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## Several components affecting the balance of payments in Europe

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### Abstract

This study aims to prove and examine the effects of current accounts, capital accounts and financial accounts on the balance of payments. Research on the balance of payments uses data from countries in the European continent. The sample of countries consists of twenty (20) countries and this study uses the time series data method, which is for four (4) years, starting from 2017 to 2020. The method used in data collection is secondary data sourced from European Statistics Recovery Dashboard. This study aims to analyze and prove the hypothesis that occurs in the current account (X1), capital

account (X2), and financial account (X3) on the balance of payments (Y), which is tested empirically using the Warp PLS 7.0 statistical tool. The results show that not all of them affect the balance of payments. Current account (X1) output has no effect on the balance of payments. Because the P value is above 5%, it has no effect on the Balance of Payments (Y). Meanwhile, Capital Accounts (X2) and Financial Accounts (X3) have an influence on the Balance of Payments which has a P value of less than 5%.

**Keywords:** current account, capital account, financial account, and balance of payments

### 1. Introduction

Balance of payments (BOP) is an overview that summarizes transactions between residents of a country and residents of another country over a certain period (usually one year). Balance of payments for purchases and sales of goods and services, grants from individuals and governments, and transactions. The balance of payments is divided into capital and financial transactions, balance of transactions, and financial items. However, what is included in the international balance of payments is only international economic transactions, while military aid transactions are not included in it.

According to the IMF (1993), the Balance of Payments Manual (BPM) is a systematically compiled record of all economic transactions including trade in goods / services, financial and monetary transfers between residents of a country and residents of other countries for a period of time.

Such as the fact that a country's balance of payments records transactions made by its residents with residents of other countries residents here in terms are:

- Individual / individual: an individual who does not represent a government for example a tourist, a population where they have a permanent residence or a place where they find a "center of interest". To determine the center of interest, it is measured by where they reach a fixed stage or where they work.
- Legal entity, the definition of a legal entity as a resident of a branch of a country is when a business has obtained the status of a legal entity and if a company has overseas company branches, the said branch is considered a resident abroad.
- The government, the population of the country it represents, for example, is a diplomat where the transactions they carry out in other countries are as international economic transactions.

The balance of payments policy is an integral part of development and has an important role in stabilizing stability in the economic sector aimed at promoting equitable development, economic growth and expansion of employment opportunities. In addition, efforts will be made to achieve fundamental changes in the structure of production and foreign trade so as to increase Indonesia's economic resilience to domestic challenges and world economic shocks, as outlined in the Outlines of State Policy. Because with this kind of record the government can see how to manage finances in economic relations with other countries and help regulate international finance, fiscal, trade, and payments.

In the trade sector, the balance of payments is to increase the efficiency and productivity of the domestic industry, support the development of non-oil and gas exports, increase price stability and supply of goods needed domestically and support an increasingly attractive business climate for investment.

Policies in the field of foreign loans that complement domestic development financing needs, and are directed at maintaining stability in the total balance of payments development. The tool policy is directed at encouraging non-oil and gas exports and supporting domestic driving.

In analyzing international trade carried out by a country, the calculation of the profit and loss achieved by the country can be seen from the balance of payments, as various transactions that have been carried out by a country against other countries.

Therefore, this study aims to determine the balance of payments that occur in European countries. The results of the study found that the higher the balance of payments made, the capital and financial transactions would increase and the lower the balance of payments made, the current account would decrease.

## 2. Literature Review

### 2.1 Balance of payments

The balance of payments is a systematic document of all economic transactions between residents of one country for a certain period of time, usually one year. The residents here are individuals, legal entities and governments. Individuals are people who reside and have a livelihood in the country. (Apridar, 2009: 135)

Hady (2009: 59) defines balance of payment (BOP) as a systematic compiled record of all economic transactions which include trade in goods or services, financial and monetary transfers between residents of a country and residents of abroad (rest of the world) for a certain period of time, usually one year.

