



BOJ
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Revision of Balance of Payments Related Statistics in Japan

November 2013
International Department
Bank of Japan

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Revision of Balance of Payments Related Statistics in Japan

I. Introduction

The Ministry of Finance (MOF) and the Bank of Japan (BOJ) will implement a major revision of balance of payments (BOP) related statistics,¹ mainly with the aim of (1) achieving conformity with the sixth edition of the *Balance of Payments and International Investment Position Manual (BPM6)*² published by the International Monetary Fund (IMF) in 2008 and (2) introducing an annual revision system. The revision will take effect for data from January 2014 onward. The revised statistics will meet the needs of data users in that the data will reflect financial and economic developments more appropriately and that the accuracy of disseminated data and the consistency of time series data will be enhanced. This paper presents the background to the revision and introduces the major changes in the BOP related statistics.³

¹ The following statistics are collectively referred to as the BOP related statistics in this paper: (1) flow statistics including the *Balance of Payments (BOP)* and the *International Transactions in Securities (based on reports from designated major investors)* and (2) stock statistics including the *International Investment Position of Japan (IIP)*, the *Gross External Debt Position of Japan (External Debt)*, and the *External Assets and Liabilities of Banks, etc.*

² The full text is available on the IMF web site (<http://www.imf.org/external/pubs/ft/bop/2007/pdf/bpm6.pdf>).

³ In revising the BOP related statistics, the MOF and the BOJ have prepared for the transition giving due consideration to the reporting burden for respondents. Partial amendments to the "ministerial ordinance concerning reporting of foreign exchange transactions, etc.," which governs, for example, the reporting forms used for the source data of the BOP related statistics, were promulgated in December 2011 and will take effect on January 1, 2014, allowing a lead time of approximately two years. In addition, instructions on the reports after the transition, including reporting forms and submission procedures, have been made available on the Bank's web site (available only in Japanese).

II. Background to the Revision and Major Changes⁴

A. Update of the Balance of Payments Manual

Japan's current BOP related statistics have been compiled and disseminated based on the fifth edition of the *Balance of Payments Manual (BPM5)*⁵ published by the IMF in 1993. However, in the time since the publication of *BPM5*, (1) based on the experience of currency crises since the mid-1990s and the like, there has been growing interest in using balance sheet data to analyze economies' vulnerability (the so-called balance sheet approach⁶); (2) there have been concrete steps toward updating the System of National Accounts (SNA),⁷ strengthening the need to harmonize macroeconomic statistics including BOP related statistics; and (3) economic activities have been transformed by globalization and the growing sophistication of financial transactions. Given these developments, the IMF updated *BPM5* and published *BPM6* in 2008.

BPM6 involves relatively few changes from *BPM5* in terms of the overall structure of the accounts or broad definitions; instead, it takes into account economic and financial developments and economic policy interests. *BPM6* has the following features reflecting the above background that led to the update:

- (1) Emphasis on the international investment position and the statistics related to finance;⁸
- (2) Enhancement of harmonization with the SNA by standardizing components and providing more detailed sectoral classifications; and
- (3) Development of data to appropriately grasp globalized company structures and production processes as well as sophisticated financial transactions.

Against this background, the MOF and the BOJ will switch to the dissemination of BOP related statistics for Japan based on *BPM6* for transactions from January 2014 onward.

⁴ See Appendix for details of the revision.

⁵ The full text is available on the IMF web site (<http://www.imf.org/external/np/sta/bop/BOPman.pdf>).

