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The Contribution of Financial Corporations to Aggregate Corporate Income

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.	not available for any reference period
..	not available for a specific reference period
...	not applicable
0	true zero or a value rounded to zero
0^s	value rounded to 0 (zero) where there is a meaningful distinction between true zero and the value that was rounded
^{p}	preliminary
^{r}	revised
x	suppressed to meet the confidentiality requirements of the *Statistics Act*
^{E}	use with caution
F	too unreliable to be published
*	significantly different from reference category ($p < 0.05$)

The Contribution of Financial Corporations to Aggregate Corporate Income

By Guy Gellatly, Matthew Hoffarth, and Luke Rispoli

This article in the *Economic Insights* series presents new income data on financial corporations derived from the revised Canadian System of National Accounts (CSNA12). It is one of a series of *Economic Insights* articles designed to emphasize key aspects of the new national accounts data and their utility for analyses of the Canadian economy. Several of these articles highlight changes to the organization of the national accounts data or draw attention to improvements in measurement.

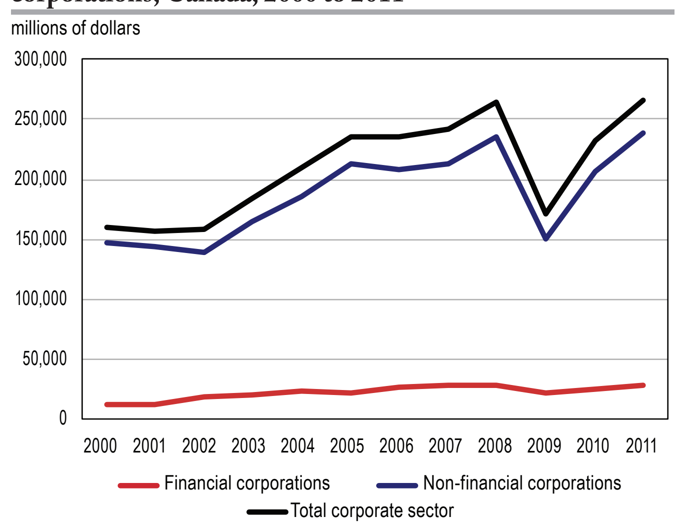
The global recession of 2008-09 focused attention on the role that financial corporations play in the movement of capital across different sectors of the global economy. As a result, this led to a demand for data that can be used to more fully assess the economic weight of financial corporations, and their relative contribution, via the provision of intermediation services and other financial services, to the production and distribution of goods and services in different sectors. One of the objectives of the revised Canadian System of National Accounts (CSNA12) is to provide data that better enumerate "the role and importance of the financial sector to the economy."[1] CSNA12 features a new, fully articulated sector account on financial corporations, which facilitates the statistical analyses of these firms.

This note utilizes data from the new sector account on financial corporations to highlight the contribution of these companies to different measures of corporate income. It examines the major income aggregates reported for corporations—net operating surplus, property income, primary corporate income, and disposable income. Each of these aggregates offers a different perspective on the role that financial corporations play in the production or distribution of aggregate income flows.

Financial corporations in CSNA12

The CSNA12 classifies a diverse set of companies that provide financial services as financial corporations, including banks, trust companies, credit unions, investment and financing companies, brokers and holding companies.[2] These companies provide productive services by channelling funds from depositors to borrowers to support the investment and consumption activities of business, governments, and households. They do so by delivering a myriad of services to clients, ranging from traditional financial services designed to facilitate safe storage and access to financial capital, to specialized planning and investment services aimed at facilitating wealth accumulation.

Chart 1
Net operating surplus, financial and non-financial corporations, Canada, 2000 to 2011



Source: Data are presented as annual estimates; quarterly data are available from Statistics Canada CANSIM table 380-0076.

1. For background, see Statistics Canada (2012).
2. The classification of the financial services sector in CSNA12 corresponds to North American Industry Classification System industries 52 and 55.

The CSNA12 explicitly depicts the income flows that financial corporations receive from, and pay out to, other sectors of the economy. These income flows are themselves diverse in that they encompass the receipts and payments of income that derive from a broad range of financial transactions—from the dividend payments that are received and paid out by investment firms that manage pension and mutual funds, to the interest receipts and payments that flow through chartered banks, to the premiums and benefits received and paid out by life insurance companies.