The definition of the international balance of payments (Balance of Payment) is a systematically compiled record of all economic transactions including trade in services, financial and monetary transfers between residents of a country and foreign residents (rest of the world) for a certain period, usually one year (Hady, 2001).

### 2.2 The Purpose of Preparing a Balance of Payments

1. Knowing the role of the external sector in the economy of a country.

The role of the external sector is reflected in, among others, the large demand for domestic products by non-residents, or vice versa. The greater the demand for domestic products by non-residents, which is reflected in the export value of the country concerned, the greater the role of the external sector in the formation of domestic products.

2. Knowing the flow of resources between countries.

Based on the balance of payments, it can be seen how much the flow of resources between a country and other countries so that it can be seen whether the country is an exporter of goods and or capital, or vice versa as an importer of goods or capital.

3. Knowing the economic and trade structure of a country  
By observing the development of the balance of payments, it can be seen the general pattern of a country's economic activity in interacting with other countries, such as the dependence on national income sources from the export of agricultural products and the dependence on investment financing sources from other countries.

4. Knowing the foreign debt problems of a country  
Based on the records of capital and financial transactions in the balance of payments, it can be seen how far a country can fulfill its obligations to other countries.

5. Used as a source of data and information in preparing the foreign exchange budget (foreign exchange budget).

By paying attention to the balance of payments surplus or deficit in a certain year, the amount of foreign exchange needed for the following year's budget can be needed, as well as the amount of loan required.

### 2.3 Balance of Payments Components

#### a. Current Account

Current Account is all transactions of goods and services that are recorded in the trade balance, if the transfer balance does not exist or is zero. The components in the current account are as follows.

- The goods trade balance (visible trade), which consists of non-monetary goods and gold.
- Services balance (invisible trade), which is payment of compensation for the use of production factors consisting of transportation and insurance costs, tourism proceeds, capital income, government, post and telecommunications, and other services including debt interest payments.
- A surplus current account shows that on the trade balance the amount of exports is greater than imports. Conversely, if the trade balance is deficit, it means that imports are greater than exports.

#### b. Capital Account

Matters that are included in a capital account transaction, namely all records containing capital transactions as follows.

##### 1. The public sector, which includes

- Receipt of loans and assistance;
- Repayment of the loan.

##### 2. The private sector, which includes

- Direct investment
- Portfolio investment.

#### c. Financial Account

In macroeconomics, a financial account is a component of a country's balance of payments that covers claims on or liabilities to nonresidents, specifically with regard to financial assets. Financial account components include direct investment, portfolio investment and reserve assets broken down by the sector.

When recorded in a country's balance of payments, nonresidents 'claims made on residents' financial assets are liabilities, while claims made against nonresidents by residents are assets.

### 2.4 Balance of Payments Stages

Each country tends to have several stages in its balance of payments, from young debtor countries to intermediate creditor countries.

1. Young debtor countries, where at this stage a country imports more than exports, the difference between the two is covered through foreign loans, allowing the country to accumulate capital.

2. Middle debtor countries where at this stage the trade balance of a country has been a surplus, but the growth in dividends and interest that must be paid for foreign loans makes the balance of the capital account less balanced.
3. A young creditor country where at this stage a country develops its exports tremendously, even the country lends money to other countries.
4. Middle creditor countries where at this stage capital income and foreign investment provide a sizeable surplus against invisible items, which are then balanced against the trade balance deficit.

**2.5 Problems in Balance of Payments Analysis**

1. Often neglecting international transactions with each other, so that an imbalance in the balance of payments is associated with one transaction alone regardless of its relationship to another. Example: investment abroad is considered to increase the deficit in the balance of payments, because it causes capital outflows. However, if viewed further, this investment will later support the export of raw materials or other activities. Likewise, the provision of assistance from other countries will increase the balance of payments deficit, even though most assistance (especially from developed countries) is in the form of assistance in the form of money spent domestically or tied aid, which means that the assistance is used to buy goods produced by the donor country help.
2. A surplus in an ongoing transaction is often considered good, whereas a deficit is considered bad. This kind of assumption is not always true. There is no need to worry about deficits or surpluses in the current account as long as the deficit or surplus is balanced by the same amount of capital inflows or outflows.
3. The decision to provide aid (aid) should be based more on the overall economic strength of the State (for example, measured by per capita income) rather than on the basis of balance of payments considerations. For

example, Indonesia has a surplus in its balance of payments, while Britain has a deficit, it does not mean that Indonesia has started providing assistance to Britain.