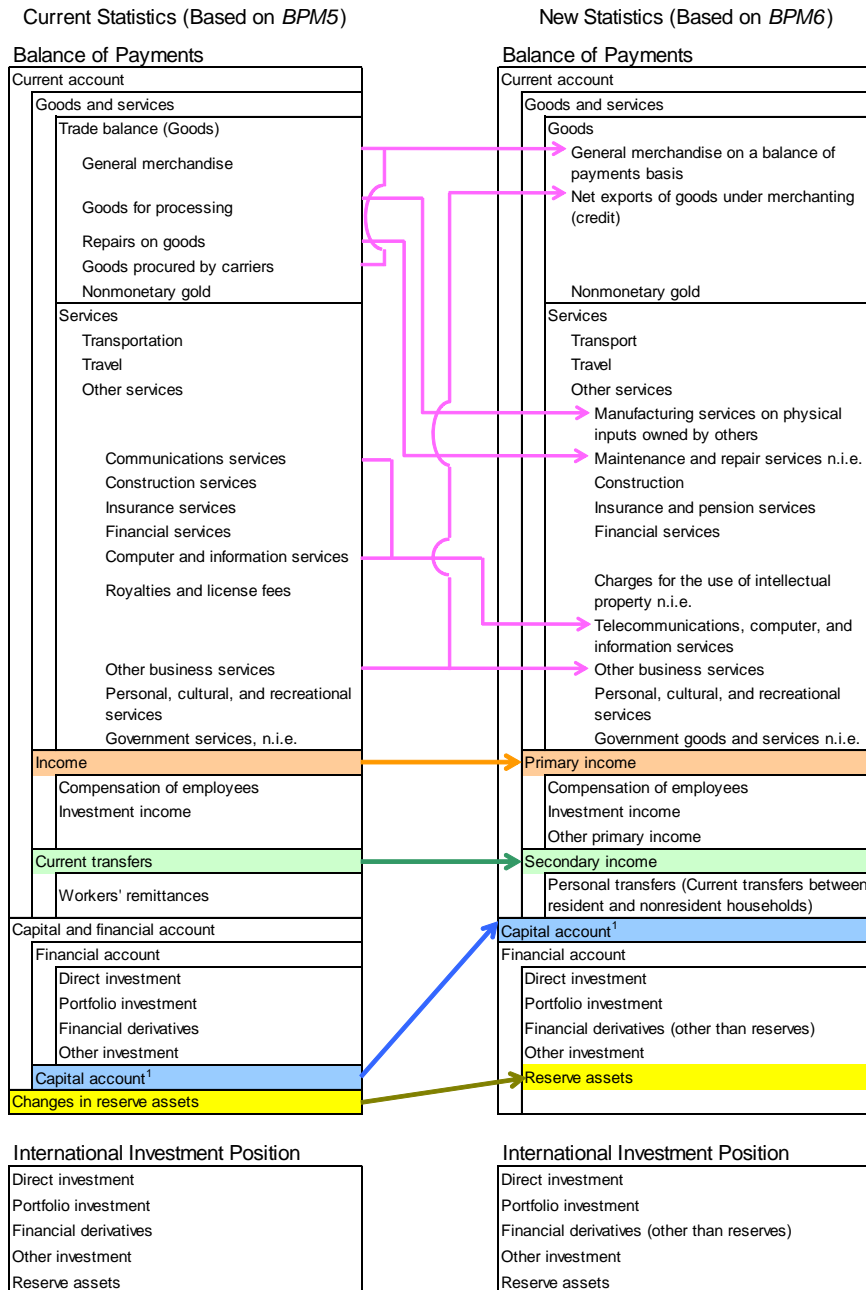
⁶ The balance sheet approach concentrates on the examination of stock variables by sector to examine a country's economic vulnerability. It is used to examine, for instance, the vulnerability of each sector by looking at currency and maturity mismatches or biases in the composition of assets, or by looking at the relationship between sectors to examine the possibility of financial shocks spilling over.

⁷ The SNA was updated in 2008, with the 1993 SNA being replaced by the 2008 SNA. *BPM6* was developed giving full consideration to the harmonization with the 2008 SNA.

⁸ The international investment position now even appears in the title of the updated manual.

Changes in arrangements and names of main components reflecting the implementation of *BPM6* are shown in Figure 1.⁹

Figure 1: Structure of the Accounts (Changes in Arrangements and Names of Main Components)



Note: 1. Includes capital transfers and gross acquisitions/disposals of nonproduced nonfinancial assets such as mineral rights.

⁹ The current "capital and financial account" and "changes in reserve assets" will be combined into the new "financial account." The "capital account" will be separated from the "capital and financial account" and treated as a main account comparable to the "current account" and "financial account."

Other changes resulting from the implementation are explained below. They are grouped into the following three categories: (1) more detailed breakdowns of financial items; (2) changes in presentation to enhance harmonization with the SNA; (3) changes in recording principles and compilation methods to appropriately grasp economic and financial activities.

1. More detailed breakdowns of financial items

Regarding financial items, the institutional sectors will be broken down into more detailed classifications and figures for additional categories will be compiled as follows.¹⁰

In the *BOP* and *IIP*, "portfolio investment," "financial derivatives," and "other investment" are currently broken down into three sectors (public sector, banks, and other sectors). In the future, they will be broken down into five sectors (central bank; general government; deposit-taking corporations, except the central bank; other financial corporations; as well as nonfinancial corporations, households, and nonprofit institutions serving households [NPISHs]) (see Table 1).

The revision of the sector classification will also apply to the *International Transactions in Securities*.

Table 1: Revision of the Classification of Institutional Sectors

Current statistics based on <i>BPM5</i> : Three sectors	New statistics based on <i>BPM6</i> : Five sectors
Public sector	Central bank
	General government
Banks	Deposit-taking corporations, except the central bank
Other sectors	Other financial corporations
	Nonfinancial corporations, households, and NPISHs

In the *BOP* "investment income attributable to investment fund shareholders" will be

¹⁰ In addition, the recording principle for data on direct investment will be changed from the directional principle to the asset and liability principle. As a result, for example, loans to a Japanese company from its overseas subsidiaries, which have been recorded as reverse investment (withdrawals of invested assets) on the asset side under the directional principle, will now be recorded as loans on the liability side under the asset and liability principle. This modification will provide a clearer grasp of Japan's assets and liabilities (see Appendix for details).

introduced as a new item under "investment income," and in the *BOP* and *IIP* "investment fund shares" will be introduced as a new item under "portfolio investment." Transactions related to investment funds will be recorded under these new items.

In the *IIP*, portfolio investment asset positions are currently disseminated by currency and type of securities. In the *BPM6*-based statistics, a detailed breakdown for both assets and liabilities not only of securities under portfolio investment but also of other debt instruments will be provided, distinguishing by currency, sector, and maturity.

2. Changes in presentation to enhance harmonization with the SNA

Presentation will be changed as follows to enhance harmonization with the SNA.¹¹

The current "financial account" and "changes in reserve assets" in the *BOP* focus on financial inflows/outflows and show inflows with a plus sign and outflows with a minus sign. The new "financial account," into which the current "financial account" and "changes in reserve assets" are combined, will focus on changes in assets and liabilities and will show increases in assets and liabilities with a plus sign and decreases with a minus sign. As a result, the signs for figures on the asset side (outward investment) will be reversed, while those on the liability side (inward investment) will remain unchanged (see Table 2). In addition, the method of calculating net figures for each item will be changed from "assets plus liabilities" to "assets minus liabilities."

