

Structural Change in Production Networks and Economic Growth*

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Abstract: We study structural change in production networks for intermediate inputs (input-output network) and new capital (investment network). For each network, we document that the share of output produced by services (relative to goods) is rising over time. While the relative prices of services that produce intermediates and consumption are rising, we find that the relative price of services that produce investment is falling over time. We then develop a multi-sector growth model to study these trends and their implications for economic growth. To match the relative price trends, inputs to intermediates production are complements and inputs to investment production are substitutes. Hence, structural change endogenously reallocates resources to the slowest growing intermediates producers and the fastest growing investment producers. Growth accounting exercises reveal that investment-specific technical change accounts for an increasing share of U.S. aggregate growth, with 20% of aggregate growth since 2000 due to investment structural change. Growth projections from our model show that structural change within investment networks alone can offset stagnating or declining growth in other sectors due to Baumol's cost disease.

JEL: E23, O14, O40, O41

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1. Introduction

Production networks—the distribution of transactions between sectors that produce and purchase commodities used in production—play a central role in shaping economic fluctuations and growth.¹ However, with changes in technology and the organization of production, these networks evolve over time. This paper documents structural change in the production networks for investment and intermediates and shows how these changes influence economic growth.

Our analysis proceeds in three steps. First, we document a rising share of output produced by services (e.g., financial services, professional/technical services) relative to goods (e.g., manufacturing, construction) within both the intermediates and investment network and then construct separate price series for intermediates and investment (and consumption) produced by goods and services sectors. Second, we develop a multi-sector model with production networks for intermediate inputs and investment to understand the relationship between structural change and economic growth. Finally, we solve a transition path of the model, calibrated to match observed patterns of structural change, and analyze the importance of structural change for postwar U.S. growth and projected future growth in GDP per worker.

The main contributions of our paper follow from our measurement of goods and services prices for different uses of output—consumption, investment, and intermediates. While the price of services relative to goods used as consumption (e.g., education and health care) and intermediate inputs (e.g., financial services and wholesale trade) are continually rising, the relative price of services used as investment (e.g., software development and R&D) is actually falling. Within our calibrated model, our finding of opposing price trends in intermediates and investment networks implies that goods and services are substitutes in investment and complements in intermediates and consumption. Thus, structural change in the investment network means that expenditures reallocate toward the producers with the fastest total factor productivity (TFP) growth, endogenously increasing economic growth—the “frontiers” of growth. Likewise, complementarity between goods and services in intermediates (and consumption) slows growth as structural change reallocates

¹Among many possible examples, see [Acemoglu, Carvalho, Ozdaglar and Tahbaz-Salehi \(2012\)](#), [Baqaei and Farhi \(2019\)](#), [Foerster, Hornstein, Sarte and Watson \(2022\)](#), [vom Lehn and Winberry \(2022\)](#), and [Kopytov, Mishra, Nimark and Taschereau-Dumouchel \(2023\)](#).

expenditures to producers with the slowest TFP growth—the “bottlenecks” of growth. As a consequence, the net impact on aggregate growth is a quantitative question. Projections generated from our calibrated model suggest that continuing structural change in the investment network is likely sufficient to offset concerns about declining growth due to [Baumol’s \(1967\)](#) cost disease.

The first step of our analysis uses national accounting data to document changes in the producers of intermediates and investment. We find that goods sectors systematically produce a smaller share of output in each production network over time, offset by increased production by service sectors. However, the specific goods and services sectors in which production is rising and falling vary by network. These changes are large, similar in magnitude to structural change observed in consumption expenditures, and widespread, occurring in nearly all sectors and in many countries.

Given that the goods and services sectors producing consumption, investment, and intermediates are distinct, we measure the price of goods and services separately for each of these final uses. To do so, we leverage expenditure-side national accounting data, mapping prices from the Bureau of Economic Analysis’ (BEA) final expenditure data on 68 consumption and 30 investment commodities in the National Income and Product Accounts (NIPA) to the goods or services sectors that produce these commodities. For intermediates, which aren’t included in GDP and are therefore not in NIPA expenditure data, we infer prices as residuals from the BEA’s sectoral gross output prices, which are a weighted average of consumption, investment, and intermediates prices. Not only is this approach internally consistent with published aggregated price data, it also produces intermediates price series that align almost perfectly with the producer price indices (PPI) published by the U.S. Bureau of Labor Statistics (BLS) for the select years that they are available.

This measurement approach yields distinct relative price patterns for goods and services across consumption, investment, and intermediates. Recent work allowing for structural change in investment (e.g., [Herrendorf, Rogerson and Valentinyi, 2021](#); [García-Santana, Pijoan-Mas and Villacorta, 2021](#); [Sposi, Yi and Zhang, 2021](#)) measures a single price for goods and services across uses and finds that the price of services has been rising faster than that of goods. We find a similar result for consumption and intermediates, but the opposite result for investment, with the price of services declining relative to goods. The key to our result is aggregation bias in the sectoral gross output prices typically used to measure goods and services prices. Since only around 5% of

services output is used for investment, the price of investment produced by services sectors is not accurately represented in the aggregate price index for the services sector as a whole. We show that this aggregation bias persists even when using more disaggregated sectoral output prices.

In the second step of our analysis, we extend the multi-sector neoclassical growth model to allow for production networks in intermediates and investment to analyze how these patterns in relative expenditures and prices impact aggregate growth. In our model, each sector produces gross output using a combination of capital, labor, and intermediate inputs. Production networks are modeled as each sector's intermediates and investment being a constant elasticity of substitution (CES) bundle of inputs, purchased from many different sectors. This setup implies that changes in relative prices across sectors, induced by changes in technology, can generate changes in the composition of intermediates and investment production—i.e., structural change in production networks. To highlight the implications of structural change for growth, we consider a special case of the model that admits a balanced growth path. We show that the higher the elasticity of substitution, the faster growth will be in either network and that the composition of aggregate growth endogenously shifts towards the network with the higher elasticity of substitution.

Finally, informed by recent work on stable transformation paths by [Buera, Kaboski, Mestieri and O'Connor \(2024\)](#), we solve a calibrated transition path of our model to study the quantitative implications of structural change in production networks. We consider counterfactual exercises where we vary which TFP series are fed into the model and/or the values for the elasticities of substitution. Our baseline calibration studies six sectors, with each of the consumption, investment, and intermediates sectors split into a goods and services subsector—a natural extension of [Greenwood, Hercowitz and Krusell \(1997\)](#) and [Ngai and Samaniego \(2009\)](#). We calibrate the elasticities of substitution in the model to obtain the best fit to observed patterns in expenditure shares and relative prices. Our calibration implies that goods and services are complements within consumption and intermediates, but substitutes within investment.

We consider two types of counterfactual exercises: historical counterfactuals that decompose the sources of U.S. growth in GDP per worker from 1947-2020 and growth projections for future decades assuming constant sectoral TFP growth. Consistent with the model's theoretical implications, TFP growth of investment producers is increasingly important over time, with its contribution

to aggregate growth rising from 43% during 1960–1980 to 94% since 2000. Furthermore, roughly 20% of aggregate growth since 2000 is driven by structural change in the investment network alone. In contrast, we find that intermediates-specific technical change has stagnated, contributing negatively to growth after 2000, and hence plays a large role in the recent growth slowdown. To analyze fears of slowing long-run growth due to structural change and Baumol’s cost disease, we use the model to project future growth. Despite recent sluggish growth, our projections do not imply a further slowdown. If anything, our model predicts mild acceleration, as structural change within the investment network is sufficient to offset the drag of Baumol’s cost disease caused by structural change in consumption and intermediates.

Related Literature Our paper connects two large strands of literature: the study of production networks as propagation mechanisms for economic fluctuations and growth, and the study of long-run structural transformation from goods to services. The production networks literature primarily emphasizes the role of static production networks in shaping fluctuations. The literature on structural change typically focuses on multi-sector models that either abstract from production networks (or treat them implicitly in a “value added” specification) or do not allow these networks to change over time.² Our contribution lies in studying the intersection of these two phenomena.

Several studies have explored how production networks shape long-run growth (e.g., [Ngai and Samaniego, 2009](#); [Moro, 2015](#); [Valentinyi, 2021](#); [Foerster et al., 2022](#)). Particularly relevant is [Ngai and Samaniego \(2009\)](#), who examine how technological change in intermediate goods sectors affects the composition of growth through investment-specific technological change (as in [Greenwood et al., 1997](#)). Similarly, [Foerster et al. \(2022\)](#) investigate how production networks, especially the investment network, influence which sectors’ TFP growth accounts for aggregate growth slowdowns. Our approach extends these insights by analyzing growth patterns across sectors defined both by their product market and the use of those products, and allowing production

²For example, [Herrendorf, Rogerson and Valentinyi \(2013\)](#) introduce value-added measures of structural change that implicitly embed indirect contributions to final production occurring via the input-output network. Absent using this approach, [Herrendorf et al. \(2013\)](#) and [Herrendorf, Rogerson and Valentinyi \(2014\)](#) argue that using expenditure-side prices to calibrate models of structural change is only appropriate when the model accounts for the input-output structure of the economy. We take this alternate approach in this paper. Beyond our new result on the substitutability between goods and services in investment, explicitly modeling the input-output network is important, as we document that structural change in the network of intermediates production accounts for nearly half of the measured structural change in value-added based consumption and investment.

networks to change endogenously, which introduces the possibility of Baumol’s cost disease.

Our work also builds on the literature that disaggregates the services sector in different ways (Buera and Kaboski, 2012; Duarte and Restuccia, 2020; Eckert et al., 2019; Buera, Kaboski, Rogerson and Vizcaino, 2022; Duernecker, Herrendorf and Valentinyi, 2024). Our approach distinguishes services subsectors by the use of their products (consumption, investment, intermediates) and emphasizes the elasticity of substitution between goods and services in producing each final use. Since these sectors aren’t directly identifiable using standard classifications, we use expenditure-side data to measure prices and productivity, similar to the measurement of investment-specific technical change in Greenwood et al. (1997).

Finally, our work relates to recent literature that has observed and begun to analyze structural change in production networks. Early work by Berlingieri (2013) and Galesi and Rachedi (2018) provides some evidence that services sectors have been rising in importance for intermediates production, and more recent work by Sposi (2019) and Sposi et al. (2021) has incorporated intermediates structural change to their models to explain the hump-shaped rise and fall of manufacturing and the global distribution of manufacturing. Most closely related to our work, Herrendorf et al. (2021) and García-Santana et al. (2021) extend structural change models to incorporate structural change in investment. Our work builds on these analyses by providing an explicit quantitative analysis of structural change in intermediates and allowing for heterogeneous prices of goods and services by use, allowing us to discover the substitutability of goods and services inputs in investment.

2. Structural Change in Production Networks

We focus on structural change within two production networks: the input-output network (the sectoral distribution over the production and purchases of intermediate inputs) and the investment network (the distribution over the production and purchases of new capital). The primary data sources for measuring these production networks in the U.S. are the Make and Use Tables from the U.S. Bureau of Economic Analysis’ (BEA) Input Output Database. These tables contain data for each sector on the value of gross output, value-added, intermediate input purchases (from every sector), and final uses (consumption, investment, etc.) of each sector’s production. The database

begins in 1947, and we study patterns of change through 2020.³ For measuring the investment network, we also use data from [vom Lehn and Winberry \(2022\)](#), who combine BEA Input Output data with BEA Fixed Assets tables to construct a time series of the investment network that covers a similar time frame and level of sector detail; we extend their data to run through 2020. Additional details regarding data sources and measurement are available in [Appendix A](#).

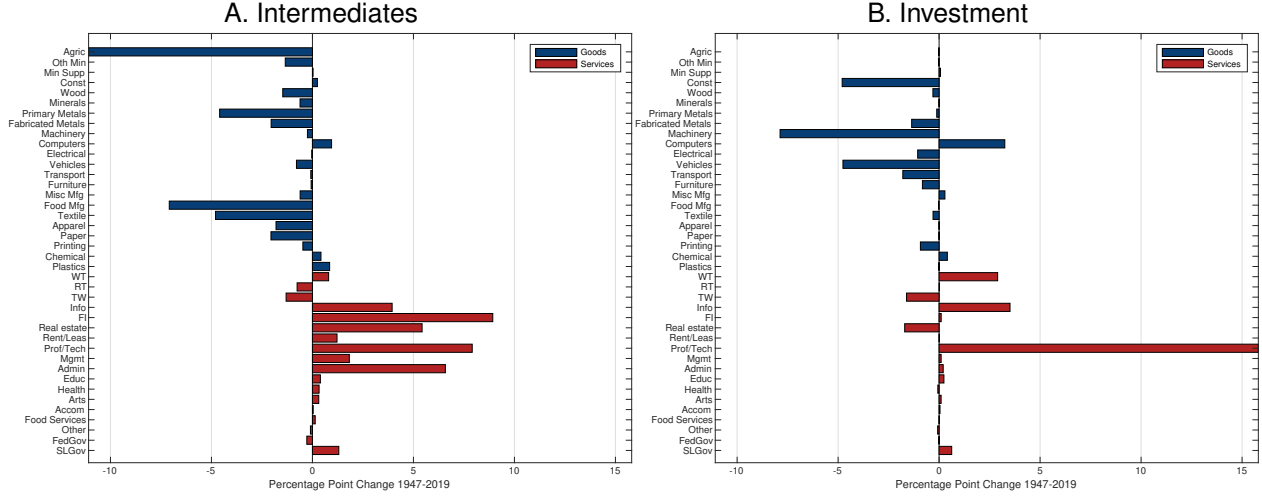
These sources allow us to compile a dataset that provides consistent coverage of U.S. production networks for 40 NAICS-defined sectors, including agriculture and government.⁴ In our main analyses, we define “goods” sectors as all agriculture, mining, construction, and manufacturing sectors (22 in total) and “services” as all remaining sectors (18 in total). We exclude three energy-intensive sectors—oil and gas extraction, utilities, and petroleum and coal manufacturing—because of their distinct role in producing energy and because of short- and long-run volatility in energy markets. However, as we show in [Appendix B](#), these sectors play no role in structural change in production networks. Since price growth in these sectors can be so large as to overshadow price growth in other producers of intermediate inputs, we exclude them from our analysis.

