Discussion of
"Monetary Policy with Supply Regimes"

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Advances in Monetary Economics Conference
IMF, September 2025

Overview

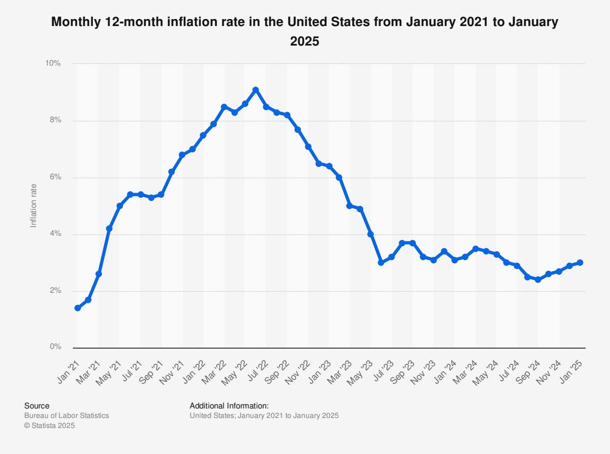
Question: How does optimal monetary policy change in the presence of supply regime shifts?

This paper: Optimal monetary policy under discretion and commitment in a standard New-Keynesian model enriched with supply regimes

Findings: after shift to a bad regime

- under commitment, optimal to allow for temporary increase in inflation
- under discretion, in equilibrium permanently higher inflation
- Taylor rule fails to keep inflation at target unless it is regime-specific

US Inflation: New Regime?



Motivation: Supply Shocks

- Are we in a new regime with tighter supply?
- It might be because of tariffs, wars, geopolitical fragmentation, but also green transition
- monetary policy under commitment in response to a permanent increase in tariffs: Bianchi and Coulibaly (2025), Werning et al. (2025), Monacelli (2025)
- monetary policy during the green transition: Del Negro et al. (2023), Aghion et al. (2024), Mehrotra (2024), Fornaro et al. (2025)
- Broad message: it is optimal to allow temporarily higher inflation in response to supply shocks of different sort

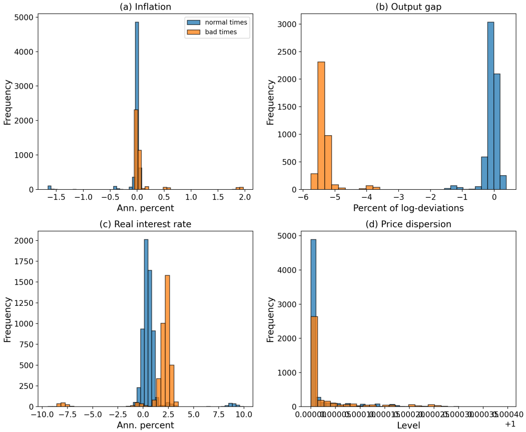
This Paper

- Regime-shifting stochastic model with two regimes: normal times and bad times
- Bad times are times with a systematically higher labor wedge

$$1+\tau_t = 1-\bar{\tau}+\xi_t+\eta_t$$

  - regime 1 = normal times: $\eta_t = 0$
  - regime 2 = bad times: $\eta_t = \bar{\tau}$
- let p_{12} and p_{21} be the probability of shifting from regime 1 to 2 and viceversa
- ξ_t is a AR(1) cost-push shock

Ergodic Distribution in the two Regimes



Comment I: Natural Interest Rates

- First result the authors emphasize: natural interest rate in SSS in bad times higher than in normal times

$$\frac{1}{\beta(1+r_2^*)} = c_2^* \left[p_{21} E_t \left(\frac{1}{c_1^*} \right) + (1-p_{21}) E_t \left(\frac{1}{c_2^*} \right) \right]$$

  where $c_2^* < c_1^*$

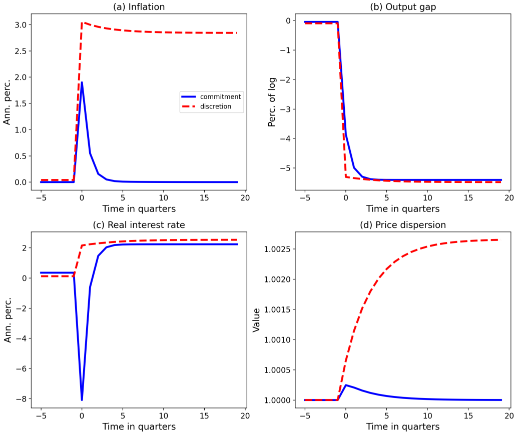
- Why? Agents expect on average higher consumption in the future because they will eventually switch to normal times

- I suggest the authors de-emphasize this result because it is reasonable to add features to the model that overturn it: e.g. in bad times there is more uncertainty

Comment II: Bi-modality

- Another result the authors emphasize: the bimodality of the ergodic distributions
- They emphasize this to contrast the model with regime shifting to a model with continuously distributed AR(1) shocks
- However bimodality is a bit a mechanical effect of a *discrete binary distribution* of shocks
- When compare the response to a shift to a bad time regime, the effects are similar

Comment III: Commitment vs Discretion



Understanding Inflation De-Anchoring

- main result: under discretion the central bank cannot avoid permanently higher inflation after shift to bad regime
- standard Phillips curve
$$\pi_t = \kappa(y_t - y^*) + \beta\pi_{t+1}$$
- under commitment: central bank commit to $y_t \to y^*$ in the long run
$\to \pi_{t+1}$ goes back to zero and inflation only increases temporarily
- under discretion: central bank cannot commit $\to$ expectations that $y_{t+1} > y^*$
$\to \pi_{t+1} > 0$ = inflation de-anchoring

Final Remarks

- great paper!
- interesting open agenda on structural changes in monetary policy