Table 2: Changes in Sign Conventions for the Financial Account

		Current financial account and changes in reserve assets based on <i>BPM5</i>	New financial account based on <i>BPM6</i>
Assets	Financial outflows = increases in assets	–	+
	Financial inflows = decreases in assets	+	–
Liabilities	Financial inflows = increases in liabilities	+	+
	Financial outflows = decreases in liabilities	–	–

¹¹ Moreover, the concept of "financial intermediation services indirectly measured (FISIM)" will be introduced to enhance harmonization with the SNA (see Appendix for details).

As a result of the above changes, the identity showing the relationship between the accounts in the *BOP* will change as follows.

Current identity: Current account balance + capital and financial account balance + changes in reserve assets + errors and omissions = 0.

New identity: Current account balance + capital account balance – financial account balance + net errors and omissions = 0.

The components currently labeled "income" and "current transfers" will be renamed "primary income" and "secondary income," respectively, in accordance with the SNA.

3. Changes in recording principles and compilation methods to appropriately grasp economic and financial activities

Major changes in recording principles and compilation methods are described below (see Appendix for details).

**Table 3: Changes in Recording Principles and Compilation Methods for Statistics
Based on *BPM6***

Full application of the change of ownership principle	The processing and repair of goods as well as merchanting, which have been treated as exceptions to the change of ownership principle, will be reclassified according to the change of ownership principle. As a result, processing and repair of goods -- which do not involve a change in economic ownership -- will be reclassified from "goods" to "services," and merchanting -- which involves such changes -- will be reclassified from "services" to "goods."
Introduction of financial dealers' margins	Transaction fees implicitly charged as part of the transaction prices for financial instruments will be excluded from the "financial account" and instead be recorded under "financial services."
Change in the treatment of sales of patents and copyrights	Patents and copyrights will be treated as produced assets rather than as nonproduced assets. Their sale will be included in the corresponding items under "other services."
Change in the treatment of securities lending transactions	Securities lending transactions, which are currently recorded under "portfolio investment" (and "other investment" as corresponding entries), will no longer be recorded, since they do not involve a change in economic ownership.

B. Introduction of an Annual Revision System

In the current *BOP*, data are revised only when the final figures are disseminated, which is two to four months after the preliminary figures,¹² and the final figures in principle are not subject to further revision.¹³ Moreover, the *IIP* at year end in principle are not subject to revision. The reason is that frequent revisions of the statistics would impair the stability of the data. However, some source data, such as those for reinvested earnings described below,¹⁴ are not available in time for the dissemination of final figures, and reported data are often corrected after the dissemination of final figures, so that one issue was to increase the frequency of data revisions in order to enhance the accuracy of the statistics and the consistency of time series data.¹⁵

In consideration of these circumstances, the data revision policy will be changed with the implementation of *BPM6* and an annual revision system will be introduced to increase the frequency of revisions. Details of the annual revision system are provided in Table 4.

¹² Preliminary figures for a month are disseminated on the sixth business day of the month after next. Monthly figures for each quarter are finalized and released on the sixth business day of the first month of the quarter after next. Therefore, the interval between the dissemination of preliminary and final figures is about two months for the last month of a quarter and four months for the first.

¹³ The final figures have occasionally been revised as needed.

¹⁴ In the *BOP* statistics, reinvested earnings are direct investment enterprises' shares of earnings that are not distributed as dividends to investors but accumulated as retained earnings. Such shares are recorded under "income" ("primary income" under *BPM6*) as if they were distributed as dividends, and the same amount is recorded under "direct investment," as if this amount was reinvested in the enterprise.

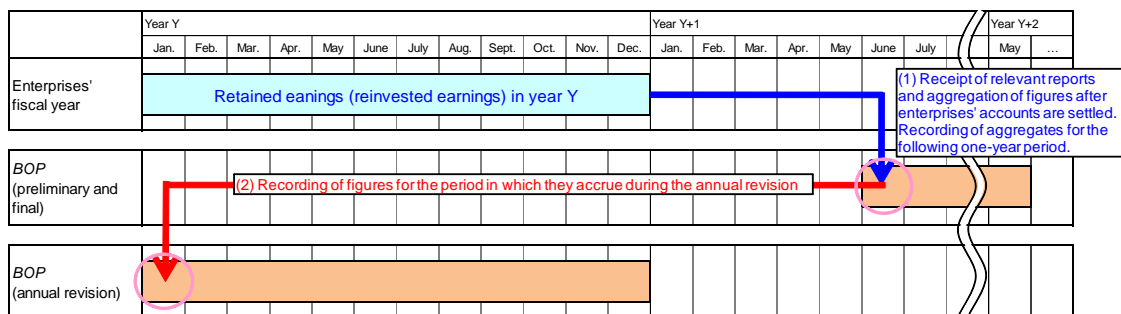
¹⁵ In 2005, the IMF assessed six major economic statistics in Japan against international standards in *Japan: Report on the Observance of Standards and Codes (ROSC) - Data Module*. In this report, the IMF recommended to review the revision policy for *BOP* data, and the government responded that it would make efforts to improve its practices when it implements *BPM6*. The full text of this report is available on the IMF web site (<http://www.imf.org/external/pubs/ft/scr/2006/cr06115.pdf>).

