NOTE 9. THE IMPLICATIONS OF THE EUROPEAN UNION FOR DATA ON EXTERNAL TRANSACTIONS IN THE QUOTA FORMULAS

97. Historically, data on current account transactions have been adjusted to exclude some receipts and payments that would have resulted in unduly large measurements of the size of the external sector. Entrepôt trade and interest flows for countries with significant international or offshore banking activity are examples (see Box 9.1). The adjustment includes only the domestic value added component of these transactions. The question arises as to whether to extend such treatment to the current account transactions of countries that form free trade access or customs unions, notably as in the 15 countries of the European Union (the EU-15).[52] The distinguishing feature of the EU-15 relevant to the issue of whether to adjust the current account data is the extent to which the gross flows that are used for quota calculations have risen in relation to the domestic value added of trade in goods and services among these countries ("intratrade").

98. The elimination of formal trade barriers was a central goal of the creation of the European Union. By 1996, neither tariff nor non-tariff barriers had any significant effect on trade in goods, and important progress had been made on trade in services. Legislative barriers to the free movement of capital and persons had also largely been eliminated. Consequently, intra-community trade has grown more rapidly than trade with countries outside the community. By 1997, the share of total trade (average of imports and exports of goods) accounted for by intra-EU trade increased to 61.2 percent, up by 2.6 percentage points from 1985.[53]

99. Based on the ongoing shifts in the structure and size of trade within the EU and with the rest of the world, there would seem to be a case for treating intra-EU trade on the same basis as entrepôt trade and international banking interest. A similar approach could be recommended for other countries with free trade arrangements, e.g., Canada, Mexico, and the United States in the North American Free Trade Agreement. Implementing such an approach would, however, require estimates of the domestic value-added component of such trade. The compilation of such data requires information to ascertain the import content of exports, or, alternatively, an analysis of the extent to which imports are very highly correlated with exports.

[52] The European Union creates an area without internal frontiers, in which the free movement of goods, persons, services and capital is ensured in accordance with the provisions of the Treaty of Rome in 1957 which established the European Economic Community, as amended by the Single European Act of 1986.

[53] Between the periods 1986–91 to 1992–96, there was also an increase in the share of foreign direct investment in European Union countries that originated from within the Union itself.

100. The effect on the calculated quotas of EU countries of excluding all of the intratrade flows within the EU—i.e., not taking into account any domestic value added of such trade—is illustrated in Table 9.1.[54] The hypothetical calculated quotas would be substantially reduced. In aggregate, the EU-15 countries' share would be reduced by 9.2 percentage points (from about 37.1 percent to about 28.0 percent). The largest declines in percentage points are for Germany, the Netherlands, France, and Belgium.

101. The question may also be raised as to whether it would be reasonable to determine a single calculated quota for the EU-15 countries on the basis of aggregated data. Under the IMF Articles of Agreement, the basis for membership, and therefore the assignment of a quota, is an entity's status as a country (Article II, Section 2). Therefore, unless a group of members becomes a single country, those members would each continue to have individual quotas. More fundamentally, the creation of the economic union, and of the European Monetary Union with its single currency, does not preclude an individual member from running into balance of payments difficulties and requesting appropriate Fund financing.

102. If problems were to emerge with the availability or quality of balance of payments data for individual countries, this could lead to difficulties in calculating their individual quotas. With the advent of monetary union in 1999, the national statistical authorities of the eleven members of EMU are expected to continue to provide GDP, reserves, and balance of payments data at the national levels, including balance of payments data covering transactions with other EMU member states. However, the loss of currency-based information for intra-EMU transactions (especially from 2002 when national currencies will be eliminated) will render certain data sources unusable for example, on capital movements within the EMU and pose certain statistical problems (see Box 9.2). The loss of currency information will, of necessity, lead to greater reliance on survey data, which will likely entail a corresponding loss of accuracy.

[54] Of course, in the case of a merger of territories into one country, the conventional definition of a country's external transactions would preclude the inclusion of trade between such territories. In the quota calculations for merging territories (Vietnam in 1976, Germany, and the Republic of Yemen in 1990), trade between the merging territories was excluded in the data used for the combined entity.

