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PROGRESS REPORT ON BALANCE OF PAYMENTS STATISTICS

(Memorandum prepared by Balance of Payments Division of the International Monetary Fund)

I. Revision of Balance of Payments Manual

1. The Fund's Progress Report presented to the tenth session of the Commission described the drafts of the goods and services, and transfer payments accounts which had been prepared as part of the revision of the Fund's Balance of Payments Manual. The revised version of these accounts was not introduced as a basis for reporting, however, pending a revision of the capital account. The revision was prepared mainly to introduce certain changes intended to co-ordinate the Manual with the OEEC and United Nations systems of national accounts, which had been discussed with these two organizations. The draft also proposed certain changes in the principles for classifying international transactions by countries and areas. Other changes were intended to clarify the exposition of the reporting schedule and its explanatory notes. In general, the changes proposed were believed to be of comparatively little significance for the actual reporting of statistics. They tended, for the most part, to adapt the Manual to existing statistical practices.

2. Drafts of the remaining sections of the Balance of Payments Manual were prepared during 1959. A draft of the capital account tables and notes was circulated for comment to the Fund's statistical correspondents in August of that year, and a second draft of this section in preparation will take into account comments received from member countries, as well as the advice of a group of national experts on balance of payments statistics which met with the Fund staff

in October 1959 to review the proposed formulation. A draft of the introductory sections of the Manual, which discusses the basic concepts and accounting framework of the balance of payments, has also been prepared and will be included in a final draft of the complete Balance of Payments Manual, which is expected to be available for distribution at the tenth session of the Statistical Commission, although it may not be possible to circulate the final draft to countries in advance of this meeting.

3. In preparing the draft of the revised Balance of Payments Manual, the Fund staff has recognized the need to take account of developments in other social accounts and to co-ordinate the concepts and logical framework of the balance of payments with these accounts, especially with the United Nations and OEEC systems of national accounts and with statements developed recently to record the financial transactions of the sectors of an economy.

4. The underlying principles for the balance of payments as drafted in the revised Manual introduce the balance of payments in the larger context of the social accounts. Thus, the revised Manual not only explains how the individual categories of the balance of payments relate to those of national income and product accounts and statements of sector finance, but gives a brief exposition of the accounting principles for all the social accounts and of those basic concepts which they have in common.

A. The underlying principles and basic methodology

5. The principles for recording transactions in the balance of payments and in other social accounts are mainly the same although there are certain differences in structure between the balance of payments, on the one hand, and national accounts and sector finance statements, on the other.

6. Both the balance of payments and the other social accounts cover economic transactions between economic units and apply the same rules of credit and debit. However, whereas the balance of payments records (with a few exceptions) transactions between residents and foreigners and covers only the resident aspect of such transactions, the national income and product accounts and statements of sector finance record transactions both between residents and between residents and foreigners and cover each economic transaction from the standpoint of both

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parties to the transaction. The balance of payments may thus be characterized as an open system for recording economic transactions, whereas the national income and product accounts and sector finance statements represent closed systems. The revised Manual analyses the implications of this difference for the rules of accounting in the balance of payments and the other social accounts.

7. The balance of payments is usually the source of data for the rest of the world account in national income and product statements and is thus used as a source for checking the estimates for production, investment, and consumption in these statements. The account for goods and services in the balance of payments is defined in such a way that it relates a country's international transactions in goods and services to the economic activity of the domestic economy as accounted for in national income and product statements. Likewise, the transfer payments account in the balance of payments covers the same transactions as transfer payments in the rest of the world account of national income and product statements and provides data for reconciling national product and disposable income for the economy as a whole.

8. Sector finance statements usually distinguish changes in the domestic sectors' foreign assets from changes in their domestic assets. The capital account of the balance of payments covers the same changes in foreign assets as those recorded in the sector finance statements and provides additional data on the type of assets; the net change in foreign assets as shown in the balance of payments is equivalent to the net change in the foreign assets of all the domestic sectors combined, as shown in sector finance statements as changes in the liabilities of the rest of the world. Likewise, the net change in foreign liabilities within each category as recorded in the capital account of the balance of payments represents the net balance of the transactions of all domestic sectors in the appropriate type of domestic financial assets, as recorded in sector finance statements, which in these statements in turn is recorded in the rest of the world account with opposite sign.

