Implementation of new international standards of the balance of payments and international investment position

The Balance of Payments of the Republic of Lithuania is compiled based on the instructions of the Balance of Payments Manual (BPM) prepared by the IMF. On the basis of this Manual, the Regulation of the European Commission, Guidelines of the European Central Bank (ECB) and recommendations for external statistics requirements have been prepared and approved. They are mandatory and are applied in all of the European Union (EU) Member States. At the same time the possibility to compile and publish internationally comparable statistics has been created. In compiling foreign direct investment (FDI) statistics, the FDI compilation manual (*Benchmark Definition* (BD4) (4th edition)), approved by the Organisation for Economic Cooperation and Development (OECD), is also followed. Until 2014, in compiling the balance of payments, BPM5 issued in 1993 had been observed. With the changing world economy, emergence of free movement of capital, etc., its content is already to be revised; therefore, in view of the changes, a new, sixth edition of the Balance of Payments and International Investment Position Manual (BPM6) has been prepared and approved. The new Manual not only covers BOP transactions, but compiling of the balance of international investment position as well. BPM6 has been harmonised with the System of National Accounts (SNA 2008) and the European system of national and regional accounts (ESA 2010).

Following BPM6 recommendations, the balance of payments and the international investment position for Q1 2014 will be published in Lithuania, as in the entire EU, in June 2014. Major changes are related to FDI, foreign trade and services calculations. Moreover, income (primary and secondary) is presented differently, more detailed indicators of financial assets and liabilities are included in addition.

General BOP changes in applying BPM6

Some new terms such as *primary* and *secondary income* have been used in the Manual. A new, wider term *personal transfers* has been used; it also comprises workers' remittances.

The application of BPM6 requirements does not entail major changes in the current account balance. However, in an overview of specific goods and services accounts, greater changes are projected due to a new treatment of *merchanting of goods*, application of the economic ownership principle, and inclusion of financial intermediation services indirectly measured (*FISIM*) into financial services. This, also new treatment of the income allocated to holders of investment fund shares will affect the primary income balance. Changes in the capital account are mainly related to the treatment of migrants' transfers.

In the financial account, the major change in the indicators to be presented is related to FDI. The directional principle, which until now had been applied in the balance of payments and investment position, is moved to the gross concept (the assets and liabilities are shown without netting).

In addition, for practical considerations (how to read and understand figures), it was decided to change the use of the negative sign in the current and capital accounts, i.e. both credit and debit records will be presented with the positive signs, except in those cases when the transaction has a negative value, for example, a reinvested loss. Moreover, the negative sign of a flow, suggesting asset growth abroad, and the positive sign, suggesting asset contraction, will no longer be used in the financial account. Hence, positive figures will signify growth in assets or liabilities, while negative figures, on the contrary, a decline in them. Balancing indicators such as *current account balance* or *net lending (net borrowing)* will always be treated as the difference between credit and debit or assets (*net acquisition of financial assets*) and liabilities (*net incurrence of liabilities*).

Methodological BPM6 changes

In implementing BPM6 requirements, the methodological principles of compiling the balance of payments are the same, only some important aspects are changing or emerging. A new term, *economic ownership,* begins to be used. Change in economic ownership is the basis for setting a time of recording on an accrual basis for transactions in goods, non-produced non-financial and financial assets. Change of economic ownership transfers all types of risk, rewards and all ownership rights and liabilities. New concepts of current account items, *primary income* and *secondary income* begin to be used.

According to BPM6, arrears on principal or interest was not imputed as a transaction and, they are not reclassified to short-term debt under other financial liabilities (as had been required under BPM5), but are kept under the respective instrument (arrears on principal under original instrument, accrued interest – offsetting entry under respective instrument).

The reallocation under BPM6 of some sectors, related to non-financial holding companies (now they will belong to the financial sector), will not have a significant influence on the presentation of the balance of payments, as they will be included under *Other sectors. S*pecial purpose entities and other similar structures are always treated as separate units, if these vehicles and the owners of these vehicles are residents of different territories.

I. Current account

Goods and services

The greatest changes under BPM6 are related to the items *Goods* and *Services*, however there will be no major changes in the overall balance of goods and services. Some types of services are presented in greater detail, which corresponds to the growing needs of users of statistics and compilers of national accounts, as the BOP data of the rest of the world is the main source for GDP calculations.

Under BPM6, merchanting of goods began to be treated as goods, not as trade-related services. Purchasing of goods from non-residents and selling them to other non-residents (the above-named goods must not appear in the purchasing country) are included into the part *Net Export of Goods* under *Merchanting.* Purchase of goods is recorded as exports with the negative sign, while the sale of goods is treated as export of goods with the positive sign; however, the difference between the purchase of goods and sale of goods will have the same effect on the current account as before.