The CSNA12 divides the income of financial corporations into three basic categories: (1) the income that is associated with the value-added that these companies create via the provision of productive services; (2) the income that is associated with the reallocation of funds from the users of financial and physical assets to the owners of these assets; and (3) the income that is received and paid out in the form of transfers (primarly taxes) to and from other sectors.[3]

The first category of income described above is referred to in the corporate sector accounts as net operating surplus. From a national accounting perspective, net operating surplus contributes directly to gross domestic product (GDP)—and represents the margin that these companies receive as payment for the provision of intermediation services, along with the explicit fees associated with financial transactions.[4] The income that is associated with net operating surplus is a subset of the total income received by financial corporations. Financial companies also receive, and pay out, property income based on their use and ownership of physical and financial assets (category 2 above). Central to these are the interest and dividend incomes that flow into and out of financial corporations from other sectors of the economy.[5] Unlike net operating surplus, the property income flows are not part of GDP but are included in the primary income account. Finally, the CSNA12 also provides detailed information on the flows of transfer income that are received and paid by financial corporations (category 3 above), which are also excluded from GDP. What follows is an assessment of the extent to which these detailed income data yield different insights into the contribution that financial companies make to incomes in the corporate sector.

Contribution of financial services to value added

For financial corporations, the **net operating surplus** is the net revenue earned from financial intermediation services. As noted previously, it can be interpreted as the margin that financial companies receive from providing financial services to final consumers in other sectors of the economy—households, businesses and governments. These are the net revenues that contribute to the creation of value added in the financial sector. By comparison, the net operating surplus of non-financial corporations is a measure of the margins associated with their productive activity, measured as the difference between operating revenues and operating expenses.

Table 1 reports on the share of net operating surplus that is accounted for by financial corporations. This is a first measure of the relative size of the financial sector, based on the margins associated with financial intermediation and the explicit fees on financial transactions. Nominal dollar estimates of net operating surplus for financial and non-financial corporations are presented in Chart 1.

From 2000 to 2011, financial corporations accounted for, on average, about 10% of the net operating surplus generated by the corporate sector. This income share exhibited some year-to-year volatility, but no obvious trend. To put this into context, the net operating surplus generated by financial corporations represents between 1% and 2% of annual gross domestic product (GDP). By comparison, the net operating surplus generated by all corporations amounts to, on balance, about 15% of total GDP.

Financial corporations and the reallocation of property income

Data on operating surplus capture, on balance, only a small portion of the net income that financial corporations receive. The new sector account for these companies reports the gross and net income flows that they receive and pay out to households, businesses, and governments, based on the use and ownership of property (financial and physical assets). These property income flows are reported net of the margins associated with financial intermediation, which, as noted earlier, are allocated directly to net operating surplus. Accordingly, flows of property income are not included in estimates of GDP.

3. These income categories are described in reference to financial corporations. However, it should be noted that they apply equally to non-financial corporations. The CSNA12 reports the gross flows of property and transfer income for all institutional sectors.
4. Adding depreciation expenditures to net operating surplus yields an estimate of gross operating surplus. Gross operating surplus is part of GDP—for financial corporations, it is the contribution that capital inputs make to the creation of value added in the financial sector. Net operating surplus is a part of the current and capital account of corporations.
5. A portion of these interest flows—that which reflects that margins associated with financial services—is allocated to net operating surplus, while the remainder of interest income is classified as property income.

Table 1
Financial corporations, percent share of corporate total, selected income measures

	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011
						percent						
Net operating surplus	7.7	7.9	11.8	10.8	11.2	9.3	11.3	11.7	10.6	12.8	10.9	10.4
Property income - receipts	80.8	80.0	78.3	79.9	78.8	77.9	78.3	77.5	77.7	76.6	75.6	77.2
Interest	86.2	86.3	83.5	83.9	83.3	84.2	85.8	84.5	83.8	82.9	81.4	79.9
Dividends	69.3	68.3	70.5	74.1	73.3	71.2	69.1	66.7	68.5	70.0	70.0	74.7
Property income - payments	48.8	48.8	45.2	47.6	44.4	43.8	46.7	48.9	48.4	50.1	44.8	45.0
Interest	60.2	59.7	53.4	58.9	58.0	59.4	62.3	62.2	61.2	57.2	56.9	58.8
Dividends	37.7	40.5	39.9	42.1	38.4	37.4	39.3	40.6	43.5	48.6	40.3	40.1
Primary corporate income	22.5	21.3	30.2	21.6	26.0	24.7	27.2	24.4	21.8	28.2	30.5	28.6
Disposible income (net saving)	25.4	22.6	39.1	21.2	27.6	26.0	30.5	25.9	21.3	23.9	34.9	29.7

Source : Shares are based on annual data; quarterly data are available from Statistics Canada CANSIM table 380-0076.

