

State-contingent price setting and monetary transmission

ChaMP Research Network, 6 July 2026



Anna Seim, Deputy Governor

Introduction

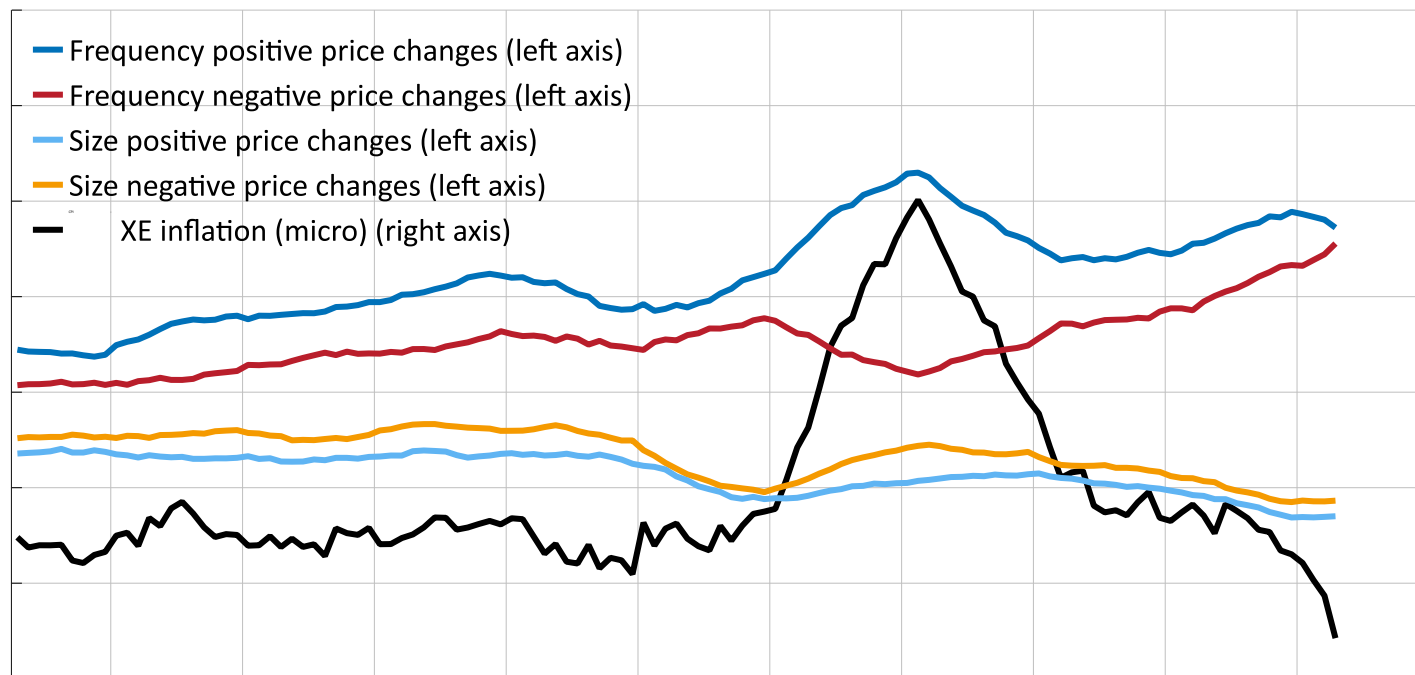
- Implications of supply shocks for inflation and optimal monetary policy?
- Price setting behaviour may be state-contingent
- Inflationary pressures may stem from
 - Higher frequency of price changes (extensive margin)
 - Greater magnitude of price changes (intensive margin)
- Policy implications?

Price-setting behaviour: key ideas

- Frictionless optimal pricing under monopolistic competition:
- $p_{it} = \frac{\eta}{\eta-1} mc_{it}, \eta > 1$
- If $\eta \rightarrow 1$: demand for firm i:s good is inelastic, good not substitutable. Mark-up high
- If $\eta \rightarrow \infty$: demand for firm i:s good is elastic, good substitutable. Mark-up low

- Standard New Keynesian Phillips Curve (NKPC):
- $\pi_t = \kappa x_t + \beta E_t[\pi_{t+1}] + u_t$
where $\kappa \equiv (1 - \theta)(1 - \beta\theta)/\theta$, and θ is the probability that a firm cannot adjust its price in a given period
- A lower θ implies more flexible prices and a steeper Phillips curve

The frequency and magnitude of price changes in Sweden 2016-2026



Note. Per cent. All series are 12 month moving average. CPI-XE inflation (micro) is 12 month moving average month-on-month. Sources: Statistics Sweden and the Riksbank.