Table 4: Annual Revision System

Statistics to be covered	The <i>BOP</i> , including regional and seasonally-adjusted data, and the <i>IIP</i> , including quarterly estimates, all of which are based on <i>BPM6</i> . Excludes direct investment by region and industry and the <i>International Transactions in Securities</i> .
Period to be covered	Two years (years Y-2 and Y-1) ¹⁶ For the <i>BOP</i> , the current revision practice, in which preliminary figures are revised and disseminated as final figures, will continue, and those figures are expected to be referred to as the second preliminary figures in the new statistics based on <i>BPM6</i> .
Frequency	Annual

As part of the initiative to improve the quality of statistical data with the introduction of the annual revision system, the time of recording reinvested earnings will be revised. Source data for reinvested earnings are taken from enterprises' financial statements and are not available until the enterprises' accounts are settled. Therefore, in other countries, compilers generally record estimates and revise data for the previous fiscal year once the source data become available. By contrast, in Japan, there is no such arrangement to revise figures, and the time of recording is conventionally delayed. Reinvested earnings are therefore recorded from the middle of the next fiscal year (i.e., with a delay of 17 months) rather than in the period in which they accrue. With the introduction of the annual revision system, the time of recording will be adjusted so that reinvested earnings are recorded in the period in which they accrue (see Figure 2).¹⁷

Figure 2: Adjustment of the Time of Recording Reinvested Earnings



¹⁶ Because data subject to the annual revision are those based on *BPM6*, which will be compiled from January 2014 onward, the annual revision in 2015 will in principle only cover figures for 2014. From 2016 onward, figures for years Y-2 and Y-1 will be subject to the revision.

¹⁷ Figures must be revised for two years or more for such an adjustment of the time of recording to be completed. Therefore, the annual revision will go back longer for reinvested earnings (and higher level items that include reinvested earnings) than for other items.

C. Other Changes

Apart from bringing Japan's BOP related statistics in line with *BPM6* and introducing the annual revision system described above, the revision of the BOP related statistics will incorporate various other changes, including the improvement of estimation methods and the extension of source data aimed at enhancing the accuracy of the statistics and their usefulness for data users. These changes cover a wide range of areas. Table 5 presents an overview of the most important items, with the Appendix providing more details.

Table 5: Other Changes

Supplementing data for "other services"	Data for small-value transactions in "other services" below the reporting threshold will be supplemented through estimation, because such transactions account for a large portion of "other services," raising coverage issues.
Change in the definition of direct investment	The criterion for a direct investment relationship will change from outstanding shares (10 percent or more of the outstanding shares) to voting power (shares that provide 10 percent or more of the voting power). Moreover, indirect holdings (e.g., through subsidiaries) will be newly recorded under direct investment.
Dissemination of data on direct investment income by region and industry	Data on "direct investment income" by region and industry will be compiled and disseminated.
Leveling of estimation errors for quarterly estimates	For quarterly estimates of the <i>IIP</i> and <i>External Debt</i> statistics, estimation errors will no longer be aggregated as the difference between figures at the end of the third quarter and the year end but instead will be redistributed across quarters.

III. Dissemination of the Current Statistics Data on a *BPM6* Presentational Basis

The switch-over to the new statistics will lead to a break in the data between December 2013 and January 2014. Considering the user needs for time series data, historical time series data consistent with the new statistics will be provided at the start of dissemination of the new statistics. Specifically, the current statistics (the *BOP* and *IIP*) based on *BPM5* will be rearranged in accordance with the standards of the new statistics based on *BPM6*; moreover, the time of recording reinvested earnings will be revised. Such data on the new *BPM6* presentational basis will be compiled retroactively and will be disseminated at the beginning of March 2014, when the preliminary figures for January 2014 will be

disseminated.

Statistics that will be disseminated on the new presentational basis are the monthly *BOP* and the year-end *IIP* from 1996, when the statistics based on *BPM5* started to be compiled in Japan, and from which data on the current basis are available.

The data on the new presentational basis will be compiled by rearranging the data collected within the current statistical framework. For this reason, they will not reflect all the changes described above and nor will they cover new items such as the more detailed sectoral breakdown, for which source data have not been collected under the current framework.

Yearly estimates for the main components on the new *BPM6* presentational basis, calculated tentatively based on the currently available data, are shown below. Changes in the figures for the "current account" mainly reflect changes in the figures for "primary income" due to the revision of the time of recording reinvested earnings. Moreover, changes in the figures for the "financial account" mainly reflect the changes in sign conventions and the incorporation of "reserve assets," which are currently recorded under "changes in reserve assets" (see Table 6).

