Balance of Payments

First quarter 2011

Statistiska centralbyrån   Statistics Sweden

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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 first quarter of 2011.

Statistics Sweden, May

Folke Carlsson

Christina Ekblom

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Summary

The surplus in the current account amounted to SEK 71.1 billion in the first quarter. This is an improvement of SEK 16.5 billion compared to the same period in 2010. An increased surplus for trade in goods has been the main contribution to this improvement. Investment income also contributed to the improvement, mostly due to direct investments which resulted in higher earnings.

The current account was also stronger than in the fourth quarter of 2010. Among other things, this was due to increased earnings on capital as well as a reduced deficit in current transfers. Imports of goods also decreased during the quarter; as a result, the trade in goods was once again at the same level as the beginning of 2009.

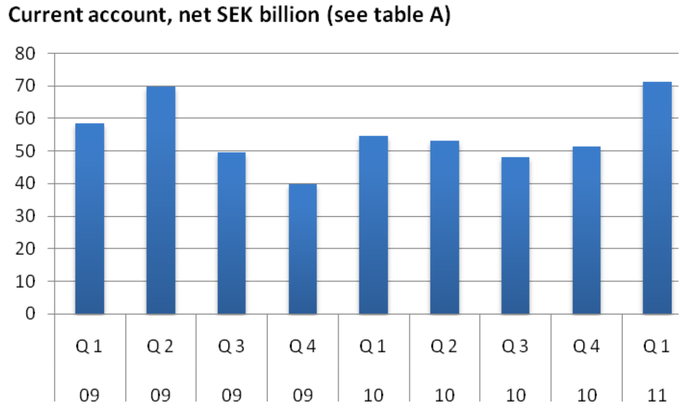
The financial account resulted in a net outflow of SEK 127.3 billion for the first quarter of 2011. It was mainly portfolio investments that contributed to the outflow with a net capital outflow of SEK 92.9 billion. The outflow is mainly due to trade with Swedish government securities and increased holdings of foreign debt securities owned by Swedish investors. Loans to other countries within other investments also resulted in a net outflow of capital.

Balance of payments first quarter 2011

Balance of payments showed a relatively large surplus of SEK 71.1 billion in the current account during the first quarter of the year. The financial account resulted in a capital outflow of SEK 127.3 billion while the capital account generated a small deficit of SEK 0.1 billion.

Current account

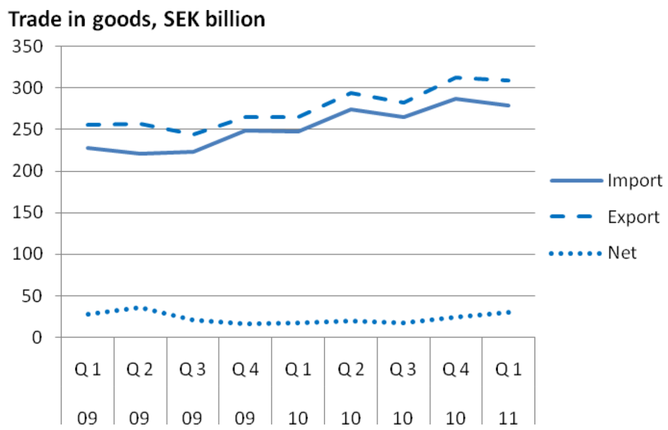
The current account comprises largely of trade in goods and services, which generated a net inflow of SEK 53.2 billion during the quarter. This is a clear improvement from the first quarter of last year when the value was SEK 39.5 billion. Above all, trade in goods has contributed to the increase, but trade in services also rose somewhat compared to the same period the year before. Investment income with increased re-invested earnings on direct investments also contributed to the larger surplus in the current account.



