Balance of Payment: Definition Convention and Accounting

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Unit Highlights:

® Definition of Balance of Payments
® Balance of Payments Accounting
® Balance of Payments Equilibrium
® Surplus and deficit in the balance of

payments

Lesson-1 : **Balance of Payment : Definition, Convention and Accounting.**

Lesson Objectives

After studying this lesson, you will be able to:

® understand the concept of balance of payment;
® explain the method of accounting the balance of payment is based on;
® differentiate the current account from the capital account and
® understand why an entry called "statistical discrepancy" appears in the balance of payments.

Introduction

Disturbances and adjustment are constantly taking place in variables concerning international transactions (e.g. the rate of exchange). Therefore, the policy markers have to keep close watch over these developments. For example, a financial manager may have reasons to believe that a particular foreign currency is going to fall in its external value and that interest rates on loans denominated in that currency is not high enough to reflect this belief. Then he might prefer to borrow in that currency. Moreover, he may postpone the repayment of loan in that currency until it is cheapened (by fall in its value). Now the values of a foreign currency are determined in the international financial environment as a whole (i.e the international macro economy) and it is essential that this environment be properly understood. This will help a manager anticipate events and react intelligently to them rather than act passively to events which have actually unfolded. A nation's balance of payments accounts provide the starting point for any serious study of this international environment. The importance of the balance of payments accounts is not obviously limited to our financial manager. There could be other policy makers (e.g. the finance minister of a country) whose objectives may be different, or who may operate under different institutional arrangements. But regardless of the objectives or institutional settings the state of the balance of payments is affected by a country's international transactions.

A country's international transactions influence the state of its balance of payments.

The balance of payments: Definitions and Conventions

Definition: The balance of payments of a country is a systematic statistical record of the flow of payments (arising out of economic transactions) between the residents of the reporting country and those of the rest of the world over a period of time (usually a year).

The balance of payments is basically a list of international transactions over a period of time, usually a year.

Simply speaking, the balance of payments provides a list of sources and amount received and paid for international transactions over a period of time. As the definition makes clear, the balance of payments is a flow per period of time like national income. And indeed, a part of it (that dealing with exports and imports) appears in the national income accounts. Moreover, the definition to be precise must answer the two questions it gives rise to: (1) What is an economic transaction? (ii) Who is a resident?

An economic transaction is an exchange of value; it involves transfer of ownership or use rights of goods and services of assets, physical or financial, between individuals, groups or institutions. An international transaction is one in which residents of two different countries are involved.

Both rules and conventions are used to define a 'resident.'

A resident may be an individual or an institution. An individual whose primary residence in a country should be defined as the resident of that country, regardless of his citizenship or passport status. Examples of residents as institutions are central and local governments, business enterprises and non-profit organizations located in a country. Focusing on residence is undoubtedly useful, because people tend to demand the currencies of the country in which they live. For example, a Briton living in New York will demand dollars (not pound sterling) to settle transactions. In practice, applying the criterion of primary residence is difficult. In many cases, arbitrary rules of thumb are, therefore, used to settle questions of residency. These include cases of diplomats, tourists, military personnel, temporary migrant workers and branches of multinational companies.

When rules break down, conventions take over. For instance, a corporation is treated (conventionally) as a resident of the country in which it is incorporated. In contrast, its foreign branches or subsidiaries are counted as residents of the country in which they are located. Tourist, diplomats, military personnel stationed abroad, temporary migrant workers, students are regarded as citizens of the country of their origin despite their location or residence in a given country. It may be noted that though residence is a blurry concept, it causes no great problem as long as the blur is slight (which is usually the case).

Let us provide a few examples to clarify these conventions. Bangladeshi students in US universities are treated as Bangladeshi residents, and therefore, whatever expenditures they incur in U.S are US exports to Bangladesh. US troops stationed in Germany are thought of as US residents, and so their purchases in Germany are Germany's exports to U.S.A(i.e. imports of the United states from Germany). If a Japanese multinational company ships cars to its affiliate in Bangladesh, this will count as Japanese exports to Bangladesh, since it is (by convention) a sale by a Japanese resident (the parent company) to a foreign resident (the Bangladeshi affiliate).

A totally different convention exists for international institutions like the United Nations, the IMF and the World Bank. These are not regarded as residents to the country of their location, nor do they have any country of origin. So they are treated as international areas outside national boundaries, and in keeping with this convention, their transactions with the residents of the country of their location are treated as international transactions and so recorded in the balance of payments of the country concerned.

