

Modernisation of the UK's National Accounts: progress and plans for *Blue Book* and *Pink Book* 2008

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Introduction and summary

The Office for National Statistics described its plans for “Modernising the UK’s National Accounts” (MUKNA) in February 2007. MUKNA outlined the plans for both the 2007 and 2008 editions of the *Blue Book*, highlighting the improvements that users would see over time. This article reports on progress and details the scope of *Blue Book* 2008 (BB08) and *Pink Book* 2008 (PB08).

Blue Book 2008 will introduce the first phase of modernisation that will deliver incremental improvements over the next three to four years. Introduction of both new methods and new IT systems at the same time has proved too challenging to meet the original plan of implementation in BB08. Instead, it is now intended to phase the introduction of new methods and systems over a number of years. The first phase in BB08 will use the new systems to update the approach used in BB06 to balance annual gross domestic product (GDP) in current prices. This will allow the resumption of benchmarking to annual surveys, which was suspended in BB07. BB08 will also see the introduction of a new and improved method for measuring banking output (FISIM); this will improve understanding of the impact of this important sector on the economy. BB08 will therefore represent a considerable step forward in quality from BB07 and provides a stepping stone towards full modernisation of the National Accounts, including annual balancing in volume terms as well as quarterly balancing, in the coming years. In *Pink Book* 2008 the analyses suspended in 2007 will be re-introduced, and a number of methodological improvements implemented.

Background: modernisation of the UK's National Accounts

The Office for National Statistics (ONS) is engaged in a modernisation of the UK National Accounts. The scope of the changes were described in ‘Modernising the UK National Accounts’ (MUKNA), first published in February 2007 and reproduced in the April 2007 edition of *Economic & Labour Market Review* (ELMR). The article described a number of improvements for both producers and users of the National Accounts:

- new and more efficient computer systems
- a more coherent picture of the economy by extending the framework for balancing income, expenditure and output
- expanded coverage of the services sector
- early estimates of GDP less prone to revision
- standardisation of methods, systems and processes

- product information balanced through supply and use tables (SUT) at constant prices (volume estimates) as well as current prices
- quarterly data to be balanced at detailed component level

MUKNA also explained ONS plans to restrict the scope of the BB07 exercise to free resources to work on the implementation of modernisation in the 2008 edition. The scope of the ‘transitional’ *Blue Book* in 2007 was reduced in a number of ways:

- supply-use balancing was postponed
- the take-on of annual benchmarks, including those from the Annual Business Inquiry and HM Revenue & Customs was greatly restricted
- a number of methodological improvements were suspended, including the new approach for estimating the service earned from the provision of financial intermediation services
- a base year of 2003 continued to be used for recent volume estimates, with industry weights also remaining at those derived from the 2003 balance

The main impact of postponing annual benchmarking was additional uncertainty about the path of the economy, in particular from 2004, the last year GDP was fully balanced. While both the Bank of England and HM Treasury considered the consequences for economic policy of the reduced scope *Blue Book 2007* to be manageable, ONS committed to monitor the quality of the subsequent quarterly national accounts outputs.

Quality of latest estimates

In ‘Monitoring the quality of the National Accounts’ (Meader and Tily 2008), ONS put forward an extended framework for monitoring the quality of the quarterly National Accounts. The article analysed the quality of the National Accounts, and in particular GDP, in terms of accuracy and coherence of the published data sets. Accuracy, or reliability, was primarily assessed by an extension of the regular revisions analyses. Coherence covered an analysis of published and unpublished adjustments made to GDP components to bring the three measures of GDP into line, together with an analysis of the coherence between GDP and both internal ONS and external indicators.

While the article primarily provided a benchmark for future quality assessments, it also suggested that there was no obvious change in quality from the indicators studied. It was noted that revisions were expected to be larger than usual when balancing and benchmarking were reintroduced.

Additionally, ONS has introduced a ‘coherence statement’ in the Quarterly National Accounts release from March 2008. This provides users with an assessment of the coherence of the three measures of GDP in each quarterly publication.