Foreign trade in goods and services

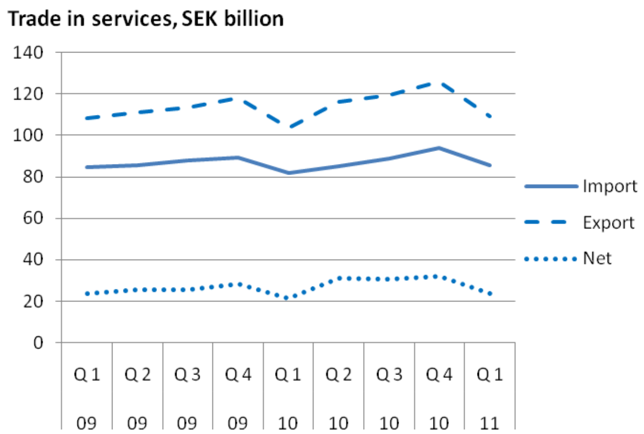
Total exports as well as imports of goods increased compared to the same period last year and are now at levels similar to the start of 2008. Exports rose more than imports, resulting in a somewhat stronger trade in goods SEK 29.7 billion. This is a clear improvement compared to all quarters of last year.

Previously there were concerns that a continuous strengthening of the Swedish krona would reduce exports and slow down growth in Sweden. The EU area is an important trading partner and last year at the krona was strengthened against the euro by an entire 12 percent. This continued even during the first quarter of the year when they krona rose against the euro by 0.7 percent. Nevertheless, exports to the EU countries increased compared to the same quarter the year before. However, exports to countries outside the EU rose even more.



The first quarter of every year normally shows a somewhat lower turnover in trade in services and 2011 was no exception. Trade in services decreased during the quarter to roughly SEK 23 billion net, but this was still an increase of SEK 2.1 billion compared to the same period one year ago. This increase occurred because exports rose nearly twice as much as imports.

The items where development was strongest during the year are, among other things, data and information services, licenses and royalties as well as transport. Concerning the first two items mentioned, exports have above all increased markedly. Exports of transports remain at the same level as last year, but imports have decreased, leading to a relatively high net figure.



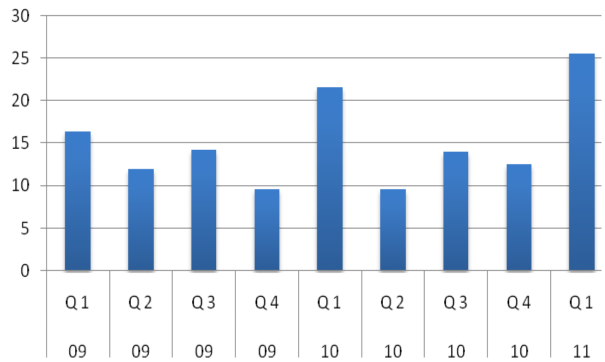
Consumption of Swedes who travel abroad continues to increase compared to the first quarter last year. At the same time, consumption of foreign travellers in Sweden has not been influenced by the stronger Swedish krona to such a great extent and consumption remains at the same levels of previous years. The development shows that imports and exports continue to move apart, resulting in a relatively high net import for the item for travel. Compared to 2010 net imports have increased by SEK 1.2 billion.

Exports of travel consist of foreign travellers' consumption when travelling in Sweden while imports correspond to expenses of Swedes when travelling abroad. The item for travel is highly affected by the seasons, and comparisons are best made with the corresponding quarter of the previous year.

Income

Income consists of both compensation of employees and investment income, which together resulted in a capital inflow of SEK 25.5 billion. Investment income in turn consist of earnings on direct investments, portfolio investments as well as other investments. The high investment income are mainly due to the high earnings within direct investments.

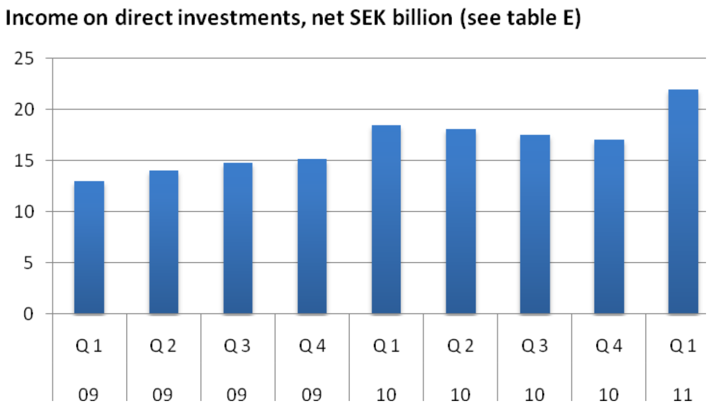
Income, net SEK billion (see table E)



