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Feasibility and Challenges of the Russian Federation for Participating in the Exercise on Improving the Sectorization of Nonresident Issuers in the Context of CPIS Reporting

Feasibility and challenges of the Russian Federation for participating in the exercise on improving the sectorisation of nonresident issuers in portfolio investment

The Central bank of the Russian Federation (the CBR) has been participating in the CPIS survey since 2001. The report covers the mandatory table, as well as the encouraged tables on the currency structure of portfolio investment, the sector of holder and the sector of issuer.

According to the prescribed timelines, the CBR submits the data to the IMF on a semi-annual basis. Since the beginning of 2017, the Bank of Russia has launched the survey on a quarterly basis and, therefore, has now been ready to provide the data to the IMF in the same terms.

The CPIS data collection is based on the security-by-security approach. The underlying sources of this information comprise of the reporting forms from end-investors, custodians, and investment managers. The data are used for the compilation of the balance of payments and international investment position of the Russian Federation.

The Bank of Russia has been disseminating the data on the sectoral structure of nonresident issuers in accordance with the CPIS framework (table 5 of the report) since the information as of the end of June 2016.

The process of nonresident sector classification implies the following steps.

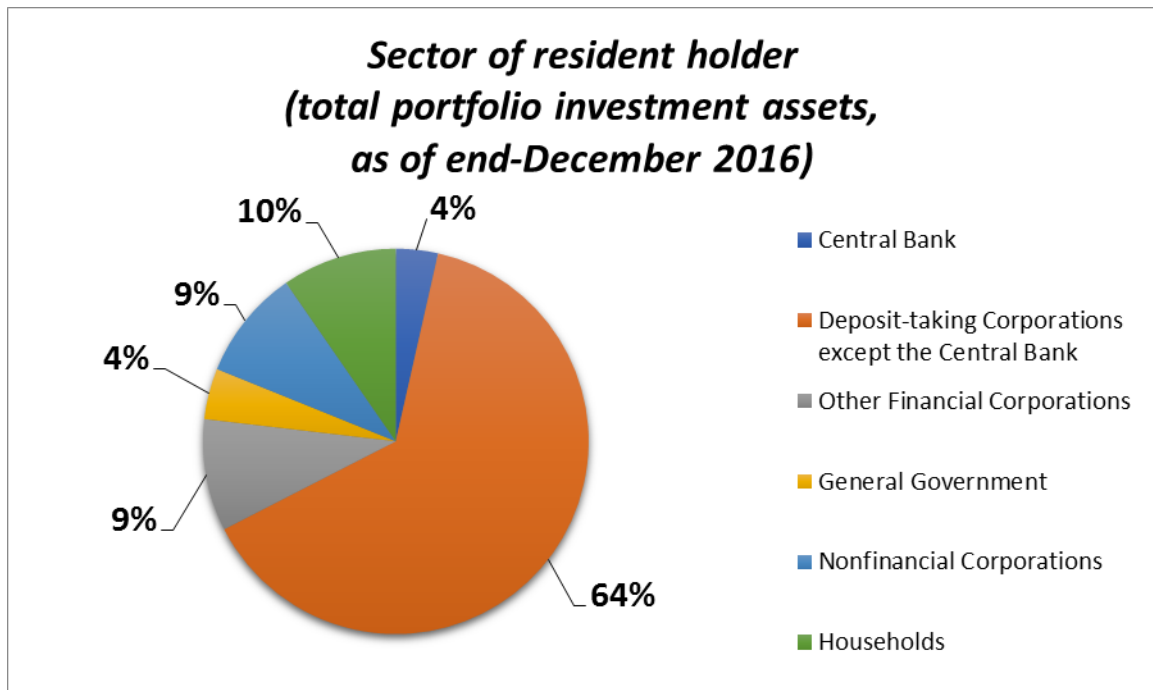
The first step implies that the CBR has elaborated and has been maintaining the data bank for the raw data on the portfolio investment of the Russian residents in foreign securities.