9. The Manual distinguishes three basic types of transactions recorded between economic units, i.e., transactions in goods and services, transfer payments, and transactions in financial claims. The balance of payments records only transactions between economic units, whereas national income and product

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statements, unlike other social accounts, include in addition some flows internal to the economic unit.

10. The transactions recorded in the balance of payments take place mainly between residents and foreigners. There are, however, several exceptions to the resident-foreigner principle, all of which are made for the purpose of giving a statement suitable for the analysis of economic relations between the domestic economy and the rest of the world. The most important exceptions are the following:

(i) Those arising from the uniform valuation of merchandise. Transactions in merchandise are valued uniformly at the customs frontier of the exporting country for both exports and imports. This uniform valuation implies: (a) That freight and insurance incurred for transfer of goods to the customs frontier, if in exceptional cases they represent transactions between a resident of the exporting country and a carrier or insurer of the importing country, have to be entered in the balance of payments of both the exporting and the importing country to offset the overstatement of receipts and payments, respectively. The exporting country records a freight payment offsetting the overstatement of export receipts; the two offsetting entries representing a transaction between foreigners. The importing country records a freight receipt offsetting the overstatement of import payments; these entries represent a transaction between residents. (b) That freight and insurance incurred by the exporter for transfers of goods beyond the customs frontier of the exporting country have to be omitted from the balance of payments of that country. This omission is rationalized by construing these costs as transactions between the importer and the carrier or insurer, the exporter acting in behalf of the importer in arranging international transportation and insurance.

(ii) Those arising from the principles followed in recording changes in foreign assets and liabilities. All changes in the foreign assets and liabilities of the compiling country resulting from economic transactions are in principle reflected in the balance of payments. This principle implies that certain offsetting changes in the distribution by sector of the compiling country's foreign assets resulting from transactions

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between residents, and, in exceptional cases, even certain changes in the distribution by holder of its foreign liabilities resulting from transactions between foreigners are included in the balance of payments in addition to the changes in the country's foreign assets and liabilities that result from transactions between residents and foreigners.

(iii) Those arising from the treatment of monetary gold as a foreign asset. By the convention adopted in the Manual, gold transactions are classified institutionally, i.e., all such transactions by monetary institutions, whether with other residents or with foreigners, are entered in the capital account, and all such transactions by non-monetary sectors, whether with resident monetary institutions or with foreigners, are entered in the goods and services account. A similar convention is employed in the United Nations and OEEC systems of national accounts.

11. The residents of a country are the economic units comprising the domestic economy. The concept of territory is not relevant in the balance of payments context, except in the sense that residents are those economic units that have a certain permanent association with the territory of the reporting country. This interpretation of the concept of resident is common to the Manual and the United Nations and OEEC systems of national accounts. When an enterprise operates in more than one country and separate units of the enterprise (such as branches and subsidiaries) can be distinguished, each unit is considered as a resident of the country in which it operates. If several countries participate in an enterprise but the participation of each cannot be distinguished as a separate economic unit, the transactions of each country to be entered in the balance of payments may be prorated on the basis of the proportionate ownership of the enterprise. A similar procedure has been established in the United Nations and OEEC standards of national accounting for attributing real capital formation by country. Enterprises using facilities (like railways and pipelines) extending over the territory of several countries are likewise regarded in the revised Manual as residents of the countries over which their facilities extend in order to preserve consistency between balance of payments and national accounts concepts. The revised Manual tentatively accepts the national accounts convention of treating fixed assets

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that are owned by non-residents as part of domestic capital in the national accounts because they are located on domestic territory. This implies that such fixed assets are regarded as part of financial rather than real capital from the standpoint of the owning country.

