

Compilation of the balance of payments in accordance with the methodology of the sixth edition of the Balance of Payments and International Investment Position Manual

1. General information

The BNB compiles the balance of payments statistics and the international investment position in strict adherence to the international methodological standards of IMF balance of payments manuals. These standards also provide for the legal basis in the area of balance of payments statistics and the international investment position of the European Central Bank (ECB) and the European Commission (Eurostat) that all EU member states must observe. The direct investment statistics adhere also to the requirements of OECD *Benchmark Definition of Foreign Direct Investment*¹.

The IMF released the sixth edition of the Balance of Payments and International Investment Position Manual (*MBΦ, 2008*) (BPM6, *the Manual*)² in 2009.

The implementation of the new methodological requirements of BPM6 by the EU countries was coordinated by the European System of Central Banks (ESCB) and the European Statistical System (ESS).

The new edition of the IMF's Manual takes into account important developments that have occurred in the global economy since the fifth edition of the Balance of Payments Manual (IMF, 1993) (BPM5) was released.

The major factors that necessitated the revisions to the Manual are:

- globalisation - the growing significance of cross-border production processes, complex structures and relations of international companies, and international labour mobility;
- financial innovation – growing diversity and complexity of financial instruments.

Although the structure of the balance of payments remains almost unchanged – current, capital and financial account, the current framework for covering and reporting cross-border economic relations has been changed in many aspects in order to reflect the new economic and technical developments. New classifications for some subitems have been adopted, as well as more detailed breakdowns of institutional sectors, and inclusion of transactions that have been previously uncovered, which enhances the value of the ensuing statistical data.

For the purpose of consistency and comparability of macroeconomic data, the Manual was revised in parallel with other basic methodological manuals, including the System of National Accounts (IMF, 2008)³

¹ www.oecd.org/daf/inv/investmentstatisticsandanalysis/40193734.pdf

² <http://www.imf.org/external/pubs/ft/bop/2007/bop6comp.htm>

and the European System of Accounts (ESA 2010)⁴, the External Debt Guide (IMF, 2013)⁵, and Benchmark Definition of Foreign Direct Investment (OECD, 2008)⁶.

With relation to this, amendments were made at EU level to the regulations in the field of external sector statistics. Included herewith are the recommendation of the European Central Bank of 23 January 2014 amending Recommendation ECB / 2011/24 on the statistical reporting requirements of the European Central Bank in the field of external statistics (ECB / 2014/2) (2014/C 51/01), and Regulation (EC) № 555/2012 of 22 June 2012 for amending Regulation (EC) № 184/2005⁷ of the European Parliament and of the Council on Community statistics concerning balance of payments, international trade in services and foreign direct investment.

At national level, amendments were made to the provisions of the Currency Law⁸ on external statistics in 2011. In 2014 the BNB adopted the new Ordinance No. 27⁹ on the balance of payments statistics, international investment position and securities statistics.

2. Key changes in the changeover to the methodological requirements of the sixth edition of the Balance of Payments and International Investment Position Manual

2.1. Changes in data presentation

- The Manual's title has been changed to Balance of Payments and International Investment Position Manual (BPM6) due to the significance of the international investment position for the economic analysis, and also providing more detailed instruction for its compilation (paragraph 1.1 of BPM6).
- Debits and credits are recorded with a positive sign in the current account according to BPM6 (debits were previously presented with a negative sign), and net items are calculated as follows:

$$\text{Net items (CA)} = \text{Credit entries (exports)} - \text{debit entries (imports)}$$

³ <http://www.imf.org/external/pubs/ft/qna/>

⁴ <http://ec.europa.eu/eurostat/web/products-manuals-and-guidelines/-/KS-02-13-269>

⁵ <http://www.imf.org/external/pubs/ft/eds/eng/edgupdate/pdf/update.pdf>

⁶ www.oecd.org/daf/inv/investmentstatisticsandanalysis/40193734.pdf

⁷ https://www.ecb.europa.eu/ecb/legal/pdf/c_05120140222bg00010002.pdf and <http://eur-lex.europa.eu/legal-content/BG/TXT/PDF/?uri=CELEX:32012R0555&from=BG>

