

Comments on:

A Look Into the Factor Model Black Box
Publication Lags and the Role of Hard and
Soft Data in Forecasting GDP

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Overview of discussion

- Summary of the paper
- Questions
- Suggestions

What they do

- Address the « Black Box » criticism that DFMs lack diagnostic statistics by computing measures for understanding the importance of individual series in the forecast
- Use these measures to assess the role of hard and soft data in forecasting euro area GDP growth in the context of unbalanced data sets

Computing DFM forecast weights allows to:

- Identify the main driving variables behind the forecast (tell stories)
- Understand differences with other models' forecasts
- Understand sources of forecast revisions
- Fine-tune the data set (minimize forecast errors)

What they find

1. Forecast weights are concentrated among a small set of series and vary considerably across different forecasting horizons
2. Differences in publication lags have important effects on the contributions of hard and soft data to the forecast
3. Real activity data are the most important source of information when using balanced data sets
4. Business survey data become much more relevant once their more timely publication is taken into account

Bottom line

- Real activity data are mostly useful for backcasting euro-area GDP growth
- We should pay more attention to soft data when using unbalanced data sets to monitor GDP at longer horizons

Questions

- How can we interpret the result that forecast weights are concentrated among a relatively small set of series?

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- How can we interpret the result that forecast weights are concentrated among a relatively small set of series?
- Are forecast weights stable over the sample?

The role of foreign variables

- Forecasting weights on US variables are low
- Gosselin and Tkacz (2007): US variables at least as good as Canadian variables in forecasting Canadian inflation
- Expand the set of foreign variables
 - More US variables (e.g. NIPAs)
 - Data for the UK, Eastern Europe, Sweden, Norway

Forecast accuracy around turning points (1)

- A more detailed study of the time paths of forecast errors might reveal large errors when the growth rate is at, or close to, a turning point
- Useful to discern the extent to which measures of forecast performance are influenced by large prediction errors that occur relatively infrequently
- Compare median-based measures of forecast accuracy (RMedSEs) with the usual RMSEs

Forecast accuracy around turning points (2)

- Survey data often represent net balances
- Dispersion across respondents may contain important additional information about changes in economic activity, especially around turning points
- Properly accounting for this might improve forecast accuracy around turning points and lead to even greater weight on survey indicators

Possible extensions

- Redo the same experiment with:
 - Consumption
 - Business investment
 - International trade
 - Inflation
- Consider information at frequencies higher than the month

Other suggestions

- Further examine the role of financial variables (money and credit indicators)
- Compare forecast weights of national vs. euro area series (Marcellino et al, 2003)

Final remarks

Very interesting and useful paper!