

TAG meeting
11-14 October, 2005
Washington D.C.

Tuesday October 12th---The Meeting began with an introduction by Shaida Badiee that led to discussion of a number of reasons that various parts of the Bank were expressing interest in when the results of the 2005 ICP will be available. This was followed by Fred Vogel's report on the state of the ICP, and a lengthy discussion. Many of the points covered are included under the topics as they were discussed below. Because many of the topics covered did not keep to the agenda they are grouped below by topic covered each day; TAG conclusions are reported here, with only some flavor of the discussion.

I. What will be published?

Before entering into reference year issues, the TAG clarified again what it understands will be published from the ICP 2005. The following was reinforced:

There will be a preliminary and a final publication for certain analytical categories (to be defined). Users will have to be educated about the PPP revision policy. The first preliminary publication e.g. for food and clothing or total consumption will be based on 2005 prices 2004 weights structure, scaled to a "nowcast" estimate of the 2005 NA values, which are based on rough extrapolations nowcast estimate of the 2005 NA values

This will enable the global office to publish PPP, price level index and volume index of the chosen analytical categories and provide donors and users with early preliminary data. Final data will be published when a stable set of NA for 2005 is available from most countries. This will be not before end-2007. In other words, between the preliminary and final data from the ICP 2005, the prices for 2005 do not change, however the NA are revised.

Action 1: the global office is to collect NA weights for the last available year from all countries and analyze their reliability

Action 2: the global office is to find out when all countries will be able to provide the 2005 National Accounts values or, alternatively, nowcast 2005 of the NA values

Action 3: the global office is to adjust the timetable and the publication calendar accordingly

The content of the publication will be subject of a separate discussion.

II. How should we obtain annual average prices for consumer goods and services?

The problem is that not all countries will have data collection for all 4 quarters of 2005 and some may run into 2006 with collecting consumer prices. In order to achieve annual average prices for 2005, the following is recommended in order of preference:

(a) If a country has a sufficiently reliable CPI then:

The CPI is used to bring prices backwards and forwards. In case there is a strong seasonal pattern for individual products, a weighted CPI shall be used (Eurostat template maybe employed).

(b) If a country does not have a sufficiently reliable CPI and inflation is low (e.g. below 5%) then:

Use just the average of the quarters available as the annual average for 2005.

(c) If a country does not have a sufficiently reliable CPI and inflation is high then:

1) If there are 2 or 3 quarters of data extrapolate to the 2005 average.

2) If there is only one quarter, use a higher level CPI index to extrapolate.

III. How to achieve national average prices (consumer goods and services)?

A. Basic Requirement for Participation in the ICP

To participate in the ICP a country must be prepared and able to provide national average prices and national accounts for the country as a whole, not simply subsets like urban areas or several urban centers.

- 1) The TAG reiterated its commitment to the above principle set out at the first TAG meeting. With respect to prices, there may be countries with no national data collection allowing them to adjust their capital city/major city prices to national averages. To make this adjustment to national prices it may be necessary to use factors available from other sources, e.g. from the national CPI. This can be done at the level of basic headings or groups of basic headings, like fresh produce. If some evidence or acceptable reasons can be provided that the capital city prices are representative of the country as a whole for the items in some headings, it maybe necessary to accept that the adjustment factor is 1.
- 2) Nothing prevents countries from making price comparisons of prices in major cities within a Region. However, the TAG would strongly recommends that any such comparisons be totally separate from the Regional or Global ICP project. Such urban comparisons would not be reliable because output totals for urban areas are not comparable across countries, and because there is no predictable relationship of urban to national prices across countries. If there were such information, then there is no reason for a country not to use the information as suggested in 1) above. Moreover, would urban comparisons require special urban weights.

IV. Prices for construction, equipment goods and health and housing services

Price collection for construction, equipment goods and housing services will happen only in 2006. This retrospective pricing is possible as the sources of prices are quite different

from consumer goods and services, for which outlets have to be visited. For both Construction and Equipment treatment of taxes is very important.

The prices collected for construction and equipment goods have to be in line with the underlying National Accounts, which record only the non-deductible VAT: Therefore:

Collectors should be told that value added taxes should not be included in construction or equipment prices at their official rates because some of these will be deductible. The prices collected should include any non-deductible taxes, like excises or fees, but not deductible value added taxes.

Information on the average non-deductible VAT for equipment goods and the average rate of non-deductible VAT over all investing sectors in construction shall be collected from the National Accounts and the correction of the prices for non-deductible VAT should be done for all countries at the level of the regional office. The TAG agreed that the respective formulations in the Eurostat pricing guidelines and in the Eurostat/OECD PPP manual should be taken over in the ICP documentation. The respective questionnaires of Eurostat for non-deductible VAT can be used by other regions.

