

**Financial Statistics Users' Group Discussion Meeting held in
association with the National Accounts User Group on
Statistics For European Monetary Union**

11 November 1999

Speech by John Vickers, Chief Economist, Bank of England

EMU STATISTICS IN UK POLICY MAKING¹

¹ I am grateful to colleagues, especially Andrew Bailey, for their help in preparing these remarks.

Monetary policy makers are avaricious consumers of statistics. It has been said that Alan Greenspan reads the US Statistical Abstract from cover to cover. True or not, I can vouch for the fact that the Monetary Policy Committee, in its monthly round of meetings, sees a great deal of data. Some of you may know that we have a day-long Pre-MPC meeting, on the Friday before the week of our rate-setting meeting, at which Bank staff present a comprehensive synthesis of the latest developments in the world and UK economies and in financial markets. Typically, we see around 300 slides that day, most containing statistics in chart or table form. Many of these statistics will already have crossed our desks, and increasingly our screens, day-by-day during the month, with accompanying briefing notes. And if that is not enough, we have at our elbows a continuously updated chartpack, which contains 500 or so charts and tables. I hope that demonstrates our consumer demand for statistics, and how it is fed.

Of course it was not always thus. Our forbears, lacking a wide array of official statistics and survey data, let alone modern information technology, necessarily had a rather narrower vision. But they had—and the Bank still has—an accurate and timely data source that the MPC blithely ignores. I refer to the wind dial in the Bank's Court Room, which was originally installed in 1805. In the days of sailing ships, which way the wind was blowing could matter a good deal for London's financial markets—*plus ça change*—and I recommend for scholarly attention the subject of wind direction in the formulation of monetary policy.

But back to the present. How interested are we in EMU data? I want to answer this question from the point of view of the Bank of England, not just the MPC—in other words covering our key responsibilities for maintaining price stability through the operation of monetary policy and for the stability of the financial system as a whole.

Starting with monetary policy, I should at the outset stress that we do not use euro area data in order in some sense to shadow the euro, ECB policy, or anything else of that sort. However, since euro area members are collectively the largest trading partner of the UK—accounting for somewhat over half of gross UK trade—the importance of the area in the MPC's conjunctural assessment and forecasting should be clear. In this respect, monitoring and interpreting economic developments in the euro area form a key element in the MPC's analysis of global developments and how they affect UK monetary policy. For that reason, we devote a good deal of attention to assessing the economic conjuncture in euro area countries, including making euro area projections as an input to our own UK projections that you see in the quarterly *Inflation Report*.

The advent of the MPC has increased in many ways the demands upon the Bank staff in terms of analytical support, and one area where we realised quite soon that more was needed was international economic analysis. To meet that need we therefore established earlier this year a separate division, headed by Andrew Bailey, in the wing of the Bank responsible for monetary analysis. The euro area is obviously a major part of the work of that division. That work is mostly consumed within the Bank (not just by the MPC), but it is more generally visible in a number of places—in the MPC minutes for instance, which typically start by reflecting the Committee's discussion of the world economy, and, perhaps less well known, in a regular article on the world economy in the Bank's *Quarterly Bulletin*, which is in some ways a supporting pillar of the *Inflation Report*.

The UK projections in the *Report* itself are based in part on an assessment of the outlook for the world economy which reflects the MPC's best collective view of, particularly, those trade volume and price variables which have most impact on UK output and inflation prospects. Indeed our quarterly forecast round starts—well over a month before the *Inflation Report*—with discussion of the world outlook. Given the focus of the MPC's work, much of our international analysis is conducted in UK trade weighted terms, and this means of course that the euro area has a large weight in it. But forecasting the euro area economy is not easy—forecasting is never easy—and there are particular challenges in relation to the euro area.

First of all, monetary union self-evidently involves—indeed is—a fundamental change of economic regime, and hence of economic relationships—though this will happen over a period of time; and, to complicate matters more, the length of that period differs across a number of dimensions, including among the member countries.

Such a fundamental change makes the interpretation of statistics especially difficult, and so makes their availability all the more important. There is a great onus on the statisticians to help us see through the complex process. And, in turn, that process also makes their life a great deal more complicated. The demand for euro-area wide statistics—prepared on a timely and consistent basis—has of course been present from day one (indeed before), but creating such harmonised data is by no means straightforward. Important strides have been made, for example in relation to ESA95, but demand will not let up, particularly for timely releases.

