BALANCE OF PAYMENTS

CONCEPTS, NOTES AND DEFINITIONS

PART I

BALANCE OF PAYMENTS CONCEPTS AND DESCRIPTION

Definition

The Balance of Payments of a country is a systematic record of all the economic transactions between residents of that country and the rest of the world. It is also a measure of changes in a country's foreign assets and foreign liabilities over a specific period of time, usually one year.

The purpose of the balance of payments is to provide information for assessing the effects of the country's international economic transactions on the domestic affairs of the economy. The balance of payments record forms part of the larger system of national accounts, particularly the national income and expenditure accounts, in which the link between domestic production and expenditure and international transactions is identified.

The balance of payments statements presented here have been compiled in accordance with the guidelines in the Fifth Edition of the IMF's Balance of Payments Manual. The accounts record three basic types of transactions –

1. Purchases and sales of goods and services against financial items, that is, against claims and exchange reserves;

2. Changes in foreign assets and liabilities that arise from other transactions, e.g. the repayment of government or commercial debt;

3. The provision or receipt of goods and services without any quid pro quo, e.g. in the form of grants or gifts.

Accounting Conventions

A basic convention of a balance of payments statement is the double-entry system of accounting, whereby conceptually every balance of payments transaction involves both a debit and a credit entry. For example, credit entries are recorded for exports of goods and services, which give rise to an off-setting debit entry in the capital and financial account representing an increase in foreign assets. The two off-setting entries are not made explicitly but are implicit in the figures that result from this method of compiling the accounts. However, because inaccuracies may exist in the data and since entries may not match in their timing, statistical discrepancies arise and it becomes necessary to include an item "Errors and Omissions" which acts as a balancing item to bring the sum of total credits and debits to zero.

Residence

The concept of residence is central to the determination of balance of payments transactions. Residents of a country include the government, individuals and business enterprises operating in the country, whether foreign-owned or not. Excluded are agencies and branches of foreign insurance and airline companies.

Agencies of foreign owned business enterprises are treated as residents of the country in which they operate. However, transactions between residents and the agencies on behalf of the foreign business enterprise, are treated as resident to non-resident transactions and are included in the balance of payments.

Branches of foreign insurance and airline companies operating in the sub-region are treated as agencies. They act as intermediaries between their head offices and residents. As such, their transactions are included in the balance of payments.

As far as individuals are concerned, the concept of residence is based on the principle of 'centre of interest'. If an individual resides for more than a year in a country, that person is considered to be a resident of that country.

Accordingly, three groups of individuals are classified as follows:

1. **Visitors (Tourists).** Persons who live in the country for less than one year are treated as non-residents. A special case is students who go abroad to study or medical patients who travel abroad for treatment. Irrespective of the length of study or treatment they are treated as residents of their country of origin.

2. **Seasonal Workers.** Seasonal workers are individuals who reside in a country for a short period of time (less than one year) for employment. For example, Caribbean workers in Canada are considered to be residents of their country of origin and non-residents in the country where they work.

3. **Foreign Government Representatives**. Representatives of foreign governments and international organisations stationed in a country and official diplomats and military personnel are regarded as non-residents. Therefore, expenditure by such persons in St. Vincent and the Grenadines for example, are included in St. Vincent and the Grenadines balance of payments as a credit entry and expenditure by St. Vincent and the Grenadines diplomats in the countries where they are stationed are included in the balance of payments of St. Vincent and the Grenadines as a debit entry.

Main Sections of the Balance of Payments

The balance of payments statement is divided into the following three main sections:

1. The Current Account
2. The Capital and Financial Account
3. Foreign reserves or Financing

In the current account, transactions are recorded in goods, that is, merchandise and repairs and procurement in port; in services, e.g. foreign travel, insurance services; in income e.g. interest charges; and in current transfer payments, that is transactions related to grants and contributions, gifts and workers' remittances and technical assistance. Net outflows of premiums paid to general insurance companies are also included in current transfers.

The current account reflects the performance of the economy during a given period. In the case of St.

Vincent and the Grenadines, it gives an indication, on the receipts or credit side, of the performance of the major export commodities and tourism. On the debit or payments side, it provides insights into the pattern of merchandise imports and the nature of expenditure on service items.

