

Globalisation: an outline of sub-topics to be presented to NSCASE, and an introduction to the first sub-topic of “Valuation of Imports and Exports of Goods in the International standards”

Introduction

1. This paper is presented to NSCASE by the Office for National Statistics (ONS) as the first in a series relating to the broad topic of Globalisation. Globalisation increasingly creates challenges for statistical compilers in their efforts to capture economic activities accurately. The international statistical community, led by the IMF Globalization Task Team (GZTT), recognises that new definitions and guidance need to be considered.
2. The paper lists the sub-topics that will be covered in the series of Globalisation papers and introduces the first of these sub-topics namely the Valuation of Imports and Exports of Goods in the International standards (Guidance Note G1 – provided in reading pack).
3. We ask NSCASE to:
 - a. Confirm if they agree with our planned course of action to follow the draft Balance of Payments and International Position Manual, seventh edition (BPM7) guidance in relation to Valuation of Imports and Exports of Goods. This involves retaining valuation on a free-on-board (FOB) basis until any point (the target being when BPM8 is introduced, likely in the next decade) at which time international standards should move to a new valuation method. Alongside this we will align with international activities and initiate an exploration of specifics associated with moving to an observed invoice-based valuation approach, which is the international goal for valuing trade in goods in future BPM manuals.
 - b. Discuss and provide any advice regarding the valuation of imports and exports of goods approaches, and any thoughts at this stage that will help ONS structure its exploration of the feasibility and net benefit of moving to an invoice-based valuation approach.

- c. Detail any further information they would like to be informed of on this sub-topic, or the sub-topics that we will present subsequently, in order for them to provide comprehensive advice to ONS.
4. Note that the International Standards for National Accounts and Balance of Payments are the System of National Accounts 2008 (2008 SNA), and the Balance of Payments and International Investment Position Manual, sixth edition (BPM6). Implementations are currently influenced by the specifics listed in European System of Accounts (ESA10). Both 2008 SNA and BPM6 will be replaced by updated guidance, in 2025 SNA and BPM7 respectively, later this decade. Note, also, that ONS trade statistics (a key aspect of globalisation considerations) align with BPM but are additionally nuanced by International Merchandise Trade Statistics 2010 (IMTS 2010) and The Manual on Statistics of International Trade in Services 2010 (MSTS 2010), for which the UN Statistical Commission has approved a revision of manuals. This approval stipulated ensuring consistency with the update of SNA and BPM.

Sub-topics to be covered in the Globalisation paper series

5. We plan to present five topics, in the order listed in points 5a. to 5e. This should provide a logical build-up of the detail, from a focus on the physical trade of goods to increasingly intangible considerations:
 - a. Valuation of imports and exports of goods. Our consideration is whether to align with the international direction of travel which involves retaining the existing approach (of free-on-board (FOB)) into the next decade, while investigating the feasibility of adopting a new valuation basis, based on transactions invoices, in the longer term.
 - b. Handling of factory-less producers, considering aspects associated with sending goods abroad for physical transformation. The international statistics community is considering numerous aspects including disentangling transactions related to global manufacturing arrangements, and clarifying the treatment of merchanting (i.e. the purchase by a resident

- (of the compiling economy) from a non-resident, and the subsequent resale to another non-resident).
- c. Global value chains and treatment of Multinational Enterprises (MNEs) and intra-MNE flows: how the value of trade is allocated. This considers the need for greater guidance on recording cross-border flows of intermediate goods before the final good is produced, to produce more accurate Global value chains and Trade in Value Added statistics.
 - d. Definition and treatment of Special Purpose Entities (SPEs) including their residency, plus considering economic ownership of Intellectual Property (IPPs) and the recording of intra-MNE transactions.
 - e. Classifying payments for Marketing assets. This addresses the question of whether we should support plans to change the recording of Marketing assets, which is currently non-produced non-financial assets.
6. Once the full set of Globalisation sub-topic papers has been presented and NSCASE advice has been received, ONS plans to present a summary of our combined plans for addressing the sub-topics, in 2024.

Valuation of Imports and Exports of Goods in the International standards

Background

7. Total trade comprises transactions in a) goods and b) services. ONS publishes UK Goods, and Services, imports and exports statistics as standalone series, based on Balance of Payments definitions. These data are also core inputs to statistics such as Balance of Payments (for which we align with BPM6 international standard) and Supply and Use Tables (SUTs) for which compliance is more complex.
8. The distinction between the physical good and the services associated with their trade is often difficult to disentangle, and complex processing activities take place to comply with international valuation standards. These standards and associated processes are recognised internationally as flawed, originating

from specifics described in points 9 to 11.

