



OESTERREICHISCHE NATIONALBANK  
EUROSYSTEM

# Discussion „Discretionary Spending is the Cycle, and Why it Matters for Monetary Policy”

**María T. Valderrama\***

Sintra, July 1<sup>st</sup>, 2025

Monetary Policy Section  
[www.oenb.at](http://www.oenb.at)



\* The views expressed here are my own and do not represent those of the OeNB or the Eurosystem

## The paper in a nutshell

Traditional consumption categories do not capture **non-homothetic preferences**, with important implications for monetary policy transmission and the amplification of shocks. Thus, the authors

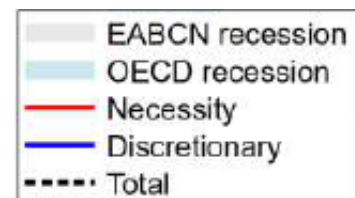
- **propose** to distinguish between *discretionary* and *necessity* spending,
- **construct** macroeconomic time series of *discretionary* and *necessity* goods
- apply a calibrated theoretical model incorporating these features and revisit the design of **optimal monetary policy**

### Main features of the theoretical model:

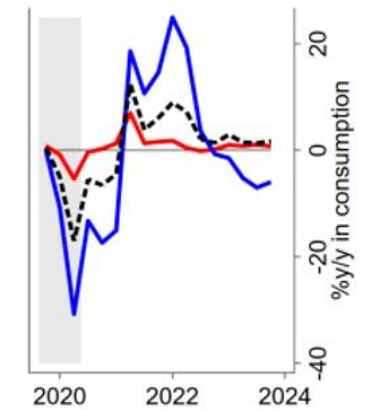
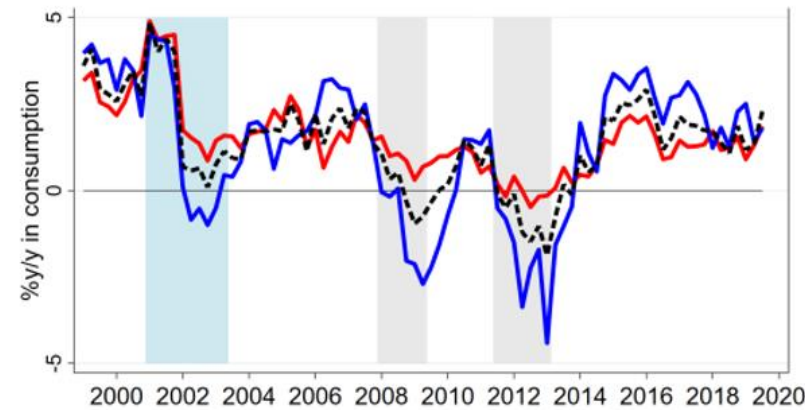
- Non-homotheticity in the utility function
- Heterogenous labor markets: high productivity/Ricardian and low productivity/HtM workers
- Higher share of HtM workers in discretionary sector
- Homogenous nominal rigidities

## Main contributions of the empirical part

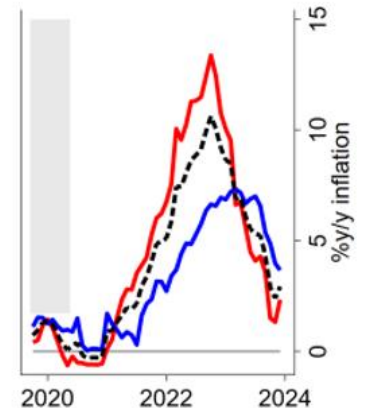
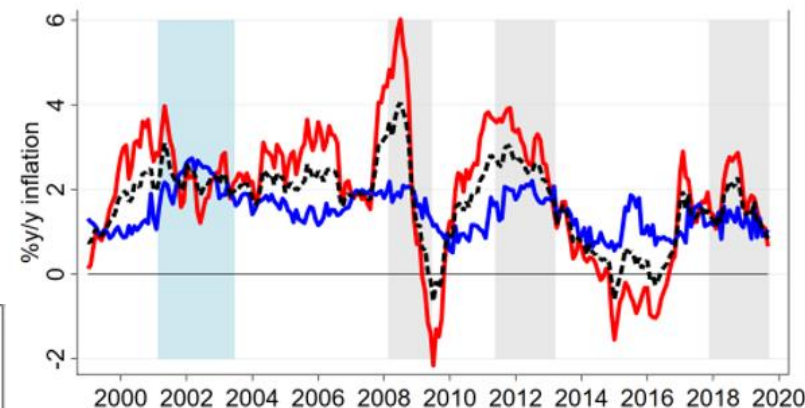
- Shows that discretionary spending is more sensitive to shocks/business cycle fluctuations
- The data work on creating new time series for necessity and discretionary categories is carefully executed and a significant contribution of the paper. Data available to other researchers (complement ChaMP collective projects!)
- More evidence of the importance of sectoral analysis and the need for better and timely granular data!



