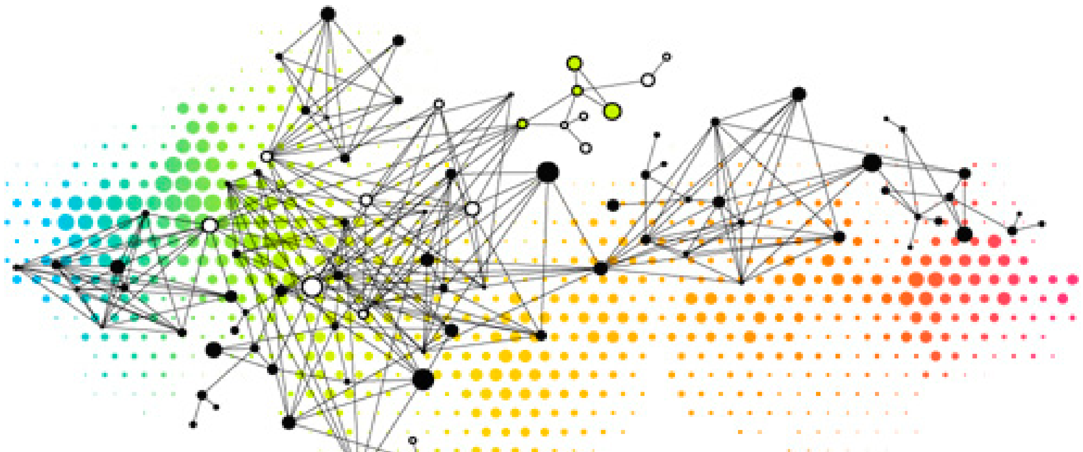

Balance of Payments Division
IMF Statistics Department

Treatment of Reserves and Fund Accounts (L8)

Course on External Sector Statistics

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Reserves Assets

- Reserve Assets are the fifth major functional category of the financial account

- Reserve assets are an essential element in the analysis of an economy's external position

A) Concept and Definition

- Reserve assets consist of those external financial assets that are both:

  - *readily available to*
  - *controlled by*

  the monetary authorities for direct financing of BOP imbalances, for managing exchange rates, and for other related purposes

  The criteria to classify financial assets as reserves are judgmental, they cannot be identified in a meaningful way simply through the application of objective criteria

A) Concept and Definition

- "Reserve assets are those external assets that are readily available to and controlled by monetary authorities for meeting balance of payments financing needs, for intervention in exchange markets to affect the currency exchange rate, and for other related purposes (such as maintaining confidence in the currency and the economy, and serving as a basis for foreign borrowing)."

BPM6, paragraph 6.64

B) Monetary Authorities

- Monetary authorities remains as a functional concept for defining reserve assets; they encompass the central bank and certain operations usually attributed to the central bank but sometimes carried out by other government institutions or commercial banks, such as government owned commercial banks
  - Example of such operations: issuance of currency, maintenance and management of reserve assets, including those resulting from transactions with the IMF
- In economies with extensive reserve assets held outside of the central bank
  - recommended to provide supplementary information on the institutional sector holdings of reserve assets held outside of the central bank

C) Identifying Reserve Assets

- The readily observable characteristics of a claim:
  - control
  - availability
  - currency of denomination
  - other clarifications, such as residency
- Two key issues among other explained below must be considered in the identification of reserve assets:
  - First, in addition to assets actually owned, which other assets are at the effective disposal of monetary authorities?
  - Second, of the assets controlled by the monetary authorities, which are available for use should the need arise?

i) Control

- In general, only external claims actually owned by the monetary authorities can be classified as reserve assets
- Nonetheless, ownership is not the only condition that confers control
- Where institutional units (other than the monetary authorities) hold legal title to external foreign currency assets, such assets can be considered reserve assets provided

i) Control

- The resident entity can only transact in these claims with nonresidents on the terms specified by the monetary authorities or only with their express approval, and
- The authorities have access on demand to these claims on nonresidents to meet balance of payments financing needs and other related purposes, and
- There is a prior law or an otherwise legally binding contractual arrangement confirming this agency role of the resident entity that is actual and definite in intent

ii) Availability

- Availability depends on any conditionality that affects the assets, including the liquidity or marketability of the asset

