

Macro-Forecasting Under Business Cycle Fluctuations

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日 時 : November 8, 1995 (15:00-17:00)

場 所 : ERB-347

Recent developments in the theory and practice of macroeconometric modeling have contributed much to enhancing model's analytical performance by providing a more sophisticated and refined framework. In spite of the theoretical advances and state-of-the-art computer-intensive techniques, the macro model was often criticized by its poor forecasting performance, receiving sharp public attentions. Such frustrating experiences are frequently observed when an economy sends mixed signals of upswing and downswing on the current business condition, especially in the neighborhood of the turning point of a business cycle. Under this situation, a forecaster can not feel confident of direction of movements, let alone magnitude of predicted variables.

As Zarnowitz (1991) emphasized the importance of errors of missing cyclical turns and shifts in the average rate of inflation, failures to detect cyclical turning points and to reflect structural changes of an economy are directly embodied in the main defects of macro-forecasts. In this lecture, we investigate how to incorporate qualitative prospects (direction) drawn by judgment on the current phase of a business cycle into a macro model framework producing quantitative forecasts (magnitude). We also evaluate the underlying model's forecasting performances along with each phase of business cycle fluctuations. Our empirical results suggest that use of high-frequency (monthly) data within a low-frequency (quarterly) model can considerably reduce the crucial risk of missing the most up-to-date monthly information on the ongoing business cycle. By doing so, an initial baseline forecasting is expected to make a good start.

(Lecture in English)