IMF COMMITTEE ON BALANCE OF PAYMENTS STATISTICS

CURRENCY UNION TECHNICAL EXPERT GROUP (CUTEG)

ISSUES PAPER (CUTEG) # 10.1

RELEVANCE OF *BPM5* STANDARD COMPONENTS FOR A CURRENCY UNION MEMBER COUNTRY, PARTICULARLY RESERVE ASSETS

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Relevance of *BPM5* standards components of a currency union member country, particularly reserve assets

1. For a currency union (CU) there is a need to compile a balance of payments statement, not least to support economic policy making by the CU institutions and economic analysis more generally. Experience has shown the need for individual countries within the CU to also produce a balance of payments statement (BOP). Economic policy makers seem to require such information, while compilation of the national accounts data requires balance of payments information. Nonetheless, an issue arises as to the relevance of the standard components for a member country of a CU. What standard components should a national BOP be based upon? In particular, does the functional category of reserve assets lose its analytical meaning when compiling a BOP statement for a country belonging to a CU? This paper proposes different options to deal with this issue, and briefly sets out the implications in terms of defining standard components for a CU's member country's BOP/IIP.

Current international standards for the statistical treatment of the issue

2. In *BPM5* there is little discussion of the relevance (if any) of compiling each of the standard components in the national data of a CU member country. Indeed, member countries of the IMF that are also members of a CU are requested to provide the IMF with a full balance of payments statement based on *BPM5* standard components. Experience suggests that national information on goods and services, income, transfers, direct investment, portfolio, financial derivatives and other investment on a country basis remain of relevance to policy makers. This stresses the link between BOP and the national accounts, as well as the monetary surveys, and the government finance statistics. However, an issue has arisen over the relevance of reserves data for countries in a currency union. The rest of this paper focuses on this issue.

3. Under current methodology (paragraph 424 of the *BPM5*) the functional category of reserves assets include those foreign assets readily available to and under the control of monetary authorities for direct financing of payments imbalances, for indirectly regulating the magnitude of such imbalances through intervention in exchange markets to affect the currency exchange rate and/or for other purposes. More recent work related to the Reserves Data Template (*Guidelines for International Reserves and Foreign Currency Liquidity—Guidelines*) emphasizes that the assets must be denominated in foreign currency (paragraph 66 of the *Guidelines*) and liquid or marketable (paragraph 65).

4. Further, the general item of reserves is composed of five categories of foreign assets of which two—SDRs and reserve position with the Fund—are country specific and are only classified as reserve assets, and another—gold—which can only be included in the financial account as a reserve asset.

Concerns/shortcomings from the current treatment.

5. Neither *BPM5* nor the *Guidelines* provide any explicit guidance on the way reserve assets of a CU should be reflected in the balance of payments statement of a CU country. However, in *BPM5* there is an implication that the countries in a currency union record holdings of reserve assets: it is recommended that each national office in a currency union acts as the central bank and that the financial assets and liabilities of a regional central bank (including presumably reserves) be allocated among national offices in proportion to the claims that such offices have on the regional central bank (paragraph 90).

6. Against this background, in June, CUTEG provisionally agreed that only assets considered reserve assets at the CU level could be classified as reserve assets in the national data. This view was taken on the grounds that the concept of reserve assets in a CU has a unitary nature, meaning that only one definition should apply for the whole CU. Further, CUTEG also provisionally agreed that the Currency Union Central Bank (CUCB) should be regarded as an institutional unit in its own right, nonresident of any specific economy but resident of the CU. In other words, its assets and liabilities are not to be allocated to member countries of the CU. These provisional decisions provide clarification as well as change to the *BPM5* approach. The rest of this note is based on the assumption that these provisional decisions will be endorsed at the December 2004 meeting.[1]

Possible treatments of the issue

7. In this paper, it is assumed that only if the monetary authorities of a member country owns and/or controls[2] foreign currency assets that meet the criteria of ready availability and control can a case can be made for including those assets in reserve assets at the national level. Further, given the provisional decisions taken by CUTEG, there are various instances, where foreign assets at the national level are not reserve assets. First, if the foreign assets are denominated in the currency of the union they cannot be classified as reserve assets, because they are not foreign currency claims (see Issues paper12). Second, if the foreign currency assets are claims on other residents of the CU, then by having only one definition of reserves for the whole CU, these assets should be excluded from reserve assets at the national level (except perhaps for foreign assets held by domestic banks but "controlled" by national monetary authorities—this instance is relevant to footnote 2). Third, if a national monetary authority transfers ownership of reserve assets to the CUCB (and has a claim on the CUCB as a consequence), then these reserve assets are no longer considered owned by the national authorities and so should not be recorded as reserve assets at the national level (Issues paper 15).

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[1] The issue of whether to create a notional national monetary authority in a centralized system and hence, inter alia, allocate some reserves to this unit is discussed in issues paper 3.

[2] In issues paper 10 it is noted that the issue of including within reserve assets foreign assets over which monetary authorities have control but not ownership is of general relevance, regardless of whether a country is in a CU or not, and so should be decided in the wider discussion of the methodology for reserve assets.

8. The question arises as to whether the concept of reserve assets is relevant at member country level at all but could be said to exist at the CU level only—that is a different classification approach could be taken to the same assets at the country and CU levels. Under this logic, even if the foreign assets are owned by the national monetary authorities and meet the definition of reserves assets at the CU level, they should not be classified as reserve assets at the national level because, in particular, foreign exchange policy is primarily decided at the CU level. In other words, this view would conceptually follow the notion that since reserve assets are held to meet balance of payments needs and influence the exchange rate, this functional category only makes sense at the level of the CU. Instead, these assets could be allocated to the relevant items of the financial account ("Portfolio investment" and "Other investment"). But this view could only apply for foreign exchange (and other claims) holdings. For the SDR holdings and the reserve position with the Fund, they have to be classified as national reserve assets as they are country specific assets. Similarly, financial gold owned by a monetary authority cannot be regarded as anything other than as a reserve asset in the financial account.

9. The alternative position is to maintain a consistent classification approach at country and at CU level. In other words, if an asset meets the definition of a reserve asset at the CU level and it is owned by and/or under the control of the national monetary authorities, it should be recognized as a reserve asset in the national data. This approach would not exclude from the national reserve data, assets owned by and under the control of the national monetary authorities that might also be "controlled" by the monetary authorities of the CU. In this way the data for reserve assets published by the member countries plus the data for reserves held at the CU level—e.g., the CUCB—would equal the total for the reserve assets of the CU. In effect, this approach makes no judgement on the analytical relevance of data on reserve assets owned and/or controlled at the national level—such as whether some or none can be used to meet a national balance of payments need or the degree of influence the national monetary authorities may or may not have over the use of the assets—except that it considers that it is analytically meaningful to identify as reserve assets those foreign assets of the individual countries that are considered as reserve assets of the CU.

4. Points for discussion

- ***Do CUTEG members agree that given experience, we should not be examining the issue of the need or not for a balance of payments statements at the national level for countries in a CU?***

- ***Do CUTEG members consider the need to question the relevance of information on goods and services, income, transfers, direct investment, portfolio, financial derivatives and other investment at the national level for countries in a CU?***

- ***Do CUTEG members have any problems with the list of instances where foreign assets at the national level are not reserve assets (paragraph7)? Are there additional instances to add?***

- ***Do CUTEG members prefer that the classification of foreign assets as reserve assets be said to be relevant at the CU level only (paragraph 9) or that a consistent approach at country and at CU level to the classification of reserve assets be adopted (paragraph 10)?***