Balance of Payments

Second quarter 2010

Statistiska centralbyrån Statistics Sweden

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Statistics Sweden
2010

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Producer
Statistics Sweden, Balance of Payments and Financial Markets
Box 24300
SE-115 81 Stockholm
+46 8 506 940 00

Inquiries
Fredrik Öhrström, +46 8 506 941 12
fredrik.ohrstrom@scb.se

Lizette Appelberg, +46 8 506 944 04
lizette.appelberg@scb.se

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Foreword

The balance of payments has been compiled and summarised by Statistics Sweden on behalf of the Swedish 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.

The report comprises the results of the second quarter of 2010.

Statistics Sweden, September 2010

Folke Carlsson

Christina Ekblom

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Balance of payments

The balance of payments for the second quarter of 2010 resulted in a surplus in the current account of SEK 51.3 billion, and a deficit of SEK 74.3 billion in the financial account. As previously, the capital account gave a negative result.

The surplus in the current account was weakened during the quarter and amounted to SEK 51.3 billion. Foreign trade in goods and services amounted to SEK 53.8 billion, which is SEK 9 billion lower compared to the second quarter of 2009. However, the gross flows for trade in goods were considerably higher and are now at the same levels as at the end of 2008. Above all, the sharp recovery of imports of goods contributed to the lower net trade. Trade in services improved by SEK 6.3 billion compared to the same period the previous year, and amounted to SEK 32.1 billion.

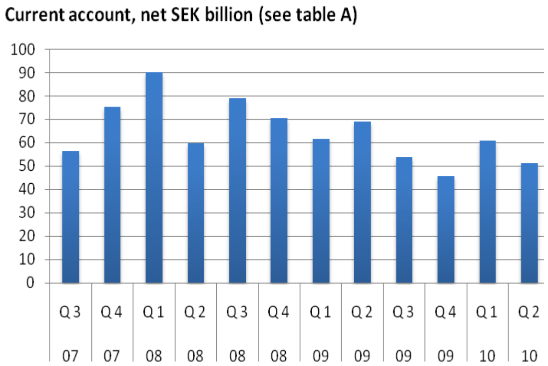
Income gave a net inflow of SEK 3.4 billion, of which income on direct investments accounted for a net inflow of SEK 22.9 billion while income on portfolio investments resulted in a net outflow of SEK 21.3 billion. Income on other investments resulted in a net inflow of SEK 2.2 billion.

The financial account resulted in a net outflow of SEK 74.3 billion. Other investments and portfolio investments again showed large net flows where other investments accounted for a net inflow of SEK 114.8 billion and portfolio investments in a net outflow of SEK 113.2 billion. Maturity and re-purchase of Swedish debt securities during the quarter caused the large net outflow for portfolio investments.

Direct investments generated a net outflow of SEK 20.4 billion. Swedish direct investments abroad resulted in a net outflow of SEK 34.9 billion, while foreign direct investments in Sweden resulted in a net inflow of SEK 14.5 billion.

Transactions in financial derivatives resulted in a net inflow of SEK 4.0 billion in the second quarter of 2010.

Current account

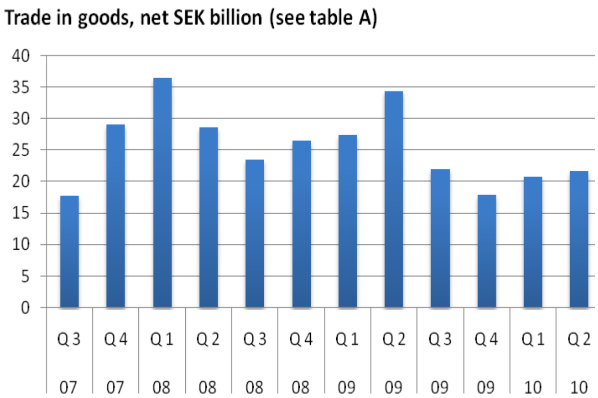


The current account resulted in a surplus of SEK 51.3 billion net for the second quarter. Compared to the same time period last year, this is a decrease by SEK 20 billion.

