Economic and financial indicators for multilateral surveillance

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Multilateral surveillance

The financial and economic crisis has demonstrated the significant degree of interdependence among major economies. The increasing number and size of multinational companies and of systemically important financial institutions that operate across countries and continents requires policy responses that are coordinated at a supranational and international level. To this end, the European Union (EU) is reforming economic governance, the Group of Twenty (G20) is carrying out a mutual assessment process and the European Systemic Risk Board (ESRB) and the Financial Stability Board (FSB) are addressing vulnerabilities in financial systems.

The reform of EU economic governance goes beyond strengthening budgetary surveillance, including the excessive deficit procedure (EDP). It aims at broadening the surveillance of EU Member States' economic policies. A mechanism will be established for the prevention and correction of excessive macroeconomic imbalances, based on two regulations which outline an excessive imbalance procedure (EIP) and introduce the possibility of imposing fines on Member States that are found to be in an "excessive imbalance position" and repeatedly fail to comply with recommendations.

The starting point of **the EIP** is an alert mechanism for the early detection of imbalances, which uses a scoreboard of economic and financial indicators. This will be supplemented by country-specific qualitative expert analysis. If an imbalance is considered to be excessive, the Member State concerned could be subject to an EIP and would be called upon to adopt an action plan to correct the situation within a specific time frame. Repeated non-compliance with recommendations could, in the case of euro area countries, eventually lead to sanctions.

The choice of indicators for the **EIP scoreboard** is based on three principles: (a) focusing on the most important aspects of macroeconomic imbalances and losses in competitiveness, which need to be corrected by structural, fiscal and financial polices with a particular focus on the smooth functioning of the euro area; (b) keeping the scoreboard simple and transparent, including by limiting the number of indicators used; and (c) ensuring the availability, timeliness and quality of the data. As a minimum, the scoreboard indicators and their threshold values will be based on the following statistics: (i) the current account balance, (ii) the net international investment position, (iii) export market shares, (iv) nominal unit labour costs, (v) real effective exchange rates, (vi) private sector debt, (vii) private sector credit flows, (viii) changes in house prices, (ix) general government debt, and (x) GDP.

In parallel, the **G20** committed in the **Seoul Action Plan** of November 2010 to coordinated policy action by all G20 members in order to achieve strong, sustainable and balanced growth, including by enhancing the mutual assessment process to promote external sustainability. The G20 also agreed on a set of indicators in February 2011 that will allow members to focus, through an integrated two-step process, on persistently large imbalances which require policy actions.

The **G20 Indicative Guidelines for Assessing Persistently Large Imbalances** are based on the following indicators: (i) public debt and fiscal deficits, the private savings rate and private debt; and (ii) the external imbalance composed of the trade balance and net investment income flows and transfers, while due account is taken of exchange rate, fiscal, monetary and other policies.

Requirements for economic and financial statistics

The **economic and financial indicators** for multilateral surveillance may comprise ratios or moving averages of the underlying economic and financial statistics and related forecasts. Some of the indicators may not be available in already existing statistics, but are specifically designed for surveillance purposes. In all cases, the indicators are intended to signal where and when the economic stance of countries or economic areas, such as the euro area, tends to imbalances that should be prevented or corrected through the implementation of policy measures either by specific countries or following a multilateral agreement among the economies concerned. The policy implications of identified imbalances must be weight against the inherent imprecision of macroeconomic statistics. In order to minimise tensions in the macroeconomic surveillance process that arise owing to the uncertainty surrounding the underlying statistics, the choice of the economic and financial indicators should take account of a number of statistical considerations.

Relevance. The indicators should indeed address the imbalances to be prevented or corrected. For example, the government deficit and government borrowing requirement are different indicators. While this may seem obvious, macroeconomic statistics measure phenomena in economies that are typically not reflected in economic models. One example is the fact that households not only consume, they also contribute considerably to gross value added in a market economy. To give another example, the significance of household indebtedness depends on the value of household assets and the distribution of the indebtedness across households.

