

State of the ECONOMY

General Summary

10/24/2013

What is the state of the economy?

Goal: Forecast Indicators

GDP

CPI

Unemployment (15 weeks +)

Issues: Default Crisis

Adds uncertainty

Unprecedented threat

- How do we deal with the debt default threat?
 - Forecast using the underlying fundamentals of the economy.
 - See what would have happened “without crisis”.
- This will allow us to better anticipate true values after the adjustment period.
- Predictions are within 1 SD of the Fed’s consensus forecast.
- 2011 event was not well predicted.

Quarterly change of
GDP

+0.922%

(0.713%)

Quarterly change in
CPI

+0.381%

(0.568%)

Quarterly change in
Unemployment

-12.9% (becomes 4.1%)

(7.83%)

Standard errors in parentheses

Note that these are changes as a percentage of current value.

List of indicators used (12):

1. Industrial production,
2. Index of industrial manufacturing,
3. Consumer sentiment,
4. Total industrial capacity utilization,
5. Producer price index,
6. CPI
7. Federal Funds rate.
8. Personal income
9. GDP
10. Unemployment (15 weeks +)
11. Quarterly seasonal indicators (4)

- Some data is released very slowly. (-6 months)
 - Forecasts must be done far in advance.
- Low R^2 for GDP and CPI (0.07 and 0.017).
- Model lacks strong theoretical background.
 - “Kitchen sink approach”, large SE
 - Likely non-normal distribution of errors.
- Depends on data since 1980.
 - Is today like yesterday?

- Predictions are within 1 SD of the Fed's.
- Indicates general, but modest improvement in the economy.

UNEMP forecast

