

# The long and variable lags of monetary policy: Evidence from disaggregated price indices\*

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## Abstract

We study how monetary policy affects subcomponents of the Personal Consumption Expenditures Price Index (PCEPI) using local projections. Following a monetary policy contraction, the response of aggregate PCEPI turns significantly negative after over three years. There are stark differences in the timing and magnitude of the responses across price categories, including some prices that show an initially positive response. We discuss theoretical interpretations of our findings and point to useful directions for future theoretical research. We also show how to re-aggregate our cross-sectional estimates and their standard errors, taking into account dependence between different prices using a Seemingly Unrelated Regression approach. Re-aggregation exercises show that changes in expenditure behavior have not accelerated the long-lagged response of inflation to monetary policy.

**Keywords:** Monetary policy; Federal Reserve; Price indices; Local projections

**JEL Classification:** C10; E31; E52; E58.

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# 1 Introduction

How monetary policy affects prices is a classic question in macroeconomics. It has gained new impetus after the inflation surge and sharp tightening in monetary policy by the Federal Reserve beginning in 2022. In most macro models, exogenous changes in monetary policy result in both a delayed and a less than one-to-one pass-through to prices. Empirical work on the question yields a range of results on the length of this delay and the size of the pass-through, leaving considerable uncertainty around the question of how long it takes for inflation to come back to target. Fed Chair Powell emphasized in his 2023 Jackson Hole speech that the Fed’s *“assessment is further complicated by uncertainty about the duration of the lags with which monetary tightening affects (...) especially inflation.”*

This paper sheds new light on this question by studying the responses of disaggregated price series to exogenous interest rate changes. Our premise is that a cross-sectional price analysis helps unpack the effect of monetary policy on inflation. If different prices display a different time lag in their peak response, for example, the aggregate series will likely mask this heterogeneity and thus be silent about a potentially important feature of the monetary transmission mechanism. Furthermore, the importance of different price series in aggregate price indices keeps changing, which might alter the transmission of monetary policy through time. Our starting point takes inspiration from a rich literature that uses micro-level price data for macroeconomic questions, e.g. [Nakamura and Steinsson \(2008\)](#).

Our focus lies on the dynamics of subcomponents of the Personal Consumption Expenditure Price Index (PCEPI). The motivation for this choice is twofold. First, the PCEPI is the price measure targeted by the Fed, so it is naturally of interest for monetary policy research. Second, the PCEPI can be disaggregated in a way that is relatively consistent through time. The Bureau of Economic Analysis (BEA) provides the PCEPI data at several levels of disaggregation. For example, the roughest level of disaggregation splits prices into prices of goods and services. The finest level of disaggregation that we study in our analysis includes the prices of, for example, corrective eyeglasses and contact lenses, electric appliances for personal care, dental services, or water transportation.

Methodologically, we use local projections ([Jordà, 2005](#)) to estimate impulse response functions (IRFs) of different prices to identified exogenous shocks to the

target Federal Funds Rate (FFR). While the aggregate price level is the subject of most previous IRF analyses, we employ a large number local projections to different levels of price level disaggregation. We use the identified monetary policy shock series of [Aruoba and Drechsel \(2023\)](#) to analyze plausibly exogenous interest rates changes. We focus on the 1982 to 2008 sample during which the Fed targeted the FFR and non-standard monetary policy was not used as a main tool. Our choice of the shock series and sample allows us to draw a connection to monetary policy in 2022 and 2023, which was arguably conducted through “traditional” interest hikes, in the same spirit as those in the pre-zero lower bound period.

Furthermore, we develop a re-aggregation procedure for our cross-sectional IRF estimates and their standard errors.<sup>1</sup> The responses of different prices to monetary policy are not independent from each other in most macroeconomic models. To take into account this dependence econometrically we propose a Seemingly Unrelated Regression (SUR) approach to a system of local projections. We estimate this system via Feasible Generalized Least Squares (FGLS) and obtain covariance estimates across price responses. These covariance estimates are needed to correctly compute standard errors of any re-aggregated IRF. Our SUR approach is a technical contribution to the literature on inference with local projections, which we survey further below. The approach could be relevant for other applications in which disaggregated local projections are constructed and aggregation is desired, for example in household-level or firm-level local projections.

Our re-aggregation procedure allows us to draw inference about a hypothetical aggregate PCEPI responses to a monetary policy change assuming different expenditure shares, such as the expenditure shares over the full sample or those at specific points in history. One experiment that is of particular interest is re-aggregation using the latest expenditure shares. Comparing this response to the response of the actual PCEPI itself will be informative about whether changing expenditure shares, e.g. due to structural change, have accelerated or decelerated the response of inflation to a change in monetary policy.

Our findings are as follows. First, after an exogenous monetary policy contraction, the headline PCEPI displays a gradual decline, with a significantly negative response at conventional levels only after 43 months. The peak reduction

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<sup>1</sup>The benefits of (re-)aggregating information from individual price components has been highlighted also in the context of measuring inflation expectations ([Dietrich et al., 2023](#)) and in forecasting ([Ajello et al., 2019](#)).

occurs after 54 months and our point estimate amounts to a roughly 4% lower price level after a 100 basis point monetary policy contraction. We estimate a very similar timing for the response of the core PCEPI, which excludes food and energy. The magnitude of the peak response of the core PCEPI is smaller, with a point estimate that implies a 2.5% price level reduction after a 100 basis point tightening. The lagged response echoes existing findings from the literature. For example, in [Christiano, Eichenbaum, and Evans \(1999\)](#), the aggregate price level does not fall to a statistically significant extent for 4 years after an FFR increase.

Second, the aggregate response masks stark differences across individual price categories. After a monetary policy contraction, some price categories respond negatively after a long delay or even a positive initial response, while others fall more rapidly. For example, we find that important categories such as gasoline and food and beverages off premises respond negatively after a long delay. For some components, such as used motor vehicles, the initial response to an interest rate increase is even positive. Other categories, such as clothing and footwear, fall more rapidly after a contractionary shock. Many categories do not respond significantly across the entire horizon we consider. One insight of this finding is that the reason why the headline and core PCEPI IRFs are flat for several years is *not* because all prices are unchanged. On the contrary, many of them change but both positive responses and different turning points make it hard to get a clean negative response in the aggregate until enough of the series start falling. It is only at a horizon of more than three years that the decline is broad-based across prices.

As part of our analysis of individual price components, we show that it is relevant to construct IRFs for both the *level* response of individual prices, as well as the cumulated *contribution* of each price to the total PCEPI. The contribution analysis makes clear that the PCEPI response to monetary policy tends to be driven by just a handful of important categories.

Third, we provide interpretations of our cross-sectional results in light of theories of price adjustment. For example, the positive, negative and many flat price responses to a monetary tightening at short horizons, and a broad-based decline in prices at long horizons, cannot be rationalized with a Calvo model. We examine the empirical relationship between the peak response of our IRF estimates and the price adjustment frequency estimates across PCEPI categories of [Carvalho, Lee, and Park \(2021\)](#). We find that the strong negative relationship that would be suggested by

Calvo pricing is not present in our results. Menu cost models and various theories of information frictions also cannot generate the IRF patterns across different prices we estimate. We speculate that theories with a heterogeneous cost channel of interest rates are a possible theoretical rationalization for our results. A monetary policy tightening could constrain the supply of goods and services by firms with financial constraints that tighten when nominal interest rates rise. In that way, monetary policy shocks could act as demand shocks to some sectors but supply shocks to other sectors in the short run, with the aggregate demand force eventually dominating across sectors at longer horizons.

Fourth, the SUR-based re-aggregation of our individual IRFs, using the latest expenditure shares, shows that the price level falls with a similar timing and magnitude as estimated with the aggregate series itself. The pattern is similar for both the headline and the core PCE. We find this to be the case when we re-aggregate IRF estimates based on rougher or finer levels of disaggregation. This result means that changes in expenditure shares, e.g. because of structural change, have not accelerated the response of the PCEPI to monetary policy. We further interpret this result by analyzing changes in consumer behavior. The most marked changes in expenditure shares that have happened over the last 60 years are a decrease in the share for food and beverages (-12 percentage points) and an increase for health care (+11 percentage points). Both categories respond to monetary policy with a long lag.

Taken together, our results echo the famous insight of [Friedman \(1960\)](#) that “*there is much evidence that monetary changes have their effect only after a considerable lag and over a long period and that the lag is rather variable.*”<sup>2</sup> We find that the idea of *long lags* in the transmission of monetary policy is substantial. We also find large differences in the timing of the response across different variables, which we point out are *variable lags* in the cross-section of prices. A corollary of our conclusions is that the price effect of the 2022-23 rate hikes, if hypothetically viewed as a sequence of unanticipated change, would take up to 2026 or 2027 to be fully reflected in the data. We discuss potential mechanisms through which a faster response than suggested by our estimates might have occurred, by inspecting state-dependence and asymmetries in our local projection setup.

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<sup>2</sup>The idea is further examined in [Friedman \(1961\)](#). An interesting review of the origin of the term “long and variable lags” is provided by [Dupor \(2023\)](#).

**Literature.** Our work connects to three strands of research. The first literature estimates the effects of monetary policy, in particular using identified monetary policy shocks. A survey on different findings and methodologies is contained in the handbook chapter by [Ramey \(2016\)](#). Recent examples are [Aruoba and Drechsel \(2023\)](#) and [Bauer and Swanson \(2022\)](#).

The second literature spans work in macroeconomics that uses disaggregated (or micro-level) price data, with [Nakamura and Steinsson \(2008\)](#) being an influential example. Comprehensive surveys are provided by [Klenow and Malin \(2010\)](#) and [Nakamura and Steinsson \(2013\)](#). Some papers in this second literature intersect with the first literature on constructing IRFs to monetary policy shocks. An early approach in this direction is [Bernanke, Boivin, and Elias \(2005\)](#) who employ a factor-augmented vector autoregression (FAVAR) approach to construct IRFs of a large number of macroeconomic time series, including a few subcomponents of both the consumer price and producer price indexes. [Boivin, Giannoni, and Mihov \(2009\)](#) extend the FAVAR approach to include a much larger set of price series. [Bils, Klenow, and Kryvtsov \(2003\)](#) use a VAR approach to separately study the response of sticky and flexible price categories of goods, linking their analysis directly empirical work on price stickiness à la [Bils and Klenow \(2004\)](#). [Balke and Wynne \(2007\)](#) use 600 8-digit PPI price series to study the disaggregated effect of monetary policy shocks in a recursively identified VAR. Different from all aforementioned papers, we use local projections instead of (FA)VARs. [Borio et al. \(2021\)](#), [Luo and Villar \(2023\)](#) and [Arnaut and Bengali \(2024\)](#) estimate IRFs of price index subcomponents to identified monetary policy shocks using local projections. Relative to these papers, we develop an econometric methodology for re-aggregation of local projection based IRFs and carry out economically interesting re-aggregation experiments. [Guerrieri, Marcussen, Reichlin, and Tenreyro \(2023\)](#) look at responses of individual prices to monetary policy and oil supply shocks.<sup>3</sup> [Buda et al. \(2023\)](#) study responses to monetary policy shocks of data that is disaggregated as well as at high frequency.<sup>4</sup>

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<sup>3</sup>Interestingly, their responses are much more rapid than ours. We suspect this is due to the different sample and shock measure. [Guerrieri, Marcussen, Reichlin, and Tenreyro \(2023\)](#) use a monetary policy measure based on high-frequency surprises during a sample that includes the zero-lower bound period. As a consequence, their results likely pick up nonstandard monetary policy, which we attempt to exclude with our explicit focus on traditional interest rate policy.

<sup>4</sup>[Buda et al. \(2023\)](#) provide evidence of significant effects of monetary policy at very short horizons. Their analysis focuses on activity data, including consumption, sales and employment.

A particularly closely-related paper to ours is [Baumeister, Liu, and Mumtaz \(2013\)](#), who also focus on PCE responses, document positive and negative responses and provide theoretical explanations. These authors use a FAVAR with time-variation in the parameters. They find that over time fewer prices exhibit a positive response to a monetary tightening and that there is a decline in the dispersion of disaggregated price responses. While we do not focus on time-varying responses, we show that both positive responses as well as dispersion among different price responses is still significant according to our analysis. The model suggested by [Baumeister, Liu, and Mumtaz \(2013\)](#) connects with the theoretical discussion we provide for our findings.

The third literature we contribute to is concerned with econometric inference using local projections. Important contributions include [Jordà \(2005\)](#), [Plagborg-Møller and Wolf \(2021\)](#) and [Montiel Olea and Plagborg-Møller \(2021\)](#).<sup>5</sup> A survey is provided by [Jordà \(2023\)](#). We contribute to this literature by proposing a system estimator that takes into account dependence between cross-sectional local projection estimates, using a SUR and FGLS approach. To the best of our knowledge, this has not been done in a local projection setting. Our SUR approach is different from the way panel local projections have typically been applied in the recent macro literature (see [Almuzara and Sancibrián \(2024\)](#) for a survey and technical treatment), because we assume a different response to a macro shock for each price, instead of a common coefficient in the cross-section.

## 2 Methodology

This section presents our methodology. We discuss the choice of data, estimation sample and econometric specification.

### 2.1 Data and sample

**Price series.** We focus on the PCEPI because it is the price measure targeted by the Federal Reserve and because can be disaggregated in a way that is relatively

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It would be interesting to also consider high-frequency variation for prices, but this is not feasible with the PCEPI data provided by the BEA. Interesting work on collecting high-frequency price data is done by [Cavallo and Rigobon \(2016\)](#).

<sup>5</sup>Local projections have also been estimated with Bayesian approaches, see [Ferreira, Miranda-Agrippino, and Ricco \(2023\)](#) and [Barnichon and Brownlees \(2019\)](#).

consistent through time.<sup>6</sup> We retrieve the aggregate PCEPI and subcategories at different disaggregation levels from the BEA. The roughest level of disaggregation ('level 1') splits the index into 2 categories, goods and services. The next level ('level 2') splits it into 4 categories, durable goods, nondurable goods, services and consumption expenditures of nonprofit institutions serving households.<sup>7</sup> 'Level 3' of disaggregation contains 17 prices series, for example motor vehicles and parts or health care. 'Level 4' contains 70 categories, for example used motor vehicles or hospital and nursing home services. Finally, our finest level of disaggregation ('level 5') contains with 136 price categories, including used light trucks or nursing homes.<sup>8</sup> A detailed overview of these different disaggregation levels is provided in the Online Appendix.

**Monetary policy shocks.** We use the identified monetary policy shocks provided by [Aruoba and Drechsel \(2023\)](#). The methodology to estimate these shocks is based on natural language processing and machine learning techniques, applied to the Fed's Greenbook (Tealbook) documents, following [Romer and Romer \(2004\)](#). [Aruoba and Drechsel \(2023\)](#) back out exogenous variation in the target FFR. The methodology is not based on using surprise changes in market interest rates, as is done in related literature, which might also reflect information effects or effects of nonstandard monetary policy.

**Sample.** We focus on the 1982 to 2008 sample, during which the Fed targeted the FFR and non-standard monetary policy was not used as the main tool. Our choice of the sample period as well the type of monetary policy shock series allows us to draw a connection to monetary policy in 2022 and 2023, which was arguably conducted mainly through "traditional" interest hikes, in the same spirit as those in the pre-zero lower bound period.<sup>9</sup>

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<sup>6</sup>Disaggregation through time is more challenging for the Consumer Price Index (CPI), where the set of subcategories is more unbalanced. Nevertheless, there is also a fairly strong overlap between PCEPI and CPI.

<sup>7</sup>We will omit this fourth category in most of our analysis, because it carries a low weight in aggregate indices and is slightly more difficult to interpret than other subcomponents.

<sup>8</sup>We do not go finer than level 5 because it is not possible at those levels of disaggregation to split the index in a way that is balanced through time.

<sup>9</sup>During 2022 and 2023 the Fed also reduced the size of its balance through quantitative tightening. Arguably, this was done in a very gradual manner and the Fed' main policy tool was again the FFR. Indeed, [Wright \(2022\)](#) argues that the balance sheet shrinkage beginning in 2022 is likely to be gradual and unlikely to have large macroeconomic effects.