The balance of payments accounting is based on the principle of double entry book-keeping.

Balance of Payments Accounting

The balance of payments accounting uses the <u>principle of double entry book-keeping</u> which requires that for every debit (credit) in the accounts, there must be corresponding credit (debit) of equal magnitude somewhere else. The following example will clarify what this means. Suppose that an American firm sells \$5 million worth of computers to a British firm and that the latter pays for its imports from a US dollar account in a New York bank. This will give rise to the following (double) entry:

Table: 7.1

	Millions of dollars	
	Credits(+)	Debits(-)

Exports (Computers)	+5	
Foreign private asset in US		-5

We see that this way of keeping records takes account not just of the flow of computers but also the flow of payments (and they move in opposite directions). The flow of payments, in this case, can be viewed as allowing Americans to reduce their indebtedness to Britain.

In the balance of payments , all transactions affecting the supply of and the demand for foreign exchange are recorded.

In the balance of payments, all transactions that affect the supply of and the demand for foreign exchange are recorded. For example, all purchases by foreigners of US stocks, bonds, real estate, bank balances and businesses will give rise to demand for dollars, and all these transactions are comprehensively recorded. As a result, it is possible to keep track of the value of items sold and the methods by which payments are made. In its turn, this helps the country keep track of the demand for and the supply of currency.

Since all sources of potential demand for dollars by foreigners and all sources of supply of dollars to foreigners are to be recorded, the number of entries will invariably be quite large. To avoid confusion and ambiguity, there must be a clear-cut rule for distinguishing the debit form the credit entries. Fortunately, there is a simple rule for this. Any transaction that gives rise to demand for dollars is recorded as a credit item in the US balance of payments with a positive sign. On the other hand, any transaction which leads to supply of US dollars in the foreign exchange market is a debit item in the US balance of payment with a negative sign. Obviously, the opposite signs will appear in other countries' balance of payment accounts. In terms of the example given before in Table 7.1, US exports give rise to demand for US dollars and hence it is recorded as a credit item with a positive sign. On the other hand, the payment made by the British firm leads to the supply of dollars in the foreign exchange market and so it must be a debit entry with a negative sign in the US balance of international transactions. More comprehensirly one can say that:

Credit transactions are demand for US dollars and arise from purchases by foreigners of goods, services, goodwill, financial and real assets, gold and foreign exchange from American residents as defined earlier. Debit transactions, on the other hand, are marked by augmentation of the supply of US dollars in the foreign exchange market through purchases by US residents of goods, services, goodwill, financial and real assets, gold and foreign exchange from foreigners.

The sum total of credits must equal the sum total of debits. This follows from the principle of double entry book-keeping.

The principle of double entry book-keeping followed in recording, one and all international economic transactions in the balance of payments, leads inevitably to one possible conclusion: the sum total of credits must equal the sum total of debits (i.e. the books must balance). We can readily verify the validity of this observation from the miniature balance of payments in Table 7.1. At the same time it is important to note that, though rooted in double-entry principles, the balance of payments accounts are rarely presented in the double-entry accounting format. Through consolidation, grouping of items and manipulation of signs, the accounts are presented in a single column, which must sum to zero.

The Structure of the Balance of Payments

There are some minor differences between countries in the ways in which accounts are presented. These stem from the fact that some international transactions do not nicely fit into the conventional categories and are treated or classified differently by different countries. Despite this, the basic structure is strikingly similar.

The entire balance of payments is usually shown as consisting of several sub-accounts and sub-balances which are reported separately for their usefulness in policy making and interpretation of international financial statistics.

The current account is the record of exports and imports of goods and services and one-directional transfers.

1. The Current Account

This account of the balance of payments is a record of exports and imports of goods and services and unilateral (one-directional) transfers. Exports of goods and services are shown with positive signs in the account, while the corresponding imports are recorded with negative signs. Conventions vary with regard to the valuation of export and imports. The value of exports are calculated on f.o.b. basis, while the imports are valued on the c.i.f basis. The difference between the total value of exports and of imports represents the visible (merchandise) trade balance which could be a surplus (positive balance) or a deficit (a negative balance).