Earnings on direct investments

Earnings on direct investments resulted in a net inflow of SEK 22.0 billion during the first quarter. Earnings on direct investments abroad amounted to SEK 68.9 billion, while earnings on corresponding foreign direct investments in Sweden totalled SEK 46.9 billion. Dividends were relatively small during the quarter which in turn means that large reinvested earnings are presented in the statistics. Reinvested earnings are a residual item in the statistics that refers to earnings in direct investment companies that are not distributed to shareholders.

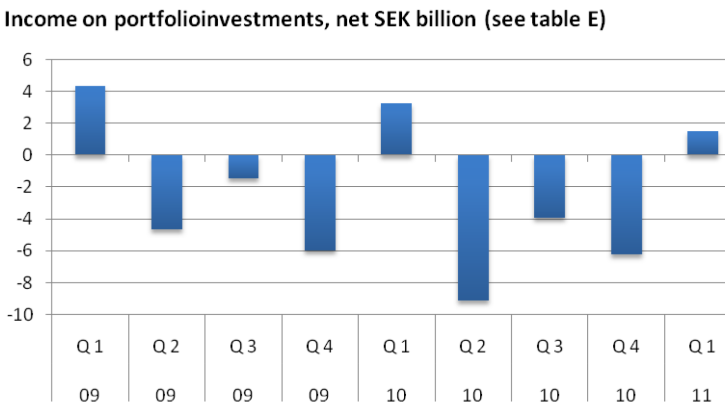
Earnings on capital for companies working with direct investments are preliminary up until they are replaced by the result of the annual survey in direct investments.



Earnings on portfolio investments
Interest on Swedish bonds fell back somewhat partly because of lower interest levels on government bonds while earnings on foreign bonds rose compared to the previous quarter.

The first dividends of the year on Swedish shares generated earnings of nearly SEK 2.0 billion abroad. However, the largest part of the dividends arrives during the second quarter. Dividends of foreign shares owned by Swedes resulted in a capital inflow of SEK 15.1 billion.

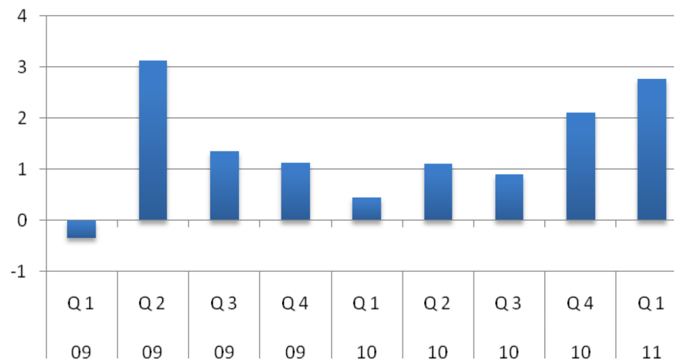
Interest and share dividends together resulted in a net inflow of capital of SEK 1.5 billion.



Earnings on other investments
Earnings on other investments abroad resulted in a net inflow of SEK 8.6 billion while corresponding foreign investment in Sweden resulted in a net outflow of SEK 5.8 billion. Even though assets and liabilities are nearly equal, earnings in other investments resulted in a net inflow of SEK 2.8 billion. The net flow is mainly due to higher earnings on assets than on liabilities.

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

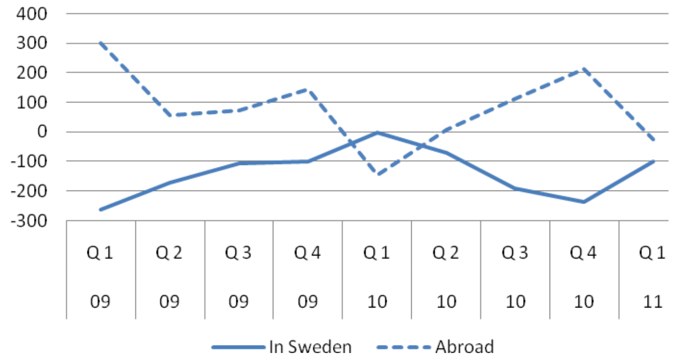
Income on other investment, net SEK billion (see table E)



Financial account

The financial account resulted in a net outflow of SEK 127.3 billion for the first quarter of 2011. It was mainly portfolio investments that contributed to the strong development.

