

Balance
of
Payments
Manual

Fourth Edition

International
Monetary Fund
1977

*John Torce
Statistics Canada*

Balance of Payments Manual

Fourth Edition

1977

International Monetary Fund
Washington, D.C., 20431 U.S.A.

Reprinted, June 1978, with minor corrections

International Monetary Fund.

Balance of payments manual. 4th ed. Washington, 1977.

xvi, 203 p.

1. Balance of payments — Handbooks, manuals, etc.
2. International finance. I. Title.

For sale to the public at US\$4.00 a copy.

TABLE OF CONTENTS

(References in parentheses are to paragraphs)

Preface	xi
1. Introduction	1
2. Conceptual Framework of the Balance of Payments and Its Relationship to National Accounts	7
Definition of the Balance of Payments (16–20)	
Double-Entry System (21–25)	
Concept of an Economy (26)	
Principles for Valuation and Time of Recording (27–29)	
Types of Transaction (30–43)	
Exchanges	
Unrequited transfers	
Allocation of special drawing rights	
Monetization of gold	
Territorial change and migration	
Reclassification of claims and liabilities	
Valuation changes	
Balance of Payments and National Accounts (44–51)	
3. Residents of an Economy	19
Definition of Residents (52–53)	
General Government (54–58)	
Individuals (59–61)	
Private Nonprofit Bodies Serving Individuals (62)	
Enterprises (63–66)	
General definition	
Types of enterprise	
Special Implications of Definition of an Enterprise (67–74)	
Breakup of single entities	
Mobile equipment	
Agents	
Residence of enterprises engaged in installation	
Leased goods	

4. Valuation	26
Concept of Market Price and Market Transactions (75-77)	
Transactions That May Lack an Actual Market Price (78-79)	
Market Price Equivalents (80-81)	
Affiliated Enterprises (82-86)	
Noncommercial Transactions (87-88)	
Financial Items (89)	
Problem of Uniformity (90-91)	
Consistency of Valuation for Interrelated Entries (92-97)	
5. Time of Recording	34
Recommended Timing (98-105)	
Need for Timing Adjustments (106)	
Timing Adjustments to Merchandise Data from Particular Sources (107-109)	
Trade accounts: general	
Trade accounts: length-of-voyage problem	
Exchange record compilations	
Adjustment of Statistics on Transactions Other Than Merchandise (110-14)	
Freight and insurance on merchandise	
Interest due but not paid	
Other services	
Contractual loans	
6. Unit of Account and Procedures for Conversion	40
Unit of Account (116-20)	
General considerations	
National presentations	
Reporting to the Fund	
Procedure for Conversion (121-37)	
Principle applicable to conversion	
Choice of rates for conversion	
Problems of implementation	
7. Analytic Presentation	49
Construction of an Analytic Presentation (140-44)	
Common Types of Analytic Balance (145-64)	
Balances on goods, services, income, and unrequited transfers	
Balances financed by reserve assets and selected liabilities	
Balances on goods, services, income, unrequited transfers, and long-term capital movements	
8. Standard Components	58
List of Standard Components (165-72)	
Application of List (173-75)	

Net Errors and Omissions (176–78)	
Major Classifications (179–80)	
Description of Detailed Classifications (181–97)	
Current account	
Capital account	
9. Current Account (Goods, Services, Income, and Unrequited Transfers)	70
Coverage (199–200)	
Rationale of Classification (201–207)	
Valuation and Timing (208)	
Gross Recording (209–12)	
10. Merchandise	75
Definition (213)	
Change of Ownership (214–25)	
Convention for recording	
Exceptions to change-of-ownership rule	
Goods not crossing frontier	
Goods crossing frontier without changing ownership	
Goods Classified in Items Other Than Merchandise (226–31)	
Goods classified in service and income items	
Goods regarded as financial items	
Special Types of Goods (232)	
Time of Recording (233–35)	
Valuation (236–47)	
Market valuation	
Point of valuation	
11. Shipment	87
Definition (248–49)	
Conventions for Recording Services on Merchandise (250–57)	
Recording of Other Shipment (258–59)	
Types of Shipment (260–65)	
Freight	
Insurance	
Other services	
12. Other Transportation	95
Definition (266–67)	
Passenger Services (268–69)	
Port Services, etc. (270–77)	
Port Services	
Charters of carriers	
Miscellaneous transportation	

13. Travel	98
Definition (278-79)	
Types of Traveler (280-86)	
Business travelers	
Students and trainees	
Excursionists	
Other travelers	
Goods and Services Covered (287-88)	
14. Investment Income	101
Coverage (289-93)	
Classification (294-98)	
Direct investment income	
Other investment income	
Time of Recording (299-300)	
Measurement and Recording of Earnings (301-306)	
Method of calculation	
Recording of reinvested earnings	
Entries for losses	
Stock dividends and bonus shares	
15. Other Goods, Services, and Income	106
Coverage (307-309)	
Definition of Official and Private Transactions (310)	
Main Types of Official Transaction (311-18)	
Embassies and consulates abroad	
Military units and agencies abroad	
Other official entities located abroad	
Joint military arrangements	
Other nonmilitary goods and services provided to or obtained by government	
Military services provided or obtained	
Main Types of Private Transaction (319-39)	
Labor income, n.i.e.	
Property income, n.i.e.	
Other goods and services	
16. Unrequited Transfers	113
Definition (340-43)	
Valuation and Timing (344-45)	
Classification (346-59)	
Private unrequited transfers	
Interofficial unrequited transfers	
Other official unrequited transfers of compiling economy	
Other official unrequited transfers of foreign economies	

17. Capital Account (Financial Items)	118
Definition (360)	
Coverage of Financial Items (361-63)	
Transactions in Assets (364-70)	
Kinds of transaction	
Parties to transactions	
Reinvestment of earnings	
Borderline cases	
Other Types of Change (371-74)	
Types to be recorded	
Valuation changes to be omitted	
Classification changes to be omitted	
Net Recording (375-78)	
Valuation and Timing (379-80)	
Classification (381-99)	
Assets and liabilities	
Functional types of capital	
Long-term and short-term capital	
Domestic sector	
Liabilities constituting foreign authorities' reserves	
Other classifications	
Problems of Measurement (400-406)	
Calculation of valuation changes	
Liabilities constituting foreign authorities' reserves	
18. Direct Investment	136
Explanation of Concept (408-14)	
Direct Investment Capital (415-18)	
Net Recording (419-20)	
Valuation (421-22)	
19. Portfolio Investment	142
Definition (423-25)	
Long-term bonds	
Corporate equities, including capital participations	
Valuation (426)	
Classification (427-28)	
Statistical Problems (429-30)	
20. Other Capital	145
Definition (431)	
Classification (432-37)	
Recording of Loans (438)	

21. Reserves	147
Explanation of Concept (439-41)	
Coverage of Foreign Exchange Assets (442-53)	
Effective control	
Availability for use	
Application of concept in specific cases	
Revaluation of Reserves (454-59)	
Valuation and Timing (460-61)	
Classification (462-73)	
Monetary gold	
Special drawing rights	
Asset and liability positions vis-à-vis the Fund	
Foreign exchange and other claims	

APPENDICES

A. Regional Balance of Payments Statements	159
Suggested Method for Regional Allocation (476-79)	
Drawbacks to Other Methods (480-82)	
Selection of Regions (483-85)	
B. Compilation of Merchandise (Item 1)	164
Introduction (486-87)	
International Standards for Trade Statistics (488-89)	
Types of Adjustment for Conceptual Discrepancies (490-94)	
Coverage Adjustments (495-500)	
Coverage adjustments to trade statistics compiled as suggested in International Trade Statistics: Concepts and Definitions	
Coverage adjustments to trade statistics defined to cover all movements of goods across border of reporting country	
Coverage adjustments to exchange record statistics defined to cover all merchandise transactions settled through banking system	
Classification Adjustments (501-503)	
Classification adjustments to trade statistics compiled as suggested in International Trade Statistics: Concepts and Definitions	
Classification adjustments to trade statistics defined to cover all movements of goods across border of recording country	

Classification adjustments to exchange record statistics defined to cover all merchandise transactions settled through banking system	
Timing Adjustments (504–13)	
Timing adjustments to trade statistics compiled as suggested in <i>International Trade Statistics: Concepts and Definitions</i>	
Timing adjustments to trade statistics defined as to valuation in terms of definition of Customs Cooperation Council	
Timing adjustments to trade statistics defined to cover all movements of goods across border of reporting country	
Timing adjustments to exchange record statistics defined to cover all merchandise transactions at time of settlement through banking system	
Valuation Adjustments (514–17)	
Valuation adjustments to trade statistics compiled as suggested in <i>International Trade Statistics: Concepts and Definitions</i>	
Valuation adjustments to trade statistics defined as to valuation in terms of definition of Customs Cooperation Council	
Valuation adjustments to trade statistics defined to cover all movements of goods across border of reporting country	
Valuation adjustments to exchange record statistics defined to cover all merchandise transactions settled through banking system	
C. Comparison of Balance of Payments Classification with External Transactions in <i>SNA</i>	177
D. Survey on Recording of Merchandise Transactions in Balance of Payments	181
Introduction (525–28)	
Survey Results (529–43)	
Physical point of valuation of merchandise	
Pricing of merchandise	
Sources of international trade data	
Relationship between merchandise and shipment items	
Implications for this Manual (544–46)	

x / BALANCE OF PAYMENTS MANUAL	
E. Survey of Direct Investment: Concepts and Definitions	187
Introduction (547-49)	
Survey Results (550-72)	
Identification of direct investment enterprises	
Direct investment capital flows	
Direct investment income flows	
Index	197

PREFACE

This fourth edition of the *Balance of Payments Manual* continues the series of handbooks that have been issued by the International Monetary Fund to guide member countries in making their regular reports on the balance of payments, as stipulated in the Fund's Articles of Agreement.

In the interval since 1961, when the third edition was published, important changes have occurred in the manner in which international transactions are conducted, as well as in the international monetary system that constitutes the setting for them. Then, too, experience during that period in applying the third edition has brought to light a number of ways in which the Manual's explanations could usefully be augmented and its recommendations clarified. The new edition is the product of a major effort that has involved reconsideration of both the technical aspects of balance of payments compilation and the analytic contexts in which the figures are to be employed.

This Manual incorporates a good deal of explanatory material that is entirely new. Some topics that were covered in a few paragraphs in the third edition are now treated in separate chapters. These subjects include the underlying principles for residence, valuation, timing, and the unit of account and conversion. In these cases, the elaboration does not denote any significant change in the principles themselves; its purpose, instead, is to provide more adequate guidance through a fuller discussion of the concepts, which are basic to the system of balance of payments accounting. In contrast, the inclusion of a chapter on analytic presentation breaks new ground as far as the Manual is concerned. Even though the chapter does not express a preference for any particular analytic approach, its description of various widely used balances is an integral part of the Manual's general subject matter and, as such, will be of interest to both compilers and users of balance of payments statements.

The classification scheme, which plays a crucial role in fostering international comparability in balance of payments reporting, has been reconsidered in detail, and the merits of the previous series have been carefully weighed against the advantages of alternative ones that

could be substituted for them. From this review have emerged the Manual's recommendations for a list of standard components, i.e., individual statistical series that can be used as building blocks for constructing a variety of presentations, focusing on different analytic balances. The selection of standard components has been approached as a task of more than technical consequence. Consideration had to be given to the suitability of the list for application by member countries with greatly differing balance of payments structures, as well as very disparate levels of development with respect to their statistics.

Perhaps the main departure of this Manual from its predecessors with respect to classification is to be found in the reorganization of the capital account. The primary categories in previous editions showed separately the sectors of the domestic economy that were the creditors and debtors; the breaking out of direct investment capital represented the only attempt that was made at classifying capital by its function. In this edition, two further functional categories—reserves and portfolio capital—have been distinguished, with a consequent deemphasis of the sectoral approach. As a result of this change, the components of the capital account should better serve the needs of analysis as they have evolved. Numerous other adjustments in the classification scheme, the nature of which will be readily apparent to users familiar with the scheme of the third edition, have also been introduced to that same end.

No catalogue has been prepared, however, that details the differences between the statistics called for by this Manual and by the third edition. Such a listing, in fact, would be much less useful for the reader or compiler than might be supposed on first consideration. Many of the more significant changes that have been introduced are rather easily discernible; cases in point are the merging of series that were previously shown separately and the breakdown of others to provide new details. Other modifications tend to be quite technical, and their effects are often difficult to characterize, let alone evaluate. For example, although this Manual continues to espouse center of interest as the principle for determining the residence of individuals, it provides a rule of thumb for deciding certain borderline cases instead of leaving their determination entirely to the compiling country, as was done in the third edition. In contrast, some of the specific guidelines previously given for distinguishing direct investment enterprises have been replaced by more explanation of the underlying concept. The implications, if any, that such changes will have for figures to be compiled in accordance with the Manual's recommendations are obviously impossible to establish in a generalized way. In summary, it can be said that differences from the third edition are

likely to be either fairly obvious or else not so substantial as to risk being seriously misleading, even to an unwary user of the statistics.

Despite the thorough overhaul that the Manual has been given and the considerable changes that have been introduced in that document, the Fund's recommendations for balance of payments compilation have actually maintained a high degree of continuity. Thus, compilers who have been producing statistics that conform reasonably well to the standards set out in previous editions should not find any great difficulty in adapting their established procedures for data collection and reporting to accord with the instructions of this Manual. Rather, the re-examination of the Manual's concepts and principles has shown that these continue to be generally valid and that the necessary adjustments could readily be made within a largely unchanged theoretical framework. This outcome has been most reassuring.

Because the Manual is intended as a practical guide in matters of statistical compilation and reporting, its recommendations should ideally be explicit and straightforward. This aim, however, has not always proved to be one that could be achieved. For one thing, some of the most fundamental concepts are complicated and cannot be described solely in terms of well-defined characteristics that could be discerned readily or of rules of thumb that could be applied mechanically. Moreover, the Fund would not issue a standard like the Manual without taking into account the views of technicians in national balance of payments offices, whose preferences sometimes differ widely, not only among themselves but in relation to those of the Fund staff. While the process of reconciling divergent opinions helps to ensure that the Manual's recommendations will be realistic and generally acceptable to compilers, it also adds to the complexity of those recommendations. Thus, items decided in this manner may be less clear-cut, and harder to explain, than those decided largely with more theoretical considerations in mind. Similarly, various qualifications and reservations have had to be incorporated in some of the explanations, in order to reflect the compromises that were worked out; the clarity and precision of certain formulations may have suffered as a result. Notwithstanding these problems of presentation, every effort has been made to avoid ambiguities and to provide in the Manual a set of recommendations that are internally consistent.

The work of producing a new edition of the Manual has been carried out by the staff of the Fund in close consultation with compilers of national balances of payments. The project was under the supervision of Mr. Charles F. Schwartz, Deputy Director of the Fund's Research Department. Much of the original drafting, and of the subsequent redrafting in light of comments from the many persons consulted, was carried out by Mr. John S. Smith, Advisor in that

Department. Mr. Arie C. Bouter, Assistant Director in charge of the Department's Balance of Payments Division (which was transferred in May 1977 to the Bureau of Statistics), also had a major responsibility for work on the volume, and the economists in his Division made many specific contributions in the drafting process.

A small, representative group of national compilers was co-opted at the outset of the project to assist the Fund staff, in the capacity of consultants, in the planning of the volume. As the work progressed, the membership of this group was gradually expanded in order to encompass a broad spectrum of expertise on difficult technical aspects, particularly in the fields of merchandise trade and direct investment. The number of compilers engaged as consultants was further increased as successive drafts produced by the staff became available for review. At the final stage, the draft was sent for comment to the entire group of national compilers who serve as the Balance of Payments Division's correspondents in member countries.

The Fund staff wishes to acknowledge with thanks its indebtedness to all the experts in national balance of payments offices who contributed to preparation of the Manual. It is especially grateful to the following consultants, each of whom participated in at least one series of meetings on the project and some of whom were called on for considerably more extensive assistance.

Argentina	Mr. Oraldo N. Fernandez
Australia	Mr. P. N. Atcherley
Belgium	Mr. J. Dolo
Brazil	Mr. Gilberto Vieira de Carvalho
Canada	Mr. D. K. McAlister
Egypt	Mr. Henry Tadros
Finland	Mr. Tuomas Sukselainen
France	Mr. Claude Hernandez; succeeded by Mr. Philippe Dulac
Germany, Federal Republic of	Mr. Kurt Senff
Ghana	Mr. S. K. Botchway
India	Mr. V. B. Kadam
Indonesia	Mr. Sujitno Siswowedagdo
Iran	Mr. Mostafa Moshtagh Ararghi
Italy	Mr. Carlo Santini
Japan	Mr. Minoru Akine
Kenya	Mr. Parmeet Singh
Netherlands	Mr. C. Bakker
Sweden	Mr. Hans Svensson
Turkey	Miss Gonul Bati
United Kingdom	Mr. Ronald W. Green

United States	Mr. David T. Devlin; succeeded by Mr. Jack J. Bame
Venezuela	Mrs. Luisa Romero; succeeded by Mr. Alcides Villalba
Banque Centrale des Etats de l'Afrique de l'Ouest (BCEAO)	Mr. Pierre Sanner
European Economic Community (EEC)	Mr. Piero Erba
Organization for Economic Cooperation and Development (OECD)	Mr. Erwin Veil

CHAPTER ONE

Introduction

1. A balance of payments statement can be broadly described as the record of an economy's international economic transactions, that is, of the goods and services that an economy has received from and provided to the rest of the world and of the changes in the economy's claims on and liabilities to the rest of the world. Such a record can be put to a variety of uses, beyond the basic one of appraising the effects of the transactions on the domestic affairs of the economy itself. As an economy's balance of payments mirrors the rest of the world's dealings with that economy, the international community is directly concerned with the statements for its individual members. Interpretation of such statements from that viewpoint is obviously made easier when all countries' statistics are based on the same concepts and are compiled in a uniform way.

2. The chief purpose of this Manual is to recommend the standard concepts, rules, definitions, guidelines, conventions, and classification scheme that are to be employed by member countries in assembling uniform statistics for a balance of payments statement, as well as to discuss the conceptual framework and analytic considerations that help form the basis for those particular recommendations. The objective is to assist compilers in collecting and organizing their underlying data in a systematic manner that will serve both to facilitate the analysis of countries' international economic relationships and to maximize intercountry comparability. To this end, examples and empirical guidelines for applying the concepts and rules are cited, and a list of standard components that can be used as the common building blocks for a variety of presentations of the statement is specified and defined in some detail.

3. The general outlines of the conceptual framework for the balance of payments are discussed in Chapter 2. In brief, the system employed is a double-entry one, recording for a given economy all transactions vis-à-vis the rest of the world. Most transactions are reflected in pairs of

equal credit and debit entries, and any entries that are not automatically paired in that way are deliberately furnished with entries of special types as an offset. The sum of all the credit entries in the statement is thus in principle numerically equal to the sum of all the debit entries, with any inequality that may in fact arise being attributable to net statistical errors and omissions. The types of transaction that can occur are described in the chapter, and the matching offsets where required are identified.

4. The second chapter also touches on other conceptual aspects for which standard treatments must be devised if intercountry comparability is to be achieved. These aspects include the scope of an economy, the principle for valuing international transactions, and the time at which such transactions are to be recorded. Finally, the chapter points out the close connection that exists between the balance of payments and related economic data, specifically, the national accounts and the international investment position.

5. The rules to be applied in determining the bounds of an economy are discussed in some detail in Chapter 3. In general terms, an economy comprises the economic entities—the government, individuals, private nonprofit bodies, and enterprises—that have a closer association with the territory in question than with any other territory. Since many entities, especially those engaging in international transactions, have some degree of association with more than one territory, a detailed set of guidelines is given to ensure that borderline cases will be treated in a uniform manner.

6. Chapter 4 examines the difficult subject of valuation. The stated basis for valuation in this Manual, in common with the national accounts as a whole, is market price. In concept, a market price is the price that a willing buyer pays to a willing seller, when the buyer and seller are independent parties whose only considerations are commercial ones; strictly speaking, each transaction that takes place under those circumstances has its own market price. Difficulties arise, however, because one or more of the conditions needed to establish a market price in that sense are frequently absent. For example, the parties to a transaction are not independent in the intended sense when they are affiliated enterprises, and commercial considerations may not always be the only ones that are of concern to the parties. Determination of the nearest equivalent to an actual market price thus often poses a practical problem.

7. Timing, which is the subject of Chapter 5, is on the whole an easier concept to deal with than valuation, although it is by no means without statistical problems that can have a significant impact on the

figures that are recorded. The basic principle adopted in this Manual is that transactions are to be recorded when the real resources or financial items involved undergo a legal change of ownership, which is taken to be the time that the parties concerned enter the transactions in their books. The chapter discusses both the treatment of transactions that do not actually reflect such legal changes of ownership and the practical problems of adjusting underlying statistical data that have originally been compiled according to some different principle.

8. The selection of a unit of account and methods of converting data expressed in various transaction currencies into that unit—topics of special importance in a balance of payments context—are treated in Chapter 6. The complete balance of payments is rarely expressed at constant prices (in effect, in volume terms). Users of the balance of payments, nonetheless, often wish at least to have a unit of account in terms of which the market prices of international transactions will be as free as possible from distortions attributable to exchange rate fluctuations. Needless to say, a completely stable unit does not actually exist, and even an artificial one could not satisfactorily be constructed, especially for a period during which the relative exchange rates of transaction currencies fluctuated markedly from day to day. Moreover, the derivation of a market price in any unit of account other than the currency actually used for the transaction poses a conceptual problem. This problem cannot be left unresolved, inasmuch as the transactions to be recorded in the balance of payments are originally denominated in a variety of currencies and must necessarily be converted to the national currency or some other unit of account before they can be aggregated. The conversion methods suggested in this Manual represent pragmatic solutions that are intended to foster a reasonable degree of international uniformity.

9. The theme of Chapter 7 is the presentation of balance of payments statistics in a format suitable for analytic use. Reduced to its simplest terms, balance of payments analysis involves a division of all the series comprising the statement into two groups that—because of the double-entry system employed—will be equal numerically but will have opposite signs (i.e., net credits vs. net debits). The items in one group are supposed to share some characteristic or characteristics that differentiate them from the items in the other group, so that the behavior of the two groups can presumably be explained in terms of those characteristics. The number of approaches that can be applied in various analytic contexts is actually quite large, and often two or more sets of characteristics are under study simultaneously. In practice, therefore, a balance of payments statement typically delineates more than two main groups for which the transactions are summarized in the

form of “balances.” These balances may be supplemented by various subsidiary, or partial, balances.

10. Because any particular arrangement of standard components is likely to have different analytic implications over time, both between countries and in various situations and contexts for any particular country, it is not the intention in this Manual to go very deeply into the subject of analysis. Moreover, this area can be quite controversial, since individual analysts naturally form their own judgments about the relative merits of different approaches. The subject has been taken up in the Manual, however, for such related reasons as the following. (a) The Manual is thought of as a source of information on all technical aspects of the balance of payments. (b) It seems the natural place in which to find some description and explanation of the considerations behind the presentations shown in other Fund publications and, more generally, in national sources. (c) The recommendations about standard components and their definition given in subsequent sections of this Manual are best understood in light of the kinds of analytic approach that influenced their formulation.

11. Chapter 8 introduces the sections of the Manual that are devoted to questions of classifying transactions and defining balance of payments items. A classification scheme is simply a systematic way of assigning all the individual transactions comprehended within the conceptual framework—or at least such of them as have been selected as being of potential interest for analyzing a country’s international economic relationships—to a manageable number of meaningful items. The choice of items relies entirely on the exercise of judgment, taking into account such considerations as behavior and size of the items, statistical convenience, and the viewpoints from which the statement is to be analyzed. Although variations from standard classification are often quite readily discernible and thus are not so apt to mislead the user as departures from the general principles for residence, valuation, and timing, they may nonetheless be a serious impediment to intercountry comparison. Moreover, it is generally within the capability of the compiler to conform to a standard with respect to classification, provided that the standard is not an unreasonable one and is explicit enough to leave little doubt about what is intended. Considerable space in this Manual, therefore, is given to a description of the border lines to be drawn between the individual standard components.

12. The discussion of classification advances by stages from the general to the particular. Chapter 8 gives a summary description of the whole classification scheme in terms of a list of “standard components.” Chapters 9 and 17 introduce the two main groups, current

account and capital account, respectively, into which the standard components are divided and elaborate the main principles as these are specifically applicable to them. Each of these general chapters is followed by a series of chapters dealing with individual components of the main group. This procedure affords convenient opportunities to discuss the overall principles in the contexts in which they are most relevant. For example, change of ownership, which is the basic consideration for the time of recording, can be elaborated most usefully under the heading of the merchandise component, as that component often gives rise to the most important of the timing problems.

13. The Manual also contains several appendices presenting materials that should be of interest to many compilers and users of balance of payments statistics. The first of these appendices concerns the compilation of regional statements, i.e., statements of an economy's economic transactions with one or more foreign geographic or currency areas, rather than with the rest of the world as a whole. In principle, regional statements should be constructed in such a way that, when the separate statements for each region with which an economy has transactions are aggregated, the resulting global statement will be in conformity with the recommendations in the main part of this Manual. Admittedly, the practical obstacles to pursuing this rather straightforward objective can be quite formidable. The preparation of regional statements has two chief aspects. First, the rules to be followed for the attribution of transactions by region must be decided. Appendix A describes a scheme for attribution of the sort that has been widely employed by compilers in constructing regional statements and discusses its implications. Second, the areas must be selected, an exercise that poses no conceptual problems and is very much a matter to be decided in the light of the use for which the statement is being compiled.

14. The next two appendices (B and C) compare the recommendations of the Manual with other international standards for related statistics. Specifically, the similarities and differences between the merchandise component of the balance of payments, on the one hand, and the United Nations' standard for external trade statistics and the Customs Cooperation Council's recommendations for customs valuation, on the other hand, are explored in some detail; and some of the balance of payments aggregates, particularly those of the current account, are reconciled with comparable elements of the rest of the world account in the United Nations' *A System of National Accounts*.¹

¹United Nations, *A System of National Accounts*, Studies in Methods, Series No. 2, Rev. 3 (New York, 1968).

15. The last two appendices (D and E) summarize the results of Fund surveys of national practices and preferences in compiling the balance of payment statistics for merchandise trade and for direct investment, respectively. Those items are large for virtually all countries and raise important issues of concept, definition, and measurement. Through the cooperation of national compilers, the Fund staff has been able to assemble considerable information about how those statistics are presently being compiled and about what direction future efforts to improve them should take. The findings of these surveys have weighed heavily in the formulation of the recommendations in the Manual on merchandise trade and direct investment. They have also shed some light on the probable quality and intercountry comparability of the estimates for those items, matters that are often in the minds of users.

CHAPTER TWO

Conceptual Framework of the Balance of Payments and Its Relationship to National Accounts

(1) Definition of the Balance of Payments

16. The balance of payments is a statistical statement for a given period showing (a) transactions in goods, services, and income between an economy and the rest of the world, (b) changes of ownership and other changes in that economy's monetary gold, special drawing rights (SDRs), and claims on and liabilities to the rest of the world, and (c) unrequited transfers and counterpart entries that are needed to balance, in the accounting sense, any entries for the foregoing transactions and changes which are not mutually offsetting.

17. While the broad coverage of a balance of payments statement can be deduced for the most part from the foregoing definition, a number of borderline situations arise that can only be dealt with by the adoption of conventions. These cases involve principally decisions as to (a) what constitutes a transaction and (b) what changes in holdings of foreign financial items in addition to those produced by changes of ownership shall be covered.

18. The strict interpretation, in the national accounts sense, of a transaction in goods, services, and income is the provision by one party to another of a real resource of that kind. A question about whether a transaction should be deemed to have occurred may arise, however, when the two supposed parties constitute a single legal entity, when a real resource is provided without an actual change of legal ownership, or when some other change that is not a transaction in the restricted sense produces similar economic effects. In this Manual, the term "transaction" is often used broadly, for convenience, to refer to any sort of change that by convention is to be shown in the balance of payments.

19. Likewise, the balance of payments entries for changes in an economy's holdings of foreign financial items do not reflect exclusively changes of ownership between a resident and a foreigner. However,

they do not comprehend, at the other extreme, all changes in the value of an economy's holdings of such items during a given period. What the exact coverage is to be is a matter of judgment; the conventions recommended in this Manual are noted in section (5) below and are specified in more detail in Chapter 17.

20. The definition of a balance of payments given above is addressed to its conceptual scope. It makes no explicit reference to other aspects that are equally important to deal with in the recommendation of standards to be applied in compilation of the balance of payments. This chapter describes the general setting within which the specific recommendations made in this Manual have been developed, in particular the nature of the system employed in constructing the balance of payments statement, the delimitation of an economy, the basic requirement for principles of valuation and time of recording, the kinds of economic transaction that could be considered for inclusion in the statement, and the formal relationship of the balance of payments to the comprehensive system of national accounts, including the international investment position. The practical implications of most of these subjects are brought out in subsequent chapters.

(2) Double-Entry System

21. The basic convention applied in constructing a balance of payments statement is that every transaction that is recorded is to be represented by two entries that have exactly equal values. One entry of each of these pairs is designated as a credit and conceived as having a positive arithmetic sign, while the other entry is called a debit and given a negative sign. Thus, in principle, the sum of all the positive entries is identical to the sum of all the negative entries, and the net balance of all the entries in the statement is zero.

22. Most entries in the balance of payments refer to transactions in which economic values are provided or received in exchange for other economic values; those values consist of real resources (goods, services, and income) and financial items. The offsetting credit and debit entries that are called for by the recording system, therefore, are often the result of making entries whose amounts are equal for the two items that have been exchanged. Where items are given away rather than exchanged, or when recordings are one-sided for other reasons, special types of entry—referred to as unrequited transfers and counterparts, respectively—are made in order to furnish the required offsets. The various kinds of entry that may be made in the balance of payments are discussed in paragraphs 30–43.

23. Under the conventions of the system, the compiling economy records credit entries (a) for real resources denoting exports and (b) for financial items reflecting either a reduction in the economy's foreign assets or an increase in its foreign liabilities. Conversely, the compiling economy records debit entries (a) for real resources denoting imports and (b) for financial items reflecting either an increase in assets or a decrease in liabilities. In other words, for assets—whether real or financial—a positive figure (credit) represents a decrease in holdings, while a negative figure (debit) represents an increase. In contrast, for liabilities (which can be seen as the obverse of financial assets) a positive figure shows an increase and a negative one a decrease. Unrequited transfers and counterparts are shown as credits when the entries to which they provide the offsets are debits and as debits when those entries are credits.

24. In practice, most balance of payments statements are condensed at least to some extent, either for statistical or for analytic reasons. The credit and debit entries for a single kind of good, service, income, or capital item may be either shown separately or aggregated; for example, instead of merchandise exports (credits) and imports (debits), a trade surplus or deficit (net credit or debit, respectively) can be shown. In the same way, two entries that record the matching credit and debit aspects of the same transaction can be consolidated into a single entry whose balance is zero, in which case the transaction has in effect been "excluded" or "omitted" from the statement. For instance, military equipment furnished as a grant can be entered as a credit in the merchandise item, with the matching debit for the unrequited transfer in a different item, or military grants can be "excluded" from the statement by offsetting the equipment against the transfer in a single, notional item that can be suppressed because its balance is zero. The apparent content or coverage of a statement, therefore, depends on whether transactions are treated on a gross or a net basis. The recommendations in this Manual specify which transactions shall be recorded gross and which net; the resulting list of standard components, however, can readily be condensed by further netting in a presentation of the statement for analytic use.

25. The double-entry system of recording can be seen as contributing importantly to the analytic potential of a balance of payments statement in still another way. When the entries are divided into two groups according to any desired criterion, the sums of the groups will always be numerically equal with opposite sign. The behavior of one group will sometimes furnish the explanation for that of the other group. The choice of the characteristics to be isolated, such as transactions undertaken for their own sake and the flows induced to

finance them, and the relationships between the partial balances that can be derived by this approach from the principal subjects of balance of payments analysis.

(3) Concept of an Economy

26. As mentioned earlier, an economy is conceived as being comprised of the economic entities that have a closer association with a given territory than with any other territory. The balance of payments of a given economy will record either an entity's transactions with the rest of the world, if the entity is considered a resident of the economy, or an entity's transactions with the economy, if the entity is considered a nonresident. Because of the double-entry system, no imbalance in the statement could arise from decisions taken about the general rules of residence or the status of particular entities, but the types of transaction to be recorded can be very much affected. An international standard with respect to residence is needed, therefore, to determine the content of items in a uniform way, as well as to promote their intercountry comparability.

(4) Principles for Valuation and Time of Recording

27. The most suitable price at which to value an economic transaction is by no means self-evident. For any given commodity, for example, there may be quoted or list prices at the wholesale and retail level; prices in commodity markets in different places; prices at which customs duties or other taxes are levied; a price implicit in the value at which the owner carries the commodity on his books, such as production cost, acquisition cost, replacement cost, or transfer cost between affiliates; or the purchase or sale price realized in an effective transaction.

28. A uniform principle of pricing must be used throughout the balance of payments for reasons such as the following: the statement will not be in balance unless the credit and debit aspects of each recorded transaction, which in practice may be derived independently from separate sources, are valued at the same price; the statements for different economies will not be comparable unless both partners adopt the same principle; and the figures can be misinterpreted by the user if they are not all based on a consistent, specified principle. The national accounts in general face similar problems, and the universal solution has been to adopt the principle of basing values on market prices or their equivalents. The definition and description of market prices are the subject of Chapter 4.

29. The time as of which a transaction is to be recorded is also of importance for the same reasons. In addition to a variety of prices, the existence of several relevant dates is entirely possible, such as the time of contract or commitment, shipment of goods, delivery of goods, customs clearance, performance of services, accrual of income, and payment. The choice of the time for recording even has some effect on the coverage of the statement; the entries for trade credits, for instance, that may appear in a statement reflecting changes of ownership will be lacking in one where the time of recording is linked to actual payments. The Manual's recommendation of a principle that is consistent with the time that ownership changes is again in agreement with the national accounts.

(5) Types of Transaction

30. The balance of payments is a record of what has taken place during a given period, in contrast to a statement of the situation on a certain date; it thus refers to changes, i.e., transactions in a comprehensive sense. Broadly speaking, the changes in economic relationships that the balance of payments registers stem primarily from dealings between two parties; these parties are usually a resident and a nonresident, and all dealings of this kind are covered in the balance of payments. In addition, however, changes fitting the same description can also come about in other ways, and some of them have traditionally been shown in the balance of payments. The recommendations as to the entries that actually should be included are embodied in the list of standard components (Chapter 8) and are spelled out in detail from Chapter 9 onward. The objective of these recommendations is to simplify the balance of payments by not extending its coverage in practice beyond what is considered relevant for particular kinds of analysis. It may be said, in very general terms, that the most prevalent type of change described below that is actually omitted is valuation changes in financial items, although such changes in reserves are shown as supplementary information.

31. Despite its name, the balance of payments is concerned not with "payments" as that term is generally understood but with "transactions" of the kind enumerated below. A number of international transactions that are of interest in a balance of payments context may not involve the payment of money, and some are not paid for in any sense. This inclusion of transactions in addition to those matched by "payments" constitutes a principal difference between a balance of payments statement and a record of foreign payments.

(a) *Exchanges*

32. The most numerous and important of the types of transaction found in the balance of payments are ones in which a transactor (economic entity) provides an economic value to another transactor and receives in return an equal value. These transactions may be characterized as exchanges. The two parties to such an exchange are residents of different economies or at least are not both residents of the economy that is the debtor for a financial item in which they are dealing. The things that are considered to have economic value and that can be provided by one economy to another may be categorized broadly as real resources (goods, services, income) and financial items. The provision of a financial item may involve not only the change of ownership of an existing claim or liability but also the creation of a new one or the cancellation of an existing one. Moreover, the terms of a contract pertaining to a financial item (e.g., its contractual maturity) may be altered by agreement between the parties; a situation of this sort is equivalent to the fulfillment of the original contract and its replacement by one with different terms. All exchanges of these kinds are to be covered in the balance of payments. The foregoing description, however, is not sufficient in itself to establish in all cases whether a transaction is to be regarded as an exchange, since the exact delineations of what constitutes an entity, an economic value, and the provision of such a value derive in part from specific conventions that have been adopted.

(b) *Unrequited transfers*

33. Transactions involving unrequited transfers differ from exchanges in that one transactor provides an economic value to another transactor but does not receive a quid pro quo on which, according to the conventions and rules adopted for the system, economic value is placed. This value that is lacking on one side is represented by an entry referred to as an unrequited transfer. The distinction between an unrequited transfer on which no economic value is placed and a service or income item (which is also nonfinancial and intangible) having economic value is largely a matter of convention and is not based on any principles or criteria that can be stated unambiguously in general terms. The provision and receipt of economic values without a quid pro quo are to be shown in the balance of payments.

(c) *Allocation of special drawing rights*

34. The allocation or cancellation of special drawing rights resembles the previous category involving unrequited transfers in that a resident

acquires or gives up a financial asset but does not exchange it for anything having economic value. It differs from the definition of an unrequited transfer, however, because only one party, the resident, is involved and thus no transfer of the asset from one entity to another can be said to occur. The allocation (credit) or cancellation (debit) itself forms the counterpart that matches the increase (debit) or decrease (credit), respectively, in holdings of the asset. These items are recorded in the balance of payments.

(d) *Monetization of gold*

35. The monetization or demonetization of gold is another unique case, which is similar to, but in principle not identical with, the allocation or cancellation of special drawing rights. Gold is a commodity that may also be regarded virtually as a foreign financial asset when it is held by the central authorities, since it has been so readily usable in place of a claim on a foreigner or in acquisition of such a claim. A change in the way in which a given stock of gold is regarded may thus bring about an apparent change in an economy's foreign financial assets. Such a change is to be shown in the balance of payments, together with a counterpart for monetization (credit) or demonetization (debit) that matches the respective entry for an increase (debit) or decrease (credit) in holdings of the financial asset. This phenomenon may occur, in principle, even when only a single economic entity—specifically, an agency of the central authorities—is involved. It may be noted in passing that, unlike the allocation or cancellation of special drawing rights, the monetization or demonetization of gold does not affect the national wealth of the economy which owns it except to the extent that the same gold may be assigned a different value as a commodity from that which it has as a financial asset.

(e) *Territorial change and migration*

36. Since an economy is defined in terms of the economic entities associated with its territory, the scope of an economy is likely to be affected by a change either in its territory or in the entities that are associated with it.

37. A change in jurisdiction over a given territory results in a change in the status of any entities associated with that territory, from residents to nonresidents with respect to the old economy and from nonresidents to residents with respect to the new economy. The net amount of real resources and capital that the old economy can be said to be providing to the new economy is equal to the net worth of the entities whose status has changed. Therefore, if the real resources and

capital that an economy provides to or receives from the rest of the world because of a change in its territory were to be recorded, a counterpart reflecting the transfer of net worth would also be needed to balance the statement; by convention, however, the balance of payments excludes both of these offsetting entries.

38. In migration, the residence of an individual is considered to have changed from one economy to another because the person concerned has moved his abode. Such a change in the body of individuals that comprise an economy has the same effects as a territorial change on each of the economies affected. In either case, certain movable tangible assets owned by the migrant are in effect imported into the new economy; the migrant's nonfinancial intangible assets issued by the old economy and his immovable and certain movable tangible assets located in the old economy become claims of the new economy on the old economy; the migrant's claims on or liabilities to residents of an economy other than the new economy become foreign claims or liabilities of the new economy; and the migrant's claims on or liabilities to residents of the new economy cease to be claims on or liabilities to the rest of the world for any economy. The net sum of all these shifts is equal to the net worth of the migrant, which must also be recorded as an offset, if the other shifts are recorded; the entries are in fact made in the balance of payments, where the offset is conventionally included with unrequited transfers rather than shown as a counterpart.

(f) Reclassification of claims and liabilities

39. The classification of financial items in this Manual reflects characteristics that are designed to bring out the motivation of the creditor or debtor. These intentions can change from time to time, thereby affecting the characteristics, and financial items are subject to reclassification in accordance with such changes. Two main cases in point are the distinction drawn between direct investment and other kinds of capital and that between reserves and other kinds of capital. For example, several independent holders of portfolio investment in the form of corporate equities issued by a single enterprise abroad may form an associated group in order to have an effective voice in the management of the enterprise on a lasting basis; their holdings will then meet the criteria for direct investment, and the change in the status of the investment could be recorded as a reclassification. Similarly, claims on foreigners can come under or be released from the direct and effective control of the resident authorities, in which case a reclassification between reserves and nonreserve capital ensues. The decision for the balance of payments has been to record the

reclassification of financial items only when the reclassification affects reserves.

(g) *Valuation changes*

40. The value of real resources and financial items is constantly subject to change. That change may stem from either or both of two causes. (i) The price at which transactions in a certain type of item customarily take place may undergo alteration in terms of the currency in which that price is quoted. (ii) The exchange rate for the currency in which the price is quoted may change in relation to the unit of account that is being used. The changes in value that accrue to the account of a given economic entity are those on assets that it has contracted to acquire but has not yet contracted to dispose of again, which are not in all cases those that it owns at a given time. Specifically, such accruals include those on assets that have not yet been delivered to the entity which has contracted to acquire them and exclude those on assets that the entity has contracted to dispose of but has not yet delivered. Valuation changes are by convention not included in the balance of payments, although supplementary information on such changes is given with respect to financial items in the category for reserves.

