Balance of Payments and Economic Growth

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Abstract: The focus of the paper shall be on Balance of payments and economic growth. Balance of Payments (BoP) is a statement or record of all monetary and economic transactions made between a country and the rest of the world within a defined period normally every quarter, half a year or on yearly basis. The balance of payments tracks international transactions. When funds go into a country, a credit is added to the balance of payments (“BOP”) while when funds leave a country, a deduction is made. Thus, a Balance of payments (BoP) deficit, on the other hand, indicates that a country’s imports are more than exports. On the other hand, Economic growth is an automatic process. Economic Growth can be measured through an increase in the GDP, per capita income, etc. Economic growth is the increase in the inflation-adjusted market value of the goods and services produced by an economy over time. It is conventionally measured as the percentage rate of increase in real gross domestic product, or real GDP. Both economic growth and balance of payments are macroeconomic objectives because Economic growth is an increase in real GDP – leading to higher living standards while Balance of payments stability refers to a sustainable or limited current account deficit/surplus. (I.e. avoid very high deficit/surplus). A country’s balance of payments tells you whether it saves enough to pay for its imports and it reveals whether the country produces enough economic output to pay for its growth and a balance of payments deficit means the country imports more goods, services and capital than it exports. Therefore, if growth is based on consumer spending and falling saving rates, this will tend to cause imports to rise faster than exports. If saving and investment rates are stable, then the economic growth is more likely to be balanced and avoid the imbalance of large current account deficits and surplus. To sum it up Balance of Payments is a very important record of financial transactions and status of any nation and its economy because it highlights the direction of economic growth or otherwise of any country and is a ground on which many important policy decisions of countries are based.

Keywords: Balance of Payment, Economic Development, Economic Growth, Inflation, Money, Price.
1. THEORETICAL FRAMEWORK

Balance of payment B. O. P is the difference in total value between payments into and out of a country over a period. The balance of payments, also known as balance of international payments and abbreviated B.O.P. or BoP, of a country is the record of all economic transactions between the residents of the country and the rest of the world in a particular period of time, Wikipedia.

In fact, the balance of payments tracks international transactions. When money or funds go into a country, a credit is added to the balance of payments (“BOP”) and similarly, when funds leave a country, a deduction is made. For example, when a country like Nigeria exports (50) fifty hides and skin to another country Ghana, a credit is made in the balance of payments of Nigeria.

2. LITERATURE REVIEW

2.1 Concept of Balance of Payment

The Balance of Payments or BoP is a statement or record of all monetary and economic transactions made between a country and the rest of the world within a defined period usually every quarterly or yearly. For example, you must have at one time or the other seen people settling accounts and monitoring small expenditures. You must have seen them set aside reserves, keep a record of all transactions and purchases, and tally their accounts and statements to ensure they are all set for the month or the quarter. Now apply this scenario to the country as a whole and that is Balance of Payments in nonprofessional terms. Thus, the Balance of Payments B. O. P of a country is a complete picture of its international transactions and a Balance of Payments B. O. P deficit, on the other hand, indicates that a country's imports are more than exports.

2.2 Concept of Balance of Trade

The balance of trade is the difference between the value of a country's imports and exports for a given period. The balance of trade is the largest component of a country's balance of payments. Economists use the BOT to measure the relative strength of a country's economy. A country that imports more goods and services than it exports in terms of value has a trade deficit. Conversely, a country that exports more goods and services than it imports has a trade surplus. In effect, a country with a large trade deficit borrows money to pay for its goods and services, while a country with a large trade surplus lends money to deficit countries. The formula for calculating the BOT can be simplified as the total value of imports minus the total value of exports.

For example, if the Nigeria imported $3 trillion in goods and services in 2015, but exported only $2 trillion in goods and services to other countries, then the Nigeria had a trade balance of -$1000 trillion, or a $1000 trillion trade deficit.

However, exports and imports are important for the development and growth of national economies because not all countries have the resources and skills required to produce certain goods and services so that scarcity and surplus of goods can be controlled through trade balance.

2.3 Concept of Economic Growth and Development

What is the difference between Economic Growth and Development? We will start by defining Economic growth and development. Having economic growth without economic development is possible.

Economic growth in an economy is demonstrated by an outward shift in its Production Possibility Curve (PPC). Another way to define growth is the increase in a country’s total output or Gross Domestic Product (GDP). It is the increase in a country’s production.

A country’s economic development is usually indicated by an increase in citizens’ quality of life. ‘Quality of life’ is often measured using the Human Development Index, which is an economic model that considers intrinsic personal factors not considered in economic growth, such as literacy rates, life expectancy and poverty rates.

We all fund economic development in one way or the other by purchasing something at the store and pay local or state sales tax. The school fees you pay, the necklace you buy, or the real estate taxes you may pay, all usually have a percentage of the sales going towards economic growth and development projects or initiatives.
2.4 Components of Balance of Payment (BoP)

The Balance of payment consist of (3) three main components, current account, capital account, and financial account. However, it is good to note that the current account must balance with the combined capital and financial accounts. Therefore below are the components in detail:

i. Capital Account: The capital account monitors the flow of international capital transactions. These transactions include the purchase or disposal of non-financial assets (for example, land) and non-produced assets. Capital account of BOP records all those transactions, between the residents of a country and the rest of the world, which cause a change in the assets or liabilities of the residents of the country or its government. It is related to claims and liabilities of financial nature. The capital account also includes money received from debt-forgiveness and gift taxes. In addition, the capital account records the flow of the financial assets by migrants leaving or entering a country and the transfer, sale, or purchase of fixed assets. The capital account consists of two major subaccounts, namely:

