The external balance sheet of the United Kingdom: developments to end–1982

This article continues an annual series, providing an inventory of external assets and liabilities. Net external assets increased very rapidly in 1982, and have more than doubled in the last two years. The increase was much larger than the measured balance of payments surplus on current account, the difference being largely explained by changes in the value of existing assets and liabilities.

The article sets the recent rise in its historical context, examining the main influences on the value of external assets and liabilities since 1970. These influences include the impact of movements in exchange rates and asset prices, the separate contributions of flows of new investment and of reinvested earnings, and the consequences of the development of North Sea oil and gas and of the abolition of exchange controls.

The main developments in 1982 (Table A) were:

- *Valuation changes—in which sterling's decline against the dollar was an important factor—sharply increased gross assets and liabilities measured in sterling, and also raised net assets by around £7–8 billion.*
- *The current account surplus of over £4 billion, with its corresponding net capital outflows, accounted for less of the rise in net assets than in 1981.*
- *After revaluations, the stock of private net portfolio investment rose by £12½ billion, more than accounting for the rise in total net assets. Just over half the increase arose from valuation changes: net acquisitions, at £6 billion, were partly a continuing effect of the abolition of exchange controls.*
- *Net direct investment abroad also rose, by almost £3½ billion.*
- *Net banking and other commercial liabilities rose by nearly £5¾ billion, acting as an important offset to the total rise of nearly £16 billion in net investment assets.*

The value in sterling of the UK's stock of overseas assets can increase through revaluations and the reinvestment of income; and by acquisitions, funded either through the sale of goods or services to abroad (contributing to a surplus on current account), or by increasing liabilities to foreigners (a capital inflow). It is natural to seek to explain the increase in *net* foreign assets in terms of a combination of revaluation effects—arising from movements in exchange rates and in the market prices of negotiable instruments—and transactions effects arising from the current account. However, this framework needs to be used with caution in two respects: the revaluations may not be permanent; and it is sometimes difficult to distinguish between revaluations and flows of interest, profits and dividends.

Valuing stocks of assets and liabilities poses problems, since these stocks encompass instruments denominated in a variety of currencies, and with varying degrees of capital certainty: and both exchange rates and interest rates can undergo substantial swings. For example, if dollar interest rates were unusually low, and the dollar unusually strong,

Table A
UK external assets and liabilities

£ billions

	End-1981	Identified trans-actions in 1982(a)	Reval-uation	Total change over year	End-1982
Private investment					
Portfolio					
Assets	**24.4**	5.9	7.4	13.3	**37.7**
Liabilities	**5.8**	0.1	0.8	0.9	**6.7**
Net assets	**18.6**	5.8	6.6	12.4	**31.0**
Direct					
Assets	**42.5**	3.9	2.9	6.8	**49.3**
Liabilities	**27.4**	3.1	0.3	3.4	**30.8**
Net assets	**15.1**	0.8	2.6	3.4	**18.5**
Net private investment assets	**33.7**	6.6	9.2	15.8	**49.5**
Net banking and other commercial assets	**– 7.1**	– 3.9	– 1.8	– 5.7	**–12.8**
Net public sector assets	**1.9**	– 1.3	0.1	– 1.1	**0.7**
Total net assets(b)	**28.5**	1.4	7.5	8.9	**37.5**
Gross assets	**319.3**	29.0	51.2	80.2	**399.5**
Gross liabilities	**290.7**	27.6	43.7	71.3	**362.0**

(a) The coverage of this inventory is less than in the balance of payments statistics so that transactions identified here do not equal total balance of payments capital flows.
(b) Totals may not match components because of rounding.

Statistical limitations

An inventory of the United Kingdom's external assets and liabilities is subject to important limitations. The coverage of certain assets and liabilities, particularly those relating to insurance and property, is fragmentary; others, though included, are difficult to identify or value accurately, so that some of the figures are no more than broad indications of magnitude.

There may be additional difficulties in distinguishing between changes that derive from balance of payments flows and revaluations. In some cases (eg direct investment and some portfolio investment), end-year stocks are derived from opening stocks and the year's flows, with an estimate for revaluations, and thus depend on the accuracy of the revaluations. In others, balance of payments flows are deduced from changes in outstanding stocks after the size of revaluations has been assessed (eg some of the banking figures). And for some items in the balance of payments (eg inward and outward direct investment relating to UK insurance companies) there are entries in the balance of payments estimates, but only partial coverage in the inventory. Some of these problems may be reflected in the balancing item — the discrepancy between identified capital account transactions and the current account— which was unusually large (£3½ billion) in 1982.

the sterling value of fixed interest dollar stock might be considered abnormally high on both counts. A substantial portion of these revaluation effects can be attributed to actual and expected inflation rates abroad and at home, with exchange rates moving to compensate to some extent for differing inflation rates, and interest rates responding to domestic inflation rates. The compensation is, however, far from complete: and neither real exchange rates nor real interest rates have been notably stable in recent years. In much the same way, although equity prices move over the longer run so as broadly to compensate for the effects of inflation, real equity values, too, move far from smoothly.