Progress

Modernisation has not progressed as fast as had been hoped at the time MUKNA was published in early 2007. This has required a re-evaluation of what is feasible for BB08, taking account the priorities of key users.

Delays to system-build and system performance problems led to the conclusion that depending fully on modernised systems for the delivery of quarterly and annual national accounts data sets from the publication on BB08 was high risk. To minimise this risk, it was decided to use the new systems to set the level of annual current price GDP, but continue to use existing systems for quarterly estimates and dissemination. It was also decided to limit annual balancing in BB08 to current prices only, rather than expanding the scope to include balancing in volume terms. Balancing in volume terms in BB08 would have required significant analytical resources and it was clear this could not be managed alongside the prime objective of using new systems for current price SUT (CP-SUT) balancing. Volume balancing will continue as a development project for implementation in the future.

The plans for BB08 are described in more detail below, but in short the aim is to:

- update the current price balancing approach used in BB06 making use of the new SUT systems to reconcile and balance the three measures of GDP for 2004, 2005 and 2006. This will allow consistency with the balances for 2003 and earlier to be maintained
- incorporate annual benchmark data for 2004, 2005 and 2006
- provide a platform for introduction of new methods in BB09 and beyond
- implement the new approach for measuring financial intermediation services indirectly measured (FISIM)

The intention is to deliver the range of improvements envisaged in MUKNA over a period of years rather than as a single ‘big bang’ in BB08. This phased approach will permit clearer understanding and better explanation of changes in each *Blue Book* round.

Plans for *Blue Book* 2008

The proposal for BB08 allows the use of modernised SUT systems to take on annual benchmark data, together with SUT balancing to determine the level of GDP in current prices in each of 2004, 2005 and 2006. Apart from the delay to constant price balancing, the main difference with earlier plans for full-SUT balancing is that balancing will be conducted at a higher level of aggregation than envisaged in MUKNA, though similar to that used in BB06 (the principle benefit of the expanded detail was to be the compilation of SUT at constant prices). A quality assessment of the balance will be published alongside the final dataset.

In a little more detail, the scope of BB08 includes:

- reworked CP-SUT balance for 2004 and preliminary ‘balances’ for both 2005 and 2006. The table below summarises years balanced in recent *Blue Book* rounds

	Years balanced BB06 to BB08			
	2003	2004	2005	2006
BB06	√	√		
BB07 ¹	√	√	X	
BB08	√	√	√	√

1. In BB07, balances for 2003 and 2004 were carried forward from the CP-SUT exercise in BB06.

- the CP-SUT approach will allow the inclusion of annual benchmarks from HM Revenue & Customs, together with annual results from the International Trade in Services and other ONS inquiries
- it allows publication of all *Blue Book* tables, including those industry tables suspended in BB07. The full *UK Input-Output Analyses* that were last published in 2006 will not be released; however, it is planned to publish the new balanced SUT tables in spreadsheet form at the level at which balancing is conducted
- as noted above, while the new expanded framework will be populated with more detailed data, balancing will be conducted at a more aggregate level. This also means that the expansion in the services industries envisaged at the time of MUKNA will not be available for BB08
- detailed SUT-balanced results may not be taken back into the detailed GDP breakdowns for all components (although higher level aggregates would be consistent). It is not yet clear where these inconsistencies may occur, but one possible example would be the detailed SUT product and industry breakdowns for gross fixed capital formation which may not be fully consistent with the detailed asset breakdowns published within ‘Business Investment’
- GDP will be revised to include allocated FISIM. This is a major methodological improvement and one that has been postponed from the last two *Blue Book* exercises (see below for more detail)

In summary, BB08 will be the first stage in the modernisation of the National Accounts. This first stage will use new systems to update the approach taken in BB06 to balance the three approaches to GDP in current prices. While progress has not been as fast as had been hoped, this still represents a considerable step forward from BB07, when SUT balancing was suspended.

