Inflation Expectations and the Supply Chain

Discussion

Nitya Pandalai-Nayar
University of Texas at Austin & NBER

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This paper: analyzes how supplier prices feed through to firms’ inflation expectations

Multiple contributions:

1. Detailed firm-to-firm network data, supplier and firm prices, linked to firm inflation expectations survey

2. Documents reason for wide dispersion in firm inflation expectations
   - Input prices matter for firm beliefs about aggregates, even orthogonal to CPI
   - Intuitive: trading partners firms frequently operate with more important than CPI
   - Analog on consumer side: grocery prices, consumer inflation expectations

3. Implications/other findings
   - Violation of FIRE, support for Lucas (1979) island model
   - Some evidence for downward rigidity in firm beliefs – inflation declines might be sluggish
   - Implications for policy – clear communication about CPI growth might not influence firm beliefs
   - Other implications?
Comment: from input price changes to sales price changes

- Wide dispersion in input price changes: median as much as 22.6%, one s.d. 23.8%
- Very limited passthrough to firm sales prices: median as much as 9.5%, s.d. 17.5%
- Puzzle: supplier firms are also buying firms in the data
Comment: Who are the important suppliers?

- Why are some input price changes so volatile?
  - firms connected to other volatile firms?
  - other costs (wages, etc)?

- Why do we care?
  - input bundle price is a weighted average of all supplier prices
  - wide variation suggests “important” firms are raising their prices the most
Comment: Do the key network suppliers affect the aggregate?

- Granular origins of inflation?
- CPI control orthogonalizes input bundle price w.r.t CPI, but not individual suppliers’
- If largest suppliers/firms in the economy raising prices $\rightarrow$ CPI affected $\rightarrow$ rational for inflation expectations to change?
Comment: Do the key network suppliers affect the aggregate?

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- If largest suppliers/firms in the economy raising prices $\rightarrow$ CPI affected $\rightarrow$ rational for inflation expectations to change?
- Placebo/robustness tests don't address this
  - construct input bundle price changes excluding firms whose own prices are correlated with CPI growth
Final thoughts

- Learning more about the firms generating the very high input price changes is important.
- Possible policy implication: CBs should target the inflation expectations of those key firms directly.
- Data available to understand these firms....
Conclusion

- Important to understand what drives agents’ beliefs
  - Lot of evidence that full information rational expectations models not great

- Very plausible role for importance of trading relationships/supply chains
  - Makes clear we need to expand measurement of agent beliefs in international more broadly

- Very useful paper with many applications!