

Exercise Sheet 1: Balance of Payments

For the following exercises use the stylized balance of payments as given in the exercise supplement:

Table 1: Stylized Balance of Payment

	Credit (+)	Debit (-)
<u>Current Account</u>		
Goods Trade		
Services Trade		
Investment Income		
Labor Income		
Unilateral Transfers		
<u>Financial Account</u>		
Direct Investment		
Portfolio Investment		
Other Investment		
Capital in Bank Accounts		
Bank Loans		
Official Reserves		

Exercise 1

For each of the following events show how it enters the balance of payments of Switzerland, if it does. Remember that every transaction enters both on the credit and the debit side such that both sides are exactly equal in the end. All transactions are denoted in Swiss Francs (Sfr).

- 1.1) A Swiss bank receives 10 million US Dollars in fees for financial services provided to U.S. customers. The fees are paid to a bank account of the Swiss bank in the U.S. Assume an exchange rate of 1:1 between Sfr and US\$.
- 1.2) The Swiss bank withdraws the 10m US\$ from the bank account and buys Facebook shares.
- 1.3) A little later, the Facebook shares loose 50% of their value.

1.4) A conglomerate of Russian farmers buys tractors for 100m Sfr from a Swiss tractor factory. They pay by taking a loan from a Swiss bank.

1.5) An immigrant from Kosovo working in Switzerland transfers 20'000 Sfr to his family in Kosovo. The family in Kosovo uses the money to buy kitchen equipment from a producer in Switzerland.

1.6) A banker living near the Swiss border in Germany works in Zurich and gets a bonus payment of 10'000 Sfr. He spends all the money by inviting his friends to a lavish, all-inclusive ski weekend in Zermatt.

1.7) A Swiss resource trading firm buys a coal mine in South Africa worth 100m Sfr. They pay by selling shares of various South African companies.

1.8) A little later, the Swiss resource trading firm makes a profit of 1m Sfr from the operation of the mine. They decide to donate all the profit to a South African charity.

1.9) A pensioner living in Germany wants to exchange 100'000 Euros of his savings into Swiss Francs. He holds his savings in a bank account in Germany. His German bank exchanges the Euros for 120'000 Sfr at the Swiss National Bank. The bank then opens a bank account with the 120'000 Sfr in its Swiss branch.

1.10) A French investor receives 100'000 Sfr worth of dividends from shares of various Swiss companies. He invests the money in Swiss government bonds.

Exercise 2

Carefully explain (using again the stylized balance of payments) how the following events lead to statistical errors in the Swiss balance of payments.

2.1) An African drug mafia smuggles drugs into Switzerland and sells them for 100m Sfr to Swiss customers. They then bring the money to a money launderer who manages to transfer the money on a bank account on a Swiss bank. The official holder of the bank account is an African businessman.

2.2) A rich British lady spends her winter vacation in St.Moritz. During the vacation she spends 20'000 Sfr from her Swiss bank account. She spends the money as she pleases and pays mostly in cash.

Exercise 3

3.1) The Philippines have a strongly negative trade balance but still a positive current account. How is this possible? Which particular entry on the balance of payments do you think "explains" the difference in the case of the Phillipines?

3.2) How would you interpret the fact that the Phillipines exhibit a current account surplus? Do you think this is a good sign for the Phillipines?

Exercise 4

4.1) Is it possible to have a current account deficit without having any foreign capital inflows? If so, how?

4.2) Name one entry on the balance of payments that you expect to be of significant importance for Switzerland while it is negligible for the USA.

Exercise 5

Explain how the following events affect the net international investment position (NIIP) of Switzerland. Note that the NIIP is always expressed in the domestic currency.

3.1) After Donald Trump has been elected president, there is a global flight to safety, leading to a strong appreciation of the Swiss franc vis-à-vis all major currencies.

3.2) An earthquake destroys several factories in Asia owned by Swiss enterprises.

3.3) Because of a new government policy that is widely considered to be very bad, the stock prices of all major Swiss companies fall.