41. When the change of ownership under a contract actually occurs, the transaction is to be shown in the balance of payments at the market value which the item has under that contract. That value, of course, reflects any price changes which affected the value of the item up to the time that the contract was made. The balance of payments, therefore, includes the realization of capital gains or losses resulting from valuation changes that accrued from the time that a contract was made to acquire an asset until a contract was made to dispose of it.

42. The difference between the realization of capital gains and losses, which is to be included in the balance of payments, and the valuation changes themselves, which are not to be included, is illustrated by the following example. A financial asset is purchased for 10 units of account (U), and its market value equivalent rises to U 15 during the same recording period. The transaction to be shown in the balance of payments is the purchase (U 10), even though the increase in holdings from the beginning to the end of the period is U 15, U 5 of which being a valuation change. To continue the example, if the asset were instead to be sold again for U 15 before the end of the period, the transactions to be entered in the balance of payments would amount to a net sale of U 5, which reflects the realization of the capital gain. The value of holdings, however, would show no net change, being nil at both the beginning and end of the period. Once more, the difference of U 5

position. When an economy provides real resources to the rest of the world on a net basis, and does not simply give such resources away, it acquires financial assets that are considered to have an equivalent value. The net provision of real resources over time, exclusive of those provided as unrequited transfers, is thus mirrored by the stock of financial items that has been accumulated. The value of that stock may also be affected by the other factors, such as changes in price, that are referred to collectively in the national accounts as revaluation or reconciliation items. A balance sheet showing the size and composition of the stock as of a given date is known as the international investment position.

50. The holdings of financial items that are depicted as the international investment position consist of claims on nonresidents, liabilities to nonresidents, monetary gold, and SDRs. Under the conventions of this Manual, land and other immovable tangibles (except structures owned by extraterritorial bodies; see paragraph 56) are considered always to belong to an economic entity of the economy in whose territory they are located, and nonfinancial intangible assets to belong to the economy that issued them. Therefore, a nonresident owner is shown as owning, instead of a nonfinancial asset of those kinds, a claim on some resident entity to which the ownership of such assets is attributed. In the same way, mobile equipment that operates in the territory of any economy for as much as a year is considered always to belong to that economy. In contrast, all other nonfinancial assets are stocks of the economy of which their owner is a resident, regardless of where they may originally have been produced or formerly owned and where they may presently be located. The foreign asset stock of an economy thus consists entirely of financial items, and this same stock can also be interpreted as the international investment position.

51. The balance of payments deals with virtually the same financial assets as the *SNA* and incorporates all the changes that result from the net provision of real resources to the rest of the world. The balance of payments also includes some of the changes in the value of claims and liabilities that are produced by what are classified in the *SNA* as revaluation or reconciliation items. In order to reconcile the change in the international investment position from the beginning to the end of a period with the capital account entries in the balance of payments for that period, those reconciliation items that have been omitted from the latter must be taken into account. The difference between an economy's claims on nonresidents, monetary gold, and SDRs, on the one hand, and its liabilities to nonresidents, on the other hand, conceptually represents the net worth of the economy arising from its relationship with the rest of the world.

CHAPTER THREE

Residents of an Economy

(1) Definition of Residents

52. The residents of an economy comprise the general government, individuals, private nonprofit bodies serving individuals, and enterprises, all defined in terms of their relationship to the territory of that economy. Included with the territory of an economy are its territorial seas and those international waters beyond its territorial waters over which the economy has or claims to have exclusive jurisdiction; overseas territories and possessions may or may not be regarded as separate economies.

53. The concept of residence underlying the definitions and rules adopted for this Manual is intended to be essentially the same concept that is used in the United Nations' *A System of National Accounts (SNA)*. The following discussion concentrates on elaborating the aspects of residence that are especially pertinent in a balance of payments context; in particular, it defines the residence of entities in terms of the sectors or parts thereof that are relevant in applying the classification scheme recommended in Chapter 8. Any differences from the wording of the corresponding passages in the *SNA* should not be taken as recommending a different coverage for the residents of an economy.

(2) General Government

54. The general government agencies that are residents of an economy include all departments, establishments, and bodies of its central, state, and local governments located in its territory and the embassies, consulates, military establishments, and other entities of its general government located elsewhere.

55. The general government of an economy covers all agencies of the public authorities not classified elsewhere: (a) government departments, offices, and other bodies, irrespective of whether they are covered in ordinary or extraordinary budgets, or in extrabudgetary

funds, that engage in administration, defense, and regulation of the public order, promotion of economic growth and welfare and technological development, provision of education, health, cultural, recreational, and other social and community services free of charge or at sales prices that do not fully cover their costs of production; (b) other nonprofit organizations serving individuals or business enterprises that are wholly, or mainly, financed and controlled by the public authorities and nonprofit organizations primarily serving government bodies themselves; (c) social security arrangements for large sections of the community imposed, controlled, or financed by the government, including voluntary social security arrangements for certain sections of the community and pension funds that are considered to be part of the public social security schemes; (d) unincorporated government enterprises that mainly produce goods and services for the government itself or that primarily sell goods and services to the public, but that operate on a small scale; and (e) public saving and lending bodies that are financially integrated with a government or that lack the authority to acquire financial assets or incur liabilities in the capital market.

56. Embassies, consulates, military establishments, and other entities of a foreign general government are to be considered as extraterritorial by the economy in which they are physically located. The construction of embassies, structures, and other works in extraterritorial enclaves by resident producers of the economy in which the enclaves are located is part of the production and exports of that economy. Wages and salaries paid to locally recruited staff of foreign diplomatic, military, and other establishments are payments to residents of the economy in which these establishments are located.

57. International bodies that do not qualify as enterprises (see paragraph 63), comprising most political, administrative, economic, social, or financial institutions in which the members are governments, form part of foreign general government for balance of payments purposes. Such bodies are not considered residents of any national economy, including that in which they are located or conduct their affairs. The employees of these bodies are, nevertheless, residents of a national economy, specifically, of the economy in which they are expected to have their abode for one year or more. In most cases, that economy will be the one in which the given international unit is located or in which the employees are engaged in technical assistance, peace keeping, or other activities on behalf of the international organization. It follows that the wages and salaries paid by the international organizations to their own employees are payments to residents of the economy in which those employees are stationed for one year or more.

58. In contrast, enterprises that are owned jointly by two or more governments are not treated as international bodies but are, like other enterprises, considered to be residents of the economies on whose territories they operate.

(3) Individuals

59. The concept of residence adopted for individuals is designed to encompass all persons who may be expected to consume goods and services, participate in production, or engage in other economic activities in the territory of an economy on other than a temporary basis. These are the persons whose general center of interest is considered to rest in the given economy.

60. In particular, the resident individuals of an economy are considered to comprise all persons living within the territory of the given economy except the following:

(a) visitors (tourists), i.e., persons in the given economy for less than one year, specifically for recreation or holiday, medical care, religious observances, family matters, participation in international sports events and conferences or other meetings, and study tours or other student programs;

(b) crew members of vessels or aircraft who do not live in the given economy but who are stopping off or laying over there;

(c) commercial travelers who are to be in the given economy for less than one year and employees of nonresident enterprises who have come to the economy for less than one year for the purpose of installing machinery or equipment purchased from their employer;

(d) employees of foreign governments and international bodies who are on a mission of less than one year in duration;

(e) official diplomatic and consular representatives, members of the armed forces, and other government personnel of a foreign economy (together with their dependents) who are stationed in the given economy;

(f) seasonal workers, i.e., persons who are, and will be, in the given economy explicitly for the purpose of seasonal employment only.

61. The categories of individual enumerated above are to be considered residents of the economy in which they normally live, that is, have their general center of interest. Border workers—persons who cross the border between two economies daily, or slightly less frequently but regularly, because they work in one economy but have their abode in the other economy—are residents of the economy in which they have their abode, not of the economy in which they are employed.

(4) Private Nonprofit Bodies Serving Individuals

62. All private nonprofit bodies classed as serving individuals are resident economic entities of the economy in whose territory the bodies are located or conduct their affairs. Such bodies are not entirely, or mainly, financed and controlled by organs of general government, and they furnish educational, health, cultural, recreational, and other social and community services to individuals either free of charge or at sales prices that do not fully cover their costs of production.

(5) Enterprises

(a) General definition

63. Resident enterprises are the actual or notional units that engage in (i) production of goods and services on the territory of a given economy, (ii) transactions in land located within the territory of that economy, or (iii) transactions in leases, rights, concessions, patents, copyrights, and similar nonfinancial intangible assets issued by the government of that economy.

(b) Types of enterprise

64. Enterprises are either privately owned and/or controlled or publicly owned and/or controlled and include both monetary and nonmonetary institutions.

65. Private enterprises include (i) incorporated enterprises, e.g., corporations, joint stock companies, limited liability partnerships, cooperatives, or other forms of business association recognized as independent legal entities by virtue of registration under company and similar acts, laws, or regulations; (ii) unincorporated enterprises, including those owned by nonresidents; and (iii) nonprofit institutions and associations mainly serving business enterprises and entirely, or mainly, financed and controlled by them. The private monetary institutions are deposit money banks, i.e., banks having liabilities in the form of deposits payable on demand that are transferable by check or otherwise usable in making payments; such banks may alternatively be characterized as the commercial institutions whose demand deposit liabilities are important or form a large proportion of their total liabilities.

66. Public enterprises are (i) public corporations (incorporated by virtue of company acts or other public acts, special legislation, or administrative regulations) that hold and manage the financial assets

and liabilities, as well as the tangible and nonfinancial intangible assets, involved in their business, and (ii) large, unincorporated government enterprises; both types sell to the public most of the goods or services they produce. The principal public monetary institution is usually the central bank, which is the publicly owned and/or controlled monetary authority; it issues currency and sometimes coin, and is commonly the chief holder of the international reserves of the country. The central bank also has liabilities in the form of the demand deposits of other banks and often of the government. Other public monetary institutions are deposit money banks.

(6) Special Implications of Definition of an Enterprise

(a) Breakup of single entities

67. The general rule governing the determination of the residence of enterprises (see paragraph 63) often makes it necessary to divide a single legal entity (e.g., a parent company operating in one economy and its unincorporated branch operating in another economy) or a single establishment (e.g., a pipeline or railway spanning the territory of two or more economies) into two or more separate enterprises. Each of these enterprises is to be regarded as a resident of the economy on whose territory its operations are carried out. The costs and proceeds of the separate units are to be calculated as if the units bought and sold at market prices, even though some, most, or all of what they receive from or transfer to the other units of the complex of which they form a part may be omitted from their records or entered only at a nominal value. The balance of payments entries should reflect the allocation to each member of the complex of an appropriate share of any common operating costs, including head office expenses and charges in respect of mobile equipment. The net income of the units should be shown as accruing to the economy where the head office is located.

(b) Mobile equipment

68. Situations involving mobile equipment—for instance, aircraft, ships, highway and railway rolling stock, fishing vessels, and gas and oil drilling rigs—often seem to present problems of residence. These problems, however, can be partly illusory; it must be kept in mind that it is not the residence of the mobile equipment that is to be decided but rather the residence of the enterprise that employs the equipment in its productive activities. The resident status of all enterprises is in fact to be governed by the same rule (see paragraph 63), whether the capital equipment that they use is immovable or mobile; an

enterprise is a resident of the economy on whose territory it engages in production.

69. Mobile equipment thus presents a problem of principle—in the sense that the residence of the enterprise operating it cannot logically be inferred from the above rule—only when it is used in production outside the territory of any national economy, i.e., in international waters or air space. Mobile equipment that merely moves between the territories of two or more economies should, in accordance with the above rule, be regarded as being operated by a separate enterprise in each of the economies where it is used in production. As a practical matter, however, equipment that moves frequently between the territories of various economies also poses a problem very similar to that of equipment used in international waters or air space. Therefore, a supplementary rule of thumb to deal with both of these cases is recommended in this Manual. This rule is that mobile equipment that is operated on more than one national territory during the course of a year, or outside any national territory, is to be attributed to a single enterprise with a determinate residence. That enterprise is considered to be the operator for aircraft, ships, highway and railway rolling stock, fishing vessels, gas and oil drilling rigs, or other mobile equipment that is not used for production primarily on the territory of any one economy for as much as a year or is used in international waters or air space.

70. In the decision on the residence of an enterprise conceived in accordance with the above rule, attention should be given to such attributes as the flag of registration of the equipment, the economy of incorporation of the company directing its operations, the residence of the owners of that company, and for an unincorporated enterprise the residence of the entity responsible for its operations. In addition, such circumstances as the fact that the equipment is subject to the laws, regulations, and protection of a particular economy, or that it is linked more closely to one economy than to others, could if necessary be taken into account.

71. In rare instances, considerations such as those in the preceding paragraph could point to more than one economy as being the residence of the enterprise operating, say, a transportation system or fishing fleet. In the case of an enterprise of that sort which is jointly organized and owned by residents of more than one economy, its transactions should be attributed to enterprises in the economies of each of its owners in proportion to the owner's share in the financial capital of the joint enterprise.

(c) *Agents*

72. Without exception, a transaction should be attributed to the economy of the principal on whose behalf a transaction is undertaken and not to the economy of the agent representing or acting on behalf of that principal. However, the services rendered by the agent to the enterprise he represents should be attributed to the economy of which the agent is a resident.

(d) *Residence of enterprises engaged in installation*

73. Problems of defining the residence of an enterprise are encountered where employees of a resident enterprise of an economy go abroad in order to install machinery or equipment that the enterprise has sold to nonresidents. In these instances, the installation services should be considered to be services that have been provided by the resident enterprise to a nonresident if the work of installation is carried out entirely, or primarily, by the employees in question and they complete the installation in less than one year. However, if a significant portion of the work of installation is performed by residents of the economy where the machinery or equipment is installed, the work of installation is likely to be substantial and will probably take a significant time to complete. Such services should then, in principle, be attributed to an enterprise resident in that economy.

(e) *Leased goods*

74. The general rule determining the residence of an enterprise applies whether it is using its own or leased capital goods. If such goods have been obtained under a financial leasing arrangement, the rule for determining the attribution of ownership of those goods should also be consulted (see paragraph 217).

CHAPTER FOUR

Valuation

(1) Concept of Market Price and Market Transactions

75. In common with the national accounting convention, balance of payments accounting employs a uniform system for pricing heterogeneous transactions in real resources and financial claims, so as to permit aggregation and intercountry comparison of the figures. As market prices are widely used in making resource transfers, the recommendation of this Manual is that they likewise be used for valuing transactions. The application of the market-price principle admittedly may give rise to major practical problems, both because of the large number of individual transactions whose values as originally reported could be in need of adjustment and because of the difficulties in devising suitable equivalents of market prices for those transactions that have not actually been market transactions. Nonetheless, no other principle of pricing adequately serves to measure the economic value of the resources transferred between economies in an equally meaningful way. It would not be appropriate, therefore, for this Manual to recommend for purely pragmatic reasons that some principle other than market price be adopted as the international standard.

76. Market price in the national accounts sense is conceived as the amount of money that a willing buyer pays to acquire something from a willing seller, when such an exchange is one between independent parties into which nothing but commercial considerations enter.¹ Any market price thus strictly refers only to the price for one specific exchange under the stated conditions, and the second exchange of an identical unit even under circumstances that were almost exactly the same in every respect could conceivably have a different market price. A market price defined in this way is to be clearly distinguished from a price quoted in the market, a world market price, a going price, a fair

¹This formulation of the concept is a paraphrase of the definition given in United Nations, *Draft International Guidelines on the National and Sector Balance Sheet and Reconciliation Accounts of the SNA*, E/CN.3/460 (July 24, 1974), para. 7.5.

market price, or any price of that kind which is intended to express the generality of prices for a class of supposedly identical exchanges rather than the one price actually applying to a given exchange. Furthermore, a market price should not necessarily be construed as equivalent to a “free market price,” i.e., a market transaction should not be interpreted as occurring exclusively in a purely competitive market situation. In fact, it could take place in a monopolistic, monopsonistic, or any other market structure. Indeed, the market may be so narrowly defined as to consist of the sole transaction of its kind between independent parties.

77. The notion of a market situation that stems from the definition above presupposes the absence of any affiliation or relationship between the parties to a particular transaction. In itself, this constitutes a sufficient condition for a particular transaction to be described as market oriented. The criterion of independence between transactors has been defined negatively as follows: “Two persons shall be deemed to be associated in business with one another if, whether directly or indirectly, either of them has any interest in the business or property of the other or both have a common interest in any business or property or some third person has an interest in the business or property of both of them.”²

(2) Transactions That May Lack an Actual Market Price

78. Although the conditions needed for establishing a market price according to the definition actually exist in at least a majority of cases with which the balance of payments is concerned, many important situations are encountered in which one or more of the essential elements are lacking. The following are examples of common circumstances under which a market price in its literal sense cannot be assumed to be determined:

- (a) an exchange of goods directly for other goods instead of for an amount of money, i.e., barter;
- (b) a transaction that occurs despite the fact that one party does not enter into the transaction “willingly,” e.g., tax payments;
- (c) a transaction in which a supposed buyer and seller are the same entity from a legal standpoint but constitute separate entities under balance of payments conventions, e.g., a branch and its parent enterprise;
- (d) a transaction between separate legal entities that are not independent, e.g., affiliated enterprises;
- (e) a transaction in which a legal change of ownership between the two parties involved does not actually occur, e.g., goods transferred under a financial lease arrangement; and

²Customs Cooperation Council, *Brussels Definition of Value*, Article II.

(f) a transaction undertaken for other than purely commercial considerations (i.e., one containing at least some element of a gift or grant), often one involving a private nonprofit entity or a general government body as one or both parties.

79. The circumstances enumerated above are by no means mutually exclusive. In any particular case, a market price may fail to exist because more than just one of the conditions necessary to establish it are absent.

(3) Market Price Equivalents

80. For purposes of balance of payments recording, therefore, it is sometimes necessary to resort to the expedient of developing proxies, or substitute measures, for market prices in those cases where no actual market prices have been set.

81. A customary approach is to construct such prices by analogy with known market prices that have been established under conditions that are considered to have been essentially the same. For example, if a buyer and a seller of given commodities customarily deal at a price reflected by some standard market quotations, those quotations could reasonably be used to value a barter exchange of the commodities between two such parties. Care must be taken, however, to limit this approach to those transactions to which it is really applicable. Transactions that are superficially alike may, in fact, be subject to implicit or concealed factors which strongly affect the value that should be placed on them.

(4) Affiliated Enterprises

82. As indicated above, transactions between affiliated enterprises integrated under the same management cannot necessarily be taken as market transactions because of the lack of independence among the parties to the exchange. But whether or not the transactions portrayed in the books of the enterprises actually reflect market values can only be judged for each individual enterprise. On the one hand, to the extent that a group of affiliated enterprises desires to allocate its gross earnings in a realistic fashion among its separate units, bookkeeping practices would have to reflect market-related pricing for all purchases and sales by the units. In that situation, the view might reasonably be taken that the pricing adopted for bookkeeping purposes, often referred to as transfer pricing, is no different from or, alternatively, is equivalent to market valuation. On the other hand, transfer pricing not based closely on market considerations could be expected to be

common among affiliated enterprises conducting business across national boundaries, since disparities between the taxes and regulations imposed by different governments are a main factor in management decisions on the optimum allocation of profits among units. In those circumstances it cannot be presumed that the mode of valuation adopted will accurately reflect economic relationships, e.g., the ratio of income to capital. Where the distortions are large, the replacement of book values with market value equivalents is desirable in principle.

83. The attempt to substitute market values for book values, however, raises questions of procedure and the choice of appropriate pricing measures intended for such a revaluation. Indeed, a value approximating the market price will frequently be difficult to estimate. The value to be placed on transactions among affiliated units is not necessarily equal even to the market price for any similar transactions of those units with outside parties, as by definition market prices are established in response to the demand and supply conditions prevailing in each specific market. Commodities that were otherwise physically indistinguishable might be viewed differently from a market standpoint and therefore have different market prices. For example, goods transferred to an affiliate might represent components but if sold to outside parties could constitute spare parts.

84. In determination of how far a transfer price deviates from or approximates a market price, the relevant comparison is not necessarily between the book value for the transfer of something from one affiliate to another and the market price for the sale of the same thing by an affiliate to an outsider. One way in which a transfer between affiliates may be evaluated is from the standpoint of its relative position in the chain of production extending to the point where a sale to an independent party actually takes place. The comparison could be made in terms of costs embodied up to that stage of production, and therefore a transfer price that did not seem commensurate with the cost of production which was incurred up to that stage would probably not be an adequate proxy for a market price. If the transfer price covered the cost of production, it could be accepted as a suitable proxy for a market price even though it was different from the price charged for similar exchanges between the affiliate and an independent party. The information on production cost available in the books of an affiliate may itself, of course, be affected by the use of transfer pricing for the input of goods and services acquired from its affiliates.

85. The exchange of commodities between affiliated enterprises may often be one that does not usually figure in an exchange between

independent parties (for example, specialized components that are usable only when incorporated in a finished product). Similarly, the exchange of services, such as management services and technical know-how, may not have a near equivalent in the types of transaction in services that usually take place between independent parties. The determination, for transactions between affiliated parties, of a value comparable to the market value may be very difficult, therefore, and compilers may have no other choice in practice but to accept a valuation in terms of explicit costs incurred in production or any other values assigned by the enterprise. Such values will probably not be entirely arbitrary, as the tax, customs, exchange control, and other public authorities usually exercise some influence over the accounting practices of these enterprises in order to put their activities on the same footing with regard to government regulations as activities between independent enterprises.

86. Since balance of payments accounting is based on the axiom of double entries, the implication is that any revaluation should in principle be applied consistently in the statement (see section (8), below). If, for example, the book value of merchandise shipped from a direct investment enterprise to its parent has to be replaced by a market-value equivalent, the double-entry rule requires, at least in principle, that the income and/or capital flows on direct investment also be adjusted by the same amount.

(5) Noncommercial Transactions

87. One important category of transaction that, by definition, is noncommercial and thus has no market price comprises the provision of economic values whose offset constitutes an unrequited transfer. In such transactions, one party provides nothing on which an economic value is placed in return for a real or financial asset received from the other party. Other transactions in addition to outright gifts may take place at an implied price that includes some element of grant or concession, so that those prices also are not market prices. Examples of such transactions could include exchanges of goods negotiated between governments and government loans bearing interest rates that are lower than would be consistent with the grace and repayment periods or other terms for purely commercial loans. Transactions by general government bodies and private nonprofit entities, which are not construed as being engaged in purely commercial undertakings, are often subject to noncommercial considerations. Unrequited transfers may also be provided or received, however, by other sectors of the economy.

88. For real resources handed over by the government or private nonprofit institutions of an economy to nonresidents without a quid pro quo, consideration of symmetry demands that the same values be reflected in the balance of payments of both the recipient and the donor. In conformity with the procedure adopted in the national accounts, such resources should be valued with reference to the explicit costs incurred in their provision.³ Transfers in kind by individuals should also be expressed in terms of the cost incurred in their provision. Imputations made in this way may not always approximate the desired basis of valuation, particularly since the values of noncommercial transactions as they appear to the donor will often be quite different from those that the recipient would be inclined to impute. It is suggested, as a rule of thumb, that the values assigned by the donor be used as a basis for recording.

(6) Financial Items

89. Changes in financial assets should be recorded in the balance of payments at the values underlying their acquisition or disposition. For financial items that are traded in an organized market, with the buyer and seller dealing with each other through an agent, the price established in the market—which will probably be the one that is recorded in the statistics in any case—will meet the definition of a market price for purposes of the balance of payments. For financial items not traded in the market, however, the application of the concept of market price may not be so apparent. In fact, cash items, i.e., those that can be redeemed on demand at their face value, have only one value which could be assigned for any purpose, so that this value could be regarded as the actual market price. The market price that is to be imputed to nonmarketable financial items, which are primarily loans in one form or another, is their face value.

(7) Problem of Uniformity

90. Charges and costs of various kinds that arise as a minor concomitant to transactions are sometimes considered to be included in the value of those transactions—especially if they are covered in the same contract—and at other times to constitute separate, additional transactions. Who presents the bill to whom for these charges is often dictated by trade practice, legal requirements, institutional arrange-

³The assignment of values in terms of explicit costs is consistent with the valuation in the SNA of the output of government and private nonprofit services that are characteristically not marketed. (United Nations, *A System of National Accounts*; see paragraph 6.71 concerning the valuation of goods and services that represent payments in kind of wages and salaries.)

ments, and similar factors that vary from country to country and with the kind of transaction. The distributive services associated with merchandise are a main case in which differences in practice could be important. This Manual's rules for achieving a degree of uniformity in the recording of distribution costs are set out in some detail in Chapters 10 and 11.

91. Taxes, duties, subsidies, rebates, discounts, and the like are another principal form of incidental cost (positive or negative) that either may be included in a transaction and taken into account in establishing its market value or may give rise to a separate transaction. When no other convention is specified (see, for example, paragraph 246), the recommendation is that the balance of payments entry should be the same in either case. Specifically, a tax, subsidy, or similar incidental charge on a transaction that can be said to be paid by a resident of one economy to a resident of another economy should always be included as part of the value of the transaction, whether such a charge is explicitly or implicitly covered in the contract or is payable separately. When not covered in the contract, a tax or duty should be added to the contract value, whereas a subsidy, rebate, or discount should be deducted.

(8) Consistency of Valuation for Interrelated Entries

92. A practical issue that may confront the balance of payments compiler is whether it is always preferable to adjust the statement to reflect market values when the size of the adjustments is substantial and a suitable means for making them can be devised. Two somewhat different situations are commonly met with in which this issue may arise.

93. First, the available data on the international transactions of a particular entity may be valued in a consistent way, but the underlying prices that have been used for compiling the reported data may be transfer prices (not based closely on market considerations) rather than market prices. The figures provided by the domestic affiliate of a foreign company, for example, might be based on such transfer prices. Views differ about whether adjustments are advisable under these circumstances.

94. Second, it is sometimes possible to make adjustments for valuation to items in only one or a few specified categories. An important standard component for which the valuation applied in the underlying statistics can occasionally be questioned is merchandise. A sampling of customs documents or a detailed comparison of the figures with partner country data may lead a compiler to conclude that at least certain kinds of goods are not valued at a reasonable

approximation of market values. Similarly, exchange records for goods may be subject to systematic overinvoicing or underinvoicing as a means of concealing capital movements. If other categories in the balance of payments have been valued consistently with the trade figures, the correction of those figures alone would be reflected in the residual item for net errors and omissions.

95. In support of the view that valuation adjustments are not usually warranted in these situations, it is argued that the use of figures valued from period to period on a consistent basis, even if that basis is not market valuation, will probably not produce any serious distortion of comparisons over time. Moreover, it is contended, the idea of a notional market value, to be adopted when the conditions that give rise to an actual market value are absent, is not very appealing, especially when the data needed to make the adjustment can be obtained only at considerable cost; a book value at least represents the value that the transactor has in fact assigned to the transaction and in most cases is readily available. Finally, the introduction of valuation inconsistencies is sometimes considered to be an undesirable practice because it produces net errors.

96. On the other side, it can be said that the use of values other than market values tends to misrepresent the relationship between the various components in the same statement and between the same items in the statements for different countries. In addition, the whole system of national accounting is predicated on valuation at market price or its equivalent; the fact that other values may pragmatically be adopted in other contexts is irrelevant. And finally, it can be pointed out that weaknesses in the statistics for certain components are rightly reflected in the item for net errors and omissions rather than concealed by allowing compensating errors in other components.

97. The general recommendation of this Manual is that any valuation adjustment should be made that will serve to bring the individual series in question closer in concept to market value, even in situations where the corresponding adjustments of related series are not possible. This recommendation, however, is not meant to be a blanket endorsement for the substitution of notional market values for reported values in a haphazard way. As the foregoing discussion in this chapter attempts to make clear, the selection of the best equivalents of market values as replacements for book values is an exercise calling for cautious and informed judgment. In most cases, sample surveys, contacts with enterprises and government agencies engaging in international transactions on a large scale, exchanges of information between compilers in partner countries, or similar statistical research will be needed to provide the basis for arriving at such a judgment.

CHAPTER FIVE

Time of Recording

(1) Recommended Timing

98. To achieve a simultaneous recording of the two entries for a given transaction in the double-entry system of the balance of payments, rules must be adopted governing the time at which transactions are deemed to have taken place. In this connection, the fact should be noted that in practice the two entries representing a transaction are often derived independently from separate sources of data, for which the principle of timing used could be different.

99. A contract usually involves a process continuing over time, and several aspects of that process can be assigned a specific date. For example, a party enters into a formal agreement to engage in a set of transactions (time of contract or commitment), provides goods or services and acquires a claim for payment, and receives settlement on that claim.

100. All the various times pertaining to a given contract have a significance from an economic standpoint. At the time of contract, for example, the price—and hence the risk for any price changes that subsequently may occur—is fixed for each of the transactions that may be covered under the contract. The time of legal change of ownership of the various assets provided under the contract, however, is generally considered to be the most relevant one for the types of analysis for which the national accounts, and the balance of payments in particular, are employed. Furthermore, many of the underlying data—specifically those derived from any type of accounting record—will already be at least approximately on that basis. Change of ownership, therefore, is adopted in this Manual as the basic principle with respect to timing; by convention, the time of change of ownership is normally taken to be the time that the parties concerned record the transaction in their books. For any entries reflecting transactions that do not actually involve a change of ownership, further rules of thumb have to be applied.

101. In many instances, no difficulty arises under this convention in perceiving the time at which the ownership of an asset changes. Numerous transactions consist of an exchange between two enterprises of, say, goods for financial assets, and accounting entries will be made in each company's books for this exchange, showing the same dates for the acquisition of the merchandise and the relinquishment of the financial asset, on the one hand, and for the acquisition of the financial asset and the relinquishment of the merchandise, on the other hand. Ideally, both parties also should be making their entries as of the same day. This treatment provides a fixed point of time to which a balance of payments transaction may be related.

102. When a contract covers more than one transaction—for example, the provision of a real resource and a related extension of credit—each of the transactions will have to be recorded in the balance of payments at the time it occurs. That is, when an importer makes payment (i.e., turns over cash to the exporter) before he acquires ownership of the merchandise (a prepayment), he must also be shown to acquire a claim on the exporter that remains outstanding for the duration of the interim period. Similarly, when an importer does not make payment until some time after he acquires the merchandise (a postpayment), he is shown in the meantime as having a liability to the exporter. These claims and liabilities are extinguished in due course, in the first instance by the delivery of the merchandise and in the second by the cash payment made for it. The creation and the extinguishing of an obligation, as well as the change of ownership of the merchandise and the payment for it, are to be shown in the balance of payments in the period in which each occurs.

103. Given the change-of-ownership criterion and the convention for implementing it, the rules that will produce a consistent timing for recording most other types of transaction can be indicated clearly. In general, the exchange of real resources and financial assets should be recorded when those items cease to be an asset in the accounts of the former owner and become an asset in the accounts of the new owner. Reinvested earnings of direct investment enterprises should be recorded when they are earned; other investment income, when it falls due for payment. Services should be recorded when they are performed. Unrequited transfers that are imposed by one party on another, such as taxes and fines, should be recorded at the time that they become due for payment without penalty; other unrequited transfers, when the resources to which they are offsets change ownership. Counterparts should likewise be recorded in the same period as the changes that they offset.

104. A contractual obligation of any sort (for example, for the payment of interest or the repayment of principal on a loan) that is not actually settled when it falls due is nonetheless to be recorded in the period when it does fall due. In a case of this kind, a new obligation must be recorded as having been created to take the place of the old obligation that was not settled. That treatment is recommended partly because the old and new obligations may have different characteristics (sector of domestic creditor or original maturity, for example) that will result in their being classified in different items.

105. Some merchandise transactions are recorded in the balance of payments even though no change of legal ownership occurs, specifically, transactions involving goods under financial lease arrangements (see paragraph 217) and some other goods shipped between direct investment affiliates (see paragraph 216). In order to achieve the same time of recording by both partners in those cases, a rule of thumb is needed. This Manual recommends for such transactions that the entries be made, whenever possible, as of the time that the merchandise crosses the customs frontier of the exporting economy.

(2) Need for Timing Adjustments

106. One consideration to be taken into account by compilers in choosing among the various statistical sources that may be available is the advantage of obtaining data that already have the correct timing. For example, records of actual drawings on loans are to be preferred to sources that quote authorization dates or program dates that will not necessarily be realized in fact. However, even the sources chosen by the compiler as generally the most suitable may not originally have been designed specifically to yield balance of payments information. Trade statistics provide a record of the physical movement of goods rather than a record of their change of ownership. An exchange record provides a listing of payments and may give no indication of whether any of those payments is made in advance of a change of ownership or afterward. Some common instances in which timing adjustments may be required are discussed in the following sections.

(3) Timing Adjustments to Merchandise Data from Particular Sources

(a) Trade accounts: general

107. Trade statistics are primarily a by-product of customs administration; they are not especially intended as a source of balance of payments statistics. Nonetheless, they are usually considered to

approximate the timing of ownership changes, because—in the absence of other evidence—physical possession may be the best available indication of actual ownership. One probable need for a timing adjustment to trade statistics arises from a failure in the statistics themselves to reflect physical movements correctly in all cases, although some systematic defects of that sort would not create noticeable errors unless the value of trade changed sharply from period to period. Such a defect, for example, arises when compilers of trade accounts cut off each month's statistics before all customs declarations have been tabulated, leaving a residue to fall into the next month. When practices of this sort lead to distortions, the amounts should be estimated and timing adjustments applied.

(b) *Trade accounts: length-of-voyage problem*

108. The change of ownership of goods can occur at times widely different from the recording of those goods in trade statistics when a lengthy voyage forms part of the process of importing or exporting. If the volume or unit value of trade changes substantially from the beginning to the end of the reporting period, the possible difference of one or two months between the shipment or receipt of goods, on the one hand, and the change of ownership, on the other hand, can be a source of error in the statement for a given country and of large asymmetries between partner countries. No empirical basis has been established for presuming that ownership normally changes either at the beginning or the end of a voyage; inquiries, perhaps on a sample basis, are required to ascertain specific practice, and timing adjustments should in principle be applied to correct the trade statistics for those classes of goods that are found to change ownership at a time other than that at which they are recorded in the trade statistics. Aggregation and comparison of world exports and imports on the basis of balance of payments data lose much of their meaning at times of rapid change in prices or volume when changes of ownership are not recorded at approximately the same time by each country.

(c) *Exchange record compilations*

109. Merchandise totals from an exchange record might well be subject to timing adjustments related to the receipt or extension of trade credit. Payment for merchandise may occur before ownership changes (involving a prepayment that creates a financial asset for the importing country) or afterward (implying receipt of trade credit, a liability for the importing country until settlement is completed). The exchange record of merchandise should be adjusted to arrive at the

correct timing for changes of ownership, with corresponding amounts entered in the capital account to cover the financing provided between the time of change of ownership and the time of payment.

(4) Adjustment of Statistics on Transactions Other Than Merchandise

110. Timing adjustments to categories other than merchandise are not often made in balance of payments compilation, although some exceptions are noted below. In practice, services tend either to be equated with the payment made for them or to be estimated from other evidence with no readily discernible need for timing adjustments; changes in the ownership of financial assets are not usually measured in any way that would give an incorrect timing; and unrequited transfers are invariably measured by the actual movement of goods, the provision of services, or the actual transfer of a financial asset. However, the following circumstances are frequently encountered and comprise principal examples where source data other than those for merchandise may require timing adjustments before they are used in the balance of payments.

(a) Freight and insurance on merchandise

111. As with exports and imports, the associated freight and insurance payments may be recorded at one time and the service may be rendered earlier or later. Timing adjustments would then be required in the current account if the payments figures were used to measure freight and insurance, with corresponding entries in the capital account for claims associated with the prepayment or post-payment.

(b) Interest due but not paid

112. Interest should be included at the time it falls due. Where payment is not made at that time and payments data are used to measure the item, adjustments would be required in the current account, together with an offsetting credit (debit) entry in the capital account for the claim associated with nonpayment, i.e., an increase in liabilities (assets).

(c) Other services

113. Services should in principle be included in the period in which they are rendered, and any obligations for earlier or later payment become capital account items. For example, the payment for port services for ships might be delayed if foreign exchange was not immediately made available to the shipping enterprise that owed bills

for stores and repairs already received. The entries for the services provided should be made in the "other transportation" item when the obligation to pay is incurred and offset by entries in the capital account representing increases in postpayment obligations. When service figures are derived from payments records, timing adjustments may be required in the current account so that the entries reflect services rendered in the period.

(d) *Contractual loans*

114. Although statistics on loan transactions may be available according to authorization or other program dates, compilers cannot always use such statistics for loan drawings without adjustment, because the actual disbursements (as required for the balance of payments) may differ from the program originally authorized. For interest payments and loan repayments, however, scheduled dates rather than actual payment dates should in principle be used for repayments that are not made on the date that they fall due. When repayments are delayed, the entries should show the discharge of the original obligation when it was due and its replacement by a different obligation, perhaps under rescheduling or waiver agreements. If the items concerned were based on payments data, appropriate adjustments would be required.

CHAPTER SIX

Unit of Account and Procedures for Conversion

115. The data on the values of transactions in real resources and financial items from which the balance of payments is compiled are expressed in a variety of national currencies or, occasionally, in other standards of value, such as a quantity of gold or the SDR. These underlying values for each economy must be converted into a single unit of account in order to put together its balance of payments statement. Furthermore, a universal unit is needed to facilitate intercountry comparisons and to permit aggregation on a regional or worldwide basis. This chapter discusses the choice of a unit of account and the manner in which conversion into that unit is to be made.

(1) Unit of Account

(a) *General considerations*

116. Two considerations should be taken into account in the selection of a unit. First, the unit should preferably be a stable one, stability in this context being understood in a very specific way. A unit is stable when the prices of the international transactions in question expressed in that unit are not affected by changes (relative to the unit of account) in the values of the currencies in which those transactions take place. For example, when the impact of a currency realignment brings about an increase of x per cent in the prices of international transactions expressed in currency A and of y per cent in currency B, a decrease of z per cent in currency C, and comparatively little change if any in currency D, currency D is to be regarded as the stable unit. Transactions expressed in a unit which is stable in this limited sense may nonetheless reflect price changes resulting from causes other than changes in the relative values of transaction currencies; that is, a series expressed in a so-called stable unit of account is not the equivalent of a volume or constant-price series.

117. The second consideration is the convenience of having a unit that can be expected to be reasonably familiar to most users of

balance of payments statistics. This unit may well be the one in which related economic data, such as trade or banking statistics, are customarily expressed. On this consideration, the construction of an "old gold," "pre-realignment," "adjusted," or other notional unit to serve as a stable unit of account is not advisable.

118. While the difficulties that would be encountered in constructing an artificial unit, therefore, may not have to be confronted directly, exactly the same problems arise in deciding which existing unit can be regarded as the stable one. A principal difficulty is the practical one of measuring the price component in the values of international transactions when expressed in various units of account—and specifically in singling out that part of price changes that can be attributed to changes in the exchange rate of the transaction currencies relative to other units of account—in order to gauge the comparative stability of the various possible units. Such a determination, in fact, can probably never be made for international transactions other than trade in commodities. Moreover, even for merchandise, the prices of different goods and of the same goods produced in different countries can react differently to the impact of a currency realignment, so that the unit that would be preferred is not likely to be the same one for each individual country. For these reasons, the theoretical ideal of expressing the balance of payments in a stable unit of account, let alone finding some universal unit that can be regarded as stable, is not actually an achievable one, even though rational estimates must be prepared.

(b) *National presentations*

119. One unit of account that a compiler naturally will want to consider using to express the balance of payments is the national currency of the compiling country. A balance of payments statement expressed in that unit will be directly comparable with the national accounts and most other economic statistics available for the country. Moreover, many of the basic statistics, for instance customs returns and banking data, will already have been expressed in the national currency. If the price of the national currency, however, has not remained constant relative to the price of the country's main reserve components or to the price of the currencies in which its international transactions are primarily denominated, the suitability of a national currency statement for many of the applications for which the balance of payments is designed may be seriously impaired. For example, an apparent growth in current transactions when expressed in national currency could occur merely because the national currency was not stable and had depreciated in comparison with currencies that were

actually used for the transactions, a circumstance that might complicate the analysis of balance of payments developments.

(c) *Reporting to the Fund*

120. Balance of payments statements in a universal unit of account, common to all countries, are needed for the Fund's purposes. The decision as to which of the familiar units is the most satisfactory to use as the universal unit is a matter of judgment. Moreover, the unit may be changed from time to time, depending on developments in the relationships among transaction currencies and on the time span covered by the balance of payments statistics for which a unit of account is being selected. In reporting to the Fund, countries are requested to express their statements in whatever unit of account they have adopted for their own use. (This request presupposes of course that, if a country with a multiple exchange rate system prepares its statement in its national currency, it will do so at a unitary rate, as recommended in paragraph 130.) The Fund may then, for its purposes, convert the figures into the universal unit that it finds most suitable in the light of existing circumstances.

(2) Procedures for Conversion

121. To provide a background for the discussion of problems that arise in converting from transaction currencies into the chosen unit of account, this section deals first with the theoretical aspect of the subject. The method that would seem most appropriate in principle, however, is found to be one that could rarely if ever be implemented by the balance of payments compiler. Therefore, the section then proceeds to review the practical options that are open to the compiler in choosing an exchange rate and in applying that rate to the original data reported to him in transaction currencies or other units of account.