The two production networks are defined as a pair of matrices for each year t , where element (i, j) of each matrix reports expenditures by sector j on intermediates or investment produced by sector i in year t . As we show in [Appendix A](#), these networks are generally sparse; for any given sector, the majority of investment and intermediates are purchased from a small set of sectors. The distribution of investment producers is fairly similar across sectors, as most sectors purchase investment goods from a collection of prominent investment hubs—construction (structures), machinery and motor vehicles manufacturing (equipment), and information and professional and technical services (intellectual property). However, there is much more sector-specificity as to which sectors are important suppliers of intermediates. In particular, the input-output network features signifi-

³These data include imported intermediates, consumption, and investment, reflecting the full set of intermediate and investment purchases by each sector, regardless of geographic origin. Because the BEA only reports total spending on imports and doesn’t differentiate how these imports are used, we cannot remove imports from the data within our measurement framework. That said, throughout the period 1947-2020, imports are never more than 8% of total consumption, intermediates, and investment in any given year, so changes in imports cannot account for the quantitatively large aggregate patterns of structural change we document below.

⁴Table [A.1](#) in [Appendix B](#) lists each of the 40 sectors and their corresponding NAICS codes. More recent vintages of the Input Output database have greater sectoral detail, but given our interest in structural change over the long run, we focus on these 40 sectors, which can be observed throughout the period 1947-2020.

Figure 1: Changes in Production Share of Intermediates and Investment: 1947-2019



Notes: Each bar represents the change in the share of intermediates (panel A) or investment (panel B) produced by each sector between 1947 and 2019. Blue bars: goods sectors; red bars: services sectors.

cant homophily—goods sectors play a large role as intermediates suppliers for goods sectors and services sectors play a large role as intermediates suppliers for services sectors.

To measure structural change in these production networks, we analyze changes in the fraction of aggregate intermediates or investment spending on output produced by sector i . For any given sector j , we define the share of intermediates and investment purchased from sector i as s_{ijt}^M and s_{ijt}^X , respectively.⁵ The share of aggregate intermediates or investment produced by sector i , s_{it}^M and s_{it}^X , respectively, can be expressed as a weighted average of the within-sector shares, s_{ijt}^M and s_{ijt}^X :

$$s_{it}^M = \sum_j \frac{P_{jt}^M M_{jt}}{\sum_k P_{kt}^M M_{kt}} s_{ijt}^M \quad \text{and} \quad s_{it}^X = \sum_j \frac{P_{jt}^X X_{jt}}{\sum_k P_{kt}^X X_{kt}} s_{ijt}^X, \quad (1)$$

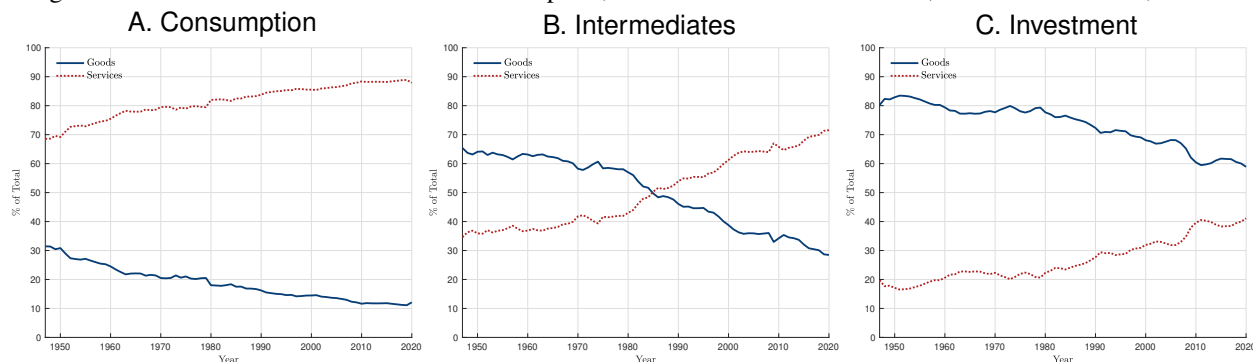
where $P_{jt}^M M_{jt} \equiv \sum_i P_{it} M_{ijt}$ is the total spending on intermediates by sector j (expressions for investment are defined analogously). Changes in s_{it}^M and s_{it}^X reflect both changes within sectors and changes in the composition of spending between sectors.

Figure 1 plots long differences in s_{it}^M and s_{it}^X for each sector i from 1947 to 2019.⁶ Changes

⁵Formally, $s_{ijt}^M = \frac{P_{it} M_{ijt}}{\sum_l P_{lt} M_{ljt}}$, where P_{it} represents the price of sector i 's intermediates at time t and M_{ijt} represents the quantity of intermediate inputs purchased from sector i by sector j , with an analogous expression for investment. We use information on total payments from sector j to sector i in year t , $P_{it} M_{ijt}$, as price and quantity are not separately observed in the network data; this notation allows for easy comparison to our model.

⁶We end in 2019 to avoid any unusual endpoint effects with the onset of the COVID-19 pandemic.

Figure 2: Trends in Production Share of Consumption, Intermediates and Investment, Goods vs. Services, 1947-2020



Notes: The figures plot the fraction of total spending on consumption, intermediates and investment produced by the goods sector (blue, solid line) and the services sector (red, dotted line). Sectors included in goods and services can be seen in Table A.1.

in these production networks are broadly characterized by a shift from goods sectors (blue bars) to services sectors (red bars). However, the specific sectors with the largest changes differ across intermediates and investment producing sectors. For intermediates, the largest increases occurred in finance/insurance, professional/technical services, administrative and waste services, real estate, and information services; the largest declines were in agriculture, primary metals, food and beverage manufacturing, and textile manufacturing. For investment, the largest increases occurred in professional/technical services, information services, and wholesale trade; the largest declines were in machinery, construction, and motor vehicle manufacturing.⁷

Given the general sectoral patterns in Figure 1, Figure 2 plots time series of s_{it}^M and s_{it}^X at the two sector level (goods and services). As structural change in consumption appears in our quantitative analysis, Figure 2 also plots the goods and services shares of total consumption production. This figure summarizes the main aggregate stylized facts about changing production networks: for each of the three uses of sectoral output, the fraction produced by services sectors is increasing over time, with the services share of investment and consumption rising by roughly 20 percentage points and the services share of intermediates increasing by more than 35 percentage points.

The rising services share in each production network may reflect increased spending on service inputs within sectors or increased intermediates spending by sectors that use services intermediates more intensively. A shift-share decomposition (reported in Appendix B) reveals that within-sector

⁷The time series of production shares for these sectors are shown in Appendix B.

changes account for roughly 50% of the increase in services-produced intermediates, compared to 75-100% for services-produced investment. These findings reflect the higher sector-specificity within the intermediates network compared to the investment network and account for the fact that the intermediates network experienced more pronounced structural change than either consumption or investment.

These stylized facts relate to the “value-added” measurement approach introduced by [Herrendorf et al. \(2013\)](#). Their approach implicitly includes structural change in the intermediates network by using input-output data to identify each sector’s overall contribution to producing consumption or investment. Given the quantitatively large changes within the intermediates network (Figure 2), we measure what portion of value-added structural change can be attributed to the intermediates network in [Appendix B](#). Our decomposition shows that structural change in the intermediates network alone accounts for roughly 50% of structural change in consumption and investment value-added.

Finally, in [Appendix B](#), we provide two additional sets of results highlighting the robustness of the stylized facts presented here. First, we provide evidence that structural change in intermediates is not merely outsourcing of services tasks. Second, we show that structural change in production networks is observed within almost all sectors in the U.S. and that these patterns are also observed in many other high-income countries, using data from the World Input Output Database (WIOD: [Timmer, Dietzenbacher, Los, Stehrer and de Vries, 2015](#); [Woltjer, Gouma and Timmer, 2021](#)).

3. The Relative Price of Services for Consumption, Investment, and Intermediates

Going back at least to [Baumol \(1967\)](#), a commonly proposed explanation for structural change patterns as illustrated in Figure 2 is movements in relative productivity, which in turn drive changes in relative prices. The common measurement approach in the existing literature assumes a single price for goods and a single price for services, aggregated across standard sectoral definitions (e.g., [Herrendorf et al., 2021](#); [García-Santana et al., 2021](#); [Sposi et al., 2021](#)). While parsimonious, this approach masks important heterogeneity in price trends across sectors specializing in the production of consumption, investment, and intermediates. For example, in the previous section, we observed that the underlying sectors contributing to the rise of services and the fall of goods are

different across investment and intermediates.⁸ Thus, to capture this heterogeneity, we instead compute goods and services prices separately for each of the use categories of consumption, investment, and intermediates.

A key challenge in measuring goods and services prices by use is that standard data sources only provide detailed price information for either sectors or uses, but not both simultaneously. For instance, the BEA Industry accounts offer detailed gross output prices by sector, clearly distinguishing goods from services, but don't differentiate these sectoral prices by the use of each sector's output.⁹ Consequently, the ability to construct use-specific prices with gross output data is limited by the extent to which goods and services sub-sectors specialize in producing consumption, intermediates, or investment (that can then be aggregated into a single price by use). However, as we demonstrate, there is a limited degree of specialization across our 40 consistently defined sectors, which significantly constrains measured price variation across uses. This diminishes the viability of a measurement approach that relies exclusively on gross output prices from the BEA Industry Accounts.

3.1. Price Measurement

To measure prices separately by use, we instead draw on data for detailed consumption and investment commodities from the U.S. NIPA and then use Input Output data to map the production of these commodities to goods and services sectors. Expenditure-side NIPA data consistently cover expenditures and prices for 68 consumption and 30 investment commodities over our entire sample, 1947-2020. Examples of consumption commodities at this level of detail include household appliances, jewelry and watches, children's and infants' clothing, dental services, and purchased meals and beverages. Examples of investment commodities include non-mining structures, office and accounting equipment, construction machinery, software, and R&D investment. As emphasized by [Herrendorf et al. \(2013\)](#) and [Herrendorf et al. \(2014\)](#), these prices partially reflect the price of intermediate inputs used in the production of these commodities. Thus, they will only be

⁸These differences are even more pronounced for consumption, where health services account for a big part of the rise of services, and produce virtually no intermediates or investment (see Table A.1).

⁹In its GDP by Industry database and integrated productivity accounts, the BEA publishes the price of the intermediates bundle each sector purchases. However, this bundle price does not identify the price of intermediate inputs produced by different sectors.

consistent with a general equilibrium framework that explicitly models the input-output structure of the economy, which we develop in the next section.

Using expenditure-side price data ensures that we properly identify differences in prices by consumption and investment uses, but we must still map these prices into the NAICS defined categories of goods and services. To map the prices of these NIPA commodities into our sectors, we use a combination of BEA Input Output data published in “bridge files” and “make tables”; these files have been used in other work (e.g., [Bils, Klenow and Malin, 2013](#); [vom Lehn and Winberry, 2022](#); [Bergman, Jaimovich and Saporta-Eksten, 2023](#)) to map commodities reported in NIPA to NAICS sectors. The combination of bridge and make files “bridges” the income and expenditure sides of national accounts, mapping NIPA commodities into the NAICS sectors that “make” them. For example, consider the NIPA consumption commodity of new motor vehicles, on which 167 billion dollars were spent in 1997. The combination of bridge and make files provides a detailed breakdown of how much each NAICS sector contributed to the final value of new motor vehicles: 71% from motor vehicle manufacturing, 22% from retail trade, 3% from wholesale trade, 1% from transportation and warehousing services, and the remaining 2% from a handful of other sectors, such as fabricated metals and machinery.¹⁰

Formally, the bridge and make files generate weights ξ_{jlt}^u , which make it possible to aggregate spending on individual commodities, l , for use u , at time t into the production of that use by sector j at time t . For example, for consumption (i.e., $u = C$), the value of consumption produced by sector j , $P_{jt}C_{jt}$ is given by a weighted sum of spending on all consumption commodities l : $P_{jt}C_{jt} = \sum_l \xi_{jlt}^C P_{lt}^C Q_{lt}^C$, where $P_{lt}^C Q_{lt}^C$ represents spending on consumption commodity l at time t . That is, total spending on consumption produced by the goods sector is given by summing up across commodities the total spending on each commodity (such as motor vehicles), $P_{lt}^C Q_{lt}^C$, multiplied by what the bridge and make files indicate is the fraction of that commodity produced by goods sectors (e.g., for motor vehicles in 1997, 73%).

¹⁰NAICS-coded bridge files for consumption are only available starting in 1997. We thus assume that the bridge file entries for consumption prior to 1997 are the same as the 1997 data. However, the BEA does publish SIC-coded consumption bridge files going back to 1967, with less detail than the latest bridge files. We have explored converting these to NAICS codes and found only very minor changes in the bridge files between 1967 and 1997, supporting our use of the 1997 bridge files for earlier years. For investment, we use the bridge files from [vom Lehn and Winberry \(2022\)](#), who extend these files back to 1947. However, in [Appendix C](#) we show that all results are robust to using a fixed bridge file.

