

“Implementation of a New Architecture for the U.S. National Accounts”  
Comments by David J. Stockton

It is a great pleasure to participate in this session on the implementation of a new architecture for the national accounts of the United States. The papers prepared for the session demonstrate the very considerable progress that has been made in laying the groundwork for what Michael Boskin noted might be the most important improvement in the national accounts in at least a generation. I will focus most of my attention on Michael’s excellent paper, and lay out what I believe to be some of the potential key macro policy implications of the new architecture. Along the way, I’ll have a few things to say about the other papers in the session.

The rubric “new architecture” covers a very ambitious program that includes, in addition to the core set of economic and financial accounts, the development of satellite accounts for the environment, health, and non-market activities. These are interesting and important lines of work, but I will confine my comments this afternoon to the core set of economic and financial accounts. That basic architecture was laid out most clearly and completely by Dale Jorgenson and Steve Landefeld in their 2006 Blueprint paper, the essence of which is summarized in their presentation of this session. The principal aim of that effort was to demonstrate the feasibility of producing a more complete, better integrated, and conceptually clearer set of accounts that track economic and financial flows and then integrates those flows into corresponding stocks. Along the way, boundaries for sectors are better defined, and industry inputs and outputs are more fully developed in nominal and real terms.

So why is this enterprise so important, and specifically why are these accounts likely to be important for the conduct of macroeconomic policy. The main reason is that, in

practice, the accounts are the central intellectual organizing device for thinking about and tracking macroeconomic developments. Indeed, the forecast prepared by the staff of the Federal Reserve Board for the FOMC is organized around the production of a reasonably detailed set of expenditure and income accounts as presented in the National Income and Product Accounts. I think its fair to say that we don't forecast at that level of detail because we believe that it helps minimize the root mean squared error of output and inflation—the pillars of our dual mandate. Instead, by organizing our forecast around the accounts, we subject ourselves and the story that we are telling about the economy and its likely evolution to the discipline required by a comprehensive system of accounting. Because we know with probability one that our forecast will be wrong, the texture provided by a forecast of the accounts allows the staff and members of the FOMC to audit the economic stories that lie behind our forecast. Tensions between the forecast and the data are often revealed first in the details of the forecast rather than in the aggregates.

Along side our forecast of the NIPAs, we have for a long time prepared a corresponding and integrated flow-of-funds forecast, which tracks major financial flows in the economy and then integrates those flows into estimates of balance sheets for the household and business sector. In normal times, interest rates and asset prices are nearly sufficient indicators of financial conditions, and financial flows are largely endogenous to the macro forecast. But as recent events have demonstrated, financial quantities can matter for macroeconomic performance. Credit availability and the channels through which credit is being provided or constricted can have important implications for economic activity. In these circumstances, our outlook for financial flows has a sizable influence on our forecast of aggregate activity and the composition of that activity across

sectors of the economy. So at least at some level, we have been attempting to implement the spirit of the new architecture in our forecasting enterprise at the Fed.

That said, I believe that the full implementation of that architecture would force even greater rigor and clarity on that process. One example is provided in the Palumbo-Parker paper—and mentioned in both the Jorgenson-Landefeldt paper and the Boskin paper—and that is the relative contribution of net saving and revaluation to changes in household net worth. As Palumbo and Parker demonstrate, an integrated financial accounting shows clearly the increasing leverage of the household sector and the vulnerability of their balance sheets to the revaluation of their assets. Those consolidated accounts bring the emerging problems in the household sector in to sharper focus.

Let me turn to the Boskin paper specifically. Michael emphasizes the potential contribution of the new architecture to the measurement of longer-term trends in productivity—an effort that receives considerable attention in the paper by Harper and company. Given Michael's experience in the executive branch, he lays out convincingly the important role played by long-term forecasts of productivity and output to fiscal forecasts and planning. Small differences in estimates can have meaningful policy implications for budget forecasting and entitlement projections.

As for monetary policy, Michael correctly notes the importance of accurate estimates of price inflation and potential output to the conduct of policy. One of the major changes in our forecasting apparatus over the past 15 years was the much greater emphasis we now place on the supply-side of our forecast, as changes in structural productivity have become more prominent in driving overall economic developments.

Michael also notes that the conflicting estimates of productivity that can be derived from our current set of accounts can lead to what he calls pejoratively “productivity shopping.” And I will readily admit that political pressures can lead to gravitation towards assumptions most favorable to ones policy position. But let me for a moment sing the praises of those discrepancies in measurement. Obviously, having the truth would be ideal. But in real-time policymaking, the data rarely speak with a single voice. Large differences in measured productivity can arise from differences in output measured from expenditure or income data and differences in labor input measured by the establishment or household surveys. Policymakers need to be confronted with these discrepancies and need to struggle with the possible sources and implications of the tensions presented by the incoming data. Quite frankly, I don’t want the economic accountants, at least in real time, filtering out or disguising those tensions. Policymakers must get a full sense of the uncertainty of the economic environment in which they are making policy.

While I strongly endorse and support the development of a new architecture for our national accounts, I do think it prudent not to oversell what this effort will be able to deliver and to recognize some its limitations. I was a bit uneasy with some of assertions in the papers. For one, I seriously doubt—as asserted by Jorgenson and Landefeld—that better integrated accounts would materially affect our ability to identify asset bubbles. Fundamental asset valuation will remain extremely challenging and rest on many assumptions that lie outside the boundaries of an even improved set of accounts. I doubt, as suggested by Boskin, that a shift in accounting methods will have a significant influence on policy debate surrounding the appropriate role and size of government. And

I don't think that, at least as currently envisioned, the new architecture of the accounts will shed much light in real time on how and where financial risks reside and is allocated in the economy, especially in the face of very rapid financial innovation. Better accounts will certainly help, but the basic conduct of macroeconomic policy will remain fraught with huge uncertainties, engendered by faulty data, misspecified models, and plain old ignorance.

That brings me to the final point that I would like to make. Many of you in this room are keenly aware of the very tight constraints we face in the production and organization of national economic statistics. The resources needed for the adequate development of new architecture for the accounts will need to compete with other high priorities for policymakers. It will come as no surprise that successful conduct of monetary policy requires timely and accurate high-frequency readings on the current state of the economy. Many of those readings are from data that form the building blocks of the accounts. But many do not. We remain committed to the measurement of industrial production, despite some overlap elsewhere in the national accounts because of its importance as a timely high-frequency indicator of economic activity.

Setting priorities in our decentralized statistical system will be difficult. The effort to produce an integrated set of accounts involves several agencies with differing missions and priorities, making the work of implementing the new architecture more challenging than otherwise might be the case. Still, I see considerable benefits in our decentralized system. Most importantly, I think that decentralization encourages innovation. I view both our Industrial Production program and our Flow of Funds accounts as operating like measurement laboratories. And I see similar attributes in many

of our sister agencies. Going forward, we are going to face some very difficult decisions on how to advance the cause improving our national accounts, while simultaneously meeting other important objectives. But I am greatly heartened by the energy, effort, and cooperation that have been evident to date in development of the new architecture. And I am confident that this project will ultimately be successful and be the generational advance that we are all looking for.