

IS THERE TRADE WITH OTHER PLANETS?

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The story of balance of payments deficits is depressingly familiar. In 1975, 88 of the 105 countries reporting to the IMF had a deficit on current account. Obviously many of the remaining 17 countries had large current account surpluses. But were these surpluses actually large enough to add up to the accumulated deficits of the first group? The failure of countries' international trade statistics to match those of their partner countries in the identical transactions is notorious. Perhaps there is a persistent bias toward pessimism in balance of payments reporting techniques.

Table 1 presents some balance of payments statistics for the world as a whole. The current account balance for the world is never exactly zero, and is indeed frequently negative, especially in the last few years. The average over the 13 years shown in the table is a deficit of \$1.97 billion.¹ Unless this world deficit represents trade with other planets, the implication is that there is a bias toward debit items in the world's balance of payments reporting techniques.²

Furthermore, the table indicates that this bias is entirely concentrated in services and government transfer payments. Some of the causes of the bias have already been analyzed in Smith (1967). Some importing countries estimate freight and insurance charges by a rule of thumb that may overstate them. Ships flying Liberian, Panamanian, and other flags-of-convenience frequently do not report their earnings to any country. In the category of government-purchased military services, the host country may underreport because the information is either difficult to obtain (for example,

Table 1: World Balance of Payments Accounts

	Billions U.S. dollars										Billions SDR's					
	61	62	63	64	65	66	70	71	72	73	74	75	76			
Goods and Services	2.0	1.1	1.7	2.4	2.0	2.6	1.0	4.5	8.5	11.8	5.8	-2.7	-16.0			
Merchandise f.o.b.	3.7	2.3	2.7	3.6	2.4	3.8	8.8	10.8	12.4	15.8	15.6	14.4	3.9			
Nonmonetary gold	0.8	0.8	0.9	0.9	0.9	0.9										
Services	-2.5	-2.0	-1.9	-2.1	-1.3	-2.1	-7.8	-6.3	-4.0	-4.0	-9.8	-16.8	-19.8			
Freight	-1.4	-1.4	-1.6	-1.9	-2.2	-2.5										
Merchandise																
Insurance	-0.0	-0.2	-0.2	-0.1	-0.2	-0.2										
Other																
Transportation	-1.3	-1.2	-1.2	-1.3	-1.0	-0.9										
Travel	0.3	0.3	0.5	0.6	1.0	1.2										
Direct Investment																
Income	0.7	1.0	1.0	0.9	0.9	0.7										
Other Investment																
Income	-0.1	-0.0	-0.2	-0.2	-0.3	-0.7										
Government n.i.e.	-1.2	-1.2	-1.1	-1.0	-1.0	-0.8										
Nonmerchandise																
Insurance	-0.2	-0.3	-0.2	-0.3	-0.2	-0.2										
Other	0.7	1.0	1.1	1.2	1.7	1.3										
Transfers	-1.9	-2.0	-1.8	-2.1	-2.5	-2.8	-3.6	-4.3	-5.2	-4.5	-6.9	-5.1	-4.7			
Private Transfer																
Payments	0.3	0.5	0.4	0.2	0.1	0.1										
Central Government																
Transfer Payments	-2.2	-2.5	-2.2	-2.3	-2.6	-2.9										
Current Account Balance	0.1	-0.9	-0.1	0.3	-0.5	-0.2	-2.5	0.2	3.2	7.4	-1.1	-7.8	-20.7			
\$/SDR							1.00	1.086	1.086	1.206	1.224	1.171	1.162			
Current Account Balance in \$							-2.5	.2	3.5	8.9	-1.3	-9.1	-24.0			

Source for 1961-66: Smith (1969), Source for 1970-76: IMF Balance of Payments Yearbook (1977)

overseas soldiers' consumption of local products) or because it is politically sensitive. In the category of government transfers there is an obvious potential incentive for the donor country to exaggerate the value of aid and the recipient country to minimize it. This is particularly easy to do, for example, in the case of transfers in the form of surplus agricultural commodities which may be evaluated by the donor country at its high support price and by the recipient country at the lower world price.

There is one possibly important source of bias toward debit items not mentioned by Smith. In countries that have overvalued exchange rates and restrictions against capital outflows, importers frequently overinvoice, in order to obtain extra foreign currency from the central bank, and exporters frequently underinvoice, in order to avoid handing over their foreign currency earnings to the central bank. If reporting in the partner country is based on more accurate invoicing, then the effect is to exaggerate the world's import figures and understate its export figures.

As one would expect from some line items in Table 1, particularly in the merchandise trade balance, there are also some biases in the credit direction mentioned by Smith. To the extent that importing countries overestimate freight and insurance charges, they underestimate the f.o.b. value of their merchandise imports. Trade between nonreporting (Communist) countries and reporting countries, which one would expect to show a surplus for the reporting countries, may have become a larger problem for the accounts since Smith's paper was written. Another factor in the merchandise balance is the habit of recording exports at the time

of shipping departure and imports at the time of arrival. If world trade is growing over time, then the timing problem creates a credit bias; it is interesting to note that 1975, a year which marked a sudden slowdown in the growth of total world trade (in nominal terms), is the first year in which the world accounts show a deficit in goods and services. In the category of direct investment income, the U.S. reports foreign net reinvested earning credits while many host countries do not report the corresponding debits; and the investment income of owners of flag-of-convenience shipping companies is reported as a credit to their country of residence while the companies may not report the debit to any country.

The possible source of bias that one thinks of first is not mentioned by Smith: smuggling. Of course to the extent that illegal transactions are not reported in either of the two countries, there would be no bias in the world balance. But often a transaction that is not reported in the country in which it is illegal (or is heavily taxed or otherwise restricted) is reported in the partner country. Since import restrictions are more common than export restrictions, smuggling is another source of bias in the credit direction.³

The importance for individual countries of the world balance of payments figures probably consists less of support for the possibility of bias toward deficit in the reported current account balance, than of evidence that systematic biases, both positive and negative, do exist in many of the line items.

FOOTNOTES

1. It must be admitted that the mean, with a standard deviation of \$7.39 billion, is statistically insignificant. However many of the individual line items have means that are significantly less than, or greater than, zero.

2. The possibility of extraterrestrial trade seems an unlikely one. However see Krugman (1978). It is interesting to note from the transfers line in the table that if extraterrestrial economies do exist, they receive substantial foreign aid from our planet, suggesting that the standard view of other civilizations as being more advanced than our own may be incorrect.

3. Of course smuggling of exports is also common in some places. For example, producers of coffee and cocoa in some African countries smuggle a very high proportion of their exports out of the country rather than turn it over to their governments at an artificially low price. This type of smuggling could be viewed as an extreme form of export underinvoicing (to avoid exchange controls), already mentioned above.