Belief-Dependent Pricing Decisions

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The paper explores price-adjustment decisions with a survey of firms’ expectations in Uruguay.

Evidence of price-setting frictions using micro-data is often based on time- and state-dependent models.

The authors investigate a third channel (belief-dependent) as driver of price revisions.

Probit model with correlated random effects.

Selected results:
- effect of expectations operates with a delay;
- larger firms are better at forecasting inflation and more attentive;
- larger firms change prices more frequently (but in smaller magnitudes) compared to small and medium size firms.
Empirical investigation is carefully done and properly detailed.

Robustness analysis (endogeneity, linear prob. model) provides convincing results.

Duration

Build a "duration" variable using the last price change of each firm’s main product.

Substitute the 12 *Taylor dummies* (indicating whether the last price adjustment occurred between one and twelve months ago).
Control Variables

- Besides inflation expectations, macro variables often used to forecast inflation are not included, Stock and Watson (1999); Faust and Wright (2013); Coibion, Gorodnichenko and Kamdar (2017).
  - inflation persistency (emerging economies);
  - marginal cost (MP transmission);
  - exchange rate pass-through (export/import firms);
  - country risk-premium and other variables that impact inflation through the expectations channel.

- Which variables remain significant in the Probit model estimation is an empirical matter.
Comments

Monetary Policy

- Inflation is high but stable in Uruguay (8% p.y.)
- Role of monetary policy in Uruguay is not discussed in the paper.
- Inflation Targeting (IT) system is relevant to coordinate expectations.
- Control for the inflation target or range. Does the probability of price adjustment depend on the IT setup?

Policy Implications

- Explore policy implications of the third channel using the micro-data:
  - Permanent versus transitory effects on inflation.
  - How does the third channel affect the MP transmission mechanisms? (power of monetary policy and the CBU’s ability to fight inflation).
  - Coordination of fiscal and monetary policies.