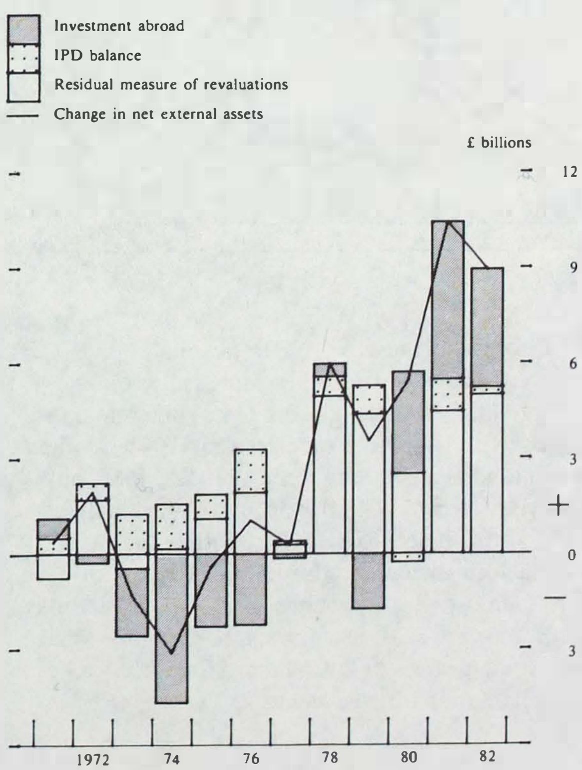
Economic behaviour will not respond fully to apparent valuation gains which are thought unlikely to be maintained. In principle, then, it might be desirable to revalue holdings in terms of an underlying exchange rate (and similarly for interest rates and equity prices), so as to distinguish the more permanent elements in current valuations. The practical difficulties are severe. These considerations should nonetheless act as a warning against giving too much weight to estimates at current market value at any one particular date, especially since those estimates are themselves less reliable than might be wished.

The 'permanent' component of revaluations is an important part of the return on assets. The remainder of the return takes the form of receipts of interest, profits and dividends (ipd), recorded in the current account. In conditions of inflation, much of these current returns—particularly in the case of interest payments on floating rate debt—amounts to an early repayment of capital. It is therefore difficult to separate net investment, revaluations and income streams in any meaningful way. The different treatment in the balance of payments of income on direct and portfolio investment causes a similar confusion between income and capital, though for a different reason. In the case of direct investment abroad, retained earnings are treated as a current account credit, with an offsetting direct investment outflow. A portfolio investment in the same company would give rise to no such effects; assets abroad would only rise through a revaluation effect, to the extent that the market value of the holding reflected the retained earnings. In principle, the effect on the value of assets held abroad might be the same in both cases: in practice it probably would not. But in the first case the increase in value would be deemed to arise from a current account surplus, and in the second it would appear as a revaluation effect.

It would, in principle, be useful to distinguish changes in net external assets from three sources: from growth in asset values broadly compensating for inflation; from the reinvestment of real income from existing net assets (after an allowance for maintaining the real value of monetary assets and for depreciation on tangible assets); and from net acquisitions. In practice, revaluations and net ipd flows together combine, in an indistinguishable way, the flows corresponding both to compensation for inflation and to real income, and are additionally affected by swings in real exchange rates and asset prices. Nor do capital flows, as recorded in the balance of payments, correspond at all precisely to net acquisitions; this is partly for the reasons already advanced but also because the balancing item—still very sizable for 1982—is likely to conceal substantial unrecorded flows.

One possible approach is to use the balance of trade in goods and services, plus transfers, as a measure of the

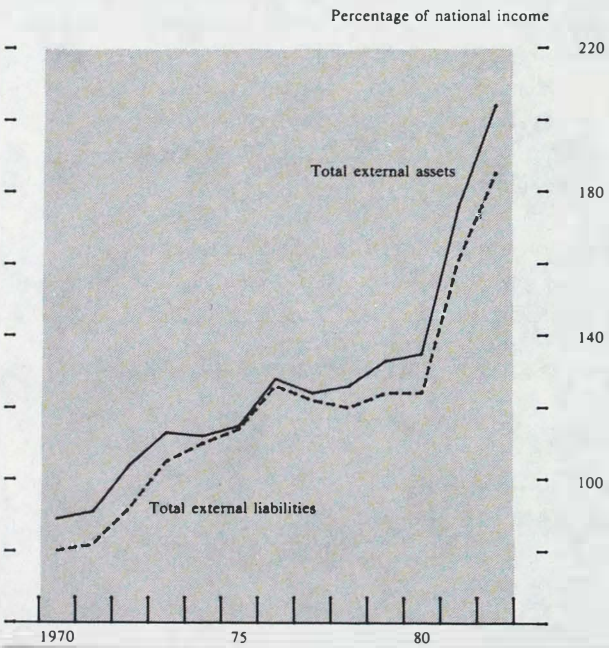
Chart 1
Sources of growth in net external assets



amount made available for net investment abroad. This balance is equal to recorded capital flows plus net ipd and the balancing item (with appropriate signs). To define 'investment abroad' in this way is to focus on the resources made available for transactions in assets with other countries by way of transactions involving flows of goods and services.

Chart 1 separates changes in net foreign assets into the contributions of 'investment abroad' and the effects of ipd flows and revaluations. (Revaluations are here defined as the residual item.) 'Investment abroad' has been negative over much of the period from 1970 to 1980. More recently, trade surpluses have added to the stock of net assets. Over almost the whole period, revaluations and the ipd balance together have been by far the most important sources of growth in net external assets, as might be expected in conditions of inflation where assets initially exceed liabilities. Both have been erratic, responding to swings in the external value of sterling as well as to movements in security prices.