Manufacturing services are related to the globalisation of the economy and development of outsourcing; therefore, the production chain as often as not takes place in even several different countries. Manufacturing services cover processing, assembly, labelling, packing of goods undertaken by other enterprises that do not own the goods concerned, but the owner of the goods pays a fee (price) for the service performed. In these cases, there is no movement of goods between the processor and owner of the goods, so only the acquisition or sale of already processed goods is recorded under the item *Goods*. Under this item, the movement of goods is only recorded when the economic ownership of goods changes, and not when goods are physically sent to another country for processing without their economic ownership changing. In those economies where the processing flows in the country and beyond are sufficiently large, such new treatment according to BPM6 will reduce the overall volume of the export and import of goods, while increasing the export and import of services at the same time. The new manual enables to more precisely record the essence of economic transactions — services will increase by the part of the value of manufacturing services performed and only the fee for the processor's performed manufacturing service will be included in the BOP section *Services*.

Due to the same reason (economic ownership remains unchanged), goods exported or imported for repair have also been transferred to the item *Services*. The value of their repair will be included in the indicator *Technical Maintenance and Repair Services.*

Goods procured in ports by carriers will be included in the indicator *General merchandise data.*

Structural changes in the BOP item *Goods* *

Goods (BPM5)	
1. Exports	2. Imports
1.1. General merchandise	2.1. General merchandise
1.2. Goods for processing	2.2. Goods for processing
1.3. Repairs on goods	2.3. Repairs on goods
1.4. Goods procured in ports by carriers	2.4. Goods procured in ports by carriers
1.5. Nonmonetary gold	2.5. Nonmonetary gold

Goods (BPM6)	
1. Exports	2. Imports
1.1. General merchandise data	2.1. General merchandise data
1.2. Net exports of goods under merchanting	2.2. Nonmonetary gold
1.2.1. Goods acquired under merchanting	
1.2.2. Goods sold under merchanting	
1.3. Nonmonetary gold	

Under BPM6, FISIM are included into the indicator *Financial Services.* Monetary financial institutions provide services to those who borrow funds and depositors, so FISIM is the difference between the interest actually paid or received and the market interest rate. These indirect payments, recorded in the interest part and only applied to loans from financial institutions and deposits held with them, must be singled out as service charges. Pure interest (without the financial intermediation service fee) is recorded in the item *Primary income.*

Margin received by financial intermediaries, when market brokers and financial dealers include all or only some of their services into the price of financial instruments being procured or sold, is additionally included into *Financial Services.*

Post and courier services are included into the indicator *Transportation.*

Structural changes in the BOP item *Services* *

Services (BPM5)	
1. Exports	2. Imports
of which merchanting and other trade-related services ↓	

Services (BPM6)	
1. Exports	2. Imports
of which:	of which:
Manufacturing services ↑	Manufacturing services ↑
Maintenance and repair services n.i.e. ↑	Maintenance and repair services n.i.e. ↑
FISIM ↑	FISIM ↑

Primary income

Apart from the already mentioned FISIM calculations, the indicators of BPM5 item *Income* are included into, and some indicators of the item *Current transfers* (taxes on products, subsidies and rent) are additionally allocated to the item *Primary income*. This change, embedded in BPM6, has been harmonised with national accounts. Major contribution to primary income will stem from the new treatment of FDI flows and reinvestments of investment fund shares. Under BPM6, all income (or actually allocated income (dividends) or reinvested income), received from investment fund shares is allocated to holders of these shares and is included into the item *Primary income*.

Secondary income

This income corresponds to the composition of the account *Current transfers* presented in BPM5. A new concept, *personal transfers*, is introduced. It comprises all current transfers performed in cash or in kind between resident and non-resident households irrespective of the relation between these households and the source of income. Workers' remittances are included into the indicator *Personal transfers*. Secondary income will also be affected by the expansion of the volume of current transfers related to pension agreements and standardised guarantees.

II. Capital account

Under BPM6, with the change of individuals' residency, personal property and holdings of the individuals' other assets are not treated as a transaction, i.e. is not considered as the change of ownership of the assets. Where the residence of the owner changes, but the ownership of asset remains unchanged, the cross-border changes in assets and liabilities between the different economies are recorded in the international investment position by reclassifying them (other changes in volume). Under BPM5 it was contrary — the change of individuals' residence was treated as a transaction.

Moreover, in the *Capital account*, the indicator *Non-financial non-produced assets* decreased by the share of patents and copyright, as it is treated as part of produced assets; it must therefore be included into the *Research and development services*.