12. The rigid application of the territorial principle to the definition of domestic capital formation in the national accounts in some cases results, however, in artificial and complicated procedures for recording economic transactions. It is therefore felt that the principle should be reconsidered, both in the balance of payments and the other social accounts. The treatment of all fixed assets on domestic territory as part of domestic capital formation may have resulted from the notion that domestic capital formation is a member of a family of national accounts concepts (characterized by the adjective "domestic") that are based on the territorial idea. The national accounts systems define an economy alternatively in terms of the territorial concept and as the sum of residents. Domestic product has traditionally been related to the territorial definition of the economy, and national product to the resident definition. As argued in the report entitled "UN-OEEC-IMF discussions to co-ordinate the Balance of Payments Manual, A Standardised System of National Accounts and A System of National Accounts and Supporting Tables" (16 November 1956), even the concept of domestic product can be defined more adequately in terms of the resident than in terms of the territorial definition of the economy. Domestic product does not necessarily represent value added on domestic territory, but rather value added in the domestic economy as measured by factor income payments made by resident economic units. Similarly, domestic capital formation is not capital formation on domestic territory, but rather real investment by residents. That domestic capital formation is a resident rather than a territorial concept is apparent from the fact that it includes changes in inventories owned by residents but held outside the territorial boundaries, but excludes changes in inventories held by foreigners on the domestic territory. There is no conceptual reason why fixed assets on domestic territory <u>must</u> be included in domestic capital formation. The criterion for classifying investment as domestic capital formation should rather be whether the assets are employed in an economic process that can realistically be regarded an integral part of the domestic economy. Exceptions to the

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classification of fixed assets on domestic territory as domestic capital might well be made where their classification as foreign-owned fixed real assets (like foreign-owned inventories) would seem more realistic and would, hence, simplify accounting procedures.

13. Such an exception might be made, for example, for embassy buildings. The buildings owned by foreign embassies are treated in the national accounts as domestic capital in the country in which they are located, implying that they provide services (measured by their rental value) in their capacity of residents to the embassies, which themselves are foreigners. In this way an embassy, which can most realistically be regarded as a single economic unit, is divided into two: a resident (the building), and a foreigner (the embassy as the agency of a foreign Government). Although the classification of the embassy proper, and of the embassy staff, as non-residents, is often justified by their extraterritorial status, the classification of the embassy building as a resident, which is implied in its treatment as domestic capital, is justified by its location on domestic territory. It would seem more realistic to treat the embassy building as extraterritorial like the embassy staff or, preferably, to dispense wholly with the concept of territory in the national accounts as in the balance of payments except for its application in determining who is a resident. A resident, of course, is a resident of a certain territory, but except for this application, the concept of territory is both unnecessary and misleading.

14. Other cases where the rigid classification of fixed assets as domestic capital may lead to unnecessarily complicated accounting procedures in the national income and product accounts as well as in the balance of payments refer to transportation facilities (such as pipelines or extensions of foreign railways) serving mainly foreign economies. In some cases it seems unrealistic to regard such facilities as an integral part of the economy of the country on whose territory they are located, and it would seem desirable that the principles for national accounting and the balance of payments should be sufficiently flexible to make their treatment as non-residents possible.

15. Before the final version of the revised _Manual_ is issued, the Fund staff will discuss these questions again with the secretariats of United Nations and OEEC, and it is hoped that it will be possible to arrive at a single definition

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of an economy, based on the resident concept, which can be applied to the _Manual_ as well as the national accounts. This should result in considerable simplification of the accounting frameworks of all three systems.

B. The revised capital account

16. The revised version of the capital account of the _Manual_ involves more extensive changes than any of the other accounts for two reasons: (a) the revised capital account considers the new forms of statistics on domestic finance that are now being developed in several countries and recognizes the importance of a co-ordination between the capital account and domestic sector finance statements, and (b) the exposition of the revised capital account has been considerably changed in order to clarify the concepts and definitions employed.

17. The basic changes introduced in the revised capital account are the following: (a) the sectoring of the economy has been expanded, (b) the sub-classification into long-term and short-term assets and liabilities has been de-emphasized, and (c) the principle of assigning transactions in long-term capital to the sector actually carrying them out (the transactor principle) has been relinquished in favour of the creditor-debtor principle.

18. The revised capital account distinguishes five sectors of the compiling country. There are two sectors for the monetary institutions whose balance sheets are recorded in the Monetary Surveys of the Fund's monthly bulletin, _International Financial Statistics_, one sector covering central monetary institutions (central bank, exchange stabilization fund, etc.) and the other covering other monetary institutions, mainly commercial banks. Furthermore, the compiling country's central government and its local governments are distinguished, and lastly there is a residual private sector.