Construction: price collection should happen in the first half of 2006, asking the contracted construction experts to provide for each component annual and national average prices of 2005. This should cause no problems as the experts are quantity surveyors with access to respective data bases. In other words, for each component one price observation will be provided, which is directly the annual and national average price.

Equipment goods: price collection should happen in the first half of 2006, asking subject-matter experts to provide directly annual and national average prices 2005 for each item definition. This should be possible as, typically, there is in each country only one or two importers, producers or distributors for a certain type of equipment and prices do not change as frequently as for consumer goods. The importers, producers or distributors can be contacted and are able to provide the information retrospectively from their records.

Housing services (rents): data collection for the price and quantity approach should be done until end-2006. As the ICP questionnaires do not require new data collection but just re-use already existing information for 2005 from national rent surveys, censuses and the National Accounts, these existing sources can be consulted at any point in time in 2006. By definition, the sources already include national and annual average prices/information.

The TAG agreed to develop a new questionnaire to be initially sent to several National Accounts or Statistical Offices designed to extract the values/quantities underlying both market and owner occupied rents in the National Accounts. This questionnaire would take into particular account of 'quality issues' such as the facilities available, rural/urban locations, and the distinction of traditional and modern housing. Paul McCarthy has

agreed to set out a draft version of this questionnaire to be tried on several countries. This questionnaire will serve at least two objectives:

- 1) Provide the minimum quantity information required to carry out the quantity comparisons for owner occupied dwellings and
- 2) Develop rent comparisons that are not independent of the national accounts.

These changes will need to be reflected in Chapter 14

Health Services: There are issues both for pharmaceuticals and for medical procedures; and for the latter, there are difficult problems in holding quality constant. One of the measurement problems is how to compare the full social cost of health services. Prices cannot be just collected, but the so-called full price has to be constructed from what the consumer pays and what the government contributes to it. This may require the involvement of government bodies dealing with health and authorities supervising pricing of health goods and services. In the ICP expenditure framework countries are requested to provide government expenditures for individuals so that all countries have a total for Actual Consumption of the Population. However, there are a variety of ways in which countries finance these expenditures that eventually go to individuals, and often government accounts do not permit one to know the subsidy for a particular drug or medical service. These issues require further TAG discussion.

The countries are advised not to start price collection until there is methodological guidance available. A pre-condition for accurate establishment of full prices is also knowledge about the health systems in place in every country, e.g. health insurance system, who pays what under what conditions, the extend of the black market for medical goods and bribing for medical services, the level of records in the National Accounts of the latter etc. This should be part of the pre-survey.

Wednesday Oct. 13th

A. Fixity

There has been concern that the TAG, the Global Office and the Regions are on the same page with respect to what is meant by fixity of results. The following is a statement on what is meant by fixity that each Region plans to follow and is fully accepted by the TAG in their later discussions of linking and aggregation. Briefly, the

TAG reinforced the idea that when linking the regional comparisons to world-results, regional fixity for PPP and volume indexes at all levels of aggregation will be preserved.

This requirement may cause problems with the comparability of countries over regional borderlines that need to be addressed when making the final choice of the aggregation index at world level.

B. Publication level of ICP results and access to more detailed information.

1) **Publication of Results at the Global Level.** The level of regional publication (paper and publicly accessible databases) for PPP, volume index, nominal and real values and PLI will be determined by every region in accordance with the views of its countries and taking account of the level of error associated with estimates at more detailed levels. The world level publication will be determined by the most restrictive region. Currently, it seems that Eurostat/OECD will be most restricted and the respective set of analytical categories for publication is attached. The ICP may decide to use more aggregated information in the area of food, compared with the level of detail currently published by Eurostat.

2) **Access to More Detailed Information for Legitimate Users:** A different question is access to more detailed data under restricted procedures than those in the public domain, e.g. for researchers in national governments, international organizations, and private researchers in the academic or private sectors. The World Bank provided a standard letter sent to providing information with various procedures for maintaining national restrictions on confidentiality. However, discussion revealed a number of technical, practical and legal issues that were not easily resolved. As a result the TAG proposed:

Action 1: The World Bank to set up a Working Group to propose guidelines for access and publication. The Working Group would need to consider both the underlying basic heading parities and expenditures that underlie the Global Comparisons but also possible Ring Country data questions.

Action 2: The World Bank to request from all regions information on the current intentions are with regard to access restrictions to regional data as input into the Working Group discussions.

III. Linking the Regions at the Basic Heading Level

Reports were provided by the Global Office on the status of the Ring comparison. At present the Ring list for consumption will be completed in two weeks. It contains about 900 items most of which are available and frequently representative in all the Ring countries. Equipment preparations are also far along as is Construction. However there remain a number of issues in these areas as well as health and housing that remain to be faced at both the Regional and Ring levels. .