- Owned assets that are immediately available and can be viewed as assets in the most unconditional form are:
  - Monetary gold
  - Special Drawing Rights (SDR)
  - Reserve Position in the Fund

ii) Availability

- Reserve assets must be readily available in the most unconditional form
- A reserve asset is liquid in that the asset can be bought, sold, and liquidated for foreign currency (cash) with minimum cost and time, and without unduly affecting the value of the asset
- The concept refers to both nonmarketable assets (e.g. demand deposits), and marketable assets (e.g. securities)
- The ability to raise funds by using the asset as collateral is not sufficient to make an asset a reserve asset
- Reserve assets generally should be of high quality

iii) Currency of Denomination

- Reserve assets must be both denominated and settled in convertible foreign currency
- Convertible currencies are those that are
  - freely usable for settlements of international transactions
  - widely traded in the principal exchange markets
- In some instances, economies may hold assets denominated in the currency of a neighboring country
- These assets should be excluded from reserve assets if the currency does not meet the definition of a convertible foreign currency, but supplementary data can be provided

iv) Residence

- Reserve assets, other than gold bullion, must be claims on nonresidents
- Conversely, the authorities’ foreign currency claims on residents, including claims on resident banks, are not reserve assets
- Claims on resident banks are presented as a supplementary item to the IIP

D) Examples of Financial Assets that Do Not Qualify as Reserve Assets

- Lines of credits that could be drawn on and foreign exchange that could be obtained under swap agreements (not existing claims)
- Real estate owned by monetary authorities – not liquid
- Silver bullion, diamonds, other – are not financial assets (are considered goods)
- Capital subscriptions to international organizations that are not readily available
- Encumbered pledged assets (e.g. collateral used for third-party loans and third-party payments) (should be excluded only to the extent of the value pledged)
- Reserve assets frozen by foreign government within whose jurisdiction they are located
- Net creditor positions in regional payment arrangements that involve reciprocal lines of credit

E) Components of Reserve Assets

Reserve assets

- Monetary gold
  - Gold bullion
  - Unallocated gold accounts
- Special drawing rights
- Reserve position in the IMF
- Other reserve assets
  - Currency and Deposits
    - Claims on monetary authorities
    - Claims on other entities
  - Securities
    - Debt Securities
      - *Short-term*
      - *Long-term*
    - Equity and investment fund shares
- Financial derivatives
- Other claims

F) Monetary Gold: Gold Bullion

- Monetary gold comprises gold bullion, including gold bullion held in allocated gold accounts (regardless of the account location) and unallocated gold accounts with nonresidents (that give title to claim the delivery of gold bullion)
  - transactions with residents in gold bullion are not recorded in BOP

- Transactions in gold bullion as reserve assets between monetary authorities and with international financial institutions are recorded as transactions in gold bullion
  - transactions with gold bullion as reserve assets with all other counterparts are recorded as other changes in assets

Example: Treatment of Gold Bullion

- Monetary authority (MA) sells reserve asset gold bullion:

(a). to a nonresident other than MA and international financial institutions (IFI): (1) demonetization immediately before the transaction shown in other changes in volume in IIP; (2) entry in goods and services for nonmonetary gold with counter entry in relevant instrument in RA or other investment

(b). to a non-MA resident entity: no international transaction, demonetization immediately before the transaction through other changes in volume in IIP

Example:
Treatment of Gold Bullion

- Monetary authority (MA) purchases gold bullion for its RA:

(a).from a nonresident entity (other than MA or IFI): (1) entry in goods and services for nonmonetary gold with counter entry in currency and deposits; (2) monetization of gold bullion immediately after the transaction shown in other changes in volume in IIP