## 2.2 Local projections for price subcomponents

We construct IRFs using local projections ([Jordà, 2005](#)). While the aggregate price level is the subject of most previous IRF analyses, we employ local projections to different levels of disaggregation of the price level. Specifically, for each PCEPI subcomponent  $i = 1, \dots, N$ , where  $N$  depends on the level of disaggregation, we run the following regression separately for each horizon  $h = 0, \dots, H$ :

$$\log p_{i,t+h} = \alpha_{i,h} + \beta_{i,h} \hat{\varepsilon}_t^m + \gamma_{i,h} X_{i,t} + \delta_{i,h} \log p_{i,t-1} + u_{i,t+h}^h, \quad (1)$$

where  $t = 1, \dots, T$  indexes the observations through time.  $\hat{\varepsilon}_t^m$  denotes the identified monetary policy shock. The estimate of  $\beta_{i,h}$  represents the IRF of price category  $i$  at horizon  $h$  to the monetary policy shock.  $X_{i,t}$  is a vector that collects additional controls. As we run the local projection in (log) levels, we always include the first lag of the left hand side variable, that is,  $\log p_{i,t-1}$ . Including lags also helps to account for serially correlated errors, as shown by [Montiel Olea and Plagborg-Møller \(2021\)](#). We further discuss the issue of serially correlated errors below.

**Selection of controls.** In principle,  $\hat{\varepsilon}_t^m$  is an exogenous regressor, so it is not required for correct identification of  $\beta_{i,h}$  that controls  $X_{i,t}$  are included. However, the choice of the controls can matter for the precision of the estimates (see also [Plagborg-Møller and Wolf \(2021\)](#)). This might especially be the case for some PCEPI subcomponents, some of which are noisy times series. We therefore use a statistical model selection procedure to select controls among a set of macroeconomic variables and each variable's first 10 lags.<sup>10</sup> For each subcomponent  $i$ , in addition to a constant, one lag of the left hand side variable, we choose a set of up to 7 control variables that maximizes the fit of the regression at a year horizon ( $h = 24$ ), using a combinatorial approach. This approach amounts to running 2,404,808,340 regressions for each local projection specification selection and maximizing goodness-of-fit.<sup>11</sup> In the selected specification, we then include

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<sup>10</sup>These variables include log industrial production, the log of a commodity price index, the unemployment rate, the federal funds rate, the log S&P 500 index, and the log nominal broad U.S. dollar index. We also include the Greenbook forecasts of inflation.

<sup>11</sup>We varied this procedure in various ways and found it to give similar estimates for  $\beta_{i,h}$  as long as at least a handful of control variables were allowed to be selected. Interestingly we found that including the USD exchange rate among the selected regressors tended to sharpen the estimates.

the monetary policy shock and two lags of the shock.<sup>12</sup>

**Standard errors.** When we analyze IRFs, we compute HAC standard errors (Newey and West, 1987) for the estimator  $\hat{\beta}_{i,h}$ . We choose a bandwidth of  $h + 1$  as is common in the literature, see e.g. Ramey (2016).

### 2.3 Re-aggregation of IRFs using SUR

For a given level of disaggregation, suppose the aggregate PCEPI is defined as

$$P_t = \sum_i^N \omega_{i,t} p_{i,t}. \quad (2)$$

Note that in practice the PCEPI is not constructed as a simple weighted average of individual prices, but we use definition (2) for expositional purposes in this section and revisit it further below.

To study the response of the PCEPI to monetary policy shocks, we can run the specification in (1) using  $P_t$  instead of  $p_{i,t}$ . When doing so, we obtain the IRF of the aggregate price at horizon  $h$  as the coefficient on  $\hat{\varepsilon}_t^m$ , which we denote  $\hat{\mathcal{B}}_h$ .

Alternatively, we can run individual local projections for each price  $i$  and obtain the re-aggregated IRF estimate

$$\hat{\mathcal{B}}_h^{agg} = \sum_i^N \omega_{i,t} \hat{\beta}_{i,h}. \quad (3)$$

This is possible due to the linearity of the local projection and the linearity of the aggregation. In large samples,  $\hat{\mathcal{B}}_h$  and  $\hat{\mathcal{B}}_h^{agg}$  are identical.

The insight into the re-aggregation of individual IRFs allows us to construct counterfactual estimates. We can construct a hypothetical aggregate PCEPI response to a monetary policy shock, assuming different actual or hypothetical expenditure shares, instead of the true shares  $\omega_{i,t}$ . For example, we can use the weights for the

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<sup>12</sup>We also tried a LASSO approach as an alternative to our combinatorial method to select controls. The LASSO approach tends to select many more controls based on  $k$ -fold cross-validation. However, our selected specifications turn out to be preferable to the LASSO specification based on standard information criteria, such as the SIC. When we restrict the LASSO to select fewer variables it also picks less significant regressors and yields a worse SIC. Given the importance of controls for precision in small samples, we think that the SIC is a useful criterion.

year 2023 to obtain

$$\hat{\mathcal{B}}_h^{agg,2023} = \sum_i^N \omega_{i,2023} \hat{\beta}_{i,h}. \quad (4)$$

$\hat{\mathcal{B}}_h^{agg,2023}$  might be different from  $\hat{\mathcal{B}}_h^{agg}$  in interesting and economically meaningful ways. It is of particular interest to carry out a re-aggregation using these latest expenditure shares. Comparing this response to the response of the actual PCEPI itself will be informative about whether changing expenditure shares might have accelerated or decelerated the response of the aggregate price level to a change in monetary policy.

**Main econometric challenge and SUR approach.** A key issue with the construction of the re-aggregated IRF estimator  $\hat{\mathcal{B}}_h^{agg}$  is the construction of standard errors. When we run (1) for two different components  $i$  and  $j$  we would expect the estimates of  $\beta_{i,h}$  and  $\beta_{j,h}$ , to be correlated. In almost any macroeconomic model with a cross-section of different goods, there is some form of co-dependence between their prices. Therefore, to correctly compute standard errors for  $\hat{\mathcal{B}}_h^{agg}$  we need to obtain appropriate covariance estimates.

To do so, we define a SUR system for each horizon  $h$ . We first stack the observations in the time dimension, for each  $i$  and  $h$ :

$$\log \mathbf{p}_{i,h} = \alpha_{i,h} + \beta_{i,h} \hat{\boldsymbol{\epsilon}}^m + \gamma_{i,h} \mathbf{X}_i + \mathbf{u}_{i,h}, \quad (5)$$

where bold symbols indicate vectors and matrices that are stacked in the  $t$ -dimension. Next, we further stack the  $N$  local projection equations on top of each other, and combine the control variables, to define the SUR system

$$\begin{bmatrix} \log \mathbf{p}_{1,h} \\ \vdots \\ \log \mathbf{p}_{N,h} \end{bmatrix} = \begin{bmatrix} \tilde{\mathbf{X}}_1 & 0 & \dots & 0 \\ 0 & \tilde{\mathbf{X}}_2 & \dots & 0 \\ \vdots & \vdots & \ddots & \vdots \\ 0 & 0 & \dots & \tilde{\mathbf{X}}_N \end{bmatrix} \begin{bmatrix} \boldsymbol{\Gamma}_{1,h} \\ \vdots \\ \boldsymbol{\Gamma}_{N,h} \end{bmatrix} + \begin{bmatrix} \mathbf{u}_{1,h} \\ \vdots \\ \mathbf{u}_{N,h} \end{bmatrix} \quad (6)$$

or, more compactly,

$$\log \mathbf{p}_h = \tilde{\mathbf{X}} \boldsymbol{\Gamma}_h + \mathbf{u}_h. \quad (7)$$

Each  $\tilde{\mathbf{X}}_i$  collects a vector of ones, the monetary policy shock and its lags, the lag

of the left hand side variable and the other control variables selected for price component  $i$ . Correspondingly, each  $\Gamma_{i,h}$  collects  $\alpha_{i,h}$ ,  $\beta_{i,h}$ ,  $\gamma_{i,h}$  and  $\delta_{i,h}$ . In this system, we allow for dependence in the  $i$ -dimension, denote  $\mathbb{E}[\mathbf{u}'_{i,h}\mathbf{u}_{j,h}] = \sigma_{ij,h}$ , and define an  $N \times N$  matrix  $\Sigma_h$  where the  $(i, j)$ -th element is  $\sigma_{ij,h}$ . The covariance matrix of the stacked residual of the local projection system  $\mathbf{u}_h$  is  $\Omega_h \equiv \Sigma_h \otimes \mathbf{I}_T$ , where  $\otimes$  is the Kronecker product and  $\mathbf{I}_T$  an identity matrix of dimension  $T$ .

**Estimation via feasible GLS.** We proceed in two steps. First, we estimate the local projection for each price  $i$  at horizon  $h$  with OLS and retrieve  $N$  residual vectors  $\hat{\mathbf{u}}_{i,h}$ . We compute  $\hat{\sigma}_{ij,h} = \frac{1}{T}\hat{\mathbf{u}}'_{i,h}\hat{\mathbf{u}}_{j,h}$  to construct the estimate of the covariance matrix  $\hat{\Omega}_h = \hat{\Sigma}_h \otimes \mathbf{I}_T$ . Second, we run FGLS to obtain

$$\hat{\Gamma}_h^{FGLS} = \left( \tilde{\mathbf{X}}' \hat{\Omega}_h^{-1} \tilde{\mathbf{X}} \right)^{-1} \tilde{\mathbf{X}}' \hat{\Omega}_h^{-1} \log \mathbf{p}_h. \quad (8)$$

The IRFs at horizon  $h$  of each price to a monetary policy shock are the entries in the vector  $\hat{\Gamma}_h^{FGLS}$  that correspond to the position of the  $\beta_{i,h}$  coefficient in the stacked system (7). The covariance matrix of  $\hat{\Gamma}_h^{FGLS}$  is

$$Var(\hat{\Gamma}_h^{FGLS} | \tilde{\mathbf{X}}) = \hat{\sigma}_{FGLS}^2 \left( \tilde{\mathbf{X}}' \hat{\Omega}_h^{-1} \tilde{\mathbf{X}} \right)^{-1} \quad (9)$$

with

$$\hat{\sigma}_{FGLS}^2 = df^{-1} \left( \log \mathbf{p}_h - \tilde{\mathbf{X}} \hat{\Gamma}_h^{FGLS} \right)' \hat{\Omega}_h^{-1} \left( \log \mathbf{p}_h - \tilde{\mathbf{X}} \hat{\Gamma}_h^{FGLS} \right) \quad (10)$$

where  $df$  corresponds to the degrees of freedom.

**Standard errors of re-aggregated IRFs.** Now we can compute the standard error of the re-aggregated IRF  $\hat{\mathcal{B}}_h^{agg}$ , defined in (3), as

$$SE(\hat{\mathcal{B}}_h^{agg})^{SUR} = \sqrt{\sum_i^N \omega_i^2 \hat{\sigma}_{\hat{\beta}_{i,h}^{FGLS}}^2 + \sum_i^N \sum_{j \neq i}^N \omega_i \omega_j \hat{\sigma}_{\hat{\beta}_{i,h}^{FGLS}, \hat{\beta}_{j,h}^{FGLS}}}, \quad (11)$$

where  $\hat{\sigma}_{\hat{\beta}_{i,h}^{FGLS}}^2$  and  $\hat{\sigma}_{\hat{\beta}_{i,h}^{FGLS}, \hat{\beta}_{j,h}^{FGLS}}$  denote the variance and covariance estimators of the IRFs. These correspond to entries of the  $Var(\hat{\Gamma}_h^{FGLS} | \tilde{\mathbf{X}})$  matrix. In a “naive” aggregation where the OLS estimates are used and treated as independent, we

would have

$$SE(\hat{\mathcal{B}}_h^{agg})^{naive} = \sqrt{\sum_i^N \omega_i^2 \hat{\sigma}_{\hat{\beta}_{i,h}^{OLS}}^2}. \quad (12)$$

Since covariances between local projections estimates  $\hat{\sigma}_{\hat{\beta}_{i,h}^{FGLS}, \hat{\beta}_{j,h}^{FGLS}}$  can be either positive or negative, the difference between the naive standard error given by (12) and the correct one given by (11) cannot be signed.

To ensure that we draw inference for our re-aggregated IRF in the same way as for the individual IRFs, we additionally construct HAC standard errors in our FGLS system. This is possible by first computing the Cholesky factorization  $\Omega_h^{-1} = CC'$  and then setting up a regression of  $C \log p_h$  on  $C\tilde{X}$ . We then estimate this system via the Generalized Method of Moments (GMM). As for the individual local projections, we choose the bandwidth  $h + 1$ .<sup>13</sup>

## 2.4 Putting our econometric approach into perspective

**Relation with panel local projections.** Our SUR approach is different from the way panel local projection are often applied in the literature that studies microeconomic responses to macroeconomic shocks. A recent econometric treatment of panel local projections is given by [Almuzara and Sancibrián \(2024\)](#). In a typical version of such a panel local projection, we would assume that  $\beta_{i,h}$  is the same across individual units of observations. By adding an additional interaction term, the coefficient might differ across a selected characteristic, such as firm leverage or distance to default as in [Ottonello and Winberry \(2020\)](#) or type of borrowing constraint as in [Drechsel \(2023\)](#). In our approach, each unit of observation has a different  $\beta_{i,h}$ , which in effect amounts to a panel local projection where we interact the main coefficient with a cross-sectional fixed effect. Our re-aggregation procedure allows us to then average the heterogeneity in the effects, to obtain an aggregate IRF. This procedure could be relevant for other applications in which disaggregated local projections are constructed and aggregation is desired, including local projections at the household, firm or bank level.

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<sup>13</sup>In practice, we implement the FGLS estimation by first running each individual local projection only with the selected controls and without the monetary policy shock included, and then we carry out the FGLS estimation with the residuals of those regressions on the left hand side and only the monetary policy shock on the right hand side. This reduces the computational burden of the estimation.

**Relation with other GLS approaches to local projections.** The FGLS estimation in our SUR procedure relates to other approaches to estimating local projections using FGLS. For example, [Lusompa \(2023\)](#) proposes FGLS as a way to account for serially correlated errors in individual local projections, as an alternative to HAC standard errors. [Tanaka \(2020\)](#) also stacks the local projections for an individual variable across horizons and treats them as a multivariate regression (SUR) system with correlated residuals. Both approaches are different from our SUR/GLS approach because they are still an approach to the local projection for one individual variable and not a cross-section of variables. Our focus is on drawing correct inference about aggregated IRFs, which makes the potential dependence across different prices crucial. It is possible to *additionally* stack our system of local projections in the horizon dimension, that is, to collect all  $\log p_h, h = 0, \dots, H$  in one big vector and collect all control matrices  $\tilde{X}$  and parameter matrices  $\Gamma_h$  each in one big matrix. Estimating this “double-stacked” system with GLS is computationally challenging in our application, as it would involve inverting matrices of several million rows and columns. We only stack the system in the cross-sectional (price) dimension and additionally account for serially correlated errors in the local projection for each given price, by computing HAC standard errors with GMM, as discussed above.

### 3 Results for aggregate and disaggregated price indices

#### 3.1 Aggregate PCEPI response

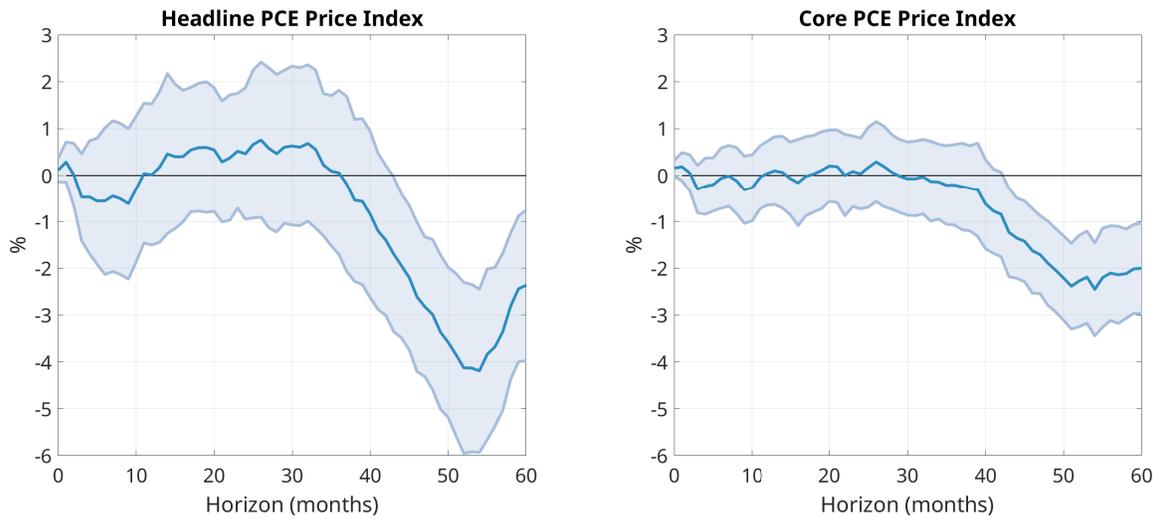
Figure 1 plots IRFs to a 1-unit (percentage point) monetary policy contraction.<sup>14</sup> The left panel shows the IRF of the headline PCEPI and the right panel the IRF of the core PCEPI, which excludes food and energy prices. In each case, we plot the response of 100 times the log of the index. The solid line reflects the point estimate and the shaded areas represent 90% confidence bands based on HAC standard errors.