(a) *Principle applicable to conversion*

122. It will be recalled that the values reflected in balance of payments entries are based on the market prices of the real resources or financial items concerned (see Chapter 4). Such a price—or, in some contracts, the basis for calculating it, which amounts to the same thing—is given in the contract made between the two parties. The particular market price (or basis for it) established at the time when the contract is made cannot be affected by subsequent developments; any provision for renegotiating the price, for instance, is tantamount to an agreement to cancel the contract under stated conditions and

enter into a new one. Any difference between the market value at which an item was acquired (the value under the contract) and the value that it may come to have up to the time that another contract is made to dispose of it is said to represent a valuation change. These valuation changes are by convention not to be included in the balance of payments.

123. A parallel line of reasoning applies, in principle, to conversions. The market value of a transaction is uniquely determined at the time when the contract to acquire the item is made, regardless of the currency or other unit in which that value may be expressed. Therefore, the value of a transaction expressed in a unit other than the transaction currency named in the contract is to be found by converting at the relationship between the transaction currency and that unit (the exchange rate) which existed at the time when the contract was made; if that method were not applied, the market value in terms of a unit other than the transaction currency would not have to be a single, determinate value but could vary as the relationship changed. In reality, the effect of any change in the exchange rate between the time when a contract is made and the time when that contract or any relevant portion of it is executed (e.g., the time of delivery or the time of payment) is to produce a change in the value of the item covered by the contract when expressed in a unit other than the transaction currency. Valuation changes of that sort, like valuation changes resulting from any other cause, are by convention not to be included in the balance of payments.

124. This principle governing conversion may be illustrated by the following example. At the time when a contract is made to buy and sell a financial item at a market value of 100 units of the currency named in the contract (the transaction currency), 0.8 unit of the transaction currency is exchangeable for 1.0 unit of national currency. By the time of delivery specified in the contract, the exchange rate has changed so that 1.0 unit of transaction currency is equal to 1.0 unit of national currency. The buyer of the asset, upon receiving delivery, may record a net increase in holdings of that asset of 100 units in terms of national currency. That net increase reflects the market value in national currency of 125 units which the asset had when the contract was made and a valuation change of 25 units by the time of delivery because of the change in the exchange rate. The change in holdings excluding the valuation change is thus 125 units, the figure arrived at by converting the market value of the asset expressed in the transaction currency at the time when the contract was made, using the exchange rate which existed at that time. That change is also the one that should in principle be recorded in the balance of payments.

125. The foregoing example can also be referred to in emphasizing a fact worth noting about conversions into a unit whose price relative to that of a transaction currency changes, namely, that such conversions are in themselves a source from which valuation changes stem. It can readily be appreciated that the buyer in the case set out above has experienced the valuation change only because the value of the asset obtained in the transaction has been converted into national currency; in the transaction currency, the value of the asset has remained unchanged. By a sale of the asset, of course, that valuation change could readily be realized (converted into a capital loss), which would make it subject to balance of payments recording. Thus, if the buyer were to sell the asset again during the same recording period for 100 units of the transaction currency, the net entry in the balance of payments expressed in that currency would obviously be zero. When the balance of payments is expressed in national currency, however, a net debit entry of 25 units results, reflecting first the increase in holdings of 125 units and then a decrease of 100 units (the latter on condition that the exchange rate that had prevailed at the time of delivery did not change thereafter). The net entry in national currency represents the realization of the capital loss that was implicitly part of the transaction disposing of the asset (see paragraph 41). That loss came about solely through a change in the exchange rate for the national currency relative to the transaction currency; no such loss could occur (at least through exchange rate fluctuation) when the transaction is expressed in the original transaction currency. This point has practical implications, as discussed in paragraph 135.

(b) *Choice of rates for conversion*

126. The exchange rates that the parties would actually take to be the prevailing ones at the time when they entered into a contract cannot be ascertained with absolute certainty. Two logical alternatives present themselves, however, as the most likely possibilities.

127. First, under the Bretton Woods regime, exchange rate fluctuations were for the most part limited to movements within a narrow band around fixed par value relationships. Transactors in general may not have taken much account of these minor fluctuations in setting their prices. Moreover, a tendency could have been expected for the fluctuations to average out over a period, making the average market exchange rate equivalent to the par value. In view of such considerations, previous editions of the Manual recommended par value conversions when the transaction currency bore a fixed relationship to the unit of account, at least when that relationship was in fact being effectively observed apart from the minor fluctuations permitted

within the narrow band. This recommendation still seems defensible in the type of situation for which it was conceived.

128. In contrast, where wider margins and floating rates are prevalent for transaction currencies, no basis exists for inferring that transactors would view as the prevailing rates any other than the spot rates being quoted in the foreign exchange markets, which reflect the rates they could actually obtain if they were to make a conversion at that time. Therefore, the exchange market rate on the contract date for spot delivery of the transaction currency against the unit of account can be taken as the rate that in principle is most satisfactory for conversion when the transaction currency is floating.

129. When two or more exchange rates for a given currency are applicable to different categories of transaction, the situation becomes theoretically very complex. In essence, the effect of multiple exchange rates is usually little different from the effect produced by an indirect tax (e.g., an import duty) or a subsidy, which is regarded as an unrequited transfer between residents, i.e., the government and the exporter or importer. The amount of this tax or subsidy would be determined by the difference between the rate applicable to the transaction and the notional, unitary rate that would be established if all international payments were channeled through an uncontrolled market. That notional rate could be considered as the equivalent of either an equilibrium rate that the authorities would be able to defend under a system of fixed par values or a market rate prevailing under a regime of free floating.

130. The above line of reasoning suggests the use of a unitary rate for conversion by an economy with a multiple exchange rate system that wished to express its balance of payments in the national currency, in order to avoid expressing transactions at a value that included an element of unrequited transfers between residents. The determination of a realistic rate under such circumstances, of course, has always proved to be a very difficult matter in practice. Any profit or loss actually realized by the authorities from the operation of a multiple rate system is considered to be, for the most part, of domestic origin, i.e., the net result of the indirect taxes on and subsidies to residents exchanging foreign currency for national currency, and vice versa. It would therefore not form part of the balance of payments.

(c) Problems of implementation

131. The theory that conversion from transaction currencies to the unit of account should be made in such a way as to reflect their relationship at the time when the contract was entered into is quite

straightforward. In practice, however, few data collection procedures specifically call for information on the contract date of transactions, and without that information no method of conversion that can be applied will produce figures which are more than an approximation of the values that are conceptually appropriate. In fact, such little evidence as is available suggests, at least for merchandise, that the interval between the date of contract and the date on which a transaction is recorded in the balance of payments is typically a long one, often extending to months rather than merely days.

132. A second problem is that usually the figures reported to a balance of payments compiler are already expressed in a unit of account (probably the national currency), having often been converted into that unit by their originator through methods over which the compiler has little control and about which he may have only sketchy information. For example, trade figures may be converted by customs officials in accordance with legislative prescriptions, whereas information supplied by enterprises would reflect the accounting conventions adopted for their bookkeeping. A balance of payments compiler, therefore, is not likely to be able to devise any method for converting these figures into still another unit of account that could achieve the objective that was considered theoretically desirable. Empirical indications are that a country's foreign trade will not be conducted predominantly in any one currency, even when the country's own currency is generally recognized as an international transaction currency; initial conversions by others of much of the "basic" data to which a balance of payments compiler has access is thus almost inevitable.

133. Adjustments of the kind that would be needed to correct deficiencies arising from both of these situations have rarely if ever been attempted. The only feasible procedure that can be suggested for making further conversions is the one that is commonly applied—namely, to convert at an average of the market rates that prevailed during the period in which the transaction was recorded. The sort of average that should be employed for this purpose is not a matter of great significance, in view of the inexact results that will be achieved by any practicable method of conversion.

134. In exceptional instances, however, enough information may be available about certain categories of transaction and certain large transactions to allow the compiler to make conversions at the rate that is specifically applicable to the transaction. Thus, transactions with the Fund take place at rates that can be precisely determined in terms of the SDR and most currencies, regardless of the original units in which the items involved in a particular transaction may be denominated.

Trade in ships and aircraft is an example of the kind of large transaction for which the compiler might be able to ascertain a rate that was more appropriate than an average market rate.

135. The practical necessity for using an average of the market rates during the period in which transactions are recorded will have the effect of eliminating some capital gains and losses that should, in principle, be covered in the balance of payments, as fluctuations in the rate during a period that can give rise to valuation changes (see paragraph 123) are ironed out by using an unchanged rate for a whole period. Moreover, the total change in the amounts outstanding between two dates in terms of a unit of account, requested as supplementary information for reserves, cannot be found by taking the difference in terms of the transaction currency and converting it at some average rate. Instead, the figures for holdings must be converted first, at the rate applicable to each date, and the difference then derived directly in terms of the unit of account. The rationale of this procedure can be explained by likening it to the occurrence of two transactions, one whereby assets are acquired under a contract made on the first day of the period and another whereby assets are disposed of under a contract made on the last day.

136. A special problem arises when two transaction currencies are named in a single forward contract. Neither of those two currencies may be the desired unit of account, and the exchange rate relationship between the two that can be inferred from the contract may well differ from the relationship implied by their respective relationships to the unit of account at the time when the contract was made. When this happens, conversion into the unit of account by use of the market rates for that day would give two different results, depending on which currency was taken as the basis for the conversion. For example, the market relationship between the unit of account, U, and two contract currencies, A and B, might be $U 1 = A 2 = B 5$ at the time when a forward contract is made, while the contract called for the purchase and sale of A 200 against B 550. The value of the contract would thus be either U 100 or U 110, depending on whether the contract value in terms of A or B, respectively, was converted. A reasonable solution in this instance is to consider that the two parties are equally exposed, in principle, to the price risk in undertaking the contract; this leads to the conclusion that conversion into the unit of account should be made at the average of the relationship between the unit of account and each of the two transaction currencies prevailing at the time when the contract is made. In terms of the preceding example, the value of the transaction under the contract would then be taken as U 105.

137. A question can be raised as to whether conversion at an average of the market exchange rates prevailing during the period in which a transaction is recorded in the balance of payments—the method commonly followed in practice—will always produce entries that in principle are internally consistent. For example, merchandise may change ownership in one period but be paid for in an earlier or later period, when the exchange rate may be different. As explained in Chapter 5 (paragraph 102), a difference in timing of this sort will give rise to entries for both the creation and the extinguishing of an obligation; of these entries, one will be the offset to the merchandise entry and the other the offset to the payment entry. Since both entries of each pair will be recorded in the same period and will thus be converted at the same exchange rate, the statement for each of the two periods will still be in balance after conversion. The value of the two pairs may be different, however, because of a change or changes in the exchange rate that came about after the contract was made (see Chapter 2). When conversions are made at the market rates for the period in which the transaction is recorded in the balance of payments, therefore, both entries of either pair may in fact contain an equal but offsetting error that is due to a valuation change, which by convention should not be included in the balance of payments. These errors could be avoided only by converting all the entries associated with a single contract at the exchange rate prevailing when the contract was made, as would be appropriate in principle.

CHAPTER SEVEN

Analytic Presentation

138. The analytic presentation of the balance of payments simply means classifying its standard components (see Chapter 8) into two or more categories according to whatever attributes are considered relevant for examining some particular aspect of a country's international economic relationships. The selection of the categories is a matter of judgment, and the interpretation to be placed on the resulting balances often has implications of a policy or political nature; analytic presentation, therefore, is likely to be a controversial subject. Its discussion in this Manual is intended to be descriptive and illustrative; this chapter should be understood in that light and not as a statement of Fund recommendations about the kinds of approach that it would always be appropriate for countries to adopt for their own purposes.

139. One point that should be apparent is that no statistical measure of payments balance can be used as a substitute for qualitative appraisal in examining the state of an economy's balance of payments, although several balances taken in combination can certainly be helpful in conveying a summary impression of the main elements. Moreover, balances are often affected by special circumstances that must be taken into account in interpreting the figures that purport to measure any given concept of imbalance. Finally, balance of payments statements, however presented, must be read in the light of other developments in the national and world economic situation that also have a bearing on the surpluses and deficits that can be compiled from the standard components.

(1) Construction of an Analytic Presentation

140. Conceptually, the net sum of all the standard components of the balance of payments is zero. When the components are divided into two analytic categories, therefore, the net sum of each category will be equal numerically, but one will be a net credit and the other a

net debit. The net sum of such a category is referred to as a “balance,” a “partial balance,” or a “payments balance.” A balance showing a net credit can be termed a “surplus,” and one showing a net debit can be termed a “deficit.”

141. In an analytic presentation, the standard components are usually arranged in a column, with all those components that comprise one of the analytic categories being listed first. The statement may then be visualized as being separated into the two categories by a horizontal line drawn between the last component of one category and the first component of the other. The surplus or deficit of the first category is thus the sum of the components said to be “above the line,” while the surplus or deficit of the second category is the sum of the components appearing “below the line.”

142. The same procedure may be followed to divide the statement into more than two categories, in which case more than one horizontal line will notionally have to be drawn. Each line will still denote the net sum of all components above it (or below it), including those that may also form part of other balances. The statement will then show two or more versions of the balance above (below) the line. The lower down in the statement the line is drawn, the more comprehensive the balance above the line becomes.

143. The standard components in this Manual are listed in an order that is quite neutral. Nevertheless, for some approaches it is possible, with a minimum of rearrangement of the components, to draw successive lines representing several of the balances most commonly employed. To obtain still other balances, however, more extensive rearrangement would be necessary. Furthermore, the individual components have been selected partly to permit the construction of as many different balances as possible; that is, the classification scheme of this Manual has been devised in such a way as to bring out characteristics of the transactions that are considered especially relevant from the standpoint of balance of payments analysis. Any selection confined to a manageable number of components, however, must inevitably fall short of satisfying some conceivable analytic interests. In particular, a compiler could not reasonably be asked to go very far in classifying transactions according to the underlying motivation of the transactors—a factor which plays an important role in a number of analytic concepts—unless that motivation were thought to be associated with some observable characteristics of the transactions.

144. One troublesome question that is likely to come up, no matter what balance it is desired to construct, is how to deal with the residual item for net errors and omissions that almost always forms part of a balance of payments statement. Insofar as components above and

below the line both contribute to the residual, the inclusion of that item either above or below the line will produce an inaccurate measure of the balance. The usual practice is to include the residual item with the category of components for which the statistics are believed to be least reliable. When the residual varies considerably from period to period in size or in sign and there is evidence to suggest that the variations reflect mostly unrecorded short-term movements of capital, the residual item is often included in the category which contains the recorded components that show similar movements. Another procedure, less common, is to show two versions of the balance, one including and the other excluding net errors and omissions. This latter treatment, in effect, leaves it to each user to decide for himself how he wants to handle the problem.

(2) Common Types of Analytic Balance

145. The number of ways in which the standard components can be combined, and thus the number of analytic balances that can be derived, is obviously large. Some of the balances encountered in practice differ from one another only in the inclusion or exclusion of a single component, because the advocates of a particular balance may see considerable significance in such a difference. Various balances have a tendency, therefore, to shade into each other over a continuous spectrum that ranges from the trade balance at the least inclusive end to the balance financed by official reserves at the opposite end. In the following discussion, related balances are grouped into several sets and described under a few main headings. That grouping is not meant to be a normative one and is introduced solely as a way of organizing the exposition. The discussion by no means exhausts the list of balances that have been employed from time to time to facilitate the analysis of developments in various countries' international economic relationships. It does, however, cover many of the broad types given prominence in the publications of member countries and international organizations.

146. In the view of a number of analysts, developments in the international monetary system since 1973 have greatly reduced the economic significance of overall balances of the type that are described in subsections (b) and (c), below. Indeed, the United States decided in mid-1976, following the recommendations of an advisory committee of experts from the private sector, to discontinue official publication of all balances of that kind; it was considered that these balances might be encouraging preconceived and perhaps misleading conclusions about the balance of payments. Among the reasons cited for this decision were the widespread floating of exchange rates, with

discretionary official intervention, and large accumulations of foreign exchange by official holders in some other countries that could be more in the nature of investments than of reserves. Another factor was the statistical difficulties encountered in drawing the distinctions among different kinds of capital flow that were needed to construct the several versions of the overall balance then being published by the United States. Insofar as the data were available, however, the U.S. statistics were to continue to be presented in sufficient detail to permit the users to calculate for themselves any of the traditional balances that they still found useful. Moreover, several partial balances of the sort described in subsection (a), below, were to be shown as memorandum items in the official tables because of their economic significance, linkage to other economic accounting systems, and wide use in international comparisons.

147. The terminology that has been applied in this Manual to identify various balances is not likely to be very illuminating to users who are not already familiar with the concepts concerned. For one thing, the same balance may sometimes be described by reference either to the components above the line or to those below the line, as in the so-called overall balance or official settlements balance. Moreover, the same term is often used to cover two or more similar but not identical versions of a particular concept. In practice, therefore, it is desirable to specify precisely the components of any balance that is being employed.

(a) *Balances on goods, services, income, and unrequited transfers*

148. A balance on goods, services, and income, or that balance plus either private unrequited transfers or all unrequited transfers, is commonly referred to as the "current" balance or "current account" balance. The balance on goods, services, and income alone measures the net transfer of real resources between an economy and the rest of the world. The balance on goods, services, income, and all unrequited transfers represents the transactions (apart from valuation changes and the like) that add to or subtract from an economy's stock of foreign financial items. The balance that includes only the private portion of unrequited transfers can be seen as an adjusted version of either of the other two. In this version the formal distinction between labor income (a component of income) and workers' remittances (an unrequited private transfer) is taken to be of little interest; when workers' remittances form the largest part of private unrequited transfers, therefore, it may seem desirable to add the latter to the balance on goods, services, and income. Moreover, official unrequited transfers are treated for some purposes as being closely akin

to official capital movements. When they are to be considered in this light, they are excluded from the current balance, which will again be composed only of goods, services, income, and private unrequited transfers.

149. The current balance, of course, is not comprehensive enough to permit a rounded evaluation of the major developments in a country's balance of payments. A deficit on the version of the current account showing goods, services, and income, for example, could be regarded as the normal and desirable situation for a country that needed to import real resources for development purposes. Conversely, a current surplus might be judged unsatisfactory if it were smaller than the amount required to sustain capital exports at what was considered an appropriate level.

150. The current balance is nonetheless a useful tool. For one thing, it wholly covers transactions of types that can generally be regarded as irreversible once they have occurred, whereas the acquisition of claims or the incurrence of liabilities is frequently subject to reversal, even in the short run. For this reason, it is usually more feasible to measure or forecast the effects of economic developments and policy changes on the current balance than on any balance that includes capital components. Balance of payments targets, therefore, are often expressed in terms of the performance expected of the current balance.

151. The statistics required to measure the current balance are frequently among those that contribute importantly to the net errors and omissions in the balance of payments. Nevertheless, the residual item is seldom included as an element of that balance. The components of the current balance are usually not very volatile and, indeed, may not even be prone to show large changes in the short run. The errors in those figures are thus rather typically of a persistent or systematic character, thereby often affecting the level of the balance more than its changes from period to period. For that reason, intercountry comparisons of current balances need to be interpreted with more caution than comparisons for a given country over time.

(b) Balances financed by reserve assets and selected liabilities

152. A type of balance that has found general use comprises above the line all standard components except reserve assets and, in most cases, certain selected liabilities that may be regarded as being related in some way to those reserves. Because a balance of this kind is, by its nature, the most comprehensive of the several balances that may appear in a statement, it is often termed an "overall" balance. It is also

occasionally referred to by some such term as the “official settlements” balance, in consequence of the fact that it is most easily measured as the net sum, with sign reversed, of the rather few components appearing below the line, i.e., reserve assets and any selected liabilities. The rationale of this concept is to provide a measure of the residual imbalance that is financed through the use and acquisition of reserves and sometimes of other financial items that could be seen as a substitute for them.

153. In principle, the authorities need to make use of reserves only if they want the exchange rate for their currency to be different from the rate that would be established by transactions in the exchange market. The logical inference would be that the overall balance is most meaningful for a country maintaining a fixed exchange rate and least relevant for one with a rate that was allowed to float freely. Despite the general resort to flexible rates early in 1973, few currency relationships have been allowed to fluctuate in a manner approaching free floating. Moreover, the Second Amendment to the Fund’s Articles of Agreement seeks “to assure orderly exchange arrangements and to promote a stable system of exchange rates.” The overall payments balance, therefore, remains relevant as one of the available tools of analysis. In the appraisal of that balance, however, it has also become necessary to take into account any changes that have occurred in the exchange rate for the national currency.

154. In the construction of a balance of the overall type, a main question that arises is what financial items in addition to reserve assets shall be excluded from above the line, on the grounds that they have some relevant characteristic in common with reserves from an analytic standpoint. The use of Fund credit, for example, is one form of liability that is almost always taken to be related to reserves, as it resembles a drawing on the reserve position in the Fund (classified as a reserve asset) in that neither may take place except to finance a balance of payments need. The difference in this case lies wholly in the largely irrelevant fact that a member’s drawing on its reserve position is unconditional, while various conditions are attached to the use of Fund credit. For many other financial items, however, the degree of similarity to reserve assets is much more a matter of opinion.

155. Some versions of the overall balance go quite far in associating other financial items with reserve assets below the line. Under one of these approaches, it is considered that all the foreign liabilities of the monetary authorities and some portion of the foreign claims (in addition to any that may already be counted as reserves) and liabilities of the deposit money banks are or may be virtually interchangeable

with, or a close substitute for, reserve assets. In this instance, the liabilities of the authorities and at least the short-term element of banking capital are excluded from above the line, i.e., all such financial items are shown not as a factor contributing to the outturn of the overall balance but as a source of financing for that balance. If the authorities have reason to expect that the deposit money banks will more or less automatically supply a substantial part of the financing needed to bridge any imbalance on other transactions in real resources and financial items, this version of the overall balance may be the one preferred. Moreover, a balance of this sort helps to bring out the link that exists between external transactions and developments in domestic liquidity.

156. A second comprehensive version seeks to refine the measurement of overall performance by excluding from above the line any transactions—in addition to the use of reserve assets—in which the authorities engage for the specific purpose of making up for a surplus or deficit in the rest of the balance of payments. “Compensatory official financing” is one name that has been given to balances of this kind. The problem here is that the motivation for extending and accepting official financing of various sorts may be ambiguous and is likely to be subject to interpretation on the part of the compiler of the presentation, so that this way of measuring the balance can be strongly influenced by a judgmental element. In addition, since the partner countries may be deemed to have different motives, this measure may turn out to be particularly asymmetrical, a characteristic which tends to complicate its use for intercountry comparison.

157. Any approach to the construction of an overall balance under which the results achieved in practice depend heavily on judgment by the compiler in interpreting and applying an underlying concept, such as that just described, is obviously subject to reservations. An opposite approach would be to exclude from above the line, in addition to reserve assets, some uniform set of liabilities defined in terms of objective criteria. One list of this sort that the Fund, among others, has regularly used comprises liabilities that are considered by the foreign creditors as part of their reserve assets; such liabilities are shown separately in the list of standard components in this Manual (Chapter 8). A major consideration for the Fund in adopting this particular criterion was symmetry, as the analysis of payments developments from a global viewpoint is often made easier when overall surpluses and deficits are in principle taken as being of equal magnitude, as they would be when reserve assets (exclusive of “revaluations”; see paragraph 454) and the corresponding liabilities form the items below the line for all countries.

158. This method of measuring an overall balance, of course, is not without important drawbacks of its own, and even its proponents admit that the figures it yields must be interpreted with caution. Specifically, the concept can be thought of as objective and symmetrical only in a formal sense, as its meaning can vary widely among countries in different circumstances and may change over time even for a single country; indeed, some consultants on the Manual project emphasized that they considered the concept to be inappropriate for their own countries. In addition, from a practical standpoint, the debtor will probably not be able to match liabilities exactly with the corresponding assets classified by the creditors as reserves.

159. An overall balance is commonly considered to be a measurement of balance of payments "performance." For reserves, however, the list of standard components provides for the reporting of supplementary information on total changes in holdings and counterpart items, in addition to the changes that come about through transactions between two parties (i.e., that involve changes of ownership; those additional changes, so-called revaluation changes, are attributable to the monetization/demonetization of gold, allocation/cancellation of SDRs, changes in prices of the items when expressed in the unit of account, and reclassifications. Such supplementary information makes it possible to reconcile items on a transactions basis above the line with total changes in the level of reserves, the counterpart items forming an intermediate category between an overall balance on the performance basis, on the one hand, and such total changes in reserves, on the other hand. The provision of this additional information reflects a view that the authorities may be influenced in their policy decisions not only by certain designated performance elements of the balance of payments but also by the revaluation changes that can produce a further change in the level of their reserves.

160. Balances of the general type described in this section can usually be compiled with a high degree of statistical accuracy, as the components below the line are usually the most reliable in the statement and the errors and omissions item thus obviously belongs above the line. Because of the feasibility of measuring overall balances indirectly from below the line, some versions at least can also be made available more quickly than balances of other sorts; this consideration does much to enhance their appeal.

(c) *Balances on goods, services, income, unrequited transfers, and long-term capital movements*

161. The current balance is too narrow a measure for some purposes, and the overall balance is addressed mainly to the problems that may be created in the short run for the authorities in providing

financing for imbalances. Therefore, a measure that may give a better picture of trends in an economy's payments balance in the longer run is often wanted. Measures of that type have come to be termed a "basic" balance.

162. In principle, the objective in constructing a basic balance is to exclude from above the line transactions that are volatile and are likely in the short run to be reversed, or at least are rather susceptible to being reversed. As goods, services, income, and unrequited transfers represent for the most part transactions that are not intended to be reversed, they are always included above the line. The determination of which capital movements can be said to share this same characteristic, however, is much more difficult. Only the equity claims of direct investors and claims that are neither transferable nor short term—particularly long-term loans, especially those of the official sector—constitute long-term movements in any formal sense, whereas in actuality many economies show a tendency over time to be net exporters or net importers of capital in other forms as well. The standard components in this Manual do not attempt in general to differentiate between types of capital on the basis of whether or not they are likely to show volatile movements. In practice, when a basic balance is to be constructed from those components, some analysts simply include above the line all capital that is nominally long term and all other direct investment capital.

163. Measurement of the basic balance in the way just described is obviously not ideal and may on occasion prove seriously defective. Attempts are sometimes made to refine the measure by adjusting it for cyclical influences—a very difficult exercise—or for specific flows that seem to be the cause of distortion, among them volatile movements in capital that is nominally long term in form and large special nonrecurring transactions. Such adjustment of specific flows is usually not a sustainable approach because the results may be unduly influenced by judgmental decisions. Users often prefer to start out with an analytic indicator in terms of a fixed list of standard components, supplemented by such other information as may be needed to interpret it properly.

164. The basic balance is one whose measurement is particularly affected by the treatment of net errors and omissions, as the residual item is usually composed of both stable and volatile elements. If users of the basic balance are more concerned with having an indicator of trend rather than of level, the exclusion of the residual item from above the line would seem warranted. While the omission of any stable elements of the residual item will affect the level of the balance, the inclusion of volatile elements could obscure its trend.

CHAPTER EIGHT

Standard Components

(1) List of Standard Components

165. The individual types of transaction that are covered by a balance of payments statement are numerous, and it is not feasible to recommend, as an international standard, that each country should compile and report separate series on every type, including some that may be important only for a few countries. It is desirable, however, to promulgate a standard that can be applied generally, no matter how simple or complicated various countries' transactions may be. Without such a guideline, studies calling for global aggregation and intercountry comparison, which are of basic importance in the work of organizations like the Fund, are rendered very difficult. The issuance of a standard, of course, is not intended to derogate from a country's freedom to collect and publish other information on its balance of payments.

166. Recommendations are given in this Manual, therefore, about the classification of the series comprising a balance of payments statement. The scheme to be used is formulated in terms of a list—which is given at the end of this chapter—of what are described as standard components. Those components, representing fairly detailed items or categories of related transactions, are consistent with one another and, when taken together, make up a complete set of accounts on the double-entry principle. In other words, the standard components are primarily building blocks, for use in constructing various analytic presentations (see Chapter 7).

167. The choice of standard components is a matter of judgment based on a number of considerations, the following being the ones that have been given the greatest weight here:

(a) The item should show a distinctive behavior, indicating that it is influenced by a different economic factor or combination of factors from other items or that it responds differently to the same factor or combination. This response to economic influences is what the balance of payments purports to make evident.

(b) The item should be important for a number of countries; importance may be seen either as a function of behavior (unusual variability, for example) or as referring merely to absolute size.

(c) Statistics for the item should be obtainable without undue difficulty, with account taken, however, of the desirability of their collection in terms of the two previous considerations.

(d) The item should be needed separately for other purposes, such as incorporation into, or reconciliation with, the national accounts.

(e) The list of standard components should not be unduly long, in view of the fact that a very large number of countries, including many that are statistically less advanced, are requested to report uniformly on them.

168. These considerations are the same ones that were taken into account in formulating the classification schemes in previous editions of the Manual. Quite a high degree of continuity has thus been maintained through successive editions—particularly in the selection of individual series—notwithstanding changes that have been introduced in the light of experience and of evolving circumstances.

169. The views of the national experts who served as Fund consultants in preparing this Manual—as well as those of the Fund staff—about the standard components that in practice should be recommended were generally in agreement. Nonetheless, some important differences arose, mainly with respect to the comprehensiveness of the list and hence, in effect, the scope of the balance of payments. The outcome has been that the list of standard components as finally drawn up includes a few items that, while needed in certain analytic contexts, would in the view of a number of national experts be better treated as correlative information not to be shown in the main body of balance of payments statistics.

170. The principal case in point concerns the provision, in the list of standard components, of information for reserves on the total change in holdings and the counterpart to valuation changes. Such information, presented as subcomponents of the changes attributable to transactions in the restricted sense, is considered by many experts to be outside the purview of the balance of payments, which they contend, in the traditional view, is most usefully conceived as a record basically of changes of ownership between residents and foreigners. Other analysts, however, believe that it has become increasingly important that the balance of payments should contain all the information needed to explain changes in the holdings of reserves. Indeed, they would generally prefer the balance of payments to show the total change in holdings and the counterpart to valuation changes as explicit components in the statement itself, rather than merely as

additional items for supplementary information, and thus they would not define reserve changes in terms of a netting of those items.

171. Two other similar instances may be important enough to warrant explicit mention. The first concerns the possible inclusion in the shipment item of a component for the distributive services performed by residents in connection with imports; by convention, this component would always comprise equal credit and debit entries. Some consultants were of the opinion that such a component should be shown, in order to cover the full c.i.f. value of imports on a gross basis in the balance of payments. In line with the method preferred in earlier editions of the Manual, however, the list continues to exclude the entries for that component. Second, the question of including an investment income component for reinvested earnings, together with its offset among the financial items, was the subject of considerable discussion. In this case, the information in question has in fact been listed as a standard component, again in accordance with the practice recommended in the third edition of the Manual.

172. The foregoing paragraphs should not be taken to imply that all differences in viewpoint among national compilers and the Fund staff could be accommodated by providing additional components within the standard list. The selection of components usually reflects some analytic consideration and cannot be based solely on objective criteria. It is not feasible, therefore, to satisfy all possible viewpoints simply by increasing the number of components, following the approach indicated above. For example, the question of whether liabilities constituting foreign authorities' reserves should be included in the same category as reserve assets, should be assembled in a separate functional category, or should be dispersed throughout the capital account presented difficulties, quite apart from the issue of whether such liabilities should be shown separately in the first place. A somewhat different case is illustrated by the decision not to classify all financial items according to the sector of the domestic creditor or debtor; that approach was the main organizing principle employed for those items in the previous edition of the Manual. Many decisions of this kind were made only after extensive debate.

(2) Application of List

173. Even though individual users of this Manual will no doubt find shortcomings in the list of standard components that is presented, this list should nevertheless go far toward fostering the international comparability of those series generally conceded to be of greatest interest for analysis of the balance of payments. In particular, it will

elicit most of the details that are necessary for the discharge of the Fund's duties, as provided in Article VIII, Section 5, of its Articles of Agreement.

174. The promulgation of a standard list carries no implication, on the one hand, that the recommendations made here are intended to inhibit countries from compiling and publishing additional data that they find important. The Fund's own requests to member countries for information, in fact, will not be limited to the list of standard components when further details are needed to understand the circumstances of particular countries or to analyze new situations that may develop. Supplementary information can also be most useful for verifying and reconciling the statistics of partner countries, for example, those on drawings and repayments on individual loans. The Fund staff will consult with countries from time to time to decide on additional details that should be reported.

175. On the other hand, it is recognized that scarcely any country is likely to have significant information to report for every component on the list. Furthermore, several components, each of which is rather unimportant for the given country, may be available only in combination, or a minor component may be grouped with one that is more significant. The standard components should nevertheless be reported to the Fund as completely and accurately as is reasonably possible under the circumstances. In this connection, a compiler will want to keep in mind that he is no doubt better placed than the Fund staff to make estimates and adjustments for those components that do not exactly correspond to his own basic series.

(3) Net Errors and Omissions

176. The principles recommended in this Manual result in a consistent body of positive and negative entries whose net total will conceptually be zero. When all the entries that have actually been made are added up, however, the balance in practice will almost inevitably show a net credit or a net debit. That balance is the result of errors and inconsistencies in the estimates and of omissions from the statement.

177. In the presentation of balance of payments statements, the standard practice is to show separately an item for net errors and omissions. That item is intended as an offset to the overstatement or understatement of the recorded components. Hence, if the balance of those components is a credit, the item for net errors and omissions will be shown as a debit of equal value, and vice versa.

178. Since some errors and omissions that occur in the course of compilation will almost certainly offset one another, the size of the residual item does not necessarily provide any indication of the overall accuracy of the statement. Nonetheless, the interpretation of the statement tends to be hampered when the net residual is large. An empirical rule of thumb that is sometimes quoted holds that a residual is large enough to create a problem when it exceeds the equivalent of 5 per cent of the gross credit and debit entries for merchandise combined (although the residual can also arise, of course, from nonmerchandise transactions).

(4) Major Classifications

179. The standard components, which are listed at the end of this chapter, are grouped into two sections:

- I. The current account, referring to goods, services, income, and unrequited transfers.
- II. The capital account, referring to financial assets and liabilities and counterparts to some of them.

This arrangement is intended to be about as neutral as any that can be devised. That is, the ordering of the components is not deliberately intended to suggest any specific analytic approach; it principally reflects common usage in most countries over the years.

180. All entries for components in Section I should show the gross debits and credits. All entries in Section II should be on a net basis, that is, each component is to be shown only as a credit or a debit; note, however, that a credit entry and a debit entry, constituting in effect separate components, may sometimes appear on the same line, specifically for drawings and repayments on certain kinds of long-term loan. Inflows of real resources and increases in financial assets (or decreases in liabilities) should be shown as debits, and outflows of real resources and decreases in financial assets (or increases in liabilities) should be shown as credits. The unrequited transfers in Section I, Group B, should be numerically equal with opposite sign to the entries for which they provide the offset. The counterparts in Section II, Group B, should be shown on a net basis and should be numerically equal with opposite sign to the corresponding changes included in the other items in that group.

(5) Description of Detailed Classifications

181. The following detailed classifications of standard components have been selected in accordance with the criteria set out in

paragraph 167. The rationale of the classification used in the current and capital accounts is discussed in Chapters 9 and 17, respectively.

I. CURRENT ACCOUNT

A. *Goods, services, and income*

182. “Merchandise” covers exports and imports of goods, as defined in paragraph 213. It represents the value of the goods and related distributive services at the customs frontier of the exporting economy, i.e., the f.o.b. value. In contrast to the treatment in the third edition of the Manual, international transactions in nonmonetary gold are included in this item rather than being shown separately, and the alternative of reporting c.i.f. values for merchandise imports is no longer suggested.

183. “Shipment” covers freight, insurance, and other distributive services in connection with merchandise on a basis consistent with the f.o.b. valuation of the merchandise item (see preceding paragraph), together with the same kinds of service performed on most other goods. As a convention, introduced for reasons of statistical convenience, shipment of merchandise beyond the customs frontier of the exporting economy is always treated as if it were a service performed for a resident of the importing economy.

184. “Other transportation” covers services performed by carriers, chiefly the carriage of passengers, that are not classified in “shipment” or “travel,” together with goods and services acquired by carriers and consumed in their operations.

185. “Travel” covers goods and services acquired from an economy by nonresident travelers during their stay in that economy and for their own use. Travel excludes international passenger services, which have been included in “other transportation.”

186. “Investment income” covers income of nonresidents from their financial assets invested in the compiling economy (debit) and income of residents from their financial assets invested abroad (credit). The list provides for a breakdown into direct investment and other income.

187. “Other goods, services, and income” covers transactions between residents and nonresidents not included in previous items in Group A. The official portion covers general government and central bank transactions; it includes transactions with nonresidents by the government agencies of the compiling economy and their personnel abroad and also transactions by private residents with foreign

governments and with foreign government personnel stationed in the compiling country.

B. Unrequited transfers

188. Entries in this group are the offsets to international changes of ownership of real resources or financial items, whether voluntary or compulsory, that do not have an offset in any other such change. One breakdown of unrequited transfers is by institutional sector.

189. "Private" transfers cover unrequited transfers between residents other than the general government and central bank of the compiling economy, on the one hand, and nonresidents other than general governments and central banks, on the other hand.

190. "Official" transfers cover interofficial transfers, together with other transfers in which either the transferor or the transferee is the general government or central bank whether of the compiling economy or of a foreign economy.

II. CAPITAL ACCOUNT

191. The capital account as developed in this Manual shows changes of ownership and other specified changes in an economy's foreign financial assets and foreign liabilities. Assets (other than monetary gold and SDRs) must represent actual claims on nonresidents, and liabilities must represent actual indebtedness to nonresidents. The two parties to a transaction in assets or liabilities may be a resident and a foreigner or, in some instances, two residents or two foreigners (see paragraph 365).

A. Capital, excluding reserves

192. The classification of standard components under this heading is based on the following criteria:

(i) the type of capital (direct investment, portfolio investment, and other capital);

(ii) the traditional distinction between long-term and short-term assets and liabilities based on an original contractual maturity of more than one year or one year or less, respectively, that has been maintained for all entries under this heading, portfolio investments being long term by definition;

(iii) the additional breakdown by sector of the domestic creditor for assets or of the domestic debtor for liabilities that has been retained for "other capital";

(iv) the customary distinction between assets and liabilities for portfolio investment and other capital; and

(v) a further breakdown of liabilities for portfolio investment and other capital to show separately any such liabilities that the foreign creditors regard as reserve assets.

193. "Direct investment" covers all capital transactions between direct investment enterprises and the direct investors themselves or any of those investors' other direct investment enterprises (see paragraph 415). The subclassification of investment abroad and in the reporting economy into equity capital, reinvestment of earnings, other long-term capital, and short-term capital should not be seen as contradicting the basic premise that the behavior of direct investment flows reflects a lasting interest on the part of the direct investor.

194. "Portfolio investment" covers investment in long-term bonds and corporate equities other than "direct investment" and "reserves."

195. "Other capital" is a residual category covering transactions in all financial assets other than "direct investment," "portfolio investment," and "reserves." A further breakdown of this group is based on the type of asset and liability and distinguishes between loans and other capital.

B. Reserves

196. "Reserves" covers those assets (together with the use of Fund credit) that are conceived of as available for use by an economy's central authorities in meeting balance of payments needs; such availability is not closely linked in principle to formal criteria, such as ownership or currency of denomination.

197. The coverage of this group derives from an analytic concept rather than from precise definitions based on observable characteristics possessed by the financial items concerned. The recording in this group also differs from that for the rest of the financial items, inasmuch as supplementary information is requested on the total change in holdings and on the counterpart to any portion of that change which is not the result of transactions between two parties. With respect to the counterparts, a separate entry is shown for the monetization/demonetization of gold, the allocation/cancellation of SDRs, and valuation changes (defined to include reclassifications, as well as fluctuations in market values).

