficit of SEK 18.6 billion during the fourth quarter, which is SEK 9.1 less than the previous quarter. The deficit has increased by SEK 6.3 billion compared to the corresponding quarter of the year before.

EU transfers are the main contributing factors causing the high deficit, and equalled a deficit of SEK 8.3 billion. The corresponding figure for the same period in 2007 was SEK 4.3 billion. Transactions associated with EU membership make up SEK 10.2 billion in outflow, which is SEK 5.5 billion less than the quarter before. Foreign aid resulted in a net outflow of SEK 5.3 billion.

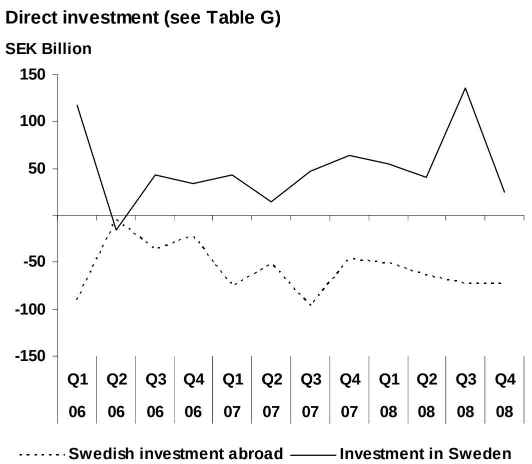
The item *other*, that is to say all other transfers that are not associated with the EU or foreign aid, resulted in a net outflow of SEK 5.0 billion, which is an increase in outflow of SEK 1.9 billion compared to the previous quarter.

Financial account



The financial account resulted in a net outflow of SEK 21.4 billion for the fourth quarter of 2008. Portfolio investments and other investments still account for the largest net flows. Portfolio investments resulted in a net outflow of SEK 170.9 billion while other investments resulted in a net inflow of SEK 111.2 billion. Direct investment also contribute SEK 48.2 billion to the net inflow. The reserve assets generated a net outflow of SEK 57.2 billion during the quarter.

Direct investment



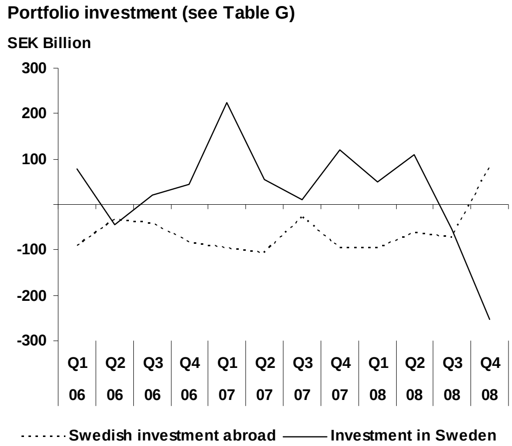
Similar to the previous quarter, direct investment of the fourth quarter showed large gross flows. The net outflow was SEK 48.2 billion, compared to the net inflow of SEK 18.4 for the same quarter of 2007. Among other things, the large flows are due to considerable re-structuring of multi-national companies which include Swedish companies.

Since the beginning of 2007 until the end of 2008, the flows of direct investment have nearly doubled. This phenomenon is seen for both direct investment in Sweden and Swedish direct investment abroad. This is partly due to increased internal transactions within companies.

Swedish direct investment abroad amounted to a net outflow of SEK 73.5 billion in the fourth quarter of 2008. Foreign direct investment in Sweden produced a net inflow of SEK 25.3 billion during the fourth quarter of 2008.

During the entire year of 2008 several large transactions have occurred regarding direct transactions in Sweden. Examples are the government sale of Vin&Sprit and the German Volkswagen's purchase of shares in Swedish Scania during the third quarter. During the first quarter, the American Nasdaq also purchased the Swedish OMX stock exchange.

Portfolio investment



Cross-border portfolio investments resulted in a net outflow of SEK 170.9 billion in the fourth quarter. This can be compared to the same period of 2007 that instead produced a net inflow of SEK 36.6 billion.

Most of the large capital inflow came from Swedish debt securities. Banks and housing finance institutions had considerable difficulties with borrowing abroad. This has resulted in large capital outflows because existing loans became due and these loans could not be renewed. In particular this concerns short-term loans. Swedish investors have re-purchased Swedish treasury bonds and mortgage-backed certificates from abroad. The total cross-border trade in Swedish debt securities gave rise to an outflow of SEK 92.0 billion during 2008. The total figure for this trade in 2007 resulted in a net inflow of SEK 408.5 billion.