The IRF of the headline PCEPI displays a gradual decline, turning significantly negative at conventional levels only after 43 months. The peak reduction occurs after 54 months and our point estimate amounts to a roughly 4% lower price level after a 100 basis point monetary policy contraction. Economically, this is a relatively

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<sup>14</sup>The Online Appendix presents the estimated IRF of the FFR to the shock.

**Figure 1: IRFS TO MONETARY POLICY TIGHTENING: AGGREGATE PRICE INDICES**



**Notes.** IRFs are estimated with local projections using the identified monetary policy shocks of [Aruoba and Drechsel \(2023\)](#). The shock is normalized to a 100 basis point increase and the unit of the left hand side is 100 times the log price index. Shaded areas represent 90% confidence bands based on HAC standard errors. The core PCEPI excludes food and energy prices.

sizeable response, but it occurs after a long lag. It is also noteworthy that the point estimate implies a slight increase in the PCEPI between years 1 and 3, but statistically it cannot be rejected that this response is equal to zero.

We estimate a very similar timing for the response of the core PCEPI. The magnitude of the response is smaller than for the total PCEPI, with a point estimate that implies a 2.5% price level reduction after a 100 basis point tightening shock. The IRF is estimated with greater precision than for the headline PCEPI. However, the long-lagged pattern is also visible for the core index.

The lagged patterns in aggregate price level responses shown in Figure 1 echo existing findings from the literature. For example, in [Christiano, Eichenbaum, and Evans \(1999\)](#), the aggregate price level does not fall to a statistically significant extent for 4 years after an FFR increase. The GDP deflator IRF we estimate in [Aruoba and Drechsel \(2023\)](#) is equally sluggish. In [Romer and Romer \(2004\)](#), the price level response to a monetary policy tightening, measured in terms of both the PCEPI and the CPI excluding shelter, turns significantly negative after 24 months.

In the Online Appendix, we provide a table with a comprehensive overview of corresponding price level responses to monetary policy shocks in the literature.

That analysis makes clear that the delayed responses we document are on the larger end but not unusual, given what the previous literature has found. Interestingly, there is some disagreement in the results between SVAR and narrative approaches on the one hand, and high-frequency approaches on the other hand. The latter approaches tend to find shorter horizons at which the effects first turn statistically significant. When it comes to the lag of the peak response, however, there is greater alignment between the findings with different methodologies to identify monetary policy shocks and estimate their effects.

What stands out about our estimates, also relative to other studies in the literature, is that it is not only generally gradual but that it is flat for several years. Our subsequent analysis unpacks the cross-sectional drivers of this pattern. It will reveal that underlying our estimated aggregate IRFs, we see strong heterogeneity in the responses of more disaggregated price indices, especially early on.

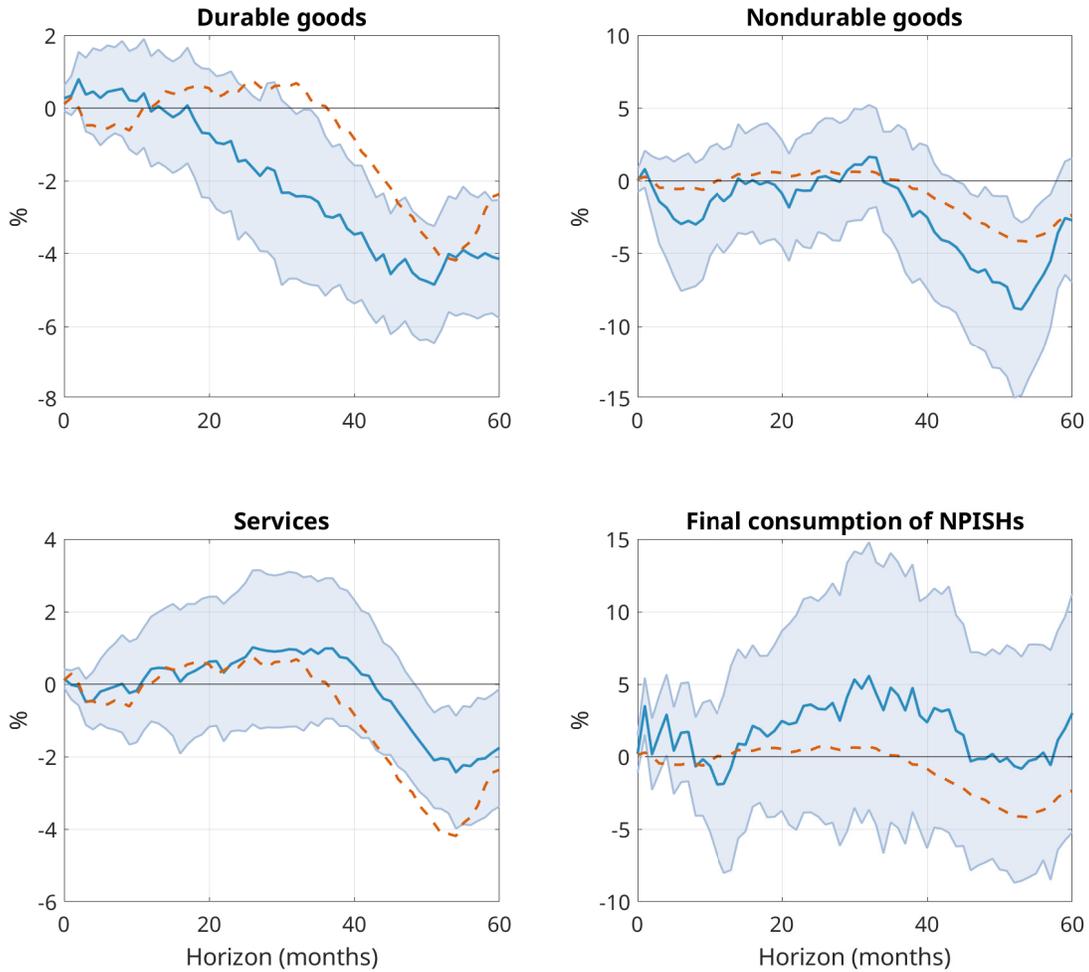
## 3.2 Responses of PCEPI subcomponents

We now analyze IRFs of disaggregated price indices, moving from rougher to finer levels of disaggregation. We skip the basic distinction between goods and services and begin with the second level of disaggregation, which separates durable goods, nondurable goods and services. We move all the way to the fifth level of disaggregation with 136 price categories.

**Disaggregation level 2.** Figure 2 plots the IRFs of prices of durable goods, nondurable goods and services to a monetary policy tightening. The figure also shows the response of prices of consumption of nonprofit institutions serving households (NPISHs), the fourth price component at this level of disaggregation. In each panel, we also superimpose the point estimate of the aggregate headline PCEPI IRF from the left panel in Figure 1, as a dashed line.

Comparing the different panels of the figure makes clear that already at this relatively rough level of disaggregation, there is meaningful heterogeneity in the dynamics of prices following a monetary policy tightening. Prices of durable goods decline at the fastest pace, with a statistically significant response after 2.5 years. They show a peak reduction of around 5% after roughly 4 years. The fact that the durable goods sector is more interest-rate sensitive is a well-known fact in the literature. See e.g. [Erceg and Levin \(2006\)](#); [McKay and Wieland \(2021\)](#).

**Figure 2: IRFS TO MONETARY POLICY TIGHTENING: DISAGGREGATION LEVEL 2**



**Notes.** IRFs estimated with local projections using the identified monetary policy shocks of [Aruoba and Drechsel \(2023\)](#). The shock is normalized to a 100 basis point increase and the unit of the left hand side is 100 times the log price index. Shaded areas represent 90% confidence bands based on HAC standard errors. The dashed line in each panel corresponds to the point estimate of the IRF of the aggregate headline PCEPI. NPISHs are nonprofit institutions serving households.

Nondurable goods prices take much longer to decline. The point estimate is more sizable than for durable goods at around 8%, but also less precisely estimated. The IRF of services prices looks most similar to the aggregate PCEPI response, but is slightly slower and smaller in magnitude. The NPISH response is entirely insignificant. In the subsequent analysis, we exclude NPISH categories, because they carry a negligible weight on the aggregate PCEPI, accounting for only 2.2% of

expenditures.

**Disaggregation level 3.** Figure 3 plots the IRFs of prices in the third level of disaggregation, which amounts to 15 price subcomponents (excluding two NPISH categories). We again show the point estimate 90% HAC bands and superimpose the aggregate PCEPI response as a dashed line.

The figure reveals quite drastic differences in the price responses to a monetary policy tightening. After a monetary policy contraction, some important price categories respond negatively after a long delay or even a positive initial response, while others fall more rapidly. Especially at short horizons there are differences across categories, with negative, positive and many flat responses. At longer horizons, the responses of the different price categories start getting more into sync, with many of them becoming significantly negative.

In particular, we find that important categories such as gasoline, food and beverages off premises, and transportation services respond negatively after a long delay. For some components, the initial response to an interest rate increase is even positive, such as for motor vehicles.<sup>15</sup> For the motor vehicle category, it turns out that the positive response is driven by the subcategory of used motor vehicles (not separately shown in Figure 3). One potential explanation might be that new vehicle purchases are so interest rate sensitive that substitution from new to used vehicles drives up the price of used vehicles.

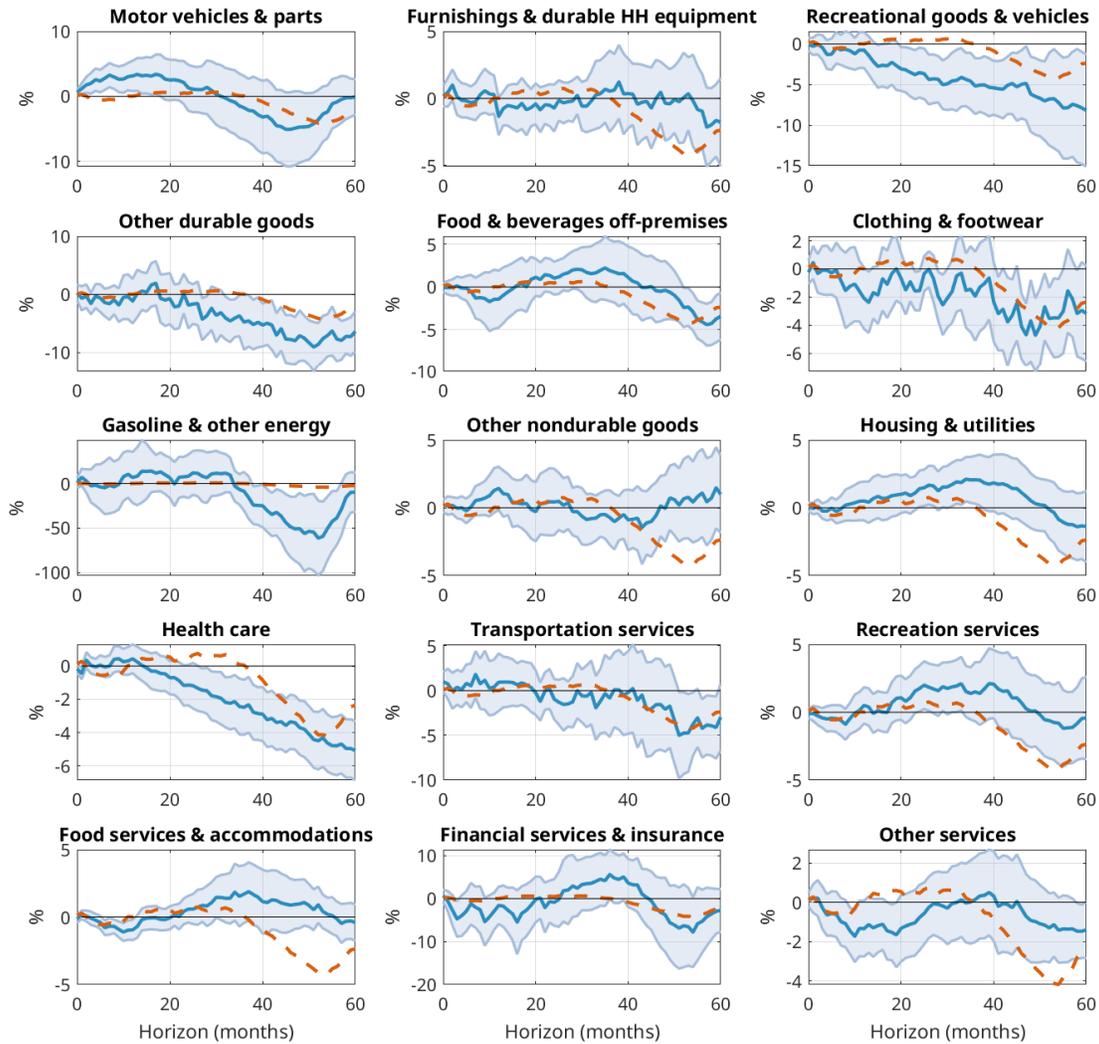
Other categories, such as clothing and footwear or recreational goods, fall more rapidly after a contractionary shock. In general, several of the durable goods categories tend to respond more swiftly, which links back to the discussion of the responses at disaggregation level 2. Several categories show responses that are not distinguishable from zero over all horizons.

The differences in magnitude across the variables are also substantial. For example, the response of gasoline and other energy products amounts to a reduction of almost 50% in the price level. The point estimates of other variables are also in the double digits of percent changes. In the Online Appendix, we show a version of Figure 3 in which we divide each IRF by the historical standard deviation of the respective (log) price series. This version of the IRFs makes clear that the responses

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<sup>15</sup>For some categories, we can tie back the positive responses to energy. For example, the price index for housing and utilities shows a positive (though insignificant) response for quite some time. We found that this is largely driven by the utilities subcategory, in particular electricity.

**Figure 3: IRFS TO MONETARY POLICY TIGHTENING: DISAGGREGATION LEVEL 3**



**Notes.** IRFs estimated with local projections using the identified monetary policy shocks of [Aruoba and Drechsel \(2023\)](#). The shock is normalized to a 100 basis point increase and the unit of the left hand side is 100 times the log price index. Shaded areas represent 90% confidence bands based on HAC standard errors. The dashed line in each panel corresponds to the point estimate of the IRF of the aggregate headline PCEPI. We exclude categories related to nonprofit institutions serving households, which carry a negligible weight on the aggregate.

are not as large when viewed in light of the historical standard deviation of a given price series. For example, in terms of standard deviations, the peak reduction in the price of gasoline and other energy products is just over 0.1 standard deviations, relative to around 50% in levels. These numbers reflect that this category is just generally extremely volatile.

**Disaggregation level 5.** We skip disaggregation level 4, which amounts to 70 price components, and go directly to the finest disaggregation level considered by our analysis. This level consists of 136 different prices.<sup>16</sup> As plotting individual IRFs becomes visually unappealing, we summarize the insights from our analysis of IRFs at this disaggregation level by means of different types of figures. The Online Appendix includes the full set of individual IRFs.

At disaggregation level 5, we find that there are around 13% of price categories for which IRFs to monetary policy contractions is never significant in any direction. Around 17% of the price categories have responses that turn positive at least once but never negative. That is, 40 IRFs at this level of disaggregation (around 30%) are never significantly negative. Also, out of the 136 series at level 5, exactly half have IRFs that are significantly positive at least once.

