

Forecast Revision and Business Cycles

--Evidence from 12 years of ESP Forecast Survey experience in Japan

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Disagreement between forecasters, which is usually measured by the dispersion of point forecasts of the panel of respondents, is of considerable interest. Prior studies intensively analyze disagreement and most indicate a positive correlation between: disagreement and forecast error, disagreement and uncertainty. However, their causality is unclear.

Does disagreement cause forecast error? We can show the disagreement equal to the variance of forecast error. However, it is possible that the variance of the forecast error rises without the increase in disagreement. Especially in the recession phase, when the Actual differs substantially from the forecast. Even if the disagreement is small the forecast error is large. Simultaneously, increase in the forecast error possibly leads the disagreement.

In this study, we test whether disagreement causes forecast error through the Granger causality test. We construct monthly cross-sectional disagreement between forecasters and forecast error using forecasts the ESP Forecast (ESPF) survey, which is the first monthly survey of macroeconomic forecasts conducted by professional forecasters in Japan. We understand that Granger causality is not necessarily true causality. However, we can show the relationship between disagreement and forecast error that prior studies have not shown.

The ESPF was launched 13 years ago in 2004. The ESPF requests respondents to provide annual and quarterly forecasts at the beginning of each month. The number of participants every month is approximately 40.

Consensus Economics, the world's leading international economic survey organization, is also a monthly survey, and is older than the ESPF. However, in Japan, the ESPF panel has twice the number of participants as the Consensus Economics panel.

Moreover, the ESPF not only collects annual multidimensional data but also quarterly multidimensional data. Although the U.S. Survey of Professional Forecasters (US-SPF) is the most famous source for examining quarterly forecasts, it is only conducted quarterly. The ability to survey quarterly forecasts monthly is an advantage that other surveys do not have.