Item 24:
Macroeconomic Imbalances Procedure

ESTP course on National Accounts
ESA 2010
Luxembourg, 16 - 20 June 2014
Eurostat, BECH Ampere

Outline
• Economic and policy context
• Macroeconomic Imbalances Procedure
• Scoreboard: Application
• Statistical challenges
• Dissemination issues
• 2014 Statistical Annex and 2014 IDRs
• Appendix

What has happened to Spain?
Policy context: the crisis

- The financial crisis, the economic crisis, and the sovereign debt crisis that swept over Europe in 2008 and the following years lead to a number of new EU Policy initiatives
- A reinforced economic agenda with closer EU surveillance
  - Europe 2020
  - Euro Plus Pact
  - European semester
- Action to safeguard the stability of the euro area
  - support mechanisms for its Member States (ESM)
Macroeconomic Imbalance Procedure
Breaking the negative feedback loop

- Fiscal Discipline
- EU supervision
- Europe 2020: Structural Reforms
- Bank restructuring, recapitalisation, funding
- Structural reforms
- Differentiated fiscal consolidation, quality of public finance
- Improved Governance (SGP, MIP, Fiscal Compact)
- Financial Stability
- Project Bonds

- Macroeconomic Imbalances Procedure
  - Six-Pack Regulation: Commission proposal of 29 September 2010 on an Enhanced Economic Policy Coordination, including Macroeconomic Imbalances Procedure (MIP)
  - MIP in place since 2011
  - Last exercise: autumn 2013
Macroeconomic surveillance: the procedure

- Commission procedure aiming to the identification of emerging or persistent macroeconomic imbalances at an early stage
- Based on a scoreboard consisting of a small number of relevant macroeconomic and macro-financial indicators
- Compiled according to the principles of the European Statistics Code of Practice of the European Statistical System
- Combined with thresholds defined by the Commission
- Annual exercise: results published in the Alert Mechanism Report

Macroeconomic surveillance: AMR and IDR

- Alert Mechanism Report identifies the countries which require in-depth reviews
- In-depth reviews, the Commission determines if imbalances exist. Depending on severity use 'preventive arm' or 'corrective arm'.
  - Not excessive: Follow-up embedded in the European Semester, i.e. recommendation integrated in country-specific recommendations.
  - Excessive imbalance: the MS will prepare a 'corrective action' roadmap for implementing adequate measures. If EA-MSs repeatedly fail to take agreed action or to deliver a sufficient corrective action plan, then sanctions (up to 0.1% of GDP).
  - 'Programme countries' are not covered but under tight surveillance

MIP at a glance
MIP: what to look at?
- Housing bubbles
- Loss of competitiveness
- Public and private indebtedness
- Financial and asset market developments, including housing
- Evolution of private sector credit flow
- Evolution of unemployment
- Evolution of current account and net investment positions of Member States
- Real effective exchange rates
- Share of world exports
- Nominal unit labour cost

MIP Headline Indicators Scoreboard

External Imbalances
- Balance of Payments
- Current account
- Net international investment

Internal Imbalances
- House price developments
- Private sector credit flow
- Private sector debt
- General government debt
- Unemployment rate
- Real effective exchange rate (REER)
- Share of world exports
- Nominal unit labour cost

Macroeconomic surveillance: the scoreboard interpretation
- MIP scoreboard indicators should not be regarded as either policy targets or policy instruments
- Their interpretation should be supplemented by economic judgment and country-specific expertise
- The composition of the MIP scoreboard indicators may evolve over time
**Current Account Balance**
- Reference indicator: past three years average of CAB in % of GDP (BOP data)
- Summarises economic transactions of an economy with the rest of the world
- Major driver of net lending/net borrowing of an economy
- High current account deficit: the economy is borrowing, typically it is importing in excess of its exports
- Different reading in catching-up economies
- Thresholds: +6% of GDP and -4% of GDP
- Sustainability to be assessed case by case

