

ICBS - Balance of Payments – Methodology summary

I. Analytical Framework, Concepts, Definitions, and Classifications

1.1 Concepts and definitions

General definition

According to international standards, the Balance of Payments is defined as a statistical statement that systematically summarizes, for a specific time period, the economic transactions of Israel with the rest of the world.

Overall conceptual framework - The Balance of Payments and BMP5 (*Balance of Payments Manual, Fifth edition, 1993 – INTERNATIONAL MONETARY FUND*)

The overall conceptual framework of the Israeli BOP is in broad conformity with guidelines outlined in the BMP5.

- Transactions between residents and nonresidents are recorded in the Balance of Payments' main accounts, namely the Current, Capital and Financial accounts, which are defined according to BMP5. The Current Account balance in principle is equal (with sign reversed) to the net Capital and Financial Account balance.
- The double-entry principle is applied and the net residual is embedded in the statistical discrepancies item.
- A clear distinction is made between Income and Goods and Services components. The Financial Account provides a separate recording of transactions in Assets and in Liabilities.
- Compilation of FDI is based on the Directional Basis principle.

Concepts and definitions used to compile the Israeli BOP are in broad conformity with guidelines outlined in the BMP5.

- The concept of residence of institutional units is broadly in conformity with BMP5 and relates to institutional units having a "center of economic interest" in the country. Examples of the application of this rule, together with one exception, are detailed below.
- Enterprises, including unincorporated branches, are considered to be residents of the economic territory where they operate, provided they have a complete set of accounts and they are operating in the territory for at least one year.
- Residence of units operating mobile equipment in international waters or airspace, is attributed to the operating enterprise's country of residence
- General government units (embassies, etc.) are considered residents of their own economy
- Regarding individuals, according to BMP5 they may cease being residents of their countries if they work continuously for a year or more in a foreign country. This principle is still not applied in the Israeli BOP with respect to foreign workers, since no distinction between them can be made according to the duration of stay. Efforts are made in order to have a more accurate statistics on foreign workers in Israel and to harmonize this statistics between different CBS departments, as Demography, Census, Labor, National Accounts and Balance of Payments.
- Transactions are defined according to BMP5 guidelines
- Both exchange and transfers (transactions without a quid pro quo) are registered
- Types of transactions are defined according to BMP5 concepts and definitions: Freight charges paid to foreign carriers are deducted from CIF value of goods' imports and registered as imports of Freight Services, goods acquired by travelers for their own use are classified as Travel Services, FDI transactions are defined applying the 10% ownership rule, reserve assets are defined according to Central Bank effective control and availability for use
- BOP transactors are defined as all resident economic entities engaged in transactions with non-residents

1.2. Classification/sectorization

- Transactions are generally classified in accordance with BPM5.
- Institutional units are classified and attributed to the relevant sector, according to the BPM5.

II. Scope of the data

2.1. Scope of the data

- Transactions coverage: The scope of resident-nonresident transactions covered by the Israeli BOP is broadly consistent with BMP5 guidelines
- Institutional units' coverage: In principle, all institutional units engaged in transactions with nonresidents are covered
- Geographic coverage: Israel, Israeli settlements in Judea and Samaria and resident territorial enclaves in the rest of the world (embassies, etc.)

2.2. Exceptions to coverage

See next item.

2.3. Unrecorded activity

Smuggling and fraudulent trading activities are not recorded in the Israeli BOP.

Also, direct investment flows related to exploration of natural resources, are still not recorded, but data on these flows are already available and will be soon incorporated into BOP. Amounts related to these flows are very small.

E-commerce transactions, also, are still not registered.

III. Accounting Conventions

3.1. Valuation

- Imports and exports of goods are valued on a f.o.b. basis
- Financial instruments traded on a regular basis are generally valued by their market value
- Direct Investment equity positions are generally valued at market values for traded enterprises. Equity capital related to non-traded enterprises, is generally recorded at book values.
- Value of transactions excludes revaluations of existing stocks.
- Conversion to unit of account - The Israeli BOP is published in US Dollars. Accordingly, original data in currencies other than the US Dollar, are converted to this currency at period average exchange rates. Efforts are made to bring some kind of transactions to exchange rates close as possible to actual transactions' dates.