In the balance of payments, trade in goods (merchandise) are usually distinguished from trade in service. The latter are frequently called invisibles. For most countries, the trade in services is a heterogeneous category. The importance of service in international commerce tends to be overshadowed by that of merchandise, because of barriers to international movement of factors (particularly labor). Among the important services that are traded internationally are travel, shipping, banking and insurance, consultancy and so on. These items tend to the respond to the same economic factors that affect the merchandise trade-relative international price, exchange rate, income at home and abroad. Interest, profit and dividends are payments for inputs and will largely be determined by accumulated stocks of past investments in and borrowing from foreign residents. Like the visible trade balance, the invisible trade balance is given by the algebraic sum of the value of invisible exports and imports.

Unilateral (one-way) transfers are payments made abroad or receipts from abroad for which there are no corresponding flow of goods or services (or payments). Receipts from abroad are recorded with a positive sign, while payments abroad are recorded negative signs. Moreover, to stay consistent with the double entry system fictitious opposite flows are imagined in the form of exports or imports of goodwill. These unrequitted transfers take the form of non-military grants, foreign aids, financial assistance, private gifts, donations and inheritances.

The net values of the balances of visible trade and of invisible trade and unilateral transfers give the balance on current account.

The net values of the balances of visible trade and of invisible trade and unilateral transfers give the balance on current account. In other words, it is the balance of goods and services plus transfers. Table 7.2 shows the various parts of current account of several countries in 1989.

Finally note that from the national income identity

$$GNP=C+I+G+(X-M)$$

it follows that the term in parentheses is the balance of goods and services. In the national income accounts it is called net exports of goods and services. When the value of output donated by the government and the private sector is subtracted from the balance on goods and services we have what is called "net foreign investment".

Table 7.2 Current Account Summaries, 1998 ($US billion)

	United States	Japan	West Germany	U.K
A. Merchandise exports	360.46	269.59	324.48	151.31
B. Merchandise imports	-475.33	-192.74	-247.77	-189.26
C. Visible trade balance (A+B)	-114.87	76.85	76.74	-37.96
D. Export of services	242.71	143.91	98.31	172.01
E. Import of services	223.14	159.53	-101.13	-157.79
F. Invisible trade balance (D+E)	19.57	-15.62	-2.82	14.22
G. Private unrequitted transfers(net)	-1.33	-0.99	-6.17	-0.49
H. Official unrequitted transfer (net)	-13.43	-3.30	-12.24	-6.93
I. Current Account Balance (C+F+G+H)	-110.06	56.94	55.48	-31.16

The Capital Account

The capital account of the balance of payment shows the details of change in net claims or assets. It is the record of net trade between domestic and foreign residents in various financial claims. The balance of trade in these financial claims then has to be equal to the net change in the home country's claim on foreign residents.

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The fundamental difference between the current and capital account lies in the fact that capital account transactions necessarily involve either acquisitions or surrender of claims on foreign residents, whereas the current account transactions have no such attribute. Therefore, the capital account transactions reflect a change in stocks, either of assets or of liabilities. These figures are net of purchases and sales of investments over the year. Note that buying or selling of the same investment may take place several times during the year. If is neither necessary nor possible to keep track of gross investments during the period.

The capital account consists of three principal types of transactions:

1. Direct Investment: Sometimes residence of a country acquire (or increase) control over a business enterprise in a foreign country. For instance, when the IBM starts a subsidiary in Germany, the US statisticians will record the outflow of American capital investment as a debit(-) entry in the US balance of payment account. Seemingly, it is a paradox to regard the commodity export as a credit and capital export as a debit in the international accounts. But this paradox will quickly disappear if one remembers that an export (import) of capital is an import (export) of securities and that international flows of securities and goods are treated in exactly analogues ways. (By this rule, a capital inflow will be treated as a credit item).

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The establishment of a subsidiary by the IBM is an instance of direct investment abroad. The acquisition of equity by the IBM gives it a measure of control over the management of its subsidiary. The MNC's are the major vehicles of this type of investment and account for a major share of private foreign direct investment.

Of course, private individual transactions in foreign direct investment are not rare, as in the buying of a second home in a foreign country.

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2. Long term portfolio investments: In contrast to direct investments, these do not give the investor a control over management. Buying shares in a foreign company or bonds issued by a foreign government are well-known examples of portfolio investments. These may be of short-term or long-term nature. If an American purchases bonds of a Canadian provincial government with an original terms to maturity of more than a year, he is making a long-term portfolio investment abroad. But note that this distinction on the basis of terms to maturity could be quite misleading. For example, imagine that you have bought a foreign government's long-term security. This will count as a long-term portfolio investment abroad, even if it is going to mature a month after you have bought it. Portfolio investments may be either private or official, depending on their sector of origin.

