

1. *What is the Balance of Payments (BOP)?*

The Balance of Payments (BOP) is a summary of the economic transactions of a country with the rest of the world, for a specific time period. It serves as an accounting statement on the economic dealings between residents of the country and non-residents.

2. *Who are the residents of the country?*

Nationality is not a basis for determining an individual's country of residence. A person is considered a resident of a country when he has stayed or intends to stay in that country for one year or more. Thus, an Overseas Filipino (OF) can remain a resident of the Philippines or can become a non-resident depending on the length of the job contract abroad.

Similarly, a business enterprise is considered a resident of a country if it engages, for a year or more, in the production of goods or services in a significant scale in that country. Branches and subsidiaries of foreign companies are treated as residents of countries where they operate their business. However, a liaison or a representative office of a foreign company, regardless of the length of its stay, does not qualify as a resident enterprise. Its presence in a country is not for operating a business but only for providing auxiliary services to the parent company. It remains as an integral part of the foreign parent's operations and thus, is treated as a non-resident where it is located.

Government instrumentalities like embassies, consulates, military establishments stationed abroad remain as residents of the country they represent.

3. *What economic transactions are engaged in by residents of a country with non-residents?*

Economic transactions are grouped into two major categories: (1) current account, and (2) capital and financial account.

4. *What are current account transactions?*

The current account covers trade in goods, services, income, and current transfers.

Trade in goods—exports and imports—is the bulk of the current account. Electronics are the country's major exports. Consequently, raw material inputs to electronics exports make up a sizable portion of imports.

Trade in services is another component of the current account. Travel receipts dominate the country's exports of services while transportation ranks as the top service imports, largely on account of payments to foreign carriers for freight of the country's imported goods. Other service transactions with the rest of the world include communication, insurance, computer and information, business and professional services.

The income sub-account records as receipts a portion of OF earnings, as well as the profit of Philippine investments abroad.¹ Disbursements are largely interest payments to foreign creditors.

The rest of remittances is lodged under current transfers together with gifts, grants and donations to and from abroad. Current transfers can be in cash and in kind.²

5. *What does the Current Account Balance (CAB) signify?*

When total exports/receipts exceed total imports/payments, the current account is in surplus. It is in deficit if the reverse is observed.

If the CAB is in surplus, the country is a “net lender” to the rest of the world in the amount of the surplus or the excess in the current account transactions. Net lending occurs when the national saving is more than the country’s investment in real assets. If in deficit, the country is said to be a “user of funds” and thus, is considered as net borrower from abroad in order to fill in the shortage. In this case, the country invested more than what its national saving can finance.

6. *What are the transactions in the capital and financial account?*

The capital and financial account consists of capital transfers, direct investments, portfolio investments and other forms of investments.

Capital transfers are also grants and donations, the intention of which is for investment (i.e., machinery and equipment, buildings and structures). This is in contrast with grants and donations lodged under current transfers whose intention is for consumption (i.e. food, clothing, supplies and materials).

Direct investment refers to capital participation in a company in which the investor has a lasting or permanent interest. By convention, this is manifested by ownership of at least ten percent of the company’s equity.

Portfolio investment is usually referred to as “hot money” since the investor’s motive is short-term as opposed to a direct investor’s lasting interest in a company. A portfolio investor will buy or sell a financial instrument at anytime there is an indication of immediate gain or loss.

Portfolio holdings may be in the form of stocks, bonds and notes, and money market instruments, which are tradable in the market and therefore can easily be acquired or

¹ Earnings of OFs whose job contracts do not exceed one year are categorized under the income sub-account.

² Remittances of OFs whose work contracts are for one year or more as well as those coming from migrants are classified as current transfers.

disposed of. In case of stockholdings, a portfolio investor is differentiated from a direct investor if he owns less than ten percent of a company's total equity.

Other forms of investments are financial derivatives, loans (trade and non-trade), holdings of currency and deposits, and other investments.

7. *What are international reserves? Who holds or manages the country's international reserves?*

International reserves, technically referred to as Gross International Reserves (GIR), are foreign assets of the Bangko Sentral ng Pilipinas (BSP) held mostly as investments in foreign-issued securities, monetary gold, and foreign exchange. These are supplemented by claims to the International Monetary Fund (IMF) in the form of Reserve Position in the Fund and Special Drawing Rights.

Being the lender of last resort, the BSP holds international reserves for the foreign exchange requirements of the country in case supply from domestic commercial banks falls short of the total demand. As the term connotes, GIR serves as stand-by fund to finance the deficit that may arise from the combined current and capital and financial transactions. Consequently, financing the deficit reduces the level of reserves. On the other hand, the BSP builds up its international reserves by the amount of the net inflow of foreign exchange resulting from surpluses in external transactions.

International reserves can also be measured on a net basis. Net International Reserves (NIR) can be derived by deducting from the GIR the BSP's short-term foreign liabilities and borrowings from the IMF.

8. *Is there an ideal level of GIR which the BSP has to maintain?*

Because of its intended use, the GIR should be adequate enough to cover external payments on the assumption that no other source of foreign exchange could be tapped. In extreme conditions when there are no export earnings or foreign loans, the GIR should be able to pay for the country's most immediate obligations—imports and debt service. By convention, GIR is viewed to be adequate if it can finance three-months' worth of the country's imports of goods and payments of services and income. Another indicator of reserve adequacy is for the level of GIR, as of a particular period, to at least provide 100 percent cover for the payment of the country's foreign liabilities, public and private, falling due within the immediate twelve-month period.

9. *What is the currency composition of the country's GIR?*

In terms of currency composition, the country's GIR (excluding gold) are held in U.S. Dollars, Japanese Yen, Euros and other foreign currencies. Historical data show that the bulk of the BSP's GIR (excluding gold) has been consistently held in U.S. Dollars.

