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Foreword

The study of finance and capital markets was a comparatively late starter among the fields that occupied the National Bureau over its first fifty years. However, as John Lintner's careful and thorough survey shows, the Bureau's studies in these areas, beginning in the late 1930's with the assistance of a series of exploratory committees, provided a wide variety of new knowledge where information had been extremely scarce. The Bureau's contribution was of two types. One was the establishment of comprehensive frameworks of accounts which were intended to be of service in studying many different questions about the whole economy or the interrelationships among sectors. Each of these studies (for example, those of the flow of funds, the stock of tangible wealth, and national and sectoral balance sheets) not only collected or organized a wide variety of data but also weighed conceptual problems and established a set of methods for later use, by the Bureau or by others such as government agencies who carried on the effort. These studies were in the tradition of the earlier work on the concepts and measurement of national income, which had gone so far in establishing the Bureau's role and reputation. The second type of study, especially those that were part of the Financial Research Program, consisted of the detailed examination of particular financial instruments and institutions, filling gaps in information and replacing casual impressions with quantitative knowledge.

An institution such as the National Bureau, whose mission is a public one, must regularly reexamine its research priorities. Some of the basic research projects which Lintner describes as the chief ornaments of the Bureau's contribution to the study of finance must have seemed distressingly long-range in their objectives, considered against the background of the urgent current problems of the 1930's, 1940's, and 1950's, when they were inaugurated. Yet, as Lintner reviews this record, it seems evident that some of the immediately least relevant projects have since had the widest benefits. These benefits have come not only from the particular publications but from the stimulus to others, in the National Bureau as well as outside, in government and other research organizations. And the stimulus has spread in widening circles to produce im-

provements both in data and in theoretical analysis, even though the original theoretical bases for some of the work, as Lintner points out, now seem primitive or have been superseded by later efforts.

That record of achievement has usually influenced the Bureau's choice of studies in favor of basic research, often involving the collection or organization of large quantities of new data. In looking toward the future, however, Lintner and the discussants of his paper seem to agree on the desirability of some redirection of effort away from the major data gathering programs, which have been a large part of the Bureau's research program in finance. They urge greater attention to analytical studies of financial markets, using theoretical developments which have occurred since the time most of the Bureau's research in this area was done.

It is a pleasure to be able to report that, as if in anticipation of the recommendations, some progress has already been made in at least two of the areas suggested for future study. One of these is the disaggregation of the residual or household sector in balance sheet and flow-of-funds accounts and another is the examination of the effect of inflation on financial markets.

On the first question, a small step was taken with the National Bureau's report to the Securities and Exchange Commission on institutional investment and the market for corporate stock, the latest publication relating to the Bureau's financial research.¹ In this report, a revised version of which will soon be published by the National Bureau, balance sheets for foundations and for colleges and universities are estimated and removed from the residual or household sector, and asset holdings of households are disaggregated by the age and wealth of the holder. As is frequently the case, the reexamination of existing data produced revisions that appeared to contradict some widely held beliefs, such as the assumption that the household sector's share in stock had been declining sharply throughout the years since World War II; it also suggested some questions for further study, such as those arising from the apparent finding that households' performance in the stock market was, in terms of capital gains, at least as good as, and probably better than, that of institutions.

¹ *Institutional Investors and Corporate Stock: A Background Study*, Institutional Investor Study Report of the Securities and Exchange Commission, Supplementary Volume I, Washington, D.C., U.S. Government Printing Office, March 10, 1971.

The second item of progress on the suggestions made at the meeting is the start, in 1971, of a major project on the effect of inflation on financial markets under a grant from the Life Insurance Association of America, the source of financing for so much of the research reviewed by Lintner. The project includes several studies. Lintner and John Piper, partly through interviews with portfolio managers to obtain information not publicly available, will examine changes in the investment policies and portfolios of several important types of financial institutions in response to inflation. Among the objects will be to ascertain the importance of new techniques, such as equity kickers, adopted by financial institutions to protect their assets against inflation.

Another study in this group, by Thomas Sargent, will attempt to measure the relations between price level changes and prices and yields on bonds and common stocks, using the experience of several different countries and periods. A third, by Stanley Diller, will study bonds convertible into common stock, considering them as one of the devices used for hedging against inflation. A comparison between yields on convertible bonds and yields on nonconvertible bonds with similar characteristics can be interpreted as a measure of expected changes in equity prices. Lester Taylor, in another of these studies, will look into the way in which households alter the distribution of their investments in response to inflation and expectations of inflation. In addition to these studies, some attention will also be directed to building up a historical record of stock price movements during inflationary periods in as wide a variety of countries and situations as possible.

The National Bureau, thanks to the participants in the colloquium, now has a large number of thoughtful recommendations for future research in finance and capital markets. We are grateful to John Lintner, to the chairman, Robert V. Roosa, the formal discussants, William J. Baumol, Sidney Homer, and James J. O'Leary, and to the Hon. Richard B. Smith, who addressed the dinner meeting, as well as all the participants in the informal discussion for their suggestions and guidance.

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