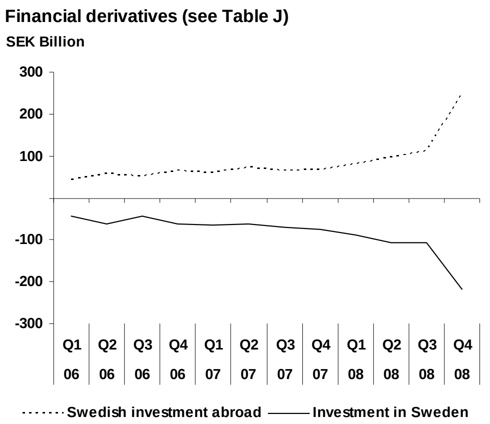
Swedish investors sold foreign debt securities for SEK 53.9 billion net during the fourth quarter of 2008. Despite sales during the fourth quarter, trade with foreign debt securities resulted in net purchases of SEK 117.5 billion for all of 2008. This is a significant decrease compared to 2007 when the total generated outflow amounted to SEK 280.9 billion.

The cross-border trade in shares generated a net inflow of SEK 23.6 billion in the fourth quarter. The capital inflow mainly arose from the sale of foreign shares. For the entire year of 2008 trade in shares had a net outflow of SEK 44.6 billion. Swedish shares accounted for SEK 9.8 billion and foreign shares for SEK 34.7 billion.

Portfolio investments for all of 2008 generated a net outflow of SEK 254.1 billion. The net inflow for all of 2007 was SEK 107.6 billion. Turbulent interest rate markets gave rise to large gross flows during 2008. Cross-border portfolio investments generated inflows during the first half of the year, which were compensated for by large net outflows during the second half of the year.

Revisions for the period 2007-2008 have been conducted for the item of portfolio investments since publishing the Balance of Payments for the third quarter, and have primarily concerned exchange rate corrections of reported basic data.

Financial derivatives

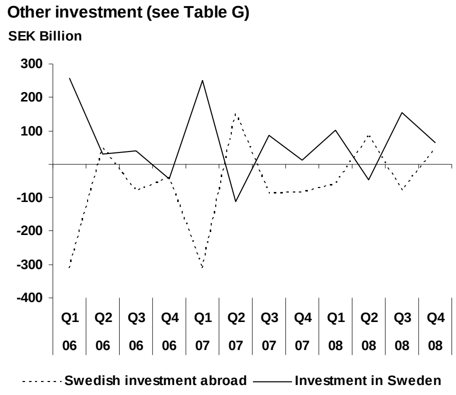


Transactions for financial derivatives for the fourth quarter of 2008 generated a net inflow of SEK 29.3 billion. This means that financial derivatives for all of 2008 have contributed SEK 15.6 billion to the net inflow of the balance of payments.

Never before in previous quarters has the net flow for transactions in financial derivatives been as significant as during the fourth quarter of 2008. This should be seen in light of the weak Swedish krona against the important currencies during the fourth quarter. A considerable portion of financial derivatives consists of currency contracts, involving increases in payment flows of realised contracts when currencies fluctuate.

Flows from financial derivatives arise through realised values from contracts which have become due, as well as through different types of premium payments. The financial instruments that derivatives are composed of are mainly options, futures and swaps. The largest volumes refer to different types of currency derivatives. Since most of the currency-related derivatives refer to currency hedging of loans and commercial flows from exports and imports etc., it can be assumed that the inflow from derivatives corresponds to the outflow of capital through trade of goods and loans that been become due.

Other investments

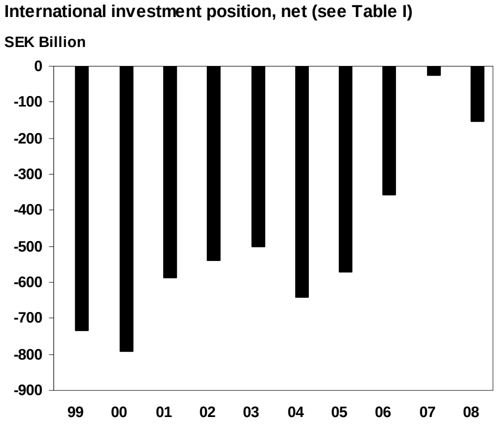


Other investments gave rise to a net inflow of SEK 111.2 billion during the fourth quarter of 2008. A net inflow of SEK 267.0 billion was recorded for all of 2008.