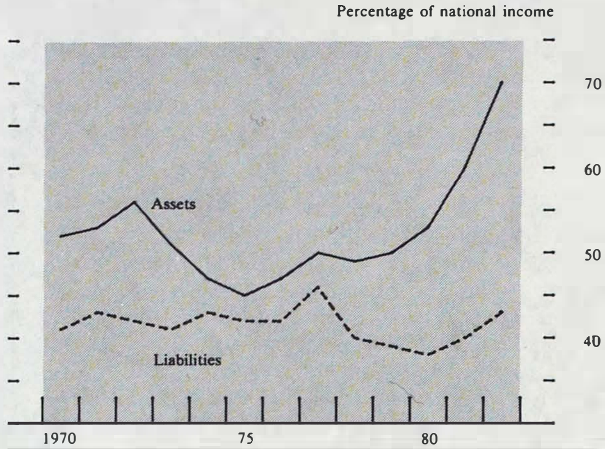
Chart 2
Total external assets and liabilities



Trends since 1970

National income—defined as GNP less capital consumption—provides a natural scaling factor for comparing stocks of assets and liabilities at different dates. External assets and liabilities each grew moderately, when divided by national income, between 1970 and 1980, but have since risen sharply (Chart 2). Most of the doubling since 1970 is attributable to the fast growth in the international foreign currency business of UK banks.[1] Since this is almost all entrepôt business, its gross size may have only minor implications for the UK economy—and the net external position of UK banks in foreign currency is very small in relation to gross assets.

Chart 3
Total external assets and liabilities excluding banks' external foreign currency business

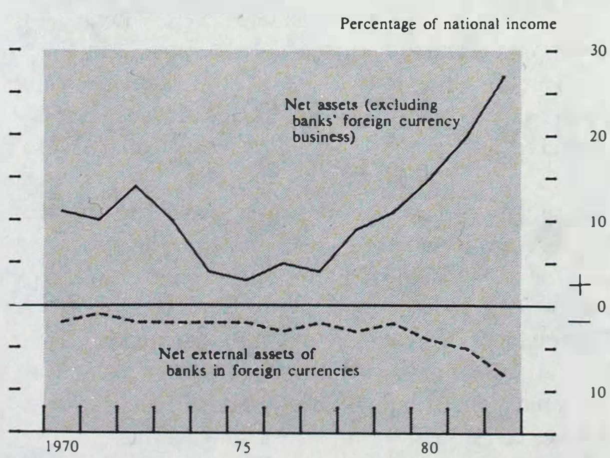


External assets and liabilities excluding such business have changed much less in relation to national income (Chart 3): what follows will chiefly consider these. Liabilities, deflated by national income, have been remarkably stable. By contrast, assets on the same basis fell steeply between 1972 and 1975, and have grown very rapidly in the last two years after a period of consolidation. These developments are mirrored in Chart 4, displaying *net* assets, excluding banks' foreign currency business.

The net liabilities of UK banks to foreigners in foreign currency (also shown in Chart 4) have been remarkably stable, when scaled by national income, until last year when banks again substantially increased their foreign investments. These investments are not directly included here, but any increase in net external deposit liabilities by which they were financed is included.

Net foreign assets are now the equivalent of 19% of annual national income, or 27% excluding banks' foreign currency business. While these are large figures, they are small compared with the replacement value of the estimated UK capital stock after capital consumption (430% of national

Chart 4
Net external assets



(1) This business was described in an article 'The international banking markets in 1982' in the March *Bulletin*, pages 43-60.

income in 1981); the current value of the capital stock employed in the North Sea alone amounted to the equivalent of 12% of national income at the end of 1982.

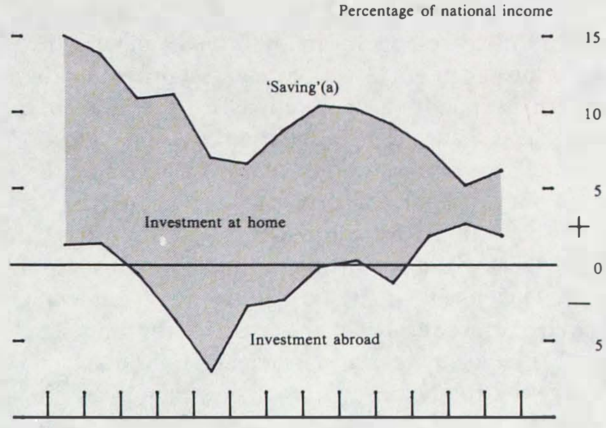
These stocks of assets are the outcome of developments in UK saving, and its allocation between capital formation at home and the acquisition of overseas assets (as well as a consequence of revaluations). Chart 5 illustrates this, defining investment at home as spending on fixed capital, net of capital consumption, plus additions to stocks. The sum of this and 'investment abroad' is fairly close to domestic saving after providing for depreciation and stock appreciation. On this basis, 'saving' fell from 15% of national income in 1971 to around 7% in 1975, with investment abroad taking most of the impact initially. Thereafter, disinvestment abroad slowed, as the trade balance recovered. From 1978, however, 'saving' has fallen again, and an increasing proportion has taken the form of investment abroad. In the three most recent years, fixed investment was low, and stocks were being heavily run down: this helped produce a large visible surplus, both directly and through the associated recession, with the necessary counterpart of a substantial net acquisition of foreign assets.