3.2. Recording basis

- In general, recognition of transactions and time of recording are according to the "change of ownership" principle, as specified in BPM5.
- Imported goods are recorded upon their release from customs points, whereas exported goods are recorded according to the date they were loaded for transport.
- The accomplishment of "milestones" (work in progress) by domestic enterprises- within some large projects for non-residents- are recognized as exports, as change of ownership is deemed to occur. In these cases, the amounts involved are recognized as sales in the financial statements of these enterprises. These additional exports are part of BOP adjustments to foreign trade statistics.
- All entries for interests include accrued interests, with simultaneous recording of financial new assets or liabilities of the same type as the original asset.
- Reinvested earnings are recorded in the period they are earned.
- Contrary to the accrual basis principle, data on dividends are recorded on the date they are paid, rather on the date they are declared payable.

3.3. Grossing/netting procedures

- Gross and net basis: According to BMP5 recommendations, transactions in the Current and Capital Account are recorded on a gross basis and transactions in the Financial Account are recorded on a net basis, for assets and liabilities items separately.

IV. Nature of the Basic Data Sources

4.1. Data source collection programs

Goods

The four major sources of data for the compilation of the Goods Account, are: 1) The Excise and Custom Department (for import and export entries), 2) The Ministry of Defense, 3) Shipping and aviation companies (for purchases and sales of sea craft and aircraft), and 4) The V.A.T. authorities (for transactions with residents of the West Bank and the Gaza Area). Export trade data are based on records of the movement of goods passing through Customs. The data are based on the definitions and the administrative rules of Customs, which have been adapted to conform as closely as possible to the definition of the balance of payments (i.e., change in ownership). Imported goods are recorded upon their release from customs points, whereas exported goods are recorded according to the date they were loaded for transport. Imports and exports of goods do not include transactions that do not involve a change of ownership, like imports for exhibitions. The Ministry of Defense estimates direct defense imports of

military equipment, by multiplying unit prices by number of items for large items (like planes) and on the basis of payments made for small items. Estimated defense imports are calculated at quarterly intervals during the year and are included only in the balance of payments (i.e., they are not in the current statistics for foreign trade).

Services

- **Transportation:** The major sources for freight and transportation services are Israeli companies that operate ships and aircraft on international routes, foreign shipping and aviation companies that operate in Israel, the Ports Authority in Israel, ship and aircraft repair companies, companies that supply food and bunker oil to ships and aircraft, and the Civil Aviation Service, Ministry of Transport. Transactions include receipts resulting from the transport of cargo by foreign carriers that are temporarily leased by Israeli companies. The data also include receipts and payments by ships owned by Israeli subsidiaries under a foreign flag (convenience flag), operated by Israeli agents only. Some reports of Israeli shipping and aviation companies include a detailed breakdown of expenditures according to type of currency and not according to the location of the expenditures—in Israel or abroad. The item of “other expenditures” in these reports, which includes information from other sources, is corrected or adjusted (like the purchase of tickets for travel abroad by Israelis in foreign currency or the purchase in Israel of bunker oil in foreign currency).
- **Travel:** Credit entries are estimated using a semiannual survey of foreign tourists, conducted by the Ministry of Tourism and under the supervision of the CBS. The survey provides the average expenditure per tourist during each half year, while the total expenditure of foreign tourists is estimated according to the mentioned average expenditure and the total number of tourists leaving Israel each quarter. This latter figure according to statistics of the Tourism Department in the CBS. Debits are estimated quarterly on the basis of an updated survey that was conducted by the CBS on 1997 – regarding average expenditure per tourist – and on current data on departures abroad of Israel residents, published by the CBS.
- **Insurance:** Insurance transactions are derived from premiums less claims paid. The data also include estimates of payments by residents of the West Bank and Gaza to social funds in Israel. (The data were estimated according to reports provided by the Employment Service). The principal sources are reports from (1) the insurance companies operating in Israel (provided by the Superintendent of Insurance); (2) Israeli shipping and aviation companies; and (3) the Employment Service.
- **Other business services:**
 - **Exports**
 - Sources include data from VAT reports on transactions exempted from VAT. These data are processed and adjusted in order to reflect total exports, from which exports of goods are deducted on a company and industry level. The remaining figures on a company level are further processed for amounts exceeding a defined threshold, in order to reflect services’ exports. In this processing, ITRS data together with companies’ reports are used in order to derive final estimations on exports. Figures below the said threshold, are considered final estimations.
 - Additional sources related to exports to the Palestinian Authority, include VAT reports on transactions with the West Bank and Gaza Area.
 - Communication services are based on direct reports from companies in the Telecommunication Industry.
 - Exports of companies that outsource production abroad (“fables” companies) are separately recorded in the Services Account. Source data on these companies are mainly based on direct reporting.
 - In several cases, purchases of domestic “start-up” companies by foreign residents are partially considered exports of (R&D) services. Details of each purchase are analyzed and data related to these transactions are based on publications and reports of the companies, press, Bank of Israel and other sources.
 - **Imports**
 - The main sources are data from the ITRS, direct reports from companies in the