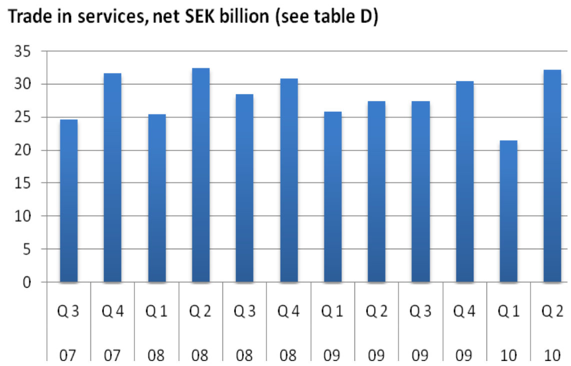
Foreign trade in goods and services

Trade in goods and services account for a significant part of the current account, and resulted in a capital inflow of SEK 53.8 billion net in the second quarter. Compared to the same quarters in 2009 and 2008, this is a decrease because trade in goods has weakened. However, trade in services amounted to SEK 32.1 billion, an improvement compared to previous periods.

Both exports and imports of goods continued to increase during the quarter, but resulted in a low net flow. Compared to the second quarter of 2009, exports and imports increased by 14 and 24 percent respectively. The stronger development for imports in this quarter also led to a relatively weak trade in goods. The increase of exports and imports was strongest in trade with EU countries.



Trade in services amounted to SEK 32.1 billion, which is higher than in previous periods. The increase is mainly from the items *other business services* and *computer and information services* as well as the item *travel* that contributed when exports increased compared to the same period in 2009.

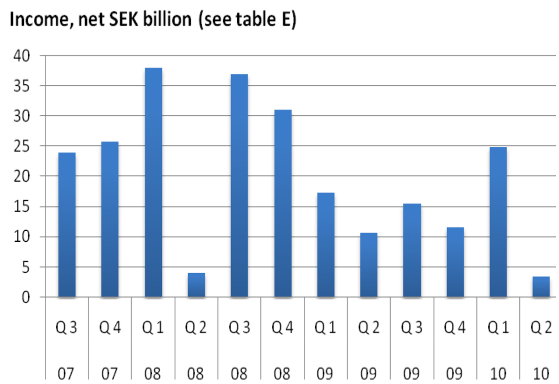


During the second quarter exports as well as imports increased for the aggregate *other business services*. The positive development is mainly due to increase income from *research and development* together with *merchanting*.

The item for travel is highly affected by the seasons, and comparisons are best made with the corresponding quarter of the previous year. Exports of travel consist of foreign travellers' consumption when travelling in Sweden, while imports correspond to expenses of Swedes when travelling abroad. Exports increased by 2 percent while imports fell 3 percent. All in all, this resulted in a relatively small deficit for the item travel, SEK 1.8 billion.

The other types of services resulted in a net inflow of SEK 14.9 billion. Both exports and imports rose compared to the previous quarter, but when looking at the previous year, exports decreased while imports were at the same level. The increase from the previous quarter is mainly because *transport* rose by SEK 1.9 billion with freight services accounting for the most part.

Income

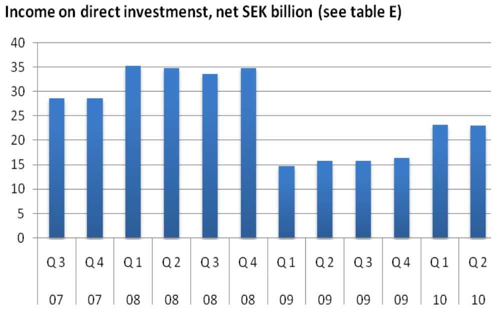


During the quarter, income amounted to SEK 3.4 billion. The corresponding amount for the second quarter of 2009 was SEK 11.8 billion. Income consists of salaries and income on invested capital.

Investment income consists of income on direct investments, portfolio investments and other investments. These resulted in a total net inflow of SEK 3.8 billion. This is about the same level as in the second quarter of 2008, while the same period in 2009 resulted in the capital inflow of SEK 12.4 billion. The relatively low level is largely due to high dividends to foreign owners for Swedish shares.

The item *salaries* resulted in a net outflow of SEK 0.4 billion, somewhat less than in the second quarter of 2009.

