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*With a degree in chemistry from Queens College, Oxford, David Ranson came to the U.S. in 1965. After earning an MBA and a Ph.D. from the University of Chicago, he has worked, taught and forecasted in finance and economics ever since.*

### **Is economic forecasting an art or a science?**

It should be a science, but it's actually an art. Science is disciplined and evidence-based decisionmaking. That's hard to find in forecasting. Forecasters are easily swayed by peer pressure and personal circumstances.

### **Give an example.**

The best-known forecasters today are employed by large financial organizations. When the finance sector is in turmoil, as it is at the moment, pessimism can sweep away objectivity. That's part of the reason why we're being told a recession is upon us.

### **How exact is economic forecasting today?**

In my thirty years of experience it seems less accurate than ever. In spite of the impressive paraphernalia of modern mathematical and statistical techniques, the economic data that forecasters rely on are arbitrary and questionable.

### **How so?**

The government publishes the data. It's often stale before it's published. Plus, it's backward-looking. Ironically, forecasters often neglect forward-looking data that financial markets offer. For example, prices in the financial markets are powerful leading indicators of inflation and economic growth. That is where exactitude is to be found.

### **What might make the Consumer Price Index more useful, and to whom?**

Officially the CPI is the authoritative measure of inflation, but it's a stark example of a backward-looking indicator. It may or may not be useful for the general public, but it's not what investors need to determine whether the economy has an inflation problem or not. Investors need information from prices that are generated in real time by markets.

### **Does the CPI do better with commodities than with services?**

Yes, much better — especially in embarrassing areas like food and energy.

### **Why is that?**

Commodities trade in centralized markets, and they are very well defined. So it's impossible to miss price changes when they occur. Markets for services, however, are decentralized, and the price of a service is hard to define. Inflation in services is often invisible.

### **How is housing included in the consumer price index?**

First, it's called 'shelter.' The government uses rental housing data to estimate the average homeowner's monthly cost of shelter. That's one of the more backward-looking indicators. Rents are set by contracts that often last for years, and they are infrequently adjusted.

### **Is a university professor's salary or a university's tuition price measured in the CPI?**

A professor's salary would not show up directly in the CPI. But it would belong in a Department of Labor wage index. The price of tuition does appear in the CPI as a service.

### **What are the consequences of making no change to inflation measurement techniques?**

Conventional indicators like the CPI give investors no warning when inflation turns upward. The prices of capital market assets respond more quickly than the government can report it. So investors who rely on government data constantly miss the boat. During an inflation, tangible assets like commercial real estate, precious metals and other commodities out-perform paper assets such as bonds, stocks and cash. This has been underway for at least four years. Large numbers of investors have missed out.

### **How might a university's investment manager use the CPI?**

Simply view the CPI as an untrustworthy lagging indicator. Only its commodity components provide timely data about inflation, and even they are fragmentary.

### **How might a university's pension and benefits manager use the CPI?**

Pensions, benefits, and sometimes salaries may be linked to this index. It may serve well enough to compensate employees for the rising cost of living.

*David Ranson regularly addresses audiences of mutual fund managers, pension fund managers, and he can be reached at [d.ranson@hcwe.com](mailto:d.ranson@hcwe.com)*

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