Standard Components of the Balance of Payments

I. CURRENT ACCOUNT

	<i>Credit</i>	<i>Debit</i>
A. Goods, Services, and Income		
Merchandise		
Shipment		
Other Transportation		
Passenger services		
Port services, etc.		
Travel		
Investment Income		
Direct investment income		
Reinvested earnings		
Distributed earnings		
Other		
Resident official, including interofficial		
Foreign official, excluding interofficial		
Private		
Other Goods, Services, and Income		
Official		
Interofficial		
Other, resident official		
Other, foreign official		
Private		
Labor income, n.i.e.		
Property income, n.i.e.		
Other		
B. Unrequited Transfers		
Private		
Migrants' transfers		
Workers' remittances		
Other		
Official		
Interofficial		
Other, resident official		
Other, foreign official		

Standard Components of the Balance of Payments (continued)

II. CAPITAL ACCOUNT

	<i>Credit</i>	<i>Debit</i>
A. Capital, excluding reserves		
Direct Investment		
Abroad		
Equity capital		
Reinvestment of earnings		
Other long-term capital		
Short-term capital		
In reporting economy		
Equity capital		
Reinvestment of earnings		
Other long-term capital		
Short-term capital		
Portfolio Investment		
Public sector bonds		
Assets		
Liabilities constituting foreign authorities' reserves		
Other liabilities		
Other bonds		
Assets		
Liabilities constituting foreign authorities' reserves		
Other liabilities		
Corporate equities		
Assets		
Liabilities constituting foreign authorities' reserves		
Other liabilities		
Other Capital		
Long-term capital		
Resident official sector		
Drawings and repayments on loans extended		
Other assets		

Standard Components of the Balance of Payments (continued)

II. CAPITAL ACCOUNT (continued)

	Credit	Debit
Other Capital (continued)		
Long-term capital (concluded)		
Resident official sector (concluded)		
Liabilities constituting foreign authorities' reserves		
Drawings and repayments on other loans received		
Other liabilities		
Deposit money banks		
Drawings and repayments on loans extended		
Other assets		
Liabilities constituting foreign authorities' reserves: denominated in national currency		
Liabilities constituting foreign authorities' reserves: denominated in foreign currency		
Drawings and repayments on other loans received		
Other liabilities		
Other sectors		
Drawings and repayments on loans extended		
Other assets		
Liabilities constituting foreign authorities' reserves		
Drawings and repayments on other loans received		
Other liabilities		
Short-term capital		
Resident official sector		
Loans extended		
Other assets		
Liabilities constituting foreign authorities' reserves		
Other loans received		
Other liabilities		

Standard Components of the Balance of Payments (concluded)

II. CAPITAL ACCOUNT (concluded)

	Credit	Debit
Other Capital (concluded)		
Short-term capital (concluded)		
Deposit money banks		
Assets		
Liabilities constituting foreign authorities' reserves: denominated in national currency		
Liabilities constituting foreign authorities' reserves: denominated in foreign currency		
Other liabilities		
Other sectors		
Loans extended		
Other assets		
Liabilities constituting foreign authorities' reserves		
Other loans received		
Other liabilities		
B. Reserves		
Monetary Gold		
Total change in holdings		
Counterpart to monetization/demonetization		
Counterpart to valuation changes		
Special Drawing Rights		
Total change in holdings		
Counterpart to allocation/cancellation		
Counterpart to valuation changes		
Reserve Position in the Fund		
Total change in holdings		
Counterpart to valuation changes		
Foreign Exchange Assets		
Total change in holdings		
Counterpart to valuation changes		
Other Claims		
Total change in holdings		
Counterpart to valuation changes		
Use of Fund Credit		
Total change in holdings		
Counterpart to valuation changes		

"Exceptional financing"
to include borrowings
for reserve purposes
only, e.g. borrowings
from chartered banks,
borrowings from IMF etc

CHAPTER NINE

Current Account (Goods, Services, Income, and Unrequited Transfers)

198. The standard components of the balance of payments statement have been grouped in this Manual (Chapter 8) under two main headings—the financial items (i.e., monetary gold, SDRs, and claims) or “capital account” and all other items, usually labeled here for convenience as “current account.” Certain characteristics common to the separate elements of each group have a bearing on how they are recorded in the balance of payments. The two groups, therefore, are treated separately, using the terminology and stressing the problems that are particularly relevant for each group. Despite this separate treatment, the recommendations for financial and nonfinancial items conform to a uniform set of underlying principles.

(1) Coverage

199. All transactions between resident and nonresident entities in economic values other than financial items, together with the offsets to economic values of any kind that are provided or acquired without a quid pro quo, are covered here under the heading of the current account. Specifically, goods, services, income, and unrequited transfers are dealt with in this general chapter.

200. The distinction between nonfinancial economic values (“real resources”) and other nonfinancial “values” that could be conceived, e.g., the intangibles in consideration of which a worker sends money to his family abroad or the benefits that might ensue from a government grant, has been taken over from the United Nations’ *A System of National Accounts (SNA)*. The precise nature of this distinction must largely be inferred from the framework and conventions of the *SNA* itself and cannot be satisfactorily defined apart from that context. In very broad terms, the values that figure in the balance of payments as real resources are goods and services, including the “services” of labor and of financial and nonfinancial assets, of a type that could be offered for sale to a foreigner under market conditions. In

contrast, unrequited transfers are transactions stemming from the non-commercial considerations, such as family ties or legal obligations, that induce a producer or owner of real resources and financial items to part with them without any return in those same forms. While the specification of the exact coverage of unrequited transfers is difficult in theory, the practical problems that can actually result are not likely to be matters of great concern to the balance of payments compiler.

(2) Rationale of Classification

201. The standard components of the current account in this Manual are largely those that have traditionally been shown in the balance of payments, although some of the border lines between components have been adjusted. When the underlying considerations stated in Chapter 8 (paragraph 167) are kept in mind, the rationale of the selection becomes rather readily apparent.

202. Merchandise almost invariably comprises the largest category of transactions between residents and nonresidents. In fact, a further breakdown of the component for merchandise, e.g., by commodity or economic class, might well be justified. Such a breakdown, however, can usually be obtained without too much trouble from the trade returns or other supplementary sources. The exact coverage of merchandise, which stops short of including all movable goods, reflects mainly the requirement for consistency with other items within the overall balance of payments framework.

203. The next item in order, shipment, refers to the freight, insurance, and other distributive services performed on goods. Those goods are by and large the ones that are classified as merchandise, so the two items are closely related; in fact, any border line between merchandise and shipment is in a sense artificial. One reason that a distinction is of interest is for the comparison of the merchandise component for economies that participate to a differing extent in providing distributive services internationally.

204. The item for other transportation pertains to activities of the domestic and foreign transport industries other than the acquisition of carriers, the carriage of goods, and the carriage of passengers within an economy of which they are not residents. The two components are (a) passenger services, mainly the international carriage of passengers, which has a connection with the following item, travel, and (b) port services, etc., mainly the acquisition of goods and services from other industries for use in the transport industry's own production (but not the acquisition of goods that are classified as merchandise, i.e., carriers, or of labor and insurance services, which are included in "other goods, services, and income").

205. Travel and investment income are two items whose importance and independence of behavior from other types of services can easily be appreciated. The latter item, which overall is the main type of international factor income, is further classified to indicate the kind of financial item on which the income is earned.

206. The remaining constituents of goods, services, and income form a heterogeneous collection. The nature of the transactions varies widely from country to country and, while particular types are important for some countries, any given type tends to be fairly small on a global basis. Transactions involving an official sector as either party are shown separately; special interest also attaches to the role of the domestic government in contrast to foreign governments, so provision is made for showing that distinction. The residual group of private (nonofficial) services is disaggregated to identify two types, labor income, n.i.e., and property income, n.i.e., that experience has proved to be of particular interest to a number of countries.

207. Unrequited transfers form a group separate from goods, services, and income because they are generally conceived as showing distinctive characteristics. The difference between real resources and unrequited transfers, however, is sometimes more apparent than real. For example, receipts by an economy from certain individuals working abroad are classified either as unrequited transfers or as labor income depending simply on how long the individuals have stayed in the country where they work. Moreover, the distinction between unrequited current and capital transfers, which is maintained in the national accounts, is not reflected in the standard components, partly because it is difficult to apply on international transactions and partly because, even if it could be applied, it would not be particularly useful for analyzing the balance of payments. Instead, the breakdown of unrequited transfers mostly parallels the one adopted for the residual group of services and is based on a similar line of reasoning.

(3) Valuation and Timing

208. The concept of market value and its specific application to current account items is discussed in Chapter 4, and the subject of timing is covered in Chapter 5.

(4) Gross Recording

209. For current account components, gross outflows from the economy and gross inflows into the economy should, in principle, be recorded (as credits and debits, respectively), and the individual

components have in fact been defined in such a way that the entries will be on a gross basis. Gross recording, however, is confined for the most part to transactions that are related to significant economic activity in the compiling country (in practice, those that involve a change of ownership). Transactions in which the compiling country merely acts as an intermediary between two foreign countries are generally not included on a gross basis, although the value of any services performed by the intermediary is recorded.

210. Exceptions to the general rule of gross recording must sometimes be made because of the practical difficulty of collecting certain information on a gross basis. A significant exception recommended as standard practice in this Manual arises from the convention applied for recording the shipment component; under that convention, certain transactions in distributive services between residents and foreigners in connection with merchandise may in some circumstances be netted out. Other cases also occur that might be viewed as recommending a net treatment but that are actually the consequence of applying the general rules and definitions consistently. The netting, for example, of goods exported and imported for processing without a change of ownership is in accordance with the change-of-ownership rule for recording merchandise; the resulting entry is conceived of not as representing net exports or net imports but as the processing service. Similarly, the netting of insurance premiums against claims is construed merely as a device for approximating the insurance service charge.

211. The recommendations of this Manual also lead to a few instances in which the credits and debits could refer to offsetting transactions between residents or between foreigners. One example is the shipment of goods up to the customs frontier of the exporting country—which when performed by the importer results in a credit (debit) to merchandise and an offsetting debit (credit) in shipment; this exception is made in establishing the uniform point at which the border line between merchandise and shipment is to be drawn. Such deliberate overstatements of the gross credits and debits are not usual, however.

212. This emphasis on gross recording in the current account stems from the fact that the credit and debit entries for any given type of current transaction are seldom related in a causal way. The provision of travel services, for example, has little connection from an economic standpoint with the acquisition by the same economy of such services, even though both are included in the single component for travel. Moreover, the gross figures are wanted in various contexts other than

the analysis of balance of payments developments. In general, gross current account transactions are usually taken as the only available indicator of the relative size of various economies in international transactions and are thus used to compare those economies and to provide weights for aggregating them. Two specific applications that are important for the Fund may be cited as examples of the need for gross figures. (a) The interim valuation of the SDR is based on a basket of currencies, selected in consideration of the issuing countries' shares in world exports of goods and services and weighted in broad proportion to those shares. (b) Relative quotas of members in the Fund depend, as one factor, on the relative size of their gross current account transactions.

CHAPTER TEN

Merchandise

(1) Definition

213. "Merchandise" covers all movable goods, with a few specified exceptions, the ownership of which changes between a resident and a foreigner. The goods included in this item should be valued at their market value and recorded for the period in which the change of ownership occurs. Distributive services in connection with goods that are performed up to the customs frontier of the economy from which the goods are exported are classified as merchandise; those that are performed beyond that frontier are classified as shipment.

(2) Change of Ownership

214. The change-of-ownership rule adopted for defining merchandise ensures, in principle, that the item is consistent as to coverage and timing with other items in the balance of payments, particularly the financial items. The international standards for trade statistics, however, as well as the customs returns in most countries, are based instead on physical movements of goods across the national or customs frontier. Although the goods that change ownership internationally are for the most part the same goods that move across the frontier, the changes and the movements often do not occur at exactly the same time.

(a) *Convention for recording*

215. For purposes of this Manual, goods for export are generally considered to change ownership when the exporter ceases to carry them on his books as a real asset and makes a corresponding change in his financial items; goods for import are considered to change ownership when the importer enters them on his books as a real asset and makes a corresponding change in his financial items. This

convention is designed to promote consistency between the merchandise and capital accounts in the balance of payments of the compiling country, as well as between the merchandise item as compiled by the exporting and importing countries. In practice, however, exporters and importers may not enter the transactions in their books as of the same time, so that significant differences in timing may result even when this convention is followed.

(b) *Exceptions to change-of-ownership rule*

216. The definition of residence adopted for this Manual has implications for the coverage of merchandise as determined by the change-of-ownership rule. Specifically, although enterprises are always considered to be a resident of the economy where they operate, enterprises in different economies may be under the same management. Such affiliation may result in transactions between the enterprises that are not subject to the legal changes of ownership which would have occurred had the enterprises been independently managed. Transactions between a parent company and a direct investment branch (an unincorporated enterprise), in fact, could never involve a legal change of ownership in the literal sense, as both parties are part of the same legal entity. Moreover, while a parent company and a direct investment subsidiary (an incorporated enterprise) constitute separate legal entities, a different balance of payments treatment for transactions between the two enterprises that take the form of a legal change of ownership and those that do not would scarcely seem either feasible or desirable. Therefore, to put transactions between all enterprises in different economies that are affiliated through a direct investment relationship on the same economic basis as similar transactions between enterprises that are not affiliated in that way, this Manual recommends that all transactions between direct investment enterprises and their parent or other related enterprises be recorded as if a change of ownership had occurred except the kinds of transaction in goods specified in subsection (d), below.

217. Some important instances can also be found in which the possession of goods passes between a resident and a foreigner who are not affiliated, without a change of ownership as stipulated above. Probably the most significant instance in which the effect of a legal change of ownership is achieved between independent parties by other means pertains to financial leasing, i.e., lease arrangements that provide for the recovery of all, or substantially all, of the cost of the goods, together with carrying charges. This Manual recommends that the basic nature of these transactions be given precedence over their legal form. Therefore, as a rule of thumb, a lease arrangement

expected to cover at least three fourths of the cost of the goods, together with the carrying charges, is to be taken as presumptive evidence that a change of ownership is intended. The full equivalent of the market value of the goods (not the cumulative total of the expected lease payments) should then be recorded as merchandise, and an offsetting entry should be made in the capital account to record the credit extended to the nominal lessee.

218. Other cases could be cited in which the effect of a legal change of ownership is brought about in some other way. For those cases, however, the recommendation is that the change-of-ownership rule for recording merchandise should nonetheless be applied strictly and literally, the only exceptions thus being the ones just noted for transactions between affiliated enterprises and under financial leasing arrangements.

219. In contrast, goods may change ownership between a resident and a foreigner without undergoing physical movement across the frontier of the economy whose resident has acquired or relinquished ownership. When goods are acquired from one economy and relinquished again to that or some other economy without ever crossing the frontier of the economy in which their temporary owner is a resident, that owner can be considered to have been engaging in a merchanting transaction rather than in a real import and re-export of the goods. This Manual recommends that the country of the temporary owner should exclude such goods from the merchandise item, unless the recording periods in which the goods are acquired and relinquished are not the same. In the latter case, increases (decreases) in stocks abroad from one reporting period to another should be shown as merchandise imports (reductions in imports); for a fuller explanation of the treatment of these transactions, see paragraph 228.

(c) *Goods not crossing frontier*

220. Goods not crossing the frontier should be treated as merchandise if a change of ownership occurs, unless that change of ownership is to be disregarded because it is not related to significant economic activity (see preceding paragraph). Examples of goods that might not cross the frontier but that nonetheless should be treated as merchandise are

- (i) ships, aircraft, and gas and oil drilling rigs and production platforms;
- (ii) goods consumed by offshore installations, e.g., gas and oil drilling rigs and production platforms;

(iii) goods salvaged and fish and other marine products caught by the compiling economy's ships and sold abroad directly;

(iv) goods purchased in one foreign country by the compiling economy's government for its own use in another foreign country; and

(v) goods lost or destroyed after ownership has been acquired by the importer but before they have crossed a frontier.

(d) *Goods crossing frontier without changing ownership*

221. Goods that cross the frontier without a change of ownership should not be covered in the merchandise item except where noted in subsection (b), above. The principal types of goods that might cross the frontier without a change of ownership are enumerated below; the recommendation that transactions between direct investment affiliates be recorded as if a change of ownership had occurred (see paragraph 216) does not extend to those goods:

(i) goods for processing and re-export by the processing economy, i.e., goods which enter into production and are physically transformed from one type of commodity to another, more highly processed type (see paragraph 222, below);

(ii) goods for servicing and re-export by the servicing economy, i.e., goods to which some value is added but which are not actually transformed physically, including those for improvement, repair, storage, labeling, packaging, sorting, inspection, and the like;

(iii) returned exports and imports (see paragraph 223, below);

(iv) goods shipped under operational, i.e., nonfinancial, leasing arrangements (see paragraphs 333–34);

(v) transportation equipment, fishing vessels, gas and oil drilling rigs, and other mobile equipment that are to operate on the domestic territory for less than one year;

(vi) direct transit trade;

(vii) shipments by a given economy to that economy's military and diplomatic establishments that are located outside the territory of that economy;

(viii) goods lost or destroyed after having crossed the frontier but before having been delivered by the exporter;

(ix) goods temporarily exported and imported, not for sale, e.g., display equipment for trade fairs and exhibitions, art exhibits, animals for breeding, show, or racing, and stage and circus equipment; and

(x) samples of no commercial value.

222. When goods for processing and re-export cross the frontier without a change of ownership, the value added to such goods by processing should, according to the general rule in this Manual, be regarded as a service performed for a foreigner. Movements of such goods, however, are treated in the international trade statistics and the national accounts as imports (exports) and subsequent exports (imports) of merchandise; that treatment differs from the change-of-ownership rule adopted for the merchandise item in this Manual. Furthermore, some processing may be virtually the equivalent of a financing arrangement whereby the processor is obtaining his raw materials on credit from the supplier. Any uniform treatment of goods for processing will thus, strictly speaking, be inconsistent with some other practice that is being followed. The recommendation of this Manual is that the change-of-ownership rule be observed for goods for processing and re-export; this recommendation applies to goods transferred between affiliates, as well as to those transferred between unaffiliated parties. Thus, when movements of goods for processing and re-export are not accompanied by a change of ownership, the goods should be excluded from merchandise and the value added by processing (i.e., the difference in the value of the goods before processing and afterward) should be recorded in "other goods, services, and income." In contrast, when a change of ownership does occur in connection with processing transactions, entries should be made in the merchandise component to record the market values of the goods before processing and afterward, and no entry should be made in "other goods, services, and income."

223. When the execution of a contract for the sale of goods is not completed after the goods have been shipped out of the exporting economy, with the result that they are later returned to their original owner, the goods are not considered to have changed ownership. It will probably not be possible to anticipate, at the time such goods originally cross the frontier, whether they will be returned in the future. It is therefore suggested, purely for statistical convenience, that any deduction from exports and imports that may later be found necessary to eliminate such goods from the merchandise item might be made in the period when the goods are returned, so that no revision to the entries would be required for the period when these goods were originally recorded incorrectly as exports or imports.

224. For other goods of the kinds listed above that do not change ownership, no entries are to be made in the merchandise item. Any services performed in connection with such goods are to be recorded in "shipment" or "other goods, services, and income," depending on the kind of service.

225. For the time of recording for goods on consignment, i.e., goods intended for sale that cross the frontier without a contract providing that ownership will in fact change, see paragraph 235.

(3) Goods Classified in Items Other Than Merchandise

226. While almost all movable goods, the ownership of which changes between residents and foreigners, are classified as merchandise, a few specified goods of that sort are classified in other items.

(a) Goods classified in service and income items

227. Some goods are classified in service and income items because the data on which those items are based usually include them indistinguishably or because their response to economic factors is different from that of most merchandise. The main examples of goods included in items other than merchandise (and the items in which they are included) are as follows:

(i) stores and fuel for carriers (Other transportation: port services, etc.);

(ii) goods acquired for their own use by travelers (Travel), by diplomatic and military missions and agencies (any official component of Other goods, services, and income), by official personnel (Other goods, services, and income: other, resident official or other, foreign official), and by workers (Other goods, services, and income: labor income, n.i.e.);

(iii) newspapers and periodicals (not in bulk) sent under direct subscription (Other goods, services, and income: other private); and

(iv) goods acquired and relinquished within the same recording period without crossing the frontier (Other goods, services, and income: other private).

228. Goods acquired and relinquished in the same recording period without crossing the frontier of the economy in which their temporary owner is a resident are not to be included by that economy in the merchandise item. If such goods are acquired in one recording period and relinquished in a later period, however, the balance of payments of their temporary owner's economy should record them as imports in the period in which they are acquired and should deduct that same amount from imports in the period in which they are relinquished; in this case, changes from one recording period to another in stocks of goods located abroad (valued at their acquisition cost) will constitute part of the merchandise item for the economy of their owner. Under either situation, any difference between the value of the goods when

they were acquired and their value when relinquished is to be entered as merchanting in “other goods, services, and income.”

(b) *Goods regarded as financial items*

229. The evidences of financial claims should not be included in merchandise, even though they have a material form and are movable. Examples of such goods are paper money and coin that are in current circulation and securities that have been issued.

230. Monetary gold is treated as a financial asset and should not be included in merchandise.

231. Nonfinancial assets belonging to an enterprise, including land, buildings, equipment, and inventories, are considered a financial investment for the owner of that enterprise, when he is not a resident of the economy where the enterprise operates. A change of ownership of these assets resulting from the acquisition of an existing enterprise is thus treated as a financial transaction and is not included in merchandise, except to the extent that such a change of ownership is actually accompanied by a physical movement of goods.

(4) Special Types of Goods

232. Sometimes the classification of certain goods as merchandise is questioned, most often because the goods may be accorded exceptional treatment under customs regulations or in the trade returns. The following examples are listed as goods of this kind, all of which should be included in merchandise if they qualify under the definition and rules in this Manual:

- (a) commodity gold (i.e., nonmonetary gold), silver bullion, diamonds, and other precious metals and stones;
- (b) paper money and coin not in current circulation and unissued securities, all of which should be valued as commodities rather than at their face value;
- (c) electricity, gas, and water;
- (d) livestock driven across frontiers;
- (e) parcel post;
- (f) government exports and imports (other than those to and from the government’s own agencies and personnel), including goods financed by grants and loans;
- (g) goods transferred to or from the ownership of a buffer stock organization;
- (h) goods exported or imported by direct investment enterprises;

- (i) migrants' effects;
- (j) smuggled goods, whether or not detected by customs; and
- (k) other unrecorded shipments, such as gifts and those of less than a stated minimum value.

(5) Time of Recording

233. For the sake of consistency between the merchandise item and other items in the balance of payments, particularly the financial items, merchandise should be recorded, in principle, as of the time that the change of ownership takes place. By convention, time of change of ownership is taken to be the time that the two parties record the transaction in their books (see paragraph 215).

234. Neither physical movement, on which the trade returns are largely based, nor payment, which is reflected in exchange records, will necessarily coincide in timing with the change of ownership of merchandise. The adjustments to statistics derived from those two sources that would theoretically be needed are detailed in Appendix B. Except for large, discrete transactions, such as deliveries of ships or aircraft, the appropriate adjustments are often quite difficult to make, since information on the actual time of change of ownership is seldom available, especially in a form that can be related to the time of physical movement or of payment for the same goods. If the overall value of trade, the regional pattern of trade, or the terms of payment for it change substantially from the beginning to the end of the recording period, however, failure to adjust for timing is likely to be a major source of error in the balance of payments statement, as well as an important cause of asymmetry between the merchandise component for different countries.

235. Goods on consignment, i.e., goods intended for sale that have not actually been sold at the time they cross the frontier, should in principle be included in merchandise only at the time ownership changes. Such goods are sometimes recorded instead, for convenience, at the time when they cross the frontier, on the assumption that a change of ownership has occurred or in the expectation that a change will shortly occur. If that treatment is followed but there is no change of ownership, the goods will subsequently have to be recorded again as a deduction from exports and imports, in the same manner as returned exports and imports (see paragraph 223).

(6) Valuation

236. The value at which merchandise should, by definition, be recorded in the balance of payments is the market value of the goods

at the place of uniform valuation, i.e., the customs frontier of the economy from which they are exported. At least two aspects of this general statement require elaboration.

(a) *Market valuation*

237. The concept of market value and its specific application to internationally traded goods are discussed in Chapter 4. The United Nations (UN) deals at length with the question of valuing exports and imports in connection with its standard for such statistics. The Customs Cooperation Council (CCC) also provides an extensive treatment of the standard to be applied for the customs valuation of imports. An effort is made in Appendix B to throw additional light on the concept of market value, as it applies to merchandise, by showing how the UN and CCC standards may be reconciled with that recommended in this Manual.

(b) *Point of valuation*

238. Goods may be delivered by the exporter to the importer—invariably signifying that a change of ownership is occurring—at any time and place from the point where they have been produced to the point where they are to be consumed. This Manual seeks to draw a clear distinction between one item that is to be regarded as merchandise proper and another item for any additional distributive services that might increase the value of that merchandise before it enters into consumption; this distinction is to be observed without reference to whether the distributive services are performed before or after the change of ownership occurs. Merchandise will thus be uniformly valued, in the limited sense that a border line between merchandise and distributive services, in respect of place of valuation, is established in accordance with one standard rule.

239. Uniformity of this kind simply means that differences in practices as to the place at which goods are delivered by exporters to importers, as well as changes in those practices from one period to another, will not have any effect on what services are to be included in the value of merchandise. No rule that can be formulated, however, will produce a point of valuation for merchandise that can be considered uniform in some more basic economic sense. Indeed, the kind of uniform valuation under consideration here could more appropriately be viewed as a matter of uniform classification, as the objective is to include in the merchandise item only a standard partial list of related distributive services; the principle that both the merchandise and the services should be valued at market prices is not in question in this context.

240. The rule adopted for this Manual is that the merchandise item shall cover, in principle, the value of the goods and related distributive services at the customs frontier of the economy from which the goods are exported, up to and including any loading of the goods on board the carrier at that frontier. That is, merchandise exports and imports are to be valued f.o.b. at the customs frontier of the exporting country. In the application of this rule, customs bonded warehouses, customs bonded manufacturing plants, and free areas are to be taken as being within the customs frontier of the economy that controls and supervises them. The customs frontier need not coincide physically with the national boundary but could be located at some place in the interior of the country.

241. While the desirability of adopting a uniform point for valuing the merchandise item is generally conceded, any of several points that might be chosen could in fact be seen as having comparable analytic advantages. The adoption of any given one of these uniform points, however, also creates problems of a statistical nature. A principal difficulty is that shipping practices are not standard, and the documents on which the compiler must usually rely as the basis for his estimates of merchandise and shipment will often cover shipping services performed on both sides of the customs frontier (or of any other uniform point) without a breakdown of the total shipping cost. For example, shipment by truck may be provided from door to door, or goods in containers may be moved on a through bill between central warehouses that are distant from the customs frontiers in the exporting and importing countries. A main consideration in specifying the customs frontier of the exporting country, rather than some other place, is that it is the point at which the customs officials will be putting their valuation on exports and, for a significant group of countries, on imports as well. It is thus the point that is perhaps most likely to be reflected in the trade statistics.

242. As a practical matter, the service of loading goods on board the carrier at the customs frontier, when such loading actually occurs, is frequently performed by or for the account of the carrier, in which case the trade statistics are likely to exclude the cost of such services and the data on freight charges will almost certainly include them. This Manual does not suggest that an attempt be made to reallocate such charges from the shipment item to the merchandise item. Instead, it explicitly recognizes that the recommended basis for merchandise may in fact turn out to be partly, or even mainly, an f.a.s. basis rather than strictly an f.o.b. basis.

243. Merchandise delivered to an importer at some point within the exporting economy might not be shipped to the customs frontier of

that economy during the same recording period. When this is the situation, an entry should be made in one period for the value of the goods at the point of delivery and in a subsequent period for the cost of shipment from that point to the customs frontier. Both of these entries are included in the merchandise item.

244. Application of the rule for uniform valuation may result in the inclusion in the merchandise item of some flows of services between foreigners or between residents of the same economy. Specifically, the exporter may deliver the goods before they reach the customs frontier of his economy, and the importer may then employ a supplier of distributive services who is not a resident of the exporting economy to ship them to the customs frontier. An offset to such a flow of services between foreigners is required in the balance of payments of the exporting country; in order to preserve a uniform valuation in the merchandise item, this Manual provides that the offsetting entry is to be made in "shipment." Similarly, if the supplier of the services is the importer himself or a resident of the importer's own economy, the services will not have been provided between residents of different economies and an offset in "shipment" will also be required in the balance of payments of the importing country.

245. The treatment of the services performed by agents in connection with transactions in merchandise also requires consideration. Some of these services apply to a transaction only generally and cannot realistically be attributed to the value of merchandise as of any particular point. As a practical way of dealing with the problem, this Manual recommends that agents' fees in connection with merchandise transactions be included in all cases in the value assigned to merchandise at the customs frontier of the exporting economy. If the agent is a foreigner from the standpoint of an exporting economy, or if he is a resident from the standpoint of an importing economy, an offsetting entry will be needed and should be made in "other goods, services, and income."

246. In some instances, fees are paid by exporters to the consulates of the importing countries. This Manual adopts the rule that such fees are not to be included in the value of merchandise at the frontier of the exporting country. A consular fee is thus treated as a cost incurred beyond the customs frontier of the exporting country; that is, a consular fee is incurred in the importing country.

247. Previous editions of the Manual provided an alternative rule for the uniform recording of merchandise, to be followed by those countries that could not readily distinguish the distributive service element in imports which were valued c.i.f. in the basic data source.

The real inconveniences resulting from not having a single standard have increasingly been felt by users of the balance of payments, and the lack of comparability between statements on different bases now seems a more serious drawback than any difficulty or error in allocating certain flows between the merchandise and shipment items. Therefore, the rule for uniform recording of merchandise propounded in paragraph 240 should be followed, even if rough estimates must be made in order to do so.

Leasing show as DR as ^{mobile} merchandise imports / exports
 + CR of L-T trade credit

As payment made, show as "interest" + "repayment
 on credits" or DR, + CR in reserves.

If leased equipment returned at end of lease, then
 show as "exports" or DR - "repayment on credits" or DR

book value?

CHAPTER ELEVEN

Shipment

(1) Definition

248. "Shipment" covers the freight, insurance, and other distributive services (a) performed by residents of the compiling country on merchandise and most other movable goods acquired or owned by nonresidents and (b) performed by nonresidents on merchandise and most other movable goods acquired or owned by residents. Such services on passengers' effects accompanying the passengers are excluded from this item, as the cost of those services is usually included indistinguishably in the statistics for passenger services, which are part of "other transportation."

249. Most of the services of shipment (specifically, the freight element) are provided by enterprises through their operation of carriers. Practical questions often arise in deciding where such an enterprise should be said to reside, as the carrier itself may operate in the territory of more than one economy or outside the territory of any economy. The residence of enterprises is discussed in Chapter 3, with paragraphs 68–71 on the residence of enterprises operating mobile equipment being especially relevant in the present context.

(2) Conventions for Recording Services on Merchandise

250. A compiling country would often find it difficult, if not impossible, to ascertain whether its own merchandise exports and imports are actually owned by a resident or by a nonresident at the time that the services of shipment are being performed. This information would be required to determine whether transactions between residents and foreigners have taken place, since shipment is performed for or on behalf of the legal owners of the goods. Any necessity for trying to relate changes of ownership of merchandise to shipping activity can be avoided by adopting a convention for constructing the entries that refer to the shipment of the compiling

country's merchandise beyond the customs frontier of the exporting country. Under a convention of this kind, certain offsetting transactions between residents and foreigners may in effect be netted against each other and so may not be included in the balance of payments, while certain transactions between residents or between foreigners may be recorded in the shipment item as both a credit and a debit. The use of a convention thus entails a departure from the general rule for the service items of showing gross flows between residents and foreigners. The problems of compilation are greatly simplified, however, because the entries required represent identifiable types of service performed by residents or foreigners, without regard to whether the merchandise in question is actually owned by a resident or a foreigner at the precise time when those services are being performed.

251. The gross flows of services between residents and foreigners for shipment of the compiling country's merchandise, which in principle are what the balance of payments entries should represent, are compared in the accompanying diagram with the entries that are to be made according to three different methods of estimation, each of which yields its own approximation to a recording of those gross flows. Each method is consistent with the valuation of merchandise at the customs frontier of the exporting country. The discussion below of methods A and B is only included as being of interest, since the recommendation here is that method C be employed.

252. Under method A, the gross recording of all flows of services between residents and foreigners in connection with the shipment of the compiling country's merchandise would be achieved, but any flows between residents or between foreigners would also be included on an offsetting basis. According to this method, the compiling country (a) would enter as credits all services performed by residents on both its exports and imports once the merchandise had been loaded on board the carrier at the customs frontier and would offset the services on imports by making a debit entry, and (b) would enter as debits all services performed by foreigners on both exports and imports and would offset the services on exports by making a credit entry. The standard component for shipment recommended in this Manual does not in fact make any provision for applying this particular method. For one thing, the services in connection with exports provided by economies other than the compiling economy have not been included in the shipping component for reasons such as the following. First, the necessary information may be rather difficult to compile. Second, the data are generally regarded as of only secondary interest in a balance of payments context. Third, in practice countries

**Shipment of Compiling Country's Merchandise:
Flows of Services Between Residents and Foreigners Compared with
Balance of Payments Entries to Be Made
Under Various Methods of Estimation**

	Flows Between Residents and Foreigners ¹		Method of Estimation ²					
			Method A		Method B		Method C ³	
	Credit	Debit	Credit	Debit	Credit	Debit	Credit	Debit
Shipment performed by compiling country								
Exports								
Exporter's account	E→I		x		x		x	
Importer's account	P→I		x		x		x	
Imports								
Exporter's account	P→E	E→I	x	x	x	x		
Importer's account			x	x	x	x		
Shipment performed by other countries								
Exports								
Exporter's account	E→I	P→E	x	x				
Importer's account			x	x				
Imports								
Exporter's account		E→I		x		x		x
Importer's account		P→I		x		x		x

¹In these columns, the symbol "E" denotes the exporter, "I" denotes the importer, and "P" denotes the producer who performs the service. The arrow shows the direction of the service flow.

²In these columns, an "x" indicates that a transaction of the type identified in the stub would constitute a balance of payments entry.

³This method is the one recommended in this Manual; the entries indicated form part of the standard component for shipment.

have rarely, if ever, adopted this approach in presenting their own statements.

253. A second method that could be considered is illustrated as method B in the diagram. That method treats shipment of the compiling country's merchandise beyond the customs frontier of the exporting country as if it were always a service performed for residents of the importing country by residents of countries other than the importing country. The compiling country would enter as credits all shipping services performed by residents, both on exports and on imports, and as debits all shipping services performed on imports,

both by residents and by nonresidents. As may be seen from the diagram, the gross credit and debit entries might thus include some offsetting flows between residents, which in principle should not be recorded in the balance of payments, and might omit some offsetting flows between residents and foreigners, which should be recorded. Among the advantages that could be claimed for method B are the following. (a) The credit and debit entries both represent aggregates that may be of interest in their own right (that is, the sum of the credits is the total earnings of residents from the shipment of the country's merchandise, and the sum of the debits is the total shipment costs incurred on the country's imports). (b) A combination of the entries on the debit side in the shipment item with the debit for the merchandise item comprehends the value of imports valued on a c.i.f. basis, on which many trade statistics for imports are compiled. (c) This treatment would be analogous to the one employed by the United Nations' *A System of National Accounts* in its rest-of-the-world account. Nevertheless, this Manual does not call for the recording of shipping services performed by the compiling country on its own imports as standard practice and thus does not adopt method B.

254. Instead, the recommended method is the one shown as method C in the diagram. That method always treats shipment of the compiling country's merchandise beyond the customs frontier of the exporting country as if it were a service performed for residents of the importing country, whether by residents of that country or of any other country. The procedure is for the compiling country (a) to enter as credits all services performed by residents on its exports once these have been loaded on board the carrier at its customs frontier and (b) to enter as debits all services performed by foreigners on its imports once these have been loaded on board the carrier at the customs frontier of the country from which they are being exported. The difference between method B and the recommended method C is that the latter excludes equal credit and debit entries for shipping services performed by the compiling country on its own imports. In comparison with method B, therefore, method C has the advantage of eliminating any offsetting flows between residents, although for economies operating international carriers it may also bring about the exclusion of even more offsetting flows between residents and foreigners than is the case under method B. However, those exclusions accord with the economic reality that, in the final analysis, the cost of shipment is borne by the importing economy, whatever the arrangements for shipping the goods may have been.

255. If the entire shipment item is shown on a net basis (either by itself or combined with other items), as may well be the case in a

summary presentation, it will not be possible to tell if any convention may have been employed in compiling the underlying figures. That is, the net flows for the shipment of merchandise would reflect the same net flows of such services between residents and foreigners, whether or not one of the three methods described above was adopted for compiling the statistics.

256. As has already been mentioned, the main purpose of specifying a convention is to provide a basis for recording the shipment of merchandise, consistent with a uniform f.o.b. valuation basis for the merchandise item, that is easier to follow in practice than the regular procedure for the current account of recording gross resident-to-foreigner transactions. Use of the convention adopted here admittedly does not obviate all the statistical problems that may arise on this score in compiling the items for merchandise and shipment. When these two items are derived from trade returns that show imports valued at the frontier of the importing country (c.i.f. valuation), a separate estimate will have to be made for the amount of distributive services performed beyond the customs frontier of the country from which the merchandise is exported. This breakdown, however, simply reallocates the element for distributive services in the c.i.f. value of imports between merchandise and shipment, so that any error in estimation will not affect the two items taken together. Furthermore, if the compiling country performs any of the distributive services in connection with its own imports, the amount of such services must be estimated separately from a total that includes similar services which it performs on exports or on other foreign-owned goods; this breakdown may be considerably more difficult to obtain than the data on total earnings. In this case, any error in estimating the breakdown will produce an equal overstatement or understatement of the credit and debit sides of the component for shipment, without affecting the net amount of the item.

257. Under the rule for uniform valuation in this Manual, shipment of merchandise is always considered to begin at the customs frontier of the exporting economy. To achieve symmetry between partner countries in recording the separate credit and debit entries for shipment, a further rule is needed to indicate the place at which the shipment of merchandise is considered to end—whether always at the frontier of the importing country or sometimes at an interior point in that country. This need arises because the recommended method for recording the shipment of the compiling country's merchandise can yield entries that are partly net, while that used for recording other shipment always shows gross transactions between residents and foreigners. The rule adopted here is that any distributive services

performed within the territory of the importing country that are covered in a single contract (e.g., a through bill of lading or an insurance policy) which pertains as well to the shipment of merchandise up to the frontier of the importing country are to be regarded as part of the shipment of merchandise. Stated conversely, services within the territory of the importing country, e.g., freight forwarding from the frontier to an interior point, that are arranged under a separate contract of their own are to be considered as part of other shipment. This rule is intended to simplify the compilation of the figures by conforming to the underlying data that are most likely to be available.

(3) Recording of Other Shipment

258. A method such as one of those discussed above can be applied only for recording services performed in the shipment of merchandise of the compiling country beyond the customs frontier of the country from which it is exported. For other shipment, the gross flows of services between residents and foreigners must be recorded in accordance with the usual practice followed throughout the current account. Such services arise mainly in connection with the merchandise of countries other than the compiling country, including direct transit trade through that country. However, they may also include shipment of goods that are not classified as merchandise, such as coastal shipping or other shipping of goods between points within a country; movements of goods to or from entities that are located outside the territory of which they are residents, e.g., government agencies and their personnel stationed abroad; and goods lost or destroyed after having crossed the frontier but before having been delivered by the exporter.

259. In addition, offsets to certain flows between residents and between foreigners that may be included in "merchandise" when the goods are valued uniformly at the customs frontier of the country from which they are exported are made in "shipment" (see paragraph 244). Specifically, credits are included by the importing country for services that it performs within the customs frontier of the exporting country, and debits are included by the exporting country for services that foreigners perform within its customs frontier.

(4) Types of Shipment

260. Three different kinds of distributive service that are classified as "shipment" may be distinguished: freight, insurance, and other services.

(a) *Freight*

261. Freight refers mainly to the carriage or transport of goods. As used in this Manual, the term also includes any ancillary services provided by a carrier in conjunction with the service of transport. In particular, freight includes the service of loading goods on board the carrier or unloading them from it, if the contract between the owner of the goods and the carrier requires that the latter shall provide that service. When such a service is performed at the customs frontier of the country from which merchandise is exported, the loading charge is classified as freight if the service is provided by or for the account of the carrier; otherwise, it is classified as merchandise. This treatment is adopted because, in practice, the statistics that can be collected on freight will usually cover indistinguishably all services that are performed by or for the account of the carriers, whereas those on merchandise are unlikely to include the loading charge if loading is provided by or for the account of the carrier.

(b) *Insurance*

262. The insurance element of “shipment” comprises insurance on movable goods during the course of shipment. Insurance services are usually a rather minor element in the shipment item, let alone the whole balance of payments. They are singled out here mainly because their recording presents conceptual and practical difficulties that require special attention.

263. On the conceptual side, the service charge that the insurer takes into account in setting premiums during a given period (the “normal” service charge) may not be the same as the net premiums (premiums less claims) payable during that period; losses may be greater or less than are expected in the longer run, claims may not yet be payable on losses that have already occurred, and premiums may have been paid in advance on risks to which the insurer has not yet been exposed. Therefore, in principle, net premiums may reflect not only a service charge but also capital gains (losses) and prepayments (postpayments). Because of the practical impossibility of sorting out these various elements, however, net premiums are customarily taken to be the measure of the insurance service, and that treatment is recommended by this Manual.

264. In the compilation of insurance statistics for the balance of payments in accordance with the method adopted here for recording shipment of merchandise (see paragraph 254), compilers may not find it too difficult in the case of merchandise insurance to estimate the net premium income of resident insurers from all merchandise insurance

and all net premiums payable, whether to resident or nonresident insurers, on merchandise imports. Under preferred method C, however, a further estimate is required to eliminate from both of those aggregates the portion of the net premium income of resident insurers that is applicable to imports, an item for which it may be particularly hard to obtain separate information. For convenience, therefore, those aggregates could be entered without making that deduction, which would mean in effect employing method B. The credit and debit entries would then be overstated, in comparison with method C, by equal amounts; this overstatement is likely to be so small that the error—which is an offsetting one in any event—would be of little practical significance.

(c) *Other services*

265. Other distributive services performed during the course of shipment that are incidental to the shipment are covered under this heading. They include such services as the following: storage and warehousing; loading and unloading that are not classified as merchandise or freight; packing and repacking; labeling and packaging; cartage, drayage, and haulage; and forwarding, handling, and transferring.

CHAPTER TWELVE

Other Transportation

(1) Definition

266. “Other transportation” covers those services not classified in other items that are performed by one economy for another through the operation of carriers and similar equipment, together with the goods and services (except labor services performed by carrier crews and insurance on the carriers themselves) acquired by one economy from another for consumption by carriers in their operations. Basically, such services are performed and such goods and services are acquired, not by the carriers but by the enterprises that operate them. It should be noted, for example, that the acquisition of a carrier by the enterprise that is to operate it—as distinct from the acquisition of goods by the enterprise for the carrier to use in its operations—is classified as merchandise.

