Monetary Trends

April 2007

FEDERAL RESERVE BANK OF ST. LOUIS

Economic Forecasts: Public and Private

The Federal Open Market Committee (FOMC) began reporting forecasts to the Congress in 1980, but only since 2005 has the report included forecasts for a 2-year-ahead horizon in the February testimony. The longer-run horizon is especially useful for understanding the policymakers' views about the desired inflation objective because, over longer horizons, it is Fed policy that drives the inflation trend.

The forecasts that Fed Chairman Ben Bernanke reports are the range and central tendency of the individual forecasts that voting and nonvoting members of the FOMC bring to the first policy meeting of the year. The central tendency of the forecasts for fourth-quarter-over-fourth-quarter gross domestic product (GDP) growth is 2 1/2 to 3 percent in 2007 and 2 3/4 to 3 percent in 2008. The central tendency for inflation as measured by the personal consumption expenditures (PCE) price index excluding food and energy is 2 to 2 1/4 percent in 2007 and 1 3/4 to 2 percent in 2008. The midpoints of the central tendency are reported in the first column of forecasts in the table. Values in parentheses are a measure of the uncertainty inherent in the year-ahead forecasts: They are the root mean forecast errors (RMSE) for the year-ahead forecasts made in the years 2000 through 2006. For the past 7 years the RMSE has been 1 percent for GDP and 0.68 percent for inflation. One way to interpret this measure is to say that we might expect the GDP outcome for 2007 to be within ±1 percent of the forecast two-thirds of the time. Of course, that interpretation also implies that we can expect it to be off by more than 1 percent about one-third of the time.

The second column lists Administration forecasts, from the *Economic Report of the President*. The real GDP forecasts for the next 2 years are very close to the FOMC's and well inside the range of uncertainty associated with any forecast. The Administration's forecasts display the same slight uptrend in 2008 as that seen by the FOMC. In the past 7 years, Administration forecasts have been slightly less accurate than the FOMC's. The Administration's inflation forecast is higher, but only for the GDP price index and not the core PCE price index. In common with the Fed, the Administration sees the inflation rate moderating in 2008.

The table also reports forecasts and RMSEs for two private-sector groups, the Blue Chip Consensus and the Survey of Professional Forecasters, as compiled by the Federal Reserve Bank of Philadelphia. All forecasts are fourth quarter over fourth quarter, except the Survey of Professional Forecasters' GDP forecasts for 2008, which are available only on a year-over-year basis. The private forecasters use the GDP price index—the same index used by the Administration. In all cases for both public and private forecasts, the outlook is for continued expansion near the perceived potential growth rate for GDP and a slight moderation in the inflation rate. With the release of the 2007:Q1 forecast, the Philadelphia Fed began to ask professional forecasters about core PCE inflation on a fourth-quarter-over-fourth-quarter basis. For both 2007 and 2008, the median forecast is 2.0 percent.

—William T. Gavin

Economic Forecasts for 2007/2008

	FOMC	Administration	Blue Chip	Survey of Professional Forecasters
Real GDP growth	2.75/2.88	2.90/3.10	2.70/3.00	2.87/3.00
	(1.00)	(1.24)	(0.94)	(1.06)
Inflation*	2.13/1.88	2.50/2.30	2.10/2.10	2.19/2.10
	(0.68)	(0.86)	(0.74)	(0.72)

NOTE: *The FOMC's inflation measure is the core price index for personal consumption expenditures. The others are the price index for GDP. The 2008 forecasts for the Survey of Professional Forecasters are year over year; all others are fourth quarter over fourth quarter. Values in parentheses are RMSEs for the year-ahead forecasts 2000-06.