Title: Business Expectations and Forecast Errors in the Interconnected Economy

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Abstract:

We construct a unique dataset that integrates information on business expectations, forecast errors, and interfirm transaction relationships to provide a new perspective on the mechanisms underlying the formation of business expectations and the generation and transmission of forecast errors (unanticipated shocks). Our main empirical findings are as follows. Firms' expectations about their growth rates are positively correlated with the number of their transaction partners, consistent with observed firm growth patterns. Greater forecast variation tends to amplify forecast errors, indicating that uncertainty is a key driver of these errors. Longer transaction relationships tend to reduce uncertainty and forecast errors, suggesting that information sharing and flexible adjustments play a role in improving forecasts. We find no evidence of either portfolio effects or amplifying effects on forecast errors arising from connections with a larger number of transaction partners. Moreover, firms' forecast errors are transmitted to their transaction partners along supply chains. These forecast error correlations stem from transaction linkages rather than from aggregate factors. Overall, this study deepens our understanding of how firms form business expectations in an interconnected economy and how forecast errors propagate through transaction networks.