3. Short-term portfolio investments: These refer to trade in securities with original terms to maturity of less than a year. For example, if a foreign resident buys a US treasury bill, it is a short-term capital inflow for the United States and will be recorded as a debit item in the US balance of payments. Even the holding of foreign currency by US citizens may be regarded as a short-term capital investment abroad. One could justify this by arguing that cash is but a special kind of security that pays no interest, but is held for the sake of the convenience it gives the holder in making transactions.

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What is the balance on capital account ?

The net value of balances of direct and of portfolio investment gives the balance of capital account. The various components of the capital account are illustrated in table 7.2 which shows highly condensed versions of current accounts of several countries for the year 1989. All official long-term transactions are subsumed in the entry "other long term capital."

Table 7.2 : Capital Account Summaries for Four Countries, 1989 (Dollar US billion)

	United States	Japan	West Germany	U.K
j. Direct Investment (net)	40.50	-45.22	-6.99	0.23
K. Portfolio Investment (net)	44.79	-32.53	-4.38	-43.17
L. Other long term capital (net)				
M. Long-term capital balance (J+K+L)	2.64	-15.86	-0.28	-1.76
N. Short-term capital balance (net)	87.93	-93.61	-11.65	-34.98
	16.32	45.86	-56.75	27.53
Balance of capital Account (M+N)	104.25	-47.75	-68.40	-7.45

The balance of payments: Remaining Entries

Apart from the entries shown in Tables 7.1 and 7.2 there are several more entries in the full balance of payments which are identifiable, but cannot be easily put into a standard category.

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Errors and omissions (or statistical discrepancy)

The government statisticians, responsible for compiling a country's balance of payments, do not always observe directly the two sides of every transaction. This can, and does, lead to errors. Some transactions are valued incorrectly. As a result, the quantity recorded for one side of the transaction fails to equal that of its counterpart. In other cases, one side of the transaction is omitted entirely. For instance, in some areas the volume of transactions is so large that the only practical method of collecting data is to resort to sampling (e.g. to collect data on travel expenditures) which leads to inevitable sampling errors. Sometimes (as in large export contracts) the transactor gets an initial payment as a start-up incentive, but receives nothing until the contract is completed. Dishonesty may be responsible for errors in recording transactions. Smuggled-in goods may not be recorded, but their payments may appear in financial transactions somewhere in the economy. Sometimes importers and exporters do not state the actual values of their imports and exports with the intention of cheating or bypassing customs regulations. Finally, we have the case of unreported flows of capital in and out of the country.

Changes in official Reserves and Liabilities

Reserves are held by a country in the form of foreign currency, gold and SDR's borrowed from the IMF. These need not be held within the country concerned. In fact, it is a standard practice to keep a part of the reserves of a country in foreign central banks.

Table 7.3 : Balance of payments Summaries For Four countries, 1989 ($US billion)

	United States	Japan	West Germany	U.K
I. Current account balance	-110.06	56.94	55.48	-31.16
M. Long-term capital balance	87.93	-93.61	-11.65	-34.98
N. Shot-term capital balance	16.32	45.86	-56.75	27.53
O. Other recorded items	1.55	-0.01	0.12	-0.54
P. Net errors and Omissions	22.60	-21.95	2.23	24.55

R. Exceptional financing		12.77	13.43	-1.94
S. Liabilities constituting other authorities reserves.	8.48		-2.95	7.19
T. Total change in reserves	-26.81			9.34

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In the course of transactions in the current and capital accounts, the net reserve position of the country may be affected. Settling transactions give the ultimate or overall balance of payments because the following identity holds:

$B = \Delta R$

where B = overall balance of payments

and ΔR = change in total official reserves.

This says that imbalance is given by the change in official reserves. It has a precise meaning in terms of the supply and demand for currency, because it measures the difference between the amount of currency that private suppliers offer and the amount private demanders want to purchase.

The data on ΔR are provided from government records on its holdings of gold, foreign currencies, IMF balance and the SDR's. It can be assumed that data on ΔR are accurately measured. No such assumption is valid for the error-prone B, as argued earlier. Since change in official reserves are assumed to be accurately measured, the discrepancy between this and the actual overall balance (i.e. current account balance on plus capital account balance regular transactions) allows us to identify the extent of errors and omission.