These developments, mirrored in the sharp fall and later recovery of net external assets as a proportion of national income, can be interpreted as the reaction of the United Kingdom to the very sharp international oil price rises of 1972–73. At that time, very large reserves of oil had been discovered in the North Sea, with investment to exploit these reserves already under way. In the following years, the stock of net external assets was run down (Chart 6)—both in the public sector[1] (particularly by borrowing under the exchange cover scheme) and in the private sector—partly to finance the build-up of the capital stock employed in the North Sea and partly to protect living standards from the full brunt of worsened terms of trade. Much of the run-down in net private external assets took the form of capital imports to finance North Sea development. In the most recent period, the North Sea capital stock has stabilised in relation to national income, and net exports of oil have reached high levels—more than sufficient to account for all the visible surplus of the last three years. This exportable surplus of oil is best seen as a temporary phenomenon, although one that will last for a number of years yet: North Sea oil is a wasting asset. It is appropriate that much of the value of production—made possible only by large investment—should be transformed into other assets.[2]

Seen in this light, acquisitions of net foreign assets in recent years—the counterpart of visible surpluses—have been an element in the transformation of the North Sea asset into other forms of capital. (The scale of such flows, even in recent years, has been less than might have been judged appropriate on these grounds, if investment abroad were the only compensation for the usage of North Sea wealth.) The repayment of large amounts of official foreign currency debt represented part of this adjustment, and has been supplemented more recently by private sector acquisitions of foreign assets. It should be remembered, however, that a large part of the very sharp improvement in net foreign assets in the last two years has been as a consequence of valuation effects (Chart 1)—visible surpluses have been of less importance than the overall change might suggest.

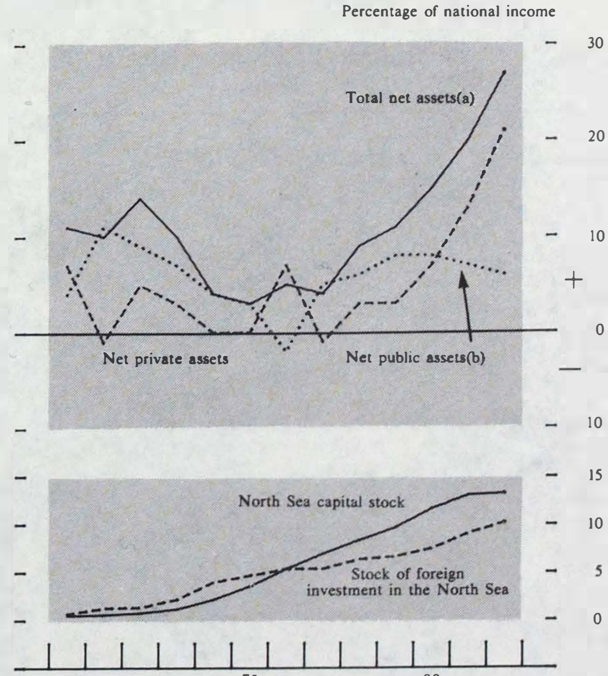
The abolition of exchange controls will have encouraged the acquisition of foreign assets. And it will have led to an

Chart 5
Saving and investment at home and abroad



(a) This measure is the sum of investment at home and abroad and is not the same as saving in the national accounts, although the two measures display similar trends.

Chart 6
The effect of North Sea oil



(a) Excluding net external foreign currency assets.
(b) Excluding official financing liabilities.

(1) The definition here subtracts official financing liabilities from public sector external assets.
(2) The article 'North Sea oil and gas—costs and benefits' in the March 1982 *Bulletin*, pages 56–73, examines these considerations further.

expansion of the scale of financial intermediation between UK residents and foreigners, since, for a given current surplus, any extra gross outflow of capital has to be matched by a corresponding inflow brought about by induced movements of interest rates, asset prices and the exchange rate relative to expectations. Furthermore, to the extent that exchange control abolition contributed to a lower exchange rate than would otherwise have been the case, an improved current surplus will have eased the greater acquisition of foreign assets. Accordingly, it is hard to argue that exchange control abolition is responsible for currently low rates of domestic investment; investment may well be more affected by the prospects for future profitability than by shortage of finance. In so far as exchange controls helped to strengthen sterling, abolition will have improved profitability, and thus may have been a factor encouraging domestic capital formation. The effects of exchange control abolition are better discussed in the context of developments in the size of gross assets and liabilities.

Gross assets and liabilities

The sizable surpluses on current account have matched part at least of the demand for foreign assets, also increased by exchange control abolition. Portfolio holdings abroad have grown very fast since 1979 (Chart 7), with financial institutions shifting to a higher proportion of overseas assets in their portfolios, though a fair amount of the growth has arisen through revaluations. Direct investment holdings have also increased, though less sharply—exchange control tended to restrict these flows much less than it did portfolio investment. Sterling lending abroad has increased sharply, with a revival of the sterling bill market following the changes in monetary control techniques introduced in mid-1981 and the earlier relaxation of restrictions (as part of the general lifting of exchange controls in 1979)