- The acquisition and disposal of non-produced, non-financial assets: This measures the purchase and sale of two types of assets: tangible and intangible assets. Tangible assets include the rights to natural resources, such as mineral rights, parts of the electromagnetic spectrum, and offshore drilling rights while Intangible assets include patents, copyrights, and trademarks.
- Capital Transfer: Capital transfers are unrequited transfers where either the party making the transfer realizes the funds involved by disposing of an asset (other than cash or inventories), by relinquishing a financial claim (other than accounts receivable) or the party receiving the transfer is obliged to. However, there are three components of the capital transfer sub-account; insured catastrophic losses, debt forgiveness and the third component is specific to the transfer of the government's assets.

ii. The Current Account: The current account monitors the flow of funds from goods and services trade (import and export) between countries in addition; the current account is a country's trade balance plus net income and direct payments. The current account, which monitors flow of funds between countries, also includes money received or spent on manufactured goods and raw materials. The current account is a country's trade balance plus net income and direct payments. In addition the current account also includes revenue from tourism, transportation receipts, revenue from specialized services (medicine, law, engineering), and royalties from patents and copyrights and revenue from stocks. The components of current account are:

- Trade:- Trade is a basic economic concept involving the buying and selling of goods and services, with compensation paid by a buyer to a seller, or the exchange of goods or services between parties. Trade in goods and services are the largest component of the current account.
- Net Income:- This is income received by the country’s residents minus income paid to foreigners. The country’s residents receive income from two sources. The first is earned on foreign assets owned by a nation’s residents and businesses. That includes interest and dividends earned on investments held overseas. The second source is income earned by a country's residents who work overseas.
- Asset Income:- This is composed of increases or decreases in assets like bank deposits, central bank and government reserves, securities, and real estate.
- Direct Transfers:- A direct transfer is a transfer of assets from one type of tax-deferred retirement plan or account to another. Direct transfers are not considered official distributions and are therefore not taxable as income or subject to any penalties for early distribution.

iii. The financial account: is a measurement of increases or decreases in international ownership of assets. The financial account monitors the flow of funds pertaining to investments in businesses, real estate, and stocks. It also includes government-owned assets such as gold.
and Special Drawing Rights (SDRs) held with the International Monetary Fund (IMF). The financial account is part of a country's balance of payments.

2.5 Importance of Balance of Payment (BoP)

Balance of Payment (BoP) is also known as the balance of international payments and if often abbreviated as BOP. It summarizes all payments and receipts by firms, individuals, and the government and current transfer payment. Below is some importance of Balance of payment:

i. A balance of payments deficit means the country imports more goods, services and capital than it exports.

ii. A country's balance of payments tells you whether it saves enough to pay for its imports.

iii. Balance of Payments is a very important record of financial transactions and status of any nation and its economy.

iv. If the country has a flourishing export trade, the government can adopt measures such as devaluation of its currency to make its goods and services available in the international market at cheaper rates and bolster exports.

v. If the economy needs support in the form of imports, the government can formulate appropriate policies to divert the funds and technology imported to the critical sectors of the economy that can drive future growth.

vi. It analyses the business transactions of any economy into exports and imports of goods and services for a particular financial year. Here, the government can identify the areas that have the potential for export-oriented growth and can formulate policies supporting those domestic industries.

vii. The balance of payment highlights the direction of economic growth or otherwise of any country and is a ground on which many important policy decisions are based.

viii. The balance of payment plays an important role in a country's competitiveness and trade performance.

ix. The government can adopt some protective measures such as higher tariff and duties on imports to discourage imports of non-essential items and encourage the domestic industries to be self-sufficient.

x. The government can also use the indications from Balance of Payments to discern the state of the economy and formulate its policies of inflation control, monetary and fiscal policies based on that.

xi. The trade data shows a clear picture of whether the country’s currency is appreciating or depreciating in comparison with other countries.

xii. When the balance of payments of a country is in equilibrium, the demand for domestic currency is equal to its supply meaning it is favourable. Equilibrium in the balance of payments, therefore, is a sign of the soundness of a country's economy.

3. RESEARCH METHODOLOGY

Several methods are available for use in collecting data in a research work. Some of these methods are so linked that a full study or research cannot be carried out using only one method. There must then be a blending of with available facts.

This research work is specifically designed to study Balance Of Payments and Economic Growth. The research design is meant to guide the researcher in the use of the best method of collecting data in the course of the study. The research design used in this study is the simple method and approach. The researcher is only interested in knowing Balance Of Payments and Economic Growth with secondary sources of data collection, the researcher obtained data from textbooks and previous write-ups on the study, as well as journals and on the internet.

4. CONCLUSION

The balance of payments, also known as balance of international payments and abbreviated B.O.P. or BoP, of a country is the record of all economic transactions between the residents of the country and the rest of the world in a particular period of time (e.g., a quarter of a year). The Balance of
Payment (BoP) statement provides a clear picture of the economic relations between different countries. Thus, the BOP of a country is a complete picture of its international transactions and it is an integral aspect of international financial management. Thus, a country’s balance of payments BoP indicates its position in international economic growth.

The balance of payments BoP statement provides information pertaining to the demand and supply of the country’s currency thus, highlighting the direction of economic growth of a country. The trade data shows a clear picture of whether the country’s currency is appreciating or depreciating in comparison with other countries. In addition, the country’s balance of payments BoP determines its potential as a constructive economic partner. In addition, a country’s BoP indicates its position in international economic growth.

Finally, by studying its balance of payment BoP statement and its components closely, a country would be able to identify trends that may be beneficial or harmful to the economy and respond appropriately in order to achieve economic growth and development.

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