9. Currently, the 2008 SNA and the BPM6 both state that trade in goods should be valued on a *free-on-board* (FOB) basis. That is, both imports and exports of goods should include each of: a) the cost of the physical good and, b) costs of insurance and freight for transporting the good between the point of leaving the manufacturer to the point of departure from that country.
10. However, although statistics on goods exports are presented on an FOB basis, many countries' statistical compilers (including the UK) receive data for imports of goods on a *Cost, insurance, and freight* (CIF) basis. The CIF basis includes, in addition to the FOB aspects, the cost of insurance and freight between the point of leaving the country that the UK is importing from, and the point of arrival in the UK.
11. The reason for goods imports data being on a CIF basis is that customs declarations data, which are the source for most countries' trade in goods statistics, comply with International Merchandise Trade Statistics (IMTS) standards which state imports should be recorded on the CIF basis. In the UK, the source data is customs declarations from HMRC.
12. The details outlined in points 9 to 11 signify that international data statistics compilers face multiple challenges that threaten the quality of some trade in goods (and as a knock on, some elements of trade in services) statistics. This is true for the UK also, where the data received from HMRC need to be adjusted to comply with SNA and BPM standards. Both the 2008 SNA (Chapters 14 and 18) and the BPM6 (Chapter 10) provide guidance for applying a *CIF-adjustment*. However, the process of applying this adjustment has three broad flaws:
 - a. Firstly, it is very challenging to do this accurately. The adjustment focuses on removing the value of services involved in transporting the goods. However, the country of residence of the services providers is very difficult to define and has a potentially large impact (not quantified) on the trade in goods statistics.

- b. Even when the *CIF-adjustment* is applied, the outcome valuation is inconsistent with a part of 2008 SNA which values domestic transactions on a different basis, namely output valuation at basic prices.
- c. The SNA and BPM specify an FOB valuation basis. However, the UK process of producing SUTs complies with European System of Accounts (ESA 2010) which states that the valuation of trade should be on a CIF basis. This means that the *CIF-adjustment* conducted on the raw HMRC customs declarations data, to comply with BPM6, is then reversed (but not necessarily using a mirror version of processes) to produce the SUTs.

13. These statuses, most notably those explained in 12a. and 12b., have influenced the international position to target a future move to a new valuation method of *observed transaction value* (which is the value recorded in invoices) based on new data sources. The invoice values method has a different basis to FOB in that it is aligned with the principle of *change in ownership* (which is the basis of the balance of payments) rather than the *cross-border* concept that currently exists. Given the difference, it is critical that a period of detailed investigation, considering both trade in goods and associated elements of trade in services, takes place. During that period, the existing guidance for valuing trade in goods on an FOB basis will be rolled forward into 2025 SNA and BPM7. This will give countries time to assess the quality of alternative data sources, impact on systems and estimates, and prepare for a transition to the new valuation method should it apply in subsequent versions of both SNA and BPM; note that we, like some other countries, anticipate facing quite substantial challenges associated with a change. Specifics relating to this international position are:

- a. Draft guidance for BPM7 Chapter 10. Goods account: Annotated Outline (which is included in the reading pack) is *“The chapter will retain the current standard for valuing general merchandise using free on board (FOB)-type valuation. However, the chapter will note that the valuation of imports and exports at the observed transaction value is*

conceptually preferred and, subject to further testing, will be introduced as the standard in the next version of the manuals...”.

- b. Consultation with Bank of England, who represent the UK at the IMF Committee on Balance of Payments Statistics (BOPCOM), has confirmed the basis of this guidance. The October 2021 AEG of BOPCOM concluded *“Countries will be encouraged to take steps and start collecting the information and testing before the next update is initiated. This will provide economies ample time to undertake the necessary institutional changes/arrangements to get access to invoice values, particularly in economies where the data are not easily accessible, as well as enough time for quality testing..”*
- c. The Task Team on International Trade Statistics, in its GNV.7 (included in reading pack), discusses the options for IMTS to record the invoice value in addition to the statistical value, to encourage data collectors to support making available data that can be used by the balance of payments and national accounts in the next decade to compile exports and imports of goods on the new valuation basis.

14. If the international exploration discussed above were to conclude that a move to the invoice-based valuation principle was infeasible, we anticipate that GZTT would propose retaining the FOB valuation for trade in goods. Guidance note G1 outlines that member states, when consulted, did not prefer this option, but they did not reject it as long as there could be improved guidance for CIF adjustments and better data sources might be found.

15. A relevant consideration in relation to point 14 is that Walter (2018), in their proposal to move to observed transaction valuation, argued that the current valuation method was designed at a time when goods circulated between countries under strict customs controls, whereas reduced customs controls prevail now. Therefore, a consideration for the UK is that the move to increased customs controls for trade in goods following the UK’s exit from the EU may increase the relevance of the FOB method for UK statistics. However, this is far from definite, and the impact of evolving trade arrangements associated with increased globalisation is a critical

consideration. Further, we note that considerations like this need to be balanced against aspects such as any misalignment with other countries' approaches to valuation which would be expected to lead to increased asymmetries with those countries' statistics.

