

Box 2 Revised compilation of current accounts

In recent years the imputed capital gains on foreign securities holding of residents has been entered as factor income in the current account, since information has been lacking about dividend payments from abroad. While this method is not in line with international standards for the compilation of national accounts, it had no significant impact on the calculation on the current account until 1998, since holdings of foreign securities and equities was very small. The stock of financial assets abroad owned by Icelandic residents has grown rapidly in recent years, particularly the stock of foreign equities. In 1994, i.e. before the final restrictions on capital movements were abolished at the beginning of 1995, Iceland's foreign equity stock amounted to 3½ b.kr. At the end of 1997 it amounted to 40 b.kr., and its value was estimated at 103 b.kr. at the end of last year. In part this rapid growth is the result of soaring share prices in foreign markets in recent years. As the stock of foreign equity multiplied the imputed gains had a progressively larger impact on the current account balance, especially as share prices rose quite rapidly over the past two years. The estimated capital gains amounted to 1.6 b.kr. in 1997 and 6.8 b.kr. in 1998, and would have been 14.8 b.kr. last year had the same method been employed as before. This would have distorted the international comparability of domestic balance of payments statistics. Although the change in methodology does not alter the underlying

economic development, the less favourable outcome of the new method underlines the sensitivity of underlying economic trends. Recent upheavals in international equity markets confirm that unrealised capital gains cannot be taken for granted. In that sense the former method of calculation concealed an inherent risk in the current account balance. On the other hand, in the long run earnings from equity ownership are largely realized through buying and selling of shares rather than direct dividend payments. International standards therefore underestimate to some extent the long term benefit to the economy of foreign equity ownership.

Chart 5

Foreign security investment at year-end 1991-1999 and imputed investment gains

