Subject: 188. Red Team priorities: Challenging the Conventional Wisdom of Economics

Dear Dr. Fischhoff and Colleagues:

Concerning the exciting possibility for behavioral scientists to recommend new Red Team projects: It would be timely, exciting, and useful to challenge conventional thinking in economics and prototype a new, multi-disciplinary, approach to national/international economic forecasting and early warning.

Expanding Upside Options

The project also could challenge conventional models and thinking about economic *opportunities*. Fresh ideas could identify ways in which the US government, in cooperation with other governments, can increase the baseline rate of innovation and GDP growth/capita of market economies by 1%/year above the pre-crisis baseline.

This creative thinking and analysis will be worthwhile: A 1% increase would be an extraordinary contribution to human welfare. It is difficult to imagine any international (or domestic) political agenda or idea to improve human welfare that would not benefit from an additional, cumulative 1% increase in the growth rate of the US and other countries. Such a goal probably

requires international cooperation - for example, to increase support for scientific research and K-12 STEM [science, technology, engineering, and mathematics] education in all countries. Some of these steps could use new, low-cost global communication technology. <1>

   - We - including the <u>Global 2025</u> and other policy planning work of the US government - are operating with limited ideas derived from the national steel plant economies of the 1930s. These ideas include limited ideas about the behavior of individuals and systems that exclude too many important variables and ideas from the government data systems of the G20 countries. We will need US government leadership for international cooperation to secure the data that are needed for rapid learning and discovery. A Red Team project can be a catalyst for a new, rapid learning system.

<u>About Early Warning Models</u>

   - About early warning requirements: I have suggested earlier, (e.g., filings # 7 and # 17, archived on www.policyscience.net at II. D) that there are compelling reasons for the DNI system to do its international economic forecasting by a new generation of sophisticated *political economy* models. These must allow the possibility that the powerful financial services industry has shown the resources and brainpower to capture and "dumb down" national political systems and regulatory bodies, limit their competence, and distort free markets in ways that change the mathematical assumptions that should inform econometric models. Also, the DNI's new (candid and realistic) forecasting models must include the failure of the ethics that normally is expected from leaders of major institutions.

   McLean and Nocera's <u>All the Devils are Here</u> (2010) is a good overview of evidence that the global financial catastrophe and recession, and America's failure of stewardship, were not caused by innocent mistakes or errors.

<u>Activating NSF and Supporting Academic World Rapid Learning</u>

   In the long run, a vibrant, innovative, and rapid learning system for the *academic* behavioral sciences would be a vital part of a national learning strategy. However, I have no insight into how to help NSF recover from its paralysis, induced by a Republican era. [If the expected coefficients and predictions for the physical universe had suddenly changed, as they did for all of

the mainstream econometric models, NSF would have shifted its relevant programs, quickly, into a fast discovery mode by now.]

Someday, the NSF system may be properly diagnosed and repaired. However we are wasting time. Even if the Red Team cannot do all of the analysis itself, it can begin by organizing the analysis and challenging the failures and weakness of conventional thinking and models. General Clapper has a duty to be in touch with reality, even if our leading research universities, academic scientists, and agenda setting institutions are still lagging.

- I am adding, to this message, a copy of a story from yesterday's <u>Financial Times</u>. It underscores a parallel awareness in the business community that our previous (conventional wisdom) models for recovery, in the US and abroad, have made errors of forecasting and policy advice that - if somebody gets organized to move quickly - we might be able to learn about and improve upon.

I also attach a supporting letter from Dr. Reischauer, former head of CBO and member of the Executive Committee of Harvard's Board, suggesting many areas in which conventional economic data systems have been losing their grip on a changing world.

best regards,
Lloyd Etheredge

 <1>   The upsides of economic and political opportunity may be even greater in some sectors. This is not the place to make a full case. However: I have outlined, earlier, the new US rapid learning healthcare/electronic health record systems that could be extended globally to benefit a major sector in every nation's economy. The Gates Foundation will (next month) begin to assess national, and perhaps global, potentials for similar evidence-driven rapid learning systems to improve achievements in K-12 educational systems.

There are many political and economic opportunities that can be supported by refined models of productivity, innovation, and performance forecasting. These, too, can be informed by recognizing opportunities for creative applications of new technologies.

AMEX CHIEF CALLS FOR JOBS TASKFORCE

By Francesco Guerrera and Suzanne Kapner in New York

Financial Times. Published: December 5 2010 22:00 | Last updated: December 5 2010 22:00

Ken Chenault, the chief executive of American Express, has called for an alliance of business leaders and politicians to find concrete ways to create millions of jobs in the US and kick-start the anaemic economic recovery.

In an interview with the Financial Times, Mr Chenault, who has met frequently with President Barack Obama and his aides, proposed a special commission to set a target for new jobs and specific measures to reduce stubbornly high unemployment.

"I'd like to see an industry taskforce between the public and private sectors to determine what businesses need to create jobs," he said. He added that it would be essential for any public-private taskforce to set a specific target and a timeframe for the new jobs in order to force government and business to take tangible steps to reduce unemployment.

Mr Chenault's proposal was given added urgency by Friday's official figures showing that employers added fewer-than-expected jobs in November, pushing the unemployment rate to 9.8 per cent of the workforce.

The call for a truce between the White House, which has attacked companies' reluctance to invest in the economy, and a business community that has been calling for more government help, was echoed in other parts of corporate America.

The Business Roundtable, the trade organisation for some of the largest US companies including Amex, said Mr Chenault's proposal was "very intriguing" and could be debated at a meeting of its members this week. The White House declined to comment.

Mr Chenault, whose company collects data on millions of retail transactions, said that high unemployment was the biggest obstacle to a faster economic recovery [. . .].

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[The Policy Sciences Center, Inc. is a public foundation that develops and integrates knowledge and practice to advance human dignity. Its headquarters are 127 Wall St., Room 322 PO Box 208215 in New Haven, CT 06520-8215. It may be contacted at the office of its Chair, Michael Reisman (michael.reisman@yale.edu), 203-432-1993. Further information about the Policy Sciences Center and its projects, Society, and journal is available at www.policysciences.org.]

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December 23, 2002

Dr. Lloyd S. Etheredge, Director
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Dear Dr. Etheredge:

Thank you for your letter and thoughtful attachment. I am in complete agreement that the economic data we collect has significant deficiencies that limit our ability to understand the economy's problems and chart future policy.

We don't collect some information that is needed and gather much that we could do without. We collect other data in insufficient detail and almost always take too long to release the data for it to be useful in policy decisions.

As you know better than I, there are many reasons for this situation. What we collect and how we collect it reflects the forces at play in the first half of the last century and those forces do not want to give anything up. Congress has little interest in devoting more scarce budget resources to collect new and better information. Few economists who use the data appreciate its limitations. They have been raised on certain data sets and treat them as if they are part of the underlying environment, not subject to change. They put a premium on continuity and don't want discontinuity in the data sets they know and use.

I don't think I would be as critical as you are about CNSTAT/NCR. I don't think they would have much of an impact even if they had done the studies and made the recommendations you think warranted. Nor do I think universities (Yale or Harvard) or the Fed could make much of a dent in the problem. Rather, I think a presidential or congressional study commission is called for—one with a clear mandate and a promise that added resources will be devoted to strengthening the statistical system based on the commission's report. Unfortunately, the prospects for such an initiative rising to the top of policymakers' lists of things to do is very, very low.

Nevertheless, I wish you well in your efforts.

Sincerely,