Options for the UK

16. We present three hypothetical options below (see Table 1), in order to demonstrate a balanced consideration of how we might go forward. However, in reality Option 2 is neither achievable within the timescale of BPM7 given the substantial exploratory and development work that would be required, nor desirable. Further, we see substantial risks associated with Option 3 because it would leave us unable to influence international standards and could result in a delay in aligning with changes in standards.

17. Therefore, we believe that Option 1 is the only realistic option for the UK to adopt in order to retain international consistency in the short term and long term.

Table 1 – Table of Proposed Options

Option	Benefits	Disbenefits	Relation to SNA/ESA
<p>Option 1: Follow the BPM7 guidance to: a) retain the current FOB valuation of trade in goods methods, and b) investigate feasibility of adopting valuation of imports and exports at the observed transaction value</p>	<ol style="list-style-type: none"> 1. It will mean we align with international standards 2. It will allow us to conduct a robust feasibility assessment before any change 3. It will enable to us to assess how to handle any discontinuities to our data series (including feasibility of dual running on different methods) 	<ol style="list-style-type: none"> 1. It retains the existing weaknesses inherent in the CIF-adjustment process (although impact on quality of estimates is not defined) 	<ol style="list-style-type: none"> 1. If no change in ESA, it would mean that we retain the current relationships in the short to medium term 2. We would not plan to align with any updates in ESA should they deviate from BPM and SNA guidance
<p>Option 2: Implement a change to the valuation of trade in goods, at the point of, or as soon as possible after, BPM7 implementation</p>	<ol style="list-style-type: none"> 1. It might improve quality of statistics. However, we do not know whether or not this is the case 	<ol style="list-style-type: none"> 1. We have no understanding of whether an alternative method would be better, or feasible 2. UK statistics would be inconsistent with international statistics 	<ol style="list-style-type: none"> 1. We would be out of line with international standards, without a clear reason
<p>Option 3: Retain the existing valuation of trade in goods standards, but do not investigate feasibility of adopting valuation of imports and exports at the observed transaction value</p>	<ol style="list-style-type: none"> 1. Would mean that resource could be utilised on other workstreams 	<ol style="list-style-type: none"> 1. We know that the current method is flawed, and that quality could be improved 2. UK would be out of line with other countries, leading to greater asymmetries 	<ol style="list-style-type: none"> 1. We would be out of line with BPM and SNA

Conclusion

18. We believe that we must align with BPM7 and 2025 SNA in retaining, for now, the current methods employed by ONS for valuing trade in goods. However, we will keep abreast of, and actively engage in, international discussions and consultations on the topic of the valuation of trade in goods (and naturally trade in services). There is no clear timetable for these international activities, but we anticipate they will intensify after 2025.
19. ONS should identify resource to initiate an ongoing consideration of specifics associated with moving to an invoice-based valuation approach. This will include the definition of information required to produce statistics on that valuation basis and an exploration of potential data sources (notably HMRC data based on invoice values, for which the quality is currently considered not suitable, but also to consider other possible data sources). Further, ONS will explore the feasibility of producing ongoing and historical estimates on any new basis, consideration of processing and other logistics, an assessment of which statistics would be impacted, and perceived advantages and disadvantages of changing. In this process ONS will engage with UK stakeholders, notably Department for Business and Trade, HM Treasury, and Bank of England, who use National Accounts, Trade and Balance of Payments statistics.
20. Because of uncertainty around a possible future change on the valuation basis within SNA and BPM guidance, we will record the downsides associated with our current processes. This will strengthen our ability to influence future international guidelines in case the international exploration results in a recommendation of retaining a FOB valuation, but with improved guidelines.
21. Until the full assessment of any changes to the manuals can be completed, we do not plan to detach from the current compliance with ESA 10.

References

BPM7 Chapter 10. Goods Account: Annotated Outline.

<https://www.imf.org/-/media/Files/Data/Statistics/BMP7/Chapters/ao-bpm-ch-10.ashx>

Joint Globalization Task Team (GZTT) paper G.1 Valuation of Imports and Exports of Goods in the International Standards (CIF to FOB Adjustment).

https://unstats.un.org/unsd/nationalaccount/RAdocs/ENDORSED_G1_Valuation_Imports_Exports_CIF_FOB.pdf

Task team on International Trade Statistics Guidance Note v7: Valuation – utilizing value in addition to CIF, FOB (Goods).

https://unstats.un.org/wiki/pages/viewpage.action?pageId=160137218&preview=/160137218/160137578/GNV.7_Valuation_utilizing%20invoice%20value%20in%20addition%20to%20CIF%20FOB.pdf

Walter, 2018, [Measuring merchandise and international freight transportation costs in the Balance of Payments](#), paper presented to the Organization of Economic Cooperation and Development (OECD) Working Party on International Trade in Goods and Trade in Services Statistics (WPTGS)