Chart 7
Composition of UK external assets

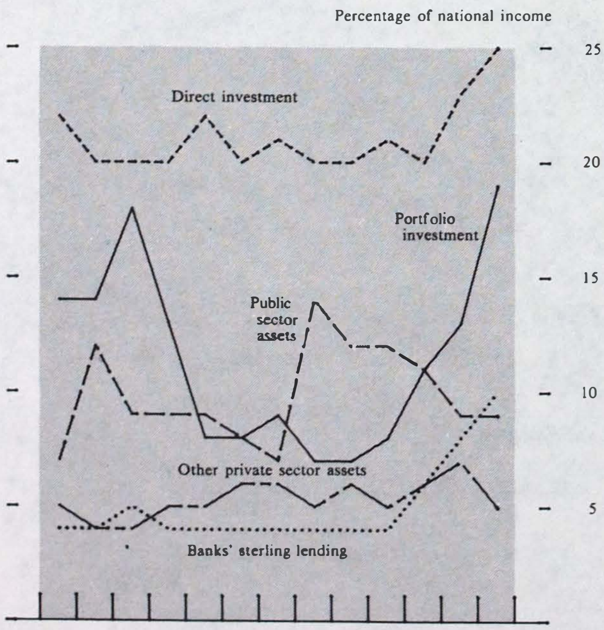
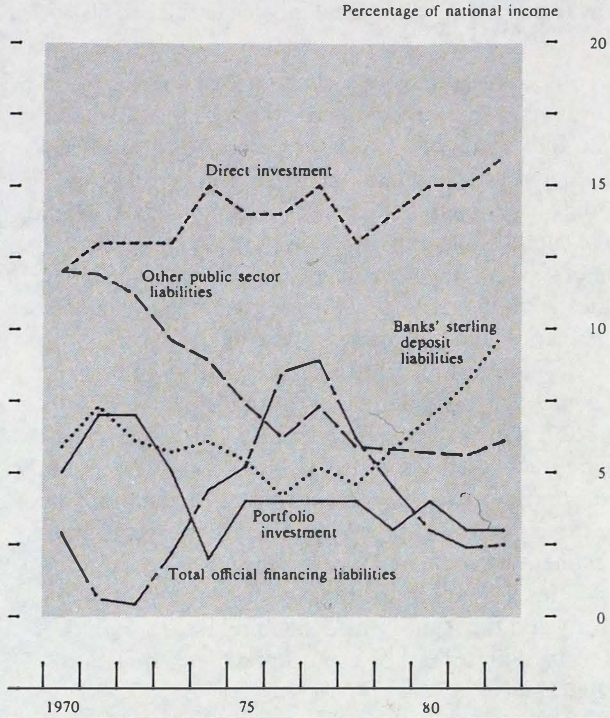


Chart 8
Composition of UK external liabilities



on the use of sterling to finance trade between foreign countries.

Total liabilities have changed little since 1970 in relation to national income, but the composition of liabilities has changed quite substantially (Chart 8). Private non-residents' sterling balances with UK banks—particularly those of foreign banks—have grown very fast in recent years after a period of decline. This is doubtless partly due to the increased integration of the London and overseas sterling banking markets following the abolition of exchange and other direct controls (reflected also in increased sterling lending to abroad), and it may also owe something to the recent coincidence of high interest rates and low industrial profitability. (Official balances have grown little, by contrast.) Mirroring that, portfolio balances shrank to low levels in 1973–74, largely because of the poor performance of UK equity prices, and have remained low since.

The recent expansion in the private sector's external balance sheet has been accompanied by a reduction in official assets and liabilities relative to income. The mid-seventies saw heavy official borrowing to finance the defence of sterling against downward pressure. This was followed by a large rise in the reserves in 1977 as attempts were made to stem the pace of sterling's recovery. Since then, intervention has been generally modest, and much official debt has been repaid ahead of schedule. Revaluations—particularly of the gold element in the reserves—have produced modest growth in official gross assets in nominal sterling terms. Official financing liabilities have fallen in nominal terms since 1977, and fallen faster than assets in relation to national income.

The main changes in 1982

During 1982 the sterling value of external assets rose by 25% to nearly £400 billion while liabilities rose at nearly the same rate, to just over £360 billion. Net assets rose by £9 billion. Valuation changes, notably those resulting from exchange rate movements, played a major part in these rises. The single most important increase, of £12½ billion, was in net portfolio investment abroad, some £6½ billion arising from valuation changes. Private direct investment added nearly £3½ billion to net assets. But banking and other commercial liabilities increased by a net £5¾ billion.

Private sector

Gross UK *portfolio investment* overseas continued to rise. Buoyant security prices (particularly in the United States) and the depreciation of sterling added £7.4 billion to the value of this investment, and new net purchases were also substantial at £5.9 billion. Approximately £4 billion of this flow was generated by financial institutions outside the monetary sector (insurance companies, pension funds etc), with banks' purchases for their own account—perhaps affected to an important extent by conditions[(1)] in the market for international bonds—responsible for much of the rest. Overseas investment in UK company securities rose modestly (£0.9 billion), a all of which was a valuation increase.

The book value (after revaluations) of *direct investment* overseas rose by £6.8 billion to stand at £49.3 billion (Table B). Non-oil companies' net new investment overseas was £3.1 billion, and £1.8 billion was added by the depreciation of sterling. Investment abroad by oil companies remained low. Overseas direct investment in the United Kingdom rose by £3.4 billion, at book value, to stand at £30.8 billion. Net new inward investment by non-oil companies (£1.3 billion) remained modest. Overseas oil companies' investment in the United Kingdom rose by £2.2 billion (to £11.8 billion), £1.9 billion of which represented a net new inflow, mainly investment in the UK continental shelf.

Net *banking and other commercial liabilities* grew by £5.7 billion (to stand at £12.8 billion). Sterling lending by banks to overseas residents continued to grow rapidly (by 31%), and was more than matched by growth in sterling deposits from abroad. In 1982, loans to non-banks in European and Commonwealth countries were dominant, whereas in 1981 new lending was mainly to banks overseas. Sterling acceptance credits accounted for most of the

Table B
Direct investment
£ millions

End-years	1979	1980	1981	1982
Outward				
All industries other than oil, banking and insurance	20,000	21,600	28,000	32,500
Banks	1,910	2,310	3,060	3,295
Oil companies	6,500	7,550	9,100	10,700
Insurance companies (investment in the United States only)	800	890	1,235	1,480
Property	900	940	1,120	1,350
Total	**30,110**	**33,290**	**42,515**	**49,325**
Inward				
UK companies other than oil, banking and insurance	12,800	15,100	15,600	16,500
Banks	1,055	1,215	1,415	1,665
Oil companies	6,750	8,150	9,650	11,800
Insurance	330	480	710	825
Total	**20,935**	**24,945**	**27,375**	**30,790**

growth in commercial bills discounted, continuing the growth in bill lending of recent years. The net external foreign currency liabilities of UK banks (excluding the effects of exchange rate movements) rose by £4.2 billion in 1982, the counterparts to this being net foreign currency lending to UK residents, and some switching by banks into sterling assets, but mainly substantial acquisitions by banks of other foreign currency assets, in particular, investments overseas.