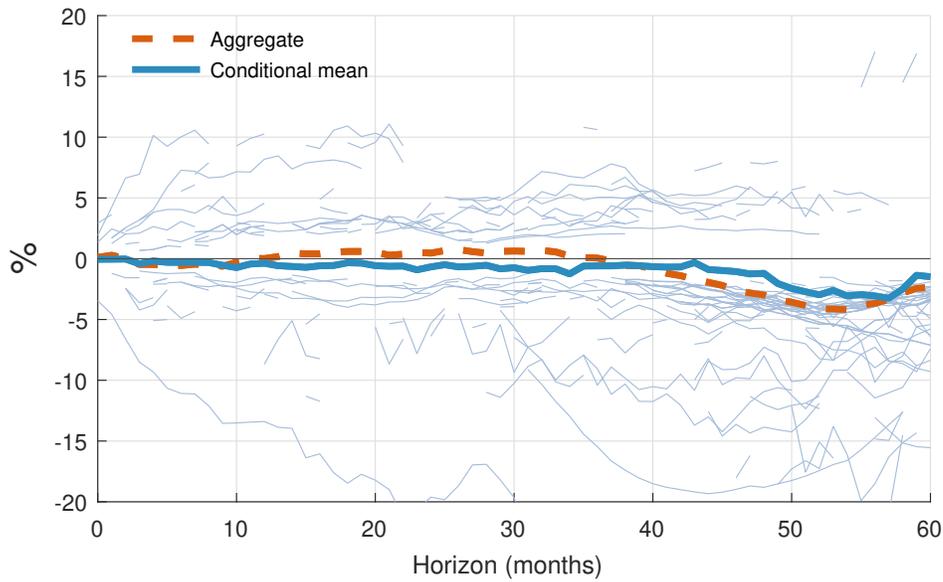
Figure 4, Panel (a) plots all disaggregation level-5 IRFs together with their mean and the aggregate response PCEPI response, but focuses only on those segments of the IRFs that are statistically significant. The plot shows that some price components are persistently and significantly positive and some are negative, even at quite large horizons. It also reveals that more responses become significantly negative at longer horizons, and positive responses cease to be statistically significant. Interestingly, the range of values of the negative IRFs widens as more IRFs turn negative. Panel (b) shows the fraction of price series that show a significant positive or negative response across horizons. At any given horizon, over 50% of series show an insignificant response. Early on, the shares of positive and negative responses are roughly the same, leading to the flat response, and then eventually as enough series

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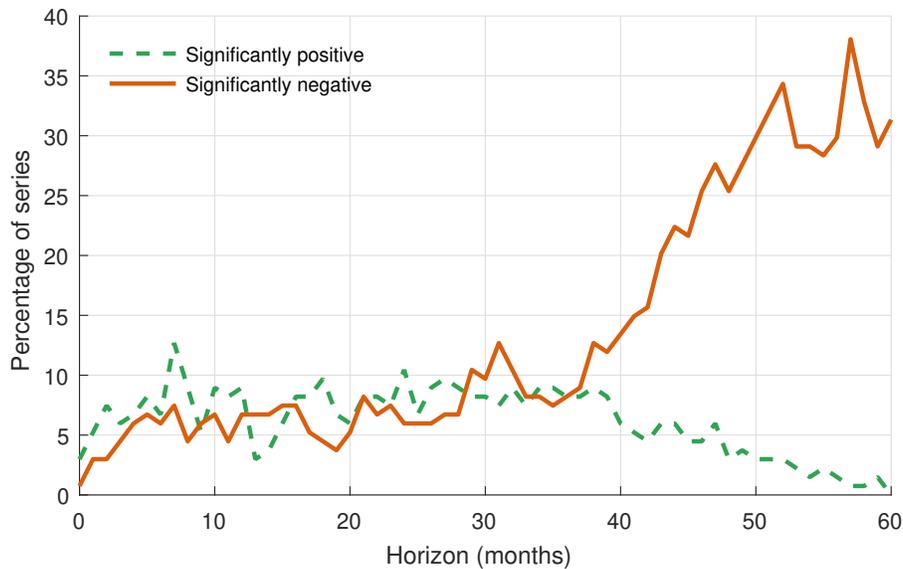
<sup>16</sup>At disaggregation level 5, the set of price components starts become unbalanced, with some categories entering or dropping out over our the sample period. We construct a balanced version of level 5 by taking level 4 and replacing all items for which data is available for all level 5 from 1959M1 onwards. There are two reasons why level 5 items may not be available. Either the level 4 item is simply not subdivided into further items (level 4 is the first level with such "terminal" items, such as "Sporting equipment, supplies, guns, and ammunition"), or at least one sub item only entered the PCEPI after 1959M1, for example "Video and audio streaming and rental" starts in 1982M1.

**Figure 4:** INSPECTING SIGNIFICANTLY NEGATIVE RESPONSES AT LEVEL 5

**(a)** Significant segments of IRFs



**(b)** Fraction of significantly positive/negative IRFs



**Notes:** Panel (a) plots those segments of disaggregation level-5 IRFs that show a significant across horizons (some outliers have been removed). The response labeled 'Aggregate' refers to the headline PCE response and the one labeled 'Conditional mean' refers to the average of the significant segments of the disaggregated IRFs. Panel (b) shows the fraction of level-5 IRFs that show a significant positive or negative response across horizons.

show a negative response, the overall PCEPI response goes negative.

The most central insight of our analysis of price subcomponents is that the reason why the headline and core response is flat and fall after 4 years is *not* because all prices are unchanged for 4 years. On the contrary, many of them change but both positive responses and different turning points make it hard to get a clean negative response in the aggregate until enough of the series start falling. It is only at horizons of several years that the price decline after a monetary policy tightening is broad-based across many price categories.

### 3.3 Responses of PCEPI contributions

In equation (2), we made the simplification that the aggregate index is a weighted sum of individual prices. However, the BEA's PCEPI is constructed as a chain-linked Fisher index. This means that the PCEPI is the geometric average of two distinct fixed-basket measures of the price level, the Laspeyres and Paasche indices. Thus, it is a nonlinear combination of all quantities and prices from consecutive periods. Consequently, the PCEPI cannot exactly be decomposed additively.

In addition to disaggregated price indices, the BEA releases data on the contribution of each subcomponent to PCEPI inflation, at different horizons. We denote this as  $con_{i,t}^q$ . Formally, PCEPI inflation over  $q$  months can be written as the sum of contributions

$$\Delta^q P_t \equiv \sum_i^N con_{i,t}^q, \quad (13)$$

where  $\Delta^q$  denotes the log-difference between  $t + q$  and  $t$ .<sup>17</sup> The  $con_{i,t}^q$  terms track the net contributions of each component to PCEPI inflation across time. Thus, they not only track the item's price but also the item's relative weight in the PCEPI. Since the  $con_{i,t}^q$  terms are contributions to the growth rate of the price level, we can cumulate them through time. We denote this *contribution level* with  $m_{i,t}^q$ . It can be recursively

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<sup>17</sup>For each price series  $i$ , we compute the contribution to PCEPI inflation between periods  $t$  and  $t + q$  using the additive disaggregation shown by [Reinsdorf et al. \(2002\)](#):

$$con_{i,t}^q = \frac{q_{it} + q_{it+q}(P_F/Q_F)}{\mathbf{p}'_t \mathbf{q}_t + (\mathbf{p}'_t \mathbf{q}_t) P_F} (p_{it+q} - p_{it}),$$

where  $p_{it}$ ,  $q_{it}$  are component  $i$ 's price and quantity in period  $t$ , bold letters represent vectors of prices or quantities, and  $P_F$  and  $Q_F$  are the price and quantity Fisher indices, respectively. The Fisher indices are  $P_F = \sqrt{(\mathbf{p}'_{t+q} \mathbf{q}_t / \mathbf{p}'_t \mathbf{q}_t)(\mathbf{p}'_{t+q} \mathbf{q}_{t+q} / \mathbf{p}'_t \mathbf{q}_{t+q})}$  and  $Q_F = \sqrt{(\mathbf{p}'_t \mathbf{q}_{t+q} / \mathbf{p}'_t \mathbf{q}_t)(\mathbf{p}'_{t+q} \mathbf{q}_{t+q} / \mathbf{p}'_{t+q} \mathbf{q}_t)}$ .

defined as  $con_{i,t}^q = \Delta^q m_{i,t}^q$ , where the first observation is normalized to 100 for each subcomponent  $i$ . Running local projections for the level objects  $m_{i,t}^q$  instead of the growth rate objects  $con_{i,t}^q$  delivers more precise IRF estimates. We focus on one-month ahead inflation ( $q = 1$ ) and drop the  $q$  superscript from now on.

It is insightful to construct IRFs of the contribution levels to a monetary policy shock. We can do so with the same setup as in (1), but using  $m_{i,t+h}$  instead of  $p_{i,t+h}$  on the left hand side. The estimates of these ‘contribution IRFs’ now *exactly* sum up to the IRF of the aggregate PCEPI. Consequently, one would only estimate a large response when a combination of three factors occurs: (i) a large response in the price series, (ii) a large increase in the weight of the price series, or (iii) a large initial weight in the PCEPI.

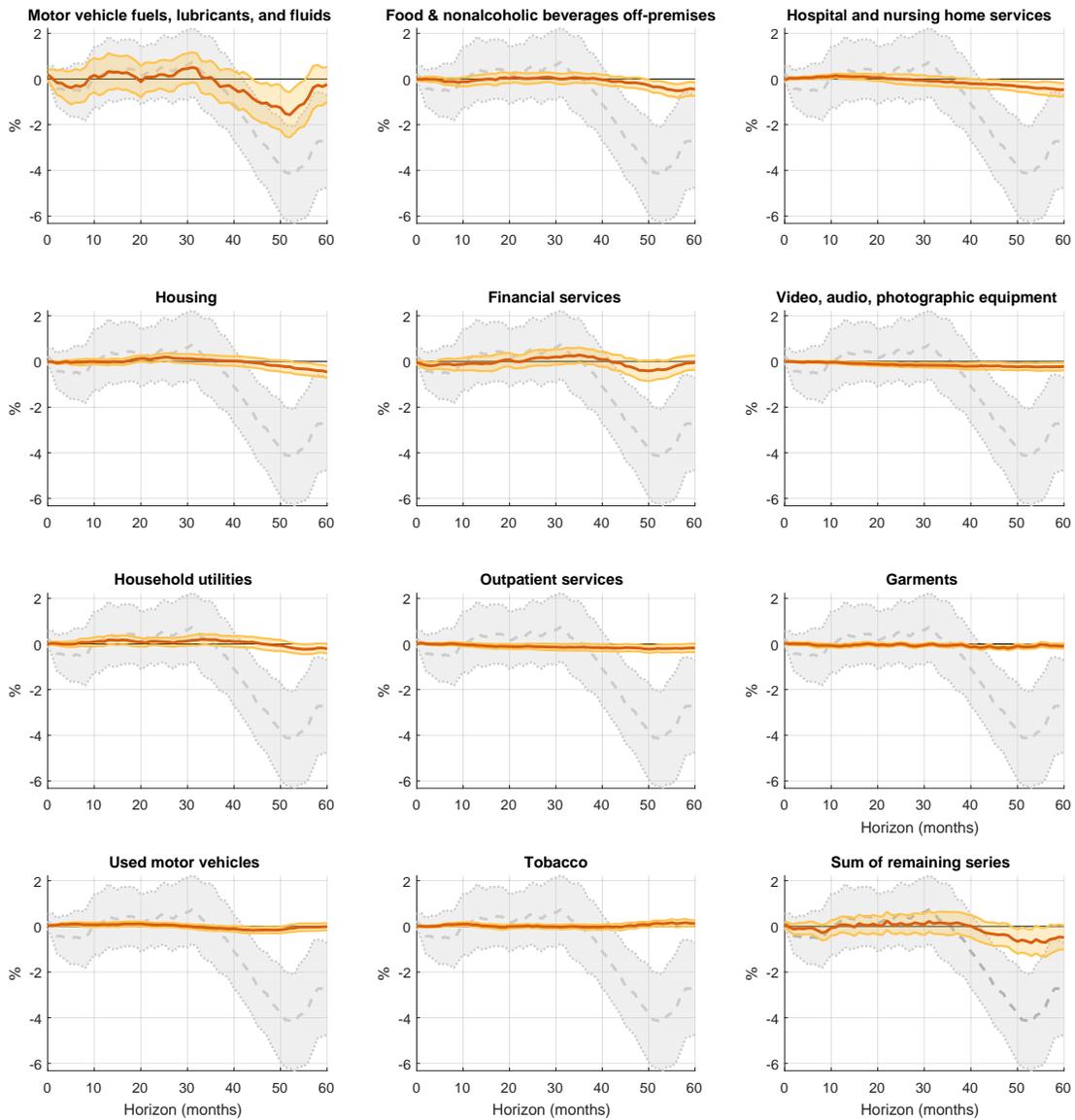
Figure 5 shows the contribution IRFs at disaggregation level 4. In separate panels, we plot the IRFs for the 11 price subcomponents with the strongest contribution to the aggregate PCEPI, in descending order. We also show as a separate IRF the sum of all remaining contribution IRFs in one panel (on the bottom right). By construction, all IRFs in the figure add up to the total PCEPI IRF, which we superimpose in each panel for comparison.

The figure reveals several insights. First, there is a lot of heterogeneity in the responses. Second, there are some positive price responses to a monetary tightening. The two insights confirm the results in the previous subsection. Third, a few components have a disproportionately large effect on the aggregate response. In fact, almost all contribution IRFs are quite flat throughout and almost all are entirely flat for the first few years. The strongest contribution comes from motor vehicle fuels, lubricants and fluids, which is a subcategory of gasoline and other energy goods. Other categories with strong contributions are food and nonalcoholic beverages off-premises and hospitals and nursing home services. Several IRFs do show a significantly negative sign after around 40 months. This is also the case for the sum of the remaining categories.

### 3.4 Interpreting our cross-sectional findings

We find that a monetary policy tightening triggers both positive, negative and many flat price responses at short horizons and a broad-based decline in prices at long horizons. While there is no clear consensus on the responses of PCEPI subcomponents to monetary policy shocks in the existing literature, and this is in

**Figure 5: IRFS TO MONETARY POLICY TIGHTENING: CONTRIBUTION SERIES**



**Notes.** IRFs of contribution series (computation described in the text), estimated with local projections using the identified monetary policy shocks of [Aruoba and Drechsel \(2023\)](#). The shock is normalized to a 100 basis point increase and the unit of the left hand side is 100 times the log price index. Shaded areas represent 90% confidence bands based on HAC standard errors. The dashed line in each panel corresponds to the point estimate of the IRF of the aggregate headline PCEPI.

fact part of the motivation for our analysis, there are some previous empirical results that point in the same direction. The closest finding is in [Boivin et al. \(2009\)](#), who

use a FAVAR approach. See in particular the top right panel in their Figure 3. These authors conclude that “a striking feature is that most indices respond very little for several months following the shock, and start falling only later.” [Baumeister et al. \(2013\)](#) obtain similar results using a FAVAR with time-varying parameters. The results in [Balke and Wynne \(2007\)](#) based on PPI data also look related to ours in that there first is a long delay and then a negative response in the aggregate price level.

Which theories of price adjustment might best explain the findings represented by our subcomponent IRFs? In what follows, we go over some basic theories of price adjustment. While the set of theories we consider might not be exhaustive, we think this discussion helps to interpret our results theoretically. First, [Calvo \(1983\)](#) pricing cannot generate IRFs to monetary policy shocks like the ones we estimate. In a Calvo model, there is a direct negative relationship between the peak response of a price to a monetary policy shock and the main Calvo parameter, which captures the probability that a firm cannot adjust its price. We can verify empirically whether our IRFs exhibit such a relation with empirical estimates of price adjustment. Figure 6 plots the peak response of a given price in our IRFs against the price adjustment frequency estimates across PCEPI categories of [Carvalho, Lee, and Park \(2021\)](#).<sup>18</sup> We normalize the peak response by each series’ historical standard deviation. The figure shows that there is, if anything, a weakly positive relationship between our peak response and the time it takes, unconditionally, for prices to adjust. A similar finding is presented in [Luo and Villar \(2023\)](#) (see their Figure 5a). Richer DSGE models with Calvo adjustment frictions ([Smets and Wouters, 2007](#)) or multi-sector models with heterogeneity in Calvo price stickiness ([Pasten et al., 2020](#)) also cannot explain our results.