Table 6: Rearranged Data Based on *BPM6* (Tentative)

Balance of Payments (Based on current <i>BPM5</i> format)					Balance of Payments (Estimates based on new <i>BPM6</i> format)				
tril. yen	CY				tril. yen	CY			
	2009	2010	2011	2012	2009	2010	2011	2012	
Current account	13.7	17.9	9.6	4.8	Current account	13.6	19.1	10.1	4.8
Goods and services	2.1	6.6	-3.4	-8.3	Goods and services	2.1	6.6	-3.4	-8.3
Trade balance (Goods)	4.0	8.0	-1.6	-5.8	Goods	5.4	9.5	-0.3	-4.3
Services	-1.9	-1.4	-1.8	-2.5	Services	-3.3	-3.0	-3.0	-4.0
Income	12.8	12.4	14.0	14.3	Primary income ¹	12.6	13.6	14.6	14.3
Current transfers	-1.2	-1.1	-1.1	-1.1	Secondary income	-1.2	-1.1	-1.1	-1.1
Capital and financial account	-14.3	-17.7	1.2	-8.2	Capital account ²	-0.5	-0.4	0.0	-0.1
Financial account	-13.8	-17.3	1.1	-8.2	Financial account	16.2	22.3	13.2	5.1
Direct investment	-5.9	-5.0	-8.7	-9.6	Direct investment ¹	5.7	6.3	9.3	9.6
Portfolio investment	-20.5	-13.2	12.9	-3.2	Portfolio investment	20.5	13.2	-12.9	3.2
Financial derivatives	0.9	1.0	1.3	-0.6	Financial derivatives (other than reserves)	-0.9	-1.0	-1.3	0.6
Other investment	11.6	0.0	-4.4	5.3	Other investment	-11.6	-0.0	4.4	-5.3
Capital account ²	-0.5	-0.4	0.0	-0.1	Reserve assets	2.5	3.8	13.8	-3.1
Changes in reserve assets	-2.5	-3.8	-13.8	3.1	Net errors and omissions	3.1	3.6	3.1	0.3
Errors and omissions	3.1	3.6	3.1	0.3					

Notes: 1. The time of recording reinvested earnings has been adjusted for data through July 2011.

2. Includes capital transfers and gross acquisitions/disposals of nonproduced nonfinancial assets such as mineral rights.

IV. Conclusion

The revision will bring Japan's BOP related statistics into conformity with the latest international standards. In addition, the revision will significantly improve the quality of the statistics in that they will reflect the economic situation more appropriately with the more

detailed breakdowns of disseminated items, and that their accuracy will also be enhanced with the introduction of the annual revision system. This will further increase the usefulness of the statistics for users.

The MOF and the BOJ will compile and disseminate useful BOP related statistics while giving due consideration to their use as well as the reporting burden for respondents.

Details regarding the Revision of Balance of Payments Related Statistics in Japan

I. *Balance of Payments (BOP)*

A. Current Account

1. Full application of the change of ownership principle¹

Transactions treated as exceptions to the change of ownership principle under *BPM5*, namely, the processing and repair of goods as well as merchanting, are treated following the change of ownership principle under *BPM6*. Accordingly, these items will also be reclassified in Japan's BOP statistics as follows.

Processing and repair of goods: The ownership of goods sent for processing or repair usually does not change to the processor or repairer but remains with the original owner that asks for processing or repair; therefore, such transactions should not be recorded under "goods" according to the change of ownership principle. However, *BPM5* recommended that goods which cross the border for processing or repair should be recorded under "goods" as an exception to the change of ownership principle, and Japan's BOP statistics have followed this treatment. Under *BPM6*, however, such transactions are regarded as services for which fees for processing or repair are paid/received. Therefore, such transactions will be relabeled as "manufacturing services on physical inputs owned by others" and "maintenance and repair services n.i.e.," respectively, and recorded under "services" and not under "goods."

Merchanting:² Under *BPM5*, merchanting is regarded as an intermediary service by brokers and treated as an exception to the change of ownership principle; therefore, in the current statistics, the amount corresponding to merchanting charges is included in "merchanting and other trade-related services" under "services." Under *BPM6*, however, merchanting is regarded as the sale of goods involving a change in ownership; therefore, it

¹ *BPM6* (paragraph 3.41) states: "The change of economic ownership is central in determining the time of recording on an accrual basis for transactions in goods, nonproduced nonfinancial assets, and financial assets."

² *BPM6* (paragraph 10.41) states: "Merchanting is defined as the purchase of goods by a resident (of the compiling economy) from a nonresident combined with the subsequent resale of the same goods to another nonresident without the goods being present in the compiling economy."

will instead be treated as "net exports of goods under merchanting" and recorded under "goods" and not under "services."³

2. Introduction of FISIM

While banks and other financial corporations provide intermediation services through their lending and deposit operations, fees for such services are usually not explicitly charged but instead indirectly charged as part of the margins in interest rates on loans and deposits. While in the SNA, this concept of "financial intermediation services indirectly measured (FISIM)" has been adopted since the *1993 SNA*, this is not the case in *BPM5*. However, *BPM6* introduced FISIM for consistency with the SNA. Accordingly, in Japan's BOP statistics, part of the margins in interest rates on loans and deposits will start to be regarded as corresponding to charges for financial intermediation services, and their value will be estimated and recorded as "financial services" under "services."⁴

Consequently, the amount of interest on loans and deposits after adjusting for FISIM will be recorded under "primary income."

Transactions to be covered in the estimates of FISIM can be broken down into two items. On the credit side, these are loans by "deposit-taking corporations, except the central bank" (excluding "interoffice accounts") classified under "loans" (FISIM on loans), while on the debit side, they are deposits by "nonfinancial corporations, households, and NPISHs" classified under "currency and deposits" (FISIM on deposits). The former correspond to loans from "deposit-taking corporations, except for the central bank" to nonresidents, excluding those through interoffice accounts, and the latter correspond to deposits by nonfinancial corporations, etc., at nonresident financial corporations.