Other investments consist mainly of loans to and from abroad as well as a number of smaller financial items that are not covered by direct investment, portfolio investments or financial derivatives.

The value of investment in other investments varies considerably from one quarter to the next and it is usually short-term capital movements between banks in Sweden and counterparts abroad that have created these fluctuations.

International investment position, net



Swedish net liability to foreign countries increased by SEK 127 billion and amounted to SEK 153 billion during the year of 2008, according to preliminary figures.

Net assets in the form of direct investment have been forecasted at SEK 514 billion, which is a marginal increase compared to last year.

The largest contributing factor for development of the international investment position is the exchange rate of the krona. As mentioned earlier, the krona has weakened considerably in 2008. Other important factors are stock market prices in Sweden and abroad, as well as the market value of direct investment companies.

In 2008 assets and liabilities to other countries in derivative instruments rose considerably. At the beginning of the year and during the first three quarters, the balance values for contracts concerning both assets and liabilities were around SEK 200-250 billion. During the fourth quarter there was a sharp rise in balance values for derivative contracts. By the end of the year balance values for assets in derivative contracts, i.e. contracts with positive market values, amounted to SEK 556 billion. Balance values for liabilities, i.e. contracts with negative market values, amounted to SEK 497 billion.

Net liabilities for other investment and portfolio investments increased during the entire year of 2008. The reserve assets have increased by SEK 32 billion during 2008 and amounted to SEK 233 billion at the end of the year.

The official compilation of Sweden's international investment position was revised to reflect market value, with the exception of direct investment, which is reported at book value. A compilation of Sweden's international investment position is published as a complement, with calculations of the market value for direct investment. According to this compilation, Sweden's net liabilities abroad equalled SEK 283 billion in 2008.

It is important to note that several sub-items in the international investment position for June 2008, such as direct investment and portfolio shares, are forecasts. The figures should therefore be interpreted with caution.

What is the balance of payments?

The balance of payments has been produced and summarised by Statistics Sweden on commission for the Swedish Riksbank since September 2007.

In a closed economy the level of investment is determined by the total savings in the economy. This means that if the savings decline for some reason, investments will also decline. In an open economy the relationship between savings and investment is not as clear, as global financial markets enable international capital to flow easily between countries. The balance of payments contains information on these flows. Put in simple terms, it is a compilation of a country's real and financial transactions with the rest of the world.

The balance of payments can be divided into the following.

- Current accounts, including regular transactions in goods and services, return on financial assets and debts, and regular transfers such as EU subsidies and fees.
- The capital account, which covers EU subsidies and foreign aid for real investment as well as the purchase and sale of rights, such as patents.
- The financial account, which can be divided into direct investment, portfolio investment, financial derivatives, other investment and the reserve assets. The financial account shows changes in external financial assets and liabilities.

Derivation of the balance of payments

A country's gross domestic product, GDP_t, is the total value of the goods and services produced in the country during a certain year t. Production is used to satisfy either domestic demand in the form of households' consumption, C_t, private investment, I_t, and public expenditure, G_t, or to be delivered abroad in the form of exports of goods and services, X_t. Domestic demand can also be satisfied by the import of goods and services, M_t. The National Income Identity shows that a country's production during an individual year is equal to the sum of domestic demand ($C_t + I_t + G_t$) and net sales of goods and services to the rest of the world ($X_t - M_t$):

$$GDP_t = C_t + I_t + G_t + X_t - M_t.^{1} \qquad (1)$$

By adding together the net incomes, F_t, i.e. Swedish income earned abroad (Swedish wage-earners' remuneration abroad and earnings on foreign capital abroad) minus foreign income earned in Sweden (foreign wage-earners' remuneration in Sweden and earnings on foreign capital in

[1] This relationship is called an identity because it must by definition be fulfilled in every individual time period.