**Net international investment position**
- Records the net financial position (assets minus liabilities) of the domestic sectors of the economy versus the rest of the world, as a stock
- Expressed in % GDP
- BOP data
- Typically, highly negative NIIPs result from persistently high current account deficits
- Threshold of -35% of GDP

**BOP: auxiliary indicators for economic interpretation**
- Sum of current account and capital account (Net lending/borrowing)
- Net External Debt (NED)
- Inward FDI flows
- Inward FDI stocks
Real Effective Exchange Rate (REER)

- Produced by DG ECFIN
- Percentage change over three years of the REER (NEER deflated by CPI, NEER computed as a weighted AVG of a currency’s exchange rates versus foreign currencies)
- Symmetric thresholds +/-5% for EA, +/-11% non EA
- Global competitiveness excluding exchange rate effects
- Drivers of persistent changes in price and cost competitiveness of each MS relative to its major trading partners (41 since 2013)
- Generally considered as an early warning indicator

REER – auxiliary indicators for economic interpretation

- Real effective exchange rate - Euro Area trading partners
  - *persistent divergence in price and cost competitiveness versus EA partners may hamper the smooth functioning of the monetary union*
- REER developments analysed together with other competitiveness indicators (ULC and EMS)

Export Market Shares (EMS)

- Percentage change of export market shares over five years (BOP goods and services data)
- Transformation aiming to capture long-term competitiveness development, structural losses
- Lower threshold: -6%
- Numerator effect: increase/decrease of MS export volume
- Denominator effect: growth of total world exports in goods and services
- Auxiliary: EMS in volumes (at constant prices) to factor out the effect of relative prices development
Nominal Unit Labour cost index
- Transformation: percentage change over three years to dampen cyclical effects and keep memory of built-up competitiveness losses
- Comparing remuneration (compensation per employee) and productivity (GDP per employed) to measure the average cost of labour per unit of output
- NA data
- EA threshold: +9%, non EA threshold:+12%
- A rise in an economy’s NULC corresponds to a rise in LC that exceeds the increase in labour productivity
- Auxiliary: NULC 10 years % change to capture longer-term losses in cost competitiveness

House Price Index (HPI)
- COMM Regulation (EU) 93/2013 on owner-occupied housing price indices + Handbook on residential property price indices
- Year-on-year change
- Threshold: +6%
- Deflated by NA deflator for final consumption expenditure of households and NPISH to reflect the value of house prices relative to the whole consumption basket
- Booms and busts in housing markets affect the real economy through a variety of channels and can be an important source of macroeconomic imbalances
- A positive value indicates that house prices grow faster than consumer spending
- Auxiliary: 3 years % change

Private sector debt - consolidated
- Expressed in % GDP (stock)
- Measuring the debt of the non-financial private sectors (non-financial corporations plus households and NPISH)
- Threshold: +160%
- Consolidated data available in 2013 to measure, by and large the amount of funds that the sector receives from other sectors
- Since 2013, exclusion of financial derivatives from securities (changed definition)
  - Improve data comparability
  - Capture liabilities contracted as funding sources
- Consolidation is highly relevant in the non-financial corporations (NFC) sector whereas negligible for households
- Auxiliary: non-consolidated data
Private sector credit flow - consolidated
- Expressed in % GDP
- Threshold: +15%
- Flow counterpart of private sector debt
- Consolidated data available in 2013
- Since 2013, exclusion of financial derivatives from securities (changed definition)
- Linked to probability of banking crises in the literature
- Auxiliary: non-consolidated data

General government gross debt (GGGD)
- Expressed in % GDP
- Threshold: +60%
- Maastricht Treaty definition: consolidated GGGD of the whole general government sector at nominal value, outstanding at the end of the year (EDP and SGP)
- GGGD comprises central government, state government, local government, and social security funds
- Data for the general government sector are consolidated between sub-sectors at the national level
- Aim at offering a broader picture of Member States’ indebtedness
- A high level of GGGD increases the vulnerability of a Member State and weakens its room of manoeuvre to deal with crisis situations