The capital and financial account records claims on the rest of the world (assets) and claims by the rest of the world (liabilities) in respect of the reporting economy, and capital transfers to and from the rest of the world. The capital account comprises capital transfers and acquisition and disposition of non-produced non-financial assets. The claims and liabilities on the capital and financial account arise from the movement of capital for investment (including direct investment or portfolio investment) and loans. For example, loans received from abroad are recorded as inflows of capital (credits), and loan repayments made to foreigners are recorded as outflows of capital (debits). Three standard categories used in the financial account are direct investment and portfolio investment (both of which tend to be long term), and other investments which include both long-term and short-term investments of the public and private sectors. Net outflows of premiums paid to foreign life insurance companies are debited here.

The foreign reserves indicate the foreign exchange available to the monetary authorities for balance of payments financing. In the ECCU this consists mainly of the Central Bank's foreign asset holdings. The change in net foreign reserves results from the transactions that have been recorded in the current and capital accounts. Indeed, a major goal of analysis of the balance of payments is to understand the reasons for the movements in the country's foreign reserves, which reflect the performance of the economy in its dealings with the rest of the world. A balance of payments deficit is financed by a draw-down on reserves (recorded with a positive sign – a credit entry – in the reserve account). A surplus on the other hand, serves to increase the reserves (recorded with a negative sign – a debit entry – in the reserve account).

Sources of Data

The statistics in this publication are based for the most part on four data sources –

1. Surveys of private and public sector establishments conducted by the statistical office and the ECCB;

2. Interviews held by statistical officers and ECCB staff with enterprises not covered by the survey;

3. Financial statements and other statistical data issued by private and public sector enterprises;

4. Financial statements and foreign exchange records reported by the commercial banks to the ECCB;

5. ECCB's financial statement.

Balance of payments surveys have been conducted annually in St. Vincent and the Grenadines since 1986. The surveys request information on the respondents' current transactions with the rest of the world regarding service receipts and payments, as well as investment and other capital flows. A major problem has been weak survey response, but there

has been considerable improvement as a result of ongoing public relations programmes.

While the IMF methodology is used as a guide, some adjustments are necessary to allow for peculiarities of the region. In the main, this refers to regional institutions and enterprises such as airlines, some shipping operations and crop insurance that have been treated as resident to host countries.

PART II

NOTES AND DEFINITIONS

CURRENT ACCOUNT

GOODS

Merchandise

This account records imports and exports of goods adjusted to conform to balance of payments standards. Imports are recorded in the BOP on a f.o.b. basis, therefore, adjustments are made to c.i.f. imports by deducting 12.0 per cent of the total. This percentage is an estimate of the cost of insurance and freight on cargo and was based on a sample survey of customs data. Primary data on imports and exports are obtained from Customs Departments through the Statistical Office. Further adjustments are made to account for under-coverage arising from instances of smuggling, inadequate reporting by the informal sector, and the omission of duty-free goods in the customs returns.

Repair on Goods

The credit entry records repairs and maintenance costs incurred on behalf of overseas shippers by domestic shipping agents. Also reflected as a credit entry are payments made locally by oil importing companies on behalf of overseas offices for repairs and maintenance to ships. On the debit side, estimates for expenditures overseas by local carriers are made.

Goods proc

The credit entry records receipts for sale of fuel, water and other supplies and for maintenance services provided to foreign ships and aircraft, while the debit entry covers payments for similar services acquired by domestic aircraft and shipping lines in foreign ports.

SERVICES

Transportation

This item covers all transportation services on the international carriage of passengers and goods separated by the categories of **Sea Transport**, **Air Transport** and **Other Transport**. Each of these categories comprises of the following elements:

Passenger Services

The debit entry covers payments by residents of member countries to foreign carriers for transportation of passengers, and the credit entry covers receipts by domestic carriers for similar services provided by non-residents. Data were obtained from surveys of airline and shipping companies.

Freight Charges

The debit entry records freight paid to overseas shipping companies or their agents (Sea transport) and payments to airline companies or their agents (Air transport) for the carriage of imports. An estimated 10.0 per cent of the c.i.f. value of imports is debited to represent sea freight. This percentage was based on a sample of survey of Customs data. The amount included for air freight was obtained from airline returns. On the credit side, the value of air and sea freight services on outgoing cargo is obtained from surveys of shipping agents.

Other Services

The credit entry records payments such as port dues paid by foreign ships and aircrafts to the seaport and airport for use of port facilities. Payments made by ships are reflected under Sea Transport and those made by aircrafts under Air Transport. Also covered under the credit entry are commissions and agency fees received by agents of foreign airlines and foreign shipping companies. Payments to non-residents for similar services would be debited.