Telecommunication Industry and VAT reports on transactions with the West Bank and Gaza Area.

Income

- **Compensation of employees**

The two main components of this item are wages paid to foreign workers and to residents of the West Bank and the Gaza Area working in Israel.

Statistics of foreign workers is mainly based on data from the National Security Institute on average wages and on estimations of total foreign workers, provided by the CBS. All foreign workers are still treated as foreign residents by the Israeli Balance of Payments, since no distinction between workers according to the duration of stay can be made and despite the considerable growth in their number during last years. Efforts are made in order to have a more accurate statistics on foreign workers in Israel and to harmonize this statistics between different CBS departments, as Demography, Census, Labor, National Accounts and Balance of Payments.

As of 1967, compensation of employees includes estimates of wages received in Israel by residents of the West Bank and Gaza Area. Data on this item are based on estimations of the CBS on total employees from this area working in Israel and on average wages paid to them, according to the Employment Service. Tax payments on these wages are classified as transfer payments.

- **Investment income**

As of 1995, Investment Income in the Israeli BOP is reported according to the full breakdown of financial instruments, types of investment and institutional sectors, as recommended by BMP5. It should be noted that a change in methodology has been implemented since 1995. Therefore, series related to this item aren't compatible before and after that year. Also, all relevant entries for interest include accrued interests, with simultaneous recording of financial new assets or liabilities of the same type as the original asset. Principal sources of data for Investment Income are the Ministry of Finance, Commercial Banks' direct reports to the CBS, the Bank of Israel, Israeli shipping and aviation companies, Insurance Companies, and CBS' estimates based on financial positions and relevant interest rates, related to certain types of investments.

Transactions in this item include estimates of undistributed earnings and simultaneous recording of these earnings under the financial account, as direct investment.

Current transfers

- **General government.** Included are receipts of the Israeli government from grants of foreign governments. The principal sources for this item are data from the Ministry of Defense and the Ministry of Finance.
- **Other sectors.** The principal sources are data from the ITRS, data from National Institutions (Jewish Agency, United Israel Appeal, Jewish National Fund), and data from nonprofit organizations. Receipts by Israeli residents – that are transferred to Israel – as settlements per the German Personal Restitution Law, are also included. Receipts deposited abroad are not recorded.

Capital Account

- **Capital transfers.** This category includes mostly migrants' transfers. For purposes of compiling the Israeli BOP, people who have received an immigrant visa are regarded as immigrants as well as people who are indeed immigrants. This category also includes residents who have been out of the country for a long period. All deposits from abroad into immigrants' accounts were classified as immigrant transfers till year 2000. From this year on, data provided through the ITRS have been classified in order to record as capital transfers only transfers to accounts of immigrants that have been in Israel for a maximum period of three years. Transfers to immigrants that have been in Israel for more than three years, are considered to be financial transactions. Series have been updated also before 2000, according to the said definition. Financial transfers abroad by emigrants are not included.

