



Government Finance Statistics

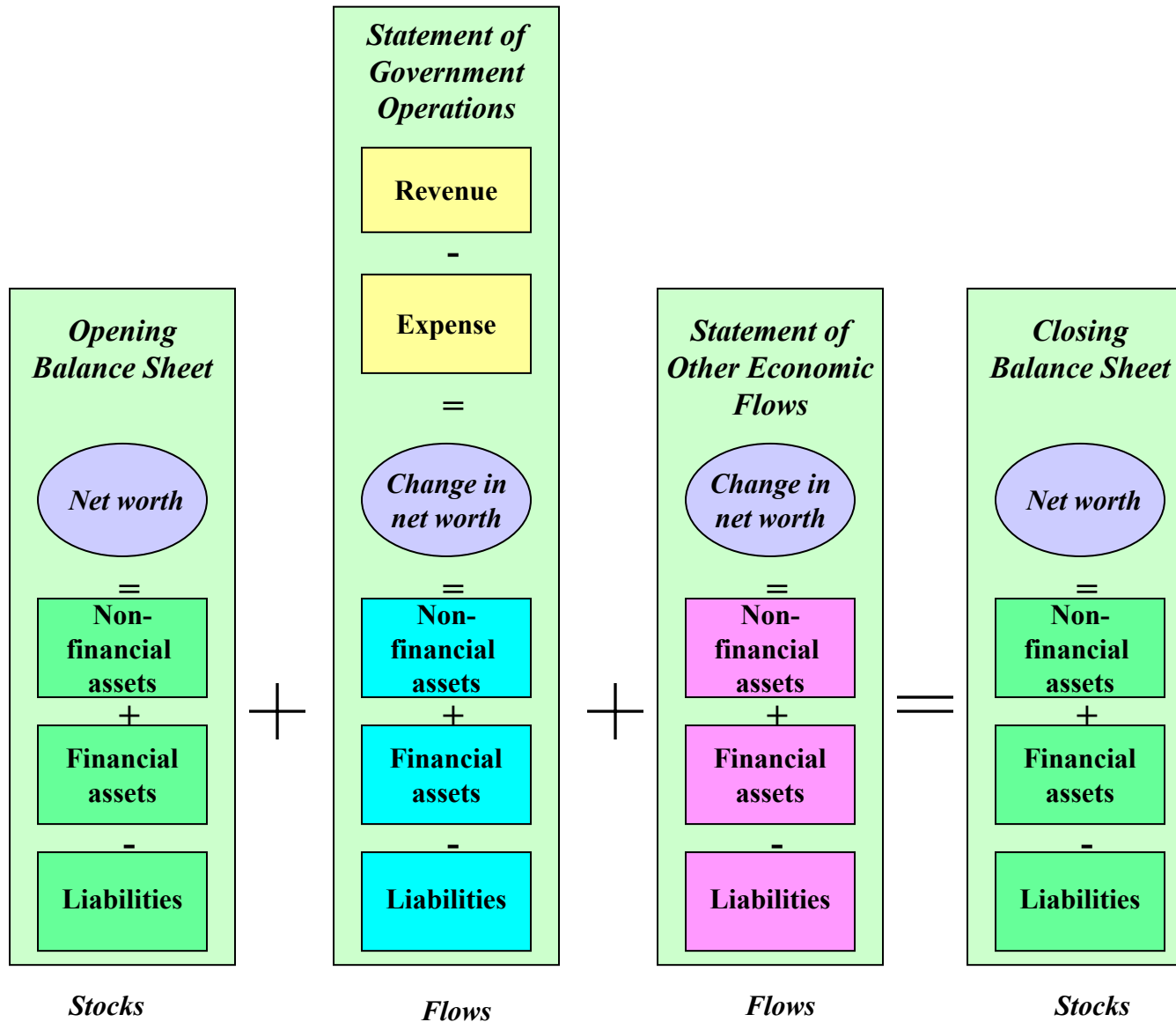
IMF Statistics Department

The Balance Sheet

Contents of Lecture

- **What is a balance sheet?**
- **Definition of assets and liabilities**
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- **Definitions and classifications of nonfinancial assets, financial assets, and liabilities**
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GFSM 2001 Analytic Framework



What is a Balance Sheet?