Travel

On the credit side, this item covers expenditure by tourists and other visitors to each member country. On the debit side, data from the commercial banks on sales of foreign exchange for overseas travel provide the basis for estimating tourist expenditure by residents of member countries travelling overseas. Expenditure overseas by residents on farm labour programmes overseas, are also debited.

INSURANCE SERVICES

Freight Insurance

The debit entry covers payments for insurance on imports provided by non-resident insurance companies and their agents. This is estimated to represent 2.0 per cent of the c.i.f. value of imports. On the credit side, the value of this service provided to non-residents by resident insurance companies is insignificant.

Life Insurance

The debit entry represents an imputed service charge for life insurance services provided to residents by non-resident insurance companies or their agents. This is estimated to be 5.0 per sent of gross life premiums. On the credit side, premiums of net claims received from non-residents by domestic insurance companies would be entered, but such transactions are negligible.

Non-Life Insurance

The debit entry represents an imputed service charge for general insurance services provided to residents by non-resident insurance companies or their agents. This is estimated to be 5.0 per cent of gross non-life premiums. On the credit side, premiums net of claims received by domestic non-life insurance companies from non-residents are entered here e.g. WINCROP in Dominica.

Re-Insurance

The entry represents net re-insurance premiums paid by domestic insurance companies.

Insurance Agents' Commission

The credit entry represents commissions received by resident agents of foreign insurance companies. On the debit side, commissions paid by domestic insurance companies to non-resident agents are entered.

OTHER BUSINESS SERVICES

This item is made up of all other transactions in services in the current account. These include payments and receipts for international communication services, for technical and professional services and royalty payments particularly by hotels and manufacturing enterprises operating under license from major international firms. Commissions and management fees paid by hotels, and construction, engineering and architectural services are also debited here. The category Financial services has been included to identify the offshore financial sector. In addition, any other miscellaneous receipts and payments for business and professional services are accounted for here.

GOVERNMENT SERVICES

Resident Government

The debit entry records expenditure by member governments on embassies and other overseas missions. The data are obtained from the governments' estimates of revenue and expenditure. In this total, salaries paid to residents stationed at foreign embassies are adjusted downwards, as only that portion spent in the country where the embassy is located should be recorded. This is based on the assumption that a portion of salaries paid to residents stationed at foreign embassies would be saved at home or used to transact business at home.

The credit entry covers government revenue from economic citizenship programmes and registration fees paid by offshore companies.

Foreign Government

The credit entry covers expenditure by foreign embassies and mission and their personnel based in St. Vincent and the Grenadines, on goods and services acquired in these countries.

Other

The debit entry is the off-setting entry for technical assistance services received from foreign governments and international agencies by the public and private sector, without a quid pro quo.

INCOME

COMPENSATION OF EMPLOYEES

Labour Income

The credit entry records gross earnings of seasonal workers mainly those on the Canadian Farm Labour Programme. The debit records gross income paid to non-residents.

Investment Income

The entries on the debit side cover income accruing to non-residents on investments made in St. Vincent and the Grenadines; the credit entries represent income earned by residents on their foreign investments.

Direct Investment Income

This comprises dividends and distributed profits, undistributed corporate profits, and interest.

The debit entry covers dividend and after-tax profits remitted to foreign head offices by branches and subsidiaries operating in St. Vincent and the Grenadines. The credit entry represents similar payments by branches and subsidiaries in foreign countries to head offices based in St. Vincent and the Grenadines.

Reinvested earnings refer to that part of after-tax corporate earnings not remitted to the investors. It is shown as a debit entry in the current account and is off-set by a credit entry in the capital account, representing an increase in foreign liabilities through reinvestment of earnings by foreign direct investment enterprises. Interest paid by direct investment enterprises on foreign loans is recorded as a debit entry, while interest earned on overseas investments by direct investors resident in St. Vincent and the Grenadines is recorded as a credit entry.

Portfolio Investment

ECCB Investment Income is a credit entry that records each country's share of interest earnings of the Central Bank's foreign investments. Other Portfolio Investment reflects investment income (subdivided into equity, bonds and notes) by institutional sectors, namely government, banks and other sectors. The credit entry records income earned from interest on overseas investments and the debit entry covers interest paid on foreign liabilities of commercial banks and statutory bodies.