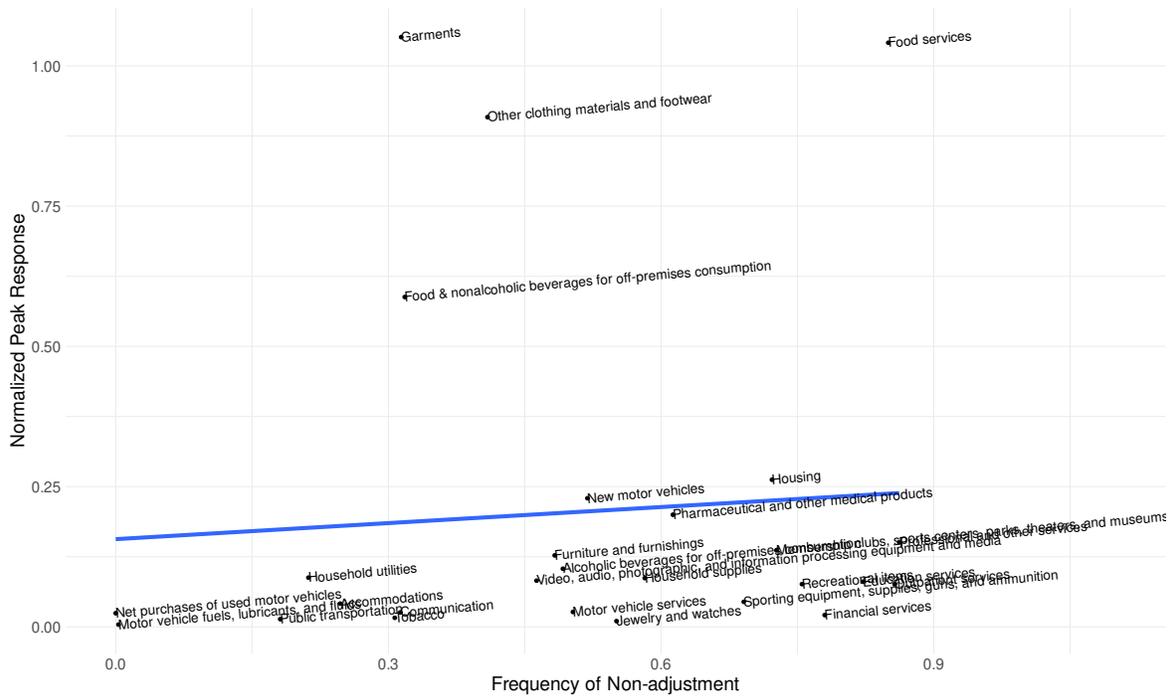
Second, our IRFs are not consistent with menu cost models in the tradition of [Golosov and Lucas \(2007\)](#). In the standard menu cost model, as the menu cost increases and thus the frequency of price changes falls, the response of inflation to unanticipated increases in nominal money supply monotonically decreases. There is no mechanism to make the response of firm-level prices switch signs. A firm either changes its price the same direction as the change in nominal money supply, because it is willing to pay the menu cost, or it does not change prices at all.<sup>19</sup>

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<sup>18</sup>In the Calvo framework, peak response and impact response coincide. So we can compare the Calvo model to multiple objects in the data, we choose the peak of our IRFs as the data analogue.

<sup>19</sup>[Gautier and Le Bihan \(2022\)](#) build a multi-sector menu cost model in which there is stronger

**Figure 6:** LAGS IN IRF PEAK RESPONSE VS. EMPIRICAL ESTIMATES OF PRICE STICKINESS



**Notes:** Scatter plot between the number of months at which the peak response of a given price occurs in our IRFs, normalized by the standard deviation of the respective price, (y axis) and price adjustment frequency estimates across PCEPI categories of [Carvalho, Lee, and Park \(2021\)](#).

The third set of theories to consider are those with information frictions. The sticky information model of [Mankiw and Reis \(2002\)](#) does not generate IRFs with an initial flat region and then a delay later on or positive responses of some producers. See for example the IRFs of inflation to a monetary policy shock in [Reis \(2009\)](#), which respond instantaneously. A flat region in the IRF is also not present in the comparison of sticky and noisy information models in [Woodford \(2001\)](#). [Mackowiak and Wiederholt \(2009\)](#) focus on rational inattention. In their model, IRFs to different shocks can have a large delay, but they are hump-shaped instead of first being flat and then showing a strong response after several years, like our estimated IRFs.<sup>20</sup> The sticky expectations model of [Auclert et al. \(2020\)](#) features an inflation response

money non-neutrality (which means inflation responds less to monetary policy shocks). But these authors do not report individual price responses.

<sup>20</sup>Further models of monetary policy with information frictions that do not generate IRFs similar to our estimates are [Adam \(2007\)](#) and [Melosi \(2016\)](#).

that is quite gradual, but also does not feature a flat part early on. Interestingly, the empirically estimated price level IRF in [Auclert et al. \(2020\)](#) based on [Romer and Romer \(2004\)](#) shocks is insignificant for several years, similar to ours.

We speculate that a model that can generate the patterns we document across subcomponents might have at least one of two features. First, there could be a cost channel through which higher nominal rates act like an increase in marginal costs to some sectors, as discussed by [Barth and Ramey \(2001\)](#) and modeled in a one-sector economy by [Ravenna and Walsh \(2006\)](#). For example, a monetary policy tightening could constrain supply of firms with financial constraints that tighten when nominal interest rates rise. If there is heterogeneity in such a cost channel across sectors, monetary policy shocks could act as aggregate demand shocks to all sectors but also as supply shocks to those sectors that feature a strong cost channel, with the aggregate demand effect eventually dominating across sectors at long horizons. [Baumeister et al. \(2013\)](#) suggest a multi-sector sticky-price model with a cost channel, in order to explain empirical price IRFs that include positive and negative responses across subcomponents. This framework comes closest what we envision as a suitable framework. We view further theoretical explorations in this direction as a promising avenue for future research.<sup>21</sup>

Second, there could be a strong demand substitution channel between different goods and services. If higher interest rates lower demand for one good and consumers instead substitute into an alternative good, then the price of the alternative good might rise, or stay stable, in the short run. As total demand decreases, all prices fall eventually as substitution forces fade away and the aggregate demand force dominates. We mentioned the possibility of such an effect as a possible explanation for the difference in the new and used vehicle responses above.

These theoretical mechanisms might arise in particular in network economies. In their analysis of PPI series, [Balke and Wynne \(2007\)](#) find that there are more initially positive responses in final goods than in intermediate goods, and more in intermediate goods than in crude goods prices. In other words, the more downstream a product is, the more likely is an initially positive response. They speculate that an input-output structure with heterogeneous financial constraints could explain their findings because, in such a model, a monetary tightening would

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<sup>21</sup>[Gilchrist et al. \(2017\)](#) and [Kim \(2020\)](#) study the interaction of financial frictions and price setting at the firm-level.

act as a cost-push shock for some (financially constrained) sectors, while in other sectors the traditional demand shock would outweigh. The model of [Luo and Villar \(2023\)](#) also generates sector specific cumulative price responses that range from negative to positive.<sup>22</sup> This mechanism connects to the idea of “Keynesian supply shocks” in multi-sector economies developed by [Guerrieri et al. \(2022\)](#).

## 4 Results from re-aggregation experiments

This section turns to our re-aggregation experiments. As explained in Section 2.3, we take individual IRFs at a given level of disaggregation and then re-build an aggregate price level IRF using hypothetical expenditure weights. We use a SUR approach to correctly aggregate standard errors such that they can account for cross-sectional dependence.

As explained in previous sections, the PCEPI is not exactly an expenditure weighted sum but a chain-linked Fisher index. Therefore, there is some approximation error in all of our re-aggregated IRFs. We verified that this approximation error is small enough to only have a negligible influence our graphical comparisons below.<sup>23</sup>

**Headline PCEPI estimates with weights from different years.** Figure 7, Panels (a)-(d), show different IRFs that are re-aggregated to the headline PCEPI IRF, together with the IRF estimated the actual aggregate headline PCEPI. We consider re-aggregation of the level-3 IRFs and level-5 IRFs and in each case we use both 1959 expenditure weights and 2023 expenditure weights.<sup>24</sup>

The SUR-based re-aggregation of our individual IRFs implies that, independent of whether 1959 or 2023 expenditure shares are used to re-aggregate, the price level falls with a similar timing than estimated with the aggregate series itself.

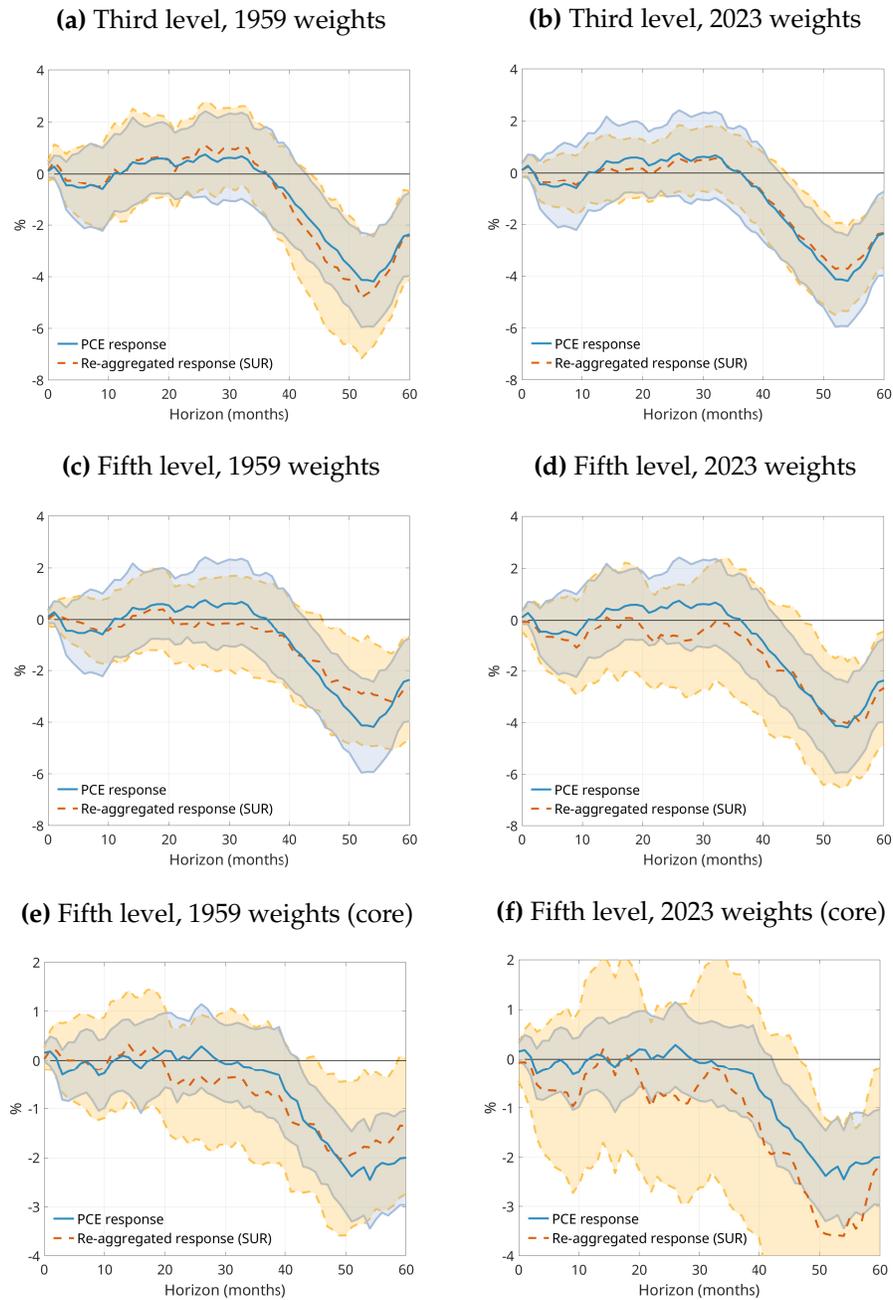
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<sup>22</sup>A network structure itself would not be sufficient without the two effects described in the previous paragraph. For example, in the model of [Afrouzi and Bhattarai \(2023\)](#) all inflation responses seem to move in the same direction. Interestingly, the network structure does introduce persistence.

<sup>23</sup>Specifically, we compared the actual aggregate PCEPI with a re-aggregation of subcomponents using the current expenditure weights for each year. These two series and their IRFs to monetary policy shocks turn out to be close to identical.

<sup>24</sup>While the estimation period for the individual IRFs is 1982 to 2008, nothing prevents us from using expenditure shares from earlier or later periods. We use the earliest and latest year for which we have these shares available from the BEA, 1959 and 2023. In the Online Appendix, we consider all years in between.

**Figure 7: RE-AGGREGATION EXPERIMENTS FOR DIFFERENT YEARS**



**Notes:** IRFs of headline PCEPI (Panels a, b, c, d) and core PCEPI (Panels e, f) to identified monetary policy shocks. Each panel contains the IRF based on re-aggregation procedure, using different levels of disaggregation and different expenditure shares (dashed lines). Each panel also shows the re-aggregated IRF as well the IRF of aggregate headline PCEPI as the solid lines. The shaded areas represent 90% significance bands based on HAC standard errors, and in the case of the re-aggregation accounting for cross-sectional dependence.

This is visible when comparing panel (a) with (b) and comparing panel (c) with (d). The magnitude of the reduction is also similar. This finding implies that changing expenditure shares through time, e.g. because of structural change, have not accelerated the response of the PCEPI to monetary policy.<sup>25</sup>

In the Online Appendix, we also provide a graphical analysis that uses the weights for every single year from 1959 to 2023, separately for different horizons. PCE shares are somewhat stale, that is, computed with a significant lag themselves, so they are likely not suitable for a year-by-year comparison. However, considering longer-term trends over a period of almost 80 years makes clear that they do not exhibit enough change to alter the response of the re-aggregated PCEPI to monetary policy shocks.

**Core PCEPI estimates with weights from different years.** Figure 7, Panels (e)-(f), repeats the analysis of Panels (c)-(d) but focuses on core PCEPI instead of headline PCEPI, re-aggregating the fifth disaggregation level. For core PCEPI, we find somewhat larger difference between the actual and the re-aggregated response. What is also different from the headline PCEPI picture is that the re-aggregated response becomes noisier. Broadly speaking, the conclusion that changes in expenditure shares have not accelerated the response of inflation to monetary policy, remains intact.

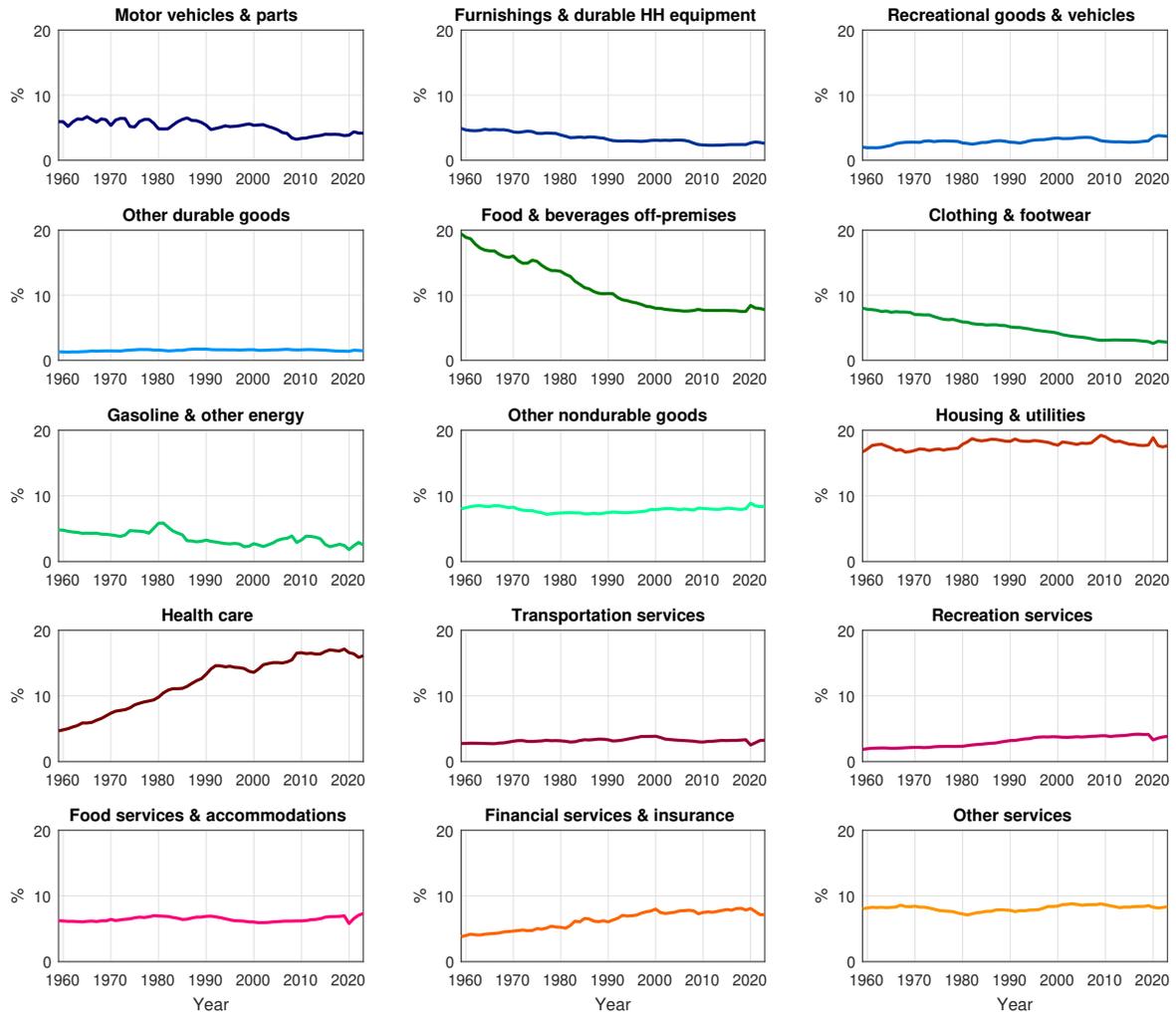
**How have expenditure weights changes through time?** We further interpret our re-aggregation result against the backdrop of the most important changes in consumer behavior. Figure 8 plots the expenditure shares corresponding to disaggregation level 3 from 1959 to 2023. It is evident that expenditure shares are relatively stable through time. The most marked changes in expenditure shares that have happened over the last decades are a decrease in the share for food and beverages (-12 percentage points) and an increase for health care (+11 percentage points).