Box 9.1. Adjustments to Current Account Data in Quota Reviews

Current transactions data used in quota calculations are adjusted for those countries with significant offshore banking activity or entrepôt trade:

1. *International Banking Interest*

The practice was established in the Eighth General Review in 1983 adjusting international banking interest (IBI) flows so that they are included on a net, rather than a gross basis in the current transactions data, for those countries with significant international and/or offshore banking activity. IBI flows are interest payments (i) by nonresidents on their borrowings from domestic banks, and (ii) by domestic banks on their borrowings from nonresidents. The inclusion of only net flows is based on the premise that when nonresident deposits with resident banks are used to make loans to nonresidents, only the net interest earnings are indicative of the relative size of the country's external transactions. That is, inclusion of flows on a gross basis would unduly inflate the data used in quota calculations.[1] Inclusion of interest on a net basis requires, in practice, deducting the lower of interest paid and interest earned from the gross data on current receipts and payments. In other words, the "value added" component of IBI is retained in the data for quota calculations. The countries for which IBI adjustments have been made include: Bahrain, the Bahamas, Belgium, Canada, France, Germany, Italy, Japan, Luxembourg, the Netherlands, Panama, Singapore, Sweden, Switzerland, the United Kingdom, and the United States.

2. *Entrepôt trade*

Analogous to the adjustments for IBI, entrepôt trade is included in current transactions data only on a net basis for those countries with significant entrepôt trade. The practice is to retain the value added of a country's re-exports trade in the country's current receipts by deducting entrepôt imports from both gross exports and imports. The countries for which entrepôt trade adjustments have been made include: Bahrain, Brunei Darussalam, Djibouti, Israel, Paraguay, San Marino, and Switzerland.

1/ See "Ninth General Review—Revised Quota Calculations," EB/CQuota/87/5, 12/22/87, pages 1–2.

Box 9.2. Intra-European Balance of Payments Statistics[1]

The introduction of the euro with the start of the third stage of European Monetary Union (EMU) at the beginning of 1999 has posed some difficulties for collecting intra-European balance of payments statistics. At present, the euro and national currencies of EMU members are being used in parallel. It is no longer necessarily possible to distinguish intra-EMU transactions by currency, which makes identification of transactions by country of origin or destination difficult.[2] These difficulties will be exacerbated when national currencies are eliminated at the beginning of 2002.

It may be noted that the most reliable source of information on goods transactions—customs data—has not been available for intra-European Union (EU-15) trade, and therefore intra-EMU trade, since 1993, because of the elimination of customs requirements within the European Single Market. Thus, since that time, most EU-15 intratrade data has been estimated from information on the underlying financial transactions (primarily from the banking system),[3] or from surveys which are usually less reliable than customs-based data.

More generally, the effects of losing currency-based information include:

- Data on credit card transactions would no longer distinguish intra-EMU trade.
- The practice of centralized clearing of accounts by multinational enterprises, which prevents statisticians from accurately observing the source and destination of balance of payments flows, has become more prevalent.
- The introduction of euro notes in 2002 will eliminate an important source of information on certain intra-EMU transactions which are thought to be substantially cash-based, such as tourism.

Furthermore, with EMU's centralized monetary policy, intra-EMU financial flows may have little practical policy implications, which could lessen the priority to be placed on producing the intra-EMU financial accounts in countries' balance of payments statistics.

[1] This information is based, in part, on unpublished papers presented at the Twelfth Meeting of the IMF Committee on Balance of Payments Statistics in Santiago, Chile, October 27–29, 1999, as well as on the 1999 Annual Report of the IMF Committee on Balance of Payments Statistics (forthcoming).
[2] For instance, errors and omissions in Germany's balance of payments were noticeably larger than normal in early 1999.
[3] Most EU-15 countries rely on a reporting system which fails to capture underlying flows that take place outside the country, except for countries with exchange controls. Such flows may be significant. Another difficulty is that the reporting system records underlying transactions on a cash basis, whereas balance of payments data should be on an accrual basis.