Other Investment

A credit entry includes interest repayments on student loans by former recipients who now reside overseas and interest on funds held at Crown Agents. It also covers bonuses and dividends paid to residents of member countries by foreign insurance companies. The debit entry consists of interest paid by the public sector on external loans, as well as payments of bonuses and dividends to non-residents by domestic insurance companies, and payments of interest by other companies on loans received from non-residents.

CURRENT TRANSFERS

General Government

The credit entry covers technical assistance given by foreign governments and agencies to the public sector in St. Vincent and the Grenadines, taxes paid by foreign insurance companies and other foreign owned companies. On the debit side, payments of contributions to regional and international organisations and taxes and pensions paid by the public sector in St. Vincent and the Grenadines to non-residents are included.

Other Sectors

The credit entry includes receipts of gifts in cash and kind and other remittances from overseas such as maintenance of children and other dependents and support for non-government organisations (NGO's). Net claim receipts by residents from foreign insurance companies on their agents (following disasters) are also included. The debit entry covers remittances by residents of St. Vincent and the Grenadines to dependents abroad, and outflows of net premiums paid by residents to foreign insurance companies.

B. CAPITAL AND FINANCIAL ACCOUNT

CAPITAL ACCOUNT

The capital account records capital transfers and transactions related to the acquisition and disposition of non-produced non-financial assets.

Capital Transfers

The credit entry covers grants in cash and kind (excluding technical assistance) received by the public and private sectors from foreign governments and agencies. Also included is an estimate of the value of the personal effects and other assets of immigrants are included.

Acquisition and Disposition of Non-Produced, Non-Financial Assets

The debit entry covers purchase of property overseas for setting up of embassies and payments by residents for obtaining franchises from non-residents. The credit entry should capture receipts from franchises granted to non-residents, and sale of land to foreign governments for setting up embassies.

FINANCIAL ACCOUNT

Direct Investment

Abroad (outward)

In this section, the credit entry records disinvestment abroad while the credit entry records new investment abroad.

In Reporting Economy (inward)

The direct investor provides a substantial part of the equity capital and effectively controls the management of an enterprise located in another country. The credit entry includes inflows of foreign equity capital, reinvested earnings, land sales to non-

residents and loans provided by foreign owners to the direct investment enterprise located in the respective member countries.

Portfolio Investment

Portfolio Investment is categorised by assets and liabilities, by type of security and by institutional sector – government, banks, other private sector.

Debit entries represent increases in foreign securities, such as debenture stock or bonds, held by residents, and decreases in similar investments by non-residents in the ECCU. Credit entries record increases in securities of resident enterprises and of the official sector held by non-residents and decreases in similar foreign investments held by residents.

Other Investments

Three categories of capital flows are captured here:-

1. Government loans – the credit entry covers disbursements of foreign loans to the public sector, and on the debit side, amortisation of public sector external debt is recorded;

2. Changes in the net foreign assets of the commercial banks and;

3. Other capital flows of the private and public sector

The latter category represents changes in long-term and short-term investments of foreign insurance companies in the St. Vincent and the Grenadines broken down into the categories of Other Assets and Other Liabilities.

Other Assets

Included under the credit entry of Other Assets are such items like principal repayments from overseas by former students, reduction in outstanding loans to non-residents and decreases in foreign currency and overseas bank deposits of domestic insurance companies. A debit entry would include increases in foreign currency and overseas bank deposits of domestic insurance companies and increases in outstanding loans to non-residents. Also included on the debit side are net premiums paid by residents to foreign life insurance companies or their agents (that is, premiums net of service charge and claims).

Other Liabilities

The credit entry records increases in mortgages to households and increases in loans to policy holders by insurance agencies, and also increases in interest and principal arrears on central government and government guaranteed loans. The debit entry covers decreases in mortgages to households and decreases in loans to policyholders by insurance agencies, and also decreases in interest and principal arrears on central government and government guaranteed loans.

Financing/International Reserves

International Reserves or Financing items are foreign assets available to the monetary authorities for regulating balance of payments imbalances. The

reserves comprise: (i) Special Drawing Rights (SDRs) with the IMF, (ii) the reserve position in the IMF, (iii) government foreign assets, and (iv) the foreign exchange holdings of the ECCU. The reserve items like the other items in the BOP, are flows which reflect changes during the year. Increases in any reserve item are entered with a negative sign (as a debit) and decreases are recorded with a positive sign (as a credit).