Both of these expenditure categories respond to monetary policy with a similarly long lag. Since we employ local projections with constant coefficients, our methodology and data cannot rule out that price stickiness or other structural

---

<sup>25</sup>The Online Appendix provides a comparison between the PCEPI IRF and the IRF of an index that we rebuilt using the data (rather than the estimated IRFs) of the level-3 subcomponents, with 2023 weights.

**Figure 8: CONSUMPTION EXPENDITURE SHARES THROUGH TIME**



**Notes:** Consumption expenditure shares through time. These correspond to expenditure categories from disaggregation level 3, for which IRFs are shown in Figure 3.

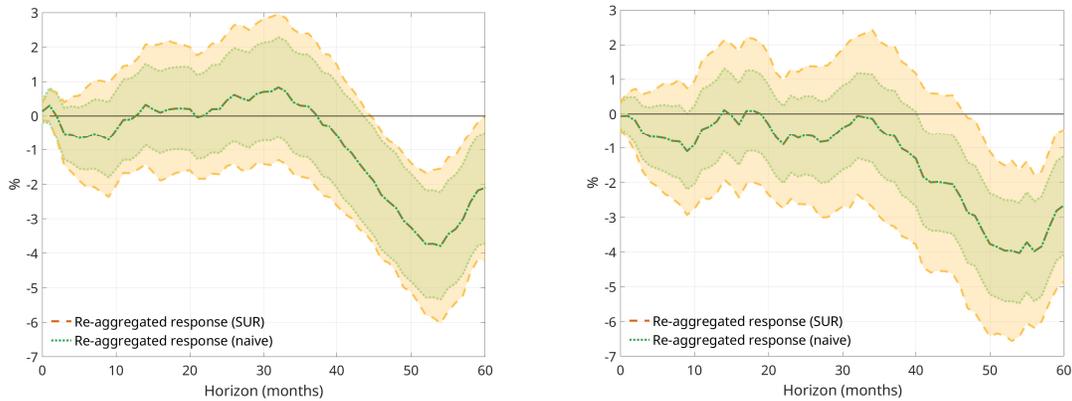
features in all or important categories might have changed over time. Such changes could have accelerated the response of prices to monetary policy over time, for example if price stickiness has fallen. However, health care services remain among the most rigid and least cyclically sensitive price categories (Stock and Watson, 2020; Carvalho, Lee, and Park, 2021). Note that health care services are also a category for which price measurement is notoriously difficult and imprecise.

**SUR-based aggregation vs. naive aggregation.** Figure 9 examines in more detail the role of correctly adjusting the standard errors to account for cross-sectional dependence in the response of different price components to monetary policy shocks. For two selected cases, the re-aggregation of level-2 IRF with 2023 expenditure weights as well as the re-aggregation of level-5 IRFs with 2023 expenditure weights, we show different IRF estimates. The dashed lines represent the correct SUR based estimate in which the bands account for dependence between different prices. The dotted line represents a naive re-aggregation where the OLS estimates are used and no estimated covariance terms are taken into account. In other words, the estimates are treated as independent.

The figure shows that, while the difference in the standard errors between these two approaches cannot be signed (see discussion in Section 2.3), we find that the errors are generally larger when we take dependence into account. Our interpretation is that price movements are mostly positively related and therefore imply positive covariance terms. It is noteworthy that for the naive version and a confidence level slightly lower than the 90% level we use throughout, one would reject a zero response early on.

**Figure 9:** THE ROLE OF CORRECT INFERENCE IN AGGREGATING

**(a)** Second level, 2023 weights, headline PCEPI      **(b)** Fifth level, 2023 weights, headline PCEPI



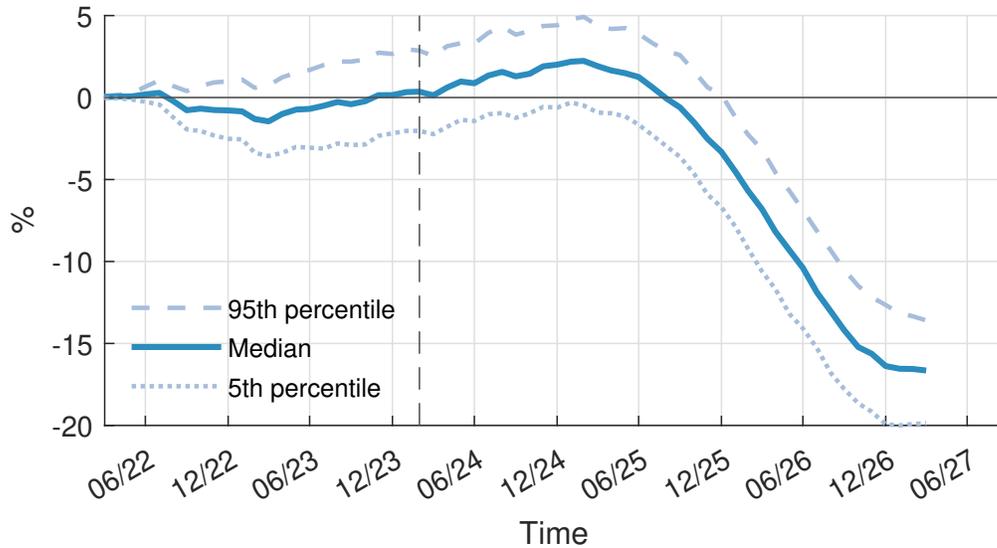
**Notes:** The dashed lines represent the correct SUR based estimate in which the bands account for dependence between different prices. The dotted line represents a naive re-aggregation where the OLS estimates are used and no estimated covariance terms are taken into account.

## 5 Broader discussion of our findings

**Long and variable lags in price responses.** Our results indicate that “long and variable lags” in the transmission of monetary policy, as described by [Friedman \(1960, 1961\)](#), are alive and well. The lags in the responses to monetary policy are *long* both for the aggregate price index and for individual price categories. While the attribute *variable* in Friedman’s original insight referred to variability across episodes, we find large differences in the size and precise timing of the response across different prices. We provide evidence of variable lags in the cross-section of prices.

The evidence uncovered by our analysis suggests that the response of inflation to the Fed tightening in 2022-2023, if hypothetically viewed as a sequence of exogenous monetary policy shocks, might not yet be fully reflected in recent economic data. To illustrate this point visually, [Figure 10](#) plots the cumulated PCEPI reduction that, according to our estimates, would result from the Fed’s interest rate increases that occurred between March 2022 and July 2023. This calculation is intentionally provocative, as it conceptualizes the Fed’s sequence of decisions as pure monetary policy shocks and assumes no other shocks occurred in the meantime. We do not intend this to be interpreted as a serious policy counterfactual, but as an illustration

**Figure 10:** CUMULATED PCEPI REDUCTION CORRESPONDING TO FED HIKES BEGINNING IN 2022



**Notes:** Cumulated estimated headline PCEPI reduction resulting from the Fed interest rate increases between March 2022 and July 2023, with 90% error bands. This calculation interprets the Fed’s decisions as pure monetary policy shocks.

that puts the timing implied by our findings into the context of the sequence of policy changes that occurred in the last few years. The figure makes clear that the estimated lags in the reaction of prices to monetary policy are so long that, based on this provocative interpretation, *none* of the Fed’s interest rate increases would be reflected in the inflation figures before the end of 2025. Of course, while this exercise helps to visualize the length of the lags we estimate, the Fed’s recent tightening should not be viewed as a series of exogenous shocks. Indeed, [Aruoba and Drechsel \(2023\)](#) estimate the Fed’s decisions in 2022-2023 as largely systematic.

**What may be different now?** There are several mechanisms that might render the lags in the response to monetary policy shorter, especially at the current juncture. In other words, there are various reasons why the analysis in Figure 10 is a limited interpretation of the price level effects of recent Fed policy. A monetary tightening that is very rapid, such as the one in 2022-23, might have a different effect on inflation, a form of nonlinearity in the effects. The effects of a policy tightening when inflation is already high might be stronger, a form of state-dependency. Or

the effects might generally be stronger when monetary policy tightens rather than when it eases (see also [Tenreyro and Thwaites \(2016\)](#)).

The Online Appendix explores state-dependence in our estimates. It shows the results from adding an interaction between the monetary policy shock and a dummy variable that is one in above-median inflation periods and zero in below-median inflation periods. We focus on both headline and core PCEPI on the left hand side of the local projection and plot the coefficient on the interaction term. This means that what appears in the plot is what is *added* to the IRFs in Figure 1 in high inflation periods. The point estimates for headline PCEPI indicate large negative effects. This means that in high inflation periods, the negative response to a monetary policy tightening might be quicker and stronger. However, the coefficient is estimated very imprecisely. We can only reject the null hypothesis that there is no state-dependence until around 30 months, a horizon that would still be considered a very long lag in the effects of monetary policy. The results for core PCEPI, shown as a separate plot, are insignificant across all horizons. Interestingly, a recent study by [Canova and Perez Forero \(2024\)](#) finds that in high inflation periods, the effects of monetary policy actually take longer than on average.

The Online Appendix also investigates asymmetries in our effects. It shows the results from adding an interaction between the monetary policy shock and a dummy variable that is one when the monetary policy shock is positive and zero when it is negative. Again, we focus on both headline and core PCEPI on the left hand side of the local projection and plot the coefficient on the interaction term. This means that what appears in the plot is what is *added* to the IRFs in Figure 1 when the shock reflects a tightening rather than an easing in monetary policy. While the point estimates are large and negative, we cannot reject the null hypothesis of no asymmetries, at any horizon and for both price level measures.

## 6 Conclusion

This paper investigates how monetary policy affects PCEPI subcomponents. We find evidence of lags in the response of prices to monetary policy shocks that are *long* in the time dimension and *variable* in the cross-section of prices. The reason why aggregate price level measures remain flat for several years after a monetary policy tightening is not because all prices are unchanged initially. On the contrary,

many prices change but both positive responses and different turning points make it hard to get a clean negative response in the aggregate until enough of the price series start falling. It is only at a horizon of several years that the decline is broad-based across most price categories. Using a re-aggregation procedure, in which we account for dependence in individual price estimates via a SUR approach, we can study hypothetical PCEPI responses to a monetary policy tightening using counterfactual expenditure shares. We find that changes in expenditure share have not accelerated the long-lagged response of inflation to monetary policy. Our findings have implications for the right calibration and time profile of monetary policy decisions, now and in the future.

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ONLINE APPENDIX TO  
**The long and variable lags of monetary policy:  
Evidence from disaggregated price indices**  
by S. Borağan Aruoba and Thomas Drechsel

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# A PCEPI categories at different levels of disaggregation

**Table A.1:** PCEPI CATEGORIES AT DIFFERENT LEVELS OF AGGREGATION

| Level | Label  | Code     | 5*  |
|-------|--|----------|-----|
| 0     | Personal consumption expenditures  | PCE      | —   |
| 1     | Goods  | PCE1     | —   |
| 2     | Durable goods  | PCE11    | —   |
| 3     | <i>Motor vehicles and parts</i>  | PCE111   | —   |
| 4     | New motor vehicles   | PCE1111  | —   |
| 5     | New autos  | PCE11111 | Yes |
| 5     | New light trucks   | PCE11112 | Yes |
| 4     | Net purchases of used motor vehicles                                       | PCE1112  | —   |
| 5     | Used autos   | PCE11121 | Yes |
| 5     | Used light trucks  | PCE11122 | Yes |
| 4     | Motor vehicle parts and accessories  | PCE1113  | —   |
| 5     | Tires  | PCE11131 | Yes |
| 5     | Accessories and parts  | PCE11132 | Yes |
| 3     | <i>Furnishings and durable household equipment</i>                         | PCE112   | —   |
| 4     | Furniture and furnishings  | PCE1121  | —   |
| 5     | Furniture  | PCE11211 | Yes |
| 5     | Clocks, lamps, lighting fixtures, and other household decorative items     | PCE11212 | Yes |
| 5     | Carpets and other floor coverings  | PCE11213 | Yes |
| 5     | Window coverings   | PCE11214 | Yes |
| 4     | Household appliances   | PCE1122  | —   |
| 5     | Major household appliances   | PCE11221 | Yes |
| 5     | Small electric household appliances  | PCE11222 | Yes |
| 4     | Glassware, tableware, and household utensils                               | PCE1123  | —   |
| 5     | Dishes and flatware  | PCE11231 | Yes |
| 5     | Nonelectric cookware and tableware   | PCE11232 | Yes |
| 4     | Tools and equipment for house and garden                                   | PCE1124  | —   |
| 5     | Tools, hardware, and supplies  | PCE11241 | Yes |
| 5     | Outdoor equipment and supplies   | PCE11242 | Yes |
| 3     | <i>Recreational goods and vehicles</i>                                     | PCE113   | —   |
| 4     | Video, audio, photographic, and information processing equipment and media | PCE1131  | —   |
| 5     | Video and audio equipment  | PCE11311 | Yes |
| 5     | Photographic equipment   | PCE11312 | Yes |
| 5     | Information processing equipment   | PCE11313 | Yes |
| 4     | Sporting equipment, supplies, guns, and ammunition                         | PCE1132  | Yes |
| 4     | Sports and recreational vehicles   | PCE1133  | —   |
| 5     | Motorcycles  | PCE11331 | Yes |
| 5     | Bicycles and accessories   | PCE11332 | Yes |
| 5     | Pleasure boats, aircraft, and other recreational vehicles                  | PCE11333 | Yes |
| 4     | Recreational books   | PCE1134  | Yes |
| 4     | Musical instruments  | PCE1135  | Yes |
| 3     | <i>Other durable goods</i>   | PCE114   | —   |
| 4     | Jewelry and watches  | PCE1141  | —   |
| 5     | Jewelry  | PCE11411 | Yes |