⁸ http://www.bnb.bg/bnbweb/groups/public/documents/bnb_law/laws_foreignexchange_bg.pdf

⁹ http://www.bnb.bg/bnbweb/groups/public/documents/bnb_law/regulations_registrationinb_bg.pdf

An exception is made for item *goods acquired under merchanting*, which are recorded as a negative credit, and for *reinvested earnings* (when losses are reported). This change is aimed to ensure consistency with the national accounts statistics (paragraphs 3.30, 3.31, 10.44 of BPM6).

- In the financial account, net items are calculated as follows:

$$\text{Net items (FA)} = \text{Assets} - \text{Liabilities}$$

- Increases in assets and in liabilities are recorded with a positive sign, and decreases are recorded with a negative sign (previously a positive sign indicated a decrease in assets and an increase in liabilities, and a negative sign denoted an increase in assets and a decrease in liabilities) (paragraph 3.31 of BPM6).

- The new items of *primary income* and *secondary income* cover subitems that have previously been reported under *income* and *current transfers*, which is a crucial step towards synchronization between the statistics of the external sector and the national accounts (paragraphs 11.1-11.7 of BPM6).

- Item *financial derivatives* has been renamed to *financial derivatives (other than reserves) and employee stock options* (paragraph 6.58 of BPM6).

- The term *trade credit* is replaced by *trade credit and advances* (paragraph 5.70 of BPM6).

- Item *other assets/other liabilities* in other investment is renamed to *other accounts receivable/payable* (paragraph 5.69 of BPM6).

- The term for the financial account entry is changed to *reinvestment of earnings*, to distinguish it from the respective item in primary income, *reinvested earnings* (which continues to be used), although they are essentially identical (paragraphs 8.15-8.16 и 11.33-11.36 of BPM6).

- The net aggregates for the current and capital account and the financial account (net lending (+)/net borrowing (-)) have the same signs (they used to have opposite signs). Net errors and omissions are derived as the difference between them, and are calculated as follows (paragraph 2.24 и 3.109-3.121 of BPM6):

$$\text{Net errors and omissions} = \text{Net financial account} - \text{Net current and capital account}$$

2.2.Methodological changes and reclassifications

Within the current account of the balance of payments, the adoption of the new methodological standards had the largest impact on items *Goods* and *Services*. However, its net effect on the current account was insignificant, as it consisted mostly in reclassification of subitems.

The adoption of the new methodological requirements had a larger impact on the financial account of the balance of payments and the international investment position, and especially on direct investment and other investment data.

2.2.1 Current account

2.2.1.1. Major changes in subitems *Goods* and *Services*

BPM6 considers the change of ownership as the only criterion in the reporting of international trade, abolishing the exceptions from that criterion that existed under BPM5 (paragraphs 10.13, 10.22, 10.24, 10.41-10.44 of BPM6). The resulting changes in the distinction between trade in goods and trade in services, and the reclassifications between both items do not in principle significantly influence the current account of the balance of payments:

- Exports and imports of goods for processing were formerly reported under *Goods*, including both the value of goods as well as the fee for the service for the processing. In accordance with the BPM6 the processing fee is included in services item *Manufacturing services on physical inputs owned by others* (paragraphs 10.62-10.71 of BPM6).
- Unlike processing, merchanting of goods which was formerly reported under *Services* is now part of *Goods* - subitem *Net exports of goods under merchanting* (paragraphs 10.41-10.49 of BPM6). *Merchanting* is defined as the purchase of goods by a resident from a non-resident and the subsequent resale of the same goods to another non-resident without the goods crossing the border of the compiling economy.
- Goods for own use or to give away acquired by travelers that are in excess of customs thresholds are reported as exports/imports of *goods* (paragraphs 10.20, 10.90 of BPM6), and not under *travel*.
- Repair of capital goods was reclassified from *Goods* to *Services* (subitem *Maintenance and repair services not included elsewhere (n.i.e.)*). Construction maintenance and repairs and Maintenance and repairs of computers are excluded. (paragraphs 10.72-10.73 of BPM6).

