BUFF/01/94

July 6, 2001

Concluding Remarks by the Acting Chairman
Macroprudential Indicators
Executive Board Meeting 01/64
June 25, 2001

Executive Directors welcomed the opportunity to discuss proposals to further the compilation, use, and analysis of macroprudential indicators (MPIs) of the health and stability of financial systems in the light of experience gained to date. They viewed the work on MPIs as an essential component of the response to the international community's call for strengthening the assessment and monitoring of vulnerabilities in financial systems. Directors noted that macroprudential analysis, including stress testing of financial systems' sensitivity to a variety of shocks, closely complements the use of early warning systems as both are important analytical tools that help to identify corrective action, thereby contributing to crisis prevention.

Directors stressed that these analyses and tests should take account of country circumstances and institutional characteristics. The importance of testing scenarios with a sufficiently high probability was also noted. Directors highlighted that aggregated data can conceal vulnerabilities and, where relevant, should be supplemented with data on dispersion, peer group analysis, and the results of stress tests. In addition, to produce valid conclusions, quantitative MPI-based assessments should be combined with qualitative assessments of risk management by both financial institutions and financial authorities. A few Directors encouraged further analytical work to develop thresholds of vulnerability for relevant indicators, while recognizing that threshold levels may vary across countries and over time.

Directors welcomed the strong positive response of compilers and users to the *Survey on the Use, Compilation, and Dissemination of MPIs* that was conducted in mid-2000. They were encouraged by the widespread interest of supervisors, policy analysts, and market participants in the use of MPIs to assess financial systems, which they considered augurs well for the Fund's cooperative approach in this area.

Nearly all Directors agreed that distinguishing between a core and an encouraged set of MPIs is helpful, and that the availability of a core set consisting of a small number of parsimoniously selected indicators useful in all countries will help prioritize future work. They considered the criteria applied to arrive at the core set, including the focus on banks and on analytical relevance, usefulness, and the availability of indicators, to be generally appropriate. While Directors expressed a variety of nuanced views on the MPIs to be included in the core set, on balance, they supported the proposed core set.

Directors also broadly supported the selection of a set of encouraged indicators, consisting of additional indicators for the banking sector, as well as indicators for the nonbank financial sector, the corporate and household sectors, and real estate markets. They agreed that the encouraged set, while including indicators that may be equally important as the core MPIs, provides flexibility in the selection of indicators that are most relevant to assessing vulnerabilities in a specific country by avoiding a one-size-fits-all approach. Some Directors would have preferred a wider set of indicators, to be used depending on country-specific circumstances, but other Directors cautioned that the set of encouraged MPIs is already ambitious. All Directors agreed that more conceptual and empirical research is needed to improve the specification of indicators in the encouraged set, including the indicators for nonbank financial intermediaries and markets. Many Directors considered that the compilation of indicators for the nonbank financial sector and the corporate sector, as well as for real estate markets, should be promoted, in light of their relevance for the health of financial systems and usefulness as early warning indicators. Directors recognized, however, that the limited availability of these indicators in many countries may moderate progress in their use.

Directors noted that selected MPIs are already being reported as part of Fund surveillance and encouraged such reporting in the future, as warranted, as well as the use of these MPIs in vulnerability assessments. They agreed that a more general compilation and greater use of MPIs, with a focus on the core set, will pave the way for a significant strengthening of Fund surveillance. Directors supported the proposal for a more systematic compilation of macroprudential data in the context of the Financial Sector Assessment Program (FSAP), which provides inputs to the Fund's Financial System Stability Assessments (FSSAs), and in those Article IV consultations where in-depth financial sector assessments are undertaken. MPIs will also be included in Article IV consultation reports where data are available. Looking forward, a number of Directors expected that progress with the compilation of MPIs will permit systematic reporting in an increasing number of cases. Directors welcomed the preparation of a *Compilation Guide on MPIs* to assist compilers as well as official and private users of MPIs, and the development of a database for MPIs in the Fund. They also stressed that countries with less developed financial and statistical systems will need timely technical assistance to support their compilation efforts.

Directors agreed that MPIs can play an important role in providing markets with information on the overall state of the financial system and contribute to the building of market discipline. They discussed and many broadly endorsed the proposal for the Fund to encourage and facilitate voluntary efforts by national authorities to initiate dissemination of the core and encouraged MPIs and their metadata. Directors considered, however, that the Fund should proceed cautiously in this area, given the constraints on the availability of data and the critical importance of avoiding misperceptions or misinterpretations by financial markets of published indicators. They therefore emphasized the need for additional efforts to buttress the quality of the disseminated information so as to ensure that an accurate depiction of the condition of the financial sector is provided to the public and investors. Some Directors supported the principle of including MPIs in the Special Data Dissemination Standard (SDDS) framework. Most Directors, however, considered such a decision to be premature in view of the still substantial limitations on the availability, quality, and international comparability of data, and a number of Directors considered that MPIs should not be included in the SDDS, even at a later stage, so as not to discourage new subscriptions and overburden existing subscribers. Directors will come back to the possible role of MPIs within the SDDS in the context of the Fourth Review of the Fund's Data Standards Initiatives, scheduled for July 2001.

Directors supported the active collaboration with relevant international standard setting organizations aimed at developing harmonized standards and practices that will improve the reliability and comparability of MPIs across countries. In this regard, special attention should be given to improving the international comparability of data for nonperforming assets and provisioning, and the valuation of liabilities as well as assets. Directors also welcomed the close collaboration with other international organizations, including the World Bank and the Bank for International Settlements, on strengthening the framework for macroprudential analysis.

Directors broadly agreed with the proposed program of work and the phasing in of various activities. They welcomed the effort to absorb the expanded work within the existing work programs for the current year and noted that additional resources needed for the timely pursuit of the work program should be considered in the context of the fiscal year 2003 budget. They looked forward to a comprehensive progress report on the work program in about 18 months.