Continued on next page

Table A.1 – continued from previous page

| Level | Label  | Code     | 5*  |
|-------|--|----------|-----|
| 5     | Watches  | PCE11412 | Yes |
| 4     | Therapeutic appliances and equipment   | PCE1142  | —   |
| 5     | Therapeutic medical equipment  | PCE11421 | Yes |
| 5     | Corrective eyeglasses and contact lenses   | PCE11422 | Yes |
| 4     | Educational books  | PCE1143  | Yes |
| 4     | Luggage and similar personal items   | PCE1144  | Yes |
| 4     | Telephone and related communication equipment  | PCE1145  | Yes |
| 2     | Nondurable goods   | PCE12    | —   |
| 3     | <i>Food and beverages purchased for off-premises consumption</i>                           | PCE121   | —   |
| 4     | Food and nonalcoholic beverages purchased for off-premises consumption                     | PCE1211  | —   |
| 5     | Food purchased for off-premises consumption  | PCE12111 | Yes |
| 5     | Nonalcoholic beverages purchased for off-premises consumption                              | PCE12112 | Yes |
| 4     | Alcoholic beverages purchased for off-premises consumption                                 | PCE1212  | —   |
| 5     | Spirits  | PCE12121 | Yes |
| 5     | Wine   | PCE12122 | Yes |
| 5     | Beer   | PCE12123 | Yes |
| 4     | Food produced and consumed on farms  | PCE1213  | Yes |
| 3     | <i>Clothing and footwear</i>   | PCE122   | —   |
| 4     | Garments   | PCE1221  | —   |
| 5     | Women's and girls' clothing  | PCE12211 | Yes |
| 5     | Men's and boys' clothing   | PCE12212 | Yes |
| 5     | Children's and infants' clothing   | PCE12213 | Yes |
| 4     | Other clothing materials and footwear  | PCE1222  | —   |
| 5     | Clothing materials   | PCE12221 | Yes |
| 5     | Standard clothing issued to military personnel   | PCE12222 | —   |
| 5     | Shoes and other footwear   | PCE12223 | Yes |
| 3     | <i>Gasoline and other energy goods</i>   | PCE123   | —   |
| 4     | Motor vehicle fuels, lubricants, and fluids  | PCE1231  | —   |
| 5     | Gasoline and other motor fuel  | PCE12311 | Yes |
| 5     | Lubricants and fluids  | PCE12312 | Yes |
| 4     | Fuel oil and other fuels   | PCE1232  | —   |
| 5     | Fuel oil   | PCE12321 | Yes |
| 5     | Other fuels  | PCE12322 | Yes |
| 3     | <i>Other nondurable goods</i>  | PCE124   | —   |
| 4     | Pharmaceutical and other medical products  | PCE1241  | —   |
| 5     | Pharmaceutical products  | PCE12411 | Yes |
| 5     | Other medical products   | PCE12412 | Yes |
| 4     | Recreational items   | PCE1242  | —   |
| 5     | Games, toys, and hobbies   | PCE12421 | Yes |
| 5     | Pets and related products  | PCE12422 | Yes |
| 5     | Flowers, seeds, and potted plants  | PCE12423 | Yes |
| 5     | Film and photographic supplies   | PCE12424 | Yes |
| 4     | Household supplies   | PCE1243  | —   |
| 5     | Household cleaning products  | PCE12431 | Yes |
| 5     | Household paper products   | PCE12432 | Yes |
| 5     | Household linens   | PCE12433 | Yes |
| 5     | Sewing items   | PCE12434 | Yes |
| 5     | Miscellaneous household products   | PCE12435 | Yes |
| 4     | Personal care products   | PCE1244  | —   |
| 5     | Hair, dental, shaving, and miscellaneous personal care products except electrical products | PCE12441 | Yes |

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Table A.1 – continued from previous page

| Level | Label   | Code     | 5*  |
|-------|---|----------|-----|
| 5     | Cosmetic / perfumes / bath / nail preparations and implements                         | PCE12442 | Yes |
| 5     | Electric appliances for personal care   | PCE12443 | Yes |
| 4     | Tobacco   | PCE1245  | Yes |
| 4     | Magazines, newspapers, and stationery   | PCE1246  | —   |
| 5     | Newspapers and periodicals  | PCE12461 | Yes |
| 5     | Stationery and miscellaneous printed materials  | PCE12462 | Yes |
| 5     | Expenditures abroad by U.S. residents   | PCE12471 | Yes |
| 5     | Less: Personal remittances in kind to nonresidents                                    | PCE12472 | —   |
| 4     | Net expenditure abroad by U.S. residents  | PCE1248  | —   |
| 1     | Services  | PCE2     | —   |
| 2     | Household consumption expenditures (for services)                                     | PCE21    | —   |
| 3     | <i>Housing and utilities</i>  | PCE211   | —   |
| 4     | Housing   | PCE2111  | —   |
| 5     | Rental of tenant-occupied nonfarm housing   | PCE21111 | Yes |
| 5     | Imputed rental of owner-occupied nonfarm housing                                      | PCE21112 | Yes |
| 5     | Rental value of farm dwellings  | PCE21113 | Yes |
| 5     | Group housing   | PCE21114 | Yes |
| 4     | Household utilities   | PCE2112  | —   |
| 5     | Water supply and sanitation   | PCE21121 | Yes |
| 5     | Electricity and gas   | PCE21122 | Yes |
| 3     | <i>Health care</i>  | PCE212   | —   |
| 4     | Outpatient services   | PCE2121  | Yes |
| 5     | Physician services  | PCE21211 | —   |
| 5     | Dental services   | PCE21212 | —   |
| 5     | Paramedical services  | PCE21213 | —   |
| 4     | Hospital and nursing home services  | PCE2122  | —   |
| 5     | Hospitals   | PCE21221 | Yes |
| 5     | Nursing homes   | PCE21222 | Yes |
| 3     | <i>Transportation services</i>  | PCE213   | —   |
| 4     | Motor vehicle services  | PCE2131  | Yes |
| 5     | Motor vehicle maintenance and repair  | PCE21311 | —   |
| 5     | Other motor vehicle services  | PCE21312 | —   |
| 4     | Public transportation   | PCE2132  | —   |
| 5     | Ground transportation   | PCE21321 | Yes |
| 5     | Air transportation  | PCE21322 | Yes |
| 5     | Water transportation  | PCE21323 | Yes |
| 3     | <i>Recreation services</i>  | PCE214   | —   |
| 4     | Membership clubs, sports centers, parks, theaters, and museums                        | PCE2141  | —   |
| 5     | Membership clubs and participant sports centers                                       | PCE21411 | Yes |
| 5     | Amusement parks, campgrounds, and related recreational services                       | PCE21412 | Yes |
| 5     | Admissions to specified spectator amusements  | PCE21413 | Yes |
| 5     | Museums and libraries   | PCE21414 | Yes |
| 4     | Audio-video, photographic, and information processing equipment services              | PCE2142  | Yes |
| 5     | Cable, satellite, and other live television services                                  | PCE21421 | —   |
| 5     | Photo processing  | PCE21422 | —   |
| 5     | Photo studios   | PCE21423 | —   |
| 5     | Repair and rental of audio-visual, photographic, and information processing equipment | PCE21424 | —   |
| 5     | Video and audio streaming and rental  | PCE21425 | —   |
| 4     | Gambling  | PCE2143  | —   |
| 5     | Casino gambling   | PCE21431 | Yes |

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Table A.1 – continued from previous page

| Level | Label  | Code     | 5*  |
|-------|--|----------|-----|
| 5     | Lotteries  | PCE21432 | Yes |
| 5     | Pari-mutuel net receipts   | PCE21433 | Yes |
| 4     | Other recreational services  | PCE2144  | —   |
| 5     | Veterinary and other services for pets                               | PCE21441 | Yes |
| 5     | Package tours  | PCE21442 | Yes |
| 5     | Maintenance and repair of recreational vehicles and sports equipment | PCE21443 | Yes |
| 3     | <i>Food services and accommodations</i>                              | PCE215   | —   |
| 4     | Food services  | PCE2151  | —   |
| 5     | Purchased meals and beverages  | PCE21511 | Yes |
| 5     | Food furnished to employees (including military)                     | PCE21512 | Yes |
| 4     | Accommodations   | PCE2152  | —   |
| 5     | Hotels and motels  | PCE21521 | Yes |
| 5     | Housing at schools   | PCE21522 | Yes |
| 3     | <i>Financial services and insurance</i>                              | PCE216   | —   |
| 4     | Financial services   | PCE2161  | —   |
| 5     | Financial services furnished without payment                         | PCE21611 | Yes |
| 5     | Financial service charges, fees, and commissions                     | PCE21612 | Yes |
| 4     | Insurance  | PCE2162  | —   |
| 5     | Life insurance   | PCE21621 | Yes |
| 5     | Net household insurance  | PCE21622 | Yes |
| 5     | Net health insurance   | PCE21623 | Yes |
| 5     | Net motor vehicle and other transportation insurance                 | PCE21624 | Yes |
| 3     | <i>Other services</i>  | PCE217   | —   |
| 4     | Communication  | PCE2171  | Yes |
| 5     | Telecommunication services   | PCE21711 | —   |
| 5     | Postal and delivery services   | PCE21712 | —   |
| 5     | Internet access  | PCE21713 | —   |
| 4     | Education services   | PCE2172  | —   |
| 5     | Higher education   | PCE21721 | Yes |
| 5     | Nursery, elementary, and secondary schools                           | PCE21722 | Yes |
| 5     | Commercial and vocational schools                                    | PCE21723 | Yes |
| 4     | Professional and other services                                      | PCE2173  | —   |
| 5     | Legal services   | PCE21731 | Yes |
| 5     | Accounting and other business services                               | PCE21732 | Yes |
| 5     | Labor organization dues  | PCE21733 | Yes |
| 5     | Professional association dues  | PCE21734 | Yes |
| 5     | Funeral and burial services  | PCE21735 | Yes |
| 4     | Personal care and clothing services                                  | PCE2174  | —   |
| 5     | Personal care services   | PCE21741 | Yes |
| 5     | Clothing and footwear services                                       | PCE21742 | Yes |
| 4     | Social services and religious activities                             | PCE2175  | Yes |
| 5     | Child care   | PCE21751 | —   |
| 5     | Social assistance  | PCE21752 | —   |
| 5     | Social advocacy and civic and social organizations                   | PCE21753 | —   |
| 5     | Religious organizations' services to households                      | PCE21754 | —   |
| 5     | Foundations and grantmaking and giving services to households        | PCE21755 | —   |
| 4     | Household maintenance  | PCE2176  | Yes |
| 5     | Domestic services  | PCE21761 | —   |
| 5     | Moving, storage, and freight services                                | PCE21762 | —   |
| 5     | Repair of furniture, furnishings, and floor coverings                | PCE21763 | —   |

Continued on next page

Table A.1 – continued from previous page

| Level | Label  | Code     | 5*  |
|-------|--|----------|-----|
| 5     | Repair of household appliances   | PCE21764 | —   |
| 5     | Other household services   | PCE21765 | —   |
| 5     | Foreign travel by U.S. residents   | PCE21771 | —   |
| 5     | Less: Expenditures in the United States by nonresidents                              | PCE21772 | —   |
| 5     | Net foreign travel (synthetic)   | PCE2178  | —   |
| 2     | Final consumption expenditures of nonprofit institutions serving households (NPISHs) | PCE22    | —   |
| 3     | <i>Gross output of nonprofit institutions</i>  | PCE221   | —   |
| 4     | Health, gross output   | PCE2211  | —   |
| 5     | Outpatient services, gross output  | PCE22111 | Yes |
| 5     | Nonprofit hospitals, gross output  | PCE22112 | Yes |
| 5     | Nonprofit nursing homes, gross output  | PCE22113 | Yes |
| 4     | Recreation services, gross output  | PCE2212  | Yes |
| 4     | Education services, gross output   | PCE2213  | Yes |
| 4     | Social services, gross output  | PCE2214  | Yes |
| 4     | Religious organizations, gross output  | PCE2215  | Yes |
| 4     | Foundations and grantmaking and giving establishments, gross output                  | PCE2216  | Yes |
| 4     | Social advocacy establishments, gross output   | PCE2217  | Yes |
| 4     | Civic and social organizations, gross output   | PCE2218  | Yes |
| 4     | Professional advocacy, gross output  | PCE2219  | Yes |
| 3     | <i>Less: Receipts from sales of goods and services by nonprofit institutions</i>     | PCE222   | —   |
| 4     | Health services to households  | PCE2221  | —   |
| 5     | Outpatient services to households  | PCE22211 | Yes |
| 5     | Nonprofit hospitals services to households   | PCE22212 | Yes |
| 5     | Nonprofit nursing homes services to households                                       | PCE22213 | Yes |
| 4     | Recreation services to households  | PCE2222  | Yes |
| 4     | Education services to households   | PCE2223  | Yes |
| 4     | Social services to households  | PCE2224  | Yes |
| 4     | Religious organizations' services to households                                      | PCE2225  | Yes |
| 4     | Foundations and grantmaking and giving services to households                        | PCE2226  | Yes |
| 4     | Services of social advocacy establishments to households                             | PCE2227  | Yes |
| 4     | Civic and social organizations' services to households                               | PCE2228  | Yes |
| 4     | Professional advocacy services to households   | PCE2229  | Yes |

## B Lagged inflation responses found in the literature

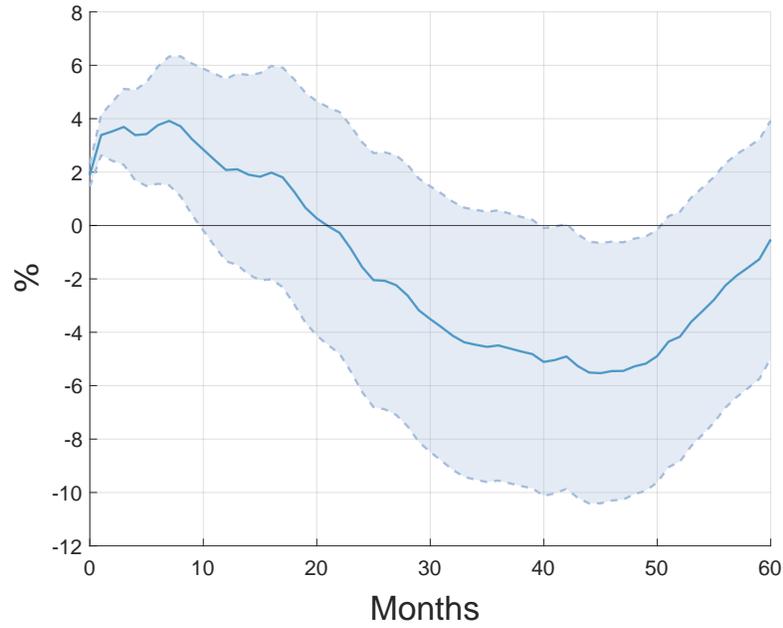
**Table B.1:** Responses of inflation/price level measure to monetary policy shocks

| Paper                            | Estimator           | Identification Type     | Sample           | Peak Response | First Negative |
|----------------------------------|---------------------|-------------------------|------------------|---------------|----------------|
| Jorda et al (JME, 2020)          | LP-IV               | Greenbook               | 1870 – 2006      | 48 (final)    | 27             |
| Auclert et al (2020)             | LP                  | Greenbook               | 1969:3 – 1996:12 | 60 (final)    | 44             |
| Aruoba & Drechsel (2023)         | BVAR                | Greenbook               | 1984:2 – 2016:12 | 35            | –              |
| Romer and Romer (2004)           | LP                  | Greenbook               | 1969:3 - 1996:12 | 48 (final)    | 24             |
| Gertler & Karadi (2015)          | Proxy SVAR          | High-frequency surprise | 1979:7 – 2012:6  | 42            | 32             |
| Kekre & Lenel (2022)             | Proxy SVAR          | High-frequency surprise | 1979:7 – 2012:6  | 45            | 0              |
| Gagliardone & Gertler (2023)     | Proxy SVAR          | High-frequency surprise | 1973:1 – 2019:12 | 32            | 0              |
| Jarocinski & Karadi (2020)       | VAR                 | Sign-restricted HF      | 1990 – 2006      | 30            | 1              |
| Swanson (2023)                   | VAR                 | HF surprise             | 1973 – 2008      | 20            | 0              |
| Bauer & Swanson (2023)           | Proxy SVAR          | HF surprise             | 1979:7 – 2012:6  | 35            | 0              |
| Miranda-Agrippino & Ricco (2021) | Proxy SVAR          | HF surprise             | 1972:1 – 2014:12 | 24 (final)    | 0              |
| Miranda-Agrippino & Ricco (2021) | Proxy SVAR          | Narrative               | 1972:1 – 2014:12 | 6             | –              |
| Miranda-Agrippino & Ricco (2021) | Proxy SVAR          | Informationally robust  | 1972:1 – 2014:12 | 24 (final)    | 0              |
| Kaminska et al (2021)            | Bayesian LP         | HF surprise             | 1990 – 2007      | 0             | –              |
| Bu et al (2021)                  | SVAR                | Fama and MacBeth (1973) | 1994 – 2017      | 8             | 6              |
| Bu et al (2021)                  | LP                  | Fama and MacBeth (1973) | 1994 – 2017      | 8             | 6              |
| Bernanke et al (2005)            | FAVAR               | Bernanke et al. (2005)  | 1959:1 – 2001:8  | 48            | –              |
| Adamek et al (2024)              | High-dimensional LP | Bernanke et al. (2005)  | 1969:1 – 2008:10 | 20            | 48 (final)     |
| Adamek et al (2024)              | FAVAR               | Bernanke et al. (2005)  | 1969:1 – 2008:10 | 50 (final)    | 50 (final)     |
| Ramey (2016) replications:       |                     |                         |                  |               |                |
| <i>Christiano et al. (1999)</i>  | VAR                 | Recursive VAR           | 1965:1 – 1995:6  | 48 (final)    | 11             |
| <i>Coibon VAR</i>                | VAR                 | Narrative               | 1969:3 – 1996:12 | 42            | 11             |
| <i>Romer &amp; Romer</i>         | LP                  | Narrative               | 1969:3 – 1996:12 | 48 (final)    | 35             |
| <i>Proxy SVAR</i>                | Proxy SVAR          | Narrative               | 1969:3 – 2007:12 | 25            | –              |
| <i>Gertler &amp; Karadi SVAR</i> | Proxy SVAR          | HF surprise             | 1979:7 – 2012:6  | 38            | 24             |
| <i>Gertler &amp; Karadi</i>      | LP                  | HF surprise             | 1990:1 – 2012:6  | 41            | 41             |

**Notes.** The responses are stated in months (columns ‘Peak Response’ and ‘First Negative’). ‘First Negative’ refers to the first response that is significantly negative, based on the significance criterion chosen in each paper. HF refers to high-frequency.