10. What is the overall BOP position? What are Net Unclassified Items?

The overall BOP position is a summary measure of the performance of the country's external transactions. This can be estimated using two approaches:

- the sum of the current account balance and capital and financial account balance, or
- the change in net international reserves due to transactions.

Ideally, these two approaches should yield the same result. However, in reality, they do not equate due to data imperfections (e.g., lag in reporting), in the current account and the capital and financial account. The discrepancy between the two approaches is termed as the "Net Unclassified Items" or "errors and omissions". Since the level of international reserves is based on a more rigid book accounting, the overall BOP position is determined by the second approach. To maintain the identity of the two approaches, the following presentation is adopted in the BOP:

$$\begin{aligned} & \text{Current Account Balance} \\ & + \text{Capital and Financial Account Balance} \\ & + \text{Net Unclassified Items} \\ & = \text{Overall BOP Position} \\ & = \text{Change in NIR due to transactions} \end{aligned}$$

Given the above equation, compilers refer to the first three items as above the line and the change in NIR as below the line.

11. What is the International Investment Position (IIP)? How does it compare with the BOP?

The IIP is a companion framework to the BOP statistics. The BOP is a flow estimate since it records transactions within a given period. The International Investment Position, on the other hand, is a stock estimate, as it records the country's foreign financial assets and foreign financial liabilities outstanding as of a certain period. The stock is the result of all the past flows plus adjustments such as exchange rate movements to account for the value of the financial asset/liability as of date of reporting.

12. What are the main components of the IIP?

The IIP links with the financial account in the BOP. Similar to the BOP, the categories of the IIP are direct investments, portfolio investments, financial derivatives, and other investments. Assets and liabilities are presented separately. International reserves also form part of the country's assets.

13. *What does the IIP measure?*

The balance in the IIP, that is, assets less liabilities or the Net International Investment Position, measures the country's financial standing with the rest of the world. A net asset position reflects net *claims* of residents on non-residents and thus may indicate some degree of stability.

Meanwhile, a net liability position reflects net exposure of residents to non-residents and thus to some extent, vulnerability. However, the quality of foreign liabilities is a major consideration in determining vulnerability. If foreign direct investments and long-term loans dominate the liability side, a country's net liability position may not be of immediate great concern.

14. *What are the uses of the BOP and IIP?*

The BOP and IIP are important tools for national and international policy formulation as countries have increasingly become interdependent. Policymakers are guided by the sources of imbalances as presented in the BOP and IIP and therefore become better equipped in determining and implementing adjustment measures. For instance, the deficit in the current account may have stemmed from lower exports of goods than imports. Given this scenario, national development programs could be directed to increase competitiveness in the global market for local products and/or develop new industries that will produce import substitutes.

The use of these statistics is enhanced when taken together as the combined use of the BOP and IIP provides a glimpse of the relationship between flows and stocks. One example is the link between trade in goods and direct investments, as this would reveal how dependent export earning potential is on foreign capital and technology. In another instance, external debt problems may be traced to chronic current account deficits. Likewise, links are established between exchange rates and the strength or weakness of the current and financial accounts.

15. *How often are these statistics compiled?*

The BOP is compiled quarterly but with a monthly breakdown. It is released to the public electronically, i.e., via the BSP's website or in the form of hard copies about 12 weeks after the reference quarter accompanied by a press release. Meanwhile, the IIP is compiled on an annual basis and released nine months after the reference year.

16. *How often are these statistics revised?*

Data on all BOP components released to the public during the reference quarter are treated as preliminary, and may be revised in any quarter of the reference year. Prior year's data may be revised coinciding with the release of the second quarter report in September of the current year and the fourth quarter report in March of the succeeding

year. On the other hand, data on all components of the IIP are preliminary when first released. Data for the previous year may be revised and the revisions are released together with the data for the reference year. For both BOP and IIP data, historical revisions are carried out in case of significant changes arising from the introduction of new classifications, compilation frameworks and methodologies.

17. *What were the recent revisions to the BOP and IIP?*

To conform with the guidelines outlined in the Balance of Payments Manual, 6th edition (BPM6), the BSP adopted the new treatment of the allocation of SDRs in the various statistics it compiles and monitors, namely the BOP, IIP, External Debt Statistics (EDS), and Monetary Financial Statistics (MFS). Prior to the adoption of the revised treatment, the allocation of SDRs under the Balance of Payments Manual, 5th edition (BPM5) was considered a non-transaction item and thus, it is not included in the BOP. Therefore, the SDR allocation did not have any impact on the BOP position. SDR allocation also had no impact on the country's external debt as it was not treated as a liability. Meanwhile, SDRs raised the country's IIP because it resulted in an increase in reserve assets (GIR).

With the implementation of the BPM6-based treatment, the SDR allocation is now treated as a transaction, particularly as a long-term liability of the monetary authority. The 2009 BOP position and end-2009 external debt of the country increased by the amount of SDR allocation. However, there was no impact on the net IIP for 2009 due to offsetting entries in both the asset and liability sides.

In addition, the BSP also revised the BOP statistics for 2008 and 2009 to reflect the inclusion of thrift banks' financial transactions based on the Financial Reporting Package (FRP) starting March 2008 and other data updates.

18. *Do other countries compile BOP and IIP?*

Most countries compile the BOP and IIP because of their importance to national planning. For international comparability, the International Monetary Fund (IMF) has set guidelines on the compilation of these statistics which member countries are encouraged to comply with. Concepts and coverage are defined in the BPM5. Compilation manuals undergo periodic updating to keep abreast with the developments in the market. As a consequence, data series are likewise subjected to revisions to conform to the latest manual.