267. Practical questions often arise in deciding where an enterprise that operates a carrier should be said to reside, as the carrier itself may operate in the territory of more than one economy or outside the territory of any economy. The residence of enterprises is discussed in Chapter 3, with paragraphs 68–71 on the residence of enterprises operating mobile equipment being especially relevant in the present context.

(2) Passenger Services

268. The main service performed by carriers that is classified in “other transportation” is the transportation of persons, as the transportation of goods is classified in the merchandise and shipment items. In addition to the services covered by fares, passenger services include any other services for which passengers make expenditures on board carriers or for which they pay charges to carriers, such as those for excess baggage and for personal effects that accompany them, e.g., automobiles.

269. The component for passenger services is defined to cover all services performed in transporting passengers between economies, together with those performed within any given economy by a carrier operated by a nonresident enterprise. Services performed within an economy by resident operators are excluded from this component. The main reason for the exclusion is the difficulty of collecting the information separately, along with the probability that it will in fact be included indistinguishably in overall estimates of other services provided to foreign travelers, nonresident workers, and foreign official personnel stationed in the territory concerned.

(3) Port Services, etc.

270. This component covers mainly port services but also includes charters and miscellaneous other services related to the transportation industry.

(a) Port services

271. The term “port services” is applied in a broad sense in this Manual to designate the procurement of all goods and most services by carriers and similar equipment for consumption in their operations. Port services do not include charter services provided by the owner of the carrier to its operator, which are nonetheless part of this same component; labor services provided by the crew, which are classified in “labor income, n.i.e.”; and insurance services, which are part of “other” goods and services.

272. The main types of goods procured by carriers are fuel, provisions, stores, and supplies. The services include lighterage, stevedoring, and other loading and unloading, when these are covered by the freight charge or passenger fare; airport and harbor dues and fees; tugboat services, pilotage, and towage; and maintenance and repair.

(b) Charters of carriers

273. Charters (leases) of carriers refer to the service provided by owners in hiring or leasing their carriers to the enterprises that operate them. The following cases that nominally involve charters are not treated as such in the balance of payments, for the sake of consistency with various conventions applied in this Manual.

274. Transportation equipment operated entirely, or primarily, within the territory of an economy for at least one year is always considered by convention to be owned by a resident entity in the economy where it operates (see paragraph 69), so that no charter

services between residents and foreigners would be recorded in the balance of payments in that situation. Instead, the actual foreign owner/charterer would be regarded as having a "direct investment" in the resident enterprise, and any payments to him would have to be construed as income on and amortization of that investment rather than as charter hire.

275. Furthermore, this Manual treats leases of goods (including the charters of carriers) that are expected to cover at least three fourths of the cost of the goods, together with carrying charges, as presumptive evidence of a financing arrangement that is equivalent to a change of ownership (see paragraph 217). No charter services would take place under those circumstances. Here again, any lease payments to the actual legal owner would have to be construed as income and amortization.

276. Finally, under many so-called charters of carriers, especially those for limited periods such as a single voyage, the owner of the carrier continues to be the operator and thus actually provides to the nominal lessee a freight or passenger service rather than a charter service as here defined.

(c) *Miscellaneous transportation*

277. Miscellaneous transportation refers to the services, other than the transport of goods and persons, performed by carriers and similar equipment. For example, fees for salvage operations and for the carriage of letter mail should be included here. By "similar equipment" is meant such equipment as towboats and tugboats, which are not themselves carriers but which have a resemblance to carriers or which perform services closely related to the transportation industry. Services provided by such equipment directly to carriers, such as towage or repairs, constitute part of the port services acquired by the carriers concerned.

CHAPTER THIRTEEN

Travel

(1) Definition

278. "Travel" covers the goods and services acquired from an economy by the individuals defined below as travelers, during their stay in that economy and to use themselves or give away. The international carriage of travelers is covered in passenger services (part of "other transportation") rather than in this component; see paragraph 269.

279. A traveler is a person staying for less than one year in an economy of which he is not a resident, for any purpose other than (a) being stationed on a military base or with another government agency of his own government (see paragraph 312), (b) accompanying a person mentioned under (a) as a dependent, or (c) undertaking a productive activity directly for an entity which is a resident of that economy (see paragraph 319).

(2) Types of Traveler

280. This Manual's list of standard components includes only one item for travel, and the following description of separate types of traveler is thus given solely for the purpose of elaborating the overall definition. Some of the distinctions discussed are also drawn in other international statistical standards.

(a) *Business travelers*

281. This category covers commercial travelers; carrier crews stopping off or laying over; government employees on official travel; employees of international organizations on official business; and employees installing machinery or equipment, when the enterprise performing the installation service is not a resident of the economy where the installation takes place (see paragraph 73).

282. Commercial travelers are those who visit an economy for sales campaigns, market exploration, or commercial negotiations on

behalf of an enterprise established in another economy. "Travel" refers to their personal acquisitions of goods and services (including those for which they are reimbursed by their employer) but not the sales or purchases that they may conclude on behalf of the enterprise they represent.

283. Government employees and employees of international organizations on official travel are to be distinguished from such employees stationed or living, respectively, in the country (see paragraph 312).

(b) *Students and trainees*

284. Instruction, training, room and board, and other goods and services acquired by students and trainees from an economy where they are studying for less than one year are recorded in "travel." For analytic or practical reasons, some balance of payments compilers prefer to classify all students as residents of their economy of origin, even if they study abroad for a year or more; such a deviation from the strict interpretation of this Manual's rules of residence could be considered permissible for the balance of payments if it were also being followed in compiling the rest of the national accounts of the same economy.

(c) *Excursionists*

285. Excursionists are travelers other than those in the above categories who do not stay overnight in the economy where they travel.

(d) *Other travelers*

286. Other travelers who spend at least one night in the economy where they travel may have come for such reasons as recreation or holiday, family matters, medical care, religious observances, and participation in sports events and conferences. They include government employees on leave in any economy other than their economy of residence or the economy where they are stationed.

(3) Goods and Services Covered

287. All goods and services acquired by travelers (as defined above) from the economy where they are traveling and for their own use are recorded under "travel." These goods and services may either be paid for by the traveler (or on his behalf) or be provided to him without a quid pro quo. Examples of the latter are free room and board received by official visitors and free instruction received by nonresident

students from the educational institutions where they are studying; in practice, information on goods and services provided without a quid pro quo will not usually be available.

288. The most common goods and services that will be entered in "travel" are lodging, meals, entertainment, and transportation within the economy visited, all of which are consumed in the providing economy, together with gifts, souvenirs, and articles for their own use that travelers take out of the economies visited. As a practical matter, this Manual does not suggest that any amounts which travelers might pay for what are, strictly speaking, "unrequited transfers" (e.g., airport taxes) should be allocated to that item instead of to "travel," since such a rigid separation between services and unrequited transfers is not essential in a balance of payments context.

CHAPTER FOURTEEN

Investment Income

(1) Coverage

289. “Investment income” covers income derived from the ownership of foreign financial assets, excluding the portfolio investor’s portion of the earnings of incorporated enterprises that are not formally distributed.

290. The most common types of investment income are dividends and interest. Dividends, including stock dividends and bonus shares, are the distribution of earnings in respect of the shares and other forms of participation in the equity of incorporated private enterprises, cooperatives, and public corporations. They represent income that is payable without a binding agreement between the creditor and the debtor. Interest, including discounts and commitment charges in lieu of interest, comprises income on loans and debt securities, i.e., such financial claims as bank deposits, bills, bonds, promissory notes, and trade advances. It is payable in accordance with a binding agreement between the creditor and the debtor.

291. Other types of investment income are the earnings of branches and other unincorporated direct investment enterprises, and the direct investor’s portion of the earnings of incorporated direct investment enterprises that are not formally distributed, i.e., earnings other than dividends. The part of those earnings that is attributed to the direct investor is proportionate to his participation in the equity of the enterprise.

292. Income derived from the use of real resources is not considered as income from financial investment but as nonfinancial income. Thus, earnings from film rentals, charters of mobile equipment, and leases of real estate (rentals) should not be classified as “investment income” but included with other items for services and income. Merchandise exported and imported under a financial leasing arrangement, however, is considered to have changed ownership (see

paragraph 217); the so-called lease payment thus consists of investment income and repayment of principal on the financial obligation that was in effect created when that change of ownership occurred.

293. Capital gains and losses are not income on investments but are part of the value of the investments. All capital gains and losses are included in the capital account (except, for practical reasons, those on insurance transactions, as explained in paragraph 263); valuation changes that are not realized in the form of capital gains and losses are not included in the balance of payments, although supplementary information on valuation changes is requested for reserves. It should be noted, however, that some debt securities, such as bonds, notes, and bills, are originally issued at a value different from the stated fixed sum that their holder has the unconditional right to receive when the obligations mature. This premium or discount should be regarded as negative interest or interest, respectively, rather than a capital loss or gain. It follows that the value of the securities to be entered in the capital account is the amount for which they are actually issued. The fixed sum paid at maturity will comprise both repayment of this original principal amount and (negative or positive) interest; the interest should be shown as investment income.

(2) Classification

294. For the purpose of balance of payments recording, the following categories of "investment income" should be distinguished.

(a) Direct investment income

295. The two components under this heading pertain to income that accrues to a direct investor from ownership of direct investment capital. (See Chapter 18, section (2) for the definition of direct investment capital.) The component for reinvested earnings covers the earnings of branches and other unincorporated direct investment enterprises (excluding any part that can be identified as having been remitted) and the direct investor's portion of earnings of incorporated direct investment enterprises that are not formally distributed (see paragraph 291). The other component of direct investment income covers any earnings of branches and other unincorporated direct investment enterprises that are identified as having been remitted, in addition to dividends and interest distributed to the direct investor.

(b) Other investment income

296. The two components referring to official income together cover income receivable or payable by the compiling economy's

general government or central bank, by a foreign general government or central bank, or by an international organization. Such income includes interest earned on deposits, debt securities, and other loans, as well as any dividends on equity securities. Moreover, official income includes all income payable to, by, or through the International Monetary Fund. Such income thus covers charges, assessments, interest, and remuneration on transactions and holdings with the IMF in both the General Account¹ and the Special Drawing Account,¹ as well as other income receivable by the official sector on reserves.

297. A government may sometimes be the direct investor in a direct investment enterprise abroad; income from such an enterprise should be classified as direct investment income rather than as other official income.

298. The component referring to private income covers investment income other than that specified above. Dividends on equity securities and interest earned on bank deposits, debt securities, and loans form the elements of this item.

(3) Time of Recording

299. Reinvested earnings of direct investment enterprises should be recorded in the balance of payments for the period in which they are earned. Dividends and interest should be recorded as of the time that they become due for payment. Remitted earnings of branches and other unincorporated enterprises should be recorded as of the time that they are transferred.

300. In explanation of this apparent difference in treatment between earnings that are formally distributed and other earnings, it is useful to recall that reinvested earnings represent the net income accruing during a given period. In contrast, dividends and remitted earnings of branches are discretionary distributions that can be made at any time—even in a period when a net loss is sustained—and are therefore not attributable to the earnings of a particular period. To determine the period in which those reinvested earnings are earned or other investment income becomes payable, reference to balance sheets, annual reports, and similar documents of the investor or the enterprise may be helpful.

¹In the Second Amendment to the Articles of Agreement these are the General Department and the Special Drawing Rights Department, respectively.

(4) Measurement and Recording of Earnings

(a) Method of calculation

301. Earnings refer to the net income, positive or negative, of an enterprise from production and property, including the ownership of other enterprises. These earnings are measured net of income or corporation taxes due for payment without penalty during the recording period by the enterprise to the economy in which that enterprise operates. This practice is followed because such taxes are considered payable by the enterprise and not by its owners.

302. Furthermore, earnings should be calculated net of any provision for depreciation of fixed capital. Depreciation is measured by the value, at current replacement cost, of the reproducible fixed assets used up during an accounting period as a result of normal wear and tear, foreseen obsolescence, and accidental damage that is not made good by repair. In the calculation of depreciation, the expected economic lifetime of the individual asset should be taken into account. Although depreciation should, in principle, be calculated at current replacement cost, data will often be available only on an historical cost basis.

303. As capital gains or losses, i.e., gains or losses resulting from the realization of valuation changes, do not stem from the operations of an enterprise, they should be excluded from the calculation of its operational earnings. Unforeseen obsolescence, catastrophes, and depletion of natural resources are treated as a capital loss at the time that the decrease in value actually occurs. Any losses on the writing off of bad debts or on expropriation without compensation should also be excluded in calculating earnings.

(b) Recording of reinvested earnings

304. Unremitted earnings of branches and other unincorporated direct investment enterprises, and the direct investor's portion of earnings of incorporated direct investment enterprises that are not formally distributed, are conceived of as providing additional capital to the enterprises, thus increasing the value of an economy's stock of foreign assets and liabilities. In the recording of such earnings in the balance of payments, therefore, entries should be made both for direct investment income and for direct investment capital. For example, the reinvested earnings of a foreign direct investment enterprise attributable to a resident direct investor should be entered in the relevant components as a credit in the current account category for investment income and as a debit in the capital account category

for direct investment. The share of portfolio investors in the earnings of an incorporated direct investment enterprise that are not formally distributed should not be entered in the balance of payments.

(c) *Entries for losses*

305. The direct investor's share in the net losses other than capital losses of an enterprise should be recorded as negative income in the direct investment income component of the balance of payments. Thus, the economy recording losses on residents' direct investment abroad should enter the losses as a negative credit, while the economy in which the direct investment is made should record them as a negative debit. This method of recording losses is adopted so that the credit side of the component will reflect the compiling economy's net earnings on its direct investments abroad, while the debit side will refer to the foreign direct investors' net earnings on direct investments in the compiling economy.

(d) *Stock dividends and bonus shares*

306. The distribution to foreign shareholders of earnings in the form of stock dividends and bonus shares should be recorded in the balance of payments in the same manner as reinvested earnings, that is, by making entries both in investment income and in the capital account.

CHAPTER FIFTEEN

Other Goods, Services, and Income

(1) Coverage

307. Goods, services, and income to be classified in this category are all the real resources that have not been classified under merchandise, shipment, other transportation, travel, and investment income. No exhaustive listing is provided for the types of transaction that fall into this category, but the amounts not included elsewhere for three types of official transaction and for private labor income and property income are to be reported here separately.

308. The relative importance of the various types of transaction covered in this item differs considerably from one economy to another. Countries may wish to show separately items that are important for them, even though they are not called for by this Manual.

309. For a description of the nonfinancial intangibles that are considered to be unrequited transfers rather than services or income and that should therefore not be included in this category, see Chapter 16.

(2) Definition of Official and Private Transactions

310. Official transactions comprise those of general government and the central bank; these sectors are defined in paragraphs 54 and 66, respectively. State and local governments, as well as central governments, are to be covered, even though no breakdown is requested. However, enterprises other than the central bank that are operated by a government are excluded. The official category covers the transactions both of the resident government with foreigners and of foreign governments with residents of the compiling economy; foreign general government is defined to include international bodies other than enterprises (see paragraph 57). All other transactors are defined as being nonofficial, that is, private parties.

(3) Main Types of Official Transaction

311. Three standard components for official transactions are distinguished in this category; they specify whether (a) both parties to the transactions are in the official sector, (b) the resident official sector is dealing with other foreign sectors, or (c) other resident sectors are dealing with foreign official sectors. From the standpoint of the compiling economy, the types of transaction in each of these groups are likely to be quite different. Some of the principal kinds that should be reported are listed below.

(a) *Embassies and consulates abroad*

312. Since these organizations are treated as residents of the country that they are representing and not of the country where they are located, remittances of cash, shipments of commodities, and any other transactions between them and residents of their home country are not included in the balance of payments. Instead, the transactions to be recorded are those with residents of the country where they are located and of other foreign countries. The following kinds of item are among those that should be reported:

- (i) wage and salary payments, representing labor income of local staff;
- (ii) personal expenditures by diplomatic and consular staff and their dependents in the country where they are stationed; and
- (iii) other expenditures by embassies and consulates for goods and services such as office supplies and furnishings, fuel and utilities, rent or purchases and sales of embassy and other buildings, official cars and their operation and maintenance, and official entertainment.

(b) *Military units and agencies abroad*

313. These are treated in the same way as embassies and consulates, and the same kinds of item should be covered. The compiler should keep in mind that the personal expenditures of military personnel and their dependents comprise their expenditures in the foreign country in which they are stationed and exclude expenditures in their own canteens, commissaries, or post exchanges.

(c) *Other official entities located abroad*

314. Many such entities of an economy will be integrated with the embassy organization, but the transactions with other economies by those with a separate existence should also be reported. Examples are aid missions (including the U.S. Peace Corps), government tourist

323. The main element of the component for “property income, n.i.e.” is income accruing to the owners of patents, copyrights, and similar nonfinancial intangible assets. Income of this sort is often referred to by such terms as royalties and license fees. While a foreigner, by the conventions of this Manual, cannot be said to purchase such assets outright from a resident of the economy whose government issues them, a foreign enterprise may nonetheless acquire the right to use such assets outside the territory of the economy that issues them. The income payable for that use constitutes nonfinancial property income.

324. This component will rarely include any income from the ownership of land. Under the conventions of this Manual, land used for commercial purposes must be used by an enterprise, and except in unusual circumstances that enterprise would be a resident of the economy where the land is located; moreover, land must always be owned by a resident of the economy where it is located. That being the case, resident-foreigner transactions with respect to the commercial use of land would seldom occur. The foreign entities that could be present in an economy to use land for noncommercial purposes would be governments or individuals. The transactions of those foreigners, including any income payable for the use of land, are to be classified in this Manual as “travel,” “official transactions,” above, or “labor income, n.i.e.”

(c) *Other goods and services*

325. This component covers all goods and services that are not specifically allocated to other items. Some of the main kinds that are appropriate to this item are listed below.

(i) *Nonmerchandise insurance*

326. All types of insurance and reinsurance are included here with the exception of the transactions in the direct insurance of merchandise and some other goods that are included in “shipment,” as described in paragraph 262. Marine and aircraft insurance—that is, insurance of the carrier, in contrast to insurance of the goods carried therein—should also be included here with nonmerchandise insurance.

327. Life insurance, like other types of insurance, can be most conveniently recorded in the balance of payments on the basis of the difference between premiums to be paid and claims to be disbursed, which is taken to represent the insurance service charge (see paragraph 263). This treatment ignores the capital element inherent in

life insurance transactions but, as international transactions in life insurance are not usually large, this simplification is recommended. Pension schemes operating through a separately organized fund are akin to life insurance, and the net amounts received and paid should be added to the amounts reported for insurance. Other types of pension disbursed and contribution collected are included in "unrequited transfers" (see paragraphs 352, 358-59).

(ii) Communications

328. Communication services include postal services and cable, telephone, and telecommunications services.

(iii) Advertising

329. Exporters and other enterprises may advertise abroad in the press and periodicals, by radio or television, or by direct mail.

(iv) Brokerage

330. Covered under this heading are all fees paid to agents by their principals other than those fees included in the value of merchandise (see paragraph 245); the brokerage and commissions charged on other transactions; and the financial services performed by banks, underwriters, and finance houses, as measured by the amounts of their charges.

331. The offsets to any agents' fees received by a resident agent from a resident or by a foreign agent from a foreigner that are included with "merchandise" (see paragraph 245) should be entered here.

(v) Management

332. An important element is the provision of management, accounting, and kindred services to a branch or subsidiary by its parent.

(vi) Operational leasing, other than charters

333. Operational leasing is leasing other than that regarded as financial leasing. For the definition of financial leasing, see paragraph 217. The charter of carriers is included in "other transportation."

334. The operational leasing of structures, machinery, equipment other than transportation equipment, films, tapes, records, and other tangible assets is included here; such leasing is sometimes referred to

as rental. The commercial value of the assets themselves is excluded from export and import totals.

(vii) Periodicals bought through subscriptions

335. Periodicals coming from abroad under subscription arrangements are classified here, not under merchandise.

(viii) Processing and repair

336. When an enterprise in one economy processes goods owned by another economy, the value of the goods that cross the frontier is excluded from the merchandise item and the fees paid for processing are entered in this item. Improvements, repairs except those classified as port services, and other nondistributive services performed for nonresidents on goods should also be entered in this item.

(ix) Merchanting

337. When goods are acquired and relinquished again without crossing the frontier of the economy in which their temporary owner is a resident, the temporary owner is considered to have been engaging in a merchanting transaction rather than in an import and re-export of the goods (see paragraph 222). Any difference in the value of the goods when they were acquired and when they were relinquished is to be entered in this item.

338. A related transaction may take the form of speculation in commodity futures, where the parties are not residents of the same economy. The question of whether or not any change of ownership of the commodity has actually taken place, if the delivery date specified in the contract to purchase coincides with that in the contract to sell, need not be considered, as the net amount of the purchase and sale (reflecting any profit or loss) is to be assigned to this item in either case. Commodity arbitrage undertaken by the resident of one economy between two nonresidents represents still another variant of the same sort of transaction and is also covered here. Speculative or arbitrage gains and losses realized on financial items, however, are to be entered in the capital account (see paragraph 370).

(x) Professional and technical services

339. These services include surveys, research, and provision of instruction and technical know-how. It may be of analytic interest to distinguish between services obtained under private aid programs (with contraentries in unrequited transfers) and other technical services (with contraentries reflecting some form of payment for the services).

CHAPTER SIXTEEN

Unrequited Transfers

(1) Definition

340. When an entry in the balance of payments records that one economy has provided another with a real resource or a financial item, the double-entry system requires that an offsetting entry be made. If that offset does not show a recompense in the form of the provision of a real resource or a financial item, it is designated as an unrequited transfer. The coverage in the balance of payments of unrequited transfers is determined by the decisions taken about two matters.

341. The first question to be considered is whether or not the provision of an economic value should be recorded even when no quid pro quo is received. If any such provision were not recorded, no offsetting entry showing an unrequited transfer would be required. The recommendation of this Manual, however, is that the balance of payments should show virtually all economic values provided by residents of one economy to another economy, including those without a quid pro quo. The statement should also show those changes in real resources and financial items affecting both a given economy and the rest of the world that may be said to result from a change of residence (migration) on the part of an individual, although it should exclude similar changes that come about through a change in the territory of an economy. Other one-sided changes in an economy's real resources or financial items do not, strictly speaking, reflect the provision of economic values between that economy and the rest of the world. Some changes of that sort—specifically, those produced by the monetization of gold, the allocation of SDRs, and reclassifications and valuation changes in reserves—are to be shown as supplementary information in the balance of payments, but their counterparts are by convention not regarded as unrequited transfers and thus are not taken up in this chapter.

342. The second question is how benefits provided or received are to be separated into (a) some that are regarded as economic values

(i.e., that constitute real resources or financial items) and (b) others on which no economic value is placed (i.e., that do not provide a quid pro quo and that thus constitute unrequited transfers). The intended distinction between intangible real resources (services and income) and unrequited transfers that offer no quid pro quo cannot be fully defined in an objective way, although a conventional view of the two categories is referred to in paragraph 200. In contrast to real resources, an unrequited transfer, which may be either voluntary or obligatory, reflects in general a benefit that cannot be quantitated, such as a better political or economic relationship between the parties; a nonspecific amount of services, such as the administrative, protective, and defense services made available by the government to a taxpayer; or an intangible provided on a compulsory basis, such as that involved in the registration of a carrier.

343. The more important kinds of unrequited transfer are mentioned in the discussion of this item that follows. Conversely, other kinds of transaction whose classification might raise questions are excluded from the category of unrequited transfers by implication, as they are explicitly allocated to the service or income items. Any remaining transactions—the only kind whose classification could thus actually be in doubt—are probably so unusual as to be of little practical importance.

(2) Valuation and Timing

344. Because unrequited transfers are not conceived as emanating directly from the productive process, their value cannot be readily appraised but should be assumed to be the same as that of the real and financial resources to which they are offsets. Those resources themselves may have no actual market value and may have to be valued at cost or even at some notional value that may be assigned to them by one of the parties to the transaction (see Chapter 4).

345. Taxes, fines, and other unrequited transfers that are imposed by one party on the other are to be recorded at the time that they become due for payment without penalty. Other unrequited transfers are to be recorded at the time that the resources to which they are offsets change ownership.

(3) Classification

346. Unrequited transfers are classified in four main categories according to the sectors of the immediate parties to the transfers: (a) private (nonofficial) unrequited transfers, (b) interofficial unre-

quited transfers, (c) other unrequited transfers of the compiling economy's official sector, and (d) other unrequited transfers of foreign official sectors; the first category is further analyzed to show separately migrants' transfers and workers' remittances. The official sector refers in every instance to general government and the central bank, as defined in paragraphs 54 and 66, respectively; foreign general government is defined to include international bodies other than enterprises (see paragraph 57).

(a) *Private unrequited transfers*

347. For the purpose of balance of payments recording, the following main categories of nonofficial transfers should be distinguished.

(i) *Migrants' transfers*

348. In the strictest sense, these transfers are not unrequited transfers, which refer to transactions between two parties, but are contraentries to the flows of goods and the changes in financial items that arise from migration (change of residence for at least a year) of individuals from one economy to another. The contraentries are thus equal to the net worth of the migrants.

349. All the household and personal effects of migrants, together with such of their movable capital goods as are actually transferred from the old to the new economy, are included in "merchandise." Those merchandise flows and the corresponding offsets should in principle be recorded at the time of migration. If "merchandise" is derived from the trade returns, no timing correction of the trade figures is suggested, but the offsets in this item are to be recorded in the same period in which the exports and imports are recorded.

350. Enterprises in which migrants retain ownership after their departure (including those that employ the land, structures, and movable capital goods that are not actually transferred), together with the migrants' nonfinancial intangible assets issued by the country from which they have migrated, become foreign claims of the migrants and consequently of the economy into which they have migrated. Migrants' claims on (liabilities to) other residents of the former economy or residents of a third economy also become foreign claims (liabilities) of the economy to which the persons have migrated. Correspondingly, migrants' claims on (liabilities to) the latter economy become claims between its residents. Changes in the net financial assets of the economies concerned and their offsets in this item are to be recorded at the time of migration. (See Chapter 17.)

(ii) Workers' remittances

351. This component covers unrequited transfers by those migrants (persons who have come to an economy and who stay, or are expected to stay, for a year or more) employed by their new economy, of which they are considered to be residents. Similar persons who work for and stay in the new economy for less than a year are considered to be nonresidents; their transactions are appropriate mainly to the component for labor income, n.i.e. (see paragraphs 319–20).

(iii) Other private unrequited transfers

352. This component covers transfers between individuals, between nonofficial organizations, and between an individual and a nonofficial organization. Such transfers include gifts, dowries, and inheritances; alimony and other support remittances, except those by former migrants; tickets sold by and prizes won from nongovernmental lotteries; noncontractual pensions from nongovernmental organizations; compensation for damages (excluding insurance indemnities); contributions to religious, scientific, cultural, and charitable organizations; and membership fees paid to nonprofit associations.

353. A remittance from a resident of a given economy to finance another resident staying abroad only temporarily is a transaction between residents of the same economy. What is to be recorded in the balance of payments are the goods and services procured abroad by the traveler or other resident to whom the remittance was made, not any sort of unrequited transfer.

(b) *Interofficial unrequited transfers*

354. These are transactions between the official sectors of two economies. They cover grants of real resources and financial items. Grants received in cash and refunds of such grants should both be recorded in this item on a gross basis.

355. The item includes voluntary subsidies to current budgets (including defense budgets), voluntary cancellation of debt, grants of technical assistance, indemnities imposed under peace treaties (reparations), and government contributions to international organizations for administrative expenses.

(c) *Other official unrequited transfers of compiling economy*

356. These are transactions between the compiling economy's official sector and private nonresidents. Some of the principal kinds that should be reported in this component are as follows.

(i) Technical assistance and scholarships

357. On the credit side, this item covers grants of technical assistance received from nongovernmental entities. On the debit side, this item covers scholarships and similar grants for on-the-job training given to nonresident individuals to finance their education in the donor's economy or abroad.

(ii) Other

358. On the credit side, this item includes taxes, fines, fees for fishing rights and carrier registrations, and tickets sold by government-sponsored lotteries. On the debit side, this item includes refunds on taxes, membership fees paid to nongovernmental organizations, grants to nongovernmental entities, noncontractual pensions, and prizes won from government-sponsored lotteries.

(d) *Other official unrequited transfers of foreign economies*

359. These are transactions between foreign governments and private residents of the compiling economy. This component has the same coverage, with credits and debits reversed, as the preceding component, "other official unrequited transfers of the compiling economy."

CHAPTER SEVENTEEN

Capital Account (Financial Items)

(1) Definition

360. The capital account of the balance of payments as constructed in this Manual comprises all transactions—in the restricted sense of changes of legal ownership, including the creation and liquidation of claims—in an economy's foreign financial assets and liabilities, together with some specified changes of other kinds (see paragraph 371) that may affect its foreign assets and liabilities and the counterparts to those changes.

(2) Coverage of Financial Items

361. An economy's foreign financial assets consist of its monetary gold, special drawing rights (SDRs) in the Fund, and claims on nonresidents. Its foreign liabilities consist of its indebtedness to nonresidents. In this and the following chapters in this Manual, foreign financial assets and liabilities are sometimes referred to for convenience simply as "foreign assets" or "assets."

362. In the determination of which financial items constitute claims on or liabilities to nonresidents, what is crucial is that the creditor and debtor must be residents of different economies. In that context, the unit in which the claim or liability is denominated—whether the national currency, a foreign currency, or a unit like the SDR—is not relevant. Furthermore, assets must represent actual claims that are legally in existence. The authorization, commitment, or extension of an unutilized line of credit or the incurrence of a contingent obligation does not establish such a claim, and the pledging or setting aside of an asset (as in a sinking fund) does not settle a claim or alter the ownership of the asset.

363. The conventions adopted in this Manual result in the ownership of some nonfinancial assets being construed instead as the ownership of financial assets, i.e., claims. Several specific cases may be noted.

(a) Immovable assets, such as land and structures (except when those structures are owned by foreign government entities), and nonfinancial intangible assets issued by a government (e.g., patents and copyrights) are construed as always being owned by residents of the economy where they are located or issued, respectively (see paragraph 63). Moreover, mobile equipment (such as ships, aircraft, highway vehicles, rolling stock, fishing vessels, and gas and oil drilling rigs) that operates within an economy for at least a year is considered to be owned by an entity residing in the economy where it operates (see paragraph 69). When the actual legal owner of such assets is a nonresident, therefore, he can only be considered to have a financial claim on a resident entity—actual or notional—that must be construed as being the owner.

(b) An unincorporated enterprise that operates in a different economy from the one in which its owner resides is taken to be a separate entity; that entity is a resident of the economy where it operates rather than of the economy of its owner (see paragraph 67). All assets, nonfinancial as well as financial, attributed to such an enterprise are to be regarded as foreign financial assets for the owner of the enterprise.

(c) Any goods transferred under a financial leasing arrangement are presumed to have changed ownership and thus to have been converted into a financial asset for the lessor and a liability for the lessee (see paragraph 217).

(3) Transactions in Assets

(a) Kinds of transaction

364. Transactions in assets (specifically, changes of ownership, including the creation and liquidation of claims) most often reflect an exchange of economic values. Financial items may be exchanged for either other financial items or real resources. A financial item, however, may also be provided by one party to a transaction without any economic value being acquired by that party in exchange for it. The offset to this latter type of provision of an asset is an unrequited transfer.

(b) Parties to transactions

365. To establish whether a transaction in a foreign asset was a transaction between a resident and a foreigner, the identities of both

parties would have to be known. The information available on transferable claims that constitute foreign assets, however, often does not permit a link between the two parties to the same transaction to be ascertained. That is, a compiler may not be able to find out whether a resident who acquired or relinquished a transferable claim on a foreigner conducted the transaction with another resident or with a foreigner, or whether a foreigner who acquired or relinquished a transferable claim on a resident dealt with another foreigner or with a resident. A recommendation, therefore, that the balance of payments be confined to transactions in assets between residents and foreigners would be impossible to implement in some cases. Instead, the balance of payments is conceived more broadly as covering all transactions in foreign assets and liabilities; such transactions include not only those in all kinds of assets and liabilities between a resident and a foreigner but also those in an economy's transferable assets between two residents or in its transferable liabilities between two foreigners.

366. Because the credit and debit entries for each individual type of capital are generally netted out according to the rules of this Manual (see paragraphs 375–78), many if not most of the transactions between residents and, to an even greater extent, between foreigners will tend to cancel each other and thus will not actually show up as entries in the statement. For assets, those transactions between resident creditors that are classified in different functional categories or domestic sectors will probably be the most prevalent type that does not net out. For liabilities, the identity of the foreign creditor is a factor only in differentiating between direct investment and other capital and between liabilities constituting reserves for foreign authorities and other liabilities.

367. Besides canceling out many transactions between residents and between foreigners, the netting procedure can also result in offsetting a transaction between a resident and a foreigner by a transaction between residents or even one between foreigners. That is, a resident may come to have a claim against a foreigner and, during the same recording period, pass it on to another resident classified in a different sector. The first resident's transaction with a foreigner will be netted out by the same resident's subsequent transaction with another resident, so that the balance of payments will show only the increase in the second resident's holdings, which were actually acquired through a transaction with another resident. The effect, of course, is the same as if the second resident had dealt directly with the foreigner, although the analytic implications of a direct and an indirect transaction could be somewhat different.

(c) *Reinvestment of earnings*

368. That part of the reinvested earnings of a direct investment enterprise which is treated in the balance of payments as accruing to the foreign direct investor (i.e., a share in the same proportion as participation in the equity of the enterprise) is conceived as being paid out as investment income and reinvested in the enterprise, thus increasing the value of an economy's stock of foreign assets or liabilities. Such reinvestment of earnings is to be shown in the capital account. In a similar way, the distribution to investors of earnings not in cash or in kind (stock dividends and bonus shares) that is included in the item for "investment income" will result in an increase in the investors' equity that is to be shown in the capital account.

(d) *Borderline cases*

369. A question may arise as to whether a transaction has taken place when the maturity of a debt instrument is extended, changing it from a nominally short-term claim to a nominally long-term claim, or when the government takes over the obligation for liabilities incurred by the private sector, altering the sector of the domestic debtor. As a change in the original terms of a contract presumably requires the assent of both parties, it seems entirely reasonable to consider that the existing claim was satisfied by the creation of a new one, i.e., that a pair of transactions between a resident and a foreigner has occurred. Changes in the maturity or other contractual terms of existing assets are thus taken to constitute transactions for the purpose of the balance of payments.

370. Another situation also concerns pairs of transactions that are very closely linked, in this instance because a transactor intends to dispose of a certain asset at virtually the same moment when ownership of it is nominally acquired. Such cases include, for example, arbitrage and certain other dealings in foreign exchange, such as those under forward contracts. The question for consideration is whether (i) two changes of ownership of the asset have actually occurred, so that any profit or loss could be regarded as the realization of a capital gain or loss, to be entered like any other realization of a capital gain or loss (see paragraph 41) in the capital account item that refers to the asset concerned, or (ii) no change of ownership has effectively taken place, so that the profit or loss could be seen as a fee for a service, an unrequited transfer, or even a counterpart in the capital account. This Manual recommends that the solution set out in (i) be adopted, because any of the entries in the capital account may in fact reflect the capital gain or loss realized on the purchase and sale of financial items

at different market prices, without any regard to the circumstance that some of those items may have been owned only very briefly.

(4) Other Types of Change

371. The value of an economy's assets of a given kind may change in several ways, in addition to the changes brought about by transactions of the type described above in section (3). Which of these other changes should be recorded in the balance of payments and which should be omitted from it are not matters that have been decided on any broad principle. Rather, the recommendations in this Manual have been formulated with the pragmatic view of producing a standard treatment that can be applied generally and that will satisfy most analytic requirements.

(a) Types to be recorded

372. Changes in the value of an economy's foreign financial items resulting from the following causes have been selected for inclusion in the balance of payments statement. Item (iii) below, however, is included merely as supplementary information (see paragraphs 454–59).

(i) Allocation or cancellation of SDRs. An increase in holdings of the asset through allocation, or a decrease in holdings through cancellation, should be entered, along with a counterpart to represent the allocation or cancellation.

(ii) Monetization or demonetization of gold. The same gold may be held, at different times, either as a commodity (nonmonetary gold) or as a financial asset (monetary gold). A change in holdings of monetary gold resulting from the reclassification of a given stock of gold should be recorded, along with a counterpart to represent the monetization or demonetization.

(iii) Valuation changes in reserves. Valuation changes reflect changes in the prices of various components of reserves relative to the unit of account. As long as an official price for gold was maintained and the effective exchange rates for currencies were based on par values that were quite stable, changes of this kind were infrequent occurrences; the authorities' concern on that score was in fact primarily with managing the composition of their reserves so as to avoid them. Under arrangements existing at this writing, however, valuation changes may come about quite often, so that their effects on reserves are of interest to keep continuously under review, along with the changes that are due to transactions. A counterpart is provided as an

offset to the valuation changes that are to be recorded as supplementary information.

(iv) Reclassification of past purchases from the Fund. Such a reclassification occurs in the following situation. A member may make a reserve tranche purchase from the Fund and record in its balance of payments a decrease in its reserve position in the Fund, which is an asset. In a subsequent recording period when the information needed to make such a determination becomes available, the Fund could determine that the member had qualified at the time of the purchase for the use of Fund credit under the policy adopted for the compensatory financing of export fluctuations. The purchase would then be reclassified. Instead of revising the original balance of payments entry (a credit) from a decrease in assets to an increase in liabilities, this Manual provides that the original entry be retained and additional entries for the reclassification, showing an equal increase in both the asset (debit) and the liability (credit), be recorded in the period in which it takes place. This recommendation is made in order to align the balance of payments entries with the statistics and accounts as published by the Fund on its own activities.

(v) Other reclassification changes in reserves. The authorities may assume or relinquish direct and effective control over assets to which they do not legally hold title. Such changes in the level of their reserves are to be recorded, along with a counterpart to the reclassification. This counterpart is needed because no entry is to be made for the resulting change in the other component that is affected by the reclassification (see paragraph 374 (ii)).

(vi) Migrants' capital transfers. At the time that a person's residence is deemed to have changed, the person's financial assets and liabilities are to be recorded in the balance of payments in the same way as if the ownership of those items had changed from a resident of the migrant's former country to a resident of the migrant's new country. From the viewpoint of the new country, financial assets and liabilities may be created or extinguished, and enterprises located in the former country, together with nonfinancial intangible assets issued by that country, become financial assets for the new country. When the balance of payments entries are derived from records of transactions, it would presumably be much easier to show only the portion of those assets that is thought of as being actually transferred. When the entries are based on data for holdings by residents, however, difficulty would be encountered in eliminating migrants' assets that are not "actually transferred." The recommended method agrees with the treatment applied in the United Nations' *A System of National Accounts (SNA)*.

The offset to a change in an economy's financial items resulting from migration is to be entered in "unrequited transfers."

(b) *Valuation changes to be omitted*

373. All valuation changes in an economy's financial claims on and liabilities to the rest of the world, except those referred to in paragraph 372 (iii), are to be omitted from the balance of payments statement.

(i) Valuation changes, except those in reserves. Such changes may stem from either one or both of two sources. First, an asset's value in the unit in which the asset is denominated may change. Second, the price of the unit in which an asset is denominated may change in terms of the unit of account used for recording the asset. It should be noted that the effects of these valuation changes are omitted from the balance of payments only for so long as the ownership of the asset does not change; when it does change, they are realized as capital gains or losses. Specifically, when an asset acquired at one price is disposed of at a different price, both the acquisition and disposition are recorded at the respective market value, and the difference in value stemming from the price change (the capital gain or loss) is thus contained in the balance of payments.

(ii) Write-offs. A valuation change resulting from the unwillingness or inability of the debtor to make full or partial repayment in settlement of a claim, including expropriation without compensation, takes on the form of a write-off when the creditor chooses to regard part or all of that claim as having been canceled. Since no contract has been made to dispose of the claim, however, the capital losses produced by such valuation changes are technically unrealized and thus are not to be included in the balance of payments.

(c) *Classification changes to be omitted*

374. All classification changes in an economy's financial claims on and liabilities to the rest of the world, except those referred to in paragraph 372 (iv) and (v), are to be omitted from the balance of payments.

(i) Changes in classification owing to territorial changes. For example, a resident entity owns an enterprise operating in some part of the domestic territory that is ceded to another economy, but the resident status of the owner itself remains unaffected. Under the conventions of this Manual, the owner has thereby acquired a foreign financial asset in place of its previous domestic asset. Such changes, however, are not to be shown in the balance of payments.

(ii) Other changes in classification of existing assets, except those in reserves. A creditor's holdings of foreign corporate equities, for instance, may be reclassified from portfolio to direct investment when it acquires enough additional equities to make it the direct investor. The reclassification of the earlier holdings is not to be entered in the balance of payments, although the acquisition of additional equities is classified as direct investment.

(5) Net Recording

375. Two or more changes in a given asset, or changes in two or more different assets classified in the same standard component, are to be consolidated into a single entry that reflects the net effect of all the increases and decreases during the recording period in holdings of that type of asset. Net decreases in claims or other assets and net increases in liabilities are recorded as credits; net increases in assets and net decreases in liabilities are recorded as debits.