(b). from a non-MA resident entity: no international transaction, monetization immediately after the transaction through other changes in volume in IIP

F) Monetary Gold: Allocated and Unallocated Gold Accounts

- Allocated and unallocated gold accounts are to be distinguished from accounts that are linked to gold (accounts indexed to gold) but do not give title to claim delivery of gold
- If monetary authority deposits gold bullion in an unallocated gold account (UGA) which is with another monetary authority or an international financial institution, a transaction in reserve assets is recorded
- If the UGA is not available on demand, a transaction in currency and deposits in other investment is recorded
- Any UGA liabilities of resident entities to nonresident monetary authorities are to be classified as other investment, liabilities, currency and deposits

Example: Treatment of Unallocated Gold Account

- Monetary authority (MA) deposits gold bullion that it owns in an UGA with a nonresident (other than MA or IFI): (1) demonetization immediately before the transaction shown in other changes in volume in IIP; (2) entry in goods and services for nonmonetary gold with counter entry in currency and deposits; (3) reclassification of currency and deposits to reserve assets through other changes in volume in IIP (if held as reserve assets)
- Monetary authority (MA) withdraws gold bullion from an UGA held as reserve assets with a nonresident entity: (1) reclassification to currency and deposits before the transaction through other changes in volume in IIP; (2) transaction is recorded in currency and deposits with counter entry in goods and services for nonmonetary gold; (3) monetization immediately after the transaction shown in other changes in volume in IIP

G) Reserve Position in the Fund

- *Reserve position in the Fund* is the sum of
  - "reserve tranche" purchases that a member country may draw from the IMF at short notice and
  - any indebtedness of the Fund (under a loan agreement) in the General Resources Account (GRA) that is readily available (payable) to the member country, including lending to the Fund under
    - General Agreement of Borrowing (GAB)
    - New Arrangements to Borrow (NAB)

Fund's accounts will be discussed further

H) Special Drawing Rights (SDRs)

- *SDRs* are international reserve assets created by the IMF to supplement other reserve assets that are periodically allocated to IMF members in proportion to their respective quotas
- Are administrated by the IMF's SDR Department
- It is required by the IMF's Articles of Agreement to keep SDR accounts strictly separate from the GRA
- In *BMP6,* the value of SDR allocation and loans from the IMF to monetary authorities are included in *reserve–related liabilities*

I) Deposits

- Deposits in reserve assets refer to those available on demand or with a fix term but redeemable on demand or on a short notice without unduly affecting the value of deposits

- Deposits included in reserve assets are those:
  - held in foreign central banks
  - the BIS
  - other nonresident deposit taking corporations
  - deposit agreements with the IMF Trust Accounts that are readily callable to meet BOP needs
- Short-term loans provided by monetary authorities to other central banks, BIS, or other deposit taking corporations are much like deposits; by convention and consistent with treatment of interbank positions, they should be reported as deposits in reserve assets

J) Securities

- Include liquid and marketable equity and debt securities issued by nonresidents
- Long-term securities (e.g., 30-year US Treasury bonds) are included
- Unlisted securities are, in principle, excluded unless they are liquid

  - Treatment of reserve assets securities under repurchase agreements is discussed further in the following slides.

K) Financial Derivatives

- Financial derivatives are recorded as reserve assets only if the derivatives pertain to the management of reserve assets, are integral to the valuation of such assets, and are under effective control of monetary authorities

- Because they pertain to the management of assets, these transactions and positions are recorded on a net basis

L) Reserve Assets - Other Claims

Other claims include:

- Short-term loans to non-deposit taking corporations that are readily available
- Long-term loans to IMF Trust Accounts that are readily repayable to meet a BOP financing need
- Loans arising from a reverse repo (unless classified as deposits)
- Other financial assets not included above (e.g., nonnegotiable investment fund shares)