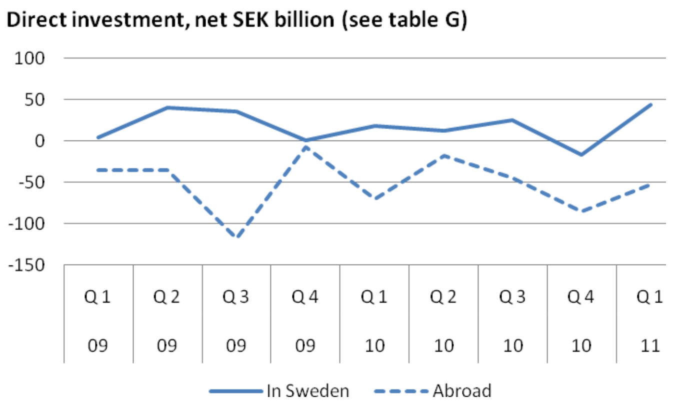
Financial account, net SEK billion (see table G)



Direct investments

Direct investments resulted in a net outflow of SEK 9.8 billion during the first quarter. Swedish direct investments abroad resulted in a net outflow of SEK 53.1 billion. Conversion of loans to equity capital contributed to the outflow in the sub item for equity capital and inflow in the sub item for loans. Reinvested earnings contributed to a larger outflow because dividends were relatively small during the quarter.

Foreign direct investments in Sweden produced a net inflow of SEK 43.2 billion during the first quarter. In addition, reinvested earnings for foreign direct investments in Sweden accounted for the main part of the net inflow.

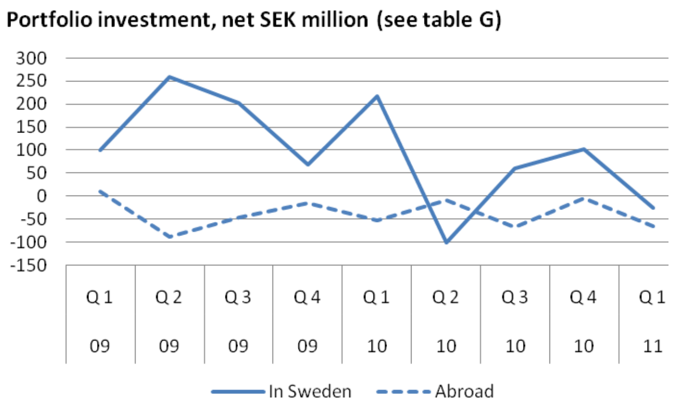


Portfolio investments

International portfolio investments in the first quarter resulted in a net capital outflow of SEK 92.9 billion. The outflow is mainly due to trade with Swedish government securities and increased holdings of foreign debt securities owned by Swedish investors. The total amount of trade in debt securities issued by the government gave rise to a net outflow of SEK 68.2 billion. In addition to the reduced volume of emissions by the Swedish National Debt Office, foreign investors' sales on the secondary market contributed to the net outflows.

Swedish investors' purchases of foreign debt securities also contributed to the capital outflow of SEK 56.3 billion. Above all, Danish bonds attracted the greatest interest, but American and Finnish debt securities were also attractive.

Cross-border trade in shares and funds resulted in a net outflow of SEK 15.2 billion. Swedish investors made net purchases of foreign shares and funds for SEK 10.0 billion.

