

June 25, 2009

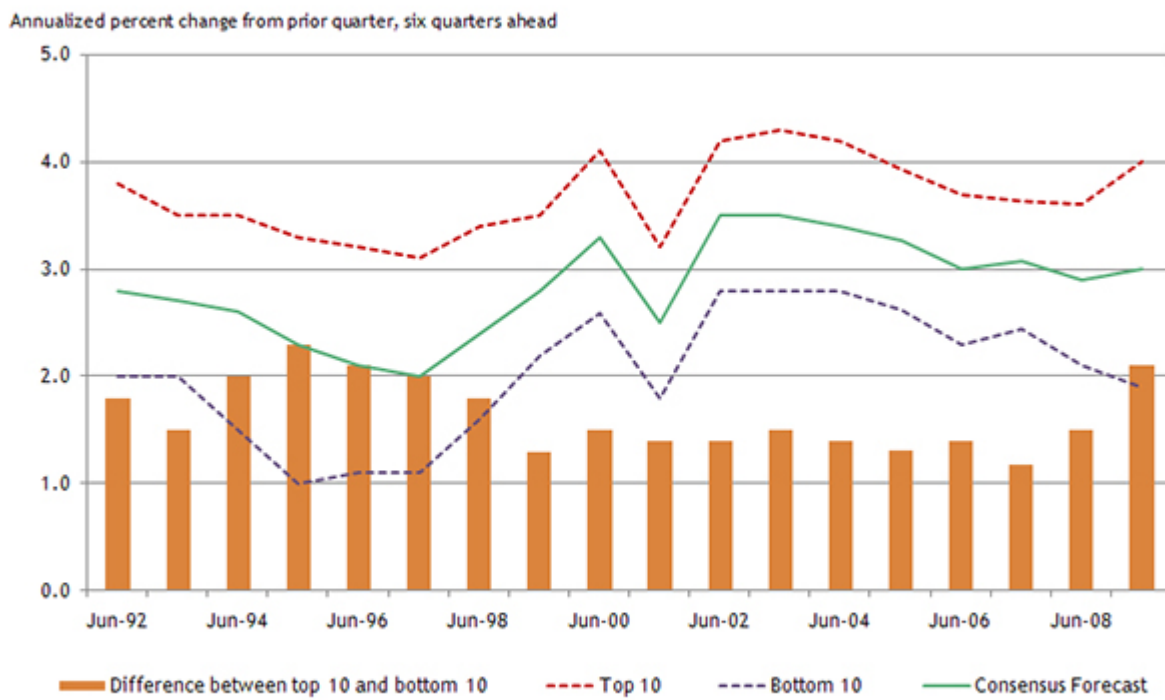
Private sector forecasts at variance

Economic forecasts are notoriously inaccurate. That isn't a statement about the ability of forecasters, but rather a statement about the complexity of the economy. If you're looking for a humbling experience, I recommend you give it a try.

And today's economy would seem to be an exceptionally difficult environment in which to forecast. As economists peer into the future, there seems to be an unusually wide range of opinion about what to expect. Uncertainty is running pretty high right now in the minds of the top prognosticators.

Consider the following predictions from the Blue Chip panel of economists concerning the economy's growth rate a year and a half from now (fourth quarter 2010). The average growth rate expected in that time frame from the panel is 3 percent, which isn't that different from the six-quarter-ahead forecast they have made every June during the past 10 years or so. But if you compare the difference between the economic optimists (the 10 highest growth forecasts) relative to the economic pessimists (the 10 lowest growth forecasts), the discrepancy between the two views is large relative to recent history. In short, the forecasts on the optimistic end of the spectrum are now more optimistic while the pessimistic forecasts are a little more pessimistic.

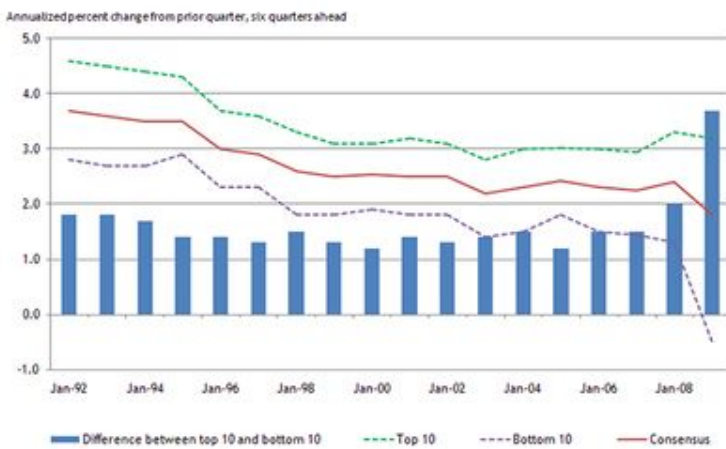
Blue Chip Real GDP Forecasts



Source: Blue Chip Economic Indicators, June 1992-2009

Uncertainty over the medium-term outlook is particularly large regarding the experts' views on inflation. In the latest survey of the Blue Chip panel, the difference between the 10 highest and the 10 lowest inflation predictions for the fourth quarter of 2010 was a gaping 3.7 percentage points (compared with an average of about 1.5 percentage points over the past decade and a half). This wide range of opinions about inflation prospects started to emerge last year as economic conditions deteriorated.

Blue Chip CPI Forecasts



Source: Blue Chip Economic Indicators, June 1990-2009

Disharmony in the panel's inflation outlook doesn't so much suggest that those expecting inflation now see greater inflationary risks—at 3.2 percent the medium-term inflation prediction of the highest 10 inflation forecasts isn't materially different from where it has been since the late 1990s. Instead, the larger variance in the inflation outlook is coming from those at the bottom of the panel's forecast distribution that are anticipating even more downward price pressure than in previous years.

Pinpointing the future trajectory of the economy is generally considered more difficult near turning points in the business cycle—though the current uncertainty would appear to be particularly large, recession or not. Such uncertainty about the future is surely adding to the challenges facing the business community as it strives to get back on its feet.

By Laurel Graefe, economic research analyst at the Federal Reserve Bank of Atlanta

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