Suggested Projects: Presidential Innovation Fellows
17 - Rethinking Federal Data for Economic Growth: Preparing for a Presidential Commission in January 2013

I [suggest a Presidential Innovation Fellow project] to develop plans for a Presidential Commission on Economic Data and Growth to rethink public data systems and achieve a 1%/year sustained increase in GDP growth above the pre-crisis baseline. [Fellows can help the White House staff:] talk with people, help to network ideas, develop options, and identify papers to be developed for a Commission that can begin in January 2013.

The federal government can do better. Government economic data were designed for the slower world of the national manufacturing economy of the 1930s. Quarterly data are estimates and we know, by using the reliable, revised data that become available in 18 months, that the largest single source of error in government forecasting is the (predictable) unreliability of the government's own data that many actors must rely upon. (By contrast to this 18 month delay, our banking system can clear almost all of the transactions of the economy within a few days.) Meanwhile the 21st century world (including the financial sector) moves much faster. Business economists have a large backlog of upgrades in US and foreign data that would help competitiveness. (Re the foreign component: this rethinking and upgrade process, across the G-20, may take several years to implement.) There appears to be a growing psychological component, including international effects. Business may under-invest in R&D.

This is a complex project to discuss in 300 words. I attach a supporting letter from Robert Reischauer (former head of CBO and Chairman of the Board at Harvard). He was an early ally in proposing the rethinking of data systems to improve economic growth. I also enclose a pre-crisis article from the Financial Times indicating the level of professional vexation of international investors with unreliable US government data systems.

Lloyd S. Etheredge
June 5, 2012

THE URBAN INSTITUTE 2100 M STREET, N.W. / WASHINGTON D.C. 20037

ROBERT D. REISCHAUER
President

Direct Dial: 202-261-5400
Fax: 202-223-1335
E-mail: RReischa@ui.urban.org

December 23, 2002

Dr. Lloyd S. Etheredge, Director
Government Learning Project
The Policy Sciences Center, Inc.
P. O. Box 208215
New Haven, CT 06520-8215

Dear Dr. Etheredge:

Thank you for your letter and thoughtful attachment. I am in complete agreement that the economic data we collect has significant deficiencies that limit our ability to understand the economy's problems and chart future policy.

We don't collect some information that is needed and gather much that we could do without. We collect other data in insufficient detail and almost always take too long to release the data for it to be useful in policy decisions.

As you know better than I, there are many reasons for this situation. What we collect and how we collect it reflects the forces at play in the first half of the last century and those forces do not want to give anything up. Congress has little interest in devoting more scarce budget resources to collect new and better information. Few economists who use the data appreciate its limitations. They have been raised on certain data sets and treat them as if they are part of the underlying environment, not subject to change. They put a premium on continuity and don't want discontinuity in the data sets they know and use.

I don't think I would be as critical as you are about CNSTAT/NCR. I don't think they would have much of an impact even if they had done the studies and made the recommendations you think warranted. Nor do I think universities (Yale or Harvard) or the Fed could make much of a dent in the problem. Rather, I think a presidential or congressional study commission is called for—one with a clear mandate and a promise that added resources will be devoted to strengthening the statistical system based on the commission's report. Unfortunately, the prospects for such an initiative rising to the top of policymakers' lists of things to do is very, very low.

Nevertheless, I wish you well in your efforts.

Sincerely,

Sixty-seven ways to guess Gross Domestic Product

by John Kay

[01 November 2005 Financial Times, p. 17]

The private value of predicting official statistics before their release is large but its social utility is zero, which is why procuring it is at once the best paid and most futile form of economic research.

At 8am last Friday, the Bloomberg financial information service carried 67 different predictions of US gross domestic product growth in the third quarter. The median was 3.6 per cent. At 8.30am, the Bureau of Economic Analysis issued its official estimate of 3.8 per cent. This modest difference was well received by the market: the Dow Jones index rose immediately by 50 points and was up 170 points – almost 2 per cent – on the day.

As the figure was announced there were cheers in some dealing rooms, commiserations in others. Wall Street economists who get these numbers right earn large bonuses: those who miss the mark soon miss their salary cheques as well.

Although these 67 figures are described as estimates of GDP growth, none of the 67 houses had really made an independent assessment of trends in American national income. The figures compiled by the BEA are based on extensive data collection using the legal powers, moral authority and financial resources of the US government under assurances of confidentiality. Such an exercise could not easily be replicated by any research firm or investment bank and is not.

Moreover, if anyone did try to measure GDP independently of the federal government, it is likely that they would come up with a substantially different answer. The official statistics are based on samples, cover only a fraction of economic activity and are open to considerable revision. The BEA's own assessment is that this figure will be revised by up to 1-2 per cent on two-thirds of occasions. It is therefore more likely than not that the number – itself still an estimate – will be outside the range of between 3 per cent and 4 per cent which included almost all analysts' judgments and the BEA's own provisional figure. If an infinitely knowledgeable analyst actually established the correct answer, his prediction would probably be off the chart: not just in this quarter, but every quarter. He would soon lose his job.

How is it that all estimates are so close together when the underlying uncertainties are so large? The 67 teams of analysts are not trying to guess what actually happened to American national income in the third quarter. The traders who use their figures do not want an estimate of what is really going on: they want an estimate of what the BEA will announce. And so the economists who service them are trying to guess the number in the press release. Their main source is other statistics that the BEA has already issued. That is why their judgments, although not necessarily right about the economy, are close to the actual BEA figure. Their analysis is also influenced by the numbers posted by the other 66 analysts. It is dangerous to be right, but safe to be conventional.

The lazy equity analyst focuses on trying to anticipate quarterly earnings announcements, forming a symbiotic relationship with company finance officers and investor relations people who are trying to massage market expectations. A better observer can sometimes add value by penetrating corporate public relations and obtaining his or her own information.

But the BEA is trying to find the truth and is better placed to do so than any Wall Street economist. The bureau is not concerned to please the market and, unlike companies, is serious about confidentiality. Financial economists might as well be lazy since they have little to add to the work of the bureau. Correctly predicting the official estimate 30 minutes before its release may be profitable but contributes nothing to our understanding of the economy. The private value of such information is large but its social utility is zero, which is why procuring it is at once the best-paid and most futile form of economic research.

Keynes likened professional investment to a beauty contest, in which “it is not a case of choosing those which are really the prettiest, nor even those which average opinion genuinely thinks the prettiest. We have reached the third degree where we devote our intelligence to anticipating what average opinion expects the average opinion to be”. And it is so, to the power of 67.