Based on these bridge and make files, we measure separate prices for consumption and investment produced by goods and services sectors using a Tornqvist index, which is a weighted average of price growth across consumption or investment commodities. For example, we measure the price for goods consumption, $P_{g-c,t}$, using NIPA price and spending data on 68 consumption commodities (P_{lt}^C and $P_{lt}^C Q_{lt}^C$ for $l \in \{1, \dots, 68\}$) according to the formula:

$$\Delta \ln(P_{g-c,t}) = \sum_{l=1}^{68} \mu_{glct} \Delta \ln(P_{lt}^C), \quad (2)$$

where $\mu_{glct} \equiv \frac{\xi_{glt}^C P_{lt}^C Q_{lt}^C}{\sum_{m=1}^M \xi_{gmt}^C P_{mt}^C Q_{mt}^C}$ is the weight (averaged across years $t-1$ and t) each consumption commodity receives in the goods consumption price index, with $P_{lt}^C Q_{lt}^C$ representing total spending on consumption commodity l and ξ_{glt}^C the fraction of consumption commodity l produced by goods sectors according to the BEA bridge/make files.¹¹ Calculations for the price of goods investment, services consumption, and services investment are analogous.

Finally, since intermediate inputs are excluded from GDP, their prices cannot be measured using expenditure-side NIPA data. However, gross output prices in the BEA Industry accounts represent an average of consumption, investment, and intermediates produced by each sector. Therefore, we can identify intermediate input prices for goods and services as the residual in gross output prices after removing consumption and investment prices. This approach ensures that our measured prices are fully consistent with the aggregated prices of the goods and services sectors.

For example, treating gross output prices as a Tornqvist index, we naturally measure price growth in intermediates produced by goods sectors as the residual of this index:

$$\Delta \ln(P_{g-m,t}) = \frac{1}{1 - \zeta_{gt}^C - \zeta_{gt}^X} \left(\Delta \ln P_{gt}^{GO} - \zeta_{gt}^C \Delta \ln P_{g-c,t} - \zeta_{gt}^X \Delta \ln P_{g-x,t} \right), \quad (3)$$

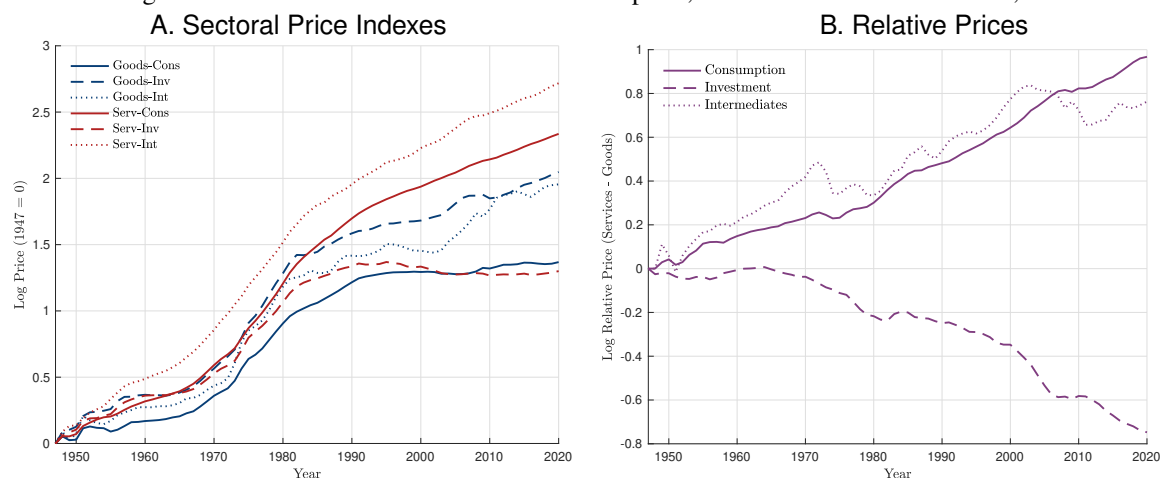
where ζ_{gt}^i is the average share (between $t-1$ and t) of goods gross output used for $i \in \{C, X\}$, and $\Delta \ln P_{gt}^{GO}$ is the log change in the goods sector gross output price.¹² The services-intermediates price is measured analogously.¹³

¹¹In the case of investment, for consistency with how we measure structural change, we use the adjusted (for used goods, etc.) spending data by commodity used to construct the investment network data in [vom Lehn and Winberry \(2022\)](#). Using the raw NIPA data generates nearly identical results.

¹²We adjust gross output prices (and, to a lesser extent, consumption and investment prices) for oil/energy price spillovers before performing this procedure. The qualitative patterns of relative price movements across goods and services sectors are robust to not making these corrections (see [Appendix C](#)).

¹³Alternatively, the Producer Price Index (PPI) published by the U.S. Bureau of Labor Statistics (BLS) provides purchasers' prices for intermediate inputs produced by different sectors. These data provide a direct measure of inter-

Figure 3: Prices of Goods and Services Consumption, Investment and Intermediates, 1947-2020



Notes: Panel A shows the time series of prices for each use (consumption, investment, or intermediates) produced by each sector (goods or services). Panel B shows the price of services divided by the price of goods for each use. All series are logged and normalized to 0 in 1947.

Figure 3 plots our price series for consumption, investment, and intermediates produced by goods and services sectors; panel A illustrates prices in log levels while panel B shows the log of the price of services divided by the price of goods for each use. Consistent with the well-known price patterns in goods and services as a whole, the price of services relative to goods rises significantly over time for consumption and intermediates. Given the rising share of services expenditures for consumption and intermediates, rising relative prices are consistent with complementarity between goods and services inputs.

Surprisingly, and in contrast to aggregate price trends, the relative price of services investment is falling. This finding arises as investment inputs produced by services sectors are primarily information technology and intellectual property products (e.g., software and R&D) whose price has fallen significantly relative to the price of goods investment (e.g., equipment or structures). Given rising expenditures on services investment, falling relative prices are consistent with the idea that goods and services inputs to investment are *substitutes*. Hence, the economic consequences of structural change in investment may be significantly different than for consumption and intermediates.

mediate input prices but have incomplete coverage of services sectors (roughly 85% of the services sectors producing intermediates) and prices for services intermediates are only available starting in 2009. Our intermediates prices are nearly identical to the published PPI data for prices of both goods and services intermediates (see [Appendix C](#)).

In [Appendix C](#), we show that this finding is robust to a variety of alternative specifications: aggregating investment prices with user cost weights instead of investment expenditures as recommended by [Holden, Gourio and Rognlie \(2020\)](#); focusing exclusively on equipment and software; making quality adjustments as in [Cummins and Violante \(2002\)](#); and holding the values of bridge files constant across all time periods. In all cases, the price of investment produced by services sectors is declining relative to the price of investment produced by goods sectors.

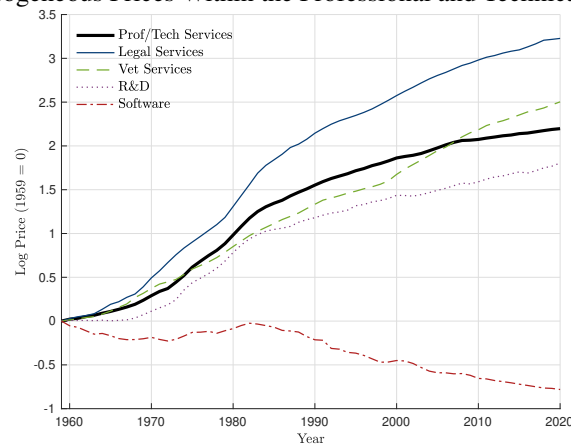
3.2. Aggregation Bias

The fact that relative price movements in goods and services investment are more consistent with substitutable inputs than complementary inputs contrasts with the elasticities of substitution calibrated by [Herrendorf et al. \(2021\)](#), [García-Santana et al. \(2021\)](#) and [Sposi et al. \(2021\)](#), who use a single price for goods and a single price for services, which implies input complementarity. If we aggregate goods and services prices across consumption, investment, and intermediates, we also find that services are getting more expensive relative to goods as a whole, because the relative price of services to goods is rising in consumption and intermediates. The reason for our different findings is aggregation bias. Because investment is a small fraction of output—on average over the period 1947-2020, investment is 21% and 5% of the gross output of goods and services, respectively—it is easy for aggregate price trends to be dominated by price movements in consumption and intermediates, masking the behavior of investment prices.

To highlight this argument, we consider an alternative construction of prices for goods and services by use, computed as a weighted average of gross output prices for the 40 consistent NAICS sectors in our industry data, with weights given by each sector's production share of consumption, investment, or intermediates within goods or services sectors (see [Appendix C](#) for details). With this approach, we find similar results for most of our price series, but we see sizable differences in the price of services investment. Although the price of services investment grows substantially less than the overall price of services when measured using gross output data, it still grows faster than goods investment, implying a rising relative price of services.

However, measuring the price of services investment using publicly available gross output prices is still subject to significant aggregation bias. The gross output price data can properly identify the price of services investment only if at least one of two conditions is met: 1) ob-

Figure 4: Heterogeneous Prices Within the Professional and Technical Services Sector



Notes: The thick line denotes the log gross output price for the professional and technical services sector, obtained from the BEA GDP by Industry database. The thin lines are the log prices of varied commodities produced by the professional and technical services sector. These detailed price series are based on NIPA Tables 2.4.4U and 5.6.4.

served services sectors specialize in producing primarily one use (consumption, investment, or intermediates), implying no within-sector aggregation bias, or 2) the price trends for consumption, investment, and intermediates within each sector are comparable. Neither of these conditions is satisfied at the 40-sector level of disaggregation. Even for the two services sectors that produce the most services investment (information and professional/technical services), only a small portion of gross output is used as investment (on average only 15% and 22%, respectively), suggesting the potential for significant aggregation bias.¹⁴

Although the professional/technical services sector is the largest and fastest growing producer of services investment (primarily software and R&D), it also produces the consumption commodities of legal services and veterinary services (along with many other commodities).¹⁵ Using underlying detail in the national accounts (only available since 1959), Figure 4 plots the time series of the prices of these commodities compared to the gross output price of the professional/technical services sector as a whole. While there has been little price growth in the investment commodities

¹⁴In more recent years, the GDP by Industry database has published price data for a more disaggregated set of industries. However, substantial evidence of potential aggregation bias persists. For example, in these data, the largest services-investment producer is miscellaneous professional/technical services, yet only 24% of its gross output is used for investment. See Appendix C for more details.

¹⁵Based on more detailed Input-Output data available only in 2007 and 2012, legal services and veterinary services are the two biggest consumption commodities and software and R&D are the two biggest investment commodities produced by this sector.

produced by this sector (software and R&D), their price trends are masked by the rising prices of consumption commodities, such as legal services.¹⁶

In contrast, using expenditure-side data to measure prices makes aggregation bias less of a concern. Using expenditure-side data, differences in consumption and investment prices between goods and services sectors are identified from heterogeneity in how much each sector produces different commodities (differences in ξ_{glt}^C and ξ_{glt}^X). These prices would be subject to aggregation bias if commodities are produced by an even mix of goods and services sectors; in the extreme case where each commodity is produced 50% by goods and services sectors, prices of goods and services would be identical. However, nearly two-thirds of our commodities are produced in large majority (more than 80%) by either goods or services, implying that the bridge/make files at the level of commodity detail in expenditure side data sharply distinguish between goods and services production of consumption and investment.¹⁷

In summary, both expenditure-side and income-side price data can be used to measure goods and services prices by use. The best approach is the one that most precisely identifies price variation along the two dimensions that define them: whether the sector's output is a good or a service, and whether the sector's output is used for consumption, investment, or as an intermediate input. Our evidence implies that the bridge/make files more precisely distinguish goods and services sectors on the expenditure side than the underlying sectoral detail on the income side distinguishes final use. Thus, expenditure-side data provide a more accurate measure of prices for goods and services sectors by use.

4. Model

To understand the observed patterns in sectoral expenditures and prices across production networks, we develop an N sector extension of the neoclassical growth model that explicitly incorporates the production networks for intermediate inputs and investment.

¹⁶In [Appendix C](#), we provide similar evidence for the information sector, the other primary producer of services-investment.

¹⁷The main instances when both goods and services contribute significantly to the production of a commodity are when delivery of the commodity to the final user involves significant "margins" due to transportation, wholesale trade, or retail trade. If we reclassify these margin sectors as goods, because they typically arise when the product is a physical good, then over 90% of all commodities would be produced in large majority by either goods or services. The patterns of relative prices we measure are robust to this reclassification (see [Appendix C](#)).

4.1. Technology

For each sector j , gross output, Q_{jt} , is produced using capital, K_{jt} , labor L_{jt} , and a bundle of intermediate goods M_{jt} according to the following Cobb-Douglas production function:

$$Q_{jt} = A_{jt} \left(K_{jt}^{\theta_j} L_{jt}^{1-\theta_j} \right)^{\alpha_j} M_{jt}^{1-\alpha_j}, \quad (4)$$

where A_{jt} is exogenous TFP in sector j .

Each sector's intermediates bundle, M_{jt} , is produced by an "intermediates bundling" sector for sector j , which aggregates intermediate goods from all sectors using a CES technology:

$$M_{jt} = A_{jt}^M \left(\sum_i \omega_{Mij}^{1/\epsilon_{Mj}} M_{ijt}^{\frac{\epsilon_{Mj}-1}{\epsilon_{Mj}}} \right)^{\frac{\epsilon_{Mj}}{\epsilon_{Mj}-1}}, \quad (5)$$

where ϵ_{Mj} is the elasticity of substitution between intermediate inputs for sector j , $\omega_{Mij} \in [0, 1]$ determines the relative importance of inputs from each sector in producing intermediates (with $\sum_i \omega_{Mij} = 1$), M_{ijt} represents intermediate inputs used in sector j purchased from sector i at time t , and A_{jt}^M represents exogenous intermediates-bundling TFP for sector j . We include this bundling TFP to allow for added flexibility when calibrating the model, but in Section 6 we show that movements in this term only have a modest effect on overall growth.

