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**Chile's Experience in Implementing *BPM5***

**Prepared by the Central Bank of Chile**

## CHILE'S EXPERIENCE IN IMPLEMENTING BPM5

### Background

The adoption of BPM5 standards in Chile's BOP has been the result of a long process which began in the mid-nineties and which is still in progress.

It has taken place in an environment of increasing liberalization, awareness of the importance of good quality and timely statistics, and technological changes. All these factors have had significant effects on data collection and compilation.

### BOP compilation before liberalization

Before this process, the Chilean economy was subject to restrictions on capital flows and other foreign exchange transactions. Although the presence and importance of the different elements in the system varied over time, its main characteristics were:

- Need for authorization -prior to materialization-, of investment, loans, and certain other international transactions.
- Obligation to surrender or buy foreign exchange to/from institutions of the so-called "formal exchange market", which is comprised mainly by banks.
- Certain transactions allowed only for institutions of the formal exchange market.
- Reserve requirements on external indebtedness, limits on banks' net foreign exchange purchases.
- Exchange rate regimes with varying degrees of Central Bank intervention: crawling peg, fixed exchange rate, freely floating exchange rate within a band.

Data collected for controlling these regulations was the backbone of balance of payments and other international statistics. The regulations and data to be reported were set out mainly in a "Compendium of International Exchange Regulations".

The data, however, were not specifically designed for statistical purposes, but rather for control. Therefore, data used for BOP compilation were, in a significant degree, by-products of administrative requirements.

One of the characteristics of the system was daily reporting of sales and purchases of foreign exchange on a one by one basis. Additionally, there were other reporting requirements, such as registration of loans, amortization schedules, and others.

For BOP compilation, data obtained from this system was supplemented by other sources, the main one being Customs declarations.

## **Impact of liberalization and increased statistical demands**

The liberalization of capital flows and other foreign exchange transactions took place gradually. With this process, flaws in sources traditionally used for statistical purposes became more apparent, as did the need to adapt data collection systems to the changing environment.

At the same time, the need for more comprehensive and timely statistics increased. So did the demand to compile them according to new international standards. BPM5 and the IIP, for example, called for different and sometimes more detailed breakdowns. In 1996, Chile subscribed the SDDS, which posed additional demands on statistics.

Both processes led the Central Bank to conduct research on new data sources. To supplement work undertaken directly by the staff, additional resources were used.

Important highlights for Balance of Payments compilation during this period were:

### **a- Introduction of direct investment surveys**

Traditional measurement of direct investment did not cover reinvested earnings, because the system was mainly settlement-based. To correct this, two annual surveys were introduced (on inward and outward investment). Reinvested earnings were introduced in Chile's BOP in 1998, with data beginning in 1992.

### **b- International trade in services project**

This project was aimed at finding sources, developing methodologies, and measuring trade in those services where information was lacking or very poor. It was conducted in two stages: by a firm of independent consultants and by a special task force hired by the Bank. Important new sources were: surveys, used for directly collecting information or as benchmarks; tax information, data provided by customs, and new forms.

### **c- Project on financial flows and stocks**

An independent consultant was hired to recommend changes in the data collection systems which provide data used mainly to compile external debt, BOP and the IIP.

### **d- Creation of the Office of Statistical Research and Information in late 2000**

This is proof of the increased importance given to statistical work at the Central Bank. Among its goals are increasing efficiency in collecting and processing data for statistics, coordinating statistical requirements, keeping respondent burden at reasonable levels, fostering the use of information available outside the Central Bank, spreading the use of technology, and meeting international standards. One of its tasks has been to improve efficiency in the compilation of data by means of surveys. In July of 2002, the Department of "Information and Surveys" was created.

## **e- New “Compendium of International Exchange Regulations (CIER)”**

The final significant step in liberalization was taken in April, 2001, when remaining restrictions on foreign exchange and international financial transactions were lifted.

The system was established in a new “Compendium of International Exchange Regulations” (CIER), which maintained the basis of the previous reporting framework, but changed its focus from regulatory to statistical purposes. Thus, the CIER has become mainly a listing of transactions and their associated reporting requirements, designed for statistical needs. This Compendium brought together much of the work of other projects, specially “c” and “b”. However, it was not possible to include in it all data requirements, because of legal considerations stemming from the application of the Central Bank law. Efforts were made to simplify and to avoid duplication as much as possible.

According to the new regulations, inflows and outflows of certain transactions, particularly financial ones, are required to be channelled through the “formal exchange market”, and data to be provided to the Central Bank. For other transactions, the only requirement is to provide information to the Central Bank.