Two conclusions on method emerged from this discussion:

- 1) The CPRD approach will be used to produce regional parities at the basic heading level as now outlined in Chapter 11.
- 2) In response to a note by Sergey Sergeev on dealing with the unequal number of price quotes that will be available in each region, the conclusion of the TAG was that this was not a matter of concern in a regression approach. Any attempt to use in a CPRD using average regional item prices would have its own problems in dealing with representative and available items. And in terms of regression

estimation it was concluded that there was value to retaining the variation in prices of items of the different Ring countries within a region.

As part of this discussion and that of the following day it was concluded that the Manual Chapters should be reorganized to have:

- .A chapter on Estimation of basic heading parities in each Region, present Ch. 10.
- A chapter on Aggregation in the Regions. Present Ch 12.
- A chapter on how the Ring Lists were actually developed.
- A chapter on how the Ring parities are to be developed at the BH level, present Chapter 11
- A chapter on Aggregation across the Regions to produce World GDP. Present Ch 13

The TAG expressed the view that the Manuel should aim at being as limited in range as possible while conveying to the users a useful description of the methods and procedures to be used in various aspects of the comparison. The extent to which the parallel work on developing poverty PPPs both by re-weighting the ICP PPPs and by using direct quantity and unit values from expenditure surveys (Deaton, Rao and others) should be a chapter in the manual, stand alone or both was also discussed.

Thursday Oct. 14th

I. Aggregation Methods within Regions

The present Chapters discuss a number of methods including the EKS and GK methods that have been used widely in the past. The discussion was extensive and the decisions for the future will be much better informed after the ICP 2005 is complete. For the present round it was agreed that the *TAG recommends use of EKS as the aggregation method in each Region.*

The TAG concluded that since there was a commitment to EKS in the OECD, and that other promising methods like the weighted CPD (Rao) had not yet been widely tried, it would for this round be advisable to use EKS. In general the TAG concluded that within each Region it was preferable not to use an average price approach such as GK. It was also agreed that the average structure approach developed by Sergeev or the Spanning Tree approach of Robert Hill were as yet too untested to be considered for this round.

There was support for Regions developing alternative aggregations for structural analysis if so desired. For example, the OECD publishes with a lag structural Tables based on GK that are essentially additive, though the form of presentation attempts to make direct comparisons with the EKS results difficult so as to not confuse the average users. The OECD and Eurostat also provide warnings to their users that EKS results for sub aggregates are not additive, and it is recommended that the Regions and the Global Office provide similar caveats in their Tables.

II. Aggregation Methods Across Regions

Several methods were considered by the TAG in some detail. At this stage it was felt that a decision on the way to go would not affect other parts of the work program so that the decision could be put off. This seemed a wise course of action because it was not quite clear on exactly how all the methods would work. However, what emerged from the discussion was an important limitation that the use of fixity in each region imposes on the choice of methods, namely, *any method will in the end be producing a scalar that would be applied to each volume and PPP at all levels of aggregation in all regions, it being unity for the numeraire region.*

In order to inform future discussions of the how to link across regions, several experiments will be carried out on the basis of previous comparisons, such as the OECD exercise that involves linking several groups of countries associated with the EU and OECD either as members or as more limited participants.

III. Numeraire

There was a discussion of the unit of account in which the Global and Regional results should be presented. For example, the results of the OECD are presented at average OECD prices. The unit of account is the US\$ but it does not have the purchasing power of a US\$. The Regions and the Global Office will be publishing relative volumes and parities across groups of countries. The volume comparisons may be in index form as well as in a unit of account. The Global Office will seek information about any existing plans for publication in the Regions.

Friday October 14th

I. Poverty PPPs: Angus Deaton provided a paper that went well beyond Poverty PPPs that had been the subject of his various binary comparisons based on very detailed household expenditure surveys. The paper in particular provided a new approach to estimating errors associated with PPP work. In the example Deaton explored, the source of error was in the household expenditures and future work can also be done to examine errors in the prices.

Associated with the paper was a discussion of the Research Project within the Bank that is coding a large number of household expenditure surveys into the ICP basic heading classification. This will make the type of work that Deaton has carried out much easier in the future and provides a ready made framework for weighting ICP basic heading PPPs using poverty expenditure distributions. Deaton also reported on a new approach he has developed to deal with the simultaneity issue involved in finding the expenditure distribution of those in poverty that itself is not independent of defining the poverty line across countries.

II. Future Business:

The four expenditure areas where TAG deliberations and recommendations are incomplete are Construction, Equipment, Housing Services and Health. In addition, there is the important question of the aggregation method to link the Regions, as well as the need to finish drafting a number of chapters of the Manual. In the next 6 months more information should become available to the TAG to seek closure on these issues.

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