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Risky business of New Year's forecasts

By [Richard W. Rahn](#) - - Monday, December 29, 2014

How many hurricanes do you think will hit the East Coast of the United States in 2015? Will the Arctic ice sheet disappear next year? How fast will the U.S. economy grow? What will the level of the Dow Jones stock index be at the end of 2015? Which team will win the World Series?

Go back and look at predictions made by the experts, and then look at what really happened. The climate alarmists 15 or so years ago were forecasting catastrophic events by this time. Yet sea levels have not been rising any faster than they have been for centuries. The major climate models were projecting steady rises in global warming each year, yet average temperatures have not risen for 17 years. Al Gore and his alarmist crowd told us that the Arctic would be free of sea ice during the summer by now and that we would be having more and stronger tornadoes and hurricanes. The Arctic sea ice is still with us, and few ships dare sail there. Many tornado and hurricane records have been broken — not because there were more — but because there have been fewer. Florida has gone a record nine straight seasons without a significant hurricane.

None of the above disproves climate change, but it should caution those who have made many rash predictions. The economist-philosopher F.A. Hayek warned about “the limits of knowledge” and the “fatal conceit” exhibited by so many “experts.” The communists and socialists claimed that they could allocate resources and income better than markets. These false claims ultimately destroyed the lives of tens of millions and caused untold human misery. Despite the never-ending failures of socialist and other collectivist schemes (such as Obamacare), colleges, governments and the media are still filled with smug — but ignorant or uncaring — individuals (think Jonathan Gruber) who still think they are smarter than markets, and thus have the self-appointed right to control your life.

Economists have little to crow about when it comes to forecasting. Most of them missed calling the Great Recession. The Federal Reserve, which employs hundreds of economists, many from the best schools, kept predicting 4 percent-plus economic growth each year, after the recession bottomed in 2009. In fact, actual growth has been about half of what they predicted — but perhaps 2015 will be the year of 4 percent growth. Too many of my fellow economists, including many of those in the administration, get things wrong, in part, because they still use Keynesian economic models that treat increases in government spending as a positive rather than a negative, among other errors.

To make an accurate forecast, one needs to know what the Fed will do in regard to monetary policy and what Congress and the administration will do in terms of taxing, spending and

regulation. One also needs to know what the economic policies of other countries will be — since the United States is not an island unto itself — and when wars and tsunamis will occur. The impossibility of knowing all of this does not mean that it is not useful to attempt to forecast, but merely that it is not scientific in the way that we can precisely predict the boiling point of water at a specific atmospheric pressure.

Forecasters need to have a good understanding of the major variables that might greatly affect their reasoning. The safest starting point for most forecasts is what happened in the previous period. Tomorrow's weather is likely to be similar to today's. One might begin an economic forecast by assuming next year is likely to look much like this year, then alter the forecast based on assumed changes in policy. For instance, if you assume the Republican-led Congress is likely to reduce government spending as a share of gross domestic product, and if you believe, as many of us do, that government spending (at the current high levels) is a drag on growth, then it is sensible to boost the growth estimate a bit — other things being equal. This same exercise needs to be repeated with each major variable — taxes, regulations, monetary actions, changes in oil prices — and what Russia's Vladimir Putin might do next.

The climate forecasters have even more variables and unknowns to deal with than do economists. We know that suddenly shutting down all of the world's coal-fired power plants would cause a global economic disaster — even though it might be marginally beneficial for the climate, unless an increase in sunspots negates the effect.

Forecasters in most disciplines have much to be modest about, and it is foolhardy to make radical changes either in public policy or in one's personal life based on pronouncements of the latest fashionable guru, the neighborhood fortune teller or the experts' forecast models. Happy new year.

Richard W. Rahn is a senior fellow at the Cato Institute and chairman of the Institute for Global Economic Growth.