The last few months have illustrated the need for timely data on activity in the euro area. Most observers share the view that activity in the euro area should pick-up in the second half of this year, but the lags in the official data in a number of countries mean that we are in the dark for longer than ideal, and often substantially longer than here in the UK. Therefore we have to go more on trust, and place more weight on available survey evidence, not just to provide a forward view of prospects, which is where such evidence is essential for all countries, but for also the recent past too. This is in no way to denigrate such survey evidence (to which we at the Bank pay a great deal of attention), nor to put official estimates on a pedestal of absolute truth (estimates are estimates and naturally subject to revision). The point is simply that more timely official data to some degree help minimize the ever-present risk of monetary policy mistakes.

The agenda for official statistics is daunting—and it is always easy for those of us on the policy side to come up with wish-lists without understanding the challenges and the work in train that already exist. But where in particular would we like to see more in terms of euro area statistics? Two subjects high on the list—and this is not meant to sound like a UK list!—would be measures of service sector output and of the rate of change of labour costs.

An academic colleague of mine once concluded a book review by saying: ‘This book fills a much needed gap’. By contrast, information on the service sector is a gap that badly needs filling. Most developed economies are now split roughly 75/25 between services and manufacturing, but when it comes to statistics the split seems typically to be more like 25/75. Economic modelling tools, such as those that we use at the Bank,¹ are necessarily calibrated on past data (what else?), but this emphatically does not imply any assumption that the economy now is just like it used to be. We know that it isn’t—as the shift towards service sector activity well illustrates—but the problem is to judge the extent, nature and consequences of structural change. Better data would assist that sort of judgment, including—perhaps paradoxically—better data about the past.

As regards labour costs and earnings growth—the *cause célèbre* of UK statistics—it is now well understood that collecting and interpreting these data is not easy, not least at a time when the structure of remuneration appears to be shifting to some degree away from fixed pay to more variable elements. But we are constantly reminded how important they are as an input to policy analysis, and flying blind is, I can assure you, not a comfortable feeling.

¹ See our book *Economic Models at the Bank of England*, published in April 1999.

I mentioned earlier that the fundamental change brought about by EMU will have an impact on different countries in different ways. For example, impacts may differ across countries on account of differences in states of economic development (the issue of productivity catch-up), differences in monetary transmission mechanisms, and so on. The single monetary policy obviously operates at the euro area level, and we need statistics to reflect that. But in my view we also need to continue to have available good quality national data, so that we can understand and assess these differences. To take one example, the issue of catching-up—the impact on productivity in the tradeable and non-tradeable sectors, and what that means for inflation in different countries—is important if we are to understand properly pressures at the area-wide level.

The general point here—that understanding the parts adds to the understanding of the whole—has an exact analogy within the UK. While the MPC's remit clearly applies to the UK as a whole—just as the ECB's clearly applies to the whole euro area—the regional and sectoral information that we gather, for example through the Bank's agents, is very important in the pursuit of that remit. Likewise for the euro area. So while David Walton rightly says² that 'European statistical integration has not kept pace with European Monetary integration', country level data remain nonetheless important.

As I noted earlier, I am interpreting my remit quite liberally today, and so I want to add something about the use of EMU statistics in the Bank's financial stability work. This work aims to assess the potential—or in the worst case actual—threats to the stability of the UK financial system. Obviously, just as the euro area looms large in our assessment of the impact of the world on the UK macroeconomic conjuncture, so the same weight is given to the area in our financial stability assessment. In this context, we are interested in the potential impact of EMU via effects on credit creation, asset prices (financial and non-financial), debt and leverage, the structure of financial intermediation (and changes in the concentration of risk among financial institutions) and financial innovation, to name just some of the more important areas.

Here, too, there is an unsatisfied demand for more statistics, though again given the scale of the change, the existence of such demand is not surprising. One notable gap until very recently concerned data on the growth of euro securities markets. Other needs exist for fully developed flow of funds accounts at the area level which provide a clear view of external financing,

² In his foreword with Thomas Mayer to 'Understanding Euroland Economic Statistics', Goldman Sachs, October 1999.

leverage, private sector disintermediation of the banking sector, and so on. But again we also need to retain good quality data at national level insofar as financial developments at national level continue to matter for financial stability. And we need to avoid having data series which have large statistical breaks at the point of EMU—though I recognise that backward adjustment of old series is not straightforward—because policymakers have to judge whether recent developments represent a significant change in relationships.

EMU is a massive challenge for policymakers in many respects, not least because it represents such a fundamental regime change. I have offered some views from the outside, or perhaps the pre-inside, on the consumption of, and demand for, EMU statistics in the Bank of England. I have not discussed how the MPC transforms the large number of statistics that we gobble each month into the single statistic that we produce—the Bank’s official interest rate. That is explained elsewhere, for example in our minutes and the *Inflation Report*. But I hope I have given a sense of how we keenly look at everything relevant to the pursuit of our inflation target, and how EMU statistics have therefore become a key part of what we look at. And as they develop, EMU statistics will grow further in importance, whatever the UK’s future monetary arrangements.