**3. Method**

This research uses Warp PLS version 7.0 software and Smart PLS 3.0 running on the computer media. The data collection method uses secondary data sourced from the eurostat database. The population of this study includes several countries on the European continent, the data of the variables studied are Current Account, Capital account, and financial account on the balance of payments. The research sample was 20 countries and used data from the last four (4) years. The following is data from research variables:

**Table 1:** Operation Variable

Variable	Indicators	Scale	Measurement
Several Components Affecting the Balance of Payments in Europe	Current Account	Nominal	Nominal
	Capital Account	Nominal	Nominal
	Financial Account	Nominal	Nominal

Analysis with SEM Warp PLS still requires several suitability indices to measure the correctness of existing indicators.

**4. Result and Discussions**

**4.1 Result**

**4.1.1 Descriptive Data**

The following data are the results of testing using the Smart Pls 3.0 statistical tool, the results show descriptive statistics of the variables Current Account (X1), Capital account (X2), Financial Account (X3), and Balance of Payments (Y). Where will be found the mean, median, minimum value, maximum value, standard deviation, excess kurtosis and skewness of each variable and of the eighty (80) total samples. The results show:

**Table 2:** Descriptive Statistic

Data	No	Missing	Mean	Median	Min	Max	St. Deviation	Excess Kurtosis	Skewness
X1	1.000	0.000	2.862	2.000	-2.000	25.000	3.040	34.990	5.027
X2	2.000	0.000	64.862	53.000	29.000	221.000	40.718	7.371	2.607
X3	3.000	0.000	63.263	48.000	26.000	323.000	44.566	15.046	3.404
Y	4.000	0.000	29515.875	27720.000	5940.000	95170.000	18980.648	3.930	1.814

Source: Result Test of SmartPLS (2021)

**4.1.2 Goodness of Fit Model Test**

The model fit indicator is based on three indicators; the mean path coefficient (APC), the R-Squared average (ARS) and the mean variance inflation factor (AVIF). P values are given for

both the APC and ARS indicators calculated by resampling estimation and Bonferroni correction (Sholihin & Ratmono, 2013). The results show:

Model fit indices and P values
Average path coefficient (APC)=0.293, P=0.001
Average R-squared (ARS)=0.148, P=0.042
Average adjusted R-squared (AARS)=0.114, P=0.073
Average block VIF (AVIF)=16.716, acceptable if <= 5, ideally <= 3.3
Average full collinearity VIF (AFVIF)=2.199, acceptable if <= 5, ideally <= 3.3
Tenenhaus GoF (GoF)=0.385, small >= 0.1, medium >= 0.25, large >= 0.36
Sympson's paradox ratio (SPR)=0.333, acceptable if >= 0.7, ideally = 1
R-squared contribution ratio (RSCR)=0.608, acceptable if >= 0.9, ideally = 1
Statistical suppression ratio (SSR)=1.000, acceptable if >= 0.7
Nonlinear bivariate causality direction ratio (NLBCDR)=0.833, acceptable if >= 0.7

Source: Result Test of WarpPLS (2021)

Thus, the APC and ARS values are significant at the alpha level below 5% and the AVIF value below the 5 value, indicating that the model is suitable.