FISIM will be estimated by comparing the actual interest rates on loans and deposits and the reference rate that contains no service element but reflects the risk and maturity structure of loans and deposits.⁵ To avoid that short-term fluctuations in interest rates are recorded as changes in the quality and quantity of services, the twelve-month-moving averages of interest credits and debits will be used in calculating actual interest rates on loans and

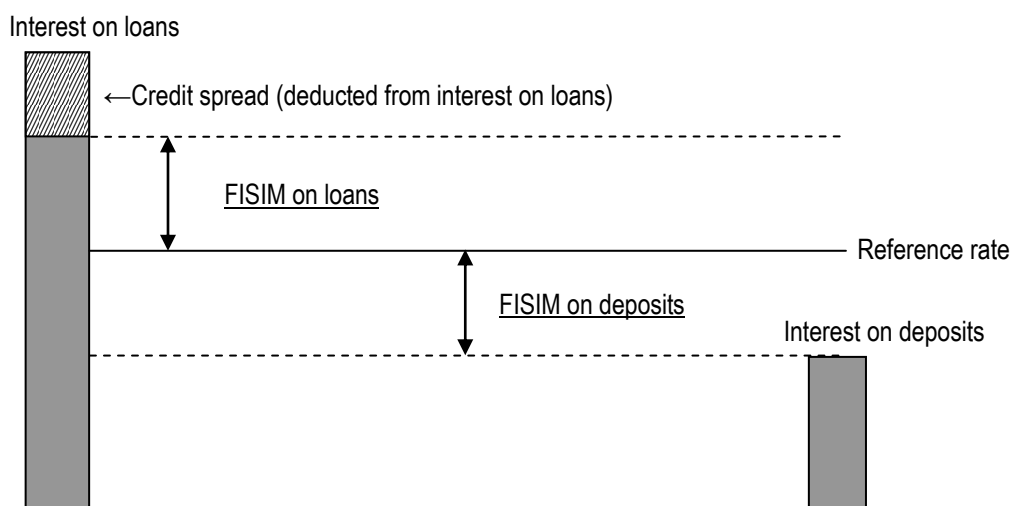
³ The purchase of goods by a resident from a nonresident will be recorded as a negative export, while the subsequent resale to another nonresident will be recorded as a positive export.

⁴ FISIM have been introduced in the SNA and BOP statistics abroad. In Japan, the Cabinet Office introduced FISIM in the SNA when benchmark year for the SNA was revised to 2005.

⁵ In Japan's BOP statistics, FISIM will be estimated in terms of three major currencies: the yen, the U.S. dollar, and the euro.

deposits. The prevailing rate for interbank borrowing and lending will be employed as the reference rate. Meanwhile, in calculating FISIM, a credit risk premium will be deducted from the interest on loans, because such a premium can be regarded as compensation for the expected cost of credit rather than charges for financial intermediation services (see Figure 1 for Appendix).

Figure 1 for Appendix: Conceptual Illustration of Calculation of FISIM



3. Introduction of financial dealers' margins

Service charges for transactions in financial instruments are broadly classified into two categories: explicit charges, and implicit charges through the spread between buying and selling prices (referred to as "financial dealers' margins" hereafter). Both charges should be recorded as "services" under the "current account." However, while the former are reported separately as service charges and recorded as "services" under the "current account," the latter are reported as part of the related financial transactions and cannot be distinguished therefrom. As a result, in the current statistics, the latter are included in components such as "portfolio investment" under the "capital and financial account."

BPM6 (paragraph 10.122) states that "the existence of a buy-sell spread . . . shows that [dealers and market-makers] serve the market in a somewhat similar way to a wholesaler, by providing liquidity and inventory" and recommends that financial dealers' margins be excluded from the "financial account" and instead be recorded under "financial services." Therefore, in Japan's BOP statistics, with the implementation of *BPM6* financial dealers' margins will be estimated by multiplying the turnover in debt securities by the relevant average spread and will be recorded under "financial services."

Consequently, transaction prices excluding financial dealers' margins will be recorded in components such as "portfolio investment" under the "financial account."

4. Change in the treatment of sales of patents and copyrights

Patents and other results of research and development (R&D) are treated as nonproduced assets under *BPM5* and their sale/purchase is currently included in the "acquisition/disposal of non-produced, nonfinancial assets" in the "capital account." On the other hand, under *BPM6* they are treated as produced assets and regarded as services. Therefore, their sale/purchase will be included in "research and development services" under "other business services" in "services" in the new statistics. This is consistent with the change in the treatment of patents and other results of R&D in the *2008 SNA*, where they were recategorized from non-produced, nonfinancial assets (intermediate goods) to produced assets (intangible fixed assets).

Similarly, the sale/purchase of copyrights (on music, video, software, literature, art, and characters), which is currently included in the "capital account," will be reclassified into the corresponding items under "services."

5. Supplementing data for "other services"

Because the threshold value for the reporting of transactions in the reports on payments and receipts (referred to as "payment reports" hereafter),⁶ one of the source materials for the *BOP*, is set fairly high, there have been issues regarding the coverage of "other services," a large portion of which consist of small-value transactions, and the main data source for which is the "payment reports."

Therefore, when switching to the *BPM6*-based statistics, data for small-value transactions in "other services" will be supplemented through estimation. Specifically, figures for each item in "other services" will be calculated by multiplying the aggregate value reported in the "payment reports" by an adjustment ratio set for each of the items.