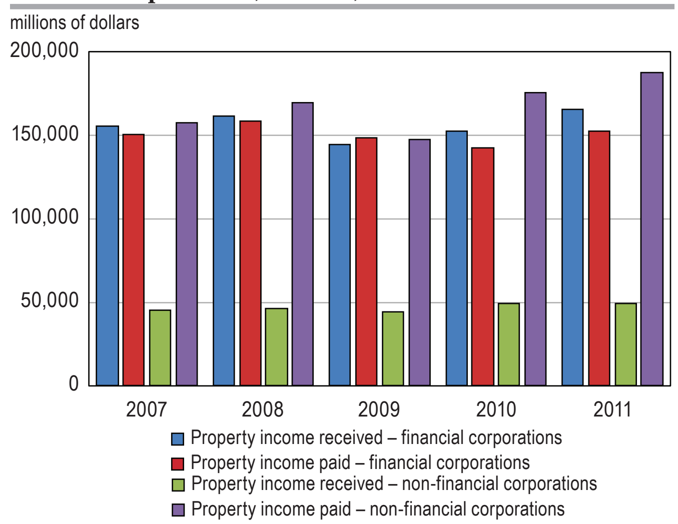
The magnitude of the gross receipts and gross payments of property income that flow through financial corporations underscores the specialized function that these companies play in reallocating funds across the economy. In 2011, the gross property income that financial corporations received from other sectors amounted to $165 billion, about six times the net revenues associated with explicit fees and financial intermediation ($28 billion). Financial corporations receive the main share of corporate interest and dividend receipts; from 2000 to 2011, financial companies took in, on average, 78% of the total annual value of these receipts (Table 1, Chart 2). During this period, their annual share of interest income fluctuated between 80% and 86% of corporate interest receipts, while their share of dividend income was between two-thirds and three-quarters of corporate dividend receipts.

On the other side of the ledger, the interest and dividend payments that financial companies make to businesses, households and governments represent a smaller share of the property income payments made by the corporate sector. Financial companies accounted for between 44% and 50% of these property income payments in each of the years studied—about 60% of interest payments, on average, and about 40% of dividend payments.

The revised CSNA subtracts property income payments from receipts to obtain a measure of **net property income**, which is reported separately for financial and non-financial corporations. The property income payments that financial companies make are comparable to their property income receipts, resulting in comparatively smaller net balances.[6] By contrast, the property income payments that non-financial corporations make to other sectors exceed their property income receipts by a sizable margin (Chart 2), leading to large negative property income balances.[7]

This underscores basic differences in the productive services provided by financial and non-financial corporations, as measured by the SNA. Financial corporations provide intermediation

Chart 2
Property income received and paid, financial and non-financial corporations, Canada, 2007 to 2011



Source: Data are presented as annual estimates; quarterly data are available from Statistics Canada CANSIM table 380-0076.

services that facilitate the flow of capital through to different sectors of the economy, while non-financial corporations use these capital flows to support their investment and production activities.

These data on net property income allow for the calculation of **primary corporate income**. Primary corporate income is the sum of net operating surplus and net property income. This broader income measure increases the relative income share of financial corporations. During the 2000s, the primary income generated by financial corporations represented between 20% and 30% of corporate primary income (Table 1, Chart 3).

6. It should be noted that, for financial corporations, the service component associated with intermediation has been removed from these property income receipts and balances.
7 Non-financial corporations have the capacity to raise their own capital directly via new issues of bonds and debentures, and through loans from affiliates.

This higher income share for financial corporations occurs because of the large negative balances of net property income that are apparent for non-financial corporations. These reflect the large payments that non-financial corporations make to finance their capital expenditures, along with the dividend and interest payments that these corporations make to households. Consequently, the share of primary corporate income accounted for by financial corporations (which adjusts for net property income) is much larger than their share of net operating surplus.

Income shares net of taxation and other transfers

The revised sector account also provides new estimates of corporate **disposable income**—the net-of-transfer incomes on which corporations can draw to finance their capital expenditures. These estimates adjust primary corporate income by subtracting out the transfers that corporations pay to other sectors, yielding a measure of corporate disposable income that is equivalent to net coraporate saving.[8] Taxes account for approximately 95% of these outward transfers.

