

Some thoughts about history, model updating and expectations

Expectations of Future depend on our understanding of the structure of the system i.e. of how the world works. Our present understanding of the system's structure is a function of our understanding of History. With new information coming/event occurring, our *interpretation* of the Past – History - changes so also our understanding of the present system changes. So we will form new expectations about the Future.

Past vs. History

Interpretation here means that we choose different set of events from the Past and redefine relations among the events – History changes. The Past is defined as a set of all events – miniscule, small, medium, big or super-big and relations among them - that has ever happened since the beginning of time. As such it is incomprehensible to an ordinary mortal in the whole.

Individual vs. Collective History

Individual history is defined as set of events from the Past and relations among them that are *known* and considered significant by an individual. The pure individual Past is a total set of events – whether lived through by the individual or transmitted via his senses to his mind in some form (through writings, oral transmitting by other individual or other audio-visual means). There might be some sense of Collective History if histories known and worked with by individuals overlap – that overlap we can call a Collective History. Events individual lives through might be significant for the Collective History especially if that individual influences many other individuals or causes events of big importance.

New History > New Mental Model of the World > New Expectations

On the basis of new interpretation of the Past, new History, an individual makes a mental construction of how the world works anew. If the new information that comes is big in significance, everyone's or nearly everyone's individual history changes i.e. collective history gets transformed. As a result most individuals will change their mental construction of the system. Their expectation about the future will now be changed as well.

Question:

Can this idea – that new information/event changes our understanding of how the world works via the change in the interpretation of the history channel - be used for economic modeling? As sketched above, by new interpretations we mean a new History set of events and new relations among them.

References:

Edward Hallett Carr, What is History? Random House of Canada Limited, Toronto 1961

Appendix:

One possible example: Let's assume there is some understanding/model of how the economic system works. Now a certain firm in a given sector or a country, in certain economic context contoured by some economic variables, defaults on its debt obligations. Let's say it was the first time ever a firm defaulted in that particular context (or a very similar one) – of all known cases (cases in History set). This will likely change the expectations about firm default likelihood via two channels. First, this event will immediately trigger the updating of the

credit model currently used... Second, this may trigger search in the past of situations when such or a similar context led to default in a different sector, country etc. or notable situations when it did not. Such cases will now likely be part of new History set which will feed into the updating of the model. *Furthermore, relations among events/ parts of the model in the new History set will likely change too.*

Vladimir Zlacký, January 2016