Selected Cases: Repurchase Agreements

- Securities that have been transferred under repurchase agreements, or similar agreements by the monetary authorities for cash collateral are assets of the original authorities and are either
  (1) included as reserve assets of the original owner with the loan generated reported as a reserve-related liability (a memorandum item) if a liability is to a nonresident, or
  (2) excluded from reserve assets and reclassified as portfolio investment assets
- In either case any loan liability to a nonresident is included within “other investment” and the foreign currency, provided it is a claim on a nonresident, recorded as an increase in currency and deposits within reserve assets

Selected Cases: Repurchase Agreements

- In the case of reverse repos, the funds provided to the counterparty should be recorded as a decrease in currency and deposits within reserve assets

- But if the claim (i.e., repo asset) is liquid and available upon demand to the monetary authorities it is considered part of the reserve assets, in “other claims” (or “deposits” if classified in national measures of broad money)

M) Reserve-Related Liabilities

- Reserve-related liabilities are defined as foreign currency liabilities to nonresidents associated with reserve assets of the monetary authorities
    - i.e., liabilities in foreign currency that can be regarded as direct claims by nonresidents on the reserve assets of a country
- Short-term reserve-related liabilities are a *memorandum item* to the IIP

N) Reserve Assets in IIP

Exclusions from balance of payments included in IIP:

- Monetization/demonetization of gold
  - Change in classification of gold bullion from nonmonetary to monetary (from monetary to nonmonetary)
- Valuation changes
- Other changes

O) Positions and Transactions with the IMF

- Quotas
- Reserve Position in the Fund
- Use of Fund Credit
- Remuneration
- IMF No. 2 Account

i) Quotas

- IMF member countries are assigned a quota on joining the Fund which consists of two components:

(a) Foreign exchange component – 25 percent of quota paid in SDRs or in other foreign currency accepted to the IMF (component of country's reserve assets) (shown in BOP as a transaction: decrease of other reserve assets; increase in reserve tranch position in the IMF)

(b) Domestic currency component – other 75 percent of quota payable in the member's own domestic currency (IMF Account No. 1 and No. 2 at a designated depository) or by issuance of promissory notes (IMF Securities Account) (not recorded in BOP/IIP; it is considered in economic terms to be of a contingent nature)

ii) Reserve Position in the Fund

- Represents the member's unconditional drawing right on the IMF, crated by the foreign exchange component of the quota subscription, plus increase/decrease through the IMF's sale/repurchase of the member's currency to meet the demand for use of IMF resources by other members in need of BOP financing
- To use its reserve tranch, a member may purchase foreign currency from the IMF with its own currency paid to the IMF Account No. 1 with the member's central bank or by issuing promissory notes
- It is recorded in BOP as a reduction in the members' reserve tranch in the IMF with offset by an increase in other reserve assets

iii) Use of Fund Credit

- When a member uses IMF credit, it "purchases" foreign exchange from the IMF in return for its domestic currency
- Use of IMF credit is shown as the member's liability (in SDRs) (with offset entry in other reserve assets, e.g. currency and deposits). The sale of domestic currency is registered in the IMF No. 1 Account (no BOP entry)
- Use of IMF credit liability is extinguished when the member uses foreign exchange or SDRs to "repurchase" its domestic currency (reverse entries are registered in BOP)

iv) Remuneration

- The IMF pays its members “remuneration” quarterly on the basis of their reserve tranch position;

- The remuneration is classified on an accrual basis as investment income-reserve assets-interest (credit) which is offset by an increase in reserve assets (debit)

v) IMF No. 2 Account

- IMF No. 2 Account is used by the IMF for administrative payments; it is reflected in member's BOP as a liability (currency and deposits)
- Transactions on this account are recorded as increase/decrease in this liability with offset entry in by the source or use of funds
- E.g., when IMF transfers funds from No. 1 Account to No. 2 Account in a member economy, in the BOP is registered an increase in country's reserve tranch (debit) (which reflects a decrease of IMF's holdings of Country's currency in No. 1 Account) with an offset entry in currency and deposits, liabilities (credit)