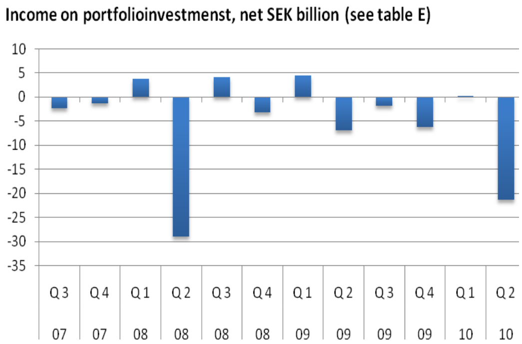
Income on direct investments



Income on direct investments resulted in a net inflow of SEK 22.9 billion during the second quarter, an increase compared to the previous year. The increase was mainly due to returns on investments abroad. Compared to the year before, these income rose by SEK 13.2 billion and amounted to SEK 61.7 billion. Income on direct investments in Sweden amounted to SEK 38.8 billion, which was an increase of SEK 6.5 billion from the second quarter of 2009.

Income for direct investment companies is preliminary up until it is replaced by the result of the annual survey in direct investments.

Income on portfolio investments

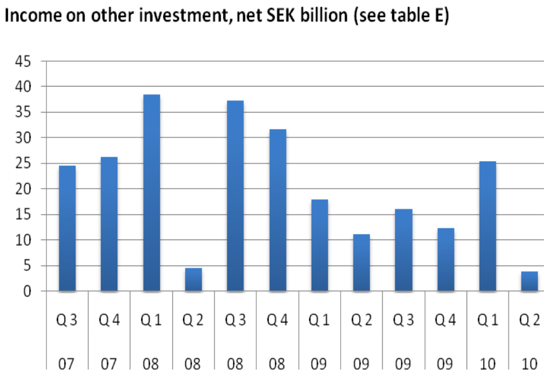


Income on portfolio investments resulted in a net outflow of SEK 21.3 billion during the second quarter. During the same quarter of 2009, the corresponding amount was SEK 7.0 billion. The outflow was mainly because Swedish shares gave higher dividends than foreign shares. Dividends on foreign shares resulted in an inflow of capital of SEK 31.2 billion, or somewhat less compared to the same period last year.

At the same time dividends on Swedish shares increased from SEK 33.1 billion to SEK 36.0 billion.

Income on debt securities generated a total outflow of SEK 16.5 billion net. Interest costs for Swedish debt securities amounted to SEK 26.2 billion while interest income on foreign debt securities was SEK 9.7 billion.

Income on other investments

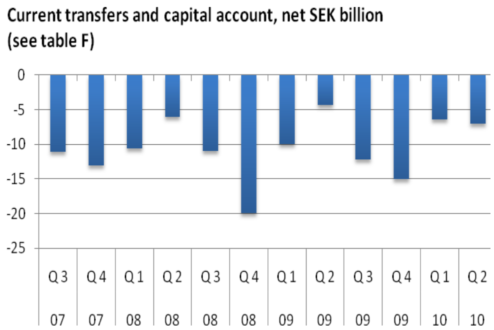


Income on other investments gave rise to a net inflow of SEK 2.2 billion, which can be compared to the net inflow of SEK 3.2 billion during the same period in 2009.

Gross flows continued at a relatively low level this quarter as well. Income on other investments abroad amounted to SEK 7.5 billion and income on investments in Sweden amounted to SEK 5.3 billion. This is comparable to the same quarter of 2009 which resulted in an inflow of SEK 11.8 billion and an outflow of SEK 8.6 billion.

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

Current transfers and capital account

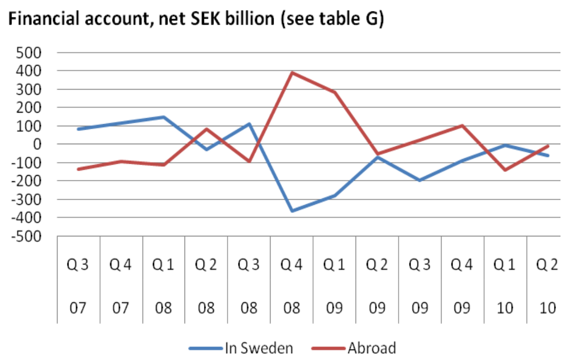


Current transfers and capital account resulted in a deficit of SEK 7.0 billion during the quarter. This is a slight increase in the deficit compared to the quarter before.