The main *Blue Book* and *Pink Book* estimates will be published as usual in the Quarterly National Accounts and Balance of Payments First Release, on 30 September. The electronic versions will be released on 24 October and the hard copies of both publications will be released on 21 November.

Base year

The base year will remain at 2003=100, although industry weights will be updated to reflect the new FISIM breakdowns and the own-account software revision that was introduced in BB07. The decision not to move forward from 2003=100 weights is partly due to the resources required to move forward to 2004 or 2005=100, but also because of the uncertainty around the industry weights that will emerge from the new re-engineered systems and processes. Updating the

existing weights to include FISIM and own-account software will ensure that the major changes are included.

FISIM

This year's *Blue Book* will introduce a new approach for the treatment of financial intermediation services indirectly measured (FISIM) in the UK National Accounts. This is a significant change to the accounts that has been taken back to 1961, bringing the UK National Accounts into line with the approach laid out under Regulation by the European Commission. See Tily and Jenkinson (2006) and Akritidis (2007) for a fuller description of the new methodology.

FISIM represents the service charge provided by financial institutions paid for by the interest differential between borrowing and lending, rather than fees and commissions. The banking industry relies heavily on revenues accruing from interest flows, but according to standard national accounting rules, earnings from interest are not part of a corporation's output, value added or gross operating surplus and therefore do not contribute to economic growth. The concept of FISIM was developed as part of the update of the System of National Accounts (1993) and the European System of National and Regional Accounts (ESA95) to provide a standard approach for measuring both the supply and use of FISIM services. Experimental FISIM estimates (current price) have been published quarterly since March 2007.

The recommended approach is to identify the purchase of FISIM services explicitly and to classify them as intermediate consumption, final consumption expenditure or exports, according to which sector incurs the expenditure (SNA93, Annex iii, paragraph 5). Payments of FISIM by financial intermediaries (interbank lending) are regarded as representing intermediate consumption. The UK currently assumes all FISIM to be consumed by corporations, rather than allocating some consumption to final consumers. This new approach to estimate FISIM increases final consumption and therefore GDP in all years since 1961. On average, the level of GDP is around 1.5 per cent higher in current price terms from previously published estimates; although the effects on annual growth rates are small.

Plans for Pink Book 2008

As with the *Blue Book* in 2007, the scope of the *UK Balance of Payments Pink Book* (PB) was reduced in a number of ways:

- the accompanying analytical text and charts were suspended
- the geographical chapter 10 was withdrawn as a result of the suspension of the tables showing the UK's International Investment Position (IIP)

As stated in the preface to PB07, the intention was to reintroduce the text, charts and geographical analysis of the UK's IIP in the 2008 edition of the PB. That is still the plan.

The 2008 edition of the *Pink Book* will also see the incorporation of a number of methodological improvements. These include:

- the inclusion of exports and imports of FISIM within Trade in Services (consistent with BB08) with an equal and offsetting revision to investment income
- the identification and inclusion of UK banks' imputed dividend payments
- a reassessment of the levels of portfolio investment abroad by UK securities dealers
- a reassessment of the level of UK shares held by non-residents
- the removal of some double counting of UK securities dealers deposits with, and loans from, banks abroad

Current price estimates for trade in services will also be subject to revision as part of the reinstated annual SUT balancing process.

Plans beyond BB08

This is the first stage in the modernisation of the UK National Accounts outlined in MUKNA. In BB09 the priority will be to expand the dimensions of the supply-use table and to extend the number of years for which the tables are compiled. The move to quarterly balancing will follow the successful incorporation of annual constant price balancing. In the meantime, the established process for completion of quarterly and annual rounds will continue.

These advances will be dependent on a considerable improvement in systems performance and this is being reviewed. It is expected that the findings of this review will, in part, determine plans for future *Blue Book* rounds. Plans for both BB09 and future *Blue Books* will be outlined in future articles in *ELMR*.

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