(1/2)

- **A balance sheet, or compilation of stocks, is a statement of the values of assets owned at a specific time and the financial claims (liabilities) held by other units against the owner of those assets**
- **Total assets minus total liabilities = net worth**
 - **Indicator of wealth**
 - **Net worth can also be viewed as the accumulation of transactions and other economic flows of all previous periods**

What is a Balance Sheet?

(2/2)

Assets	Opening balance sheet	Closing balance sheet	Liabilities and net worth	Opening balance sheet	Closing balance sheet
Non- financial assets			Liabilities		
Financial assets			Net worth		
Memoran- dum items					

Definition of Assets and Liabilities

(1/4)

- An economic asset is an entity:
 - Over which **ownership rights** are **enforced** by institutional units, individually or collectively;
 - From which **economic benefits** may be derived by its owner by holding it, or using it, over a period of time

Definition of Assets and Liabilities

(2/4)

- Ownership rights must be both **established** and **enforced**:
 - 0-0 => atmosphere and certain other naturally occurring assets
 - 1-0 => government-owned land that is so remote or inaccessible that the government cannot choose to enforce its ownership rights
 - 1-1 => national parks

Definition of Assets and Liabilities

(3/4)

- Economic assets must be able to provide **economic benefits**
 - Benefits from **use of an asset**, such as land or machinery in production
 - **Property income**, e.g., interest, dividends, rents
 - Benefits by functioning as a **store of value** (holding gains and losses)

Definition of Assets and Liabilities

(4/4)

- **Governments can create economic assets by:**
 - exercising their **sovereign power**, e.g., territorial sea, electromagnetic spectrum
 - **Regulating** or **restricting** a certain type of economic activity, e.g., landing rights at airports, retail distribution, taxis, casinos, etc.
- **Financial asset for one unit is liability for another unit**

Valuation of Assets and Liabilities

(1/4)

- **Assets and liabilities on the balance sheet should be valued**
 - as if they were acquired / incurred on the date to which the balance sheet relates, taking into account age, condition, and other relevant factors
- **Thus: all assets and liabilities should be value at their **current market value****
 - For nonfinancial assets, the value **includes** all transport and installation charges, and all costs of ownership transfers
 - Values of financial assets **exclude** these costs

Valuation of Assets and Liabilities

(2/4)

- **Different methods for valuation:**
 - **Market prices** (observable prices)
 - Investors, producers, consumers, creditor/debtor, etc.
 - Financial claims, real estate, transport equipment, crops, livestock, inventories, etc.
 - **Similar markets** (no observable prices – estimates)
 - Recent transactions (regularly, actively, and freely traded)
 - Similar assets (stock exchange, close substitutes)

Valuation of Assets and Liabilities

(3/4)

