## The Conference Board<sup>®</sup> France Business Cycle Indicators<sup>SM</sup>

## MAY 2006 BENCHMARK REVISIONS

## FRANCE LEADING ECONOMIC INDICATORS AND RELATED COMPOSITE INDEXES

The May 17, 2006 release incorporates benchmark revisions into the composite indexes. The composition of both the coincident (CEI) and leading indexes (LEI) for France have been revised and methodological changes have been made to the LEI effective with this release.

Real imports and retail sales series will no longer be used as components of the CEI. Personal consumption of manufactured goods and wages and salaries (financial and non-financial companies) have been selected as new components for the CEI. In addition, total paid employment (private and government) has been replaced with a broader employment series: number of employees in the private nonagricultural sector. As a result of these changes, the new CEI has a broader coverage of the French economy and better articulated turning points at business cycles.

The composition of the LEI has been changed by omitting four components that had unreliable cyclical timing and excessive volatility. The dropped components are: the bond yields, change in stocks, consumer confidence index, and personal consumption of manufacturing goods. A new component, industry production expectations, diffusion index, was added to the LEI. These changes should help the LEI be a better predictor of future economic activity. In addition, this release also incorporates two major methodological revisions to the LEI for France: 1) a new method for calculating the contribution of the yield spread in the LEI and 2) a trend adjustment to the LEI. The new measure of the yield spread improves the performance of the LEI by better reflecting the way the yield spread anticipates cyclical economic turning points. The trend adjustment facilitates interpretation and use of the LEI.

The new measure of the yield spread, one of the current components of the LEI, uses the same interest rate spread in the calculations. The revision involves a shift from using the yield spread in the LEI to using the cumulative sum of the yield spread. The primary effect of this revision is to change the way the contribution of the yield spread is calculated. With the revision, the contribution of the yield spread will be calculated from the value of the yield spread in a given month instead of its change over the previous month. Currently, the yield spread contributes negatively - i.e., reduces the growth rate of the index - to the LEI whenever the spread is declining and this happens before recessions, but at many other times as well. The new measure will contribute negatively to the LEI only when the spread inverts; that is, when the long rate is less than the short rate. The cumulative measure of the yield spread provides a less "noisy" leading indicator, one that better reflects the effect of the yield spread on future economic activity.

This benchmark revision also institutes an old and well-known trend adjustment procedure to the leading index. This procedure does not affect the cyclical properties of the LEI, but it offers two advantages: 1) The long-term trend in the LEI will be "fixed" as the procedure equates the trend in the LEI to the trend that is measured by the average growth rate in the coincident index (CEI). This means that the trend of the LEI will not vary with changes in the composition of the index or set of indicators used to calculate it. This facilitates the interpretation of the indexes as cyclical measures and provides a more consistent framework for their use. 2) The trend adjustment makes the growth of the leading index more similar to that of the coincident index. In turn, the levels of these indexes are more meaningful since the coincident index is a measure of current economic activity. While the composite indexes are mainly used to indicate directional changes in aggregate economic activity, many users also regard them as measures of the level of economic activity. The trend adjustment facilitates this use.

The benchmark revisions also bring the composite indexes up-to-date with historical data revisions in the components and update the standardization factors used in their calculation. This maintenance procedure, typically done once a year, usually does not change the cyclical properties of the indexes and has, as expected, very small effects.

These changes are the result of research at The Conference Board (TCB) and regular consultations with its Business Cycle Indicators Advisory Panel and other experts. The Conference Board continuously monitors the behavior and performance of the composite indexes and their components and makes changes from time to time. This revision is consistent with long-standing TCB policy to make changes to the indexes when research indicates substantial improvements are possible. Because of these revisions, the composite indexes and their monthly changes are no longer directly comparable with previous releases. Similar methodological changes had been introduced into the US LEI last year and will be incorporated into the LEIs of other countries covered by the TCB's global indicators program.

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