Don't bet on economic forecasting

You can't predict the future. Commentator Justin Wolfers believes economists shouldn't be trusted to either.

TEXT OF STORY

KAI RYSSDAL: If you really think about it, what the Fed's trying to do when it meets to set interest rates is an amazingly complicated thing: Tease out what a $14 trillion economy's going to look like six months or a year from now, and then apply the right policy.

Commentator and economist Justin Wolfers says forecasting the economic future truly is a dark science.

JUSTIN WOLFERS: Economists and meteorologists know that forecasting is hard. But when we get it wrong, we just get wet. When economists get it wrong, we get the Great Recession. And so in the past decade developing a new generation of models.

But two young researchers have raised big questions for this research program. They compared state-of-the-art models and elite forecasters. What did they find? All the leading approaches Translation: Our forecasts of GDP, inflation and interest rates have been way off.

Here's a neat way of thinking about how badly these models fail. If in 1997, you'd trained a parrot that if you asked him what inflation will be 3.5 percent, and interest rates won't change," then your parrot would have done as well as those Ph.D-toting economists hired by the Fed to get a salary.
Academic economists thought we were smarter than your parrot. We've trumpeted progress wait for it -- "Dynamic Stochastic General Equilibrium models." They're not just a mouthful decade of intense research. But if you ask these models to predict the future, they're no better.

Now, statisticians don't pretend to understand the economy, they just crunch the numbers. I worse.

Perhaps you trust people instead of computers. But the Fed's economists were no better. At private sector, you really shouldn't. Their prognostications were also dismal.

Now, you probably knew that most economists failed to predict the 2007 recession. What's Recession arrived, our complicated models failed to recognize the new reality.

Bob Dylan sung it best: "You don't need a weatherman/To know which way the wind blow:

And according to this new research, you don't need an economist to know which way the economic winds are blowing.

**KAI RYSSDAL:** Justin Wolfers is a professor of business and public policy at the Wharton University of Pennsylvania.
09/22/2010

PLEASE!! I wish that APM would post a link, a reference, even a googleable hint of where this 'study' was performed. In just the FACTS...."

By M.J. Dicere
09/22/2010

Me too! Reference please.

By max mass
09/22/2010

Reference please!

By bhupen K
09/21/2010

I would also like the link to the material reference in this commentary.

Long term forecast are always unreliable and because no one can accurately predict the future, they are just best guess

Nothing can be inferred from this commentary. Predicting the future is always an imperfect science and no one should e

However the important thing about planning is that we have to start somewhere and hence we must have some foreca: point and we adjust from there. Hence the forecast.

By D Ferman
From KS, 09/21/2010

Sounds somewhat like Gideon Rachman (and Professor Niall Ferguson, neither exactly young) in the Financial Times, FT on Sept. 6, 2010.

By George McKee
From Cypress, TX, 09/21/2010

Testing predictions against reality has been a fundamental principle of science for 400 years. It's about time that econo philosophical blinders and begins to face its actual skill at dealing with the real world, however poor that skill might be. need to make this review an annual exercise, updating it with the latest versions of each model.

By James Wick
From Martin, TN, 09/21/2010

Have my own forecast method for the econ., trends in fruit tree sales. In the mid 1860's there was a surge in fruit tree sales (Depression) this repeated in early 1920 (10 years prior to Great Depression) and wholesale producers sold out of stock rocketed about 5 years ago.... forecast, we are at least 4 years away from any major improvement and likely to worsen

By Ken Schulz
From Bethel, CT, 09/21/2010

Another listener who would like a reference to the study to which Prof. Wolfers refers...

By Jonathan Lovelace
From Milan, MI, 09/21/2010

The thing about meteorology is that *short-range* weather forecasting is actually quite accurate. It's the long-range forecast you'd expect from a basic understanding of statistics. But there's another difference between short-range weather models and economic forecasting: daily weather forecasts are based almost entirely on actual data, whereas climatic assumptions, often without regard to whether those assumptions bear any resemblance to reality, especially in academ

By J.R. Gaines
09/21/2010

Can you give me a link to the research being reported? I would like to read the full text.

Thanks,

J.R.

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