The UK non-bank private sector deposited a further £1.1 billion abroad during the year; after allowing for valuation changes the value of deposits rose to £6.6 billion. These deposits remain small in relation to the domestic money stock.

Public sector

The net external liabilities of the public sector (excluding the reserves and official financing items) rose by £1.5 billion, more than accounted for by a £1.7 billion increase in overseas holdings of gilts; capital gains arising from the substantial fall in UK interest rates were mainly responsible.

Official financing liabilities rose by £0.6 billion during the year, mainly reflecting the fall in the sterling exchange rate. The United Kingdom continued to repurchase sterling swapped for foreign currency with the IMF under the oil facility, which was finally settled, after some earlier rescheduling, in January 1983.

Official reserves, valued at end-year market rates, rose by £1 billion. There were net drawings of £1.4 billion over the year but the fall in the exchange rate and the rise in the price of gold added £2.4 billion.

(1) See 'International financial developments' on page 184 and earlier *Bulletins*.

Table C
UK external assets and liabilities

£ millions

End-years	1979	1980	1981	1982
External assets				
Private sector				
Private investment abroad:				
Direct	30,110	33,290	42,515	49,325
Portfolio	12,000	18,100	24,400	37,700
Total private investment abroad	42,110	51,390	66,915	87,025
UK banks' assets				
Balances, advances and overdrafts in:				
Sterling	1,449	3,821	5,863	8,061
Foreign currencies	120,438	137,742	210,534	262,565
Commercial bills discounted	4,683	6,153	8,778	11,621
Deposits held abroad (other than by banks)	2,638	4,069	4,989	6,646
Suppliers' trade credit on exports	4,652	4,688	5,607	5,768
Advance and progress payments on imports by UK businesses	342	400	339	391
Total banking and other commercial claims	134,202	156,873	236,110	295,052
Total external assets of the private sector	**176,312**	**208,263**	**303,025**	**382,077**
Public sector				
Inter-government loans by the United Kingdom	1,281	1,230	1,221	1,192
Subscriptions to international financial organisations (excluding the IMF)	1,491	1,544	1,765	2,009
Other official assets	364	397	447	484
Refinanced export credit	1,741	1,243	852	814
Total public sector lending etc	4,877	4,414	4,285	4,499
Official reserves	13,170	13,275	11,960	12,939
Total external assets of the public sector	**18,047**	**17,689**	**16,245**	**17,438**
Total identified external assets	**194,359**	**225,952**	**319,270**	**399,515**
External liabilities				
Private sector				
Overseas investment in the UK private sector:				
Direct	20,935	24,945	27,375	30,790
Portfolio	4,530	5,100	5,800	6,700
Total overseas investment in the private sector	25,465	30,045	33,175	37,490
UK banks' deposit liabilities in:				
Sterling	8,520	11,564	14,601	19,087
Foreign currencies(a)	124,793	143,777	219,152	278,191
Suppliers' trade credit on imports	2,491	2,176	2,283	2,220
Advance and progress payments on exports by overseas customers	2,177	2,496	2,861	2,866
Direct borrowing abroad by UK non-bank private sector	3,164	3,345	4,268	5,451
Overseas deposits with building societies	38	25	25	32
Total banking and other commercial liabilities	141,183	163,383	243,190	307,847
Total external liabilities of the private sector	**166,648**	**193,428**	**276,365**	**345,337**
Public sector				
Inter-government loans to the United Kingdom	1,547	1,376	1,649	1,847
Overseas investment in the UK public sector:				
British government stocks held by:				
Central monetary institutions and international organisations	1,290	2,248	2,461	2,892
Others	2,900	3,471	3,478	4,710
British government foreign currency bonds	375	335	402	327
Local authority securities and mortgages	175	200	230	220
Foreign currency securities issued by public corporations(b)	187	158	164	161
Other borrowing abroad by:				
Public corporations(b)	793	582	645	477
Local authorities(b)	29	37	43	41
Overseas holdings of Treasury bills and non-interest-bearing notes	1,218	1,044	999	1,133
Overseas deposits with local authorities	17	22	42	26
Total public sector borrowing (other than official financing)	8,531	9,473	10,113	11,834
Official financing liabilities:				
Net drawings on the IMF	481	301	191	35
Foreign currency borrowing by the Government	1,798	1,045	—	—
New York bond issue by the Government	157	146	183	216
Foreign currency borrowing by public bodies under the exchange cover scheme	4,090	3,460	3,889	4,621
Total official financing liabilities	6,526	4,952	4,263	4,872
Total external liabilities of the public sector	**15,057**	**14,425**	**14,376**	**16,706**
Total identified external liabilities	**181,705**	**207,853**	**290,741**	**362,043**

(a) Excludes borrowing by banks on behalf of the Government, and of other public bodies under the Treasury's exchange cover scheme, which is included under official financing liabilities.