Policy implications

1. Higher **frequency of price changes**

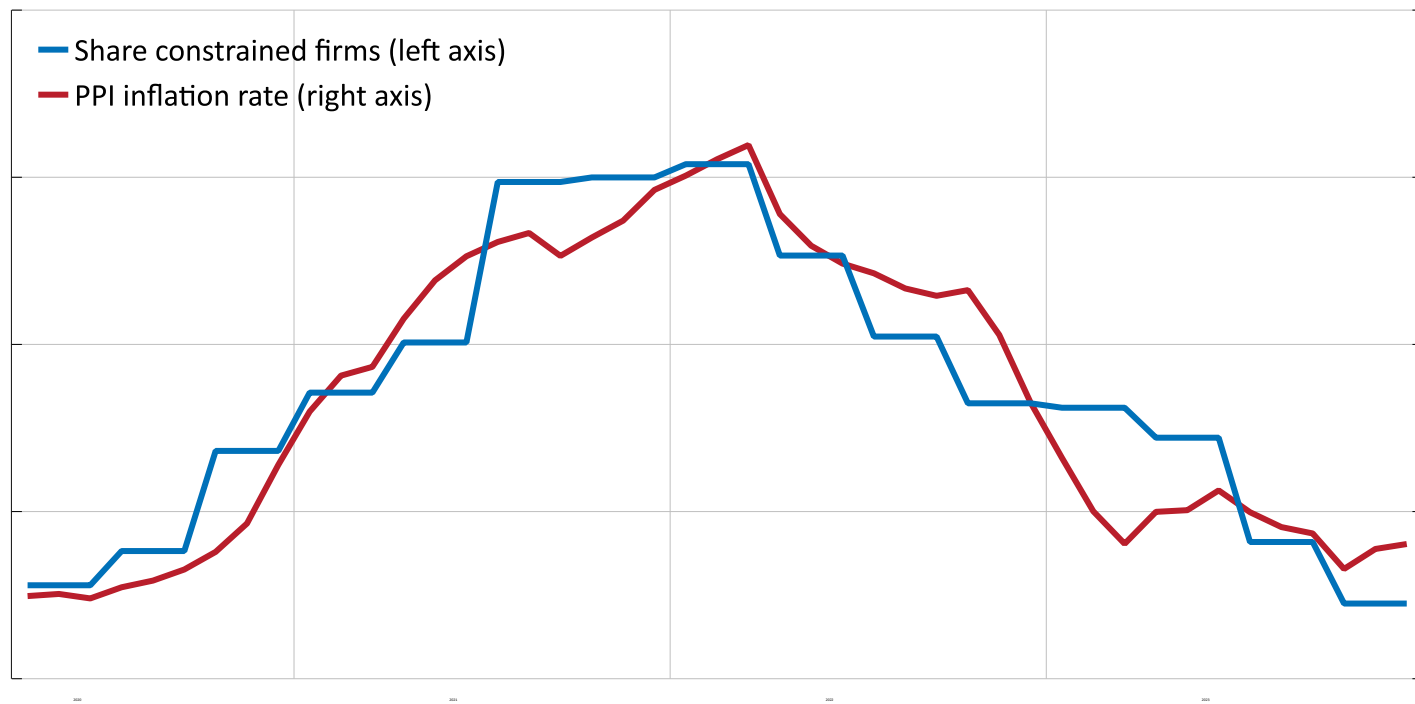
- A steeper Phillips curve
- Faster monetary transmission
- Lower sacrifice ratios: less costly, in terms of the output gap, to reduce inflation

2. Larger **magnitude of price changes**

- No change in the slope of the Phillips curve
- Slower monetary transmission
- Higher sacrifice ratios

Capacity constraints and PPI inflation in Sweden 2020-2024

Capacity constraints during the inflation surge



Note. Per cent. Source: Ahlander, Amberg and Klein (2026). *Do Capacity Constraints Affect the Pass-Through of Monetary Policy to Prices?*

Factors to monitor going forward

- Since monetary transmission takes time: need to monitor **forward-looking** indicators
- **Frequency**
 - Microdata on frequency of price changes
 - Changes in price-setting behaviour revealed in, e.g., surveys on pricing plans
- **Marginal costs**
 - Cost indicators, input prices, transportation costs
 - Firms may have tried to build resilience by introducing cost indexation and clauses in their contracts post-pandemic
- **Mark-ups**
 - Capacity constraints correlated with inflation
 - Economic slack matters for how effectively central banks can curb supply-driven inflationary pressures

Concluding remarks

- Historical parallel: the twin-peaked inflation time series of the 1970s
- Memory of recent inflation surges may make expectations more prone to de-anchoring
- Balloon analogy of inflation: could be that once inflated, it is easier to inflate again
- Need to closely monitor forward-looking indicators to understand the drivers of inflation

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