376. Net recording for each standard component distinguished in the capital account is specified partly because the gross data for transactions or other changes are often not available. Changes derived from records showing amounts outstanding at the beginning and end of the reporting period, for example, always represent net changes. In addition, however, gross changes may be of limited interest or may even tend to be somewhat misleading. Gross recording, for example, would give added prominence to the transactions between residents and those between foreigners that are covered in the statement, and in particular to such of those transactions as are likely to be of least interest to users of the statement. Even though gross entries could be a relevant factor in analyzing developments in an economy's payments position, inasmuch as they provide evidence of variations in activity or turnover from period to period, other indications of this phenomenon would no doubt be available.

377. The fact that this Manual specifies drawings on some loans separately from repayments on those loans (see paragraph 438) might seem to be an exception to the general rule of net recording. The loans that are so treated, however, all have original maturities of more than one year, so that the drawings and repayments in any statement covering the period of a year or less will probably not refer to the same loans. Moreover, the extension of loans, which is usually a voluntary act, is differently motivated from any contractual repayments that occur during the same period. Drawings and repayments, therefore, form separate components from the standpoint of behavior, even though the underlying assets happen to be of a type that

falls under the same category according to the other characteristics (function, term, and sector) that are being used generally to classify capital items.

378. In the totaling of net credits and debits for two or more separate components, the net approach is always to be favored. The interpretation to be placed on a summary item showing separately net credits and debits would be most uncertain.

(6) Valuation and Timing

379. Changes in assets that stem from transactions between two parties are valued so as to reflect the market value of the asset that is stipulated by the contract made to acquire or relinquish it. Other types of change should reflect the difference in the market value equivalent of the owner's holdings immediately before and after the change being recorded is deemed to have occurred. The concept of market value and its specific application to foreign financial items are discussed in Chapter 4.

380. The time at which transactions in financial items are considered to take place for purposes of recording is when the creditor and debtor enter the claim and liability, respectively, on their books. For many such transactions, a date (the "value date") is actually specified, for the very purpose of ensuring that the timing agrees in the books for both parties. The contracts to acquire or dispose of such items may, of course, have been made at an earlier time. Other types of change generally occur, or are deemed to occur, as of a stated date, and that date is the relevant one for balance of payments recording.

(7) Classification

381. The primary purpose of the classification for the financial items adopted in this Manual is to distinguish categories that exhibit different patterns of behavior. The changes in an economy's holdings of financial items that are recorded in the balance of payments come about for a wide variety of reasons, such as to settle actual or prospective imbalances resulting from autonomous transactions; to influence exchange rates; to make capital gains (or avoid losses) on past or future valuation changes, including those resulting from exchange rate changes; to take advantage of interest rate differentials; to establish or expand enterprises or take over their operations; and to obtain or provide additional real resources. In the collection of data, it is usually not feasible to inquire into the underlying causes and motivations for changes in holdings. However, behavior is also

associated to a considerable degree with such attributes as the type of asset and of holder. Characteristics of that kind which are readily observable can thus be used as a basis for developing a classification scheme.

382. These considerations have given rise to the application in this Manual of three main approaches for classifying all financial items—by assets and liabilities, by functional category, and by original contractual maturity. These approaches should be regarded as being employed simultaneously, even though they must be introduced consecutively in presenting the data. That is, instead of listing the standard components according to functional categories, as has been done in the list in Chapter 8, the list could have been organized instead, and the data can at any time still be rearranged, to focus mainly on the classification according to either of the other approaches, involving the separation of assets from liabilities and of long-term capital from short-term capital. This point is of some importance, as the relative weight attaching to the various criteria depends partly on the specific analytic purpose for which the data are to be used.

383. Other subordinate classifications can be used to identify more specifically certain types of asset included in categories produced by the uniform application of the main approaches for classifying all financial items. Some individual items of this kind are called for in the list of standard components; others, which may be significant only for certain countries, can be compiled as supplementary information.

(a) *Assets and liabilities*

384. The distinction between assets and liabilities is almost always likely to be of interest. Even for financial intermediaries that in effect borrow and relend abroad the same funds, the terms of the borrowing and lending are usually different, so that the two offsetting flows may have different implications for the balance of payments. For direct investment, however, such a distinction is not very meaningful, in view of the affiliation between the two parties that allows them wide latitude to enter into whatever financial arrangements between them they find convenient.

(b) *Functional types of capital*

385. The classification used in this Manual distinguishes three broad categories of capital (plus a fourth, residual group), the behavior of which may be expected to be influenced by the type of transaction in which they are predominately employed.

(i) Reserves, which are instruments available to the authorities for financing or regulating payments imbalances. The changes in the holdings of such items usually reflect for the most part a response to the aggregate surplus or deficit accruing on account of transactions between residents and foreigners that are undertaken for their own sake, i.e., the so-called autonomous transactions. Alternatively, they may reflect action taken by the authorities to influence the autonomous transactions by intervening in the foreign exchange market to affect the exchange rate for the national currency.

(ii) Direct investment capital. The direct investor seeks to have, on a lasting basis, an effective voice in the management of an enterprise operating outside his own economy. To achieve this position, the investor must almost invariably provide a certain, often substantial amount of the equity capital in the enterprise and may also decide to supply other capital to further its operations. Because of the direct investor's special relationship to the enterprise, his motives in supplying capital will be at least somewhat different from those of other investors and will thus probably cause that capital to show a characteristic behavior.

(iii) Portfolio capital. Investment in long-term bonds and corporate equities, other than the investment of reserves and direct investment, forms a category that is often quantitatively quite large and that may sometimes be sufficiently unlike other capital in its behavior to warrant separate recording.

(iv) Other capital. This residual group comprises a number of different kinds of capital. In practice, however, it would usually not prove feasible to draw any further distinction between the various types along functional lines, as the possible reasons for the flows are too numerous and varied. Other breakdowns are used, therefore, to bring out differences in behavior among components of this category.

(c) *Long-term and short-term capital*

386. The traditional distinction between long-term and short-term capital, based on the formal criterion of original contractual maturity, has been retained in this Manual. Long-term capital is defined as capital with an original contractual maturity of more than one year, or with no stated maturity (e.g., corporate equities). Short-term capital is capital payable on demand or with an original contractual maturity of one year or less and includes currency.

387. The adoption of this criterion does not reflect a presumption that it will serve in a satisfactory way to distinguish short-term movements, i.e., those that are temporary and likely to be reversed in

the short run, from more permanent or less volatile movements. In many instances, original maturity obviously has no necessary bearing on the length of time that an investment will be held, although it does appear to be one factor taken into account by investors in some circumstances, with the result that in practice it may tend to influence the behavior of the capital concerned. In any event, the distinction is one that is widely employed and can be applied mechanically without posing major problems of compilation.

388. Capital assigned to the category of reserves is not divided between long-term and short-term capital. While formal maturity may be one factor tending to differentiate that category from other types of capital, it is not likely to affect the behavior of the various components of the category. Portfolio investment, by definition, consists entirely of long-term capital, since it comprises long-term bonds and corporate equities, the latter being classified as long term because they have no stated maturity.

(d) *Domestic sector*

389. The identity of the domestic creditor or debtor, in terms of its economic sector, is a characteristic of financial items that in some cases influences their behavior. In previous editions of the Manual, especially the third edition, considerable emphasis was placed on classification by domestic sector as a main approach to be followed throughout the capital account. That approach has the advantage of being one that can, at least in theory, be applied objectively to all financial items. Moreover, a sector breakdown is often relevant for analyzing financial relationships within an economy, including the holding by sector of foreign assets.

390. In contrast, the present Manual distinguishes sectors only for the residual category, other capital. Experience has indicated that the domestic sector of the creditor or debtor often has less discernible influence on behavior than have other characteristics that can be identified. Moreover, since several sectors typically need to be distinguished, that approach tends to produce a classification scheme comprised of a great many items, only a few of which are relevant for a given country. In addition, for liabilities the choice between sectoring by debtor or by transactor is a difficult one, because behavior could be related to either characteristic and, whichever basis is chosen, statistical problems are likely to be encountered. For such reasons as these, this Manual does not call for a systematic breakdown of the financial items by sector, although it is recognized that some countries may find it useful to follow that approach in presenting their own statements.

391. Where classification by sector is specified in this Manual, the sector to be identified is that of the domestic creditor for assets and of the domestic debtor for liabilities. Since the creditor is always the owner of the asset, the creditor is invariably one party to any change of ownership of the asset; therefore, for assets sector attribution by creditor and by transactor coincides. A claim on a domestic debtor, however, may change ownership between a domestic creditor and a foreign creditor. Then the domestic sector of the debtor may not coincide with that of the transactor. Nevertheless, the sector of the debtor is the one which is to determine the classification of the change of ownership that has occurred, as the original nature of the liability is generally considered more significant than the identity of the present holder of the claim. For types of liability where the foreign transactors (creditors) may be of particular interest, a further breakdown by sector of foreign transactor could be adopted by the compiling country.

392. In the determination of the domestic sector to which a transaction is to be attributed, guarantees and financial intermediation where the intermediary is not actually the legal creditor or debtor are not to be taken into account. Although these aspects undoubtedly have an influence on the behavior of capital, they seem unlikely to constitute the main motivation of the capital flow in question. That is, while the availability of government credit insurance could be a factor in the extension of a trade credit, the private exporter's decision to undertake the underlying merchandise transaction and arrange the financing for it is presumably a more basic consideration; government-insured trade credits are thus treated like private trade credits rather than like government lending.

(e) *Liabilities constituting foreign authorities' reserves*

393. In the rearrangement of standard components for the purpose of constructing analytic presentations (see Chapter 7), users may wish to group certain liabilities with reserve assets if they consider that those liabilities perform a function similar to reserves in the context of the approach that analysts are following. For example, the fact that a drawing on the reserve position in the Fund is unconditional when balance of payments need is present, while the use of Fund credit is conditioned on the pursuance of policies designed to overcome the problem, is not usually seen as a relevant distinction in measuring the size of the deficit that has been financed by the authorities. Therefore, the use of Fund credit—construed as a liability for the member—is customarily included in analytic presentations with changes in reserve

assets, a practice that has also been followed in setting out the functional category for reserves in this Manual.

394. Relationships between most other liabilities and reserve assets, however, are not nearly so straightforward. For one thing, reserve assets may be viewed as performing more than one function (see Chapter 21), and the liabilities that might be related to them in each of those functions could be somewhat different. Furthermore, the underlying cause of changes in particular liabilities may be impossible to assign with any reasonable degree of assurance. It must be taken for granted that liabilities classified in the category for direct investment capital would never be regarded as constituting a close substitute for reserve assets, but the same does not necessarily hold true for any other type of liability. While the approach to the classification of financial items adopted in this Manual provides for distinguishing several characteristics of liabilities other than those on direct investment (principally, portfolio vs. other investment, original contractual maturity, and sector of domestic debtor), those distinctions generally do not tend to throw much light on the question of whether the liabilities might under some circumstance take on a similarity to reserve assets from a functional standpoint, although the segregation of a domestic sector for deposit money banks could obviously be viewed as a major exception to this generalization.

395. It is not easy to find additional objective criteria that would go any appreciable way toward singling out the liabilities that may be wanted as building blocks for types of analytic presentation that focus on some version of an “overall” balance (see Chapter 7). The solution adopted here is to specify that any liabilities which constitute reserve assets when seen from the side of the creditor are to be shown as separate standard components, even though the compiling country itself (the debtor) may not in fact regard some or any of them as a supplementary means of financing its payments balance or as an offset to its own reserves. Therefore, each type of liability (except in the category for direct investment, which by definition could never constitute reserves) is broken down to show “liabilities constituting foreign authorities’ reserves” as one component.

396. How the behavior of liabilities of this kind is to be interpreted naturally depends on the purpose of the analysis and the factors that brought about the changes recorded in the balance of payments. The figures—along with those for reserves, of course—clearly do not purport to be a satisfactory measure under all circumstances of the means that may have been employed by the authorities to finance a payments imbalance, or thus of the size of that imbalance. Moreover, their interpretation may sometimes be uncertain; for example, a shift

in holdings of claims on deposit money banks in a reserve currency country from a foreign central bank to foreign private deposit money banks may or may not be taken as an indication of strength in the reserve country's own payments position. Nevertheless, changes in the liabilities that are the counterpart of another economy's reserve assets are a very useful element in understanding the global process of reserve creation and destruction.

(f) *Other classifications*

397. The simultaneous and uniform application (where called for) of the first three approaches to classification listed above, together with the sectoring of one functional category and the breaking out of liabilities constituting foreign authorities' reserves, produces a rather large number of individual items, for each of which several characteristics are specified. By grouping and regrouping the items, those characteristics that are of interest in a particular analytic context can be emphasized and the distinctions that are less important can be suppressed. However, sometimes the items can usefully be subdivided further, on a selective basis, to distinguish additional characteristics that may have a bearing on behavior.

398. The following are the main such distinctions that are called for in this Manual.

(i) "Direct investment" is separated into investment in the reporting economy and abroad, and long-term direct investment capital is divided between investment in corporate equities, the reinvestment of earnings, and other long-term capital.

(ii) "Portfolio investment" is split into public sector bonds, other bonds, and corporate equities.

(iii) "Other capital" shows loans separately for most components.

(iv) The liabilities of deposit money banks that constitute foreign authorities' reserves are broken down by currency of denomination.

(v) The individual types of asset that make up reserves are specified in detail.

399. In addition, in the functional category for "reserves," supplementary information is given for each of the individual types on total change in holdings and the counterparts to revaluation changes.

(8) Problems of Measurement

(a) *Calculation of valuation changes*

400. While data on the amounts of certain financial items outstanding on given dates may be readily available in some cases, it would usually

not be possible to estimate very accurately from that information alone the entries required in principle for the balance of payments. The difference between the market value of assets outstanding at the beginning and at the end of a period may include both (i) transactions valued at market value during the period and (ii) valuation changes during the period, including those in assets that may have been acquired or disposed of (or both) during the period. The amount included for transactions must be known separately, however, as either valuation changes must be excluded from a balance of payments statement (see paragraph 24) or, for reserves, they must be entered with their matching counterpart as supplementary information; both treatments require that the amount of the valuation changes be estimated separately from the transactions.

401. The collection of statistics on the valuation element—either to use in deriving entries for transactions from data on changes in amounts outstanding or because of their interest as supplementary information—is very difficult in practice. To compile these figures, it would be necessary to know the amount outstanding at each and every point in time at which a change in the market price occurs, including any such change that resulted from the fluctuation of the exchange rate for the currency in which the asset is denominated relative to the unit of account in which the statement is compiled. Such a direct approach to the measurement of valuation changes would at best be feasible only if changes in market value were very infrequent. This condition clearly does not hold for assets, such as securities, whose market prices fluctuate from day to day or, under a regime of floating exchange rates, for assets not actually denominated in the unit of account. The only possible method to use in the vast majority of cases, therefore, is to collect information on transactions in addition to any figures that may be available on the amounts outstanding. Valuation changes can then be derived from the two separate sets of data as the source of any difference between transactions and changes in level, although allowance must be made for any monetization/demonetization of gold, allocation/cancellation of SDRs, reclassifications, or changes in coverage of the economy or its residents that affect the data for amounts outstanding.

402. Figures for valuation changes that are derived by the method just described pertain to valuation changes in those assets that are owned by the economy during the period in question, not necessarily to the changes that accrue to the economy during that period. In consequence, the figures may include some changes that accrued to the economy in a previous period and omit some that accrue in the given period. Furthermore, since a change may accrue to the account of some entity that has contracted to acquire an asset rather than to its

current owner, the figures pertaining to assets owned by residents may include changes that have accrued to nonresidents, as well as offsets to changes that had accrued to nonresidents in earlier periods. These characteristics inherent in the figures obviously may affect the interpretation to be placed on the valuation changes recorded for a given period, even though any distortion will tend to cancel out over a succession of periods.

403. When total changes (or the valuation element) in holdings of an asset are to be expressed in a unit of account other than the unit of denomination, and when the relationship between the two units has changed during the period, the total changes must be calculated from amounts outstanding that have been expressed in the desired unit of account. They cannot be obtained by conversion of changes derived from amounts outstanding that are expressed in either the original unit of denomination or some other unit of account (unless, of course, the two units have maintained a fixed relationship).

(b) *Liabilities constituting foreign authorities' reserves*

404. One component that is to be shown separately for all kinds of liability (except direct investment capital) refers to liabilities that, from the viewpoint of the foreign creditor, constitute part of its reserve assets (see paragraph 395). Inasmuch as the proper identification of certain assets as reserves is not always a clear-cut matter even for their holders (see Chapter 21), the problem of identification is likely to be even more complicated from the side of the debtor, who presumably has less access to the facts on which judgment is to be made. In many cases, the only practicable procedure will be for the compiler in the debtor country to adopt a rule of thumb.

405. The general considerations to be kept in mind in formulating such a rule are that a foreign creditor will probably classify as reserve assets any liability of the compiling economy (i) that is repayable on demand or in the short run, that is marketable, or that the debtor is in fact prepared to redeem on short notice; (ii) that is repayable in an asset that the debtor would regard as a reserve asset; and (iii) that is owed to a central bank, central government, or other agency of the central authority except a public nonmonetary enterprise.

406. Specifically, one of the following two rules has sometimes been applied. Because the overwhelming majority of monetary assets (i.e., assets that can be used to make payments) owned by the authorities will be reserve assets, the debtor's economy could consider that any monetary liabilities to foreign central authorities were to be classified, in the absence of information to the contrary, as liabilities constituting

reserves. Alternatively, the debtor could decide to classify in that category only its liabilities to foreign monetary authorities if the available evidence suggested that a significant part of other foreign authorities' holdings, say, holdings by public nonmonetary enterprises, represented a type of asset that is not likely to form part of the reserves for the creditor economies.

CHAPTER EIGHTEEN

Direct Investment

407. This chapter elaborates the concept of direct investment and discusses guidelines that can be helpful in drawing the distinction called for in this Manual between direct investment and other types of capital. In the formulation of the recommendations and guidelines contained in this chapter, the findings of the Fund's Survey of Direct Investment: Concepts and Compilation were drawn on heavily. For a description of that Survey, see Appendix E.

(1) Explanation of Concept

408. Direct investment refers to investment that is made to acquire a lasting interest in an enterprise operating in an economy other than that of the investor, the investor's purpose being to have an effective voice in the management of the enterprise. The foreign entity or group of associated entities that makes the investment is termed the direct investor. The unincorporated or incorporated enterprise—a branch or subsidiary, respectively—in which direct investment is made is referred to as a direct investment enterprise.

409. The benefits that direct investors expect to derive from their voice in management are different from those anticipated by portfolio investors having no significant influence over the operations of the enterprises. From the viewpoint of the direct investors, enterprises often represent units in a multinational operation, the overall profitability of which depends on the advantages to be gained by deploying the various resources available to the investors in units located in different economies. Direct investors are thereby in a position to derive benefits in addition to the property income that may accrue on the capital that they invest, e.g., the opportunity to earn management fees or other sorts of income. Such extra benefits are not likely to be realizable in the short run, so that the investors' association with the enterprises can be expected to continue for a considerable period. In contrast, portfolio investors are primarily

concerned about the safety of their capital, the likelihood of an appreciation in its value, and the return that it is bringing them. They will evaluate the prospects separately with respect to each independent unit in which they might invest and may often shift their capital with changes in these prospects.

410. The establishment of a border line that will adequately serve to set direct investment capital apart from other types of capital, which may have many of the same observable characteristics, is sometimes not a simple matter. As the difference basically depends on the motives of the investor, objective criteria will not necessarily enable the balance of payments compiler to make the desired distinction in all instances. Some degree of equity ownership, however, is almost always considered to be associated with an effective voice in the management of an enterprise. At one extreme, foreign-owned branches and other unincorporated enterprises and wholly-owned foreign subsidiaries (incorporated enterprises) are universally regarded as direct investment enterprises. At the other extreme, foreign influence that is not accompanied by at least some ownership of voting stock is rarely, if ever, seen as constituting direct investment.

411. In the greatest number of instances of direct investment, ownership tends to be concentrated in the hands of a single foreign investor or a group of associated investors. The distinction between direct and portfolio investment becomes increasingly difficult to establish as the overall proportion of foreign ownership decreases and as that ownership is dispersed among various owners and among various economies. To obviate the need for a case-by-case examination and to achieve reasonable consistency in applying the concept, many countries rely for evidence of direct investment on the proportion of foreign ownership of the voting stock in an enterprise. Some countries use more than one percentage as a criterion, depending on the degree of dispersion of foreign ownership among foreign investors. These national practices, which have no doubt developed largely out of experience, are currently quite diverse; hence it would not be very helpful to single out any one percentage criterion as the most reasonable standard that could be applied by every country.

412. When foreign ownership is concentrated in the hands of one investor or a group of associates, the percentage chosen as providing evidence of direct investment is typically quite low—frequently ranging from 25 per cent down to 10 per cent. Since the previous edition of the Manual was prepared, the apparent tendency has been toward adopting percentages at the lower end of that range. That tendency

seems to have developed in growing recognition of the fact that—especially for large corporations of the type that are likely to engage in multinational operations—a small, organized group of stockholders may well have an influence in management that is much more than proportionate to its share in the equity capital.

413. Besides some criterion applying to ownership by a single investor or group, a number of countries consider foreign ownership that is widely scattered but substantial in the aggregate to be evidence of direct investment. When diffuse foreign ownership approaches 100 per cent it is usually taken to constitute direct investment, probably on the grounds that no resident owner is present who could have an effective voice in management. As ownership becomes more scattered, so that no single investor or group, either resident or foreign, can be identified as actually being the one most influential in the management or as meeting whatever presumptive criterion is being applied, some countries treat the enterprise as a direct investment enterprise if ownership by unassociated investors in a given foreign country reaches more than one half of the total.

414. Much stress is often laid on the difficulty of defining direct investment precisely and of applying the concept in practice. It may be pointed out, however, that these problems, serious though they may seem, do not necessarily have a corresponding importance for the validity and intercountry comparability of the statistics on direct investment. Most direct investment enterprises, in fact, either are branches or are subsidiaries that are wholly owned by foreigners or in which a clear majority of the voting stock is held by a single foreign investor or group. The real borderline cases are thus likely to form a rather small proportion of the universe. Moreover, since an enterprise is most apt to be inconsistently classified when the share of the investor in question is quite small, the weight of the doubtful cases tends in principle to be further reduced by adherence to the prescription of this Manual that only the direct investor's share in the capital and income flows is to be classified as direct investment (see below).

(2) Direct Investment Capital

415. Once the direct investment enterprise has been identified, the question arises as to which capital flows between that enterprise and entities in other economies could characteristically be expected to show a distinctive pattern of behavior. Since the main feature of direct investment is taken to be the lasting interest of the direct investor in the enterprise, the logical answer must be that it is only the capital

supplied by the direct investor that is relevant in this context. This Manual, therefore, recommends that the category for direct investment capital be confined to capital that is provided by the direct investor—either directly or through other enterprises related to that investor—to the direct investment enterprise (or received by the investor from that enterprise). For the economy where the investment is located, such capital includes funds provided both by the direct investor directly and by other foreign direct investment enterprises of the same direct investor. For the economy of the direct investor, such capital includes only funds provided by the resident investor; it does not include funds for which the direct investor merely makes the arrangements or guarantees repayment, e.g., loans from outside parties to an incorporated direct investment enterprise.

416. A further aspect for consideration is whether all forms of investment by the direct investor should be classified as direct investment capital. The equity capital supplied by the direct investor and the reinvested earnings attributed to him (see paragraph 291) are two types where the direct investment relationship is undoubtedly a primary factor. For other long-term capital and for short-term capital, however, the justifiability of assigning the flows attributable to the direct investor to the category for direct investment can vary widely with the practices of the investors concerned, which may change from one period to another. Moreover, the formal distinction between the long-term and short-term elements of “other” direct investment capital is often found to be misleading. Although all these flows are recorded in this Manual as direct investment, provision is made for distinguishing the main types separately.

417. In previous editions of the Manual, flows of short-term capital between monetary institutions and their direct investment affiliates were allocated to other categories of capital rather than to direct investment, on the grounds that the flows presumably reflect the regular business activities of those institutions more than the direct investment relationship. The same line of reasoning has increasingly become relevant for the nonmonetary sectors also, since short-term investment funds are frequently channeled directly through affiliates instead of through the banking system. Nevertheless, this Manual retains the recommendation of the previous edition that the short-term element should be excluded from direct investment capital only for flows between affiliated monetary institutions.

418. Direct investment capital flows include those that create or dissolve the investment as well as those that serve simply to maintain, expand, or reduce it. Thus, when a foreigner who previously had no equity in an existing resident enterprise takes over the management

interest in that enterprise from a resident, the market value of equity holdings acquired and any other capital invested by the foreigner should be recorded as direct investment. When the acquisition of equity by a foreigner has been gradual, however, the reclassification—from portfolio to direct investment—of shares that were acquired in periods before the take-over occurred should be regarded as a reclassification of the existing investment and should not be shown in the balance of payments (see paragraph 374 (ii)).

(3) Net Recording

419. Direct investment is commonly referred to as an asset for the economy of the direct investor and a liability for the economy in which the direct investment enterprise operates. Actually, the investor and the enterprise may have claims on each other, although the investor could most often be expected to have net foreign claims and the enterprise net foreign liabilities. Any change in the investor's net position that represents a capital transaction should be reflected in the balance of payments. While the gross transactions in assets and liabilities between the two parties that may or may not affect the net position might sometimes be of interest, this Manual provides that capital transactions between the direct investor and the enterprise are to be reported on a net basis.

420. Notwithstanding this provision, a distinction between assets and liabilities in the category for direct investment capital is not sufficient, conceptually at least, to denote whether an entry refers to a resident direct investor or a resident direct investment enterprise, as either can have a net asset or a net liability position vis-à-vis the foreign partner. Thus, separate subcategories are given for investment abroad and investment in the compiling economy, each of them providing for the recording of either net assets or net liabilities.

(4) Valuation

421. The problem of obtaining market values for transactions connected with direct investment deserves special attention. Because the direct investor and the direct investment enterprise are never wholly independent parties, one important condition needed to establish an actual market price for transactions between them is not satisfied. Data derived from the books of either the investor or enterprise may, therefore, reflect prices assigned for transfers among affiliated parties that are not a reasonable equivalent of market prices. As these books cannot be kept in balance without applying a

consistent method of valuation for all items, the use of a transfer price for one item has the consequence that some other item is also valued at a corresponding transfer price. For the capital and income items in isolation, the balance of payments compiler may have great difficulty in deciding whether the values reported actually represent an approximation of market values. If the goods and services entries from a given set of books are in need of adjustment to achieve a market valuation for them, however, it follows that the capital and/or income items will in principle require a matching adjustment (see paragraph 86).

422. The serious problems connected with the determination of the equivalents of market price for transfers among affiliated enterprises are a likely source of asymmetry in the balance of payments statements of the partner countries. Even if transfer prices are accepted in lieu of market price equivalents by the compilers in both countries, the transfer prices at which the affiliated parties in the two countries record the same transactions may very well not be identical, since local regulations and practices can lead to the application of different valuation principles for the books kept in various countries.

CHAPTER NINETEEN

Portfolio Investment

(1) Definition

423. The category for portfolio investment adopted for this Manual covers long-term bonds and corporate equities other than those included in the categories for direct investment and reserves. The definitions of those instruments, which are adapted from the definitions in the United Nations' *A System of National Accounts (SNA)*, are as follows.

(a) *Long-term bonds*

424. Bonds, debentures, etc., that have an original contractual maturity of more than one year are covered here. These securities give the holder an unconditional right to a fixed money income (that is, an income in the form of interest, which is not dependent on the earnings of the debtor), and they are usually issued and traded in organized markets. A bond, with the exception of a perpetual bond, also gives the holder the unconditional right to a stated fixed sum on a specified date or dates. Bonds are considered to include negotiable certificates of deposit, preference shares (except participating preference shares), and marketable promissory notes. Bonds with optional maturity dates, the latest of which is more than one year after issue, are considered to be long term. Mortgages are not classified as bonds.

(b) *Corporate equities, including capital participations*

425. Instruments and records acknowledging claims to the residual value, and residual income, of incorporated enterprises, after the claims of all creditors have been met, are covered here. Ownership of equity is usually evidenced by shares, stocks, participations, or similar documents.

(2) Valuation

426. Transactions in portfolio securities are to be entered at market values; any changes in market value while securities are still in the holder's possession (valuation changes) should be omitted. Transactions in securities generally take place under the conditions necessary to establish an actual market price, e.g., in an organized market, so that the valuation of transactions is not likely to prove very troublesome in practice. The elimination of valuation changes, however, from series derived from amounts outstanding may well present difficulties (see paragraph 401).

(3) Classification

427. The main approaches to classification applied generally throughout the capital account produce only a two-way breakdown—between assets and liabilities—for portfolio investment, as all capital in that category is nominally long term by definition. While the various instruments included in the category could be expected to be rather similar from the standpoint of behavior, the category is sometimes a large one and a further breakdown may help to shed light on the aggregate movements.

428. The primary breakdown that is recommended in this Manual is between public sector bonds, other bonds, and corporate equities. Public sector bonds are defined to comprise all bonds issued by general government, including international organizations, and by publicly owned and/or controlled bodies. In addition, liabilities of each type in this category are subdivided to show separately any that constitute reserves for foreign authorities. Other classifications that are sometimes applied in national statistics include those by sector of the creditor or debtor or of the transactor and those by new issues, retirements, and transactions in outstanding securities. Schemes based on these or other observable characteristics of the investments may well be needed by certain countries for which portfolio investment is important to supplement the breakdown called for in this Manual.

(4) Statistical Problems

429. Statistics on changes in holdings of portfolio investment are usually obtained from one of two main sources. First, data on transactions may be reported by the transactors or their agents (such as banks, security dealers, and brokers) for statistical or exchange control purposes. These data, however, may include amounts for service charges on the transactions; such charges should not be

allocated to the capital account but should be classified in other goods and services (see paragraph 330). Second, information on the amounts outstanding may be shown in security registers, surveys of investment position, and the like. In either case, a main problem is to determine whether the owners of the assets are residents or foreigners, as securities are often held in the name of a nominee rather than that of the principal. Moreover, residents may carry out transactions in foreign markets, and securities originally issued in the domestic market may subsequently be traded in markets abroad; transactions of these sorts may well escape recording. These possibilities give rise to difficulties in recording portfolio investment.

430. When the balance of payments entries are derived as the difference between amounts outstanding on two dates, adjustments for valuation changes between those dates will probably be necessary (see paragraph 400). Book values of asset holdings may reflect current market prices of the securities concerned rather than the prices at which the securities were bought and sold; the latter prices are those required for the balance of payments.

CHAPTER TWENTY

Other Capital

(1) Definition

431. "Other capital" is a residual category, which should thus include all capital transactions that are not covered in the categories for direct investment, portfolio investment, or reserves.

(2) Classification

432. The types of capital included in "other capital" will probably be heterogeneous and vary considerably from country to country. While the breakdown by assets and liabilities and by forms that are nominally long term and short term goes some way toward identifying characteristics that are likely to be of interest, further details are usually wanted. This Manual recommends an additional subdivision of "other capital" by three sectors of domestic creditor or debtor; a separate component for each type of liability to show liabilities that constitute reserves for foreign authorities; and, except for short-term assets and liabilities of deposit money banks, a distinction between loans and other assets or liabilities.

433. The classification of "other capital" is only designed to show a few of the main items that can be expected to be of some significance for a number of countries. It will, therefore, probably not give the amount of detail or designate particular items that may be required for some purposes. The sector classification is a very abbreviated one, for example, and such items as trade credits do not appear separately. Each additional distinction that is applied uniformly throughout this category, however, tends to increase substantially the total number of series to be compiled.

434. The central bank has been included with the general government in a single "official" sector; for a description of the general government and the central bank, see paragraphs 54 and 66,

respectively. Any assets and liabilities of a central bank that are not classified in this Manual as “reserves” or “liabilities constituting foreign authorities’ reserves” are for the most part types that, under the institutional arrangements existing in many countries, would belong in the general government sector anyway. Such items will consist mainly of capital subscriptions to international nonmonetary organizations, especially development finance institutions; payments agreement balances, both current and consolidated; and loans, other than those under inter-central-bank arrangements. The inclusion of the central bank with general government thus should help to improve the intercountry comparability of the various components of the official sector.

435. Deposit money banks refer to all public and private monetary enterprises except the central bank, as defined in paragraph 65. It is important to note that transactions of deposit money banks should often be classified in other categories specified in this Manual, rather than in “other capital.” Thus, these banks may operate in more than one economy, in which case a direct investment relationship exists; they may issue or hold long-term securities, including long-term negotiable certificates of deposit, that constitute portfolio investment; and the foreign exchange held by public banks, and sometimes even that held by private banks, forms a part of the reserve assets of the economy. However, transactions in nominally short-term instruments between deposit money banks that are direct investment affiliates are to be included in “other capital” rather than in “direct investment” (see paragraph 417).

436. Loans refer to direct transactions between a borrower and lender, when the lender either does not receive any security (e.g., a bill, bond, or corporate equity) evidencing the transaction or else receives a nonnegotiable instrument, such as a lien or mortgage created as a surety.

437. Capital other than loans will include, among other things, currency, deposits, and short-term bills and bonds.

(3) Recording of Loans

438. For the components referring to long-term loans, drawings and repayments are to be shown separately rather than as one net entry (see paragraph 377). Specifically, drawings on long-term loans extended by residents are to be shown as debits; repayments on loans of this same type are to be shown as credits. Conversely, drawings on long-term loans received by residents are to be shown as credits and repayments as debits.

CHAPTER TWENTY-ONE

Reserves

(1) Explanation of Concept

439. “Reserves” is singled out as a category because the kind of capital that it is designed to comprise can perform a distinctive and important function in the context of an economy’s international transactions. The category may be described as the monetary gold, special drawing rights (SDRs) in the Fund, reserve position in the Fund, use of Fund credit, and existing claims on nonresidents that are available to the central authorities either to finance payments imbalances directly or to manage the size of such imbalances by intervening to influence the exchange rate for the national currency.

440. The interest attached to reserves is not intended to suggest that they are the only means at the disposal of the central authorities for dealing with imbalances. Those authorities may, among other things, incur or liquidate liabilities in addition to the use of Fund credit; they may encourage other sectors of the economy to engage in foreign borrowing; they may impose controls to forestall disequilibrating capital movements; or they may allow the exchange rate to float freely without intervention. The use or acquisition of reserve assets and Fund credit, therefore, is not necessarily a close measure of the imbalance that may have been of concern to the authorities. The central authorities, moreover, may hold reserves out of motives other than those mentioned above, such as to preserve confidence, to satisfy domestic legal requirements, or to serve as a basis for foreign borrowing. Nevertheless, the international liquidity afforded by countries’ reserves is a key element in the whole process of international adjustment.

441. The difficulty of deciding just what assets are carrying out the function of reserves, differences of opinion about the most appropriate measurement of reserves for various purposes, and the political and policy implications of such matters—these and other reasons inhibited the placing of much emphasis on an explicit category for reserves in

previous editions of the Manual. In spite of problems of that sort, increased concern with the management and deliberate creation of international liquidity makes it undesirable to continue in this Manual to avoid including recommendations on the coverage of reserves. These recommendations, however, should obviously not be interpreted as ruling out the possibility that either the Fund or its members might wish to adopt different indicators of this element of international liquidity for certain purposes.

(2) Coverage of Foreign Exchange Assets

442. Even apart from questions about how reserves as conceived above should be measured to suit various purposes, the financial assets in that group cannot unambiguously be identified in a meaningful way simply through the application of objective criteria. The readily observable characteristics of a claim—legal ownership, original contractual maturity, marketability, currency of denomination, and the like—are not sufficient to establish whether a claim is actually available to the central authorities to use for the indicated purposes. It must be emphasized at the outset, however, that reserves (like the rest of the capital account) always refer to assets that actually exist. Claims that could be created under agreements which are in force—for example, foreign exchange that could be obtained under swap agreements and other lines of credit or through the use of Fund credit under stand-by arrangements—do not constitute existing claims. Conversely, assets that are pledged, committed, earmarked, set aside in sinking funds, blocked, sold forward, or otherwise encumbered by their holder are nonetheless existing assets and are not precluded on those grounds alone from forming part of the reserves.

443. Two types of question arise in identifying reserve assets. First, what assets, in addition to those that they actually own, could be considered as effectively being at the disposal of the central authorities? Second, which of the assets that they control are available for use, should the need to use them eventuate? Decisions on these questions depend partly on an exercise of judgment, and the considerations may be rather evenly balanced in borderline cases.

(a) *Effective control*

444. The aspect of control can be appraised only with reference to the institutional framework in individual economies. In the most restricted sense, the central authorities control absolutely only those assets to which legally they hold title. In the broadest sense, almost any asset owned by a resident of the economy or held in that

economy may ultimately be subject to the control of the authorities by virtue of their authority. Neither of these extreme views can usefully be adopted for the balance of payments. Instead, the concept of reserve assets is intended to encompass those assets over which the central authorities are actually exercising direct and effective control.

445. The test of control is to be applied quite strictly and literally. As a general rule, only foreign claims actually owned by the central authorities would be found to form part of the reserves. For example, any statutory power to acquire assets that is maintained solely on a stand-by basis would not be considered an effective exercise of control, while the potentiality for transferring assets to or from the authorities through a change in monetary policy, thereby inducing private deposit money banks to change their holdings of foreign assets, would be deemed to be too indirect. Nevertheless, ownership is not a necessary condition for control. For instance, private deposit money banks may sometimes be allowed to hold legal title to foreign assets but may be permitted to deal in them only on the terms specified by the authorities or only with their express approval; such assets would still be subject to the authorities' direct and effective control.

446. It is not intended, except possibly in unusual circumstances, that direct and effective control should be construed as extending, as far as the private sector is concerned, beyond the assets owned by monetary institutions. That is, while it could be decided that certain claims on foreigners owned by private deposit money banks were reserve assets, those same claims would cease to be reserves if they were sold by the banks to private residents other than monetary institutions, whatever the institutional arrangements in the economy concerned might be. The authorities should, in principle, be able to provide data on any assets that they could be said to control without actually owning them, as that information appears to be prerequisite to effective control.

(b) Availability for use

447. Whether an asset controlled by the authorities is available to them to use in case of need is dependent on any conditionality that affects it, including as one main aspect its liquidity or marketability. Owned assets that are immediately available, such as gold, SDRs, and reserve positions in the Fund, are the most unconditional form. An approach to defining reserves that is based on degree of conditionality, however, cannot be adopted. For one thing, ranking of all available assets according to conditionality is not a feasible undertaking. Furthermore, even if such a ranking were made, it would still be a

matter of judgment to decide exactly what degree of conditionality must exist before an asset was considered not to be available for use in accordance with the concept of reserves, that is, where the border line between reserve assets and other assets should be drawn if conditionality were adopted as the criterion to be applied.

448. A more promising approach is to consider, in each case, whether there is an expectation, backed by a reasonable degree of assurance, that the conditions could be satisfied if and when the need to use the asset in question were to arise. It can be seen that formal impediments to usability, such as a distant date of nominal maturity for marketable securities, would not necessarily disqualify an asset from being regarded as a reserve asset. The importance of conditionality as a criterion for identifying reserves is also a function of the magnitude of reserve holdings relative to the potential need to use them. If the authorities' holdings of assets exceeded any conceivable amount that might be needed cumulatively in, say, the medium term, such excess holdings would presumably not be ineligible to be counted as reserves solely because of a considerable degree of illiquidity that limited their availability on demand.

(c) Application of concept in specific cases

449. The intended application of the concept of reserves may be clarified by a discussion of some of the borderline cases that are commonly encountered. In some instances, however, the treatment recommended is as much a matter of convenience, convention, or longstanding practice as the result of a clear balance in its favor of the considerations that are relevant from a conceptual standpoint.

450. The central authorities presumably hold or exercise control over foreign assets for one of two reasons: (i) for the purpose of having them available as reserves or (ii) as a concomitant of pursuing some other objective. These reasons are not always mutually exclusive; for example, reserves that are in excess of immediate needs can be invested in World Bank obligations, thus providing development aid. Assets that are held for both reasons are generally to be classified as reserves. In contrast, assets in the form of direct long-term loans for development and other purposes would normally not be reserves, unless there is an expectation that they could be liquidated as required to meet balance of payments needs. Asset balances on payments agreements, to the extent that they are not settled promptly, have much in common with other types of tied loan that the authorities might make to stimulate exports, provide aid, or further

some other aspect of government policy; all payments agreement balances, therefore, have conventionally been excluded from reserve figures. Subscriptions to international nonmonetary organizations, assets redeemable only in inconvertible currencies, and assets whose use is blocked or otherwise effectively restricted by the issuer provide further clear examples of types of asset that are usually not considered to be reserves.

451. Most other foreign assets held by the authorities, however, are likely to be appropriate to the reserves category. Working balances of the government qualify fully as reserve assets, as by definition they are available for immediate use. Committed assets cannot be excluded, since they, like all other reserves, exist to meet needs; it would be illogical to consider that an asset was any less a reserve simply because the specific need for which it was to be used was a foreseeable one. Lending to the Fund that is readily repayable comprises a reserve asset. The transfer of foreign claims by the private deposit money banks to the authorities just prior to certain accounting dates can result in a portion of the assets held by the authorities being committed, in effect, to the reversal of the transfer soon after those dates, whether or not the commitment is a formal one. While such operations undoubtedly distort the reserves figures, the distortion must be interpreted as the result of a seasonal influence, and the omission of such holdings from the reserves could thus be justified only as a seasonal adjustment.

