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What Is the Balance of Payments?

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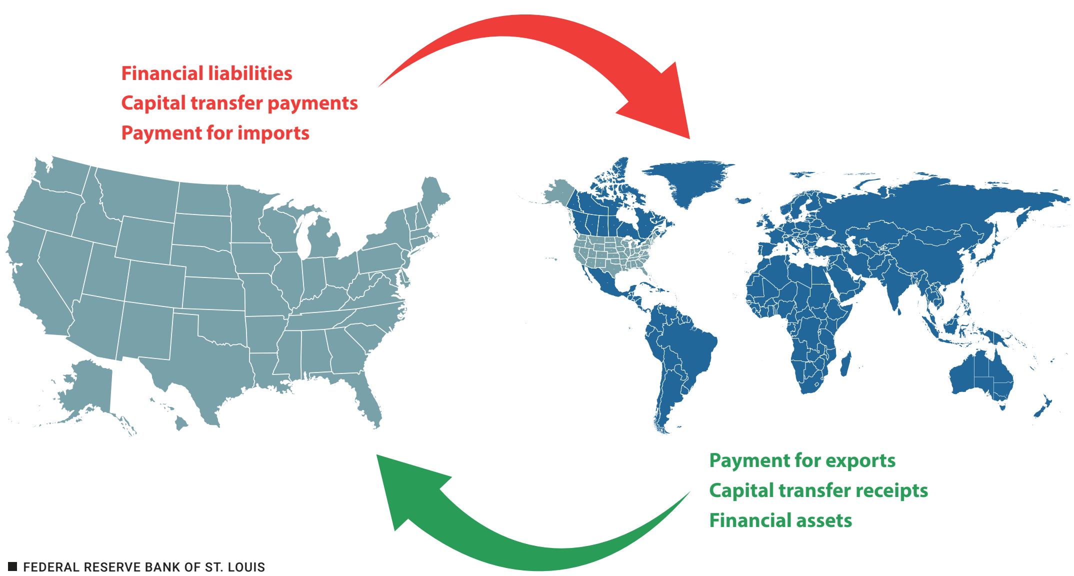
A lot of attention is paid to the importing and exporting of goods and services, but there are other types of economic transactions between countries that trade with each other. Countries need a way to record not just the movement of goods and services between trading partners, but also the debit and credit of other financial transactions and investments.

Enter the Balance of Payments

The **balance of payments** is an accounting system; it is a summary of all the transactions involving goods, services, and investment between one country and all other countries over a given time. Any transaction that causes money to flow into a country is a credit to balance payments accounts, and any transaction that causes money to flow out is a debit.

Trade involves the movement of goods and services, but there are also many other transactions recorded in balance of payments accounts. Transactions between countries can be divided into three general categories: exports and imports, capital transfer receipts and payments, and financial assets and liabilities, as shown in the graphic below.

International Trade Transactions Circular Flow



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When money is received by the U.S. it is recorded as a credit in the balance of payments. When money leaves the U.S. as payment it is recorded as a debit in the balance of payments.

Capital transfer receipts and payments are capital (money or assets) that are transferred from one country to another. For example, a capital transfer can be the interest you receive on a savings account balance at a foreign bank or the money sent to someone in another country as a gift. Financial assets and liabilities refer to borrowing and lending in foreign markets. For example, you purchase stock on a foreign stock exchange or take out a loan from a foreign bank.

Examples of Transactions Recorded in the Balance of Payments

Exports	Capital transfer receipts	Financial assets
Resources, goods, and services produced domestically but sold abroad	• Interest received • Remittances received	• Buying stock • Buying bonds • Making a deposit in a bank account
Imports	**Capital transfer payments**	**Financial liabilities**
Resources, goods, and services produced abroad but sold domestically	• Interest paid • Remittances paid	• Taking out a loan • Issuing bonds

NOTE: Income earned on foreign assets (such as interest and dividends) is recorded in the current account, while the purchase or sale of the assets themselves is recorded in the financial account.

Is Balance of Trade Different from Balance of Payments?