Financial Account

- **Direct investment.** Data for components except reinvested earnings are compiled from the ITRS, by a Direct Reporting System (DRS) and data from the Israel Securities Authority, as a secondary data source. The ITRS covers cash transactions made through the domestic banking system, but not cash transactions made through foreign bank accounts of enterprises or non-cash transactions. These two last items are covered by the DRS. Reinvested earnings are compiled primarily from the companies' accounts of resident enterprises. The basic criterion for the definition of Direct Investment is a 10 percent ownership by the investor, for Inward as well as Outward investments.
 - **Equity capital** transactions include non-cash acquisition of equity, such as through the provision of capital equipment. Purchases and sales of land and buildings between residents and non-residents, are also included in equity capital transactions. Expenditures related to Natural Resources Exploration are still not included in the Direct Investment data.
 - Data on **Other Capital** transactions don't include bonds, trade credits and financial leases. The data exclude – according to international standards – transactions between affiliated banks and between affiliated financial intermediaries involving deposits, loans, and other claims and liabilities related to usual banking and financial intermediation activities. Contrary to the international standards, 1) the data don't include short-term financial transactions, such as cash management transfers, between non-financial direct investment enterprises and affiliated SPEs primarily engaged in financial intermediation, 2) the data don't include transactions related to permanent debt between affiliated banks and between affiliated financial intermediaries.
 - **Reinvested earnings** are recorded in the period in which they are earned and losses are recorded as negative reinvested earnings.
 - **Dividends** are recorded net, rather than gross, of any withholding taxes. Also, dividends are recorded according to actual payments, instead of according to the date they are declared payable.
- **Portfolio investment.** Purchases of foreign securities through local banks are reported in the ITRS. Securities purchases through residents' foreign accounts are reported in the DRS. Portfolio investments of non-residents in Israeli shares traded abroad, are estimated by the difference between the total market value of Israeli shares traded abroad and the two following items: 1) data from the Israeli Securities Authority on direct investors and 2) holdings of foreign securities by residents, reported by the banking system.
Regarding portfolio investments of non-residents in Israel: the main sources are the ITRS and data from the Israeli Securities Authority.

4.2. Source data definitions, scope, classifications, valuation, and time of recording

Source data broadly complies with BOP requirements.

In some cases, where these data differ from the standards or its quality cannot support reliable estimates, changes have been implemented in order to develop alternative sources. Regarding ITRS data related to exports of services, for example, it was found that they differ in a remarkable way from alternative data sources based on business surveys and VAT data. As declared by the Bank, quality of ITRS series related to services are deteriorating and the

Bank won't support these series in the future. In view of that, it was decided to base international trade in services estimates on different data sources and to develop a new methodology.

In some other cases, actual source data are still not supporting requirements, as mentioned above regarding dividends, foreign workers and permanent debt related to Other Capital transactions in FDI.

4.3. Source data timeliness

Source data timeliness generally is in accordance to required timeliness of BOP series, with a few exceptions:

Data on trade with the Palestinian Authority through VAT files, are not delivered to CBS in time and/or are not complete.

In several cases, data on working financial balances and other financial assets and liabilities of the government abroad, are not delivered in time from the MOF.

4.4. Source data assessment

Direct reports from companies and/or other units are currently assessed, according to previous reports and/or alternative available data.

ITRS financial data are also currently assessed and checked, mainly by the Bank of Israel and in a lesser extent by the CBS, upon the receipt of quarterly data for BOP items.

Regarding assessment of ITRS data related to the BOP Current Account, CBS is currently checking the reliability of these data for the main items in the account. In several cases, results from this assessment led to changes in source data, as was the case for main items in the Income Account and the Service Account.

Regarding the Income Account, relevant differences were found between ITRS data and calculations of interests according to balances and relevant market rates. A further checking of banking data indicated that amounts related to items not included in investment income – as payments related to derivatives – were included in ITRS data. As these data couldn't be adapted to BOP needs, source data related to the Income Account have been changed. Actual data includes now direct reporting from commercial banks and are according to the details in item 3.3.1 (Investment Income) and in item 3.1.1 (Investment Income) above.

ITRS data related to the services account have also been checked against alternative sources, leading also to changes in data sources, as detailed in item 3.1.2 above.

V. Compilation Practices

5.1. Source data statistical techniques

- **Seasonal Adjustment**

As of September 2003, the Current and Capital Account of the Israeli BOP have been published including seasonally adjusted estimates. Seasonally adjusted series are based on U.S. Dollar current prices and have been calculated and incorporated into the BOP data since 1992.