Unemployment rate
- Number of unemployed persons as a percentage of the labour force based on International Labour Office (ILO) definition
- 3 year backward average
- Threshold: +10%
- Aim to monitor high and persistent rates of unemployment
- Several auxiliary indicators covering unemployment since 2013
**Total financial sector liabilities**

- Expressed as year on year growth rate
- Threshold: +16.5 %
- Aim at measuring the evolution of the sum of all liabilities of the total financial sector to capture its linkages with the real economy
- A very broad measure of the expansion of the exposure to potential risks in the financial sector
- Good early-warning qualities
- Added in 2012
- Auxiliary: Financial sector leverage (debt-to-equity ratio)

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**Data sources**

- NSIs and Eurostat are the main provider
- The CBs and the European Central Bank produce some indicators from the BoP
- The REER indicators are compiled by DG ECFIN
- The International Monetary Fund provides a figure for global exports
The role of Eurostat

• Provide methodological support in the process of choice and definition of indicators
• Produce and supply the relevant statistical data
• Ensure high quality of data
• Foster harmonisation of production processes
• Foster documentation of production processes

The scoreboard website

• Dedicated section of the Eurostat website: scoreboard website
• Quarterly and additional data easily accessible in the same page
• Data up-to-date
• Data available for all member states
• Users can also find metadata in the standard ESMS format
• And, for each indicator, a direct link to a table containing longer time series
Statistical challenges
- Comparability, Reliability, Consistency
- Last 10 years of data (plus inventories and quality reports)
- In 2014
  - ESA 2010
  - BPM6

The Statistical Annex 2014
- 11 headline indicators + 28 auxiliary indicators
- REER
  - Basket extended to 41 trading partners (China, Brazil, Russia, South Korea and Hong-Kong)
  - Better accounting for the increasing role of some emerging economies when measuring competitiveness
  - Export market shares compared to advanced economies

Statistical developments
- Handbook on residential property price indices released in April 2013
- On-going work on backward data calculation aiming at increasing the length of back series
**Statistical developments (cont.)**

- Debt of the non-financial private sectors now measured in consolidated terms
  - Consolidated debt corresponds, by and large, to the amount of funds that the sector receives from other sectors
  - Non-consolidated debt gives the total gross indebtedness of the sector, including debts between two entities of the same sector
  - Unavailability of data for all countries in 2013

- Financial derivatives excluded from the definition of the private sector debt
  - Removing derivatives from the definition improves the comparability of data among the EU Member States
  - Capture liabilities contracted as funding sources

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### 2013 scoreboard – flashing indicators

| IE | 6 | IDR - Imbalances (just out of programme) | IT | 2 | IDR - Excessive Imbalances |
| ES | 6 | IDR - Imbalances | UK | 3 | IDR - Imbalances |
| CY | 6 | IDR - Imbalances | HU | 3 | IDR - Excessive Imbalances |
| PT | 4 | programme | SE | 3 | IDR - Imbalances |
| SL | 5 | programme | EE | 3 | IDR - Imbalances |
| NL | 5 | IDR - Imbalances | SI | 3 | IDR - Excessive Imbalances |
| DE | 4 | IDR - Imbalances | SK | 3 | IDR - Excessive Imbalances |
| FR | 4 | IDR - Imbalances | BG | 2 | IDR - Imbalances |
| LU | 4 | IDR - Imbalances | DK | 2 | IDR - Imbalances |
| HU | 4 | IDR - Imbalances | LV | 2 | IDR - Imbalances |
| BE | 3 | IDR - Imbalances | LT | 2 | IDR - Imbalances |
| MT | 3 | IDR - Imbalances | PL | 2 | programme |
| AT | 3 | IDR - Imbalances | RO | 2 | programme |
| FI | 3 | IDR - Imbalances | CZ | 1 | IDR - Imbalances |
| | | | | | |