While the balance of payments is a record of the flow of money used to make all international sales and purchases, the **balance of trade** refers to "net exports," or the amount of goods and services sold abroad minus the purchases of goods and services from other countries. The balance of trade is just one part of the balance of payments. In the table above, the balance of trade would be the total of only the first column, while the balance of payments would include all three columns.

The transaction categories in the table are divided into two broad accounts: the current account and the capital and financial account. The current account is the section of a country's balance of payments that records its exports and imports of goods and services, its net investment income, and its net transfers. (Note that the table is a sample of the types of transactions recorded in the balance of payments and is not a complete list.) The capital and financial account is the section of a country's balance of payments that records movements of capital into and out of a country. Balance of payments is a form of double-entry accounting, meaning every credit has a corresponding debit. In other words, current account + capital and financial account = 0.

To learn more about the balance of trade and how it is recorded in balance of payments accounts, read this *Page One Economics* article on international trade.

Why Does the Balance of Payments Equal Zero?

As an accounting principle, a buy (debit) for one country is a sell (credit) for another. In a closed system, as shown in the above graphic, the money must be accounted for as either a credit or a debit. There is no money "leakage" between trading partners. This is an extension of the **circular flow model** in which an expenditure for one person becomes income for the other person.

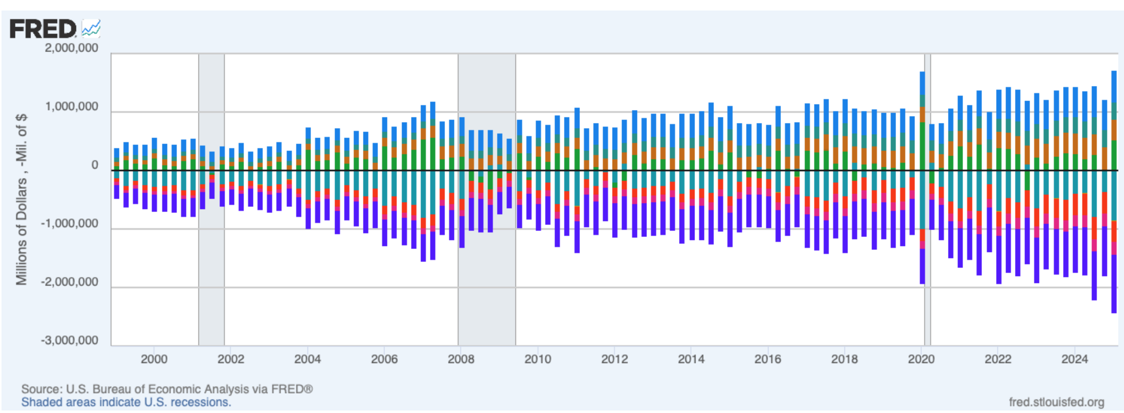
Let's look at an example. Country A purchases a good from Country B. Country B must now decide what to do with the currency it receives for the sale of the good to Country A. Country B could do one of the following:

1. Hold the currency as a cash reserve.
2. Use the currency to purchase something from Country A or invest in a financial asset in Country A.
3. Exchange the currency on the foreign exchange market for a different currency.

Most of the time, a country will choose the above option 2 and use the foreign currency it receives to make investments or other purchases from the original country. In our example, this would mean Country B receives funds for a good it sells to Country A but then uses the same currency to purchase a financial asset, such as a bond, from Country A. When this is done, there is an inflow in financial capital to Country A. So, while you might have a trade deficit in goods and services (current account), it is often offset by a surplus in financial transactions (capital and financial account). In our example, this would mean Country A has a debit for the purchase of a good from Country B, but then has a credit when Country B invests in a financial asset in Country A.

We can see this play out when we look at the U.S. balance of payments in the FRED graph below. You'll notice that the total financial inflows—everything above the zero line—is mirrored in the financial outflows—everything below the zero line. While not all catagories of transactions are perfectly mirrored, the totals are generally symmetrical.

U.S. Balance of Payments



SOURCE: [U.S. Balance of Payments](), U.S. Bureau of Economic Analysis via FRED, Federal Reserve Bank of St. Louis; accessed August 26, 2025.

To learn more about the U.S. balance of payments, read this FRED Blog from July 2025.