452. Assets created under reciprocal facilities for the temporary exchange of demand claims between two economies (so-called swap arrangements) require special mention. The claims acquired by the economy initiating the exchange are certainly reserves, since the whole purpose of the exchange is to provide the initiating economy with assets that can be used to meet balance of payments needs. The reason for regarding as reserves the reciprocal claims acquired by the partner economy is not as clear cut, but their inclusion with reserves has more often than not proved in practice to be helpful in appraising developments.

453. Assets not actually owned by the authorities will not usually qualify as reserve assets under a strict application of the criteria discussed in paragraph 445. Nevertheless, the possibility that such assets may do so cannot be entirely precluded. Any cases that may arise should be rather readily apparent to the balance of payments compiler; if the authorities can be said to be exercising effective control, assets of that kind will have to be quite distinctive in character. An example would be assets temporarily transferred by the

authorities to the private deposit money banks, with some special inducement (such as an agreement to repurchase them at a price that assured the banks of realizing a profit) to the banks to hold them.

(3) Revaluation of Reserves

454. For want of a better term, all changes in reserve holdings that do not come about through exchanges or unrequited transfers are referred to for convenience in this section as “revaluations.” That term thus comprises not only the changes in the value of holdings resulting from fluctuations in their price (“valuation changes”) but also those changes that are attributable to “reserve creation,” i.e., the monetization/demonetization of gold, the allocation/cancellation of SDRs, and reclassifications.

455. Before the institution of the SDR and the later advent of major currency realignments and widespread floating, revaluation was a phenomenon that was rarely associated with reserve holdings, with the notable exception of the monetization and demonetization of gold. Reserves, in fact, usually were deliberately held in gold or in other forms that were regarded as safe from valuation change. Holdings of monetary gold itself, however, were subject to change through monetization and demonetization. Increases in an economy’s gold reserves because of monetization were recorded in its balance of payments; these increases were offset by a counterpart that was rationalized as equivalent to the export of the gold as a commodity or, at least, the making available of such gold for export. Demonetization was entered as the reverse of that process.

456. The establishment of the SDR as a new reserve asset has brought into prominence a further kind of change that can have an important effect on reserve holdings. The allocation or cancellation of SDRs is an occurrence that can be considered almost identical with the monetization/demonetization of gold in its implications for reserve holdings. Indeed, the allocation of SDRs was originally conceived as an alternative to gold monetization in bringing about an adequate degree of global reserve ease; that is, SDR allocation permits individual economies to register surpluses in their balances of payments without the incurrence of corresponding deficits by other economies—a function that gold ceased to fulfill when new supplies began to be outstripped by nonmonetary demands. Therefore, provision is made in the balance of payments for entering the changes in SDR holdings resulting from allocation or cancellation. The offset, however, could hardly be construed as analogous to a commodity export, so a new category has been set up in the capital account for

the specific purpose of making a place in which that counterpart can be entered.

457. Since the time that SDRs were first allocated at the beginning of 1970, a number of developments have taken place that have made valuation changes in reserve assets an even more common occurrence. These developments include the realignment in December 1971 of par values and the subsequent establishment of central rates for major currencies, including most of those in which reserves are customarily denominated; the announcement of a further devaluation of the U.S. dollar in February 1973; the widespread floating of currencies that began early in 1973; the adoption in mid-1974 of an interim method for valuing the SDR in terms of a basket containing some floating currencies; and the large divergence that evolved between the official price and the private market price for gold, leading to agreement that the official price for gold should be abolished. As a result of developments such as these, together with other possibilities foreseen in connection with the reform of the international monetary system, the various reserve components can now show frequent valuation changes relative to each other. No unit of account can be adopted for balance of payments purposes in terms of which valuation changes in reserve holdings would be likely to be precluded—a consideration that was formerly a main factor in selecting a unit of account in which to express the balance of payments.

458. Previous editions of the Manual in general recommended the exclusion of revaluation changes from the balance of payments. However, as an exception to the rule, monetization/demonetization of gold was included. Later, the allocation or cancellation of SDRs also came to be covered in the balance of payments (for reasons indicated in paragraph 456). In this Manual, the main components in the category for reserves all refer to changes other than revaluation changes in the various types. For each individual type, however, supplementary information is provided on total changes in holdings and on the counterparts to those changes that are the result of revaluation changes. The monetization/demonetization counterpart for gold and the allocation/cancellation counterpart for SDRs are shown separately, but any reclassification counterparts are to be included with those for valuation changes.

459. A balance of payments statement constructed from the standard components, therefore, will approximate the so-called performance basis that is favored in a number of analytic approaches (see Chapter 7). The use of the supplementary information on total changes and revaluation counterparts will permit, in addition, presentations in which all changes in official reserve items are shown and their relationship to the rest of the balance of payments is made evident.

(4) Valuation and Timing

460. Questions of valuation and timing hardly presented themselves in connection with reserves under the regime whereby such holdings were almost entirely in the form of gold, of assets such as the SDR and reserve positions in the Fund the value of which was maintained in terms of gold, and of claims denominated in currencies whose par values bore a fixed relationship to gold. This situation has ceased to exist. However, uncertainties about future developments in the international monetary system, such as the value that will be attributed to monetary gold since the official price has been abolished, make it impossible, at least at this writing, to formulate rules about valuation and timing that would have lasting validity. The problems that can arise under these conditions with respect to valuation are perhaps obvious, but it should also be noted that it may be almost equally important and difficult to decide at what time valuation changes shall be deemed to have occurred.

461. For the Fund's own operational purposes, questions of valuation and timing are handled consistently with the provisions of its Articles of Agreement and with decisions of its Executive Directors. Those procedures are as suitable for constructing the balance of payments entries as any alternatives that can be suggested, but they are subject to adaptation to meet changing circumstances. They cannot be cited here, therefore, as even a temporary standard. Compilers are advised to consult with the authorities in their countries, who are kept currently informed of the Fund's practices, or with the Fund directly on any questions which arise about valuation and timing that affect the recording of reserves in the balance of payments.

(5) Classification

462. Although the individual elements of reserves are largely interchangeable from a functional standpoint, several components are shown that may have somewhat differing implications, especially when the balance of payments is used as background for studies of world liquidity and the adjustment process.

463. For each type of reserve, the change in level of holdings from the beginning to the end of the reporting period is shown as supplementary information. The offset to any portion of that change which is required when the change is not wholly the result of a transaction between two parties is shown as a separate counterpart or, for monetary gold and SDRs, as two separate counterparts. The

“counterpart to valuation changes” refers mainly to changes that have come about from fluctuations in the price of the item. However, any changes that have been produced by reclassifications should also be assigned to the valuation counterpart. Reclassification counterparts are not shown separately, because instances in which the central authorities begin or cease to exercise effective control over a given type of asset are too infrequently encountered in practice to warrant providing a separate item for them. If reclassifications should occur, the amounts should be specified in reporting to the Fund.

(a) *Monetary gold*

464. Monetary gold is gold owned by the authorities (or others subject to their effective control, under institutional arrangements that sometimes exist) that is held as a financial asset. Other gold (nonmonetary gold) owned by any entity, including the authorities that also own monetary gold, is treated in this Manual like any other commodity.

465. Authorities that add to their holdings of monetary gold by acquiring commodity gold, i.e., newly mined gold or existing gold offered on the private market, or that release monetary gold from their holdings for nonmonetary purposes, i.e., for sale to private holders or users, are deemed to have monetized or demonetized the gold, respectively. Any increase in monetary gold holdings that results from monetization is shown as a debit in the item for total changes in gold holdings, offset by a credit in the counterpart item for monetization; any decrease in holdings that results from demonetization is shown as a credit in total changes, offset by a debit in demonetization.

466. The gold that is being monetized (demonetized) may or may not have been acquired from (relinquished to) a nonresident. If a change of ownership between economies has also taken place, that change should be recorded—in addition to the entries required to show the monetization (demonetization)—as an import (export) of merchandise in the current account and as a credit (debit) in the capital account, assuming that a financial item was used (received) to pay for that import (export). It should be noted that the same gold need not have the same value as a financial asset which it has as a commodity.

(b) *Special drawing rights*

467. Changes in the authorities' holdings of SDRs come about either through allocation and cancellation or through transactions in which

SDRs are paid to or received from the Fund, participants in the Special Drawing Account,¹ or other holders. The main kinds of transaction are those in which SDRs and other reserve items are exchanged.

468. An increase in SDR holdings as the result of an allocation, which shows up as a debit in the item for total change in SDR holdings, is offset by a credit in the counterpart item for SDR allocation; the reverse entries would be made in the case of a cancellation.

(c) Asset and liability positions vis-à-vis the Fund

469. A member may have either—or occasionally both—of two positions in relation to the Fund's General Account² that are recorded in the category for "reserves." One position constitutes an asset for the member and is referred to as its reserve position in the Fund, while the other is a liability termed its use of Fund credit.

470. A member's reserve position in the Fund is the sum of the reserve tranche purchases that a member could make and the amount of any indebtedness of the Fund under a loan agreement that is readily repayable to the member. Reserve tranche purchases are purchases that do not cause the Fund's holdings of a member's currency to exceed 100 per cent of its quota; however, the Fund has decided to exclude purchases and holdings under the policy on the use of its resources for compensatory financing of export fluctuations. Under the Second Amendment to the Fund's Articles, purchases and holdings under other policies can also be excluded if the Fund so decides.

471. A member's drawing other than a drawing against its reserve tranche position constitutes the use of Fund credit. A reduction in the Fund's holdings of the member's currency that are in excess of that member's quota minus its reserve tranche position effects a repayment of such use.

472. The accompanying table shows one way in which these two positions vis-à-vis the Fund may be calculated from the amounts outstanding that are shown on balance sheets of the member. A nonmember, by lending to the Fund, may also acquire a reserve position in the Fund.

¹In the Second Amendment to the Articles of Agreement, this is the Special Drawing Rights Department.

²In the Second Amendment to the Articles of Agreement, this is the General Department.

(d) *Foreign exchange and other claims*

473. Foreign exchange and other claims cover assets in the form of claims on nonresidents. Foreign exchange covers the claims that are shown as the “foreign exchange” element of the series for “international liquidity” published by the IMF in *International Financial Statistics (IFS)*. Other claims cover any additional claims that constitute reserve assets, as that concept is described in this Manual. The distinction is made solely to facilitate reconciliation with the *IFS* series for “foreign exchange,” which may omit some claims for various practical reasons. For example, the *IFS* data may not always cover working balances abroad of government nonmonetary agencies, on which it may be difficult to obtain information promptly or at monthly intervals.

Positions in the IMF General Account

	Amount Outstanding at	
	Beginning of period	End of period
1. Subscription payments		
2. Add: Member's lending to the Fund		
3. Deduct: Member's currency held by the Fund		
4. Add: Drawings under compensatory financing policy		
5. Total (1 through 4): Reserve position in the Fund, if positive, or use of Fund credit (excluding drawings under compensatory financing policy), if negative		
6. Add: Drawings (-) under compen- satory financing policy		
7. Total use of Fund credit (5, if negative, plus 6)		

For notes to lines in the table, see p. 158.

Notes to lines in the table on p. 157

1. Subscriptions are equal to a member's quota. A subscription paid in advance of a quota increase does not affect a member's position in the General Account until the date that the increase takes place. Payments in advance, therefore, are not to be included in the balance of payments.

2. A member's lending to the Fund changes not only through new loans made and repayments received on earlier loans but also through the transfer of claims on the Fund from or to other members.

3. In addition to currency with the depository, the Fund's holdings include nonnegotiable, noninterest-bearing demand obligations, payable at face value by a member in its currency.

4. The Fund has adopted a policy on the use of its resources for the compensatory financing of export fluctuations. Drawings under that policy do not figure in the calculation of a member's reserve tranche position and hence of its reserve position in the Fund. Therefore, the amount of a member's currency held by the Fund as the result of such drawings (included in the preceding line) must be eliminated in ascertaining whether the member has a reserve tranche position. In other words, a drawing under the compensatory financing policy is always treated as a use of Fund credit, whether or not the member has a reserve tranche position; in all other cases, the reserve tranche must be fully drawn before a use of Fund credit can take place. Furthermore, a regular reserve tranche drawing can be reclassified in a subsequent period as a drawing under the compensatory financing policy, restoring to that extent the member's reserve position in the Fund.

5. The difference between positive totals on the two dates, or between a positive figure and a nil entry, shows the total change in the reserve position in the Fund during the period. The difference between two negative totals, or between a negative figure and a nil entry, shows the total change in the use of Fund credit other than use under the compensatory financing policy. When the figure is positive at one date and negative at the other, the reserve position in the Fund and the use of Fund credit other than use under the compensatory financing policy have both changed during the period. The amounts of the separate changes are represented by the difference between the positive figure and zero for reserve position in the Fund, and between the negative figure and zero for use of Fund credit. Those amounts are shown separately in the balance of payments, as credit entries when the amount outstanding at the beginning of the period is positive or as debit entries when that amount is negative.

6 and 7. See note to line 4. Any change in a drawing outstanding under the compensatory financing policy is a change in the use of Fund credit over and above any other use that has been calculated from line 5.

APPENDIX A

Regional Balance of Payments Statements

474. The main body of this Manual deals with the compilation of global balance of payments statistics, i.e., figures primarily concerned with the international economic transactions of an economy with the rest of the world as a whole. Similar statistics can also be compiled, however, on a regional or other partial basis, showing an economy's external transactions with some designated group of nonresidents, usually with the residents of a selected foreign economy or group of economies. This Appendix discusses some aspects of that subject. An assemblage of all the partial statements of this sort for a given economy can be viewed in principle, of course, as a breakdown of the global statement for that economy.

475. The topic is assigned to an Appendix because the Fund has not considered it necessary, at least for its own purposes, to make special recommendations about the rules to be followed for partial statements. Compilers, moreover, are likely to find that an attempt to adhere to any standard rules for splitting up the global entries represents a major statistical undertaking. Nonetheless, because international organizations and individual countries may wish to have some standard of reference on the preparation of regional statements, a system that is compatible with the recommendations made in this Manual about the compilation of a global statement is spelled out in the following section.

(1) Suggested Method for Regional Allocation

476. The recommendations in this Manual can be seen, in fact, as applying as much to the preparation of a statement for individual national territories or groups of territories (see section (3), below) as to a global statement. All that is necessary is to substitute a specific reference to the foreign economy under consideration (say, economy A) for each general reference made to nonresidents, foreigners, or the rest of the world. The definition given at the beginning of

Chapter 2, for example, can be adapted to read that the compiling country's *regional* balance of payments *with economy A* is a statement on (a) transactions in goods, services, and income between the compiling economy and economy A, (b) changes of ownership and other changes in the compiling economy's claims on and liabilities to economy A, and (c) unrequited transfers, counterparts, or other entries that are needed to balance any entries for the foregoing transactions and changes which are not mutually offsetting.

477. Consistently with the criterion of change of ownership that largely determines the coverage of the merchandise item (see Chapter 10), merchandise would logically be allocated to the region in which its former owner, for imports, or its new owner, for exports, is a resident. Analogously, service and income items would be attributed to the region whose resident rendered or acquired the service (or received or paid the income). Changes in claims and liabilities would be posted to the region where the foreign debtor or creditor, respectively, is a resident. Finally, an unrequited transfer or counterpart would obviously be appropriate to the same region where the entry that it offset was made.

478. The foregoing manner of regional allocation is not designed to be internally consistent and thus may not produce a balanced statement for a single region. Specifically, a transactor residing in the compiling economy may make payment to or accept payment from a transactor in a foreign economy in the form of a claim on a resident of still another foreign economy; this situation arises when, as frequently happens, claims on a reserve currency country are used by other economies as the medium for making settlements. The inconsistencies stemming from the allocation of transactions in real resources to the region of the foreign owner/transactor and changes in financial items to that of the foreign creditor or debtor, however, are explicitly recognized in presenting a regional statement compiled in that way. Thus, an item is provided for "multilateral settlements" to restore an accounting balance in the regional statement by serving as an offset to the inconsistencies. That item may be seen to represent in concept the settlement of an imbalance in the compiling country's transactions with one foreign region by a transfer to or from that region of claims on or liabilities to some other foreign region or regions.

479. The data needed to compile statistics on multilateral settlements, however, are seldom available. In practice, therefore, the item is usually derived as a residual; however, it can be calculated only in combination with the item for "net errors and omissions," which is also a residual or balancing item. It should be noted that inconsistencies or errors of this or any other kind in classifying entries regionally

obviously could not have any effect on a global presentation. Since a global statement could not be anything but the sum total of all regional statements, it follows that the multilateral settlements appearing in individual regional statements must cancel each other out for all regions taken together.

(2) Drawbacks to Other Methods

480. Procedures for regional allocation of global balance of payments entries other than the one dealt with in the preceding section can readily be conceived. The third edition of the Manual, for instance, prescribed that financial items other than the types customarily used for settlements between economies should be allocated to the region of the foreign party to the transaction rather than to that of the foreign creditor or debtor; a rule of thumb suggests that all foreign assets and liabilities of monetary institutions and all short-term assets and liabilities of the other sectors shall be regarded as the settlement items. Since a primary distinction by sector is not called for in this Manual, that particular procedure might no longer be feasible. Furthermore, the fact that the region of the foreign party is not applicable as a criterion in cases involving changes of ownership either between residents or between foreigners (see paragraph 365) tends to detract considerably from any appeal that this approach might have.

481. For real resources, criteria of allocation other than the residence of the owner/transactor can likewise be devised. It might be considered more practical, for example, to base the merchandise item on trade statistics showing, say, the foreign country to or from which the goods are shipped instead of the one in which their new or former owner resides. If that approach is adopted and merchandise is allocated in a regional statement to the country of shipment, while the corresponding changes in financial items are allocated to the economy of the creditor or debtor, the resulting inconsistency no longer represents exclusively multilateral settlements, as that concept is described in paragraph 478. Indeed, the discrepancy does not even have any clear analytic interpretation that can be placed on it. The third edition of the Manual thus suggested, in effect, that any inconsistencies which were not actually the result of multilateral settlements should be offset by what it referred to as "regional adjustments." Adjustments of that kind are all intended to reallocate to the region of the foreign owner/transactor any entries that are originally ascribed to some other region, other than entries for financial settlement items that are intentionally attributed on a creditor/debtor basis. The purpose of that

reallocation is to make the final discrepancy in each regional statement represent nothing but multilateral settlements, as such settlements appear to be the only form of entry stemming from inconsistency that is of possible interest in its own right.

482. While the justification for regional adjustments is clear, it is rarely possible as a practical matter to carry them out. A more realistic and straightforward procedure for regional allocation, therefore, may be simply to adopt, as the stated objective, the method suggested in the preceding section and to accept that any imbalance which actually shows up in a regional statement is likely to be a combination of multilateral settlements, regional adjustments (equivalent under this approach simply to misallocations), and other net errors and omissions.

(3) Selection of Regions

483. Regional statements generally refer to a classification of entries according to the residence of a foreign economic entity that has something to do with the entry being recorded, usually because the entity is either the owner/transactor or the creditor/debtor. Generally, the rules on residence given in this Manual (see Chapter 3) would presumably be applicable for determining the residence of that entity. A region would then comprise a national territory or a group of national territories, as the residence of any entity is based on its association with a specific territory. The methods of allocation discussed above are concerned principally with a regional classification of that sort. A "regional" statement, however, is sometimes conceived in other ways. A statement may be prepared that shows, for example, those transactions which were originally denominated in a certain currency or which were undertaken with the "residents" of a particular currency area rather than a national territory. Because a region is mainly thought of as being a geographic concept, statements of these latter types might more accurately be termed "bilateral" statements rather than regional statements.

484. When a method of allocation is adopted whereby financial items, or at least those used for settlements, are attributed to the region of the creditor or debtor, special provision must be made for the entries pertaining to assets that are not in fact claims, specifically, monetary gold and SDRs. Changes in those items, even when a change of ownership is involved, must in principle be regarded as unallocable, although such a category, of course, need not be shown separately but could if desired be included by definition with some region. It may also be recalled (see paragraph 57) that international organizations are not residents of any national territory. Transactions

with those organizations, therefore, must be shown in a region of their own, unless they are purposely combined with one of the other regions for which a statement is being prepared.

485. The regional breakdown that will be relevant for any economy depends primarily on the use to which the statement is to be put. Neither this Manual nor the Fund's requests for balance of payments data contain a standard list of countries or regions for which the reporting economy should compile separate statements.

APPENDIX B

Compilation of “Merchandise”

(1) Introduction

486. Data on merchandise are unlikely to be collected in exactly the way required to fit the definition of this Manual. Instead, national balance of payments compilers generally derive such data by making conceptual adjustments to statistics that are being collected for other purposes, e.g., trade returns and exchange record statistics. As an aid to such adjustment procedures, this Appendix outlines the adjustments that need to be made to the trade and exchange record statistics in terms of the conceptual differences between the merchandise item and each of the following:

(a) trade statistics defined as to coverage, valuation, and timing in accordance with the concepts and definitions of the United Nations;¹

(b) trade statistics defined as to valuation in accordance with the definitions of the Customs Cooperation Council;²

(c) trade statistics defined to cover all movements of goods across the border of the reporting country; and

(d) exchange record statistics defined to cover all merchandise transactions at the time of settlement through the banking system.

487. It is recognized, however, that the trade and exchange record statistics that are available to balance of payments compilers may not conform entirely to any of the above definitions, and the procedure adopted in this Appendix should not be interpreted to imply that compilers should first adjust their own data to one of the definitions referred to and thereafter adjust them further for use in the balance of payments. Instead, the adjustments indicated here should be applied only insofar as the basic statistics already conform to one of the definitions and for that reason are at variance with the balance of

¹United Nations, *International Trade Statistics: Concepts and Definitions*, Statistical Papers, Series M, No. 52 (New York, 1970).

²Customs Cooperation Council, *Explanatory Notes to the Brussels Definition of Value* (Brussels, 1971).

payments definition; other discrepancies between these basic statistics and the merchandise item can be eliminated directly. Inasmuch as the international standards referred to under (a) and (b) of paragraph 486 do not greatly differ from the merchandise item, they are of considerable value in providing a much more detailed description and discussion of that item than is given in this Manual. However, those standards do not replace or modify in any respect the definition of the merchandise item given in paragraph 213.

(2) International Standards for Trade Statistics

488. Trade statistics are defined by the United Nations¹ as covering, with certain exceptions, "goods which add to or subtract from the stock of material resources in a country as a result of their movement into or out of the country." Imports are recorded at their value at "the frontier of the country of import (including unloading charges at the frontier, if any)" and exports at their value "free on board or free on rail or road vehicles at the frontier of the country of export."

489. The definition of the customs valuation for imports developed by the Customs Cooperation Council² (which would also be applicable for the most part to exports) suggests that:

For the purposes of levying ad valorem duties of customs, the value of any goods imported for home use shall be taken to be the normal price, that is to say, the price which they would fetch at the time when the duty becomes payable on a sale in the open market between a buyer and seller independent of each other.

The normal price of any imported goods shall be determined on the following assumptions:

(a) that the goods are delivered to the buyer at the port or place of introduction into the country of importation;

(b) that the seller bears all costs, charges, and expenses incidental to the sale and to the delivery of the goods at the port or place of introduction which are hence included in the same price;

(c) that the buyer bears any duties or taxes applicable in the country of importation, which are hence not included in the normal price.

A sale in the open market between a buyer and seller independent of each other presupposes:

(a) that the price is the sole consideration;

(b) that the price is not influenced by any commercial, financial, or other relationship, whether by contract or otherwise, between the seller or any person associated in business with him and the

buyer or any person associated in business with him other than the relationship created by the sale itself;

(c) that no part of the proceeds of any subsequent resale, other disposal, or use of the goods will accrue either directly or indirectly to the seller or any person associated in business with him.

Two persons shall be deemed to be associated in business with one another if, whether directly or indirectly, either of them has any interest in the business or property of the other, or both have a common interest in any business or property, or some third person has an interest in the business or property of both of them.

When the goods to be valued

(a) are manufactured in accordance with any patented invention or are goods to which any protected design has been applied; or

(b) are imported under a foreign trade mark; or

(c) are imported for sale, other disposal, or use under a foreign trade mark,

the normal price shall be determined on the assumption that it includes the value of the right to use the patent, design, or trade mark in respect of the goods.

(3) Types of Adjustment for Conceptual Discrepancies

490. The statistics in the basic sources may differ from the standard for the merchandise item in the balance of payments with respect to coverage, classification, timing, and valuation. The basic statistics may thus require adjustments for any or all of these conceptual differences when they are used for the balance of payments.

491. Coverage adjustments refer to conceptual discrepancies between the merchandise item and the basic data sources arising from the fact that certain goods change ownership (or are construed to change ownership) without being recorded in the basic data, while others are recorded in the basic data without changing ownership. Trade statistics are usually defined in terms of border crossings of goods; therefore, additions to trade statistics have to be made for goods that change ownership (or are construed to change ownership) without crossing a border, and deductions have to be made for goods that cross a border without changing ownership. Exchange record statistics are usually defined in terms of payments with a financial item through the banking system. Therefore, additions to exchange record statistics have to be made for goods that change ownership without payment through the banking system.

492. Classification adjustments refer to conceptual discrepancies between the merchandise item and the basic sources arising from the

recording in those sources of goods that are classified in the balance of payments in an item other than merchandise. In particular, trade statistics for imports need to be adjusted for freight and insurance services beyond the customs frontier of the exporting economy, which are not classified as merchandise in the balance of payments. Similarly, in exchange records, payments for freight and insurance services beyond the customs frontier of the exporting economy often are not distinguished from those for merchandise, and deductions need to be made for any payments for such services.

493. Timing adjustments refer to conceptual discrepancies between the merchandise item and the basic sources arising when goods are recorded in the latter at a time different from that when the change of ownership takes place. Trade statistics are defined in terms of border crossings of goods, so that adjustments are needed for balance of payments purposes when the change of ownership takes place in a period other than that in which the goods cross the frontier of the economy providing or acquiring them. Exchange record statistics are defined in terms of payment with a financial item that passes through the banking system, so that adjustments are needed when the change of ownership takes place in a period other than that in which the payments are made.

494. Valuation adjustments refer to conceptual discrepancies between the merchandise item and the basic sources that arise when goods are recorded in those sources at a value other than the market value. Thus, when customs import (and export) statistics are defined in terms of the value of the goods for the purpose of levying customs duties, adjustments have to be made to the trade statistics for any difference between that value and the market value of the same goods.

(4) Coverage Adjustments

(a) *Coverage adjustments to trade statistics compiled as suggested in International Trade Statistics: Concepts and Definitions*

495. On the one hand, merchandise imports or exports not covered in the main body of trade statistics and therefore to be *added* to those statistics are the following:

- (i) Goods acquired from abroad by offshore installations operating in the economy.
- (ii) Goods purchased from one foreign economy by the compiling economy's government for its own use in another foreign economy's territory.
- (iii) Migrants' effects, including those transferred across the border.

(iv) Fishing vessels and gas and oil drilling rigs that begin or cease to be operated by a resident enterprise without entering or leaving, respectively, the territory of the economy.

(v) Other goods acquired from abroad but not brought into the owner's territory except those goods that are for resale to another economy during the same reporting period in which they are acquired.

(vi) Goods lost or destroyed after having been delivered but before crossing the frontier. (Goods lost or destroyed inside the frontier of the exporting economy are not recorded in either the exporting or the importing economy's trade statistics, and an adjustment should be made to the statistics of both economies if that loss or destruction has taken place after delivery. Goods lost or destroyed between the frontiers of the exporting and importing economies are recorded in the exporting economy's trade statistics but not in those of the importing economy, and an adjustment should be made to the statistics of the importing economy if that loss or destruction has taken place after delivery.)

(vii) Goods salvaged and fish and other marine products caught by domestic vessels and sold abroad or to foreign vessels, and vice versa.

(viii) Commodity gold (i.e., nonmonetary gold).

(ix) Goods shipped under financial leasing arrangements.

496. On the other hand, goods to be *eliminated* from the main body of trade statistics are the following:

(i) Returned exports and imports.

(ii) Goods lost or destroyed after having crossed the frontier but before having been delivered. (Goods lost or destroyed inside the frontier of the importing economy are recorded in both the exporting and the importing economies' trade statistics, and an adjustment should be made to the statistics of both economies if that loss or destruction has taken place before delivery. Goods lost or destroyed between the frontiers of the exporting and importing economies are recorded in the exporting economy's trade statistics but not in those of the importing economy, and an adjustment should be made to the statistics of the exporting economy if that loss or destruction has taken place before delivery.)

(iii) Goods shipped without a change of ownership for processing and re-export. (Goods for processing and re-export are generally recorded in the trade statistics both before and after processing takes place; thus, adjustments to the statistics for both exports and imports are needed for balance of payments purposes in the processing

economy as well as in the economy that sent the goods for processing and received them back after processing.)

(b) *Coverage adjustments to trade statistics defined to cover all movements of goods across border of reporting country*

497. On the one hand, merchandise imports or exports not covered in trade statistics defined to cover all movements of goods across the border, and therefore to be *added* to the statistics for balance of payments purposes, are those specified in paragraph 495, items (i) through (vii), inclusive.

498. On the other hand, goods to be *eliminated* from trade statistics defined to cover all movements of goods across the border are the following:

- (i) Returned exports and imports.
- (ii) Direct transit trade.
- (iii) Shipments by residents to military, diplomatic, and other government establishments and personnel of their own government located outside the national territory.
- (iv) Shipments by residents to offshore installations operating in the economy.
- (v) Goods shipped for rental or nonfinancial leasing.
- (vi) Goods lost or destroyed after having crossed the national frontier but before having been delivered (see also paragraph 496(ii)).
- (vii) Goods shipped without a change of ownership for processing and re-export (see also paragraph 496(iii)).
- (viii) Goods shipped without a change of ownership for improvement, repair, storage, labeling, packaging, sorting, inspection, and the like.
- (ix) Goods temporarily exported or imported and not for sale (e.g., display equipment for trade fairs and exhibitions; art exhibits; animals for breeding, show, or racing; and stage and circus equipment).
- (x) Samples of no commercial value.
- (xi) Returnable containers.
- (xii) Carriers engaged in transporting goods or passengers solely between countries.
- (xiii) Mobile equipment, such as carriers, fishing vessels, and gas and oil drilling rigs, that enters or leaves the territory for less than one year.
- (xiv) Goods salvaged and fish and other marine products caught by domestic vessels and landed in national ports.

(c) *Coverage adjustments to exchange record statistics defined to cover all merchandise transactions settled through banking system*

499. On the one hand, merchandise imports and exports not covered in exchange record statistics defined to cover all merchandise transactions settled through the banking system, and therefore to be added to those statistics for balance of payments purposes, are the following:

- (i) Gifts and grants of goods.
- (ii) Barter trade.
- (iii) Shipments between affiliated enterprises not settled through the banking system.
- (iv) Goods paid for out of the proceeds of loans raised abroad and not repatriated.
- (v) Goods paid for with other financial assets held abroad.

500. On the other hand, goods to be *eliminated* from exchange record statistics defined to cover all merchandise transactions settled through the banking system are goods acquired from abroad but resold during the same reporting period without crossing the frontier.

(5) Classification Adjustments

(a) *Classification adjustments to trade statistics compiled as suggested in International Trade Statistics: Concepts and Definitions*

501. Services to be *eliminated* from the main body of import statistics and to be recorded in the balance of payments in "shipment" are freight, insurance, and other distributive services (except agents' fees) rendered between the frontiers of the exporting and importing countries.

(b) *Classification adjustments to trade statistics defined to cover all movements of goods across border of reporting country*

502. Goods to be *eliminated* from trade statistics defined to cover all movements of goods across the border, and to be recorded in the balance of payments in items other than merchandise, are the following:

- (i) Stores and fuel for carriers.
- (ii) Goods acquired for their own use by travelers.

(iii) Newspapers and periodicals sent under direct subscription (not in bulk).

(iv) Securities issued.

(v) Paper money and coin in current circulation.

(vi) Monetary gold.

(c) *Classification adjustments to exchange record statistics defined to cover all merchandise transactions settled through banking system*

503. Services to be *eliminated* from these statistics and to be recorded in the balance of payments in "shipment" are freight, insurance, and other distributive services (except agents' fees) rendered beyond the customs frontier of the exporting country.

(6) Timing Adjustments

(a) *Timing adjustments to trade statistics compiled as suggested in International Trade Statistics: Concepts and Definitions*

504. Merchandise imports and exports not covered in the trade statistics for the relevant period, and therefore to be *added* to those statistics, are goods that change ownership during the reporting period but that cross the frontier either in an earlier period or in a later one.

505. Goods to be *eliminated* from the statistics are goods that cross the frontier during the reporting period but that change ownership either in an earlier period or in a later one. For goods on consignment, however, it would usually be more convenient, and have little practical effect on the figures, if the goods were recorded instead at the time when they cross the frontier, in the expectation that a change of ownership would shortly occur or on the assumption that a change had already occurred.

506. The adjustments that are needed in principle are summarized in the following matrix (the total of each of the four pairs of consecutive lines of individual adjustments that need to be made to the basic data is equal to the net changes in stocks that the adjustments represent):

Table B2. Timing Adjustments Applicable to Economies
Using Exchange Record Statistics for
Balance of Payments Purposes

Data	Period of		Adjustment to			Change in Trade Credits
	Change of ownership	Payment	Assets	Merchan- dise	Liabilities	
Change in trade credits received on:						
1. exports	later	current		deduction	addition	increase
2. exports	current	earlier		addition	deduction	decrease
Net change (1 plus 2)						
3. imports	current	later		addition	addition	increase
4. imports	earlier	current		deduction	deduction	decrease
Net change (3 plus 4)						
Net change (1 through 4)						
Change in trade credits extended on:						
5. exports	current	later	addition	addition		increase
6. exports	earlier	current	deduction	deduction		decrease
Net change (5 plus 6)						
7. imports	later	current	addition	deduction		increase
8. imports	current	earlier	deduction	addition		decrease
Net change (7 plus 8)						
Net change (5 through 8)						

513. Table B2 not only pertains to the additions and deductions that have to be made to the exchange record data for compiling exports and imports in the reporting period in question, but it also gives the adjustments that have to be made to the exchange records for compiling movements in trade credits in that period. Such adjustments follow from, and serve as an offset to, the timing adjustments that are made for compiling exports and imports.

(7) Valuation Adjustments

(a) *Valuation adjustments to trade statistics compiled as suggested in International Trade Statistics: Concepts and Definitions*

514. Adjustments have to be made for fees payable to consulates of the importing country. As the standard for international trade statistics

suggests that consular fees are to be included in the value of merchandise exports and imports f.o.b. the frontier of the exporting country, but this Manual provides that such fees are not to be included in that value, an adjustment to the value of merchandise in the trade statistics is necessary for balance of payments purposes.

(b) *Valuation adjustments to trade statistics defined as to valuation in terms of definition of Customs Cooperation Council*

515. Adjustments have to be made to the statistics for the following:

(i) The difference between the market price at which the goods have been sold as stipulated in the contract and the price at which the import duty on the goods is assessed (see also paragraph 489). (For balance of payments purposes, goods should be recorded at the price for which they have been sold under the contract. Since the customs valuation of the goods is also generally based on the purchase/sale contract price for bona fide sales, in most cases no adjustment on this account will be needed. In a period of abnormal price fluctuations or when there is an unusually long delay between the purchase/sale contract date and the time when the duty becomes payable, however, customs valuation may be based on the price that the goods would fetch at the time when the duty becomes payable. In these circumstances, a price change between the conclusion of the purchase/sale contract and the time when the duty becomes payable may lead to a customs valuation that is inappropriate for the balance of payments. Significant differences may result, for example, if goods are stored for some time in a bonded warehouse. Then an adjustment to the value of the goods recorded in the import statistics is necessary for balance of payments purposes.)

(ii) Special quantity discounts. (Occasionally, one single purchase/sale contract may cover goods that are destined for import into more than one economy, for example, when the buyer is a multinational enterprise that has the goods delivered to several of its branches. Under such a contract, the quantity discount that the buyer receives may be larger than the quantity discount that he would have received if he had made his purchase in installments—a separate contract for each economy to which the goods are delivered. The Customs Cooperation Council recommends that, in such a situation, the customs statistics should reflect the price which the goods would have fetched if the special quantity discount had not been available, i.e., that the price for which the goods were sold should be adjusted upward to eliminate the special discount. The balance of payments item for imports, however, should reflect the price for which the goods were actually sold. Any adjustment by customs to the value of

imports for the purpose of eliminating such a special quantity discount received by the importer, therefore, should be excluded in recording the transaction in the balance of payments.)

(c) *Valuation adjustments to trade statistics defined to cover all movements of goods across border of reporting country*

516. These statistics have not been defined in terms of valuation. Therefore, valuation adjustments cannot be specified, although they certainly may be necessary.

(d) *Valuation adjustments to exchange record statistics defined to cover all merchandise transactions settled through banking system*

517. By definition, no valuation adjustments are needed.

APPENDIX C

Comparison of Balance of Payments Classification with External Transactions in *SNA*

518. The principles applied in compiling the balance of payments are broadly the same as those governing the construction of the external segment of the national accounts. This aspect of the correspondence between the two systems is discussed in terms of coverage, valuation, timing, and accounting convention in Chapter 2 of the Manual. Despite the similarities in approach, however, differences between the balance of payments and the rest-of-the-world account of the United Nation's *A System of National Accounts (SNA)* arise for the main reason alluded to in that chapter, namely, because of the differing classification schemes adopted in each of the two systems. This Appendix addresses itself, therefore, to the subject of how the results produced by the two classification schemes are to be compared.

519. The classification of the rest-of-the-world account used in the *SNA* is designed to serve the needs of economic analysis in such fields as overall economic planning and policy formulation, input-output, production functions, factor shares, consumer demand, distribution and redistribution of income, and flow of funds. These subjects are likely to be of secondary interest in the context of balance of payments analysis, which is usually concerned with identifying imbalances between the domestic economy and the rest of the world and tracing the effects of those imbalances and their financing on international economic relationships and the adjustment process. The items into which the changes shown in the balance of payments are grouped, therefore, differ considerably from the classification of the same changes that is used in the *SNA*.

520. Despite this difference in emphasis, the distinguishing of a major aggregate termed "net lending to the rest of the world" in the national accounts, which is matched in the rest-of-the-world account by "net acquisition of financial assets," is closely paralleled by the division between nonfinancial items and financial items, respectively, that appears in the balance of payments. However, "net lending" in

the national accounts classification (a) includes the counterpart for the monetization/demonetization of gold; (b) excludes purchases and sales of any gold, in addition to monetary gold, that is deemed to be held as a financial asset; (c) includes the capital gains and losses on arbitrage transactions in financial items; (d) includes the write-off of bad debts; (e) includes the net purchases of nonfinancial intangible assets; (f) excludes the market value of the goods shipped under financial leasing arrangements but includes the rental fees earned under such arrangements; (g) excludes earnings reinvested in direct investment enterprises; and (h) excludes shipments of commodities between a parent enterprise and its subsidiary that do not involve a change of ownership. In the balance of payments, (a) the counterpart for the monetization/demonetization of gold is shown in the capital account; (b) all purchases and sales of gold not classified as monetary gold are included in the merchandise item; (c) capital gains and losses on arbitrage transactions in financial items are included in the capital account; (d) the write-off of bad debts is treated as a valuation change and therefore excluded from the statement; (e) net purchases of nonfinancial intangible assets are included in the capital account; (f) the full market value of goods shipped under financial leasing arrangements is included in the merchandise item and balanced by entries in the capital account; (g) the direct investors' share of reinvested earnings is shown as investment income and is balanced by entries in the capital account; and (h) shipments of commodities between a parent enterprise and its subsidiary without a change of ownership are included with merchandise except in certain specified cases.

521. While the foregoing constitute the main explicit differences between "net lending" in the *SNA* and the net balance on "current account" in the balance of payments, additional differences might possibly be inferable, depending on the interpretation given to certain rules of one system or the other. For example, an unequivocal statement cannot be made about whether the "adjustment to change-of-ownership basis" in the *SNA* is applicable to a change of ownership by imputation, such as occurs under that system when goods are sent abroad on consignment; if it is not applicable, a difference with the balance of payments exists in that respect.

522. "Net lending" in the national accounts is further broken down into three main groups (which could be designated as exports and imports of goods and services, other current receipts and disbursements, and other net lending, although only the first actually bears that label) that have no real analogues in the classification adopted for the nonfinancial items in the balance of payments, as they would

require distinctions that cannot readily be made within the framework chosen as most appropriate for balance of payments classification. Thus, for example, the expenditures that are seen from a balance of payments standpoint as "travel" are viewed in the national accounts either as "direct purchases abroad by households," as "other commodities" (reimbursable outlays of commercial travelers), as "direct purchases abroad, government services" (reimbursable outlays of official travelers), or even as "other current transfers" (airport taxes). In the balance of payments, the nonfinancial items are differentiated or grouped mainly according to functional categories, whereas in the national accounts the emphasis is on the distinction between transactions that are appropriate to the production accounts and those that are appropriate to the income and outlay accounts, to conform with the articulated accounting framework of the *SNA*.