19. The sectoring is carried out on an institutional basis, but the border line between the sectors depends on the function of the transactions undertaken by the various institutions. Therefore, a government institution having a monetary function (say a government-operated deposit bank) is included in a monetary sector rather than in the central government sector, and a public corporation whose international transactions are more like those of a private enterprise than those of a public corporation that is a mere instrument of central government policy is

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included in the private sector. In borderline cases, the Manual classification by sector gives priority to comparability with national statements of sector finance rather than to the comparability of data between countries.

20. The traditional, formal distinction between long-term and short-term assets and liabilities is applied in the revised capital account only to the private and central government sectors. The distinction is considered to be unimportant for the monetary sectors, for whose assets and liabilities, liquidity rather than formal maturity is important in the balance of payments from an analytical point of view, and it is not applied to the local government sector because its holdings of foreign assets and liabilities are usually unimportant in the balance of payments. This sector is distinguished in the Manual only for reconciliation with sector finance statements.

21. Changes in long-term as well as short-term foreign assets and liabilities are, with a few minor exceptions, assigned in the revised capital account to the sector that is creditor or debtor, mainly because the creditor-debtor principle represents a step towards a co-ordination of the balance of payments and sector finance statements. The only significant exception to this principle is that changes in assets and liabilities of the compiling country against the International Monetary Fund are assigned to central monetary institutions whether the transactions are carried out by such an institution or by the central government.

C. Schedule for completion of revised Manual

22. The final draft of the revised Manual takes into account comments received from member countries and has been co-ordinated with relevant statistical standards issued by the United Nations and the Organization for European Economic Co-operation through extensive consultations with these organizations. Nevertheless, it is not proposed to print the final version of the revised Manual until the second half of 1960 nor to make it the basis for balance of payments reports to the Fund until 1961. It is realized that reporting countries need time to familiarize themselves with the new document, and it is also considered desirable to provide a further opportunity for making minor amendments before printing a definitive edition. A final meeting to discuss the co-ordination of the revised Manual with the latest versions of the United Nations and OEEC systems of national accounts (including some amendments to these systems now under consideration) is tentatively scheduled

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for June 1960, and it is hoped that the few minor problems of co-ordinating the basic concepts of the three systems that are still outstanding can be resolved.

23. Although reports will not be requested on the basis of the revised Manual in 1960, countries will be encouraged to use it for reporting purposes on an experimental basis this year wherever possible and to let the Fund staff know of any difficulties encountered in using the new tables or in interpreting the explanatory notes. It is hoped that as a result of such a practical test of the reporting schedule, it will be possible to remove any remaining ambiguities in the text and to improve the explanatory material in other ways. A number of changes have already been made as the result of experience gained through using the revised Manual as a basis for the course in balance of payments techniques given under the Fund's training programme (see next section).

II. Training Programme

24. The Balance of Payments Division has, as mentioned in earlier progress reports, the responsibility for that part of the Fund's training programme in which a course in balance of payments techniques is given. The current balance of payments course is being attended by ten trainees from ten member countries. An added feature in the current course is the availability of the revised Balance of Payments Manual in draft form as mentioned above.

III. Balance of Payments Yearbook

25. As mentioned in the Progress Report to the tenth session of the Commission, The Fund's Yearbooks are designed (1) to publish current balance of payments statements as they become available, (2) to publish reissued data periodically, and (3) to make available, with minimum delay, final data for the most recent period common to all reporting countries.

26. The current loose-leaf volume, the eleventh in the series, contains basic statistics with explanatory notes for the years 1957 and 1958, showing the international transactions of some seventy-five countries. This information brings to date the basic statements in Volumes 5, 8, 9 and 10, and these five volumes together provide a comprehensive record of available balance of payments statistics covering the period 1947-1958. For the majority of countries, regional

details of the basic data are shown, and statistics for the first halves of 1958 and 1959 are given for countries reporting such information. Volume 11 also contains summary statements covering several years for all individual countries.

27. A new feature of Volume 11 is the provisional balance of payments statements in basic form that accompany each monthly issue. These statements make it possible to issue basic data with a minimum of delay; in some instances, the statements have been processed and are ready for distribution within ten days after the Fund receives the underlying statistics from the reporting countries.