Capital is sector-specific and follows a standard law of motion, depreciating at rate δ_j :

$$K_{jt+1} = (1 - \delta_j)K_{jt} + X_{jt}. \quad (6)$$

Investment, X_{jt} , is produced in an "investment bundling" sector for sector j 's capital with the following aggregation technology:

$$X_{jt} = A_{jt}^X \left(\sum_i \omega_{Xij}^{1/\epsilon_{Xj}} X_{ijt}^{\frac{\epsilon_{Xj}-1}{\epsilon_{Xj}}} \right)^{\frac{\epsilon_{Xj}}{\epsilon_{Xj}-1}}, \quad (7)$$

where ϵ_{Xj} is the elasticity of substitution between investment inputs in sector j , $\omega_{Xij} \in [0, 1]$ determines the relative importance of different inputs in producing investment (with $\sum_i \omega_{Xij} = 1$), and X_{ijt} is investment inputs used in sector j purchased from sector i at time t . A_{jt}^X represents exogenous investment-bundling TFP for sector j , which is included for calibration flexibility.

4.2. Preferences

There is an infinitely lived representative household with preferences given by:

$$\sum_{t=0}^{\infty} \beta^t U(\{C_{it}\}_{i=1}^N), \quad (8)$$

where $0 < \beta < 1$ is the discount factor and C_{it} is consumption produced by sector i . We assume that the period utility function, $U(\{C_{it}\}_{i=1}^N)$ follows a log CES structure, with

$$U(\{C_{it}\}_{i=1}^N) = \ln \left(\left[\sum_i \omega_{Ci}^{1/\epsilon_C} (C_{it} + \bar{c}_i)^{\frac{\epsilon_C-1}{\epsilon_C}} \right]^{\frac{\epsilon_C}{\epsilon_C-1}} \right), \quad (9)$$

where ϵ_C is the elasticity of substitution between consumption products, $\omega_{Ci} \in [0, 1]$ determines the relative importance of consumption products from each sector in aggregate consumption (with $\sum_i \omega_{Ci} = 1$), and \bar{c}_i is a sector-specific non-homotheticity to allow for income effects in structural change.¹⁸ Our framework abstracts from preferences over leisure, assuming the household inelastically supplies one unit of labor each period.

4.3. Equilibrium

We study the competitive equilibrium of this economy with representative profit-maximizing firms in all markets. The price of final output in each production sector j is denoted by P_{jt} ; the price of the intermediates bundle is given by P_{jt}^M . The household owns the capital stock and accumulates capital in sector j by purchasing new investment goods from the investment bundling firm for sector j at price P_{jt}^X . The household rents sector-specific capital to each sector j at a rental price R_{jt} . Since labor is common to each sector and freely mobile, there is a single wage paid to the household, denoted by W_t . For reference, we provide a full listing of equilibrium conditions in [Appendix D](#).

In equilibrium, all markets (final output, labor, capital, as well as intermediate and investment bundling) clear. Final output from each sector can be used as consumption for the household or as an input to intermediate and investment bundles across sectors, implying a market clearing relationship of:

$$C_{jt} + \sum_i M_{jit} + \sum_i X_{jit} = Q_{jt}. \quad (10)$$

The extent to which each sector produces consumption, intermediates, and investment depends on preference and bundling parameters; in Section 5, we consider a calibration in which each sector j specializes in the production of only one final use: consumption, investment, or intermediates.

With constant returns and competitive markets, the price indices for the bundle of intermediate

¹⁸We allow for non-homotheticities in preferences to better fit the evidence on consumption structural change; our quantitative results on how structural change in production networks affects growth are robust to setting $\bar{c}_i = 0 \forall i$.

inputs, P_{jt}^M , and the bundle of investment, P_{jt}^X , are given by:

$$P_{jt}^M = \frac{1}{A_{jt}^M} \left(\sum_i \omega_{Mij} P_{it}^{1-\epsilon_{Mj}} \right)^{\frac{1}{1-\epsilon_{Mj}}}, \quad (11)$$

$$P_{jt}^X = \frac{1}{A_{jt}^X} \left(\sum_i \omega_{Xij} P_{it}^{1-\epsilon_{Xj}} \right)^{\frac{1}{1-\epsilon_{Xj}}}. \quad (12)$$

Furthermore, manipulating the first order conditions for each sector's production generates the following expression for the price of final output produced by each sector j :

$$P_{jt} = \frac{1}{A_{jt}} \left(\frac{R_{jt}}{\theta_j \alpha_j} \right)^{\theta_j \alpha_j} \left(\frac{W_t}{(1-\theta_j)\alpha_j} \right)^{(1-\theta_j)\alpha_j} \left(\frac{P_{jt}^M}{1-\alpha_j} \right)^{1-\alpha_j}. \quad (13)$$

Finally, we describe the equilibrium conditions determining structural change in production networks. From the first order conditions for the intermediates and investment bundling sectors, we derive the model expression for the shares of intermediates or investment spending by sector j on products made by sector i at time t , denoted s_{ijt}^M and s_{ijt}^X :

$$s_{ijt}^M \equiv \frac{P_{it} M_{ijt}}{P_{jt}^M M_{jt}} = \omega_{Mij} \left(\frac{P_{it}}{A_{jt}^M P_{jt}^M} \right)^{1-\epsilon_{Mj}}, \quad (14)$$

$$s_{ijt}^X \equiv \frac{P_{it} X_{ijt}}{P_{jt}^X X_{jt}} = \omega_{Xij} \left(\frac{P_{it}}{A_{jt}^X P_{jt}^X} \right)^{1-\epsilon_{Xj}}. \quad (15)$$

These intermediates and investment expenditure shares depend on the relative prices of each sector's output, and the CES scale (ω) and elasticity parameters (ϵ) in the bundling sectors. Movements in relative prices across sectors can thus induce structural change in production networks. The aggregate share of intermediates or investment spending on products made by sector i , s_{it}^M and s_{it}^X is given by a weighted average of these sectoral expenditure shares, following the same relation described for the empirical work in equation (1). As in Section 2, these expressions show that changes in production networks in the model can reflect both changes in production processes within sectors (changes in s_{ijt}^M and s_{ijt}^X) and changes in the composition of spending across sectors.

4.4. Structural Change and Economic Growth

To develop intuition for the connection between structural change and economic growth, we consider a special case of the model that allows us to derive closed-form expressions for aggregate GDP and thus illustrate how structural change in production networks affects aggregate growth.¹⁹

¹⁹These assumptions, along with the assumption that $\bar{c}_i = 0 \forall i$, can also be used to derive an aggregate balanced growth path for our model; we discuss the aggregate balanced growth path in more detail in an earlier draft of the paper, [Gaggl, Gorry and Vom Lehn \(2023\)](#).

This special case requires strong assumptions; however, we do not impose these assumptions for the calibration and quantitative exercises in Sections 5 and 6. For this special case, we use aggregate investment as the numeraire and measure aggregates in units of aggregate investment; thus, TFP growth in the production of consumption will not impact aggregate GDP (as in [Ngai and Pissarides, 2007](#); [Herrendorf et al., 2021](#)). However, our quantitative exercises measure GDP in a more data-consistent fashion (as a chained index number). The intuition we develop here regarding investment and intermediates structural change and economic growth also applies to consumption structural change in those exercises.

For this special case, we impose the following assumptions:

Assumption 1. *The parameters of sectoral production functions are the same across all sectors, i.e., $\alpha_j = \alpha$ and $\theta_j = \theta$ for all j .*

Assumption 2. *The parameters governing the evolution of capital—both parameters of the investment bundling sectors and the depreciation rate—are the same for all sectors j , i.e., $\delta_j = \delta$, $\omega_{Xij} = \omega_{Xi}$ and $\epsilon_{Xj} = \epsilon_X$ for all j . Furthermore, each sector's investment bundling TFP is the same, i.e., $A_{jt}^X = A_t^X$.*

Assumption 3. *The parameters for intermediates bundling are the same for all sectors and each sector's intermediates bundling TFP is the same, i.e., $\omega_{Mij} = \omega_{Mi}$, $\epsilon_{Mj} = \epsilon_M$, and $A_{jt}^M = A_t^M \forall j$.*

With these assumptions, we state the following proposition defining aggregate GDP:

Proposition 1. *Under assumptions 1 – 3, aggregate GDP, denoted in units of the numeraire (aggregate investment), is given by:*

$$Y_t = \sum_i P_{it}^V V_{it} = \sum_i (P_{it} Q_{it} - P_{it}^M M_{it}) = \mathcal{A}_t K_t^\theta, \quad (16)$$

where V_{it} represents real value added in sector i , P_{it}^V is the price of value added, $\mathcal{A}_t = \frac{\alpha}{1-\alpha} (1 - \alpha)^{\frac{1}{\alpha}} B_t^X (B_t^M)^{\frac{1-\alpha}{\alpha}}$ where $B_t^X \equiv A_t^X (\sum_k \omega_{Xk} A_{kt}^{\epsilon_X - 1})^{\frac{1}{\epsilon_X - 1}}$ and $B_t^M \equiv A_t^M (\sum_k \omega_{Mk} A_{kt}^{\epsilon_M - 1})^{\frac{1}{\epsilon_M - 1}}$, and $K_t = \sum_i K_{it}$.

Proof. See [Appendix D](#). □

Aggregate GDP has the same Cobb-Douglas structure as sectoral real value added (with labor dropping out because it is in unit aggregate supply). With investment as the numeraire, aggregate TFP, \mathcal{A}_t , only depends on TFP growth that expands the frontier of investment production, either through TFP growth stemming directly from investment producers (B_t^X) or TFP growth originating from their intermediate suppliers (B_t^M).

Given this expression for aggregate GDP, our primary interest lies in tightly characterizing the composition of aggregate TFP growth, \mathcal{A}_t , as this is closely related to aggregate GDP growth.²⁰ Define the gross growth rate for any variable Z_t between time periods t and $t + 1$ as $\gamma_{t+1}^Z \equiv \frac{Z_{t+1}}{Z_t}$. Then, the growth rate of aggregate TFP is given by $\gamma_t^A = \gamma_t^{B^X} \left(\gamma_t^{B^M} \right)^{\frac{1-\alpha}{\alpha}}$. Because the growth rate of aggregate TFP depends on both $\gamma_t^{B^X}$ (the direct effect of TFP growth originating from investment producers) and $\gamma_t^{B^M}$ (the indirect effect of TFP growth stemming from intermediates suppliers), there is a direct connection between the aggregate growth rate and structural change. To see this, consider the model expressions for these two sources of aggregate growth:

$$\gamma_t^{B^M} = \gamma_t^{A^M} \left(\sum_i s_{it-1}^M (\gamma_{it}^A)^{\epsilon_M - 1} \right)^{\frac{1}{\epsilon_M - 1}}, \quad (17)$$

$$\gamma_t^{B^X} = \gamma_t^{A^X} \left(\sum_i s_{it-1}^X (\gamma_{it}^A)^{\epsilon_X - 1} \right)^{\frac{1}{\epsilon_X - 1}}. \quad (18)$$

In addition to the Cobb-Douglas parameters on capital (θ) and value-added (α), equations (17) and (18) illustrate that the growth rate of aggregates depends on four components: growth in intermediates-bundling TFP ($\gamma_t^{A^M}$), growth in investment-bundling TFP ($\gamma_t^{A^X}$), and two weighted sums of TFP growth in each individual production sector i , where the weights are determined by the composition of intermediates and investment production (s_{it}^M and s_{it}^X).

Differential TFP growth across sectors, which generates differential time paths of relative prices, can induce structural change in production networks—captured by changes in s_{it}^M and s_{it}^X . Equations (17) and (18) highlight that the impact of this structural change on aggregate growth critically depends on the elasticities of substitution in the CES aggregators: ϵ_M for intermediates and ϵ_X for investment. Proposition 2 formalizes this relationship:

Proposition 2. *Assume that assumptions 1-3 hold. (a) Assume that the distribution of intermediates (investment) production across sectors i in time period $t - 1$, s_{it-1}^M (s_{it-1}^X), is taken as given;*

²⁰Along an aggregate balanced growth path, for example, aggregate GDP growth is proportional to the growth rate of aggregate TFP.

that is, $\frac{\partial s_{it-1}^M}{\partial \epsilon_M} = 0$ ($\frac{\partial s_{it-1}^X}{\partial \epsilon_X} = 0$). Then, in time period t , the growth rate $\gamma_t^{B^M}$ ($\gamma_t^{B^X}$) is weakly increasing in ϵ_M (ϵ_X). (b) Assume that the distribution of intermediates (investment) production across sectors i in time period 0, s_{i0}^M (s_{i0}^X) is taken as given; that is, $\frac{\partial s_{i0}^M}{\partial \epsilon_M} = 0$ ($\frac{\partial s_{i0}^X}{\partial \epsilon_X} = 0$). If $\mathbb{E} [\sum_{s=1}^{t-1} \ln(\gamma_{is}) \mid \gamma_{it}^A = a]$ is weakly increasing in a with a probability measure across sectors of s_{it-1}^M ; that is, there is weak positive dependence across sectors between the cumulative log history of TFP growth up to $t - 1$ and TFP growth in t across sectors, then for all $t > 0$, the growth rate $\gamma_t^{B^M}$ ($\gamma_t^{B^X}$) is weakly increasing in ϵ_M (ϵ_X).