Harmonisation. All countries should compile a given indicator using the same statistical concepts and implementing similar methodologies. While progress has been achieved in agreeing on international statistical standards, progress on their implementation is very uneven across the world, including across developed economies. Indeed, harmonised indicators only prevent distortions occurring as a result of the way they are measured. For example, the public sector of a developed market economy is hardly comparable with the public sector of a communist emerging market country, even if the same definition is applied when measuring it.

Consistency among indicators. A set of indicators should be composed of individual indicators that are consistent and that complement each other. For example, in the case of indicators relating to the institutional sectors of an economy, the sector classification should cover the whole of the economy, but the sectors should not overlap – unincorporated enterprises should either be classified in the households sector or in the non-financial corporations sector. Moreover, flows and stocks should ideally correspond to each other such as deficit and net debt; the borrowing requirement and gross debt; or savings plus net capital transfers and changes in net worth.

International statistical standards. Although harmonisation and consistency among indicators is thinkable outside the scope of existing international statistical standards, this is not practical. Cross-country harmonisation takes considerable time as it has to be in the context of the heterogeneous institutional frameworks of the economies. There is also a risk that harmonisation outside the scope of international statistical standards could fail owing to political considerations in the multilateral surveillance. Moreover, international statistical standards offer a range of statistics relating to a selected indicator that are useful for its analysis and for statistical quality assurance.

Reliability. The greater the role of an indicator in triggering significant policy actions, the stronger its statistical foundation must be. Thus, the collection and compilation of the underlying statistics must be verifiable and the use of judgement should be kept to a minimum. The general government deficit indicator for the excessive deficit procedure is an example of EU statistics that should be reliable.

Timeliness and revisions. The degree of timeliness required is typically not very high, as multilateral surveillance is not part of day-to-day policy-making but is used to assess the economic stance following national policy decisions and is focussed on imbalances that build up gradually and can only be prevented or corrected in the medium term. The underlying statistics should therefore not be flash estimates that are naturally subject to revisions. The timetable for multilateral surveillance is best designed by taking into account the release and revision cycles of the underlying statistics. This is obviously a challenge and is an area of tension between policy-makers and statisticians. For practical reasons, in the multilateral surveillance process sensible cut-off dates may be applied for the indicators. Otherwise, policy decisions may become invalid due to revised data or, what is more likely, the underlying statistics may not be revised, irrespective of new data becoming available.

Consistency over time. Multilateral surveillance is focused on current and future imbalances; the understanding of past imbalances is only relevant insofar as it is useful in this respect. Projections are therefore a common feature of multilateral surveillance processes. The reliability of projections is typically enhanced by long time series of underlying statistics without frequent or significant breaks.

The choice of economic and financial indicators for multilateral surveillance must also be based on statistical considerations. To neglect them would be a grave error.

Statistical governance of the selected indicators

Obtaining economic and financial statistics is costly. The collection of data from reporting agents, the compilation of statistics by national statistical institutes and central banks, and their dissemination to the public and to supranational and international organisations involves many parties. The introduction of new and large-scale multilateral surveillance processes requires the reallocation of human and financial resources and a review of the statistical priorities. The continuous provision by all economies of statistics that are relevant, harmonised, reliable, timely, subject to only moderate revisions, consistent over many years, and without gaps is enormously costly and is unlikely to be achieved even in cases where high importance is attached to multilateral surveillance.

It is, therefore, necessary for any large-scale multilateral surveillance to entrust a **high level statistics committee** with the detailed implementation and continuous provision of the indicators and the underlying statistics. In the case of the statistics on the excessive deficit procedure, this role is filled by the Committee on Monetary, Financial and Balance of Payments Statistics which brings together senior statisticians from the European Statistical System and the European System of Central Banks. The provision of the scoreboard indicators and the economic and financial statistics underlying the EIP will likewise need to be supported by a committee of senior government and central bank statisticians. In the context of the G20, there is an urgent need for a working group on statistics. This would complement the successful work of the Inter-Agency Group on Economic and Financial Statistics which is composed of representatives of the statistics departments of the Bank for International Settlements, the European Central Bank, the European Commission (Eurostat), the International Monetary Fund, the Organization for Economic Co-operation and Development, the United Nations and the World Bank.