Data requirements in the new CIER underwent important changes:

- The daily notification system was expanded to cover not only sales and purchases of foreign exchange but all inflows and outflows, regardless of their conversion to the national currency.
- Codes used in the notification system were simplified (reduction from 250 to 132) and redefined. A “dictionary” of the codes was set up.
- Thresholds for reporting certain transactions, and/or for identifying individual transactions and transactors, were expanded.
- The daily notification system was supplemented by forms, when statistical needs could not be adequately met by the settlement-based system, and when it was possible to clearly define the reporting population. This meant that sample surveys- in which the sample changed over time- were not included. The forms replaced, in many cases, previously existing ones that were not suited to statistical needs. Efforts were made to simplify the number and content of the forms. Examples of new forms are quarterly reports on transportation – one applied to domestic companies and another to representatives of non-resident ones - and quarterly forms provided by insurance companies.
- The new system also has made more use of technology, such as Internet, for collecting the data, and of databases for storing and accessing it.
- Significant efforts were made- and continue to this date – to explain the new requirements to data providers.
- One of the main advantages of collecting information using the CIER is that its data requirements are mandatory, as opposed to surveys conducted by the Central Bank, which are answered on a voluntary basis.

## **Introducing and disseminating BPM5 categories**

The move to BPM5 was planned for May of this year, when data for the first quarter of 2002 was scheduled to be released.

As a result of the above-mentioned projects and other statistical activities, the most important problems that needed to be solved in order to move to BPM5 had been addressed. However, it must be said that all BPM5 categories and standards could not be met. Implementing BPM5, therefore, is an on-going process, in which it has been necessary to establish priorities and to be realistic as to what can be accomplished.

One of the problems that had to be dealt with was that the periods covered by the new data varied across different categories. Also, some new data sources still needed time before they could be deemed reliable. Emphasis had been given to setting up permanent data sources and methodologies, rather than to collecting historical data. As a result, it was decided to disseminate a quarterly series, beginning in 1996, calculated on a best efforts basis, drawing upon different sources and estimations.

The new quarterly series was released in May, in summary form. A detailed version will be disseminated during the last quarter of this year. The release of new BOP data was accompanied by a methodological note explaining the new categories, as well as the main differences with previous definitions. The coming publication will include a more comprehensive methodological note.

In addition to the BOP series, in end-June of this year, an annual IIP series, covering end-year positions going back to 1997, was released for the first time.

### **Changes in BOP:**

The new BOP series differs from the previous one in several ways. Besides different breakdowns and categories stemming from BPM5 definitions, new data sources and methodologies were used, some sources were updated, and other revisions to data were performed.

Among the most important changes are the following:

#### **-Breakdown of goods**

Goods were broken down into BPM5 categories, with the exception of goods for transformation, which are not deemed to be significant. The results were higher levels for both credits and debits, averaging close to 8% and 5% above those of the former series. The main change resulted from a revision of the numbers and methodology used for calculating trade through the free zones.

## **- Breakdown of services**

Adopting BPM5 standard components increased the categories into which these transactions were broken down<sup>1</sup>. The process also involved reclassifying some transactions to/from goods or income. Additionally, there was an important change in estimated levels for overall services -lower credits (average 5 %), higher debits (average 3 %)- resulting from new data sources and methodologies.

## **- Income**

The main change was the breakdown into different categories, as the accrual principle had already been partially adopted. At this stage, it was not possible to extend this principle across income associated to all financial assets and liabilities. Another change was due to updating data for the more recent periods, for which the latest surveys were incorporated, or to a revision of the process used to expand the results of the samples.

## **- Financial account**

Most BPM5 categories and breakdowns in the financial account were calculated. This involved reclassifying financial flows across different accounts. Use was made of data from regulatory institutions, as well as detailed information available in the Central Bank.

Among these changes, Direct investment was expanded beyond “equity” and “reinvested earnings”, to cover “other capital”. However, only “Liabilities to direct investors” were considered within this category of direct investment in Chile, and only “Claims on affiliated enterprises” in the case of Direct Investment abroad.

Another significant change was the use, for the first time, of BIS data on deposits held by the non-banking sector, which replaced previous estimates.

The results were important changes in the composition of capital flows, as well as in overall levels.

## **- Reserve Assets**

The main change was the adoption of the standard components of BPM5 for this category, except for “foreign exchange”, which was only broken down into “currency and deposits” and “securities”. Accrued interest on reserves was registered within the underlying instruments, instead of as part of “other investment - other assets”.

## **Reactions**

The reactions of domestic users- mainly economists, journalists and other analysts- to the new BOP presentation, have been generally positive. The most important problem that has been expressed is that the period covered by the new series is too short. Efforts have been made to answer questions, and to continue to publish, as supplementary information, some categories which are deemed useful.

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<sup>1</sup> To protect confidentiality of data, “Air Transport” was added to “Other Transport”, as all air credits are accounted for by one company.