Along with the changes connected with the stricter observation of the change of ownership criterion, the BPM6 has adopted the following changes in item *Services*:

- *Computer and information services* are no longer a separate category, but are reported together with telecommunications services (paragraph 10.141 of BPM6).

- *Postal and courier services*, formerly reported under *Computer and information services*, are already reported under *Transport* (paragraphs 10.82-10.85 of BPM6).

- *Construction* (previously construction services) is calculated on a gross basis, i.e. goods and services purchased in the country where the construction is located will be added to the service costs (paragraphs 10.101-10.108 of BPM6).

- The changes to subitem *Other business services* are related to its structure, and more detailed breakdown (paragraphs 10.159-10.160 of BPM6).

2.2.1.2. Primary and Secondary income – major changes in items *Income* and *Current Transfers*

- The sub-items of the former items *Income* and *Current transfers* (BPM5) are redistributed between the new *Primary* and *Secondary Income* items, which is an important step towards the harmonization of the external statistics with the national accounts statistics.

- The structure and contents of the new items – *Primary* and *Secondary Income* do not completely coincide with the structure and contents of the former *Income* and *Current transfers* items. *Primary income* reflects the receipt and payment of income related to the use of resources (labor, capital, land), taxes of production and imports and subsidies while *Secondary income* presents the redistribution of income (paragraphs 11.1-11.9 и 12.1-12.11 of BPM6).

- Along with *compensation of employees* and *investment income*, *primary income* now covers certain components previously included under current transfers, i.e. *taxes on products and production*, *subsidies*, and *ren.* (paragraph 11.8 of BPM6).

- *Investment income on direct investment* now covers the income between affiliates, which was previously (according to BPM) reported under portfolio or other investment. Affiliates are enterprises that are under the control or influence of the same immediate or indirect investor, but neither fellow enterprise controls or influences the other fellow enterprise (paragraphs 10.97-11.100 of BPM6).

- Income on intercompany lending between affiliated financial corporations (except insurance companies and pension funds) is now reported under other investment income (it was previously reported under direct investment income) (paragraph 6.28 of BPM6).

- Along with the changes ensuing from the implementation of BPM6, another change was introduced – interest on credits received or extended, including on intercompany credits, is already accrued monthly on the basis on respondents' declaration (through Form SPB-1) of loan specifications (interest rate, repayment schedule, outstanding amount on the reported loan). Until now only accrued interest reported by respondents on a quarterly basis (through Forms SPB-4 and SPB-4A) was included. In accordance with the double-entry principle, interest accrued is included in the financial account as well as an increase in claims/liabilities on loans (including on intercompany loans) (paragraphs 3.27 и 11.49 of BPM6).

- Income on portfolio investment according to BPM6 covers reinvested earnings of investment funds (paragraphs 11.37-11.39 of BPM6), which were previously not included under BPM5.

- The reserve assets income is reported as a separate item under *Income* (paragraph 11.109 of BPM6).

2.2.2. Capital account

- The capital account according to BPM6 provides more detailed breakdown in comparison with BPM5. The debits and credits of item *Gross acquisitions/disposals of non-produced non-financial assets* are recorded on a gross basis (paragraphs 13.7 и 13.113 of BPM6), rather than netted as in BPM5.

- Transactions related to inheritances (legacies), which were previously recorded under current transfers, are now recorded in the Capital Account (paragraph 13.31 of BPM6).