Proof. See [Appendix D](#). □

The proposition establishes the following ideas. Starting from any initial distribution of intermediates or investment production, the higher the elasticity of substitution is for the investment or intermediates network, the higher the composite of TFP growth in that network, $\gamma_t^{B^X}$ or $\gamma_t^{B^M}$, will be in the next period. Then, provided that growth rates are sufficiently stable over time (that future growth rates are positively correlated with cumulative past growth rates – the weak positive dependence assumption), starting from any initial distribution of intermediates or investment production, a higher elasticity of substitution in either network will generate faster composite TFP growth in that network for all future time periods.

The intuition for this result can be seen from the limiting cases when sectoral TFP growth rates are constant over time.²¹ For example, if $\epsilon_M < 1$ (i.e., gross complements), then as $t \rightarrow \infty$, $\gamma_t^{B^M}$ will converge to the *slowest* TFP growth rate among producers of intermediates. This is because movements in relative prices will ultimately cause s_{it}^M to converge to unity for the slowest growing sector. In contrast, in the case of gross substitutes (i.e., $\epsilon_M > 1$), this growth rate will converge to the *fastest* TFP growth rate, as all expenditures ultimately become concentrated on this sector.

Furthermore, when one production network features complementarity in sectoral inputs and the other features substitutability, the network that features gross substitutability will become endogenously more important for aggregate growth over time. Resources are reallocated toward the fastest-growing producers in the network with substitutability (“frontiers”), while resources are allocated to the slowest-growing producer in the network with complementarity (“bottlenecks”).

²¹The weak positive dependence assumption is trivially satisfied if sectoral TFP growth rates are constant over time.

Thus, structural change in production networks can affect the aggregate growth of the economy. The remainder of the paper focuses on the model’s quantitative implications for aggregate growth when we study GDP measured as an index number (per national accounting conventions) and do not impose these assumptions.

5. Calibration, Transition Path, and Structural Change

To examine the quantitative implications of our model, we calibrate all model parameters and numerically solve the model’s transition path, where we use our evidence on relative prices to identify sectoral TFP. A key challenge for calibration is determining the appropriate level of aggregation. On the one hand, we document in Section 2 that the primary patterns of structural change in production networks can be summarized using just two sectors: goods and services. On the other hand, in Section 3 we emphasize significant heterogeneity in relative price trends across consumption, investment, and intermediate input producers within these two broad sectors.

Thus, to accommodate this heterogeneity in price trends, we focus on a six-sector aggregation, with each sector defined by the interaction of its product market—goods or services—and the eventual use of these products—as final consumption, investment, or an intermediate input. The resulting six sectors are goods-consumption (e.g., books, toys, food), goods-investment (e.g., buildings, machines, vehicles), goods-intermediates (e.g., primary metals, chemicals), services-consumption (e.g., education, health care), services-investment (e.g., software, R&D), and services-intermediates (e.g., financial services, wholesale trade). Consequently, our calibration assumes that each sector in the model fully specializes in the production of either consumption, investment, or intermediates.

5.1. Calibration: Non-CES Parameters

We calibrate the non-CES aggregator parameters using BEA data from 1947-2020 at the 40 sector level. For each parameter $(\alpha_j, \theta_j, \delta_j)$, we first obtain implicit values at the 40-sector level and then aggregate those values to the six sectors in our calibration. This procedure is potentially subject to the aggregation bias described in Section 3, but the expenditure-side national accounting approach we developed for price measurement is not feasible for these parameters. Furthermore, we are less concerned about the impact of aggregation bias for these parameters, as they are not allowed to change over time in our model and because our quantitative results are robust to setting

these parameters to common values across sectors.

We calibrate α_j using each sector’s ratio of nominal value added to nominal gross output, θ_j using one minus the ratio of nominal labor compensation to nominal value added (minus taxes and adjusted for self-employment), and δ_j using the implied depreciation rates for each NAICS sector published in the BEA Fixed Assets database. We aggregate to six sectors using a weighted average of the 40-sector parameter values, where each sector is weighted by its production of each use—consumption, investment, or intermediates—as a fraction of total goods or services production.²² We average these sectoral parameter values over the entire sample 1947-2020 and use the average as the calibrated value of each parameter. For the discount factor, we choose a common value of $\beta = 0.96$.

Table 1 reports these parameter values. The most notable heterogeneity in these parameters across sectors is that α_j is lower for goods sectors, as goods sectors are much more intermediates intensive than services sectors. Also, θ_j is relatively low for the goods-investment sector, reflecting the high labor share of the construction sector that contributes to goods-investment.

5.2. Calibration Strategy: CES Parameters

To calibrate the CES aggregator parameters for investment and intermediates—the share parameters ($\omega_{Xij}, \omega_{Mij}$) and the elasticity parameters ($\epsilon_j^X, \epsilon_j^M$)—we first construct the share of goods and services investment and intermediates for each of our six sectors. Similar to the calibration targets for non-CES parameters, we generate these by aggregating intermediate and investment expenditure patterns across the 40 BEA sectors in proportion to each sector’s role in producing consumption, investment, or intermediates within goods or services. Again, there is a potential that this approach is subject to aggregation bias. As we do not have sufficient data to rule out this possibility, it is a question for further research. However, our results are robust to assuming all sectors have the same CES technologies with common elasticities of substitution for investment and intermediates.

Using these BEA shares, we calibrate the CES aggregator parameters for investment and intermediates given the observed empirical evidence on relative prices. We do this in two steps. First,

²²For example, to get parameter values for the goods-consumption sector, we weight parameter values for each goods subsector k with the weight $\frac{P_{kt}C_{kt}}{\sum_{l \in \text{Goods}} P_{lt}C_{lt}}$.

Table 1: Model Parameter Values

Panel A: Household Preference Parameters

| | β | ω_{Cg} | ϵ_C | \bar{c}_g | \bar{c}_s |
|-------|---------|---------------|--------------|-------------|-------------|
| Value | 0.96 | 0.13 | 0.28 | 0.00 | 0.54 |

Panel B: Sector Specific Production Parameters

| | θ | α | δ | ω_{Xg} | ϵ_X | ω_{Mg} | ϵ_M |
|-------------------------|----------|----------|----------|---------------|--------------|---------------|--------------|
| <i>Goods Sectors</i> | | | | | | | |
| Consumption | 0.36 | 0.36 | 0.09 | 0.81 | 4.10 | 0.81 | 0.29 |
| Investment | 0.21 | 0.46 | 0.12 | 0.79 | 3.40 | 0.71 | 0.52 |
| Intermediates | 0.35 | 0.42 | 0.09 | 0.82 | 3.81 | 0.77 | 0.44 |
| <i>Services Sectors</i> | | | | | | | |
| Consumption | 0.37 | 0.69 | 0.05 | 0.80 | 1.80 | 0.44 | 0.00 |
| Investment | 0.40 | 0.68 | 0.09 | 0.72 | 2.84 | 0.34 | 0.00 |
| Intermediates | 0.37 | 0.66 | 0.07 | 0.81 | 2.49 | 0.32 | 0.00 |

Notes: Panel A reports preference parameters for the household: β is the discount factor, ω_{Cg} is the goods share parameter in consumption, ϵ_C is the elasticity parameter in consumption, and \bar{c}_g and \bar{c}_s are non-homotheticity parameters for goods and services consumption, respectively. Panel B reports the calibrated parameter values for production technologies in each of the six sectors. The parameters θ and α are Cobb-Douglas exponents in production (θ for capital within value-added, α for the value-added portion of gross output), and δ is the depreciation rate of capital. The parameters ϵ_X and ϵ_M represent the elasticity of substitution between goods and services inputs within investment and intermediates, and ω_{Xg} and ω_{Mg} represent the share parameter attached to goods inputs (with $1 - \omega$ being the share parameter for services) within investment and intermediates. The elasticities ϵ_M reported as 0.00 for the three services intermediate bundles are small positive values rounded to two decimal places; our numerical solver imposes a lower bound of $\epsilon_M \geq 0$.

for each sector, j , the share parameters are calibrated so that the model matches the initial fraction of expenditures on intermediates or investment purchased from sector i in the year 1947.²³ We then combine equations (14) and (15) with equations (11) and (12) to obtain the following equations used to calibrate the elasticities of substitution:²⁴

$$S_{gjt}^M = \frac{\omega_{Mgj} P_{g-m,t}^{1-\epsilon_{Mj}}}{\omega_{Mgj} P_{g-m,t}^{1-\epsilon_{Mj}} + (1-\omega_{Mgj}) P_{s-m,t}^{1-\epsilon_{Mj}}} \quad (19)$$

$$S_{gjt}^X = \frac{\omega_{Xgj} P_{g-x,t}^{1-\epsilon_{Xj}}}{\omega_{Xgj} P_{g-x,t}^{1-\epsilon_{Xj}} + (1-\omega_{Xgj}) P_{s-x,t}^{1-\epsilon_{Xj}}} \quad (20)$$

where $g-x$, $g-m$, $s-x$, $s-m$ denote the sectors for goods and services (g and s) that produce investment and intermediates (x and m) respectively. Given calibrated values for all ω parameters, we calibrate the elasticity parameters using equations (19) and (20) and our empirical price series, minimizing the least squares differences between the model series for structural change and the

²³We normalize relative prices to 1 in 1947 so that these parameters are independent of the elasticity parameters.

²⁴To obtain these calibration equations, we need the model expressions for CES bundling technologies in investment and intermediates, optimization by the household and firms, and perfect competition. The remaining parts of the model are not needed to obtain these equations.

data series for structural change in each of our six sectors over the years 1947-2020.

To calibrate the CES aggregator parameters in consumption, we use similar moments to discipline model parameters. We calibrate the share parameter, ω_{Cg} , to match the share of consumption expenditures on goods in the year 1947, and we calibrate the elasticity of substitution, ϵ_C , to minimize the least square difference between the model and data series for the consumption expenditure share on goods from 1947-2020. For the non-homotheticity parameters, \bar{c}_i , we assume that $\bar{c}_g = 0$ and calibrate \bar{c}_s to minimize the least squares difference between the ratio of real services consumption to real goods consumption, C_{st}/C_{gt} , in the model and the data.²⁵

Parameter values for all CES aggregators and the non-homotheticity terms in preferences are also reported in Table 1. Consistent with our price measurement, the calibrated values for the elasticity parameters confirm that goods and services are complements in the bundling of intermediates in all sectors (elasticities less than one), but substitutes in investment bundling in all sectors (elasticities greater than one).²⁶ For consumption, our calibration yields a goods share (ω_{Cg}) of 0.13 and an elasticity of substitution (ϵ_C) of 0.28, with $\bar{c}_s = 0.54$. The elasticities for consumption and intermediates imply strong complementarity between goods and services, consistent with existing literature (e.g., Herrendorf et al., 2021; García-Santana et al., 2021; Sposi et al., 2021).

The six-sector calibration fit for structural change in intermediates and investment can be found in Appendix E; the model’s overall fit to structural change depends on the aggregation of structural change in each sector, so we assess the fit after we describe how we solve for the transition path of the model.

5.3. Transition Path and Calibrated TFP Series

Because our full model does not admit a balanced growth path, we solve for the model’s transition path between two steady states. Furthermore, in our model, relative sectoral prices depend on wages and sectoral rental rates of capital. Thus, for the model to match the relative prices used in calibrating the CES bundling technologies requires that some TFP series be calibrated along the

²⁵Because these moments in the model depend on the actual level of consumption, these parameters can only be calibrated along the model’s transition path, which we describe in detail in the following subsection.

²⁶Given the novelty of our estimates for the elasticities of substitution in investment, we also report values of these elasticities if we calibrate them to different time periods within the window 1947-2020 in Appendix E. Although the magnitudes vary across each time period, we find that they are consistently greater than 1.

transition path. First, we describe how we calibrate the TFP series, then we describe the assumptions used in solving the transition path.

The model has two types of TFP: TFP in each of the six sectors' production technologies (sectoral TFP) and TFP in the bundling technologies (bundling TFP) for intermediate and investment inputs. For five of our six sectoral TFP series, we calibrate TFP by matching relative output prices in the model to relative output prices in the data, as constructed in Section 3. We calibrate TFP for the final sector to match the aggregate series for GDP per worker, given by a Tornqvist aggregate of sectoral real value added (from the 40 BEA sectors) divided by total employment (measured as the sum of sectoral employment as recorded in the BEA's Industry Accounts and NIPA Table 6.4).²⁷

We measure growth in intermediates and investment bundling TFP using a log first-order approximation of the equilibrium intermediate and investment input price indices (equations (11) and (12)), for years t and $t - 1$. When log-linearized around the average expenditure share in these two years, the resulting expression can be rearranged to solve for the growth in bundling TFP. For example, intermediates bundling TFP for sector i is computed as:

$$\Delta \ln(A_{it}^M) = - \left(\Delta \ln(P_{it}^M) - \sum_{j=g-m, s-m} \left(\frac{P_{jt} M_{ijt}}{P_{it}^M M_{it}} \right) \Delta \ln(P_{jt}) \right), \quad (21)$$

where $g-m$ and $s-m$ are the goods-intermediates and services-intermediates sectors and $\left(\frac{P_{jt} M_{ijt}}{P_{it}^M M_{it}} \right)$ is the average between t and $t - 1$ of the share of intermediate spending by sector i purchased from sector j . We measure $\Delta \ln(P_{it}^M)$ using BEA GDP by Industry data on the price of intermediate bundles by sector, aggregated to the six-sector level. We use a similar equation to identify investment bundling TFP.²⁸

Using this approach to measure the bundling TFP series simplifies our calibration as it is done independently of the model's calibrated parameters and fit. The relative values of intermediates and investment bundle prices along the transition path closely match those observed in the data, suggesting that the cost of this approximation is negligible. This is perhaps unsurprising as we

²⁷If we instead calibrate the final TFP series to match aggregate TFP growth, we obtain very similar results.