Seasonal adjustment is based on the X12- ARIMA program. All series are monitored

yearly and series without seasonality are included according to original estimates. Annual figures derived from seasonally adjusted series are not forced to be equal to annual figures from original data. Consequently, seasonal adjusted quarterly data are not strictly coherent with annual data.

- **BOP Adjustments to Foreign Trade data**

- **Exports** – The main adjustments to exports are:

- Addition of Goods exports to the Palestinian Authority (Judea, Samaria and Gaza Area). These exports are not registered through customs and data are based on specific VAT files. Due to partial lack of data, quarterly first figures are based on estimates based on previous data, which are updated in the following quarters.
- Adjustments to exports based on “work in progress” (milestones), as explained above (See item 3.2). Data on these exports are based on direct reports of large companies, engaged in this kind of projects. A register of these (only large) companies is maintained and updated by the BOP department.

- **Imports** – The main adjustment to imports are:

- Uniform value adjustment (CIF-FOB). Estimates of freight services supplied by foreign carriers on imported goods, have been recently revised according to a new methodology. New estimates are based on reported physical quantities and prices by type of freight (containers, bulk, other general cargo) and by country of origin imports. Freight charges related to fuels and coal, are reported separately.
- Addition of Goods imports from the Palestinian Authority (Judea, Samaria and Gaza Area). These imports are not registered through customs and data are based on specific VAT files. Due to partial lack of data, quarterly first figures are based on previous data, which are updated in the following quarters.
- Imports of “duty free” shops, that are not registered through customs, are estimated yearly from financial statements of the companies and estimated quarterly according to VAT distribution of revenues and quarterly revenues’ rate of change.
- Purchases of imported goods by military, diplomat or other foreign residents are deducted from total imports, according to customs’ data
- Imports of military equipment registered by customs are deducted from total imports and substituted by quarterly data received from the Ministry of Defense.

- **Other business services**

A survey was launched starting year 2004, covering exports and imports of other business services. This survey will allow the classification of these services according to EBOPS and would improve total estimates. The survey will be conducted annually.

- **Investment Income**

Portfolio debt assets – Income estimations on these assets are calculated according to quarterly positions and quarterly interest market rates, based on an average between US

Treasury Bills and US Government Bonds with maturity of 3 years.

Loans and deposits assets –*Banks* - According to direct reports to the CBS of the major 5 commercial banks in Israel. The share of these banks in the main financial variables of the whole banking system in Israel is approximately 80%.

These reports include average quarterly balances of banking loans/deposits abroad, total actual interest received in each quarter and accrued interests at the end of each quarter. From these data, interests earned are derived, according to actual interest received plus the difference in accrued interests between the beginning and end of each quarter. An average rate interest is then calculated, based on interests earned divided by average loan/deposits balances. This average rate is then applied to the total balance of loans/deposits of domestic banks, in order to get final estimations of interest income, to be registered in BOP.

Loans and deposits assets – *Other sectors* - Interests on loans to foreign residents are calculated according to average quarterly balances and interest market rates based on US dollar LIBOR, with a delay of 4 months.

Interests on deposits of residents abroad, are calculated according to quarterly deposits balances and adjusted interest rates, based on average rates of the banking system deposits abroad, estimated by the procedure detailed above.

Portfolio debt liabilities – Income estimations on these liabilities are according to specific outstanding balances and financial terms of these liabilities, as published in financial statements of the issuing domestic companies (There are very few companies having relevant amounts of portfolio debt abroad).

Loans liabilities – *Other sectors* - Interests on loans from foreign residents are calculated according to average quarterly balances and interest market rates based on US dollar LIBOR, with a delay of 4 months.

Deposits liabilities – *Banks* – The same as for Deposits Assets of the banking system, as detailed above.

Dividends and reinvested earnings –Data are compiled by the Bank of Israel through the ITRS (Dividends) and through companies' accounts of resident enterprises and the DRS (Reinvested earnings).

5.2. Validation of intermediate results

Data are currently checked against previous figures and alternative sources.

5.3. Assessment of discrepancies and other problems in statistical outputs

Statistical discrepancies are currently assessed and investigations on possible sources of these discrepancies are currently conducted.