Q: What is balance of payments? What are its components?

Ans: The balance of payments (BOP) is the record of all international financial transactions made by the residents of a country. Balance Of Payment (BOP) is a statement which records all the monetary transactions made between residents of a country and the rest of the world during any given period. BOP statement of a country indicates whether the country has a surplus or a deficit of funds i.e when a country's export is more than its import, its BOP is said to be in surplus. On the other hand, BOP deficit indicates that a country's imports are more than its exports.

BOP has another component that is Financial Accounts.

Current Account

The current account is used to monitor the inflow and outflow of goods and services between countries. This account covers all the receipts and payments made with respect to raw materials and manufactured goods. It also includes receipts from engineering, tourism, transportation, business services, stocks, and royalties from patents and copyrights.

Capital Account

All capital transactions between the countries are monitored through the capital account. Capital transactions include the purchase and sale of assets (non-financial) like land and properties. The capital account also includes the flow of taxes, purchase and sale of fixed assets etc. by migrants moving out/in to a different country. The deficit or surplus in the current account is managed through the finance from capital account and vice versa.

3 major elements of Capital account:

Investments

Foreign exchange reserves

Loans & borrowings

Financial Account

The flow of funds from and to foreign countries through various investments in real estates, business ventures, foreign direct investments etc is monitored through the financial account. This account measures the changes in the foreign ownership of domestic assets and domestic ownership of foreign assets. On analyzing these changes, it can be understood if the country is selling or acquiring more assets (like gold, stocks, equity etc).

CURRENT ACCOUNT	CAPITAL ACCOUNT
1. Current account records the trading in goods and services in the current period.	Capital Account records the movement of capital in and out the economy.
2. Current Account shows the net income of the country	Capital Account shows the change in the ownership of the nation's assets.
3. Current Account is mainly concerned with receipts and payment of cash and non-capital items.	Conversely, Capital Account has thoroughly considered the sources and application of capital.
4. The key components of current account are export and import of goods and services, the investment the income and current transfers	On the other hand, foreign direct investment, portfolio investment and Loans by the government of one country to the government of another country are the key components of Capital Account.

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