²⁸We measure the sectoral investment bundle price as a Tornqvist index of the price of different investment commodities in the NIPA, weighted by sectoral investment spending on each commodity as reported in the BEA Fixed Assets database and used in the construction of the investment network.

expect the growth in these bundling TFP series to be small, as they are a residual of observed intermediates and investment bundle prices. That is, they largely consist of aggregation error leftover in intermediate input and investment bundle prices after accounting for the average price of investment inputs produced by goods and services sectors.

In solving the transition path of the model, we draw on recent work on stable transformation paths in [Buera et al. \(2024\)](#) to inform how we specify initial and terminal conditions of the solution path. When solving a transition path between two steady states, specifying when the economy is in an initial steady state and when it converges to a terminal steady state is potentially arbitrary. However, [Buera et al. \(2024\)](#) show that for a fairly general class of models admitting structural change, with constant growth in sectoral TFP, there exists a unique stable transformation path (STraP) between two asymptotic balanced growth paths reached as either $t \rightarrow -\infty$ or $t \rightarrow \infty$.²⁹ This stable path determines a “natural” level of capital, which can discipline the initial condition prior to the transition defined by time-varying growth rates in each TFP series.

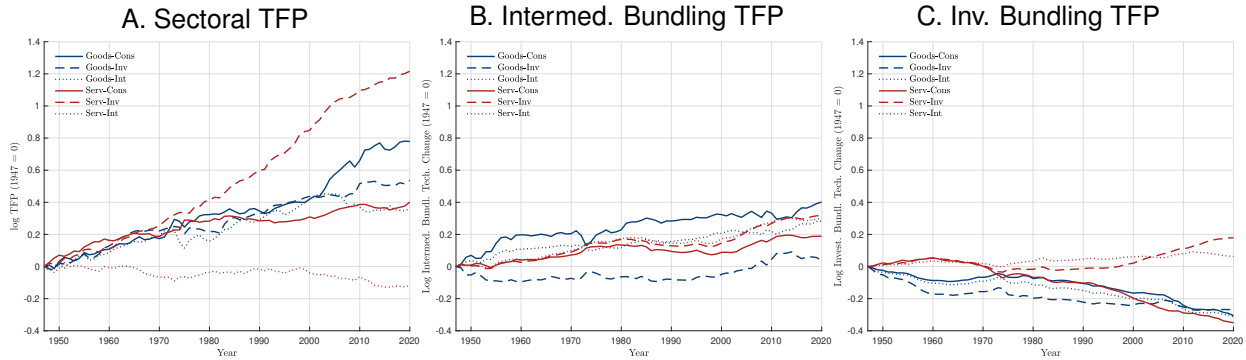
Given this insight, we start our model simulation in a constant steady state in 1897, 50 years prior to our time period of interest, 1947-2020, allowing the economy sufficient time to converge to a STraP before transition dynamics begin in 1947.³⁰ We assume that all TFP series grow at a constant rate from 1897-1947. We assume zero growth for bundling TFP over this period, as it functions as a residual from price measurement. For each sectoral TFP series, we set the growth rate of TFP to match approximately constant growth in relative prices and GDP at the levels observed from 1947-1957, as these are the data moments we calibrate TFP to match on the transition path.³¹ Likewise, to ensure that behavior at the end of our sample window is unaffected by arbitrary terminal conditions of the model, we also allow for constant TFP growth for 50 years after 2020. This allows the dynamics of capital near the end of our sample window to be consistent

²⁹We note that while similar, our model is technically not covered in the class of models for which [Buera et al. \(2024\)](#) prove the existence of a stable transformation path.

³⁰In the simulations illustrated in [Buera et al. \(2024\)](#), the half-life of convergence to the STraP is 8 years, so 50 years provides a conservative time frame to allow for convergence.

³¹Specifically, we first calibrate the TFP series such that the relative price and GDP growth remain exactly constant from 1897-1947. However, because of sectoral heterogeneity, constant relative price growth implies non-constant TFP growth. Thus, after an initial calibration step, we solve the model again with exactly constant sectoral TFP growth from 1897-1947, with growth rates set to the median growth rate of TFP in the original calibration needed to hold relative prices and GDP growth constant from 1897-1947.

Figure 5: TFP Series, 1947-2020



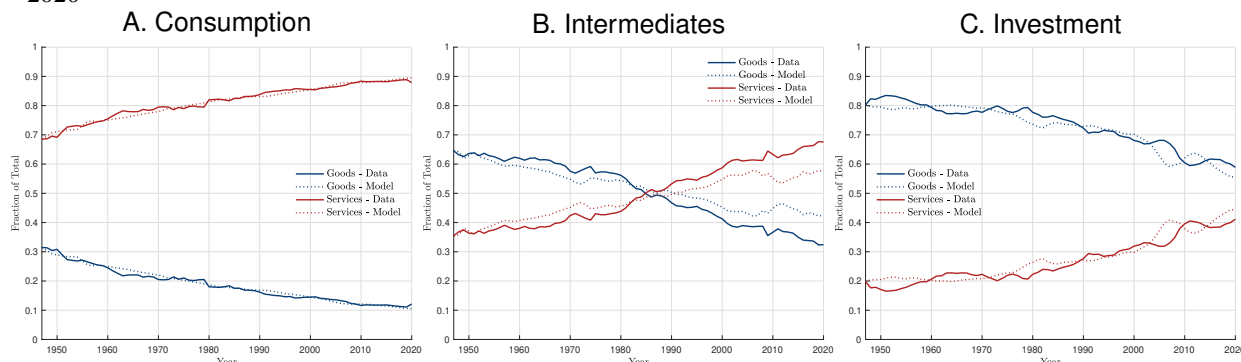
Notes: Panel A shows log sectoral TFP over time for each sector, A_{it} ; panel B shows log intermediates-bundling TFP over time, A_{it}^M ; panel C shows log investment-bundling TFP over time, A_{it}^X . In the figures, all log TFP series are normalized to 0 in 1947.

with converging to a terminal STRaP; we determine TFP growth for this window in the same way as the early period, assuming constant bundling TFP and disciplining sectoral TFP growth based on relative price and GDP growth in the years 2010-2020. After 2070, we assume that growth in all sectoral TFP series gradually slows to zero until 2090, and then assume the model reaches a final steady state in 2130. However, our results are not sensitive to reasonable variation in TFP growth outside the window 1947-2020; for example, assuming zero growth in TFP prior to 1947 and beginning the simulation in 1927 yields nearly identical results.

Figure 5 displays calibrated sectoral TFP (panel A) and measured intermediates and investment bundling TFP (panels B and C) for each sector (in logs). Given that sectoral TFP is calibrated to match relative price data, it is unsurprising that growth in sectoral TFP follows nearly the opposite ranking of growth in each sector's observed prices in panel A of Figure 3. That said, there are some notable differences between these series and observed price dynamics. For example, because services sectors use much larger shares of services intermediates whose prices have been rising rapidly, the underlying technology growth in services sectors is faster than what is observed from relative prices alone. This explains why TFP in services investment grows significantly faster than in goods consumption, despite the two sectors showing very similar price patterns. This highlights the importance of accounting for underlying production networks in accurately identifying sectoral TFP growth.

On average, intermediates and investment bundling TFP growth is low (0.3% and -0.2% a year,

Figure 6: Model Calibration Fit to Structural Change Patterns in Consumption, Intermediates and Investment, 1947-2020



Notes: The figures plot the fraction of total spending on consumption, intermediates, and investment produced by the goods sector (blue lines) and the services sector (red lines). Data series are solid lines; model series are dashed lines.

respectively, averaged across sectors). As we show in our growth accounting exercises below, these series play only a minor role in generating economic growth in the postwar period.

5.4. Structural Change

We next solve for aggregate structural change along the transition path and present the model's fit to patterns of structural change in consumption, investment, and intermediates in Figure 6; we report the model's fit for the ratio of real consumption in goods and services and for structural change within each of our six sectors in Appendix E.³² Overall, the calibrated model provides a good fit to patterns of structural change, though a couple of comments are warranted. First, given that we abstract from adjustment costs and uncertainty about the future price of investment, it is not surprising that, while the model matches long-run structural change in investment, it does not generate some of the short and medium-run fluctuations observed in the data.³³

³²In our model, all sectoral production technologies are Cobb-Douglas, implying a constant share of spending on intermediate inputs over time. For consistency, the data series for aggregate structural change in each of our six sectors in Figure 6 is constructed with the assumption of a constant share of intermediates spending within sectors. Specifically, aggregation weights are given by the product of gross output and the average ratio of intermediates spending to gross output. This generates slightly different patterns of structural change than seen in Figure 2.

³³As noted in vom Lehn and Winberry (2022), introducing an investment network into a multi-sector growth model tends to generate a counterfactually volatile distribution of investment expenditures. In our framework, this volatility interacts with heterogeneity in each sector's share of investment purchased from goods to generate volatility in the aggregate structural change in investment. Since we are interested in the trend behavior of structural change, we present aggregate structural change in investment with a smoothed share of investment expenditures by each sector to mitigate this volatility. Alternatively, we obtain similar results if we smooth all TFP series and calibration targets. Given our interest in long-run outcomes, our subsequent results are not substantively affected by either this short-run volatility or the alternative of smoothing all driving forces fed into the model.

Second, the model reproduces 70% of the rising share of intermediates produced by services. The model fit is even stronger before 2008, explaining more than 80% of the overall increase, but fails to capture a substantial portion of the increased share of services intermediates thereafter. However, despite the imperfect aggregate fit to intermediates structural change, we show in [Appendix E](#) that the model results reproduce the contribution of within-sector and between-sector forces to structural change in intermediates. One possibility is that the imperfect fit of the model may reflect data limitations or additional heterogeneity in intermediates prices beyond what we can observe in the data. Given the challenges in measuring intermediates prices, the model does a good job of capturing the overall pattern of structural change in intermediates.

6. Growth Accounting along the Transition Path

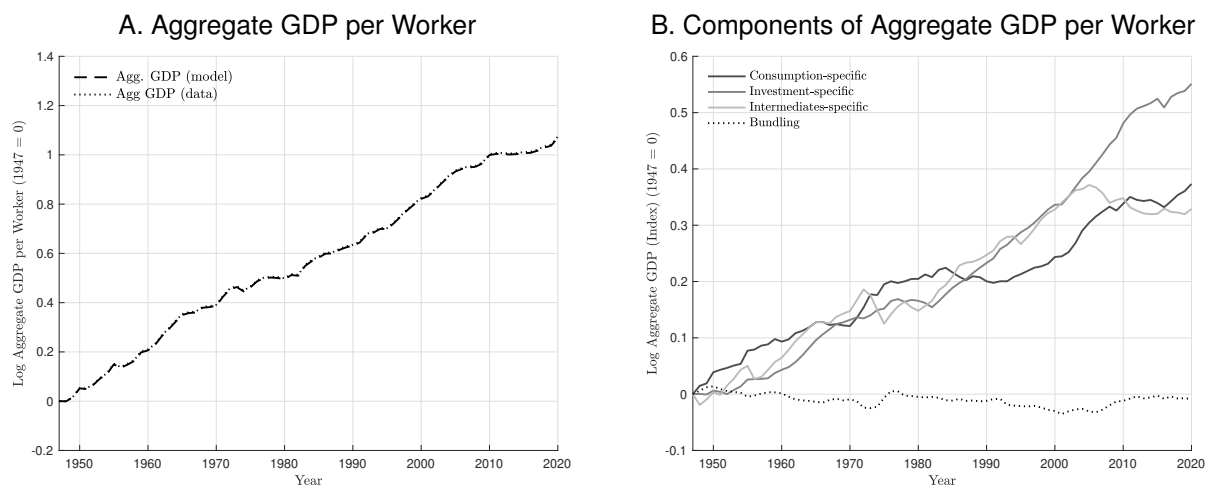
We now conduct two sets of growth accounting exercises along the transition path of our model. First, we decompose the historical growth rate of aggregate GDP for the U.S. into growth generated by consumption-specific, investment-specific, and intermediates-specific technical change. We also analyze counterfactual transition paths with no structural change in consumption, intermediates, or investment to assess the role of structural change in generating economic growth over time. Second, we consider projections of U.S. economic growth based on different scenarios of structural change. One important purpose of these projections is to investigate the extent to which substitutability in investment inputs may reduce projected future growth slowdowns related to [Baumol's \(1967\)](#) cost disease.

6.1. *Decomposing Historical Growth*

From the transition path, we compute the time series for aggregate GDP as a Tornqvist index, Y_t ; this is identical to aggregate GDP per worker in our model since labor supply is fixed in unit supply.³⁴ The left panel of [Figure 7](#) plots the log of aggregate GDP per worker in the model and the data (normalized to 0 in 1947); given our calibration strategy, these match exactly. GDP per worker grows at a fairly steady rate over most of the sample but shows a pronounced slowdown since 2010.

³⁴The U.S. national accounting system uses a Fisher ideal index number instead of a Tornqvist index; however, our model is calibrated to match GDP per worker measured using the latter. The two indices produce nearly identical results for U.S. data.

Figure 7: Aggregate GDP per Worker Growth and its Composition, 1947-2020



Notes: Panel A shows the time series of aggregate GDP per worker in the model and in the data, both measured in logs (normalized to zero in 1947); panel B shows counterfactual evolutions of aggregate GDP per worker for four cases: (1) only TFP growth among consumption producers (“Consumption-specific”), (2) only TFP growth among investment producers and in investment-bundling (“Investment-specific”), (3) only TFP at intermediates producers and from intermediates bundling technical change (“Intermediates-specific”), and (4) only TFP growth in investment bundling and intermediates bundling (“Bundling”).