**4.1.3 Analysis on the Test of Qualitative Data**

Of the 80 questionnaire data distributed, it is used as an indicator of convergent validity which is part of the measurement model in SEM-PLS. The output is expected to show the construction on the column and the indicator on the existing row, the following results are obtained:

\*\*\*\*\*  
 \* Combined loadings and cross-loadings \*  
 \*\*\*\*\*

**Table 3:** Qualitative Data

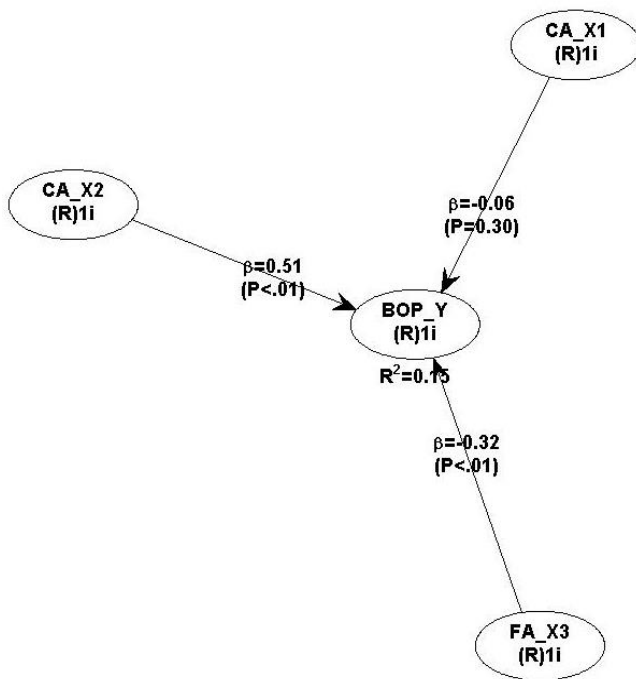
	CA_X1	CA_X2	FA_X3	BOP_Y	Type (aSE)	P value
X1	1.000	-0.000	0.000	0.000	Reflect0.083	<0.001
X2	-0.000	1.000	-0.000	-0.000	Reflect0.083	<0.001
X3	0.000	-0.000	0.000	0.000	Reflect0.083	<0.001
Y	-0.000	0.000	1.000	1.000	Reflect0.083	<0.001

Source: Result Test of WarpPLS (2021)

Notes: Loadings are unrotated and cross-loadings are oblique-rotated. SEs and P values are for loadings. P values < 0.05 are desirable for reflective indicators.

**4.1.4 Hypothesis Testing**

The result of hypothesis testing on the data above is that the Current Account (X1) output has no effect on the balance of payments (Y) and the output of the Capital Account (X2) and the Financial Account (X3) has a greater effect on the balance of payments (Y). The following is testing of the partial coefficient individually of each independent variable can be seen in the following figure:



Source: WarpPLS result test (2021)

**Fig 1:** Testing Result WarpPLS 7.0 (2021)

**4.2 Discussion**

From the results of the above discussion, Current Account (X1) output has no effect on the balance of payments.

Because P values are above 5%, it has no effect on the balance of payments (Y). Meanwhile, Capital Accounts (X2) and Financial Accounts (X3) have an influence on the Balance of Payments, which have P values below 5%.

In addition, R-squared shows the variation in the relationship of all variables from the independent variable to the dependent variable, explaining the magnitude of the relationship is 0.148 or 14.8%, which means that the variables Current Account (X1), Capital Account (X2), and Financial Account (X3) explain the variations. to Y is 14.8% and Adjusted R-squared shows the value of the determination coefficient which has been adjusted to the variation of the relationship between X1, X2, and X3, namely 0.114 or 11.4%. So “Adjusted R-squared <R-squared”

**5. Conclusion**

Current Account Output (X1) has no effect on the Balance of Payments (Y). So that the European Union must increase current asset activities in the form of exports to other countries and reduce imports from other countries. In order to increase income from an economic perspective and increase transactions in the balance of payments.

In addition, the output of Capital Accounts (X2) and Financial Accounts (X3) must be further increased because they significantly affect the balance of payments, thereby generating profits for the European Union and increasing economic activity.

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