Table 9.1. Actual and Calculated Quotas for the EU-15 Countries and Other Members

	Actual Quotas		Calculated Quotas (Including EU-15 intratrade) 1/		Hypothetical Calculated Quotas (Excluding EU-15 intratrade) 2/		Change in Shares
	Amount (In millions of SDRs)	Share (In percent)	Amount (In millions of SDRs)	Share (In percent)	Amount (In millions of SDRs)	Share (In percent)	(In percentage points)
	(1)	(2)	(3)	(4)	(5)	(6)	(6)-(4)
EU-15 3/	64,339.5	30.3	202,449.3	37.1	133,673.4	28.0	-9.156
Germany	13,008.2	6.135	49,132.1	9.007	33,899.1	7.090	-1.917
France	10,738.5	5.065	30,435.0	5.580	21,243.6	4.443	-1.136
United Kingdom	10,738.5	5.065	27,227.4	4.992	19,437.4	4.066	-0.926
Italy	7,055.5	3.328	22,804.1	4.181	15,881.3	3.322	-0.859
Netherlands	5,162.4	2.435	15,442.1	2.831	8,066.8	1.687	-1.144
Belgium	4,605.2	2.172	13,248.5	2.429	6,582.0	1.377	-1.052
Spain	3,048.9	1.438	11,343.3	2.080	7,861.5	1.644	-0.435
Sweden	2,395.5	1.130	6,886.0	1.262	4,722.8	0.988	-0.275
Austria	1,872.3	0.883	6,972.5	1.278	4,420.8	0.925	-0.354
Denmark	1,642.8	0.775	5,450.0	0.999	3,635.9	0.760	-0.239
Finland	1,263.8	0.596	3,463.0	0.635	2,362.0	0.494	-0.141
Portugal	867.4	0.409	3,046.1	0.558	1,686.3	0.353	-0.206
Ireland	838.4	0.395	3,320.4	0.609	1,803.3	0.377	-0.232
Greece	823.0	0.388	2,091.0	0.383	1,476.1	0.309	-0.075
Luxembourg	279.1	0.132	1,587.8	0.291	594.6	0.124	-0.167
United States	37,149.3	17.521	94,099.0	17.251	94,099.0	19.682	2.430
Japan	13,312.8	6.279	55,658.4	10.204	55,658.4	11.642	1.438
Saudi Arabia	6,985.5	3.295	7,159.1	1.312	7,133.9	1.492	0.180
Canada	6,369.2	3.004	17,830.8	3.269	17,769.0	3.717	0.448
Russia	5,945.4	2.804	10,052.3	1.843	10,229.4	2.140	0.297
China	4,687.2	2.211	9,042.6	1.658	9,042.6	1.891	0.234
India	4,158.2	1.961	4,156.0	0.762	4,156.0	0.869	0.107
Switzerland	3,458.5	1.631	8,697.2	1.594	8,697.2	1.819	0.225
Other members	65,623.4	31.0	136,314.3	25.0	137,642.0	28.8	3.799
By WEO group:							
Advanced economies:	133,990.9	63.195	411,706.7	75.479	343,097.5	71.763	-3.716
Major industrial economies	98,372.0	46.396	297,186.9	54.484	257,987.8	53.961	-0.523
Other advanced economies	35,618.9	16.799	114,519.7	20.995	85,109.7	17.802	-3.193
Developing countries	61,922.5	29.205	104,840.4	19.221	105,671.5	22.102	2.882
Net creditors	10,775.0	5.082	15,785.9	2.894	15,922.7	3.330	0.436
Net debtors	51,147.5	24.123	89,054.5	16.327	89,748.8	18.772	2.445
of which: HIPC or least developed countries	7,567.4	3.569	7,210.5	1.322	7,264.7	1.519	0.198
Transition economies	16,115.6	7.601	28,912.1	5.301	29,331.9	6.135	0.835
Total	212,029.0	100.0	545,459.1	100.0	478,100.9	100.0	

1/ As used at the eleventh general review.

2/ Intratrade data are from the IMF's Direction of Trade Statistics database and include merchandise trade data only.

3/ The sum of the EU-15 countries' individual quotas.