The deficit is mainly due to a net outflow of transfer payments in connection with the EU, which after the low level of the first quarter amounted to SEK 3.1 billion. Foreign aid to developing countries also contributed to the deficit by SEK 2.8 billion.

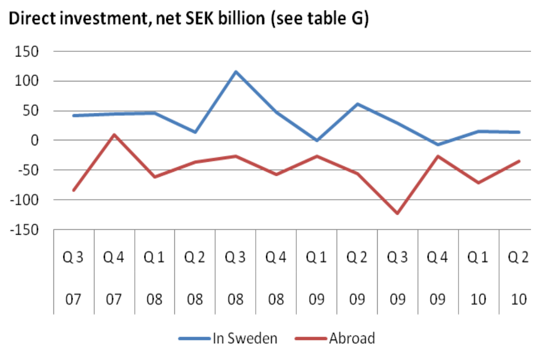
The capital account has two main components: capital transfers as well as transfer of rights etc. Transfers in the capital account are different from those in the regular transfers in the current account because the purpose of EU subsidies, gifts etc. is to encourage the recipient to make a real investment. Inheritance and migration are also included in the capital transfers.

Financial account



The financial account resulted in a net outflow of SEK 74.3 billion for the second quarter of 2010. This can be compared to a net outflow of 121.4 billion for the same quarter of 2009. Like in previous quarters, the portfolio investments and other investments show the largest flows. Other investments accounted for an inflow of SEK 114.8 billion, while portfolio investments resulted in an outflow of SEK 113.2 billion. The reserve assets gave an outflow of SEK 59.5 billion during the second quarter.

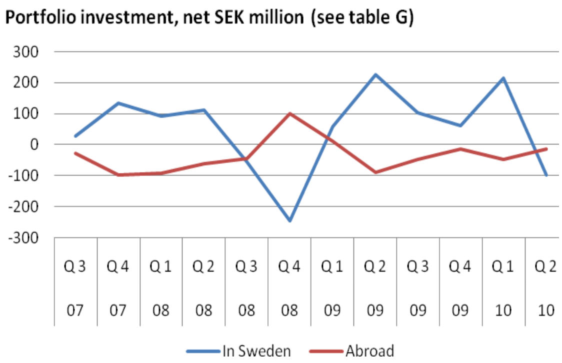
Direct investment



Direct investments produced a net outflow of SEK 20.4 billion during the quarter. Activities in direct investments have been relatively low during the quarter. Swedish direct investments abroad resulted in a net outflow of SEK 34.9 billion.

This outflow was mainly due to reinvested earnings. Reinvested earnings is an item in the statistics that refers to earnings in direct investment companies that are not distributed to shareholders but are reinvested in the company. Foreign direct investment in Sweden produced a net inflow of SEK 14.5 billion. Similar to Swedish direct investments abroad, the reinvested earnings account for the largest flow.

Portfolio investments

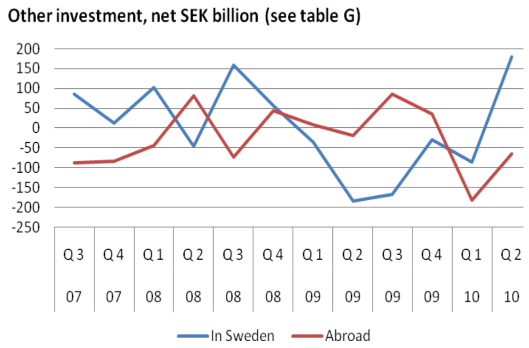


Portfolio investments resulted in a net outflow of SEK 113.2 billion during the second quarter of 2010. During the same quarter in 2009, portfolio investments produced a net inflow of SEK 167.7 billion. The outflow for portfolio investments is mainly due to the maturity of Swedish debt securities.

Swedish portfolio investments abroad resulted in a net outflow of SEK 13.9 billion during the quarter. Swedish investors made net purchases of foreign shares for SEK 21.5 billion, mainly in Norway and the US. At the same time, net sales of foreign bonds were made for SEK 20.3 billion, while net purchases of foreign certificates were made for SEK 12.7 billion. Sales were mainly made for American bonds, while purchases were to a large extent made for British bonds.