| IE | 6 | IDR - Imbalances (just out of programme) | IT | 2 | IDR - Excessive Imbalances |
| ES | 6 | IDR - Imbalances | UK | 3 | IDR - Imbalances |
| CY | 6 | IDR - Imbalances | HU | 3 | IDR - Excessive Imbalances |
| PT | 4 | programme | SE | 3 | IDR - Imbalances |
| SL | 5 | programme | EE | 3 | IDR - Imbalances |
| NL | 5 | IDR - Imbalances | SI | 3 | IDR - Excessive Imbalances |
| DE | 4 | IDR - Imbalances | SK | 3 | IDR - Excessive Imbalances |
| FR | 4 | IDR - Imbalances | BG | 2 | IDR - Imbalances |
| LU | 4 | IDR - Imbalances | DK | 2 | IDR - Imbalances |
| HU | 4 | IDR - Imbalances | LV | 2 | IDR - Imbalances |
| BE | 3 | IDR - Imbalances | LT | 2 | IDR - Imbalances |
| MT | 3 | IDR - Imbalances | PL | 2 | programme |
| AT | 3 | IDR - Imbalances | RO | 2 | programme |
| FI | 3 | IDR - Imbalances | CZ | 1 | IDR - Imbalances |
**Number of flashing Indicators**

- At least one indicator was outside the thresholds for all MSs (without CZ, all MSs at least 2)
- 6 out of 11 is the maximum number of flashing indicators (7 in the Scoreboard 2011 as published in 2013)
- For RO, under financial assistance programme, only 2 indicators are flashing: CA and NIIP
- Some indicators are no flashing at all: HPI yoy, private sector credit flow, total financial sector liabilities yoy

**Flashing indicators - country with excessive imbalances**

- **HR:**
  - NIIP as % GDP: -89 (th. -35%)
  - EMS % change over 5 years: -24.7 (th. -6%)
  - Unemployment rate 3 y. AVG: 13.8 (th. 10%)
- **IT:**
  - REER % change over 3 years: -6.2 (th. ±5%)
  - EMS % change over 5 years: -23.8 (th. -6%)
  - General government sector debt in % GDP: 127 (th. 60%)
- **SI:**
  - NIIP as % GDP: -45 (th. -35%)
  - EMS % change over 5 years: -19.9 (th. -6%)

**Flashing indicators - country with no imbalances**

- **DK:**
  - EMS % change over 5 years: -18.6 (th. -6%)
  - Private sector debt % GDP: 239 (th. 133)
- **LU:**
  - 3 y AVG CAB in % GDP: 7 (th. 6)
  - EMS % change over 5 years: -18.3 (th. -6%)
  - Private sector debt % GDP: 317 (th. 133)
- **MT:**
  - REER % change over 3 years: -7.7 (th. ±5%)
  - Private sector debt % GDP: 155 (th. 133)
  - General government sector debt in % GDP: 71 (th. 60)
**IDRs 2014 – countries overview**

- Covering 17 countries: 16 announced in November plus IE exiting the programme
- Excessive Imbalances: HR, IT, SI (could trigger the corrective arm)
- Imbalances for 11 out of 17 (preventive arm)
- No imbalances: DK, MT, LU
- Specific monitoring of policy implementation for: HR, IT, SI and IE, ES and FR
- SGP: for FR and SI risk of non-compliance with 2014 budgetary target

**Reading of the scoreboard**

- No single indicator can capture all potential risks:
  - Analysis in connection with other scoreboard indicators
- The number of flashes is not the key criteria
- The scoreboard should be read also over time
- The severity of a breach of a threshold can be considered
- The auxiliary indicators play an important role

