The OECD Task Force on Financial Services

Conclusions of the meeting 7-8 October 2004
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Task Force: A Two-step process


   Included:

   - Definition of financial corporations.
   - Identifying and measuring the production of financial services.
   - Treatment of portfolio and financial property management in national accounts.

   **Report** presented at 2003 NAEM
Task Force: A Two-step process


2. Extended mandate (2003):
   - Price-volume split of financial and non-life insurance services.
   - Treatment of specialised units
   - Allocation issue
Task Force: Meeting of 7-8th October 2004

1. Redrafted general definition of financial corporations.

2. Extension of assets and liabilities taken into account in production measure.

3. First thoughts on the reference rate, the allocation and holding gains and losses.

4. First thoughts on price and volume issues.
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Financial corporations:

“...all resident corporations or quasi-corporations principally engaged in financial intermediation or in auxiliary financial activities which are closely related to financial intermediation”.
Financial Intermediation:

• “...a productive activity in which an institutional unit incurs liabilities on its own account for the purpose of acquiring financial assets by engaging in financial transactions in the market”.

• “...collect funds from lenders and transform, or repackage, them in ways that suit the requirement of borrowers”.

“...A financial intermediary does not simply act as an agent for other institutional units but places itself at risk by incurring liabilities on its own account”.
Issues statement:

• The definition of financial corporations is mainly related to financial intermediation (activity).

• “risk taking” and “repackaging” are key elements for financial intermediation.

• No specific reference is made to any particular composition of assets and liabilities.

• Ambiguity about the role of own funds.
Extended definition of financial corporations (paragraph 1)

Financial corporations consist of all resident corporations or quasi-corporations that are principally engaged in providing financial services including insurance and pension funding services to other institutional units. The production of financial services is the result of financial intermediation, risk management, liquidity transformation and/or auxiliary financial activities.
Extended definition of financial corporations (paragraph 1)

Financial intermediation, risk management and liquidity transformation are productive activities in which an institutional unit incurs financial liabilities for the purpose of acquiring mainly financial assets. Corporations engaged in these activities obtain funds by taking deposits and issuing bills, bonds or other securities. They use these as well as own funds to acquire mainly financial assets by making advances or loans to others and by purchasing bills, bonds, or other securities.

- Lists the specialised units to be included.
Extended definition of financial corporations (paragraph 2)

Unincorporated financial enterprises such as individuals and households lending money are included in the financial corporations sector, as resident corporations or quasi-corporations, if they can, on demand, produce a complete set of accounts that are separable from those of their owners in their personal capacities. However, individuals and households lending money among the members of the same household are not considered as providing financial services to other units and are therefore not included in the financial corporations sector.
Extended definition of financial corporations (paragraph 3)

Institutional units providing financial services to only one unit or a group of units are considered as financial corporations if they acquire and invest funds independently of the parent group and keep a complete set of accounts. In particular this applies to treasury units providing financial services to individuals or a company group. If the client is resident in another country, the unit is treated as a corporation in the country of residency of that unit.
Conclusions and recommendations (1)

The Task Force supports the extended definition of financial corporations for the forthcoming revision of the SNA but recommends the case made for “money lenders” also includes such units active in developed countries.
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Identifying financial services

- Financial services: the output that financial corporations produce and provide to their customers, explicitly or implicitly

- Financial instruments: the means through which financial corporations provide packages of financial services to their customers. Neither input in an SNA 93 sense (labour, capital, goods and services) nor output in terms of production of financial corporations.
Notion of an extended measurement of production

• All balance sheet items potentially involved in producing financial services.

• There should be no direct relationship between financial services and instruments/activities (requires indirect measurement).

• Extension of the deposits/loan case to other instruments includes securities other than shares (e.g. bonds), shares.
Conclusions and recommendations (2)

- There are implicitly-priced financial services attached to assets and liabilities other than deposits and loans.
- The majority of the Task Force favours a global approach which does not associate elements of production of financial services with type of financial instrument. Rather, property income inflows and outflows from all relevant assets and liabilities should be considered jointly when calculating the output. However, any such global approach has to explicitly incorporate elements of allocation.
- The global approach has to be further elaborated.
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The choice of reference interest rate: Issues

- A single or several benchmark/reference rate(s) reflecting the maturity structure of financial assets.
- How to measure the risk free rate(s) of various maturities?
Conclusion and recommendations (3)

- A majority of the Task force supports the use of a single reference rate.

- **Maturities** are seen as an important issue which must be dealt with specifically.

- The issue of **subsidized interest flows** has to be taken on board.

- Work on **imports** and **exports** must be coordinated with work done by the IMF.
Issue of allocation

- The SNA 93 clarifies that....’’ in principle, total output of financial services should be allocated among the various recipients or users of the services for which no explicit charges are made ’’.
- Difficult to find conceptually appropriate methods for allocating implicitly priced services.
- A significant development work on allocating implicitly priced services was undertaken within the European Union.
Holding gains and losses: Current treatment

- Accrue during the accounting period to owners of financial and non-financial assets as a result of price changes.
- Represent changes in value of an asset due to changes in its price that constitute neither transactions nor income.
- Appear in the revaluation account.
Holding gains and losses: Issues

- Expectations of holding gains provide incentives to engage in productive processes.
- Holding gains are an integral part of the decision making process.
- Holding gains are components of returns on financial assets which might be considered.
Conclusions and recommendations (4)

- The Task Force agrees that if holding gains or losses are to be considered to be a proxy when measuring the output of indirectly-priced financial services, ex-ante (expected) –and not ex-post (actual)- holding gains/losses would be the appropriate measure.
- There was no agreement in the Task Force on if and how to include expected holding gains in the measurement of indirectly-priced financial services.
- **Further work** needs to be done in this field.
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Price-volume split of financial services indirectly measured: Issues

- No directly observable price or quantity representative of the output

- Methods:
  - Volumes based on extrapolation of base period values
  - Derivation of volume indicators by breaking down the different activities generating financial services (e.g. granting of credits, savings, money transfers etc.).
Conclusions and recommendations (5)

- The Task force recommends that **further investigation** is made into the definition of feasible consumer price indices for implicit financial services.

- More work needs to be done in the **numerical confrontation** of current practices so as to carve up meaningful differences.
Price-volume split of non-life insurance services: Issues

- The output at constant prices: measured by deflating the current output by an appropriate index or indices (mostly CPI and PPI relating to insurance services).
- Calculation based on detailed insurance branches: the volume is calculated for each insurance branch and then the results are aggregated. In the case double deflation is used, both the premiums and claims are deflated by feasible indices.
- How to handle the issue of risk when choosing volume and price indicators?
Conclusions and recommendations (6)

- There was no agreement in the Task Force on whether to recommend single or double deflation of non-life insurance output.
- The Task force recommends that further investigation is made into the definition of risk adjusted consumer price indices by branches for non-life insurance services.
Future work of the Task Force

- Further elaborating the recommendation about the global approach to be based on property income inflows and outflows for calculating the production of financial services.
- Handling the issue of maturities for the choice reference interest rate approach.
- Further investigating the definitions of feasible consumer price indices for implicit financial services and risk adjusted consumer price indices by branches for non-life insurance services.
- Collecting more information on various practices of allocating indirectly priced financial services.