## **Deviations from BPM5**

As was mentioned, not all BPM5 categories and definitions have been adopted, because only areas deemed most significant in Chile's case were dealt with first. Also, at the time the series was released, some data sources were still being tested. This is a long process, and it is expected that the data will become more reliable over time. The move from control to statistics has been significant and will take time to complete.

The main areas where deviations from the standards remain are:

### **-Merchandise trade:**

Goods for transformation are not measured:

A project to collect data is underway, based on information included in the modified Customs Declarations, which were introduced in 1999 (Imports), and late 2001 (Exports). However, some additional breakdowns need to be included in these Declarations before this can be achieved.

### **-Financial derivatives:**

A project has been carried out this year (2002), and a methodology to measure flows and positions was developed. Data on individual contracts, which has been collected for some years by the Central Bank, will be used to derive data for both stocks and flows for BOP and IIP. Most of the information that is needed is already being reported to the Bank, and only a few additional data are required.

### **-Accrual of interest:**

This principle is being applied partially. Data for additional categories is being collected on new forms, but needs to be checked for reasonableness before it is introduced in the series.

### **-Capital account:**

Sources and methodology for this category need to be developed.

## **Challenges that remain and lessons learned from implementing BPM5**

Significant progress has been made in recent years regarding new data sources and methodologies, enabling the Bank to align BOP statistics more closely with BPM5 (May, 2002) and to issue the first comprehensive IIP (June, 2002). However, some lessons may be learned, and many challenges remain.

Among them, the following may be pointed out:

- Need to ensure high-quality data: although new sources have been developed, it is essential that the data meet quality standards. The new forms provide data to support statistical compilation, but the data need to be analyzed and cross-checked as much as possible, to ensure their quality.

- Importance of good coverage: improving the rate of response, mainly by means of persuasion, is necessary, specially in surveys, which are conducted on a voluntary basis. Fining policy for non-compliance of reporting obligations established in the CIER is an advantage but to some degree also a problem, as the system was created for administrative purposes, and the intention is to obtain data by means of persuasion rather than by applying fines.
  
- Training of human resources in the Bank is necessary to improve efficiency and high quality data. The move from control to statistics requires a change in the skills of the staff that receives the data. BOP staff is working closely with them, explaining concepts on the forms, checks for consistency which should be carried out, answers to frequent questions, and other matters.
  
- Improving communication with respondents, explaining to them the purposes and details of data requirements. For this, meetings have been held with respondents and business associations, both to develop the new forms in the CIER, and to explain the purposes of the new data requirements. Detailed Manuals are being prepared to assist respondents in filling the forms used for Transportation. This activity is time-consuming but necessary.
  
- Finding an adequate balance between requirements of data and reasonable respondent burden, avoiding duplications, and making use of information available outside the Bank. For this, agreements with other institutions for data sharing have been used, and may be improved or expanded. Examples are the agreement with the National Tourist Board to conduct surveys on tourism, which was changed in 2001, and requests for data on pension funds' portfolio investment abroad, which was agreed with the regulatory agency.
  
- Linking reporting categories, as much as possible, to accounting practices and operational concepts, in order to facilitate reporting and increase response rates. An example is the form designed for reporting of insurance companies, which was linked to the companies' financial statements.
  
- Improving surveys: for this, it is important to develop and use a directory. Work is being conducted to improve the existing directory, which is available to all the Bank. Also important in the application of surveys, is defining adequate forms and keeping them as simple as possible, developing a follow-up process, improving the response rate, defining samples, treating non-response, estimating the population from samples. Conducting surveys is a relatively new activity in Chilean BOP compilation. It requires considerable expertise and coordination. Surveys are not mandatory, and are being used only when it is not possible to obtain the data from the notification system, the forms in the CIER, or others. Forms - included in the CIER - are preferred, given their mandatory nature.
  
- Increasing efficiency by use of technology, both for collecting and processing data. This is being done, mainly by using internet, and developing data bases.



- Reconciling the needs and results of data for short-term monitoring, with those for BOP and IIP. The former require higher frequency and shorter lags, but are less detailed, have lower coverage, or less comprehensive. This is an important problem, as there are sometimes different sources and methods for the same items, provisional and definitive.
- Need for ongoing assessment of statistical practices and procedures, comparison with other countries' experiences. During the course of 2002, the reporting requirements set out in the CIER are being assessed, both in terms of response rates, quality of data, reporting burden, use of data, possible duplication of requirements, and others. One aspect to be considered is the use of residual categories and the country attribution, both of which should be closely monitored. Another aspect is examining other countries' systems of data collection. In defining collection methods in Chile, the legal framework has posed some constraints on what could be "ideal" solutions (example: the Bank could not make reporting of positions of external assets and liabilities mandatory).
- Need for flexibility to adapt statistical compilation to new conditions and requirements.
- Need to meet international standards and to face external assessment (examples: BOP5, IIP, SDDS, ROSCS, data provision to BIS).