The adjustment ratio for each item will be calculated based on the assumption that the population of transactions for each item underlying the sample of transaction data reported

⁶ In principle, reporting is not required for transactions amounting to 30 million yen or less per settlement.

in the "payment reports" follows a Pareto distribution.⁷ The ratio will be calculated annually for each item based on the corresponding data from the "payment reports" for the previous year.

6. Dissemination of direct investment income by region and industry

In the current statistics, flow data for "direct investment" by region and industry are disseminated quarterly, and data for direct investment positions are disseminated annually at year end. However, data for "direct investment income" earned from "direct investment" are currently disseminated only by region. This makes it difficult to carry out detailed analyses such as on the rates of return on direct investment.

In the *BOP* from 2014 onward, data on "direct investment income" by region and industry will be disseminated quarterly to meet users' analytical needs.

B. Financial Account

1. Change in the recording principle of direct investment

For the *BOP* and *IIP*, the recording principle for data on direct investment will be changed from the directional principle currently employed to the asset and liability principle (see Table 1 for Appendix). This modification will allow a clearer grasp of Japan's external assets and liabilities; moreover, it will improve consistency with other stock statistics, such as the *External Debt*, facilitating comparison of data between the statistics.

⁷ The reason for assuming a Pareto distribution, which is thick on the left and thin on the right, is that in the frequency distribution of amounts reported in the "payment reports" for each item under "other services" the number of reports decreases significantly as the amount per settlement increases.

Table 1 for Appendix: Change in the Recording Principle of Direct Investment

<p>Current statistics based on <i>BPM5</i>: Directional principle</p>	<p>Under the directional principle, investments of a Japanese company in overseas subsidiaries are classified as assets (outward investment) and investments of a foreign company in Japanese subsidiaries are classified as liabilities (inward investment). Investments from a subsidiary in its parent company are recorded as reverse investments, namely withdrawals from the parent company.</p> <p>For example, investments from an overseas subsidiary in its parent company in Japan are not recorded on the liability side but recorded as reverse investments on the asset side.</p>
<p>New statistics based on <i>BPM6</i>: Asset and liability principle</p>	<p>Under the asset and liability principle, investments of a Japanese company in overseas affiliated companies are classified as assets (outward investment) and investments from overseas affiliated companies in a Japanese company are classified as liabilities (inward investment), regardless of whether the company is a parent company or a subsidiary.</p>

2. Change in the definition of direct investment

In the current BOP related statistics, direct investment is defined as an investment where an investor owns 10 percent or more of the outstanding shares of the investment enterprise. In the new statistics, however, in line with *BPM6*, to focus more clearly on control and influence, direct investment will be redefined as an investment where an investor owns shares that provide 10 percent or more of the voting power in the investment enterprise.

Moreover, given that not only direct participations but also indirect participations, such as through holding companies, are on the increase within enterprise groups, retained earnings of indirectly held enterprises, such as a subsidiary of a subsidiary, will be newly recorded under "direct investment." Transactions in loans and debt securities with indirectly held enterprises will also be reclassified under "direct investment." The definition of "direct investment income" will also be changed accordingly.

3. Change in the treatment of securities lending transactions

Securities lending transactions are currently recorded under "portfolio investment," on the pretense that a change in ownership has occurred. The same amount as a corresponding entry is recorded under "other investment." However, such transactions do not involve contractual changes in ownership. Moreover, because they are large in volume, their inclusion has made it difficult to grasp actual transactions in securities. On this basis, *BPM6*

recommends that securities lending transactions should not be recorded under "portfolio investment," so that in Japan's new *BPM6*-based statistics they will no longer be recorded under "portfolio investment" or "other investment."

Meanwhile, based on the above reasoning, figures excluding securities lending transactions are already compiled and disseminated as reference data in Japan's BOP related statistics.

4. Introduction of new items related to investment funds

In the current statistics, investments in investment funds, except for those treated as "direct investment," are classified according to the type of funds: investments in corporate-type funds are recorded under "equity securities," while those in contract-type funds are recorded under "bonds and notes." In the *BPM6*-based statistics, investments in and withdrawals from investment funds, irrespective of the type of funds, will be recorded as "investment fund shares," a new item under "portfolio investment." In accordance with this classification, "investment income attributable to investment fund shareholders" will be introduced under "investment income" in "primary income" for distributed dividends of investment funds.

II. *International Investment Position (IIP)*

A. Expansion of the Coverage of Financial Derivatives

Regarding the *IIP*, in addition to the more detailed breakdown of financial items explained in the main text and the changes in the *BOP* described under I. *Balance of Payments (BOP)* above, which also apply to the *IIP*, the coverage of financial derivatives will be expanded.

Specifically, when switching to the *BPM6*-based statistics, "financial derivatives," which currently include positions in options and futures, will be expanded to include swap positions.

B. Leveling of Estimation Error for Quarterly Estimates

For quarterly estimates of the *IIP* and *External Debt* statistics, figures for the first through the third quarter are disseminated first as preliminary estimates based on the preliminary flow data of the *BOP*, and then as revised estimates based on the final flow data. By contrast, while year-end figures are also first disseminated as preliminary estimates based on the flow data of the *BOP*, final data released later are based on reports submitted for the

compilation of the *IIP*. As a result, the difference between the estimates based on adding up the flow data and the final data compiled based on the reports -- that is, the cumulative estimation error -- will show up only as the difference between the figures at the end of the third quarter and at year end (see Figure 2 for Appendix).