There are several data sources:

1. For the Central bank sector the data are derived from the CBR's investment portfolio, comprising of the securities, which are not included in the international reserves:
 - 1.1 Securities under REPO agreements;
 - 1.2 Securities, which cannot be attributed to the international reserves.
2. For the sector of deposit-taking corporations, the information is collected on a quarterly basis from the banks' reports on their own portfolio investment in foreign securities. The reporting implies the full coverage of respondents, the mandatory basis, it doesn't have thresholds for reported sums and purports monetary penalties for failures to submit the required data.
3. The Bank of Russia collects the information on other financial intermediaries, except insurance companies and investment funds, by applying the quarterly samples. The list of responding organisations is formed on the basis of additional data sources such as the ITRS data, the financial reports of companies and other wellsprings. This sample is derived and specified by the CBR at the beginning of each quarter from the complementary information about the investment of these companies in foreign securities. There is the same legal framework for the data collection as for deposit-taking corporations.
4. For investment funds and insurance companies, the Bank of Russia receives the data on securities holdings from the mandatory reports about the asset structure of these companies, which includes, in particular, the security-by-security information for both domestic and foreign securities. The reporting forms are submitted by all organisations to the CBR on a monthly basis. The principles of full information, mandatory reporting and the fines system are applied by the Bank of Russia for investment funds and insurance companies in the same way as for other supervised organisations.
5. The sector of nonfinancial and other financial corporations, except other financial intermediaries, which are not subject to the CBR's supervision, is compiled by using the following sources of information:

- 5.1. Samples for end-investor surveys devoted to portfolio investment in foreign securities. The list of respondents is determined by the Bank of Russia at the beginning of each year and then new companies are added to the sample on a quarterly basis. This list is formed with the usage of the ITRS data, the financial reports of companies and other sources of information. Reporting is not mandatory, however, in the future the CBR is planning to make it compulsory.
- 5.2. Custodian and investment manager reports about portfolio investment of their clients in foreign securities are submitted to the CBR on a quarterly basis. The framework implies mandatory reporting with the full coverage of respondents and no thresholds for reported sums.
6. The Bank of Russia receives the data on the securities holdings of NPISHs and households from custodian and investment manager reports which do not also have any thresholds.
7. The government sector is compiled by using custodian reports within the same general reporting framework with mandatory reporting, the full coverage of respondents and no thresholds for reported sums.

For the purpose of the elimination of the double counting of securities, the CBR has added an indicator of the organisation, in which securities are held in all data sources (reporting forms submitted by deposit-taking corporations, other financial intermediaries, including insurance companies and investment funds, as well as nonfinancial organisations and other financial corporations). This attribute enables the Bank of Russia to account for securities owned by the Russian residents and kept in foreign custodians. In addition, it helps to maintain the consistency between companies' reports and the information from the custodian system.



