Savings & Flow of Funds: Enhancing and Improving Flow of Funds Accounts
April 2012

Background & Key Lessons

Building off of earlier work and a May 2010 workshop, CFSP hosted, “Savings and Flow of Funds: Enhancing and Improving Flow of Funds Accounts,” a workshop held in Cambridge, MA in April 2012. CFSP Faculty Director Robert M. Townsend and Narapong Srivisal, a PhD student at the University of Chicago, hosted more than 30 researchers and high-level policy makers from a number of international organizations.

Flow of funds accounts represent a set of integrated financial accounts that measure the uses and sources of funds by sector within an economy. The goal of this workshop was to identify opportunities and best practices for improving flow of funds accounts, particularly in developing countries. With better flow of funds data, researchers and policy makers can more accurately measure a broader set of economic analyses focused on savings, investment, and intermediation.

“We are interested in a larger picture [of financial access] which looks at the consequences of integrating disconnected sectors with the formal sector … for both the newly-arrived participants and for the economy as a whole,” explained Townsend in his opening remarks. “I can’t imagine how to do that without having good flow of funds data.”

The workshop helped to generate important discussion on how to improve flow of funds accounts and shared plausible applications when using the data in the context of developing countries. It began with two country-focused presentations which highlighted the Consortium’s recent work.

- In Mexico, the National Commission of Banking and Securities in Mexico (CNBV) has worked to complete a publicly available database of savings and credit indicators at the municipality-level in order to understand regional trends and historical patterns in Mexico’s financial system. For example, CNBV can identify areas of net borrowing versus net saving and track the portions of lending and saving facilitated by non-regulated, non-bank financial institutions, which are tracked through both questionnaires and in-person interviews. Interestingly, the data show that while commercial banks are lending more, non-bank financial institutions are actually receiving more savings in many regions.

- Collaborative work with Thailand’s National Economic and Social Development Board (NESDB) and the University of the Thai Chamber of Commerce (UTCC) seeks to expand data inputs and reorganize existing data in order to make the country’s flow of funds data more informative. Specifically, the acquisition of more financial data for non-financial corporations is planned, and better estimates of flows between each pair of sectors will be made.
Following these country-level examples, presentations focused on the following applications of flow of funds data:

- A comprehensive flow of funds model for India is one of the first of its kind to be developed. The model estimates the demand function for each sector's financial assets, which is then used to estimate and compare India's equilibrium prices and interest rates under various financial regulation regimes. Discussion focused on how to add dynamics in the model to reflect changing asset demand functions and equilibrium conditions, particularly in developing economies which may not have reached a steady state.

- Another application looks critically at the design of models of financial frictions and how to select appropriate parameters using micro-level evidence from observations of financial markets. To better inform models, financial statements of non-financial firms are necessary, particularly for privately held firms which may not currently share such data. In addition, there was discussion regarding the interpretation of firms' financial constraints; most models simply look at total available flow of funds and observed investment of the firms. Detailed flow of funds data that allow researchers to investigate how different types of firms use different instruments to finance their investment differently could be helpful.

- Flow of funds data from the U.S. is used to look at the effects of a credit crisis on consumption and savings decisions. Research finds that households typically want to reduce debt and increase (precautionary) saving by decreasing consumption and working more following a crisis, especially in the short run. Flow of funds data were helpful in calibrating parameters related to households’ debt and bond holding. However, discussion identified how more detailed flow of funds data could help in improving models of crisis by augmenting active intermediaries and adding a greater variety of assets to better capture more complex financial systems in the real world.

- Other work looked at puzzling trends in U.S. household wealth and changes in asset holdings in the 1970's. It constructs a model to explain how expected inflation, developments in credit markets, and changing demographics contributed to changes in asset prices and holdings during volatile time periods. Flow of funds data were used to identify household sector net asset demands, and these data were supplemented with a micro-level survey of consumer finances to identify saving and investment behaviors.

To conclude the workshop, a panel discussion brought together a diverse group of practitioners to discuss the actual compilation of flow of funds data, policy implementation, and academic research.

- One panelist discussed the financial instruments and data sources used in constructing flow of funds accounts and identified how the net acquisition of financial assets and net incurrence of liabilities is calculated. He concluded by describing Thailand's plan to improve flow of funds accounts.

- Another panelist described the overall lack of modeling of financial intermediation in academic research, but identified several interesting questions for future work using flow of funds data: what is the contribution of financial intermediation to economic development; and what are the consequences of financial crises?
• The use of flow of funds data in policy was discussed by one panelist. Policymakers, he explained, want solid empirical and theoretical evidence. In Africa, policymakers are keen to measure and evaluate the effectiveness of development aid, especially at the household level, and track remittances. At a macroeconomic level, flow of funds accounts are integral in understanding economic transformation and smaller pieces such as asset pricing, capital flight, and financial sector regulation.

Future Research Areas from the Workshop

The workshop helped identify a number of opportunities for CFSP to make an impact in the field and supported current research priorities:

CFSP Opportunities:

• Continuing to support improvements in flow of funds accounts is important for both researchers and policymakers seeking to understand economic growth. Additionally, CFSP should play a role in sharing successful projects. For example, CFSP is partnering with CNBV to disseminate a database on savings and credit indicators at the regional level, which fills in gaps in Mexico’s flow of funds data.

• Research using flow of funds continues to explore important issues of economic development such as monetary policy, investment, capital flight, and parallel markets and microfinance.

Action Items

• A proposal will be drafted for Thailand’s NESDB with detailed suggestions on how to improve Thailand’s flow of funds accounts. CFSP will work with the NESDB to sign a Memorandum of Understanding to support improvements in the country’s flow of funds accounts.

• Following this work, a summary note on what has been learned from existing flow of funds accounts will be written, with a particular emphasis on how including the financial statements of the various sectors can be useful for analysis.