



# *Office Memorandum*

To: Members of the Executive Board

October 19, 2010

From: The Secretary

Subject: **Note on Spillover Reports**

As agreed at the September 1, 2010 Executive Board meeting on the Fund's surveillance mandate, attached for the **information** of Executive Directors is a note prepared by staff and discussed with EDs representing the five pilot cases (China, Euro Area, Japan, United Kingdom, United States) clarifying the expectations, process, and logistics for experimenting with "spillover reports" for systemic economies.

Questions may be referred to Ms. Shannon (ext. 35664) and Mr. Dauphin (ext. 39705) in SPR.

This document will shortly be posted on the extranet, a secure website for Executive Directors and member country authorities.

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## **SPILLOVER REPORTS**

*This note clarifies the process for experimenting with spillover analysis and reporting for the five economies that make up the bulk of world GDP and financial flows (the United States, the Euro Area, China, Japan and the United Kingdom). This note outlines the intended scope, logistics and reporting procedures for the pilot reports. The case for a common approach, with uniform treatment across the chosen cases is clear, but so is the need for flexibility and acceptance that there will be learning in any new initiative.*

### **A. Scope**

1. The exercise aims to assess the systemic implications of the concerned members' economic and financial policies, tracing out the transmission channels of monetary/exchange rate, fiscal, financial and structural policies on core elements of the global economy. Such channels include trade, capital flows (banks and nonbanks), financial exposures, confidence effects, and the impact on global risk aversion. The goal is a richer understanding of policy spillovers through staff analytical work and direct dialogue with both originating and affected countries. This is expected to help inform the debate on safeguarding global economic and financial stability, strengthen the Fund's bilateral and multilateral surveillance activities, highlight the policy dilemmas facing members, and point to possible areas for policy coordination. The focus will be on systemic effects, but the reports may also examine if spillovers vary across regions or types of economies (e.g., advanced, emerging, low income).
2. The goal is not to analyze how we got to the situation we are in but, informed by the analysis of the transmission channels exposed by the crisis, to anticipate the cross-border impact of established policies (i.e., in line with existing guidance for surveillance, those in place or announced that are, to staff's best judgment, likely to be implemented), as well as policies under consideration. The analysis will focus on spillovers with the greatest impact—positive or negative—on other countries and global conditions. Thus, for instance, it will cover issues such as the potential impact of exits from extraordinary policies (monetary and fiscal stimulus), financial sector reforms (new legislation/Basel), and structural reforms (those affecting potential growth, long-term fiscal measures, and monetary/exchange rate frameworks).

### **B. Timing and logistics**

3. All five spillover assessments will be conducted in the context of the Article IV consultations for participants next July. This timing allows for the spillover analysis to inform—and be informed by—multilateral surveillance activity, including the Fall 2011 WEO/GFSR and EWE.
4. Staff will prepare a preliminary assessment of spillovers based on its own analysis. It will complement the use of traditional macroeconomic models with a number of other analytical tools to capture transmission channels beyond those typically covered by macro-models. The team will be multi-departmental (including staff from the area department

Article IV team), bringing expertise across the Fund to dismantle “silos.” Staff’s work will be subject to the normal internal review process at all stages.

5. Based on preliminary analysis, staff will hold discussions individually with the respective authorities from both the economies where the spillovers originate and where the main systemic effects are felt. For affected countries, at a minimum, staff will consult the authorities of the four other economies for which spillover reports are also conducted, as well as major emerging markets. The selection of other countries will be informed by staff’s initial analysis—e.g., if this analysis shows that a particular spillover has systemic effects via a particular group of countries or regions, authorities from such economies would be consulted (for logistical convenience, with representative cases).

6. The initial analysis will involve short visits—ideally one—to each country/area, while the discussion of policy implications will be taken up as part of the Article IV mission:

- During the winter/early spring, staff teams will visit each country/area to hear the views of authorities on inward and outward spillovers and discuss its early findings. Staff will strive to minimize the burden on the authorities, with short (2-3 days) visits at the convenience of country authorities. It is not expected that meetings will need to be held at the ministerial level. Staff’s natural interlocutors for the studies are likely to be the international divisions of Ministries of Finance, Central Banks and relevant supervisory authorities, but other expertise may also be needed, as might technical meetings. Staff may also have discussions with academics, think tanks, and market analysts to enrich the analysis. To the extent possible, these visits will be timed to coincide with the Article IV mid-cycle staff visit.
- Around May, the leader of the spillover team will take part in the relevant policy meetings of the Article IV consultation mission, to bring the perspective of the spillover analysis and the feedback from staff visits to the broader economic discussion and the Article IV consultation team’s policy recommendations.

### **C. Reporting**

7. The staff’s assessment will be appropriately integrated into the Article IV report and summing up for each member/area, with the detailed analysis and discussion provided in a related background spillover report. The paper will present the full range of views of affected countries without individual attribution. A list of members consulted will be provided.

8. Consistent with the Fund’s overarching principle guiding its transparency policy to “strive to disclose documents and information on a timely basis unless strong and specific reasons argue against such disclosure,” the expectation is that the participants of the trial run will consent to the publication of the spillover report on their respective economies. Nevertheless, the five pilot cases retain the right not to consent to its publication. Corrections and deletions will be handled in line with the transparency policy.