523. The suggestion is often heard that technicians concerned with national accounts and balance of payments statistics would find it helpful to have available a detailed comparison of the two systems. The Fund staff has been in sympathy with this idea and did in fact attempt to construct such a comparison to form part of this Appendix. The project, however, could never be satisfactorily carried to completion. The amount of detail involved in a reconciliation of this sort proved to be so great that its intricacies became obviously impossible for even the most interested reader to follow. Moreover, such an exercise could never hope to be exhaustive. Detailed as the Manual and the *SNA* are, they still are less than clear or are entirely silent on many fine points that are judged to be of little practical interest. Questions in these areas are thus left to be settled on a case-by-case basis if and when they arise, with the result that a comparison in the abstract of the two systems soon runs into difficulty of interpretation on this score. Finally, experience over the years has been that one or the other system is often in the process of revision, so that a comparison rather quickly becomes outdated; the *SNA* is undergoing revision at the present writing. In short, the achievable results have seemed likely to be of little practical value, as well as being unsatisfactory from a purely theoretical standpoint. Users of the Manual who may have specific questions about congruity are invited, of course, to consult with the Fund staff.

524. The problems of comparison created by the use of groupings in the national accounts that cut across items deemed useful for balance of payments analysis are, if anything, even more complicated with respect to the classification of financial assets in the two systems. For example, the classification scheme of the capital account of the external transactions account of the *SNA* relates to the different types

of financial item, i.e., gold, currency and transferable deposits, bills and bonds, corporate equity securities, etc. In the balance of payments, however, the primary distinctions, in addition to that between assets and liabilities, are in terms of function and maturity. Thus, it is virtually impossible, from a technical standpoint, to transform the capital account from one system to the other in a meaningful fashion.

APPENDIX D

Survey on Recording of Merchandise Transactions in Balance of Payments

(1) Introduction

525. During the preliminary stage in preparing this Manual, balance of payments compilers suggested that it would be helpful to know more about national practices and preferences in the statistical treatment of merchandise transactions. A questionnaire, therefore, was sent to all Fund members. This Appendix summarizes replies from the 75 countries that responded to the survey; those countries accounted for about three fourths of world trade in 1973.

526. The survey's two principal objectives were to obtain information about the physical point of valuation of merchandise and the most common methods of valuation (or pricing). In addition, respondents were asked for details of their primary source of international trade data and for the relationship between the merchandise and freight items in their balance of payments statements.

527. Prior to a report on the outcome of the survey, a brief comment seems necessary on some difficulties that arose in interpreting the replies. To make it easier to summarize the replies, the questionnaire required respondents to choose from a short list of possible answers to each question. This list, however, did not always cover every conceivable possibility, and the answers provided sometimes proved to be not adequately defined or not mutually exclusive; some imprecision may thus have been introduced in the responses, as noted below. Apart from difficulties of interpretation arising from the form of the questionnaire, generalization about the results is also complicated by the great difference in size of the countries that responded.

528. The problem of multiple responses was handled by including each response in the survey results as though it were a separate answer, a procedure that did not greatly alter the results. The more important problem of disparate economic size has been dealt with by

analyzing both the unweighted answers and answers weighted by Fund quotas, noting instances where the practice of a majority of all countries differed markedly from the practice of a number of the large countries.

(2) Survey Results

(a) Physical point of valuation of merchandise

529. The questionnaire included questions concerning the physical point of valuation of merchandise, i.e., the line drawn between the distributive services to be considered as part of the merchandise item and those to be classified in other items. Respondents were requested to indicate the valuation point called for in basic source documents and known variations in actual reporting. They were also asked whether source documents were adjusted to change, or correct, the physical point of valuation for deriving balance of payments statements. Finally, countries were invited to indicate both the physical point of valuation that minimized their data availability problems and the one that they preferred as an international standard.

530. Six different physical valuation points were explicitly listed as possible answers: f.o.b. at establishment of exporter; f.o.b. at national border of exporting country; f.o.b. at customs frontier of exporting country; c.i.f. at establishment of importer; c.i.f. at national border of importing country; and c.i.f. at customs frontier of importing country. While these points covered the bulk of possibilities for most countries, compilers in some countries may have had difficulty in fitting their answers to the specific choices on the list. For example, countries valuing part, or all, of their trade transactions on a free-alongside-ship basis or a cost-and-freight basis would not have found the list exhaustive. This problem may have led some respondents to select answers from among those given that did not actually coincide with the valuation point used or desired. Therefore, caution must be exercised in interpreting replies about the physical point of valuation of merchandise trade, particularly those relating to imports recorded on an f.o.b. basis (which appeared to present the most difficulty).

531. Country preferences and practices regarding the physical point of valuation for exports, in sharp contrast to those for imports (discussed below), clearly indicated almost unanimous support for valuing exports on an f.o.b. basis. Practically all respondents felt that this concept both was superior to the c.i.f. alternatives and presented fewer data collection difficulties. Accordingly, virtually all exports of the responding countries were collected from source documents requesting f.o.b. valuations. A strong preference for applying the

f.o.b. concept at the customs frontier was also apparent; almost two thirds of the respondents not only used that physical point for valuing exports but indicated that it constituted their conceptual ideal and the point for which data were most readily available. Most of the remaining countries considered that f.o.b. the national border of the exporting country constituted the best international standard and generally collected their export statistics on that basis. Virtually no significant discrepancies were noted between the valuation basis requested in source documents and that actually reported, and few countries felt compelled to correct or adjust data in source documents to conform more closely to the physical point of valuation required for their balance of payments statistics.

532. Weighting responses by Fund quotas did not significantly change the broad picture. About 60 per cent of the weighted answers indicated that exports were valued f.o.b. the customs frontier of the exporting country, while another one third suggested that exports were valued f.o.b. at the national border of the exporting country. An interesting finding is that, although about one fifth of the weighted responses expressed a conceptual preference for valuing exports f.o.b. at the establishment of the exporter, very few countries actually requested valuation on this basis; apparently conceding that there would be additional collection difficulties, most proponents of this concept tended to request data valued f.o.b. at the national border of the exporting country.

533. Any consensus regarding the appropriate conceptual point for valuing imports proved difficult to discern, since the practices reported varied widely. Although some 75 per cent of the reporting countries indicated that they used source documents requesting c.i.f. import valuations, predominantly at the customs frontier, the weighted responses indicated that source documents were evenly divided between import valuations on a c.i.f. and on an f.o.b. basis. Furthermore, about two thirds of the weighted replies preferred the f.o.b. concept as an international standard. Source documents calling for valuation on a c.i.f. basis most commonly requested data valued at the national border of the importing country, but a substantial proportion asked for valuation at the customs frontier of that country. Most of the imports reported on source documents requesting f.o.b. valuations were based on value at the establishment of the exporter, but a good number were recorded on documents calling for valuation at the customs frontier of the exporting country.

534. Without regard to the c.i.f./f.o.b. distinction, the source documents of almost two thirds of the responding countries called for

the customs frontier as the physical point of valuation for imports, while those of another quarter specified the national border. The weighted replies, however, suggest that none of the alternative physical points of valuation for imports (establishment of transactor, customs frontier, and national border) was much more frequently requested than the others. Only 10 per cent of the reporting countries used source documents specifying the establishment of either the exporter or the importer as the physical point of valuation for imports, but this small group included the United States, thus explaining the relative importance of this valuation point in the weighted responses.

535. Known discrepancies between the point of valuation requested on source documents and valuations reported in practice were relatively minor. However, nearly half of the reporting countries responsible for almost two thirds of the aggregate imports of the respondents indicated that they made at least some adjustments to basic source data to change the physical point of import valuation for balance of payments purposes. Typically, adjustments were made to convert c.i.f. source data to an f.o.b. basis, although the precise valuation points intended for the f.o.b. equivalents were not usually specified.

536. More than four fifths of the respondents believed that import values were easier to collect on a c.i.f. basis. A clear majority of these countries felt that it would be simpler to value imports at the customs frontier of the importing country, while the remainder saw advantages in valuing imports at the national border of that country. Of the few countries choosing to value imports f.o.b., practically all preferred the customs frontier as the physical point of valuation.

(b) *Pricing of merchandise*

537. The questionnaire sought information concerning the pricing basis requested in the source documents used to collect data on merchandise transactions, the basis employed in practice for the balance of payments, and the basis respondents would prefer as the international standard. For each of these three questions, two alternative prices, or methods of valuation, were cited: invoice value (i.e., actual transactions value) and value for customs duty purposes. To the extent that some countries might not have regarded these alternatives as exhaustive or mutually exclusive, the problems mentioned in section (1) again call for caution in interpreting the replies.

538. About three fourths of the countries reported that they requested and obtained invoice value for the purpose of pricing exports. About the same proportion regarded this concept as the

appropriate one for an international standard. In terms of the weighted responses, more than 90 per cent requested invoice value and more than four fifths of the respondents said their exports were valued primarily on this basis.

539. Similarly, invoice value was regarded as the ideal basis for valuing imports by about three fourths of the respondents, although a slightly lower proportion reported that they requested or actually collected figures for imports valued on this basis. The difference between the stated ideal valuation and the valuation in practice was more marked in the weighted results. Although more than 90 per cent of the weighted replies indicated a preference for invoice value as the international standard, slightly less than half of the weighted answers indicated that source documents requested invoice value and only about one third of such answers showed that imports were actually recorded on that basis. Thus, despite the almost unanimous agreement that invoice value was the ideal international standard, the weighted responses indicated that most imports were reported at the value for customs duty.

(c) Sources of international trade data

540. Customs documents and exchange records were listed as the two principal sources of international trade data. Customs documents predominated; about 85 per cent of the weighted survey replies indicated that they were the primary source for measurement of exports and imports. Exchange record data were used for most of the remainder. The unweighted results indicated that about two thirds of the countries surveyed rely chiefly on customs data to measure both exports and imports, while the other third depends mainly on exchange records. Some countries reported using other sources, but usually to supplement customs or exchange record data.

541. Replies concerning the nature of source documents suggest that trade statistics record the vast majority of world exports at the approximate time of shipment, while recording a similar proportion of world imports at the approximate time of arrival in the importing country. This difference accounts for much of the recorded asymmetries in world aggregations of trade statistics (apart from the c.i.f. valuation of many imports). It also highlights the importance of timing adjustments for balance of payments purposes, as recommended in Chapter 5 of this Manual.

(d) Relationship between merchandise and shipment items

542. Respondents were requested to indicate their sources for estimating the value of freight and insurance transactions and to

explain any inconsistencies between these data sources and the physical point of valuation used in the merchandise accounts. Special surveys were reported to be the most common source of data on freight and insurance transactions for balance of payments statements, being used by almost two fifths of the respondents. Slightly more than one fifth reported using exchange records as the source of this information, while almost one fifth used customs documents. Various other sources were used by the remaining countries.

543. Very few inconsistencies were reported between the physical point of valuation used to estimate the value of freight and insurance and that used to estimate the value of merchandise transactions in each country's balance of payments.

(3) Implications for this Manual

544. The survey on merchandise trade uncovered substantial general support for the proposition that trade should be valued at invoice value. The relationship between this concept and that of market value is discussed in Chapter 4 of this Manual.

545. The survey also established an almost unanimous preference for valuing exports on an f.o.b. basis, with a clear majority advocating f.o.b. at the customs frontier as the conceptual ideal. Furthermore, it found that most exports were in principle being valued on that basis. Thus, in adopting the physical point of valuation for exports as f.o.b. at the customs frontier of the exporting country (see paragraph 240), the Manual bases its recommendation on a widely accepted concept and endorses the practices already most common for valuing world exports.

546. The position reported with regard to imports was less clear. Although the survey showed that, for the most part, imports are valued c.i.f., there was evidence that many countries regard this situation as less than ideal. Many have attempted to adjust their basic import data to an f.o.b. basis for balance of payments purposes, and one inference could be that, in some cases, recourse to c.i.f. import valuations was the result of data collection difficulties. Despite the lack of firm agreement on a theoretical ideal, the framers of this Manual feel justified in advocating that imports be valued f.o.b. at the customs frontier of the exporting country—the only concept capable of providing symmetry with the recommended treatment of exports.

APPENDIX E

Survey of Direct Investment: Concepts and Compilation

(1) Introduction

547. As part of the project of preparing this Manual, the Fund staff undertook to conduct a survey of member country concepts and practices concerning direct investment flows. For this purpose, the U.S. consultant on the project supplied an extensive list of questions that the Fund staff sent to 25 countries representing a cross section of members. This Appendix summarizes responses from the 21 countries that submitted replies.

548. No explicit attempt was made to weight answers in terms of a responding country's relative importance as an initiator or recipient of direct investment flows, as deciding on appropriate weights would have been particularly difficult. However, it may be noted that, according to information published in the *IMF Balance of Payments Yearbooks* covering the five years 1967-71, the United States contributed about two thirds of the net direct investment capital flows abroad attributable to respondents in the aggregate and received one eighth of the net direct investment capital inflows. In recognition of this dominant position, the text notes major instances where the practice or viewpoint of the United States differed from that of most respondents.

549. Direct investment capital and income flows are generally held to reflect transactions between an enterprise in one economy and an investor or investors with a lasting interest in the enterprise that reside elsewhere. The following discussion of the survey results is set out in three subsections. The first outlines the respondents' concepts of direct investment enterprises and of direct investors, and reports on the practical difficulties encountered in attempting to compile data. The next two subsections are addressed to conceptual and compilation aspects of the transactions that are most commonly regarded as direct investment capital and as direct investment income flows, respectively.

(2) Survey Results

550. This Appendix provides a general assessment of the replies to the questionnaire. It should be noted at the outset that the respondents all firmly believed in the importance of separating direct investment from other types of investment flows. Most felt that the different behavior of direct investment justified such a distinction, but few elaborated on the expected behavioral differences. Other reasons given in support of separately distinguishing direct investment included the desire to measure the degree of foreign influence on the domestic economy and to show direct investment as a supplementary form of development finance.

(a) Identification of direct investment enterprises

551. The first section of the survey was designed to ascertain the most common criteria used to identify direct investment enterprises. It specifically wished to test the proposition that foreign participation (representing some share in ownership, which implies voting rights or an effective voice in management) is the essential criterion. The answers tended to provide broad support for this proposition.

552. In searching for a working definition of direct investment enterprises, the survey found general agreement on restricting the concept to corporations, unincorporated businesses, or branches of foreign companies engaged in activity for the purpose of making a profit. A degree of foreign ownership was generally accepted as the main distinguishing feature of a direct investment enterprise; indeed, respondents would not classify a capital flow as direct investment unless the investor possessed or acquired some degree of ownership of the enterprise. About half the respondents regarded a specified degree of foreign ownership as the sole criterion of such an enterprise. The nature of the foreign owner (for example, government or business corporation) was usually considered irrelevant. The vast majority of countries considered that foreign ownership implied the equivalent of a voting interest or an effective voice in the management of an enterprise.

553. Countries generally relied heavily on minimum (albeit diverse) percentages of foreign ownership to identify direct investment enterprises, whether these were operating in the reporting economy or abroad. Many also examined other forms of foreign participation to supplement this central criterion, but few based their identification on other elements in the absence of some degree of foreign ownership.

554. Opinions were divergent on the appropriate minimum proportion of direct foreign ownership necessary to qualify an enterprise as a

direct investment enterprise. Country practices for identifying direct investment enterprises fell into three groups of about the same size. The first rejected reliance on specific "rule of thumb" percentage criteria, preferring to treat each case on its merits. The second evoked the other extreme and applied a uniform percentage ownership test, regardless of the degree of diffusion of the investment flows in terms of the cohesion of investors or the number of investing countries. These uniform percentages ranged, country by country, from at least 5 per cent foreign ownership to more than 50 per cent. The remaining group of respondents distinguished between different sources of investment flows and adopted minimum percentage criteria for each of them. Typically, members of this group raised their requisite minimum percentage of ownership interest as the cohesion of investors declined, presumably to reflect the lessening of direct influence; they drew no distinction between associated investors in one country and those in more than one country; and they adopted minimum identification criteria that were generally fairly similar. Single or associated foreign investors were most commonly required to hold at least a 25 per cent ownership interest before there was considered to be presumptive evidence of a direct investment enterprise. As foreign ownership became more scattered, as with unassociated foreign investors from a single country, the most common requirement generally doubled to a 50 per cent minimum ownership interest. Few respondents reported on the extreme case of unassociated investors from more than one country, but those that did generally required complete foreign ownership of the enterprise before classifying it as a direct investment enterprise.

555. In addition to asking for information on the means of identifying direct investment enterprises in terms of direct foreign participation, the questionnaire also sought advice concerning the treatment of indirect, nominal, and mutual ownership. Indirect ownership is defined as occurring when a foreign investor met the reporting country's presumptive test of ownership in a resident enterprise that, in turn, met the same test of ownership in another resident enterprise, with the foreign investor thus exerting only an indirect voice in the management of the latter. Only one third of the respondents, including however the United States, considered such a concept when identifying a domestic direct investment enterprise; even fewer looked to indirect resident ownership when determining the status of a nonresident enterprise. In contrast, when resident brokerage companies, trustees, or dummy companies acted solely as agents or representatives of a foreign interest, about half of the respondents related their identification decision to the effective voice

of the foreign enterprise, on whose behalf the nominal owner was operating, in the management of the resident enterprise. Mutual ownership refers to enterprises in two countries, each holding at least the minimum percentage of direct ownership in the other that would be needed to qualify it as a direct investor. When this situation occurred, respondents generally regarded both of them as direct investment enterprises.

556. Respondents were asked to report on the sources of the data that they used to identify direct investment enterprises and direct investors. In general, information was normally obtained from resident investors concerning acquisitions of interests in, or the establishment of, direct investment enterprises abroad. Similar information concerning foreign direct investors' interests in domestic enterprises was almost always sought from the domestic direct investment enterprise. In both cases, respondents generally relied on surveys to collect data on ownership interests, although many used exchange control authorities (and, to a lesser extent, commercial banks) as important indirect sources of this type of information.

(b) *Direct investment capital flows*

557. Another group of questions concerned direct investment capital flows to established direct investment enterprises. These questions sought to determine whether direct investment capital flows are normally limited to transactions that change a direct investor's debt and equity interest in a direct investment enterprise. Questions were also asked to determine how countries classify reverse capital flows, reinvested earnings, and enterprises' transactions with investors that are not direct investors.

558. The questionnaire established that, with minor exceptions, countries classify direct investment capital flows abroad in accordance with the same standards and concepts that they apply to the classification of direct investment capital flows to the reporting country.

559. Respondents displayed almost unanimous approval, in principle, for the definition of direct investment given in the third edition of the Manual (viz., "The term, direct investment, is used to refer to investment made to create or expand some kind of permanent interest in an enterprise; it implies a degree of control over its management"). Thus, a majority of the reporting countries considered all changes in a direct investor's equity share in a direct investment enterprise as a direct investment capital flow, regardless of how the share was acquired. The great bulk of them regarded all transactions in company-

issued stock that changed a direct investor's equity share in a direct investment enterprise as direct investment capital flows, but a minority group excluded some transactions that changed the direct investor's equity share in surplus accounts. Furthermore, although a majority (including the United States) agreed with the concept of treating reinvested earnings as offsetting flows of direct investment capital and income, a small group of respondents, including the United States, did not record reinvested earnings in their balance of payments accounts at the time of the survey. Most countries felt that reinvested earnings should be computed as the direct investor's share of net incorporated enterprise earnings, exclusive of its share of declared dividends.

560. Respondents generally applied exactly the same criteria to identify direct investment capital flows to both incorporated and unincorporated direct investment enterprises, with less than half separately distinguishing these two forms of business enterprise.

561. Some respondents also included as direct investment capital flows certain equity transactions affecting the foreign ownership share of specified, or all, persons who were not direct investors. For example, a few countries included changes in the ownership share in a resident direct investment enterprise of all foreigners, and one included changes in the ownership share of all residents of the country of the direct investor.

562. The reported treatment of capital flows in nonequity forms was rather varied. Almost every respondent regarded changes in at least some forms of long-term debt of direct investment enterprises to direct investors as direct investment capital flows; a clear majority afforded similar treatment to specified short-term debts of this kind. Indeed, almost two thirds of the respondents considered any change in the liabilities of a direct investment enterprise to a direct investor as a form of direct investment capital flow.

563. In response to the questions concerning compilation practices and sources used to compile estimates of direct investment capital flows, there was considerable agreement that, following the sale of an equity interest to a direct investor, the resultant direct investment capital flow should be recorded at the time payment is received by the resident seller. A comparison of changes in the asset and liability positions shown in the financial accounting records of resident direct investment enterprises and resident direct investors was by far the most common procedure for estimating direct investment capital flows.

564. One part of the questionnaire was designed to establish how countries related their estimates of direct investment capital flows to

end-of-period stock positions. The respondents that made annual estimates of their country's total international asset and liability position often published the direct investment asset and liability situation as a component. Most of these countries estimated their direct investment position from cumulated changes in direct investors' shares in the net assets of direct investment enterprises (making appropriate valuation adjustments as circumstances warranted), combined with special surveys of foreign investment stock positions made at intervals to obtain benchmark data.

565. Nearly all the responding countries collecting data on re-invested earnings of resident direct investment enterprises obtained their information from the financial accounting records of the resident enterprise. Information pertaining to the reinvested earnings of direct investment enterprises operating abroad was obtained, with equal frequency, from the books of either the resident direct investor or those of the direct investment enterprise abroad.

566. Opinion was evenly divided as to whether direct investment capital flows should be netted against transactions by which the direct investment enterprise acquired an ownership interest in its foreign direct investor.

567. In an attempt to determine the quantitative importance of conceptual differences between countries and of individual types of direct investment capital flows, countries were requested to provide estimates of specified direct investment capital flows during 1970. To the extent that data were available, the answers implied that the treatment of reinvested earnings was quantitatively the major definitional inconsistency among countries in recording direct investment capital flows. Equity transactions were the paramount form of direct investment capital flows, comprising well over half of the reporting countries' estimates for both direct investment capital in the reporting country and abroad. For those countries reporting reinvested earnings flows, these were the next most important type, accounting for more than one third of their net direct investment capital flows in 1970. Except for direct investment capital flows abroad in the form of long-term loans, other net types of direct investment capital flows were of markedly less quantitative importance.

568. Not all countries could provide the requested disaggregation of direct investment capital flows by type of direct investment enterprise. Returns containing this information, however, attested to the overwhelming importance of incorporated enterprises in direct investment capital flows; resident incorporated direct investment enterprises received almost three fourths of reported direct invest-

ment capital flows to the reporting country in 1970, and more than four fifths of reported direct investment capital flows abroad were to foreign incorporated direct investment enterprises in that year.

(c) *Direct investment income flows*

569. A part of the questionnaire concerned the treatment of direct investment income flows. Its main purpose was to establish the importance of exceptions to the general rule that direct investment income must be associated with a prior direct investment capital flow. It then proceeded to identify the types of income flow that countries subjected to this test.

570. Most responding countries distinguished between direct investment and portfolio investment income in their balance of payments presentations, and all countries reported symmetrical definitions of direct investment income payments and receipts. In general, association with a direct investment capital flow was regarded as both a necessary and a sufficient condition for specified income flows to be classified as direct investment income. Substantial agreement also existed concerning the types of income flow that qualified for consideration as direct investment income. Virtually all the responding countries regarded a direct investor's share of the dividends of a direct investment enterprise as direct investment income. About two thirds went further and included the direct investor's share of the net earnings of the direct investment enterprise; at the time of the survey, the United States was in the minority group that did not include that share. Most countries also regarded interest payments, on either long-term or short-term debt, by direct investment enterprises to direct investors as direct investment income. Respondents almost unanimously agreed, however, that payments of various fees (i.e., rental fees, royalties and license fees, and management service fees) to direct investors by direct investment enterprises should not be regarded as direct investment income. In any case, among the reporting countries only the United Kingdom and the United States were able to separate fees or royalties paid to foreigners by resident direct investment enterprises from those paid by other resident enterprises. Many of the countries not disaggregating foreign payments of fees or royalties in this manner implicitly included such transactions of direct investment companies as direct investment income, although most said they would exclude them if they possessed the necessary data.

571. In response to the questions on sources and methods used to compile estimates of direct investment income flows, most of the

reporting countries considered that direct investment income payments occurred at the time when cash payments, requiring foreign exchange, were made. Some also took into account the time of recording of these income payments as liabilities in the direct investment enterprises' accounting records, but very few relied solely on this criterion. More than three fourths of the reporting countries recorded direct investment income payments on a gross basis (i.e., they did not offset any income received by direct investment enterprises on account of any equity share in their foreign direct investors), and practically all the countries recorded direct investment income payments after deduction of taxes withheld by the government.

572. In the special estimates provided for 1970, there were relatively more variations in the treatment of specified types of income, and particularly reinvested earnings, than there were of direct investment capital flows. In absolute terms, the U.S. practice of not including reinvested earnings in its estimates of direct investment income flows was most important. Varying treatments of interest transactions between direct investment enterprises and their direct investors also caused a substantial degree of noncomparability between individual country estimates of direct investment income flows.

INDEX

INDEX

(The numbers refer to paragraphs)

-
- “Above-the-line” items. See Analytic presentation
 - Accounting system, 21–25, 180
 - Advertising, 329
 - Affiliated enterprises, 216
 - Agents, 72
 - Agents’ fees, 245, 330–31
 - Aid missions and services, 314, 317
 - Aircraft
 - Insurance, 326
 - See also Mobile equipment
 - Airport fees, 272, 288
 - Alimony, 352
 - Analytic presentation, 138–64
 - Animals, live, 221(ix), 232(d)
 - Arbitrage profits, 338, 370
 - Armed forces personnel, 60(e)
 - Art exhibits, 221(ix)
 - Assets
 - blocked and in inconvertible currency, 450
 - committed, 451
 - financial. See Capital account
 - nonfinancial, 231
 - nonfinancial intangible, 50, 63, 321, 323, 363(a)
 - Bad debts, 43, 303, 373(ii)
 - Baggage fees, 268
 - Balance. See Analytic presentation
 - Balance of payments, definition of, 16–20
 - Banks, 65, 66, 434–35
 - Barter, 78(a)
 - Basic balance, 161–64
 - “Below-the-line” items. See Analytic presentation
 - Bilateral statements, 474–85
 - Bonds, 424, 428, 437. See also Securities
 - Bonus shares, 290, 306, 368
 - Border workers, 61, 319
 - Branches. See Direct investment
 - Brokerage, 330
 - Buffer stocks, 232(g)
 - Buildings, 231, 363(a)
 - Bunker fuel, 227(i), 272
 - Cable services, 328
 - Cancellation of debt, 355. See also Write-offs
 - Capital account
 - classification of, 381–99
 - coverage of, 361–63
 - definition of, 360
 - other capital, 431–38
 - problem of measurement of, 400–406
 - recording, 371–78
 - standard components, 191–97
 - transactions, 364–70
 - valuation and timing, 379–80
 - Capital gains and losses, 41–42, 125, 293, 303, 370
 - Carriers
 - crews of, 60(b), 281
 - insurance, 326
 - registration, 358
 - See also Mobile equipment

- Cartage, 265
- Catastrophes, 303
- Center of interest, 59–61
- Central bank, 66, 434
- Central government. *See* General government
- Certificates of deposit, 424. *See also* Securities
- Change of ownership, 100–102, 214–25.
See also Time of recording
- Charter services, 273–76. *See also* Leasing,
nonfinancial (operational)
- C.i.f. valuation. *See* Valuation
- Circus equipment, 221(ix)
- Claims
 - insurance, 262, 327, 352
 - See also* Capital account
- Classification
 - adjustment of, to basic statistics, 490,
492, 501–503
 - of financial items, 381–99
 - of other capital, 432–37
 - of portfolio investment, 427–28
 - See also* Components, standard; Reclas-
sification
- Coastal shipping, 258
- Coin, 229, 232(b), 437
- Commercial banks, 65, 435
- Commercial travelers, 60(c). *See also* Travel
- Commissions, 330
- Commitment charges, 290
- Committed assets, 451
- Commodity gold. *See* Gold
- Common stocks, 425. *See also* Securities
- Communications, 328
- Compensation of employees, 312(i), 319–20
- Compensatory financing of export fluctua-
tions. *See* International Monetary
Fund
- Compensatory official financing, 156
- Components, standard, 165–97
- Concessions, 63
- Consignment goods, 235
- Consular fees, 246
- Consulates, 312. *See also* General govern-
ment
- Contracts, forward, 136, 370
- Contributions. *See* Unrequited transfers
- Conversion, 121–37
- Copyrights, 63, 323, 363(a)
- Corporate bonds and equities, 425, 428
- Counterparts, 22, 34–40, 103, 463
- Coverage, 490–91, 495–500
- Crews of carriers, 60(b), 281
- Currency, 229, 232(b), 437
- Current account, 179–90, 198–212
- Current (account) balance, 148–51
- Customs frontier, 240
- Customs returns, 214, 232
- Damages, 352
- Debentures, 424. *See also* Securities
- Debt cancellation, 355. *See also* Write-offs
- Deficit. *See* Analytic presentation
- Demonetization of gold. *See* Gold
- Depletion, 303
- Deposit money banks, 65, 435
- Deposits, 437
- Depreciation, 302
- Destroyed goods, 221(viii), 258
- Diamonds, 232(a)
- Diplomatic personnel, 60(e). *See also* Gov-
ernment
- Direct investment, 193, 385(ii), 407–22,
547–72
- Direct investment income, 295, 569–72
- Discounts, 91, 290, 293
- Display equipment, 221(ix)
- Distributive services
 - as component of merchandise, 171, 213,
238–40
 - as component of shipment, 257, 265
 - See also* Shipment
- Dividends. *See* Investment income
- Double-entry system, 21–25, 180

- Dowries, 352
 Drayage, 265
 Duties, 91, 129
- Earnings, distributed. See Investment, income
 Earnings, reinvested. See Reinvested earnings
 Earnings, workers', 319–20
 Economy, concept of, 26
 Electricity, 232(c)
 Embassies, 312. See also General government
 Enterprises, 58, 63–74
 Equities, corporate, 425. See also Securities
 Errors. See Net errors and omissions
 Exchange rate. See Conversion
 Exchange record, 31, 109, 234
 Exchanges, 32
 Excursionists, 285
 Exhibits, 221(ix)
 Exports. See Merchandise
 Expropriation, 43, 373(ii)
- Fares, passenger, 268
 F.a.s. valuation. See Valuation
 Fees. See specific types
 Film rentals, 334
 Financial items. See Capital account
 Financial leasing, 74, 217, 275, 292, 322, 363(c)
 Financial services, 330
 Fines, 103, 345, 358
 Fish, 220(iii)
 Fishing
 rights, 358
 vessels. See Mobile equipment
 Floating rates, 128–30
 F.o.b. valuation. See Valuation
 Foreign exchange assets. See Reserves
 Forward contracts, 136, 370
- Forwarding, 265
 Freight, 261. See also Shipment
 Fund (IMF). See International Monetary Fund
 Futures, 338
- Gas, 232(c)
 Gas drilling rigs. See Mobile equipment
 General government, 54–58. See also Official transactions
 Gifts, 87, 232(k), 288, 352. See also Unrequited transfers
 Gold
 commodity (nonmonetary), 232(a), 464
 monetary, 230, 361, 464–66
 monetization/demonetization, 35, 372(ii), 455, 465–66
 Gold tranche position. See International Monetary Fund
 Goods, 226–31. See also Current account; Merchandise; and specific types
 Government
 enterprises, unincorporated, 55
 general, 54–58
 personnel 60(d) and (e), 258, 281, 283, 286, 312
 purchases abroad, 220(iv)
 Grants. See Unrequited transfers
 Gross recording. See Recording, gross and net
 Guaranteed credits, 392
- Handling, 265
 Harbor fees, 272
 Haulage, 265
 Highway vehicles. See Mobile equipment
- IBRD obligations. See World Bank obligations
 Immovable assets, 50, 363(a)
 Imports. See Merchandise
 Improvements, 221(ii), 336
 Income. See Investment income; Labor income; Property income

200 / BALANCE OF PAYMENTS MANUAL

- Indemnities, 355
- Individuals, residence of, 59–61
- Inheritances, 352
- Inspection, 221(ii)
- Installation of machinery, 60(c), 73, 281
- Instruction, 339
- Insurance
 - merchandise, 262–64
 - nonmerchandise, 326–27
- Intangible assets, nonfinancial. *See* Assets
- Interest. *See* Investment income
- International bodies
 - capital subscriptions, 434, 450
 - contribution to administrative budgets, 355
 - employees of, 57, 60(e), 281, 283
 - residence, 57
- International investment position, 49–51
- International Monetary Fund (IMF)
 - charges, 296
 - transactions, 134, 469–72
 - See also* Special drawing rights
- Inventories, 231
- Investment
 - direct. *See* Direct investment
 - income, 205, 289–306. *See also* Direct investment income
 - portfolio, 194
 - See also* Capital account
- Joint enterprises, 71
- Joint military arrangements, 315
- Labeling, 221(ii), 265
- Labor income, 312(i), 319–20
- Land, 50, 63, 231, 321–24, 363(a)
- Leases, 63
- Leasing
 - financial, 74, 105, 217, 275, 292, 322, 363(c)
 - nonfinancial (operational), 273, 322, 333–34
- Liabilities. *See* Capital account
- License fees, 323
- Liens, 436
- Life insurance, 327
- Lighterage, 272
- Line of credit, unutilized, 362
- Livestock, 221(ix), 232(d)
- Loading costs, 242, 261, 265, 272
- Loans, 436, 438, 450
- Local governments. *See* General government
- Locally recruited staff, 56
- Long-term capital, 386–88
- Losses
 - capital. *See* Capital gains and losses
 - investment income, 305
- Lost goods, 221(viii), 258
- Lotteries, 352, 358
- Mail
 - carriage, 277
 - fees, 328
- Management, 332
- Marine insurance, 326
- Marine products, 220(iii)
- Market price
 - definition of, 75–89
 - See also* Valuation
- Membership fees, 352, 358
- Merchandise, 182, 202, 213–47, 486–517, 525–46
- Merchanting, 219, 227–28, 337
- Migration, 36, 38, 348–50, 372(vi). *See also* Workers
- Migrants' effects, 232(i). *See also* Migration
- Military agencies and establishments, 54–56, 60(e), 313
- Military services, 315, 318
- Mobile equipment, 50, 68–71, 220(i), 221(v), 363(a)
- Monetary gold. *See* Gold
- Monetary institutions, 64–66, 434–35
- Monetization of gold. *See* Gold
- Money. *See* Currency
- Mortgages, 424, 436
- Motion-picture film rentals, 334

- Motor vehicles. See Mobile equipment
- Multilateral settlements, 478–79

- National accounts. See *System of National Accounts (SNA)*.
- Net errors and omissions, 144, 151, 164, 176–78
- Net recording. See Recording, gross and net
- Net worth, 37–38, 51
- Newspapers, 227(iii)
- Noncommercial transactions, 87–88
- Nonfinancial intangible assets. See Assets
- Nonfinancial (operational) leasing. See Leasing
- Nonmerchandise insurance, 326–27
- Nonmonetary gold. See Gold
- Nonmonetary institutions, 64
- Nonprofit bodies
 - government, 55
 - private, 62

- Obsolescence, 303
- Official settlements balance, 152–60
- Official transactions, 296, 307, 310–18, 346, 354–59
- Offshore installations, 220(ii)
- Oil drilling rigs. See Mobile equipment
- Omissions. See Net errors and omissions
- Overall balance, 152–60
- Overinvoicing, 94
- Ownership. See Change of ownership

- Packaging, 221(ii), 265
- Packing, 265
- Paper money, 229, 232(b), 437
- Parcel post, 232(e)
- Partial balance. See Analytic presentation
- Participations, 425. See also Securities
- Passengers
 - effects of, 248
 - services to, 268–69

- Patents, 63, 323, 363(a)
- Payments agreement balances, 434, 450
- Payments balances. See Analytic presentation
- Peace Corps, 314
- Pensions, 327, 352, 358
- Performance balance, 159
- Periodicals, 227(iii), 335
- Personal effects, 268, 287–88
- Pilotage, 272
- Pipelines, 67
- Port services, 227(i), 271–72
- Portfolio investment, 194, 385(iii), 423–30
- Postal services, 328
- Postpayments, 102
- Precious metals and stones, 232(a)
- Preference shares, 424. See also Securities
- Premium price, 293
- Premiums, insurance 262–64, 326–27
- Prepayments, 102
- Prices. See Valuation
- Private transactions, 298, 310, 346
- Processing, 222, 336
- Professional services, 339
- Profits, undistributed. See Reinvested earnings
- Promissory notes, 424. See also Securities
- Property income, 292, 321–24
- Public enterprises, 66

- Railways, 67
 - rolling stock. See Mobile equipment
- Real resources, 22, 200
- Rebates, 91
- Reclassification, 39, 372(iv) and (v), 374(i) and (ii), 454, 462–63
- Reconciliation items, 49–51. See also Reclassification; Valuation changes
- Record rentals, 334
- Recording, gross and net
 - capital account, 375–78
 - current account, 209–12

202 / BALANCE OF PAYMENTS MANUAL

- direct investment, 419–20
- entries for components, 24, 180
- grants, 354
- labor income, 319
- loans, 438
- Regional statements, 474–85
- Reinsurance, 326
- Reinvested earnings, 103, 171, 291, 295, 299–300, 304, 368, 416
- Rentals, 334
- Repacking, 265
- Repairs, 221(ii), 272, 336
- Reparations, 355
- Research, 339
- Reserve position in the Fund. See International Monetary Fund
- Reserves, 172, 196–97, 385(i), 439–73
- Residents, 52–74
- Residual item. See Net errors and omissions
- Rest-of-the-world account, 45, 47
- Returned merchandise, 221(iii), 223
- Revaluation items. See Reconciliation items
- Rights, 63
- Royalties, 323

- Salaries, 312(i), 319–20
- Salvage fees, 277
- Salvaged goods, 220(ii), 495(vii)
- Samples, 221(x)
- Savings and lending bodies, public, 55
- Scholarships, 287, 357
- Seasonal workers, 60(f), 319
- Sector classification, 172, 389–92, 433–35
- Securities, 229, 424
 - unissued, 232(b)
- Services. See Current account and also specific types
- Services on merchandise, 250–56
- Shares, 424, 425. See also Securities
- Shipboard expenditures, 268
- Shipment, 171, 203, 241, 248–65
- Ships
 - stores, 227(i), 272
 - See also Mobile equipment
- Short-term capital, 386–88
- Silver bullion, 232(a)
- Sinking funds, 362
- Smuggled goods, 232(j)
- SNA. See System of National Accounts
- Sorting, 221(ii)
- Souvenirs, 288
- Special drawing rights, 34, 361–62, 372(i), 456, 467–68. See also International Monetary Fund
- Speculative gains and losses, 338, 370
- Stage equipment, 221(ix)
- Standard components, 165–97
- State government. See General government
- Stevedoring, 272
- Stock dividends, 290, 306, 368
- Stocks abroad of goods, 219, 228
- Stocks (corporate equities), 425. See also Securities
- Storage, 221(ii), 265
- Structures, 363(a)
- Students, 60(a), 284
- Subscriptions
 - capital, to international nonmonetary organizations, 434, 450
 - to periodicals, 227(iii), 335
- Subsidies, 91, 129, 355
- Surplus. See Analytic presentation
- Surveys, 339
- Swap arrangements, 442, 452
- System of National Accounts (SNA), United Nations, 44–51
 - comparison with balance of payments classification, 518–24
- Tape rentals, 334
- Taxes, 91, 103, 358
- Technical assistance, 355, 357
- Technical services, 339

- Telecommunication services, 328
- Temporary exports and imports, 221(ix)
- Territorial change, 36-37, 374(i)
- Theatrical equipment, 221(ix)
- Time of recording
 - adjustment of, need for, 106, 490
 - adjustment of, to merchandise data, 107-109, 493, 504-13
 - adjustment of, to other data, 110-14
 - change of ownership, relation to, 214-15, 233-34
 - of financial items, 380
 - of investment income, 299-300
 - of reserves, 460-61
 - of unrequited transfers, 345
 - principle of, 29, 98-105
- Tourists, 60(a). *See also* Travel
- Towage, 272
- Trade
 - credits, 102, 433
 - See also* Merchandise
- Trainees, 284
- Transactions
 - capital, 364-70
 - definition of, 18
 - types of, 30-43
- Transfer price, 82, 84
- Transferring, 265
- Transfers. *See* Unrequited transfers
- Transit trade, 221(vi), 258
- Transportation, 184, 204, 266-77, 288
 - equipment. *See* Mobile equipment
 - See also* Shipment
- Travel, 185, 205, 278-88
- Tugboat services, 272

- Underinvoicing, 94
- Undistributed profits. *See* Reinvested earnings

- Unit of account, 115-20
- Unrequited transfers, 22, 33, 87-88, 103, 188-90, 198-200, 207, 340-59
- Use of Fund credit. *See* International Monetary Fund

- Valuation
 - adjustment to basic statistics, 490, 494, 514-17
 - market price, relationship to, 75-97
 - of direct investment transactions, 421-22
 - of financial items, 379
 - of merchandise, 236-47
 - of portfolio investment, 426
 - of reserves, 460-61
 - of unrequited transfers, 344
 - principle of, 27-28
- Valuation changes
 - as a subcomponent, 170
 - calculation of, 400-403
 - causes of, 40-43
 - conversion of, 122-25
 - in reserves, 372(iii)
 - to be omitted, 373
- Visitors, 60(a). *See also* Travel

- Wages, 312(i), 319-20
- Warehousing, 265
- Water, 232(c)
- Workers
 - earnings of, 319-20
 - remittances by, 351
 - See also* Migration
- Working balances, 451
- World Bank obligations, 450
- Write-offs, 43, 303, 373(ii)

International Monetary Fund, Washington, D.C. 20431, U.S.A.
Telephone number: 202 477 7000
Cable address: Interfund