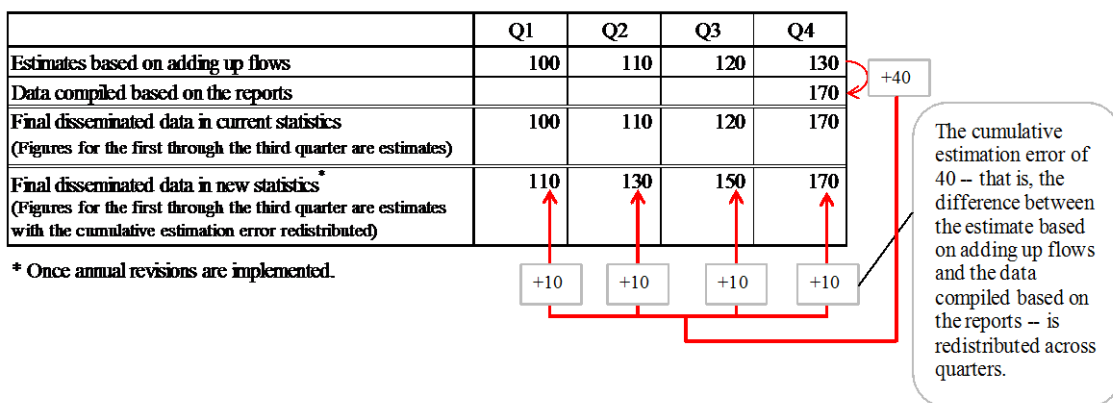
Given that this cumulative estimation error in fact builds up as the sum of errors arising when figures for the investment position for each quarter are estimated, the estimation error will be redistributed across quarters in the annual revision.⁸

This is done essentially by dividing the difference between the preliminary estimates and the final data compiled based on the reports for the *IIP* into four equal parts and adding these to the position at the end of each quarter.

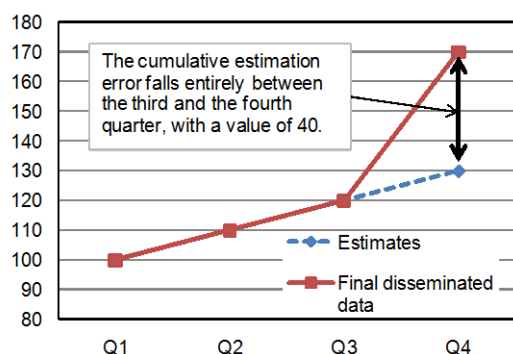
⁸ Quarterly *IIP* and *External Debt* statistics in 2014 will be compiled by adding flow data of the new *BPM6*-based statistics to the data for year-end 2013 of the current statistics, giving rise to the following issues: (1) it will not be possible to compile figures classified into the five sectors that will be introduced in accordance with *BPM6*, and (2) figures for items that involve a change in definition, such as direct investment, will be distorted. Therefore, it is planned that quarterly figures for 2014 will be compiled and disseminated based on the new breakdown of sectors and definitions using year-end figures when compiling the year-end 2014 figures based on *BPM6*.

Figure 2 for Appendix: Illustration of Redistribution of Cumulative Estimation Error

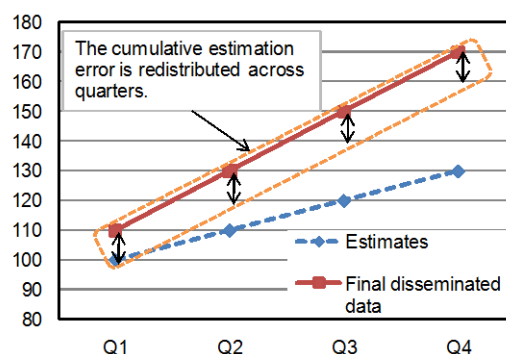
Example: The investment position for each quarter is estimated by adding up flow data, yielding the series shown in the first row below. In the fourth quarter, a discrepancy of 40 – the cumulative estimation error – arises when comparing the estimated value with the data based on the reports for the *IIP*.



Current statistics based on *BPM5*



New statistics based on *BPM6*



The cumulative estimation error of 40 is not aggregated as the difference between the third and the fourth quarter but redistributed across quarters. In this example, 10 is added to the investment position of each quarter.

III. International Transactions in Securities

The *International Transactions in Securities* are statistics on cross-border transactions in securities that are compiled with an emphasis on timeliness and cover only major financial institutions designated by the Minister of Finance in advance. As these statistics have much in common with portfolio investment in the *BOP*, the following changes will be made to maintain consistency between the two sets of statistics when switching to the *BPM6*-based statistics.

A. Sign Conventions for Net Transactions in Foreign Securities by Residents

Regarding net transactions in foreign securities by residents, the current *International Transactions in Securities* show net sales with a plus sign and net purchases with a minus sign. This convention will be reversed for transactions from January 2014 onward, where net purchases will be shown with a plus sign, while net sales will be shown with a minus sign.

B. Partial Changes in Labels of Types of Securities

From January 2014, the types of securities currently labeled "equity securities," "bonds and notes," and "money market instruments" will be renamed "equity and investment fund shares," "long-term debt securities," and "short-term debt securities," respectively, in accordance with their labels in the "financial account" of the *BOP*. "Equity securities other than investment fund shares" and "investment fund shares or units," which are sub-items of "equity and investment fund shares" in the *BOP*, will not be disseminated in the *International Transactions in Securities*.