The tasks of such a high level statistics committee mainly pertain to the implementation of the requirements for economic and financial statistics detailed in the previous section. They focus in particular on the harmonisation of the statistics, their availability and timeliness, the alignment of the statistical releases and revision policies, the easy accessibility of the data, and, increasingly, on monitoring the reliability of the data – a task for which the committee must operate with a high degree of independence. The progress achieved and the areas for improvement would need to be reported regularly to policy makers. Experience has shown that multilateral surveillance without careful monitoring of the quality of the indicators and the underlying statistics is not likely to be sustainable.

Preparedness of official statistics

The national, supranational and international authorities involved in compiling **official statistics are well equipped to support multilateral surveillance**. The harmonisation of statistics for economic areas, such as the EU, and also worldwide has a long history and tradition.

Official statistics are supported by **international statistical standards**. A number of major standards, including the System of National Accounts 2008 and the IMF Balance of Payments and International Investment Position Manual, sixth edition, have recently been updated and adopted following a worldwide consultation process. Other manuals and handbooks, such as the Public Sector Debt Statistics Guide and the Handbook on Securities Statistics, are in the process of being updated. Official statistics are also guided by the **Fundamental Principles of Official Statistics** of the United Nations Statistical Commission (UNSC) and the **quality frameworks**, such as the IMF Data Quality Assurance Framework, the European Statistical System Code of Practice and the public commitment on European statistics by the European System of Central Banks, that are derived from and build on these fundamental principles. Furthermore, seven supranational and international organisations are sponsoring the **Statistical Data and Metadata eXchange (SDMX)** standard that will be implemented step-by-step.

Moreover, compilers of official statistics are very well connected at the regional and international level. They also have an **accepted governance structure**, laid down in part in supranational and international legislation. In this context, the UNSC, the IMF Balance of Payments Committee, the OECD Statistics Committee, the Irving Fischer Committee, the Committee on the Coordination of Statistical Activities and the Inter-Agency Group on Economic and Financial Statistics are notable international bodies, while the European Statistical System Committee, the ESCB Statistics Committee and the Committee on Monetary, Financial and Balance of Payments Statistics are notable EU bodies.

Main challenges ahead

With regard to the EU, the legislative package on strengthening EU economic governance will be adopted in the coming months. In parallel, the European Commission (Eurostat and DG ECFIN) and the European Central Bank will organise the implementation of the EIP scoreboard and the provision of a database to contain the EIP indicators, threshold values and underlying statistics. These statistics will be coordinated with the macroeconomic statistics used by the ESRB for the macro-prudential oversight of the EU financial system.

At the level of the G20 the arrangements are less straightforward. While the Inter-Agency Group on Economic and Financial Statistics, in line with the IMF staff and FSB Secretariat progress reports on “The Financial Crisis and Information Gaps”, continuously promotes the further development and implementation of the international standards for macroeconomic statistics and for data supporting financial stability, there is not yet a **G20 working group on statistics**. This hampers the statistical support that the statistical authorities of the G20 economies are able to offer for G20 initiatives.

Nevertheless, the **Inter-Agency Group on Economic and Financial Statistics** has made considerable progress on (i) agreeing harmonised reporting templates under the updated international statistical standards, (ii) arranging for a better coordinated data flow among supranational and international organisations, and (iii) presenting harmonised statistics in a timely fashion on the Principal Global Indicator (PGI) website, with the further objective of developing the PGI website into a showcase for SDMX compliance, including metadata and visualisation tools.

The increasing need for multilateral surveillance is one of the clear lessons of the financial and economic crisis. To the extent that multilateral surveillance is based on indicators, there is much to gain from close cooperation between policy-makers and statisticians.