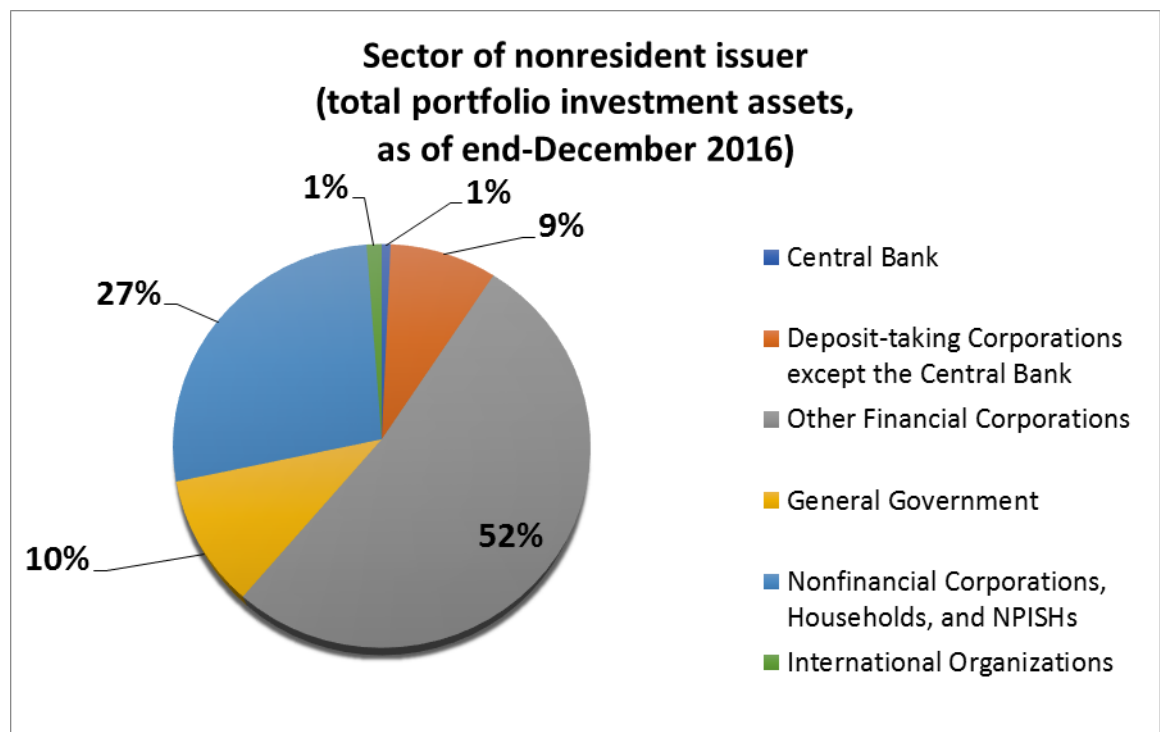
Given the information, mentioned above, the structure of the data bank contains the following main characteristics derived from the indicators filled in by respondents:

1. Security type (equity or debt securities);
2. Identification number (ISIN);
3. Quantity of securities;
4. Security currency;
5. Nominal price of a security (if applicable);
6. Market price of a security;
7. Country of residence of issuer;
8. Maturity for debt securities (short-term and long-term debt instruments);
9. Identifier of the organisation in which securities are held (domestic custodians or foreign custodians or self-custody);
10. Sector of resident holder aggregated by each security for custodian and investment manager reports (non-financial corporations, other financial corporations, general government and households);
11. Sector of nonresident issuer.

The requirement to submit the data on the sector of nonresident issuer has been introduced by the Bank of Russia in the reports of deposit-taking corporations since 2012, in the reports of other financial intermediaries and nonfinancial corporations since 2015.

There is the following breakdown of sectors of nonresident issuers in reporting forms:

1. general government;
2. monetary authorities;
3. deposit-taking corporations;
4. insurance companies and pension funds;
5. money market funds;
6. other financial corporations, which consist of all corporations and quasi-corporations primarily engaged in financial intermediation except depository corporations, insurance corporations and pension funds;
7. nonfinancial corporations and households.



The methodological guide for reporting organisations issued by the Bank of Russia contains full contact information of the CBR's specialists and clear recommendations for compilers on the classification of sectors of nonresident issuers, which are based on CPIS Guide (Second Edition). The CBR provides respondents with the full methodological

assistance in case of difficulties, arising from the classification of nonresident sectors, faced by the reporting agents. Besides, the CBR's specialists provide respondents with training programs on a regular basis.

The reporting organisations submit the data on the sector of nonresident issuer to the Bank of Russia only for statistical purposes, which, in turn, creates additional burden for them. The current supervision system and the requirements of compulsory financial reporting do not call for such detailed information.

Moreover, the sectoral classification of nonresident issuers for the data submitted by custodians is performed by the CBR itself, as these organisations have not yet been ready to provide the data of good quality. This situation arises from the fact that the main function of the Russian custodian system purports the registration of the ownership rights on securities, but not the collection of additional analytical data on securities holdings kept in the system. Some small custodians do not have the access to global analytical systems, providing international news, trade facilities and financial information, such as Bloomberg or Thomson Reuters, therefore, the manual classification of sectors of nonresident issuers is difficult for these companies.