Panel B of Figure 7 shows four counterfactual series for the log of GDP per worker based on transition paths where only a subset of TFP series grow. First, we allow only TFP growth in goods-consumption and services-consumption (“consumption-specific technical change”), holding all other TFP series fixed at their initial values. Second, we allow only TFP growth in goods-investment and services-investment sectors, as well as in investment bundling TFP (“investment-specific technical change”). Third, we allow only TFP growth in the goods-intermediates and services-intermediates sectors, as well as in intermediates bundling (“intermediates-specific technical change”). Finally, we construct GDP per worker only using investment and intermediates bundling TFP. These bundling TFP series are already included in investment- and intermediates-specific technical change, but we consider them separately to illustrate their limited contribution to overall growth. Table 2 presents the corresponding numerical growth decomposition both for the entire sample and for three (approximately) twenty-year intervals beginning in 1960; decadal numbers beginning in 1950 are in Appendix E.

Based on this decomposition of GDP growth, we make three observations about the sources of aggregate GDP growth. First, all three sources of technical change – consumption, investment, and intermediates – significantly contribute to aggregate growth. From Table 2, over the entire sample

Table 2: GDP Growth Decomposition, 1947-2019

| Sources of GDP Growth | Aggregate GDP per Worker Growth: $\Delta \ln(Y_t)$ | | | | | | | |
|------------------------|--|-----|--------------|-----|--------------|-----|--------------|-----|
| | 1947-2019 | | 1960-1980 | | 1980-2000 | | 2000-2019 | |
| | $\Delta \ln$ | % | $\Delta \ln$ | % | $\Delta \ln$ | % | $\Delta \ln$ | % |
| All | 1.04 | 100 | 0.29 | 100 | 0.33 | 100 | 0.22 | 100 |
| Investment-Specific | 0.54 | 52 | 0.12 | 43 | 0.17 | 52 | 0.20 | 94 |
| Intermediates-Specific | 0.32 | 31 | 0.08 | 29 | 0.18 | 55 | -0.01 | -4 |
| Consumption-Specific | 0.36 | 35 | 0.11 | 39 | 0.04 | 12 | 0.12 | 54 |
| Bundling | -0.01 | -1 | -0.01 | -2 | -0.03 | -8 | 0.02 | 11 |

Notes: The table shows long-run log changes in aggregate GDP per worker across different periods for five alternative simulations: (1) the full model simulation with all measured TFP series (calibrated to match the data exactly) and counterfactual simulations with TFP growth only from (2) investment producers and exogenous investment-bundling TFP ("investment-specific technical change"), (3) intermediates producers and exogenous intermediates-bundling TFP ("intermediates-specific technical change"), (4) consumption producers ("consumption-specific technical change"), and (5) both investment-bundling and intermediates-bundling TFP. Counterfactual changes are expressed as a percent of the change from the full model; these may not exactly sum to 1, given the nonlinear relationships between individual technology series and the aggregates. Furthermore, the bundling TFP series are already included in the investment- and intermediates-specific technical change counterfactuals, so adding their percentage contribution will overstate total growth.

of 1947-2019, consumption-specific technical change accounts for 35%, investment-specific technical change accounts for 52%, and intermediates-specific technical change accounts for 31% of aggregate GDP growth.³⁵

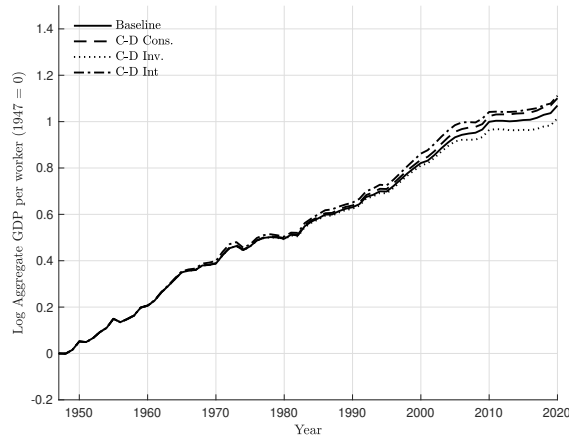
Second, for most of the sample, technical change in investment and intermediates bundling contributes very little to aggregate GDP growth; Table 2 shows that this source of technical change contributes almost nothing to total growth since 1947. However, it has recently become more important, accounting for 11% of GDP growth since 2000, although this is partly offset by accounting for -8% of GDP growth from 1980-2000. In Appendix E, we separately decompose the contribution of intermediates and investment bundling TFP, and find that intermediates bundling is slightly more important.

Third, the importance of investment-specific technical change is rising over time. Table 2 shows that this source of technical change accounts for 43% of aggregate growth during 1960–1980, 52% during 1980–2000, and 94% during 2000–2019. Furthermore, Figure 7 and Table 2 highlight that intermediates-specific technical change stagnates and even declines after 2000.

As discussed in Section 4.4, the rising importance of investment-specific technical change could reflect either changing TFP growth rates or the endogenous reallocation of resources across sectors.

³⁵Because of model nonlinearities, these contributions sum to more than 100%.

Figure 8: Aggregate GDP Growth, Cobb-Douglas Counterfactuals, 1947-2020



Notes: This figure shows GDP growth for the baseline transition path of the model and three counterfactuals – where consumption, investment, or intermediates aggregation is assumed to be Cobb-Douglas in place of CES. In each simulation, the same TFP series are fed in, but the Cobb-Douglas assumption shuts down structural change in either consumption, investment, or intermediates.

Table 3: GDP Growth, Cobb-Douglas Counterfactuals, 1947-2019

| Sources of GDP Growth | GDP Growth: $\Delta \ln Y_t$ | | | | | | | |
|----------------------------|------------------------------|-----|--------------|-----|--------------|-----|--------------|-----|
| | 1947-2019 | | 1960-1980 | | 1980-2000 | | 2000-2019 | |
| | $\Delta \ln$ | % | $\Delta \ln$ | % | $\Delta \ln$ | % | $\Delta \ln$ | % |
| Baseline | 1.04 | 100 | 0.29 | 100 | 0.33 | 100 | 0.22 | 100 |
| Investment Cobb-Douglas | 0.98 | 95 | 0.29 | 99 | 0.32 | 98 | 0.17 | 80 |
| Intermediates Cobb-Douglas | 1.08 | 104 | 0.30 | 103 | 0.36 | 110 | 0.22 | 100 |
| Consumption Cobb-Douglas | 1.07 | 103 | 0.29 | 101 | 0.34 | 103 | 0.23 | 109 |

Notes: The table reports log changes in aggregate GDP per worker, $\ln(Y_t)$, across different periods under different assumptions regarding CES bundling technologies. The table reports counterfactuals for the cases where consumption, investment, or intermediates aggregation is Cobb-Douglas, ruling out structural change in that commodity. For each period, we show the long-run log change and the portion of aggregate growth accounted for by the counterfactual simulation in percent.

To explore the importance of endogenous reallocation, we consider counterfactuals where we use all calibrated TFP series, but solve the transition path assuming one of consumption, investment, or intermediates bundling technologies is Cobb-Douglas. This assumption rules out structural change in that use. Figure 8 presents the counterfactual aggregate GDP series, and Table 3 reports the contribution of reallocation forces to aggregate GDP growth (100% minus the percent contributions reported in the second column of each panel in the table).

As expected, when the aggregation of investment inputs is Cobb-Douglas, growth is lower, as resources no longer reallocate to the fastest growing producer of investment. Over the entire

sample, Cobb-Douglas investment aggregation implies 5% lower total growth in GDP per worker, but this effect is much larger since 2000, where growth is 20% lower. When either intermediates or consumption is Cobb-Douglas, growth is faster, as resources no longer reallocate toward the slowest growing producer. Over the entire sample, the effect of complementarity in aggregation in either of these products is to reduce GDP growth by about 3-5%, though the effect attributable to consumption since 2000 is 9%.

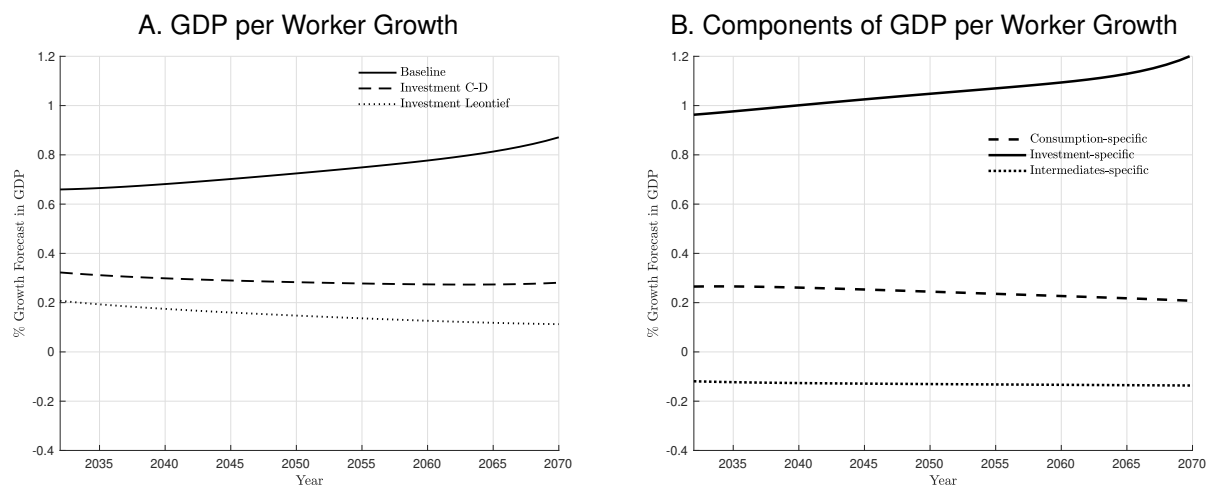
These findings lead us to three observations about U.S. economic growth and its recent slowdown. First, investment-specific technical change is an increasingly important force in generating economic growth and structural change in investment has played a substantial role in driving that growth since 2000. Second, structural change in consumption and intermediates has exerted a modest drag on aggregate growth, and the drag from consumption has been larger since 2000. Finally, intermediates-specific technical change has stagnated, with a negative total contribution to growth since 2000, and appears to be a significant contributor to the recent slowdown in economic growth. Thus, although significant attention has been paid to bottlenecks in supply chains since the COVID-19 pandemic, we find substantial sluggishness along this network in the years preceding the pandemic.

6.2. GDP Growth Forecasting and Baumol's Cost Disease

A long-standing concern with structural change, going back at least to [Baumol \(1967\)](#), is that if resources reallocate to the slowest growing producers in an economy, economic growth will stagnate. In our model, strong complementarity between goods and services as inputs for producing consumption and intermediates implies that structural change in these sectors reduces economic growth. However, our finding of substitutability for goods and services as inputs in investment production has the opposite effect: structural change in this sector boosts economic growth. To assess the relative strength of these forces, we analyze our model's predictions for future economic growth under a variety of scenarios.

To forecast future growth, we assume that all TFP series grow at a constant rate from 2021-2070 along the transition path, with growth rates determined by the average growth in each series from 2010-2020. This latter period of the transition path provides a meaningful window into concerns about Baumol-style stagnation, as constant growth in each TFP series implies that changes in

Figure 9: GDP Growth Forecasts and Counterfactuals, 2032-2070



Notes: Panel A shows the annual growth rate (in %) of aggregate GDP per worker in the model simulation from 2032-2070, where all TFP series grow at a constant rate; panel B shows counterfactual evolutions of the growth rate of GDP per worker over this period for three cases: (1) only TFP growth among consumption producers ("Consumption-specific"), (2) only TFP growth among investment producers and in investment-bundling ("Investment-specific"), and (3) only TFP growth in intermediates, both at intermediates producers and from intermediates bundling technical change ("Intermediates-specific"). Panel A also includes counterfactual GDP growth forecasts for the case where investment aggregation in each sector is Cobb-Douglas and where investment aggregation in each sector is Leontief.

aggregate growth primarily reflect the effect of ongoing structural change in the economy. To further focus on the limiting growth dynamics implied by the CES technologies, we discard the first 10 years of this window, in which GDP per worker growth partially reflects delayed capital accumulation dynamics from changes in TFP observed during the end of our data window.

In Panel A of Figure 9, we plot the predicted annual growth rate (in percent) of GDP per worker from 2032 to 2070 (solid line). Growth in GDP per worker is low in our forecast, starting at 0.66%, reflecting the low observed growth in sectoral TFP from 2010-2020. However, the figure shows that GDP gradually accelerates from 2032 to 2070, rising to 0.87% in 2070.

Panel B illustrates the channels underlying this growth forecast by plotting the growth rate of GDP per worker in counterfactual transition paths where we allow for TFP growth only for consumption producers, investment producers (and bundling technologies), or intermediates producers (and bundling technologies). Consistent with Baumol's cost disease, we see that when TFP growth occurs only in consumption or intermediates, aggregate growth is slowing over time, with reallocation to the slowest growing producers.³⁶ However, because of substitutable inputs in investment,

³⁶In the case of intermediates, the slowing is less pronounced because from 2010-2020, TFP growth in goods-

when there is only TFP growth at investment producers, growth is rising over time.

Finally, panel A of Figure 9 also presents counterfactual scenarios where the elasticity of substitution in investment inputs is set to either 1 (Cobb-Douglas) or 0 (Leontief)—assumptions commonly made in the literature. Consistent with Proposition 2, with a lower elasticity of substitution, aggregate growth is substantially lower and declining over time. These counterfactuals demonstrate the strength of Baumol’s cost disease in standard growth models. Our baseline simulation, which shows rising aggregate growth in GDP per worker, reveals that investment reallocation serves as a critical counterbalance to the forces driving long-run stagnation from Baumol’s cost disease. This mechanism appears sufficient to fully offset the growth drag caused by structural change in consumption and intermediate production.