(b) Excludes borrowing under the Treasury's exchange cover scheme.

Notes and definitions

Assets and liabilities denominated in foreign currencies are valued at the exchange rates ruling at the end of each year; all securities other than those included as direct investment are valued at closing market prices at the end of each year or at estimates of such prices. Some items, because of their relative unreliability, are more heavily rounded than others.

Assets

Private sector

Direct investment
All industries other than oil, banking and insurance represents investment by UK companies in their overseas branches, subsidiaries and associates. Direct investment by a number of public corporations is included. The figures are extrapolated from Department of Trade surveys covering total net asset values attributable to investing companies, ie book values of fixed assets *less* accumulated depreciations, *plus* current assets, *less* current liabilities. Book values of assets acquired some years ago may differ considerably from current market or replacement values and, in individual cases, may be quite unrealistic, but only book values are readily available. Estimates for 1979–82 are derived from the 1978 survey and investment flows each year, with adjustments being made for changes in the sterling exchange rate; however, the effect of the depreciation or appreciation of sterling against other currencies on the value of overseas assets in UK companies' books cannot be evaluated precisely because companies have in the past adopted differing methods of valuation.

UK banks' direct investment overseas represents investment in overseas branches, subsidiaries and associates. The figures are based on a census of overseas assets and liabilities completed by listed banks as at the end of 1977, together with subsequent flows of direct investment reported annually by banks; for 1982 the reporting population for flows is based on the new monetary sector introduced at the end of 1981. Investment is defined as the sum of equity, loan and working capital, *plus* reserves.

Investment abroad by oil companies is measured on a basis broadly comparable with the other direct investment estimates, except that unrelated trade credit is included. Outstanding foreign currency issues abroad are netted off for 1979; they are subsequently included within portfolio investment in UK company securities. The estimates include the Shell Transport and Trading Company's 40% share of the net assets of the Royal Dutch/Shell Group outside the United Kingdom. The treatment of fixed assets varies, but an attempt has been made to allow for changes in the value of sterling. The figures for 1981 and 1982 are not entirely consistent with earlier figures owing to a change in the accounting conventions of certain oil companies.

Insurance companies' direct investment in the United States is derived from US Department of Commerce estimates, the 1982 figure being an extrapolation by the Bank of England.

Property
These estimates relate to personal sector and pension fund investment made directly in property abroad and should be interpreted as no more than a broad indication of magnitude.

Portfolio investment
Estimates of UK portfolio investment have been rebased from end-1979 using information from financial institutions as far as possible; transactions data for other investors (including industrial and commercial companies and persons) are taken from a portfolio investment enquiry conducted by the Bank of England each quarter since July 1980 (and temporary reporting arrangements prior to that) and revaluation factors deduced from movements in financial institutions' holdings are applied to estimates of holdings by those investors. The estimates for earlier years which underlie the charts in the article have been revised upwards, in order to avoid discontinuity in the series, partly using information from financial institutions, with some allowance to remove the effect on their figures of the investment currency premium.

UK banks' assets
There is a break in this series at end-1981 reflecting the introduction of the new monetary sector, but the coverage is wider than the monetary sector (see additional notes to Table 14.1 in the March *Bulletin*). Details of the size of the break have been recorded in the statistical annex. Sterling—but not foreign currency—acceptances are included within *commercial bills discounted,* because most are owned by UK banks and discount houses. Export credit refinanced with ECGD and the Issue Department of the Bank of England is deducted from *UK banks' assets* and included in public sector claims; in the June 1982 article it was left in *UK banks' assets.* Bills drawn on overseas residents lodged with banks for collection are covered by *suppliers' trade credit on exports.* Direct investment by banks is included within *direct investment.*

Deposits by UK non-banks with banks overseas
These estimates are derived from the banking statistics of countries in the BIS reporting area (as defined in footnote (a) to Table 13.1 in the statistical annex, except that there is no coverage of deposits at the foreign branches of US banks); they also include US dollar commercial paper and bankers' acceptances and, from end-1980, short-term US Treasury debt. Currency exchanges (which were treated in the June 1982 article as a *miscellaneous* entry under *private investment abroad*) are also included. Until the ending of exchange controls these were used as a method of financing investment abroad and, being of a long-term nature, existing investment of this type will remain outstanding for some years, even though the free availability of foreign currency to UK residents has meant that new use of this method of finance has ceased. The corresponding liabilities are included in direct borrowing from abroad by UK companies. Because of expansion in coverage, there are breaks in the series of +£215 million in 1979 and +£695 million in 1980.

Suppliers' trade credit on exports
This comprises trade credit extended by UK traders, other than oil companies, to overseas concerns other than affiliates or parent companies. Trade credit extended to parent companies and affiliates overseas is included under *direct investment.*

Public sector

Other official assets
These comprise other overseas assets of the central government, including the assets of such official bodies as the Commonwealth Development Corporation and the UK Atomic Energy Authority. The figure for *property* which was shown as a separate estimate in the June 1982 *Bulletin* has been discontinued, owing to suspected overlap with *other official assets.*

Refinanced export credit
That part of export credit which is refinanced with the ECGD and the Issue Department of the Bank of England is deducted from UK banks' assets and included in public sector claims.

Official reserves
For the purposes of this article, gold, foreign currencies and SDRs are valued at end-year market rates. These valuations differ from those used in the figures released each month by the Treasury (see the additional notes to Table 17 in the statistical annex in the March *Bulletin*) but are consistent with those used for other assets denominated in foreign currencies which are included in the inventory. For end-1982 the market valuation used here exceeded the valuation in the monthly press release by £2.4 billion.