Table 7.3 gives the full balance of payments accounts for several countries in 1989. The balances on current account and on short and long term capital accounts are taken from Tables 7.1 and 7.2. One can easily verify that the overall balance (including the settling transaction) is zero by finding the algebraic sum of each column of Table 7.3.

Questions for Review

MCQ's (Pick the correct answer)

1. The balance of payment is a systematic statistical record of
   a. a country's domestic revenues and expenditure
   b. the flow of payments between the residents of the reporting country and those of the rest of the word.
   c. cash receipts and cash payments.
   d. the values of total exports and imports.
2. For the balance of payments purposes, a resident may be
   a. an individual
   b. the ministers
   c. an institution
   d. both (a) and (c)
3. If the principle of double entry book-keeping is strictly followed for each and every transaction, then
   a. total of credits should exceed total of debits
   b. total of credits should fall short of total of debits
   c. total of credits must equal the total of debits
   d. there is no definite relationship
4. The entire balance of payments account consists of several sub-accounts and sub-balances, because this device is useful
   a. for understanding the country's unemployment
   b. for understanding the country's inflation
   c. for policy making and interpretation of international financial statistics
   d. for predicting the countrys, GNP.
5. The so-called 'invisibles' refer the trade in
   a. goods
   b. services
   c. goods as well as services
   d. none of the above.
6. The invisible trade balance is given by
   a. the algebraic sum of the value of invisible exports and imports
   b. value of invisible exports only
   c. value of visible exports only
   d. none of the above
7. The capital account of the balance of payments is the record of
   a. change in net assets or claims
   b. change in the value of visible exports
   c. change in the value of invisible exports
   d. algebraic sum of the value of visible exports and imports.
8. The establishment of a subsidiary abroad by the IBM is an instance of
   a. direct investment
   b. portfolio investment
   c. export expansion
   d. none of the above
9. Portfolio investments give the investor(s)
   a. a control over investment
   b. no control over investment
   c. some control over investment

   d. both (a) & (c)
10. An item entitled 'statistical discrepancy' is included in the balance of payments, because government statisticians
    a. make mistakes in calculation
    b. are Pone to judgmental error
    c. cannot always observe directly the two sides of every transaction in spite of their best efforts.
    d. want to show that they too do make mistakes.

Short Questions

1. How is a 'resident' normally defined for balance of payments purposes? Why are conventions too required for this definition?
2. Why are international institutions like the United Nations and the World Bank not regarded as residents of the country of their location? Briefly explain.
3. What do you think are the advantages of drawing up the balance of payments accounts on the principles of double entry bookkeeping?
4. How are debit and credit transactions distinguished in the balance of payments?
5. "Some institutional transactions do not nicely fit into conventional categories and are treated or classified differently by different countries. Despite this their basic structure is strikingly similar." Can you account for this similarity? Explain.
6. The entire balance of payments account consists of several sub-balances. Do they serve any useful purpose? Elaborate.
7. For unilateral transfers, there are corresponding fictitious entries in the form of exports or imports of goodwill. What are these entries for? Explain.
8. Explain how 'net foreign investment' is calculated from the current account.
9. "The capital account is the record of changes in net claims or assets." Explain.
10. Distinguish between Direct Foreign Investment and Portfolio Investment.

Essay-type Questions

1. What is a balance of payments? How is it structured?
2. Describe the various components of the balance of payments. Discuss their importance in understanding the net international indebtedness of a country.
3. Bring out the essential differences between the capital account and the current account of a balance of payments. Which account records the international portfolio investments?

Answer: 1.b, 2.d, 3.c, 4.c, 5.b, 6.a, 7.a, 8.a, 9.b, 10.c

Lesson-2: **Balance of Payments Equilibrium**

Lesson Objectives

After studying this lesson, you will be able to:

® explain balance of payments equilibrium;
® explain what autonomous and accommodating transactions are and
® understand how payments imbalances are dealt with.

As mentioned earlier, the construction of the balance of the payments is based on the principle of double -entry book - keeping so that for every debit entry there is an equal and opposite credit entry. The implication of the method of recording transactions is that, in the accounting sense, the overall balance must always be zero, as we have seen in Table 7.3. What does it mean in economic terms? Particularly, does it mean that the country never faces any problem with respect to its external trade? Unfortunately, this is not so. The balance of payments may always balance, but may not always be in equilibrium. Dis equilibrium in the balance of payments is a sign of imbalance and is a cause for worry. But what is a dis equilibrium in the balance of payments?