7. Conclusion

We document that services sectors have produced a larger share of both intermediates and investment over time. To understand these patterns, we develop a framework that allows us to study structural change in both consumption and production networks. Explicitly modeling intermediates allows us to use expenditure-side prices on final commodities, rather than income-side sectoral gross output prices, to discipline the model in a way that is internally consistent (as discussed by Herrendorf et al., 2014). Using novel price series disaggregated by both sector and final use, we find that goods and services are substitutes in the production of investment, rather than complements, as found in previous studies. We show that aggregation bias accounts for differences in these findings, with expenditure-side prices able to capture price growth in the production of investment that is easily averaged out in gross output prices.

This finding relates to a concern of Baumol (1967)—that structural change leads to a systematic reallocation from productive/innovative goods sectors to less innovative services sectors, eventually leading to an economy where the least productive sector dictates all economic progress. While the intermediates network in our framework does indeed appear to suffer from Baumol’s “cost disease”, we find the investment network to be the primary engine of growth in part because it is systematically shifting toward the most productive services (e.g., software development and R&D). Our findings thus provide some optimism for the impact of sectoral reallocation on aggregate eco-

intermediates and services-intermediates is very similar (and negative).

conomic growth.

Data Availability Statement

All data and computer code necessary to reproduce all figures and tables in this manuscript are provided in a replication package available at <https://doi.org/10.5281/zenodo.18780294>.

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Appendix A. Data Sources and Details for Production Networks and Price Measurement

Appendix A.1. Measuring Production Networks

Our primary data source for measuring production networks and related data is the BEA Input-Output (IO) database, especially the time series of Make and Use tables from 1947-2020 and the time series of the investment network generated by vom Lehn and Winberry (2022) (henceforth *vLW*).³⁷ These data cover 40 NAICS-defined economic sectors, including agriculture and government (43 if energy-intensive sectors are included); Table A.1 lists the 40 sectors and corresponding NAICS codes. More recent vintages of the IO database allow for greater sectoral detail, allowing the construction of more detailed investment networks. Given our interest in structural change over the long run, we focus on data for 40 sectors that are consistently defined for the entire sample of 1947-2020.

The core of the Use table is a square matrix that reports intermediate input expenditures by different sectors (organized along columns) on specific commodities (organized along rows). These commodities are named and assigned NAICS codes based on which sectors are major producers of the given commodity, but more than one sector may be involved in the production of a given commodity. The mix of sectors that produce a given amount of each commodity is observed in the Make table, which is a square matrix reporting commodities along columns and the amounts of each commodity produced by each sector along rows. The final input-output matrix in each year is the matrix product of a scaled Make table, where each column is scaled by its sum (thus summing to 1) and the unscaled Use table.

The data from *vLW* reports the matrix of sectoral spending and production of new investment. Following their procedures, we extend the investment network data through 2020. Since *vLW*'s investment matrix reports commodities rather than sectors in each row, we adjust their data using the Make matrix. Our final investment network is represented by the product of the scaled Make matrix and the unscaled, extended investment network from *vLW* for 1947-2020.

For reference, we provide an illustration of the average structure of production networks in the United States from 1947-2020. For visualization, it is convenient to present scaled versions of

³⁷Data are available at <https://www.bea.gov/industry/input-output-accounts-data> and <https://doi.org/10.7910/DVN/CALDHX>.

Table A.1: Average Share of Intermediates and Investment Production: Avg. 1947-2019

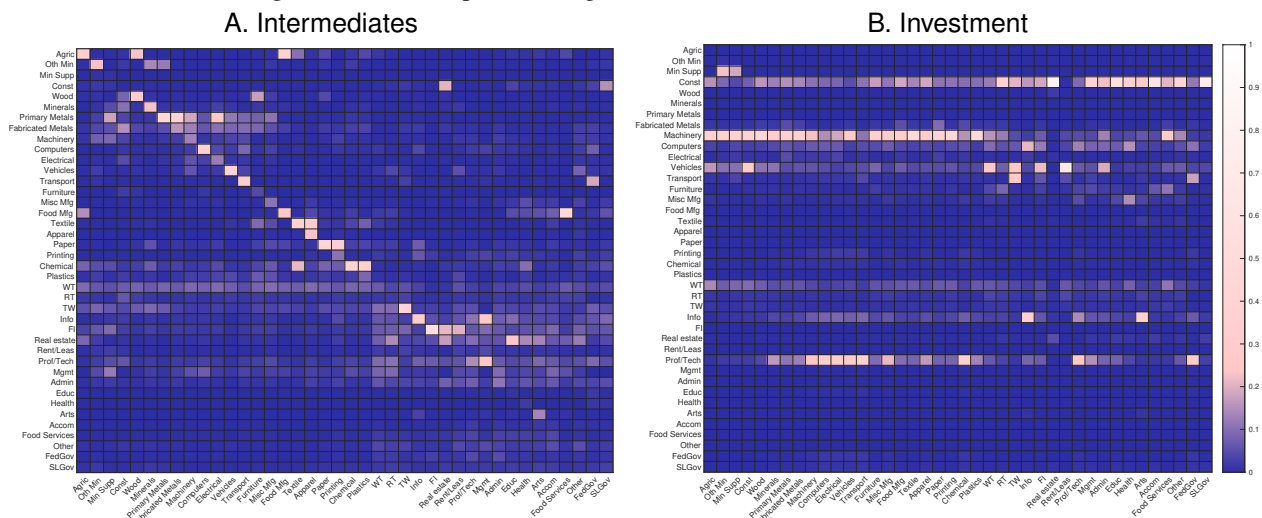
| Goods Sectors (NAICS Codes) | % of Prod. | | Services Sectors (NAICS Codes) | % of Prod. | |
|---|------------|------|--|------------|------|
| | Int. | Inv. | | Int. | Inv. |
| Agriculture, forestry, fishing and hunting (11) | 5.2 | 0.0 | Wholesale trade (42) | 5.4 | 3.7 |
| Mining, except oil and gas (212) | 1.2 | 0.3 | Retail trade (44-45) | 1.8 | 1.3 |
| Support activities for mining (213) | 0.1 | 2.0 | Transport and warehousing (48-49, minus 491) | 5.5 | 0.9 |
| Construction (23) | 1.7 | 36.2 | Information (51) | 4.2 | 5.8 |
| Wood products (321) | 1.3 | 0.5 | Finance and insurance (52) | 7.1 | 0.1 |
| Non-metallic mineral products (327) | 1.5 | 0.1 | Real estate (531) | 4.4 | 1.7 |
| Primary metals (331) | 4.4 | 0.1 | Rental and leasing services (532-533) | 1.2 | 0.0 |
| Fabricated metal products (332) | 3.8 | 1.2 | Professional and technical services (54) | 4.9 | 9.7 |
| Machinery (333) | 1.6 | 8.7 | Management of companies and enterprises (55) | 2.8 | 0.1 |
| Computer and electronic products (334) | 2.2 | 6.5 | Administrative support and waste services (56) | 3.1 | 0.1 |
| Electrical equipment manufacturing (335) | 1.1 | 1.3 | Educational services (61) | 0.2 | 0.2 |
| Motor vehicles manufacturing (3361-3363) | 3.0 | 8.7 | Health services (62) | 0.2 | 0.1 |
| Other transportation equipment (3364-3369) | 1.4 | 4.4 | Arts, entertainment and recreation services (71) | 0.4 | 0.1 |
| Furniture and related manufacturing (337) | 0.3 | 1.1 | Accommodation services (721) | 0.5 | 0.0 |
| Misc. manufacturing (339) | 0.8 | 1.2 | Food services (722) | 0.9 | 0.0 |
| Food and beverage manufacturing (311-312) | 4.4 | 0.1 | Other private services (81) | 1.5 | 0.1 |
| Textile manufacturing (313-314) | 1.8 | 0.3 | Federal government (n/a, but incl. 491) | 1.0 | 0.5 |
| Apparel manufacturing (315-316) | 0.6 | 0.0 | State and local government (n/a) | 1.3 | 0.8 |
| Paper manufacturing (322) | 2.3 | 0.0 | | | |
| Printing products manufacturing (323) | 1.1 | 0.5 | | | |
| Chemical manufacturing (325) | 4.2 | 0.4 | | | |
| Plastics and rubber products (326) | 1.6 | 0.1 | | | |

Notes: The table reports the average share of total intermediate and investment production by 40 consistent sectors. Individual components may not exactly sum to totals due to rounding. Sectors are classified according to the NAICS-based BEA codes, with 2007 NAICS codes in parentheses. Government sectors as defined by the BEA do not have naturally corresponding NAICS codes.

the two networks, with elements s_{ijt}^M and s_{ijt}^X representing sector j 's share of total expenditures on intermediates (M) or investment (X) made by sector i in year t .

Figure A.1 plots heatmaps of the scaled input-output network (panel A) and the scaled investment network (panel B), averaged over the entire sample period. These heatmaps show the sparsity of both the input-output and investment networks; for any given sector, the majority of investment and intermediates are purchased from a small set of sectors. For the investment network, the distribution of investment producers is fairly similar across sectors. Most sectors purchase investment goods from a collection of prominent investment hubs—construction (structures), machinery and vehicles manufacturing (equipment), and information and professional/technical services (intellectual property). However, for the input-output network, there is much more sector-specificity as to which sectors are important suppliers of intermediates. In particular, we observe significant homophily in the input-output network—goods sectors play a large role as intermediates suppliers for goods sectors and services sectors play a large role as intermediates suppliers for services sectors.

Figure A.1: Heatmaps of Average Scaled Production Networks, 1947-2020



Notes: Panel A shows the scaled input-output network for intermediate goods; panel B shows the scaled investment network for new capital goods. Each (i, j) element shows the fraction of total expenditure by sector j (columns) from producing sector i (rows).

The BEA Use tables also contain data on the final uses of each commodity, including consumption. We measure structural change in consumption by constructing final consumption produced by each sector as the product of the scaled Make matrix and the sum of private final consumption and government consumption vectors in the Use table. While the Use table has information on the final use of each commodity as new investment, we use sums of the data from the investment network to compute total production of investment by each sector.

Appendix A.2. Data Sources for Price Measurement

We measure the price of consumption and the price of investment produced by goods and services sectors using expenditure-side accounting data. We start with final expenditure data (prices and total expenditures) for 68 consumption commodities (NIPA Tables 2.4.4 and 2.4.5) and 30 investment commodities (NIPA Tables 5.3.4, 5.3.5, 5.5.4, 5.5.5, 5.6.4). The 68 consumption commodities are the finest disaggregation available for the postwar period (after omitting commodities produced primarily by the energy-intensive sectors omitted from our analysis: motor vehicle fuels, fuel oils and other fuels, water supply and sanitation services, electricity, and natural gas). The 30 investment commodities (2 structures, 24 equipment, 3 intellectual property, and residential commodities) are a subset of the 33 investment commodities used in [vLW](#). Due to data limitations,

primarily on detailed investment prices not studied by vLW, we combine light trucks and other trucks into a single commodity, all software into a single commodity, and residential structures and residential equipment into a single commodity.³⁸

With this mapping, we measure price growth for goods-consumption, services-consumption, goods-investment, and services-investment as a Tornqvist index as described in Section 3. The weights in that index depend on the sector's production share for each commodity, constructed from the BEA's published bridge files for consumption commodities³⁹ and the bridge files constructed by vLW, which we extend forward through the year 2020 using the latest BEA bridge files for investment. Both of these bridge files are multiplied by the scaled Make file. Since we focus primarily on the differences between goods and services production, we aggregate the final bridge files to two sectors, goods and services (as defined in Table A.1).

We also modify the bridge files for investment from vLW by assuming that goods produce the entirety of structures (including residential investment). In the original bridge files from vLW, a small fraction of structures (roughly 7% of non-mining structures and 11% of residential investment) is produced by services, primarily margin contributions from sectors like real estate and finance. However, because overall investment production by services is low compared to goods, especially early in the sample (as seen in Figure 2) and because investment spending on structures is large, absent any adjustment, a sizable portion of the services investment price is determined by structures prices, although the amount of total services investment production coming from structures is falling over time, from 1/3 in 1947 to less than 10% by 2020. This is unappealing because 1) it is unlikely that the price of structures investment reflects the price of these margins and 2) because the exact contribution of these services margins is determined in part by imputation (see Appendix A of vLW for further details). Thus, we set the services contribution to the production of structures equal to zero in our final bridge files. However, even without this adjustment, Appendix C documents that services investment prices are still significantly decreasing relative to

³⁸The 33 investment commodities in vLW are approximately the finest level of disaggregation of investment commodities possible while accurately tracking each commodity's production by different sectors over time. It is possible to study patterns in more finely disaggregated non-mining structures, but the mix of sectors producing these structures is the same for each commodity. Thus, further disaggregation does not yield additional insight. For this case, we aggregate prices for detailed structures to a single investment price for non-mining structures using a Tornqvist index.

³⁹Available at <https://www.bea.gov/products/industry-economic-accounts/underlying-estimates>

goods.

We measure intermediates prices using the procedure described in Section 3. Gross output prices by sector are implicitly an average of the price of all commodities produced by that sector. Thus, using the price of consumption and investment produced by goods or services, we identify the price of intermediates produced by goods or services as the residual in gross output prices.

For all prices, we make adjustments for the exclusion of oil/gas prices; these adjustments are described in [Appendix C](#).