**The scoreboard in AMR 2012 to 2014**

<table>
<thead>
<tr>
<th>AMR</th>
<th>2012</th>
<th>2013</th>
<th>2014</th>
<th>NISP/NIIP/ESM/FIS/JSO/AVO</th>
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<tbody>
<tr>
<td>NL</td>
<td>3</td>
<td>4</td>
<td>4%</td>
<td>CA/REER/ESM/PSD/AVO</td>
</tr>
<tr>
<td>FR</td>
<td>3</td>
<td>3</td>
<td>3%</td>
<td>CA/REER/ESM/PSD/AVO</td>
</tr>
<tr>
<td>DE</td>
<td>3</td>
<td>3</td>
<td>3%</td>
<td>CA/REER/ESM/PSD/AVO</td>
</tr>
<tr>
<td>HR</td>
<td>-</td>
<td>-</td>
<td>-%</td>
<td>CA/REER/ESM/PSD/AVO</td>
</tr>
<tr>
<td>IT</td>
<td>2</td>
<td>2</td>
<td>2%</td>
<td>CA/REER/ESM/PSD/AVO</td>
</tr>
<tr>
<td>BE</td>
<td>3</td>
<td>3</td>
<td>3%</td>
<td>CA/REER/ESM/PSD/AVO</td>
</tr>
<tr>
<td>MT</td>
<td>3</td>
<td>3</td>
<td>3%</td>
<td>CA/REER/ESM/PSD/AVO</td>
</tr>
<tr>
<td>FI</td>
<td>4</td>
<td>4</td>
<td>3%</td>
<td>CA/REER/ESM/PSD/AVO</td>
</tr>
<tr>
<td>SE</td>
<td>4</td>
<td>3</td>
<td>3%</td>
<td>CA/REER/ESM/PSD/AVO</td>
</tr>
<tr>
<td>UK</td>
<td>4</td>
<td>3</td>
<td>3%</td>
<td>CA/REER/ESM/PSD/AVO</td>
</tr>
<tr>
<td>SI</td>
<td>2</td>
<td>2</td>
<td>2%</td>
<td>CA/REER/ESM/PSD/AVO</td>
</tr>
<tr>
<td>DK</td>
<td>2</td>
<td>2</td>
<td>2%</td>
<td>CA/REER/ESM/PSD/AVO</td>
</tr>
<tr>
<td>BG</td>
<td>4</td>
<td>2</td>
<td>2%</td>
<td>CA/REER/ESM/PSD/AVO</td>
</tr>
</tbody>
</table>
Dimensions of IDRs

- External competitiveness: CA and EMS
- Internal competitiveness: Labour costs
  - Wages
  - Labour taxation
  - Adjustment capacity of the labour market (employment rate, participation of specific groups)
- General government debt
  - Sustain to the financial sector
  - Owners of public debt
- Degree of healthiness of the private sector
- Social indicators

Conclusions

- The MIP scoreboard is an evolving set of indicators whose composition and performance in terms of early warning need to be monitored
- It is used within the AMR as the initial step of the IDRs process
- Economic interpretation cannot be constrained to official statistics
- Quality of indicators is crucial and NSIs and Eurostat can play an important role

ESTP course on MIP

- Taking place from 9 to 11 of December 2014
- Deadline for registration is 10 of October 2014
Thank you for your Attention!!

Appendix

Macroeconomic imbalances: risks
General Government debt and GDP exposed to:
- Private indebtedness
- External debt
- Competitiveness
- Asset and House price bubbles
- Banks & financial leverage
Progress in rebalancing

Most of adjustment so far has been by the deficit countries. The euro area may record a moderate surplus.

Source: Eurostat (BoP), Commission services forecast.

Trends in the EA

Saving and investment gaps by sector

Surpluses were largely due to high savings of the private sector, most notably households and non-financial corporations.
Intra-euro area imbalances have declined, while surpluses with the non-EA and RoW increased.

[Di/con]vergence in external positions
Current account positions in the EA: surplus vs. deficit countries

Source: EUROSTAT
Competitiveness developments

Competitiveness divergence: REER vis-à-vis the euro area average (Euro area = 100)

Relative loss in competitiveness
Relative gain in competitiveness

Source: DG ECFIN

Across-the-board increase of private debt

Sector decomposition of private indebtedness (% of GDP)

Source: EUROSTAT

Rebalancing needs and prospects

Current Account
Level of Total Debt

Source: EUROSTAT; ECFIN