Sweden) it is possible to rewrite (1) in terms of gross national income, GNI_t:[2]

$$GNI_t = C_t + I_t + G_t + X_t - M_t + F_t. \quad (2)$$

Rewriting (2) gives:

$$GNI_t - C_t - G_t = S_t = I_t + X_t - M_t + F_t, \quad (3)$$

where S_t refers to the total national savings in the economy. The national savings consist of the consolidated public sector savings, $T_t - G_t$, where T_t is tax income, and households' savings, $GNI_t - T_t - C_t$.[3]

According to:

$$S_t - I_t = X_t - M_t + F_t. \quad (4)$$

The difference between S_t and I_t is often called net external investment and the difference between X_t and M_t is called trade in goods. $X_t - M_t + F_t$ is called the current account. Equation (4) thus shows that there is a simple connection between net investments and trade in goods. For a given net income, changes in the difference between S_t and I_t will always be followed by corresponding changes in the difference between X_t and M_t. Equation (4) also shows that it is not possible in the short term to reduce a deficit in the trade in goods without at the same time increasing national savings or reducing domestic investment.[4] It is also interesting to note that equation (4) means that if households' savings are as great as domestic investment, public sector savings will develop roughly in line with net exports over time.[5]

In the same way as national savings can be divided up into the consolidated public sector's savings and households' savings, domestic investments can be divided up into public sector investment and private investment. This division indicates that if the public sector's investment exceeds its savings, and if this is not completely counteracted by a savings surplus in the private sector, it must by definition be matched by a deficit on the current account. A growing deficit in the current account can thus be a sign among many that the central government's expenditure is greater than its income.

By combining the national income identity (1) with the national budget restriction, it is possible to derive the balance of payments. According to the budget restriction, the country's total expenditure in each time period is limited by the income in the same period and the country's possibilities to borrow:

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[2] These incomes are often called primary incomes. Net incomes consist of wages, capital earnings and current transfers.

[3] This means that the national savings are identical to the sum of the public sector savings and households' savings.

[4] Net incomes are assumed to be constant in the short term.

[5] This relationship means in actual fact that the public sector's budget balance will covary with trade in goods during certain periods of time.

$$GDP_t + r_t A_t = C_t + I_t + G_t + (A_{t+1} - A_t). \quad (6)$$

where A_t are the net external assets during period t and $r_t A_t$ is the interest earnings on these assets. The net assets in turn consist of the capital account and the financial account. It is simple to obtain the balance of payments from (1) and (6).

$$X_t - M_t + F_t = -(A_t - A_{t+1}). \quad (7)$$

The left side of the balance of payments (7) is, as mentioned earlier, the current account, which consists of the sum of trade in goods and net incomes. The term $(A_t - A_{t+1})$ on the right side shows how the net external assets change over time. Please note that if Swedes make net purchases of foreign assets, the capital account and the financial account will show a net deficit, i.e. $A_t - A_{t+1} < 0$. Equation (7) thus means that the sum of the current account, the capital account and the financial account is always identical to zero.[6]

The connection to the international investment position

As the financial account measures external net lending, a change in the current account will - by definition - always be matched by a similar change in the net external claims. A surplus on the current account is thus matched by an increase in external net claims - private or public sector. The surplus can also be reflected in an increase in the foreign currency reserve, as these transactions are included in the financial account. A deficit on the current account instead means that the net purchaser abroad must pay either by selling external assets or by increasing external liabilities.

This means that if, for instance, Sweden were to buy more assets abroad than are sold abroad (this is the same as saying that the net total of the financial account is less than zero), Sweden must at the same time sell more goods and service abroad than it buys from abroad. Put simply, the total outward payments from a country must correspond to the total inflow of payments.

The international investment position shows a country's total net debt and reports in the form of stock data on all domestic sector assets and liabilities abroad. The net total of assets and liabilities is thus a measure of a country's wealth relative to other countries. Stock data is reported at market value and can be divided up exactly like the financial account, into direct investment, portfolio investment, financial derivatives, other investment and the reserve assets.[7]

The relationship between the international investment position and the transactions in the balance of payments is illustrated below. Changes in the net external position are due to transactions that have been implemented and registered in the financial account and to changes in exchange rates

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[6] Because there are a number of sources for measuring the items in the balance of payments, there can arise measurement errors such as periodisation errors and thus there is included a residual in the form of an errors and omissions item.

[7] In certain cases the book value is used instead of the market value, because the base for calculating market value is insufficient.

and asset prices. In addition, the stocks can be affected by, for instance, write-downs of claims (an example of other corrections in the diagram). If the current account shows a deficit or surplus over a longer period of time, this entails a build-up of either a net liability or a net asset.

	Changes in the international investment position depending on				
Opening balance	Transactions	Price changes	Exchange rate changes	Other corrections	**Closing balance**