III. Financial account

Under BPM6, the concept *capital* is no longer used in the *Financial account.* The classification of institutional sectors and financial assets and liabilities remains the same as the classification of national accounts. The sector financial corporations is broken down into subsectors. A new indicator, which balances the financial account — *Net crediting* or *Net borrowing* has been introduced.

Direct investment

Basic changes are related to FDI recording. In BPM5, FDI was presented according to the directional principle (the country's investment abroad and non-residents' investment in the country were recorded on a net basis). According to the new methodology, the total flows of assets and liabilities are presented. It means that total assets abroad and total foreign liabilities are recorded separately, without netting these flows according to the direction of investment. The example could be loans granted to a non-resident direct investor. By applying the directional principle, these foreign assets are subtracted from the current liabilities to the non-resident, while applying the assets and liabilities principle, these loans are recorded on the *Assets* side, current liabilities — on the *Liabilities* side. This increases both acquisition of net financial assets and incurrence of net liabilities, while not affecting net FDI (flows and balances).

Structural changes in the BOP item *Direct Investment* *

Direct investment (BPM5)	
1. Abroad	2. in Lithuania
1.1. Equity capital	2.1. Equity capital
1.1.1. Claims (+)	2.1.1. Claims (–) ↓
1.1.2. Liabilities (–) ↓	2.1.2. Liabilities (+)
1.2. Reinvestment (+)	2.2. Reinvestment (+)
1.3. Other capital	2.3. Other capital
1.3.1. Claims (+)	2.3.1. Claims (–) ↓
1.3.2. Liabilities (–) ↓	2.3.2. Liabilities (+)

Direct investment (BPM6)	
1. Net acquisition of financial assets	2. Net incurrence of liabilities
1.1. Equity, other than reinvestment of earnings	2.1. Equity, other than reinvestment of earnings
1.1.1. In direct investment enterprises (+)	2.1.1. In direct investment enterprises (+)
1.1.2. In a direct investor (+) ↑	2.1.2. In a direct investor (+) ↑
1.2.3. Between fellow enterprises (+) ↑	2.2.3. Between fellow enterprises (+) ↑
1.2. Reinvestment of earnings (+)	2.2. Reinvestment of earnings(+)
1.3. Debt instruments	2.3. Debt instruments
1.3.1. In direct investment enterprises (+)	2.3.1. In direct investment enterprises (+)
1.3.2. In direct investor (+) ↑	2.3.2. In direct investor (+) ↑
1.3.3. Between fellow enterprises (+) ↑	2.3.3. Between fellow enterprises (+) ↑

It should be noted that the directional principle will continue to be applied in FDI statistics as a means of detailed investment analysis.

BPM6 presents investment of fellow enterprises. The concept of direct investor and indirect investor enterprise remained unchanged. Fellow enterprises are units that are controlled by a direct investor, but do not control or have any influence on each other (they are not themselves in a direct investment relationship). According to the extended directional method, assets and liabilities between fellow enterprises are allocated to inward and outward direct investment depending on the residency of the ultimate parent.

Insurance technical reserves are allocated to FDI (debt instruments), while all debt transactions (loans, financial derivatives, clearing accounts) between financial corporations (MFIs, investment funds, other financial intermediaries, except insurance corporations and pension funds), are not allocated to FDI transactions.

In order to increase the analytical value of FDI data, BPM6 recommends to always treat special-purpose entities and other units of a similar structure as separate units, if the such entities and the owners of these entities are residents of different territories not engaged in economic activities, but manage the main share of foreign assets. Moreover, it is recommended that direct investment inflows into the country are recorded according to the ultimate beneficiary principle.

Portfolio investment

A major change in the content of portfolio investment is related to the treatment of the accrued income of mutual funds. All income received from investment fund shares (irrespective of whether it has been allocated or not) should be allocated to the holders of these shares. The treatment of income generated by investment fund shares is similar to that of FDI income.

Other investment

Other investment will be affected most by a different treatment of fellow enterprises. Under BPM6, the financing of fellow enterprises should be allocated to *Direct investment*, not to *Other investment*, as previously. Transactions of other equity securities not allocated to *Direct* or *Portfolio investment* (e.g., equity participations in international organisations) are now separately included into the indicator *Other investment.* The new allocation (or cancelation) of special drawing rights is now included into the indicator the *Central Bank's Net Incurrence of Liabilities.* Amounts receivable and amounts payable are singled out from insurance reserve (including re-insurance), pension and standardised guarantees, and are presented in greater detail.

Official reserve assets

BPM6 does not present any methodological changes to the calculations of official reserve assets.

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*Changes marked in red font.

↑ – marked indicators that are included in the item; ↓ – marked indicators that are excluded from the item.