

**IMF COMMITTEE ON BALANCE OF PAYMENTS STATISTICS**  
**RESERVE ASSETS TECHNICAL EXPERT GROUP (RESTEG)**

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**ISSUES PAPER (RESTEG) # 3**

**CLARIFICATION OF CURRENCY OF DENOMINATION**

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## BALANCE OF PAYMENTS TECHNICAL EXPERT GROUP

### ISSUES PAPER (RESTEG) # 3

#### CLARIFICATION OF CURRENCY OF DENOMINATION

1. One of the criteria for an asset to be included in reserve assets is that it is a claim in foreign currency. However, what is meant by a claim in foreign currency—currency of settlement, currency of denomination? And how should assets indexed to another currency be treated? There is no clear guidance in the fifth edition of the *Balance of Payments Manual (BPM5)* on the treatment of such assets.

#### **I. Current international standards for the statistical treatment of the issue**

2. *BPM5* states in paragraph 426 that “The financial assets comprising reserves cannot unambiguously be identified in a meaningful way simply through the application of objective criteria...” The same paragraph goes on to suggest that supplementary information concerning the arrangements would be useful. Supplementary information in this context could be applied to the clarification of the currency of denomination.

3. The *Guidelines* are clearer. In paragraph 24 it states that “the template specifies that only instruments settled (i.e., redeemable) in foreign currency are to be included in the resources and drains (as covered in sections I through III of the Template).” Later it states that “reserve assets must be foreign currency assets” (paragraph 66). In other words, the *Guidelines* regards a foreign currency asset as one that is settled in foreign currency.

4. To reinforce this view the *Guidelines* further states that with regard to denomination and indexation, “instruments denominated in foreign currency or indexed to foreign currency but settled in domestic currency (and other means) are to be reported as memorandum items” (paragraph 25). So, the Template includes a section for reporting such liabilities of the monetary authorities in Section IV(1) (a) and (b), and provides guidance in paragraphs 242, and 247–254. According to paragraph 247, the rationale for including information on these financial instruments is that they resemble instruments that are settled in foreign currency, and although settled in domestic currency could have an impact on the foreign currency liquidity of the monetary authorities—investors could immediately sell the domestic currency proceeds for foreign currency.

5. The guidance in the *External Debt Statistics: Guide for Compilers and Users (Debt Guide)* is consistent with that in *Guidelines*. Paragraph 6.13 states that “the attribution of external debt by currency is primarily determined by characteristics of future payment(s). Foreign currency debt is defined as debt that is payable in a currency other than the domestic currency.” The *Debt Guide* also defines what it means by domestic and foreign currency (paragraph 6.12). A domestic currency is defined as “that which is legal tender in the economy and issued by the monetary authority for that economy or for the common currency area to which the economy belongs.” The common currency area covers currency unions and

is also defined in the *Debt Guide*. A foreign currency is a currency that is not the domestic currency.

## **II. Issues arising from the current treatment of currency of denomination**

6. The guidance from the *Guidelines* could be introduced into the new *Manual*, with foreign currency assets being determined by the currency of settlement (redemption). Assets denominated in one foreign currency but settled in another foreign currency could be classified as reserve assets provided the settlement currency is convertible (see Issues paper 2) (and the other reserve asset criteria are met).<sup>1</sup>

7. However, assets denominated in domestic currency but settled in foreign currency while regarded as foreign currency assets could be excluded from reserve assets, along with foreign currency assets indexed to the domestic currency. This exclusion could be on the grounds that assets denominated or indexed to the domestic currency could sustain a significant loss of value in a crisis affecting the domestic currency, the very time when reserve assets are most required to meet a balance of payments financing need, and investing in assets linked to the domestic currency is not good reserve management practice. So, only assets denominated and settled in foreign currency and not indexed to the domestic currency could be regarded as reserve assets.

8. Pooled asset arrangements settled in foreign currency by the issuer could be regarded as foreign currency assets even if some of the underlying assets are denominated or indexed to domestic currency (see the further discussion in Issues Paper 6). If part of the claims denominated in foreign currency were to be settled in domestic currency and part in foreign currency only that percentage settled in foreign currency could be regarded as foreign currency assets.

9. Financial instruments denominated in foreign currency and settled in domestic currency (and other means), such as sovereign debt, indexed securities, nondeliverable forwards (NDFs) contracts and NDFs options, would be excluded from reserve assets (but continue to be reported as a memorandum item to the Data Template).

## **III. Possible treatments**

10. It is proposed that the treatments in the *Guidelines*, as described above, be introduced into the new *Manual*. Also a definition of domestic currency, based on that in the *Debt Guide* could be introduced.

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<sup>1</sup> Although convertibility might not be sufficient in all such circumstances. In one recent example, a country issued bonds in domestic currency to be settled in a foreign currency, but exchange controls limited the amount of foreign currency that could be taken from the country.

**IV. Points for discussion**

11. *Are the proposals set out in paragraph 10 acceptable?*

12. *Should assets denominated in or indexed to the domestic currency be excluded from reserve assets, even if settled in foreign currency?*

13. *Are there further examples of assets that are denominated in one currency but settled in another, that require discussion in the new Manual?*

**References**

*BPM5*, paragraph 426

*Guidelines*, paragraphs 24-25, 66, 242, 247-254

*Annotated Outline*, paragraph 5.56

*External Debt Guide*, paragraphs 6.12-6.13