Problems § 2

1. We look at the presentation of the BoP for the euro area as a table:

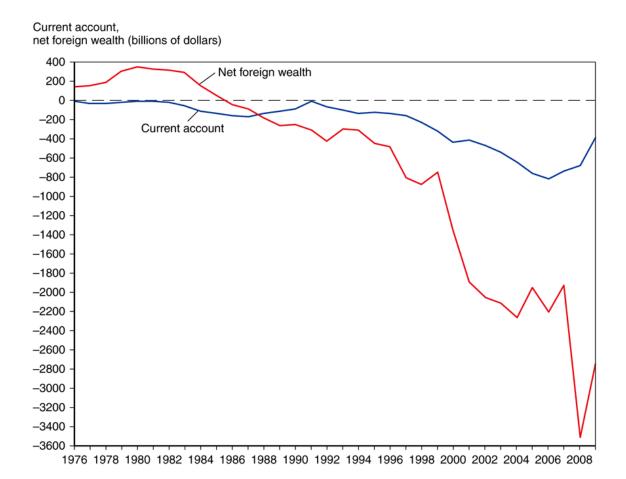| Account	€ bn, 2020
1. Balance of Foreign Trade	
2. Balance of Trade in Services	
3. Balance of Income Payments (Primary Income)	
4. Balance of Current Unilateral Transfers (Secondary Income)	
5. Capital Account	
6. Commercial Financial Account	
7. Official Settlements Balance	

a) Please make the book-entries for the following transactions in the table above. For each transaction, please …

- … enter the number of the transaction (e. g. (4) for transaction (4) below)

- … denote a credit entry by a plus (+) and a debit by a minus (-)

- … enter the numerical value of the entries

- … indicate the economic character of the entries by using the symbols from the script (e. g. EX_G for an export of goods)

(1) A resident of the euro area imports a DVD in the amount of €30 from Japan by using his credit card. The Japanese producer deposits the money in his bank account in Berlin.

(2) A resident of the euro area invests in Japanese stocks that Sony is just issuing (amount €500). Sony deposits the money in its bank account in Brussels.

(3) A bank from the euro area forgives €100 debt to the governments of both (a) Argentina and (b) Greece.

(4) During his travel in India, a resident of the euro area eats in a restaurant. He pays the bill in the amount of €20 by his Visa credit.

(5) A resident of the euro area buys a company in the USA. To finance this purchase in the amount of € 700, he takes a credit from an American bank.

(6) A resident of the euro area holds Russian government bonds. The Russians make the annual coupon payment in dollars (in the amount of €10); the European investor sells them to the European Central Bank.

(7) A poor professor of economics from the university of Siegen gets his annual bottle of red wine from his rich colleague in California (€5).

(8) Americans are on holiday in the well-known tourist resorts of the Siegerland. They pay dollars (in the amount of €90) to a hotel. The hotel sells the dollars to the European Central Bank.

(9) A French investor is shocked by news from China: his Chinese debtor has surprisingly gone bankrupt so that the investor looses 80% out of his total credit of €50.

b) Please calculate the following balances and indicate their symbols:

b_1 Balance on trade in goods

b_2 Balance on trade in services

b_3 Balance of trade

b_4 Balance on primary income (balance on trade in factor services)

b_5 Balance on current transfers

b_6 Balance on current account

b_7 Balance on capital account

b_8 Balance on commercial financial account

b_9 Balance on official settlements

b_{10} Balance on financial account

c) Please calculate the "Balance of payments". Why is this a highly misleading name?

d) Please check the overall consistency of your entries.

2. We look at exhibit 2.1.1 (3a) from the script. It visualizes the BoP as an account.

a) Please try to condense the BoP in just two accounts, the "current account" and the "capital and financial account".

b) Please try to express the statement of the condensed BoP account in an equation.

3. This problem is based on Feenstra/Taylor (2012), pp 575 n.

   Please interpret the balance on financial account (FA) in terms of exports and imports of assets (A), domestic (D) and foreign (F). Please use the following symbols: EX_A^i, IM_A^i, $i = D, F$.

4. We look at the graph showing net foreign assets and the balance on current account for the USA from the beginning of 1976 to the end of 2009.

Current account,
net foreign wealth (billions of dollars)

a) Using suitable equations, please comment the impact of the balance on current account on net foreign wealth:

   a_1 within one period

   a_2 over time

b) Is the current account sufficient to explain the development of net foreign wealth?