Conclusion

Balance of payments is a valuable tool used to assess how a country interacts in world markets. By exploring the different categories of transactions, we can learn a lot about a country's economy and its relationships with trading partners. The balance of payments may be a challenging concept at first, but if we keep in mind that an expenditure for one person becomes income for someone else, it is much easier to understand how this accounting system attempts to track a country's global transactions as a series of credits and debits.

Glossary

Balance of payments: A summary of all the transactions involving goods and services and investment that all individuals, firms, and the government of one nation makes with all of those in all other nations in a given time period.

Balance of trade: The difference between a country's total exports and total imports. Also known as "net exports."

Circular flow model: An economic model illustrating the exchange of resources, goods, and money in an economy.

References

"The US balance of payments." Federal Reserve Bank of St. Louis FRED Blog, July 28, 2025.

Wolla, Scott. "International Trade: Making Sense of the Trade Deficit." Federal Reserve Bank of St. Louis *Page One Economics*, November 2016.

Name_______________________________________ **Period**________

Reading Q&A

What Is the Balance of Payments?

After reading the article, complete the following:

1. Which of the following best describes the balance of payments?
   a. It records only the importing and exporting of goods and services between countries.
   b. It is a summary of all financial transactions between one country and all other countries.
   c. It tracks only the movement of investments between trading partners.
   d. It is used exclusively to record the debit and credit of goods and services.

2. Which of the following is an example of a financial asset that would be recorded in the balance of payments?
   a. Your grocery purchases at the local grocery store
   b. Your purchased stock in your favorite foreign car company
   c. Interest received on your savings account at a foreign bank
   d. Imports sold to a country

3. Which of the following is an example of a capital transfer that would be recorded in the balance of payments?
   a. Your grocery purchases at the local grocery store
   b. Your purchased stock in your favorite foreign car company
   c. Interest received on your savings account at a foreign bank
   d. Imports sold to a country

4. How would the following transaction be recorded in the balance of payments? The U.S. receives payment for exports of airplanes to France.
   a. A debit on the U.S. balance of trade
   b. A credit on the French balance of payments
   c. A debit on the U.S. balance of payments
   d. A credit on the U.S. balance of payments

5. How would the following transaction be recorded in the balance of payments? British foreign investors purchase U.S. Treasury bonds.
   a. A credit on the U.S. balance of payments
   b. A debit on the U.S. balance of payments
   c. A credit on the British balance of payments
   d. A credit on the British balance of trade

6. What is the balance of trade?
   a. The total amount of a country's exports minus its imports
   b. The sum of all financial transactions between one county and all other countries
   c. The total exports of a country plus its total imports
   d. All the trade deficits in a country's history plus its trade surpluses

7. Which of the following best describes the relationship between the balance of trade and the balance of payments?
   a. The balance of trade is the total flow of money used to make all international transactions, while the balance of payments includes only goods and services.
   b. The balance of payments records all international transactions, while the balance of trade focuses specifically on the difference between exports and imports.
   c. The balance of trade includes all financial transactions, while the balance of payments tracks only net exports.
   d. The balance of payments is part of the balance of trade, focusing on the flow of goods and services.

8. Why does the balance of payments generally equal zero?
   a. Money must always be accounted for as either a credit or a debit.
   b. Countries cannot exchange currencies on the foreign exchange market.
   c. A buy for one country is always a sell for another country.
   d. Financial transactions are independent of trade in goods and services.

9. What are the possible actions a country can take with the currency it receives from international markets?
   a. Hold it as a cash reserve, use it to purchase products or investments from the original country, or exchange it on the foreign exchange market.
   b. Use it to purchase goods or to invest in financial assets in the currency's origin country.
   c. Exchange it on the foreign exchange market or hold it as a cash reserve.
   d. Use it to purchase financial assets in its own country or hold it as a cash reserve.

10. What does a country most often do with the foreign currency it receives?
   a. It holds the foreign currency as a cash reserve.
   b. It exchanges the foreign currency for a different currency.
   c. It uses the foreign currency to make investments or other purchases in the country from which it was received.
   d. It spends the foreign currency domestically.