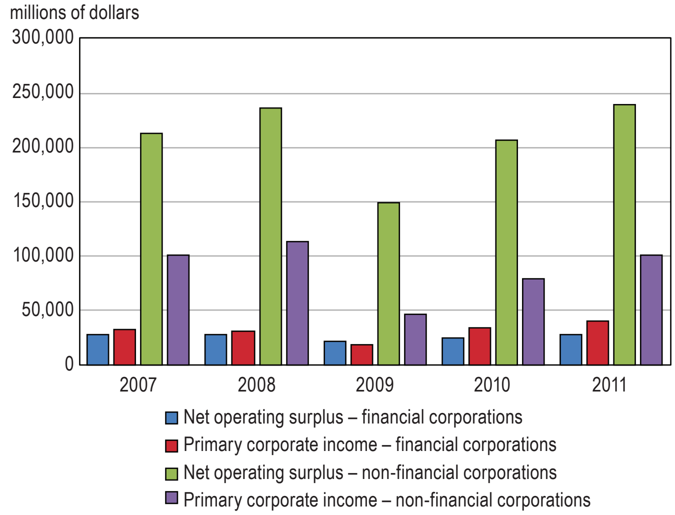
Recent data on all three income measures—net operating surplus, primary business income, and corporate disposable income—are reported in Chart 4.

During the 2000s, financial corporations typically generated between 20% and 40% of annual corporate disposable income—or equivalently, net corporate saving—with large year-to-year fluctuations. For the majority of years examined, these net-of-transfer income shares are qualitatively similar to those obtained when primary income is used (Table 1).

Conclusion

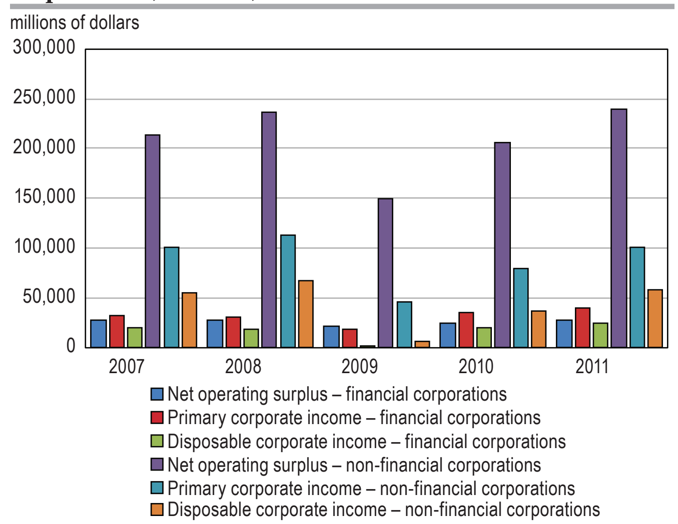
CSNA12 features a new sector account for financial corporations. It reports gross and net income flows for a sequential set of income measures that can be used to enumerate the relative importance of different income sources. When combined with data on non-financial corporations, these data offer new insights into the contribution that financial companies make to different corporate income flows. This analysis has provided a first assessment of these data.

Chart 3
Net operating surplus and primary corporate income, financial and non-financial corporations , Canada, 2007 to 2011



Source: Data are presented as annual estimates; quarterly data are available from Statistics Canada CANSIM table 380-0076.

Chart 4
Various income estimates, financial and non-financial corporations, Canada, 2007 to 2011



Source: Data are presented as annual estimates; quarterly data are available from Statistics Canada CANSIM table 380-0076.

8. That is, it is the corporate equivalent of the net saving rate reported for the household sector.

These data highlight the specialized function that financial corporations play in terms of reallocating incomes across the economy. About 80% of the gross receipts of property income that flow to corporations in the form of interest and dividend payments are received by financial companies. These companies also pay out slightly less than half of the total property income payments made by the corporate sector. The magnitude of these flows underscores the diverse composition of the financial sector as measured by CSNA12, as it encompasses different types of financial companies that together offer a broad mix of financial services—from investment firms that oversee pension and mutual fund portfolios, to insurance companies, to traditional lenders such as banks and credit unions.

The income data also demonstrate that the relative contribution that financial companies make to corporate incomes depends on the income metric used. The margins that financial companies earn from explicit fees and the provision of financial services represent about 10% of the net operating surplus earned in the corporate sector. These are income flows that contribute directly to GDP. The income share of financial companies is substantially higher when net flows of property income, which are not included in GDP, are used to construct a broader measure of primary corporate income. Financial companies account for about 20% to 30% of the primary income earned by corporations. Adjustments for net transfers, on balance, yield qualitatively similar shares to those obtained when primary income is used.

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Statistics Canada. 2012. "A New Presentation of the Quarterly National Accounts". Latest Developments in the Canadian Economic Accounts. Catalogue No. 13-605, May. Ottawa: Statistics Canada. http://www.statcan.gc.ca/pub/13-605-x/2012001/article/11671-eng.htm