Liabilities

Private sector

Direct investment
All industries other than oil, banking and insurance represents investment in branches, subsidiaries and associates in the United Kingdom by companies incorporated abroad. These estimates are based on the 1978 survey by the Department of Trade and are comparable to those for outward direct investment.

Foreign banks' direct investment in the United Kingdom represents investment in those UK banks which are branches, subsidiaries or affiliates of overseas companies. The figures are calculated on a basis comparable to that for *UK banks' direct investment overseas.*

Investment by overseas oil companies in the United Kingdom. These estimates include the Royal Dutch Petroleum Company's 60% share of the net assets of the Royal Dutch/Shell Group in the United Kingdom.

Investment in UK insurance companies. This series has been created by aggregating annual flows onto a notional base level of £50 million at 1968. The resulting levels have been grossed up using the Financial Times financial shares index to allow for capital revaluation.

Portfolio investment in UK company securities
The market value of inward portfolio investment in listed ordinary shares at end-1975 is available from the Department of Industry's survey of UK company share registers at that time. Adjustments have been made to exclude holdings of a direct investment nature, and an estimate of holdings of debentures and preference shares has been added. The result has been used as a benchmark for subsequent years, the estimates for which are calculated by applying changes in market values and reported transactions. Up to July 1980, details of issues and redemptions of foreign currency securities, other than those issued by oil companies, were obtained from various sources, including the press: nominal amounts outstanding for each issue were estimated and adjusted for changes in the market price of the security. The new portfolio investment enquiry introduced with effect from July 1980, which covers inward investment also, does not distinguish between sterling and foreign currency securities issued by UK companies. Since the new enquiry thus embraces transactions in foreign currency securities issued by oil companies, outstanding issues abroad by these companies are included here from end-1980; for previous years, they are netted off from the oil companies' assets abroad.

UK banks' deposit liabilities
There is a break in this series at end-1981 reflecting the introduction of the monetary sector (see *UK banks' assets*). Details of the size of the break are recorded in the statistical annex. The figures exclude borrowing by UK banks to finance the government's \$2.5 billion and \$1.5 billion loans and loans to other public sector bodies under the Treasury's exchange cover scheme; such borrowing is included in *official financing liabilities.* Commercial bills for imports drawn on UK residents and lodged with UK banks by non-residents are included in *suppliers' trade credit on imports.*

Direct borrowing abroad by the UK non-bank private sector
This item was treated in the June 1982 article as *overseas investment in the private sector.* Estimates are derived from the banking statistics of countries in the BIS reporting area (as defined in footnote (a) to Table 13.1 in the statistical annex), except that there is no coverage of borrowing from the foreign branches of US banks. The figures are adjusted to avoid overlap with other items particularly borrowing by the UK public sector, and trade credit relating to shipbuilding; in respect of shipbuilding credit they differ from the 1982 article. They include some borrowing via issues of US commercial paper. Currency exchanges also are now added (see note on *deposits by UK non-banks with banks overseas*). There is a break of £110 million in the series in 1980 because of an expansion of coverage.

Suppliers' trade credit on imports
This comprises trade credit received on imports from non-residents, other than affiliates or parents. Trade credit received from affiliates or parents overseas is included under direct investment.

Public sector

British government stocks
These comprise British government stocks and nationalised industry stocks guaranteed by the Government. Figures for the holdings of central monetary institutions and international organisations are based on mid-November data, adjusted for changes in market prices and transactions between then and end-December. Figures for other holdings are estimated partly by the same method (where the holdings are through UK listed banks) and partly from the stock registers at the Bank of England.

British government foreign currency bonds
These represent the bonds, denominated in US dollars, deutschemarks, Swiss francs and yen, which were sold to overseas official holders of sterling in April 1977 in order to help promote an orderly reduction in the international reserve role of sterling.

Local authority securities and mortgages
The estimates relate mainly to amounts held directly by non-residents or lodged with the Crown Agents and banks in the United Kingdom.

Foreign currency securities issued by public corporations and local authorities
These represent outstanding issues which are not covered by the Treasury's exchange cover scheme. Each issue has been valued at the end-year market price and then converted into sterling at end-year middle-market rates. Identified holdings of public sector foreign currency bonds by UK residents have been excluded.

Other borrowing abroad from banks etc by public corporations and local authorities
These figures comprise borrowings, net of repayments, that are not covered by the Treasury's exchange cover scheme, expressed in sterling at end-year exchange rates. Foreign currency borrowing from UK banks is excluded.

Net drawings on the IMF
This comprises net drawings on the IMF, less other countries' net purchases of sterling, except where such transactions affect the UK reserve position in the IMF. Sterling liabilities to the IMF resulting from the UK sterling subscription are excluded, as is the sterling subscription from the assets side.

Foreign currency borrowing by the Government
This represents net drawings under both the \$2.5 billion facility announced in 1974 and the \$1.5 billion facility originally taken up in 1977. Borrowings from UK and overseas banks are included.

Foreign currency borrowing by public sector bodies under the exchange cover scheme
This includes foreign currency borrowed through UK banks, the issue of foreign currency securities, and other borrowings abroad by public corporations and local authorities. Each issue has been valued at the end-year market price. Identified holdings of public sector foreign currency bonds by UK residents have been excluded. (These estimates differ slightly from other published figures, where issues are included at nominal prices, and where currencies other than the US dollar are converted into US dollars at parity or central rates, and the resulting total is then converted into sterling at the middle-market exchange rate ruling at the end of the period.)