2.2.3. Financial account

2.2.3.1. Direct investment

- An essentially different approach is adopted in the reporting of direct investment. In accordance with BPM5, direct investment recording was based on the **directional principle**, thus including both the initial transaction establishing the direct investment relationship between the direct investor and the direct investment enterprise, and all subsequent transactions between them. Irrespective of whether they were related to assets or liabilities, all transactions and positions were reported depending on the initially established relationship between the transactors – Bulgarian investment abroad, or foreign direct investment in Bulgaria. Thus, direct investment was reported on a net basis (direct investors' assets minus liabilities) (Appendix 9 of BPM6).

- In accordance with BPM6 and the OECD *Benchmark Definition of Foreign Direct Investment*, with the new **Asset/Liability principle** the leading criterion is whether the transaction/position is connected with an asset or a liability of the local person, and the initial direct investment relationship between the transactors comes second. In practice, this means that direct investment is reported on a gross basis, as the other items of the financial account. This change has no impact on the values of the direct investment transactions, but their presentation according to BPM6 is completely different. Because of the analytical importance of the former method of direct investment reporting, i.e. the directional principle, the BNB will continue to compile and publish direct investment data based on that principle, in parallel with the data published following the new requirements of BPM6 (paragraphs 6.42-6.45 of BPM6).

- Another change is related to the distinction of transactions between fellow enterprises in the coverage of direct investment. Fellow enterprises are enterprises that are under the control or influence of the same immediate or indirect investor, but neither fellow enterprise controls or influences the other fellow enterprise. Transactions between fellow enterprises could previously be recorded under *portfolio investment* (equity and debt securities) or under *other investment* (loans, financial lease, trade credits and advances, or other accounts receivable/payable). In accordance with BPM5, the BNB recorded these transactions as *direct investment*, so in practice this change would not influence the direct investment data compiled in accordance with BPM5.

- In accordance with the new requirements, permanent debt between banks and intercompany lending between other financial intermediaries (except insurance companies and pension funds) is no longer included under direct investment, as it is considered a normal practice between financial intermediaries. Permanent debt transactions between banks are reported under *other investment* (paragraph 6.28 of BPM6).

- Payments of superdividends (payments that are disproportionately large relative to the recent level of earnings) will be recorded as a withdrawal of equity (paragraph 11.27 of BPM6). In accordance with BPM5, they were reported as payments of income on direct investment.

2.2.3.2. Portfolio investment

- *Portfolio investment* now covers the retained earnings of investment funds (paragraphs 11.37-11.39 of BPM6). (The data on retained earnings of investment funds are to be included in the balance of payments statistics of Bulgaria before end-2015, based on the new reporting requirements to them, in force since 2015).

- Equity in international organizations (in the form of securities) is included in *portfolio investment* (paragraph 6.32 of BPM6), and not in *direct investment*.

2.2.3.3. Financial derivatives (other than reserves) and employee stock options

In accordance with the requirements of ECB, transactions in financial derivatives are reported on a net basis. Thus:

- Financial derivatives assets are not added to the financial account assets;
- Financial derivatives liabilities are not added to the financial account liabilities;
- Net financial derivatives calculated as the difference between assets and liabilities, are added to the assets and the balance of the financial account.

2.2.3.4. Other investment

- A separate subitem *other equity* is introduced under *other investment*, where equity in international organizations (other than securities) will be recorded (paragraph 6.32 of BPM6). Such transactions were reported as direct investment in accordance with BPM5.

- A new subitem *Insurance, pension, and standardized guarantee schemes* is introduced (paragraphs 5.62-5.68 of BPM6)

- SDR allocations (that IMF members may use when in need of balance of payments support, by exchanging them for convertible currencies) are already recorded as incurrence of a liability in *other investment* (paragraphs 5.35, 6.61 и 7.70 of BPM6).

- In accordance with BPM56 and paragraph 5.118 of ESA 2010, short-term loans between deposit-taking corporations are recorded under deposits, and not loans, as previously according to BPM5. In accordance with the ECB and Eurostat requirements, all credits (irrespective of their maturity) between deposit-taking corporations are reported as deposits in the compilation of BOP statistics.

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