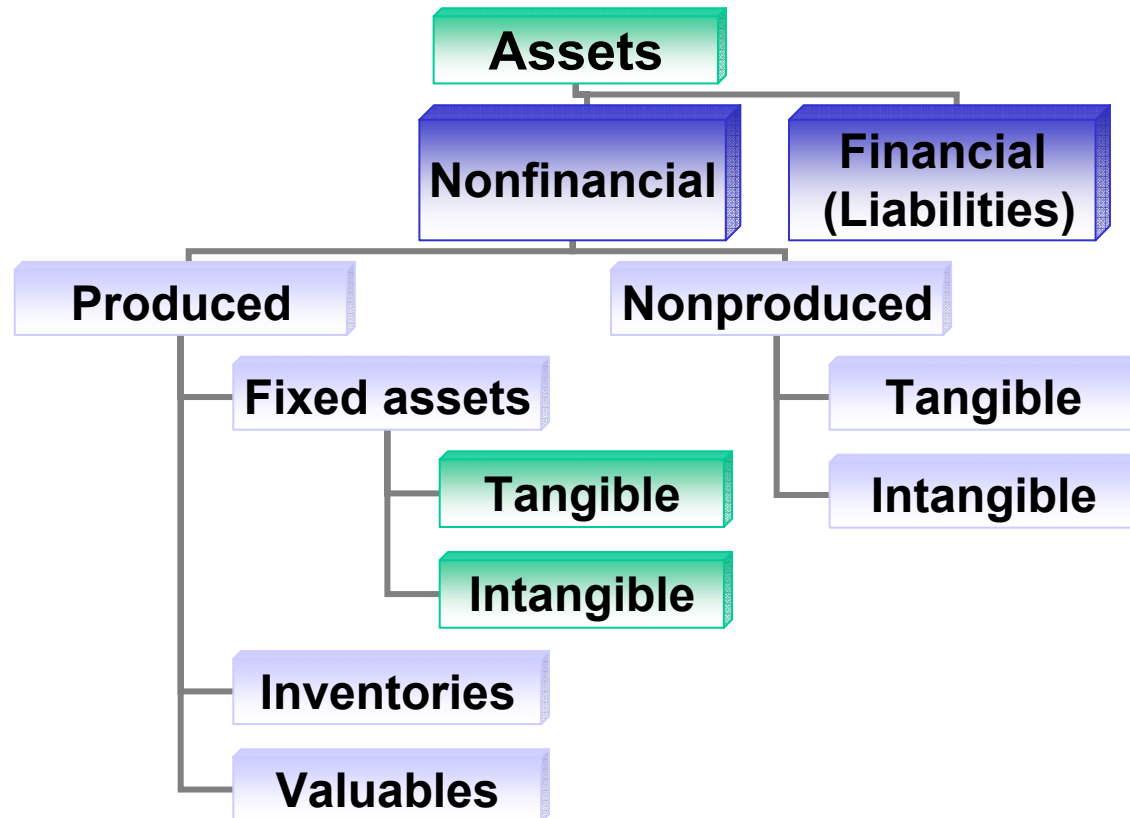
- **Different methods for valuation (continued):**
 - **Perpetual inventory method** (written-down replacement cost)
 - Initial acquisition cost
 - Appropriate revaluation (price changes)
 - Allowance for consumption of fixed capital, amortization, or depletion
 - Many fixed assets, nonproduced intangible assets, such as patented entities

Valuation of Assets and Liabilities

(4/4)

- **Different methods for valuation (continued):**
 - **Present value method** (PVM – discount rate)
 - Present value of future economic benefits
 - Certain financial, natural (timber/subsoil) assets, and intangible assets
 - **Market exchange rate**
 - Convert into national currency at market exchange rate prevailing on date to which balance sheet relates
 - Mid-point between buying and selling spot rates

Main Types of Assets



Definition of Nonfinancial Assets

(1/2)

- **Four main categories of NFAs**
 - **Fixed assets**
 - Produced assets that are used repeatedly or continuously in production processes for more than one year
 - **Inventories**
 - Goods and services held by producers for sale, use in production, other use at a later date
 - **Valuables**
 - Produced goods of considerable value acquired and held primarily as stores of value

Definition of Nonfinancial Assets

(2/2)

– Valuables (continued)

- Not used primarily for purposes of production or consumption
- Expected to appreciate (or not decline) in real value over time

– Nonproduced assets

- Tangible naturally occurring assets **over which ownership rights can be enforced** (e.g., land, subsoil assets)
- Intangible nonproduced assets (constructs of society by legal or accounting actions—patents, leases, etc.)

Classification of Nonfinancial Assets

(2/2)

61 Nonfinancial assets

611 Fixed assets

- 6111 Buildings and structures
- 6112 Machinery and equipment
- 6113 Other fixed assets

612 Inventories

- 6121 Strategic stocks
- 6122 Other inventories

613 Valuables

613 Nonproduced assets

- 6131 Land
- 6132 Subsoil assets
- 6133 Other naturally occurring assets
- 6134 Intangible nonproduced assets

Definition of Financial Assets and Liabilities (1/3)

- **Financial assets** consist of **financial claims**, monetary gold and SDRs allocated by IMF
- Financial claims are assets that entitle one unit, owner of asset, to receive one or more payments from a second unit (debtor) according to terms and conditions specified in the contract between the two units
 - **Financial claim** is an **asset** because it **provides economic benefit** to creditor by acting as **store of value** and earning **property income**