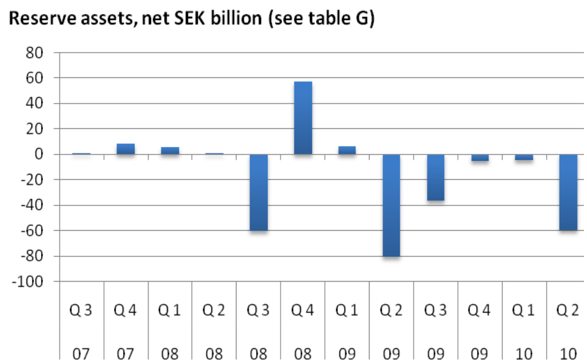
Foreign portfolio investments in Sweden produced a total net outflow of SEK 99.3 billion. The net outflow is mainly due to the maturity of Swedish debt securities and because Swedish investors purchase Swedish debt securities from foreign investors on the secondary market.

Other investments



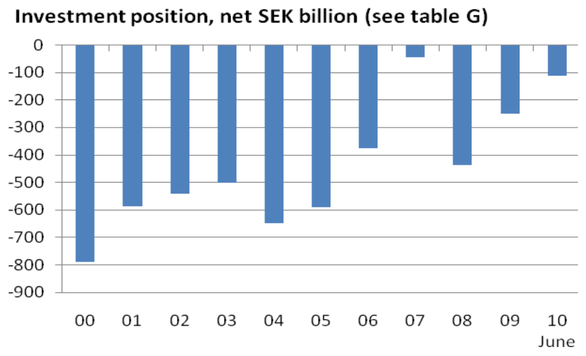
The item other investments, mainly consisting of loans to and from other countries, resulted in a net inflow of SEK 114.8 billion during the second quarter. Swedish investments abroad mainly consist of loans to foreign counterparts, and produced a net outflow of SEK 65.9 billion. Banks and housing credit institutions account for the bulk of the net flows. Foreign investments in Sweden mainly consist of debts to foreign counterparts and resulted in an inflow of SEK 180.7 billion. Banks and housing credit institutions account for the largest part of this borrowing, but the Riksbank has also borrowed from abroad.

Reserve assets



The Riksbank has strengthened its reserve assets during the second quarter by SEK 59.5 billion. Bank assets and securities in foreign currency account for the bulk of this strengthening.

International investment position, net



The Swedish net debt against other countries decreased during the first six months of 2010 and amounted to SEK 112 billion at the end of June.

Net assets in the form of direct investment have been estimated at SEK 392 billion, which is a decrease compared to end of 2009 when net assets amounted to 447 billion. This decrease is because of fewer Swedish direct investments abroad.

The net liability for portfolio investments dropped somewhat during the first half of 2010 and amounted to SEK 895 billion. The value from the end of 2009 has been replaced by the value of the outcome from Statistics Sweden's annual survey on Swedish portfolio holdings abroad. This has led to a revision of the foreign debt for the period.

The value of assets and debts abroad in derivatives increased during the first six months. By the end of the year balance values for assets in derivative contracts, i.e. contracts with positive market values, amounted to SEK 447 billion. The corresponding balance values, i.e., contracts with negative market values, amounted to SEK 365 billion. This results in net assets of SEK 81 billion.

As for other investments, both assets and debts have increased during the first half of the year, because Swedish counterparts borrowed from and loaned to foreign counterparts. The lending was greater than the borrowing, thus reducing net liability, which amounted to SEK 102 billion at the end of June. This is a drop in liability of SEK 94 billion, compared to the end of 2009. During the first half, the Riksbank has strengthened the reserve assets, which amounted to SEK 411 billion.

The official compilation of Sweden's international investment position is presented at market value, with the exception of direct investment, which is reported at book value. As a supplement, the international investment position is also published, using market value for direct investments. This calculation is only done once a year.

The report on Sweden's assets and liabilities is published separately every six months, and instruments are presented by sector. The international investment position will be published on 7 September 2010.

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 ($X_t - M_t$):

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

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]

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

Rewriting (2) gives:

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

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:

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

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

[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**