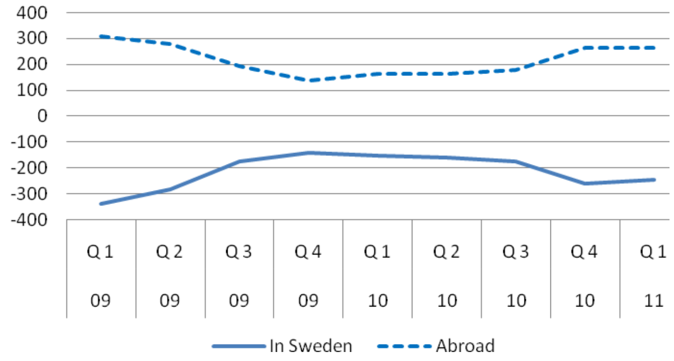


Financial derivatives

Transactions in financial derivatives contributed with a relatively large net inflow of SEK 15.3 billion. The gross flows are of the same high level as in the previous quarter. Matured currency swaps contributed the most to the flow.

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.

Financial derivatives, net SEK billion (see table G)

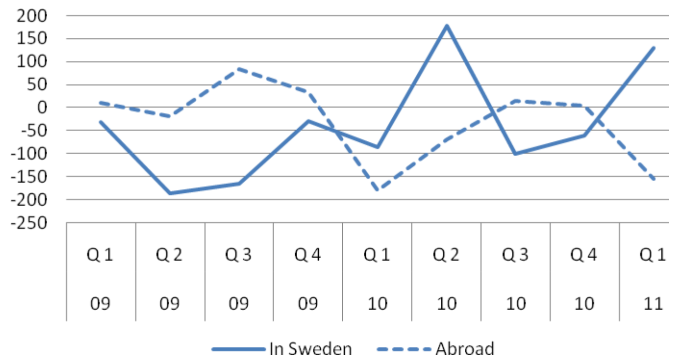


Other investments

Other investments produced a net outflow of SEK 25.3 billion during the first quarter. Lending to other countries produced a net outflow of SEK 154.2 billion while borrowing from other countries produced a net inflow of SEK 128.9 billion. The flows were mainly between the Nordic countries.

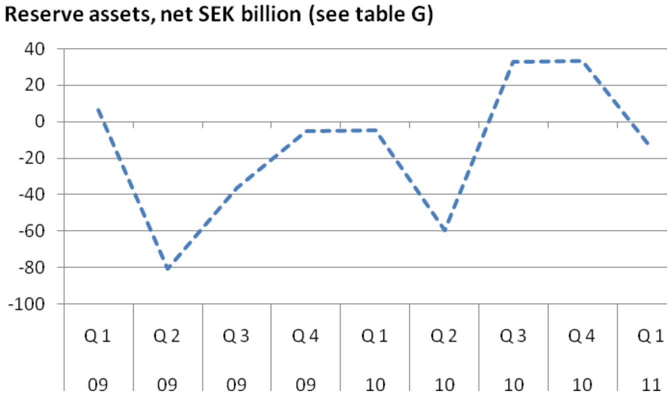
Other investments mainly consist of loans of the bank sector to and from other countries, excluding loans of securities. Among other things, these include promissory note loans, deposits and repurchases.

Other investment, net SEK billion (see table G)



Reserve assets

Transactions in the reserve assets resulted in a net outflow of SEK 14.5 billion during the first quarter when the Riksbank strengthened the reserve assets. The outflow is due to increased holdings of foreign bank assets and debt securities.



What is the balance of payments?

The balance of payments has been produced and summarised by Statistics Sweden on behalf of 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. The balance of payments is quite simply a summary of a country's real and financial transactions with the rest of the world

The balance of payments can be divided into the following:

- The current account, 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 is divided into direct investments, portfolio investments, financial derivatives, other investments and the foreign exchange reserve. The financial account shows changes in external financial assets and liabilities.

Derivation of the balance of payments

A country's gross domestic product, BNP_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 sector fees 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 ($X_t - M_t$):

$$BNP_t = C_t + I_t + G_t + X_t - M_t. \quad (1)$$ [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, BNI_t:[2]

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

Rewriting (2) gives:

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

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, $BNI_t - T_t - C_t$.[3]

According to (3) the following applies:

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

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 the trade account. $X_t - M_t + F_t$ 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 the trade in goods during certain periods of time.

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

where A_t are the net external assets during period t and $r_t A_t$ are 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):

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

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 in 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 reserve assets, 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 services 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. 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]

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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.

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 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**

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