Definition of Financial Assets and Liabilities (2/3)

- **Financial claims (continued):**
 - **Contractual relationship between two units**
 - **Creditor receives additional benefits in form of interest or other property income payments and/or holding gains**
- **Examples of financial instruments that are not assets**
 - **Contingencies**
 - **Conditional arrangements not binding on both parties (e.g., guarantees, lines of credit, etc.)**

Definition of Financial Assets and Liabilities (3/3)

- When a financial claim (i.e., financial asset) is created, a **liability** of equal value is simultaneously incurred by the debtor
 - Liability (debtor) is counterpart of financial asset (creditor)
 - Exception is monetary gold and SDRs
- *Thus:* **Liabilities** are **obligations to provide economic benefits** to the units holding the corresponding financial claims

Classification of Financial Assets and Liabilities (1/2)

- **Classification of financial assets and liabilities are based on**
 - **Liquidity and legal characteristics** of the instruments that describe underlying debtor-creditor relationship
 - No underlying debtor-creditor relationship for monetary gold and SDRs
 - Liquidity → negotiability, transferability, marketability
 - **Residence** of the other party to the instrument
 - Debtor residence for financial assets
 - Creditor residence for liabilities

Classification of Financial Assets and Liabilities (2/2)

	FINANCIAL ASSETS (62)			LIABILITIES (63)	
	Domestic	Foreign	Monetary gold & SDRs	Domestic	Foreign
Total	621	622	623	631	632
• Currency & deposits	6212	6222		6312	6322
• Securities other than shares	6213	6223		6313	6232
• Loans	6214	6224		6314	6324
• Shares & other equity	6215	6225		6315	6325
• Insurance technical reserves	6216	6226		6316	6326
• Financial derivatives	6217	6227		6317	6327
• Other accounts receivable/payable	6218	6228		6318	6328

Memorandum Items to Balance Sheet

(1/4)

- **Provide supplemental information on items related to, but not in balance sheet**
 - **Debt**
 - Comprises all liabilities that require payment(s) of interest and/or principal by debtor to creditor at date(s) in the future
 - Nominal value
 - Market value
 - **Arrears**
 - Debt is in arrear when not liquidated by its due-for-payment date
 - Useful for policy analysis and solvency assessments

Memorandum Items to Balance Sheet

(2/4)

– Obligations for social security benefits

- **GFS system does not recognize liability for government promises to pay social security benefits in future (e.g., retirement benefits, health care)**
- **Show as memorandum item:**
 - Present value of social security benefits that already have been earned according to existing laws/regulations, but are payable in the future
 - Calculated similar to liabilities for employer retirement scheme

Memorandum Items to Balance Sheet

(3/4)

– **Contingent contracts**

- **Are contracts that create a conditional financial claim on a unit**
- **That is, claim only becomes effective if stipulated condition(s) arise**
- **Collectively, important for policy and analysis**
- **Can be potential assets or liabilities**
- **Examples:**
 - Government guarantees repayment of loan by another borrower (contingent liability)
 - Pending legal case in which government has claimed damages against another party (contingent asset)

Memorandum Items to Balance Sheet

(4/4)

- **Own-account capital formation**

- Compensation of employees, use of goods & services, CFC, other taxes on production minus other subsidies on production

- **Uncapitalized military weapons and weapon-delivery systems**

- Destructive weapons and vehicles, other equipment and structures that deliver such weapons are **not fixed assets**
- Useful to know their current market value for some analytic purposes

Supplemental Cross-classification of Financial Claims by Sector (1/2)

- **To fully understand financial assets and liabilities of government sector**
 - **Need to also look at sectors that have provided financing (not only type of instruments)**
- **All financial claims are associated with two parties**
 - **Can cross-classify instruments of financial claims with sector of the second party**

Supplemental Cross-classification of Financial Claims by Sector (2/2)

SECTORS

Domestic

- Other general govt units
- Central bank
- Other depository corporations
- Financial corporations n.e.c.
- Nonfinancial corporations
- Households and NPIs serving households

Foreign

- International organizations
- General government
- Financial corporations other than international organizations
- Other nonresidents