The second step devoted to the sectoral breakdowns is connected with data checks, making adjustments to submitted information and data enrichment.

There are several additional sources of information used by the Bank of Russia in the process of classifying the sectors of nonresident issuers.

- i. global analytical systems with financial software, financial market data, and media (for instance, Bloomberg or Thomson Reuters);
- ii. commercial specialised databases (for example, Interfax, BvD Orbis and CBONDS);
- iii. Moscow Exchange (MOEX), including the data provided by the National Settlement Depository;
- iv. Other Internet sources.

The presence of the ISIN code significantly simplifies the process of checking the data on sectors of nonresident issuers. Currently, approximately 95% of foreign securities, representing portfolio investment of the Russian residents, have the ISIN code. The classification of such financial instruments is mostly performed automatically by applying

global analytical systems. This approach is targeted on the reduction of the manual part of the classification process.

The software used in the CBR's system allows the automatic downloads of data on the sector of nonresident issuer from the global analytical systems. The computer system checks the sector from the end-investor reports and enriches the data from custodian reporting forms. In case of discrepancies between the data from the analytical systems and the information contained in the end-investor reports the CBR's experts perform additional data checks by using all available sources.

The technical peculiarity of this work implies that for money market fund classification it is necessary to use the sequential set of criteria in comparison with other sectors for which it is enough to apply only the industry description.

However, the approach, described above, has a set of limitations.

The global analytical systems cannot ensure the full coverage of requested securities, which have the ISIN code, some of them cannot be found in the databases of Bloomberg or Thomson Reuters.

In some cases these systems provide contradictory information on the same securities since the classification of sectors is made by the experts of the companies by using different sources of data and is, to some extent, subjective.

Many conduit companies are classified by using the sector of the parent companies on behalf of which they issue securities.

Sometimes the organisations with a significant share of the government control are included in the general government sector.

A standalone issue arises from the classification of holding companies, which can be classified as nonfinancial organisations or other financial organisations depending on their primary activity (paragraphs 4.84 and 4.85 of the BPM6). The experts of the global analytical systems and the CBR do not have enough information to classify these companies in the right way. This may be the reasons for discrepancies between the Bank of Russia classification for holding companies and the information from the CPIS reports of other countries, participating in the survey.

Thereby, even given the usage of automated process based on the databases of the global analytical systems, there is a strong need for manual checks of the compiled data.

When there are no ISIN codes for reported securities, the volume of manual work increases significantly. Firstly, the specialists of the Bank of Russia connect the information about the same securities received from different reports. This process is partially automated due to the fact that the name of the issuer can be written in several ways. Then, the CBR checks the correctness of the sector classification.

The third step purports the compilation of the CPIS report and its submission to the IMF.

After all data checks the final report devoted to portfolio investment of the Russian residents in foreign securities is generated in the prescribed format.

Given the international recommendations on confidentiality issues for data dissemination, the approach to data publication can be conditionally divided into two parts.

The first part implies that the requirements of the OECD presented in the «OECD Benchmark Definition of Foreign Direct Investment» have to be met.

The second part is connected with the secondary confidentiality, which should be done for all data presentations and breakdowns by sector of nonresident issuer, instrument and country of issuer, given the final goal to uncover the top level aggregates (for example, the portfolio investment in one country) by covering the minimum amount of details in encouraged breakdowns.

This mechanism takes into account the confidential indicators, which are made before the current step of the process in order to ensure cross-table confidentiality.