(a) Consumption



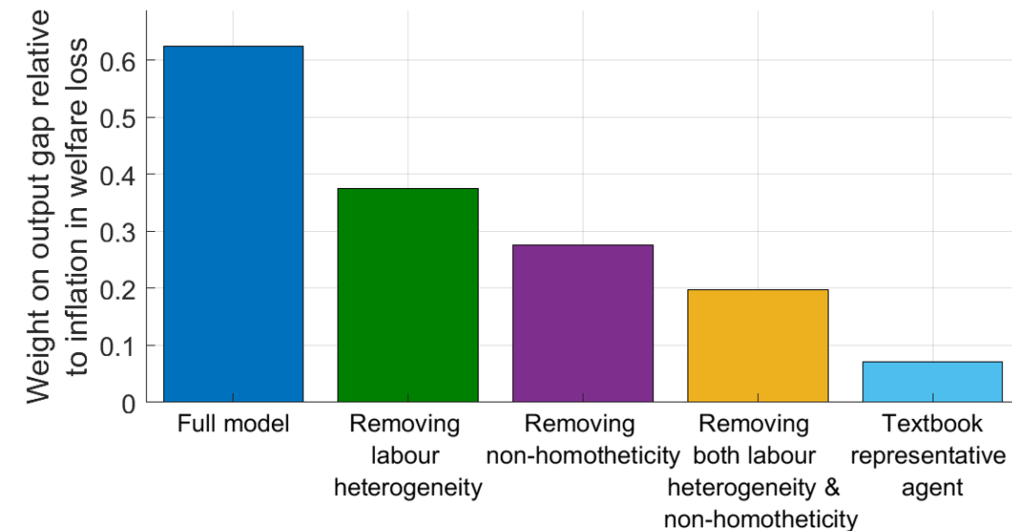
(b) Inflation



## Policy recommendations from the theoretical part

- Since HtM households are more exposed to output fluctuations, output stabilization becomes more important.
- **ECB should target inflation in discretionary good prices**
- ECB's policy rule should put **more weight** on the output gap
- **Question:** Should smoothing the income loss for hand-to-mouth households be the responsibility of monetary policy, or rather fiscal/labor market policies, such as an unemployment insurance? What is more welfare maximizing?

Welfare function coefficients



Sources: Authors' calculations

Notes: Chart shows the relative weight on the output gap vs inflation. This is the weight on the variance of consumption in the welfare function in the main text, divided by the sum of the weights on necessity and discretionary inflation. The full model includes labour heterogeneity (low income disproportionately employed in discretionary sectors), non-homothetic preferences and hand to mouth households. The bars remove elements of these features, by setting relevant parameters equal to the aggregates or averages.

## What is needed to validate the model and the policy prescription?

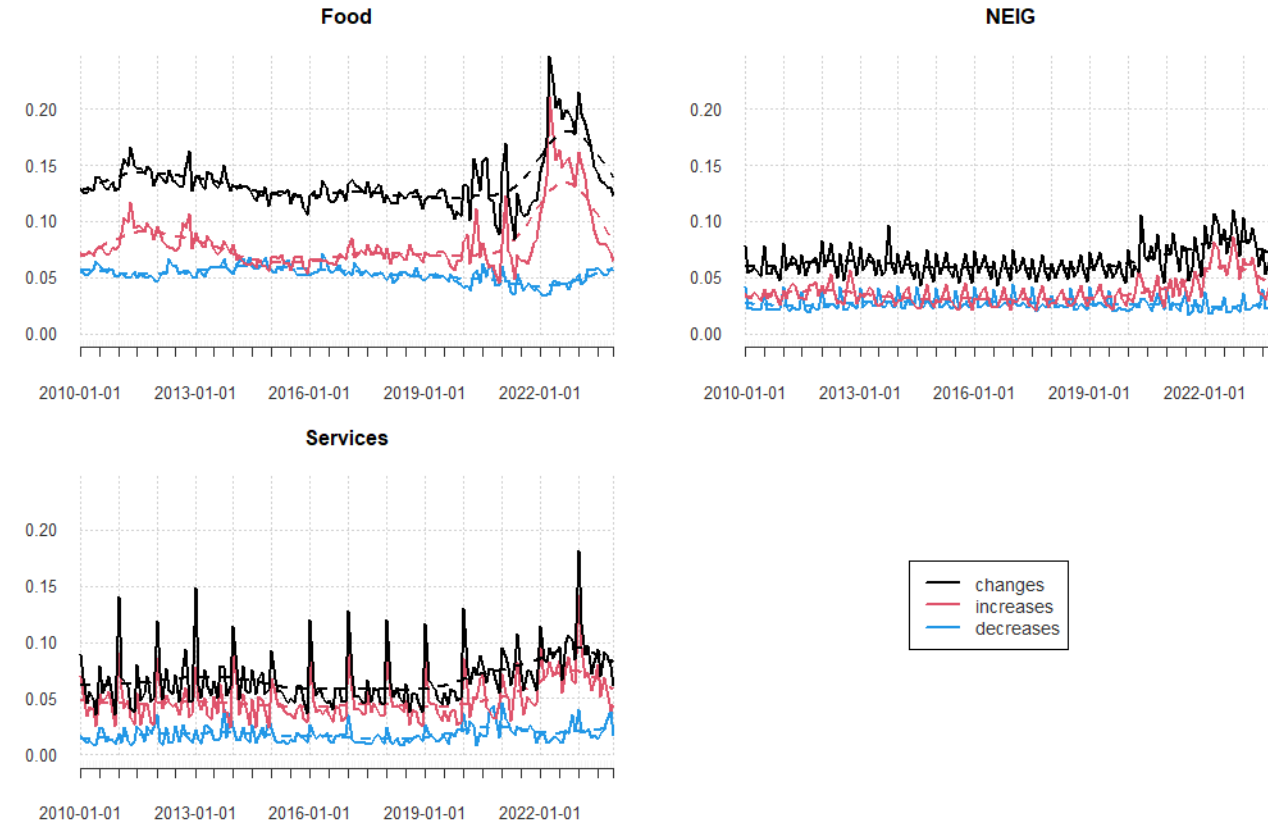
Optimal monetary policy models with heterogeneous nominal rigidities already prescribe targeting sectors with more rigid prices, as monetary policy tends to be more effective. **Why is this model better?**

