REFLECTIONS ON THE MEANING AND MEASUREMENT OF UNOBSERVED ECONOMIES: AN EDITORIAL COMMENT.

The nature and extent of unrecorded economic activities is an important economic and policy issue for any country, and their measurement is a challenge for academic research. The exchange between Edgar Feige[1][2] and Friedrich Schneider[3] highlights the difficulties facing researchers in this field. These difficulties range from data collection at the micro and macro level, to the choice of econometric techniques, and to the interpretation of the results.

An estimate of a hidden quantity, be it the output of an informal sector or unreported taxable income, is necessarily uncertain, and we cannot expect the level of accuracy in the measurement of the underground economy to be similar to that for the estimate of the formal economy. What we should expect is a well-grounded choice of the methodology and transparency in the description of data analysis, which would allow independent replication and assessment of the validity of the results.

We find Schneider's use of the MIMIC model in the measurement of underground economy unconvincing from a statistical perspective. As pointed out by Trevor Breusch[4], this model is not appropriate for the analysis of macroeconomic data, because the endogenous links across macroeconomic aggregates are inconsistent with the MIMIC assumptions on the correlation structure in the set of variables. However, Schneider has provided a considerable amount of information about the model and how it was applied to the data in his work.

In contrast, Feige's work refers to estimates by the officers of the national statistical agencies (many of which were made available to him in personal correspondence), but does not describe the methods they employed. Here, we were unable to assess the estimates independently, because we have not been provided with sufficient information about the methodology. It is not impossible that the appropriateness of the methodology used by some countries is also questionable.

In rounding up this exchange we would like to express hope that the difficulties will not deter future research in the measurement of underground economy. In this challenging task, as in any empirical analysis, we need both further careful data analysis and transparency about the methods.

Nigar Hashimzade and Chris Heady

---

[1] Feige, E.L. Reflections on the Meaning and Measurement of Unobserved Economies: What do we really know about the "Shadow Economy"? JOTA Vol. 2 No. 1 (2016): Special Issue: The Shadow Economy.
[2] Feige, E.L. Professor Schneider's Shadow Economy (SSE): What do we really know? A Rejoinder. JOTA Vol. 2 No. 2 (2016).
[3] Schneider, F. Comment on Feige's paper 'Reflections on the Meaning and Measurement of Unobserved Economies: What do we really know about the "Shadow Economy"?' JOTA Vol. 2 No. 2 (2016).
[4] Breusch, T. "Estimating the Underground Economy using MIMIC Models." JOTA Vol. 2 No. 1 (2016): Special Issue: The Shadow Economy.