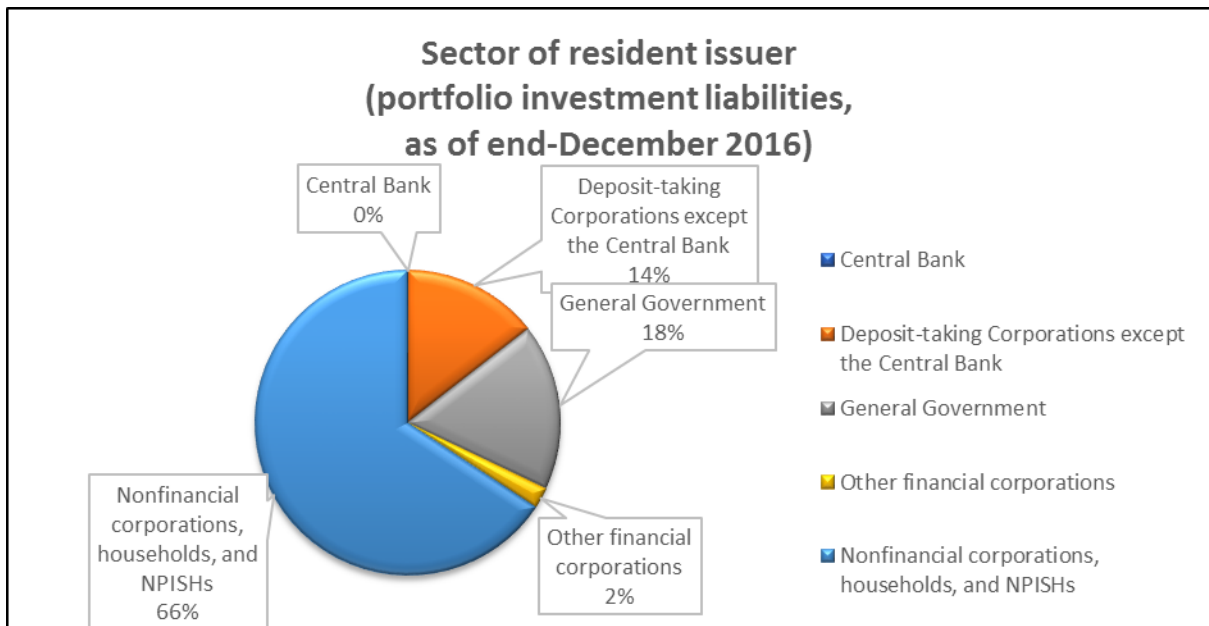
The primary confidentiality is performed in the Bank of Russia automatically, the secondary confidentiality is made in a semi-manual way (the mix of manual amendments and Excel macros). However, the CBR is planning to develop an automated system, which will use a multidimensional table (cube) for confidentiality indicators with the maximum breakdown on the «from whom to whom» level (sector of issuer versus sector of holder).

However, with the rising granularity of data the degree of confidentiality increases. Given the growing number of primary characteristics for each statistical indicator, the probability of using «C» (confidential) for it redoubles. Therefore, the attempt to join all indicators together in one matrix (security type-country of issuer-holder-issuer) may lead to the prevailing number of «C» in this table.

The usage of different sources of data by the CPIS compilers from reporting countries may result, in our opinion, in information asymmetry for final aggregates and sector breakdowns, which, inevitably, will reduce the consistency of the data and, in turn, the analytical value of this information.

Given the described situation, the Bank of Russia fully supports the initiative on the part of the IMF to organize a centralized exchange of information across economies aimed at enhancing the sectorization of nonresident issuers of securities held by domestic investors. The Bank of Russia is ready to submit the data on the sectoral belonging of the Russian securities issuers. The CBR has a full access to the Russian business register and maintains its own register of other financial intermediaries. The Bank of Russia supervises all deposit-taking corporations and almost all other financial corporations.

The remaining part of other financial corporations, which formally do not have a financial market participant license, is classified by the CBR by using the data on the code of the primary economic activity of the company, assigned by the Russian Statistical Agency (Rosstat). Thus, the Bank of Russia is able to classify the sector of the Russian securities issuers at a high level of quality.



Some difficulties, in our opinion, may be encountered in the future if the Russian securities do not have the ISIN code. Besides, the differences in the written name of the company from several sources of information, in Russia there are many companies with the

same official name. For instance, apart from the public company Vimpelcom, there are more than 10 companies, which have this word as a part of their official names. Nevertheless, the Bank of Russia supposes that this problem refers mainly to small and medium enterprises, which raise a small amount of foreign portfolio investment.