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The usual approach to an analysis of dis equilibrium is based on a distinction between autonomous and accommodating transactions in the balance of payments. The autonomous transactions are those which are undertaken for their own sake, usually in response to business incentives. Their values are determined independently of the balance of payments position of the country. They may frequently be affected by the exchange rate, but are not intended to affect the rate or the state of international transactions. All other transactions are called accommodation transactions. They are not undertaken for their own sake, but to fill a gap left by autonomous transactions e.g. to preserve or enforce a price of foreign exchange.

Surplus and Deficit

When the balance of payments is not in equilibrium, there will be either a surplus or a deficit. By definition, when the balance of autonomous transactions is zero, the balance of payments is in equilibrium. When the sum of autonomous receipts (credits) exceed the sum of autonomous payments, there is a surplus. On the other hand, when the total of autonomous payments is greater than the total of autonomous receipts, there is a deficit in the balance of payments.

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Unfortunately making a distinction between the autonomous and the accommodating transactions of the balance of payment is not as easy as it may seem. The distinction may be analytically sound, but is difficult to apply in its theoretical purity in practice. The reason is simple. The distinction is based essentially on motives of making a transaction. But motives are not observable apart from the action they lead to, and the difficulty of inferring motives from actions is well- known. For instance, if short-term capital movements are prompted by interest rate differentials between two countries, they may be called autonomous transactions; but some short term movements may be the result of financing a transaction which is itself autonomous (for example, a merchandise export). Then the capital movements must be deemed accommodating. It is not always easy to tell one from the other.

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Despite these difficulties, there is a long tradition of calling certain categories of items in the balance of payments as autonomous and others as accommodating. Accordingly, a great majority of trades in goods and long-term capital movements are regarded as autonomous, while most short-term capital movements are thought of as accommodating. This may or may not to be reasonable approximation to reality, depending on the nature of the prevailing policy regime. An item may be autonomous under the fixed exchange rate regime with limited capital mobility between nations. It may cease to be so when the exchange rates are flexible and international capital mobility is high.

Conceptually, the imbalance in international transactions should be measured by the net value of accommodating transactions undertaken to keep the exchange rate from changing. This is basically the same as the change in the country's international resources-if it deals with external imbalance solely by financing its deficits or surplus. The principal measure of external balance that the US has used is the balance of official reserve transactions. It measures the net change in the country's international reserves, and consists of net change in reserve assets(gold, foreign currency, borrowing rights in the IMF) and the net change in US liabilities to foreign monetary authorities.

Countries facing dis-equilibrium in their balance of payments can correct it through policies designed to make the exchange rate consistent with equilibrium. Or, they may choose to make the given exchange rate consistent with balance in international transactions.

Some of these are;

1. Lowering the domestic price level so as to cheaper in home goods and services relative to those abroad;
2. Easing the monetary policy in order to make domestic securities less attractive relative to those abroad;
3. Expanding government expenditures can help increase the demand for imports and reduce the excess net sales abroad.
4. Exchange controls or other direct controls on purchases from abroad can reduce excessive net purchases abroad.

Questions for Review

MCQ's (Pick the correct answer)

1. The balance of payments always balances because, it is
   a. based on the principle of double entry book-keeping
   b. always in equilibrium
   c. the value of exports must equal the value of imports
   d. manipulated by the accountants to produce this result.
2. When the balance of payments is in equilibrium, the balance of autonomous transactions is
   a. zero
   b. negative
   c. positive
   d. none of the above
3. A great majority of trades in goods and long-term capital movements are regarded as
   a. accommodating transactions
   b. autonomous transactions
   c. systematic transactions
   d. none of the above.

Short Questions

1. How are autonomous and accommodating transactions distinguished in the balance of payments?
2. "While the distinction between autonomous and accommodating transactions is sound theoretically, it is quite difficult to apply in practice in its theoretical purity." Explain the source of the difficulty.
3. "The principal measure of external balance that US has used is the balance of official resource transaction." Can you explain the logic behind this?

Essay type Questions

1. Explain what is meant by equilibrium in a country's balance of payments. Can it be in dis-equilibrium if the balance of payment always balances? Elaborate.
2. Define surpluses and deficits in the balance of payments. How do they arise?
3. Briefly discuss the various ways in which a dis-equilibrium in the balance of payments may be corrected.

Answer : 1.a, 2.a, 3.b