

[Predictions are difficult...](#) [1]

Written by [Tim Worstall](#) [2] | Sunday 18 May 2008



...Especially about the future. Tim Harford points this out in his column in [the FT](#) [3]:

There is a simple reason why most economic forecasts are useless, which is that forecasting is hard. We don't fully understand the underlying economic processes that produce the results we wish to forecast (growth, inflation, house prices), nor can we measure all the variables accurately, nor anticipate the sudden shifts caused by politics or technological change.

Now that is fairly obvious, and it's why economists have predicted successfully nine of the last three recessions. It might also be why I pay so little attention to macroeconomics (no, it's not solely because I can't get my head around the mathematical models) and prefer to assume that if we get the microeconomics of the incentives that people face at least roughly right then things will pretty much work out OK.

There's a larger point there though: one that Hayek made repeatedly. We simply don't know enough about the economy to be able to plan it: if we can't even forecast growth or inflation, then how can we forecast sufficiently well to be able to plan anything else? The number of houses needed? The technological changes that are going to happen? The demand for sugar? It's simply not possible to do so thus we shouldn't even be trying.

Harford does point out that at least baby steps are being taken though. One major problem with the forecasts is that not only don't they anticipate changes called "structural breaks", a change in technology say which changes the necessary assumptions of the models. Not only do they not anticipate them (and thus make them useless) they fail to even recognise them when they have happened.

But even if structural breaks cannot be predicted, that is no excuse for nihilism. Hendry's methodology has already produced something worth having: the ability to spot structural breaks as they are happening. Even if Hendry cannot predict when the world will change, his computer-automated techniques can quickly spot the change after the fact.

This is an advance: at least we can now say why our model has failed to mimic the real world, even if only after the fact. No doubt in another century or two we'll be able to predict such structural breaks and at that point perhaps planning, perhaps even socialist calculation, might be possible.

So, until 2208 we seem to be stuck with the only useful calculation and planning method we've so far discovered, markets and their interactions. It's good to get these things sorted out for a few lifetimes at a time, isn't it?

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