- The authors need to **bring the model to the data!**
- Need to show that the statistical properties of the data generated by the model **replicate the stylized facts** presented in the first part of the paper
- This is particularly relevant when estimating different policy rules. It is not enough to switch off some parameters, but each model variant should be re-estimated to **ensure fit before comparing** policy and welfare outcomes.
- It would also be helpful to show a **counterfactual analysis**: If the ECB had adopted this strategy in 2021, would we be better off?
- **Possible extensions**: Adopting the non-homothetic preferences (PIGL) and the corresponding price index in Hochmuth et al. (2023) would allow authors to use a theoretically consistent price index directly in the Taylor rule and provide a useful benchmark, especially in the context of optimal monetary policy.

# What is missing? Heterogenous nominal rigidities



- ChaMP Research Network, show that **sectoral price rigidities are crucial and time varying for transmission** (Ghassibe and Nakov, and Karadi et al, Ascari et al, forthcoming)!
- Without estimating the model, it is difficult to determine **which channel is quantitatively significant**
- Thus, the authors could **compare** their channel with other competing drivers of the business cycle (e.g., importance of price heterogeneity, production networks, etc. )
- **Does the policy prescription remain the same?**



Source: Consumer price micro-datasets from the national statistics institutes of Germany, France, Italy, Spain, Austria, Greece, Estonia, Latvia and Lithuania. Data for 2023 include DE, FR, IT, ES, AT, EE, LV, GR until Dec 2023 and LT until March 2023. Calculations: "Consumer Price Stickiness in the Euro Area During an Inflation Surge" E. Gautier, C. Conflitti, D. Enderle, L. Fadejeva, A. Grimaud, E. Gutiérrez, V. Jouvanceau, J.-O. Menz, A. Paulus, P. Petroulas P. Roldan-Blanco, E. Wieland, mimeo. Notes: The chart shows the weighted average frequencies of price changes (excluding sales) for all sectors and by aggregate product category. VAT changes are controlled for over the whole sample.

## Conclusions

- Innovative and intuitive mechanism to explain business cycle fluctuations
- Data work and data availability for other researchers valuable contribution to the field
- **The robustness of the policy prescriptions could be enhanced by :**
  1. **Bringing** the model to the data
  2. **Including** other heterogeneities (heterogeneity in price setting, time variation, etc.) relevant for the transmission mechanism
  3. **Quantifying** the importance of this transmission channel relative to other channels
  4. **Comparing** policy prescriptions from these other competing channels



**Danke für Ihre Aufmerksamkeit**

**Thank you for your attention**

[www.oenb.at](http://www.oenb.at)

[oenb.info@oenb.at](mailto:oenb.info@oenb.at)

 Oesterreichische Nationalbank

 @oenb.at

 @oenb

 @nationalbank\_oesterreich

 @nationalbankoesterreich

 OeNB





## REFERENCES

1. Ascari, G., Carrier, A., Gasteiger, E., Grimaud, A., & Vermandel, G. (2025). Monetary policy in the Euro Area, when Phillips curves ... are curves, mimeo
2. Gautier, E., Conflitti, C., Enderle, D., Fadejeva, L., Grimaud, A., Gutiérrez, E., Jouvanceau, J, Menz, V.-O., Paulus, A., Petroulas, P., Roldan-Blanco, P., Wieland, E, “Consumer Price Stickiness in the Euro Area During an Inflation Surge”, mimeo
3. Ghassibe, M. and Nakov A. (2025) Business Cycles with Pricing Cascades, Forthcomming ECB Workign Paper
4. Hochmuth, P., Pettersson, M., and Weissert, C. J. (2023). A Nonhomothetic Price Index and Cost-of-Living Inequality. Unpublished manuscript.
5. Karadi, P, A Nakov, G Nuño, E Pasten and D Thaler (2025), “Strike while the Iron is Hot: Optimal Monetary Policy under State-Dependent Pricing”, CEPR Discussion Paper No. 19339. <https://cepr.org/publications/dp19339>