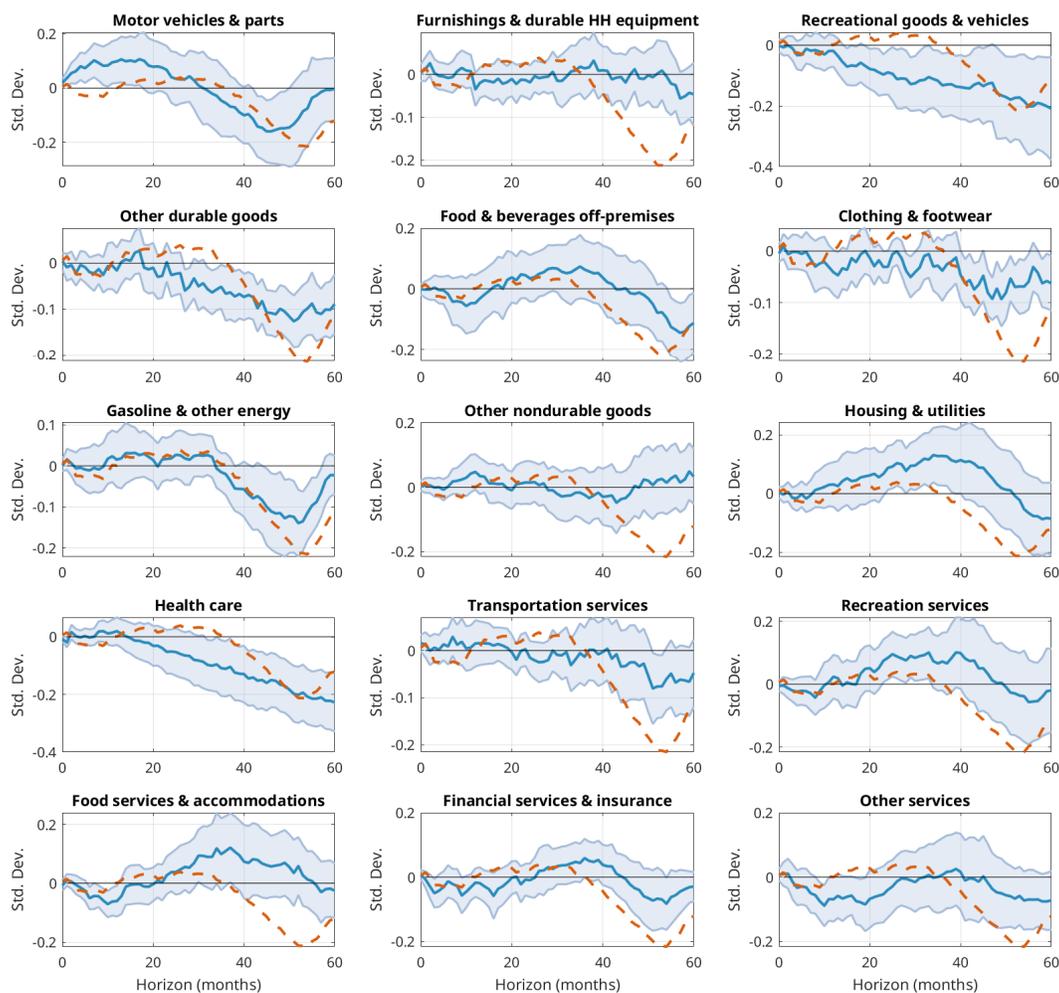
## C Response of the Fed Funds Rate to the shock

Figure C.1: IRFS TO MONETARY POLICY TIGHTENING: RESPONSE OF THE FED FUNDS RATE



## D Standardized IRFs for disaggregation level 3

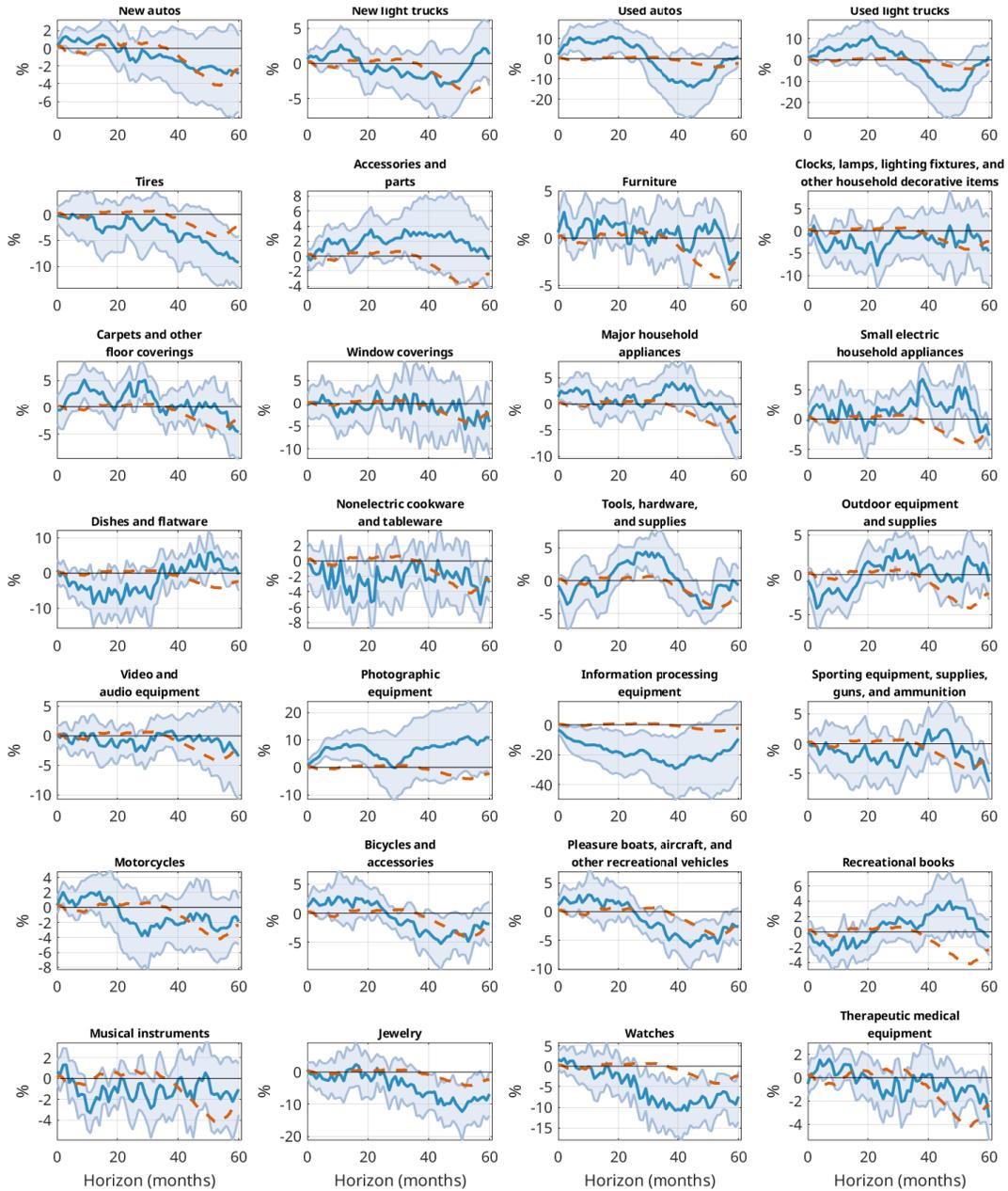
Figure D.1: IRFS TO MONETARY POLICY TIGHTENING: DISAGGREGATION LEVEL 3 (STANDARDIZED)



**Notes.** This figure repeats Figure 3 in the main text, but instead shows the IRFs as standardized, i.e. based on dividing each IRF by the historical standard deviation of the respective (log) price level series. The different panels make clear that the responses, for example the one of gasoline and other energy projects, are not as large as Figure 3 might suggest, when viewed in light of the historical standard deviation of a given price series.

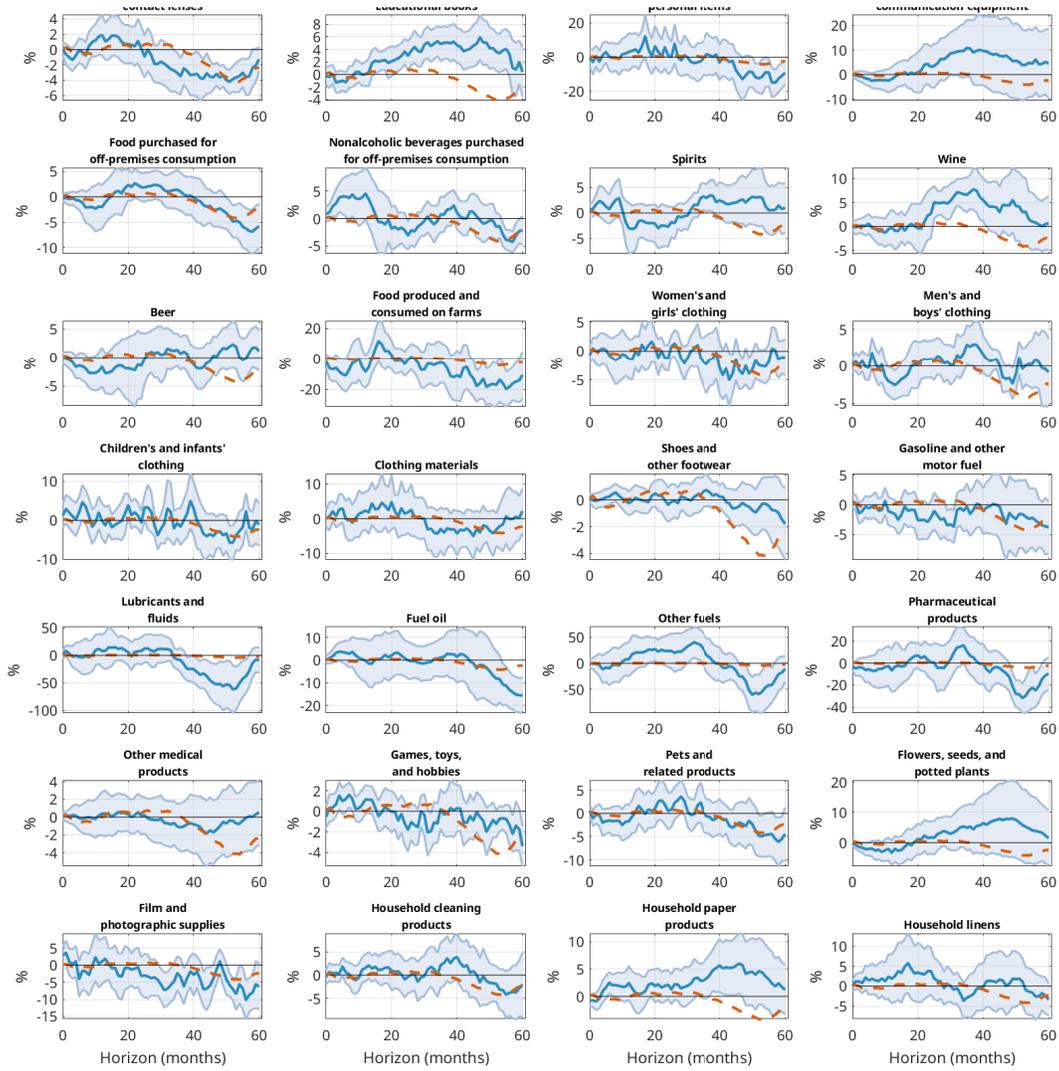
## E Full set of IRFs for disaggregation level 5\*

Figure E.1: IRFS TO MONETARY POLICY TIGHTENING: DISAGGREGATION LEVEL 5\* (1/5)



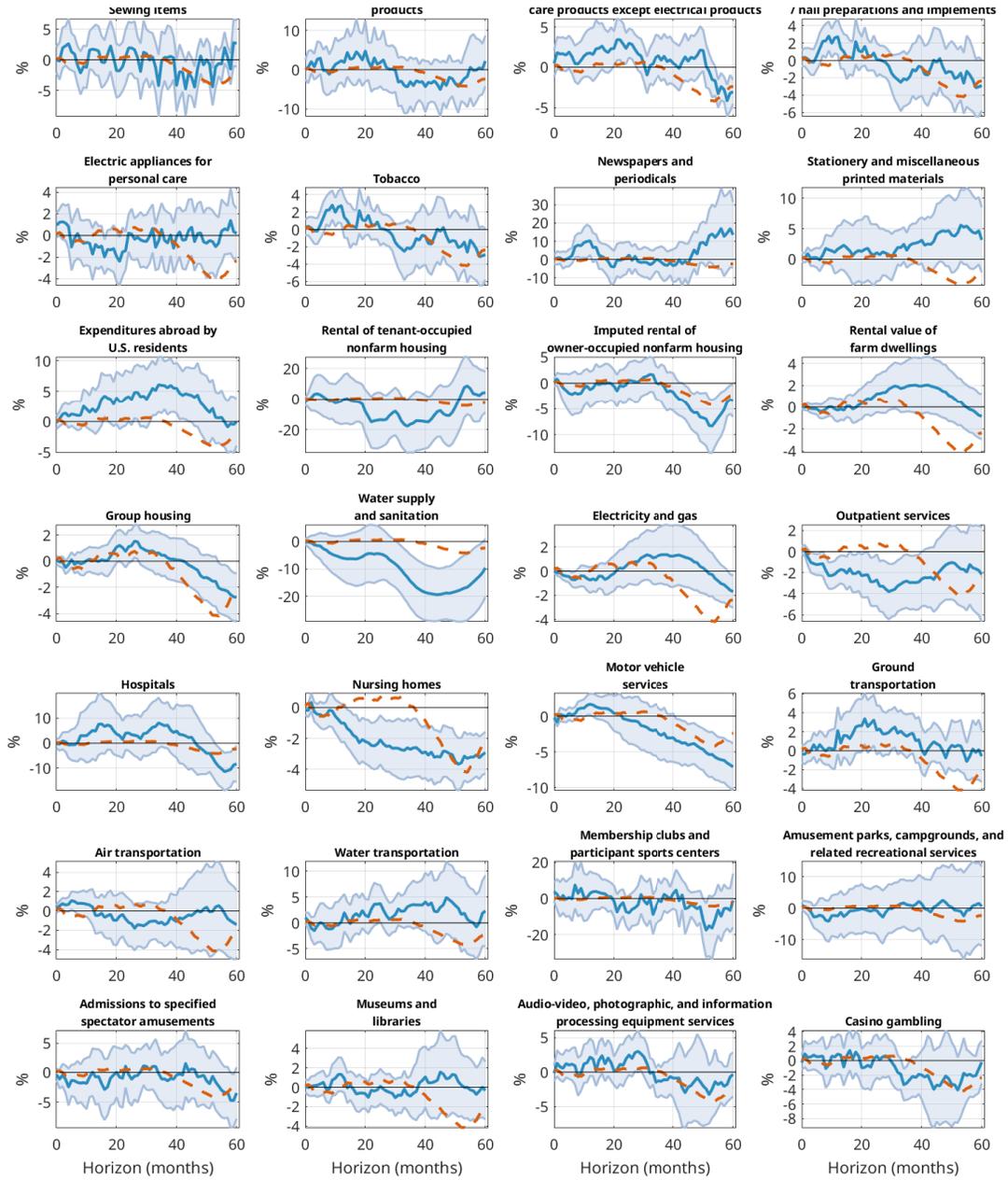
Notes. IRFs estimated using local projections using the identified monetary policy shocks of [Aruoba and Drechsel \(2023\)](#). This figure repeats Figure 3 but for series 1–28 at level 5\*.

**Figure E.2: IRFS TO MONETARY POLICY TIGHTENING: DISAGGREGATION LEVEL 5\* (2/5)**



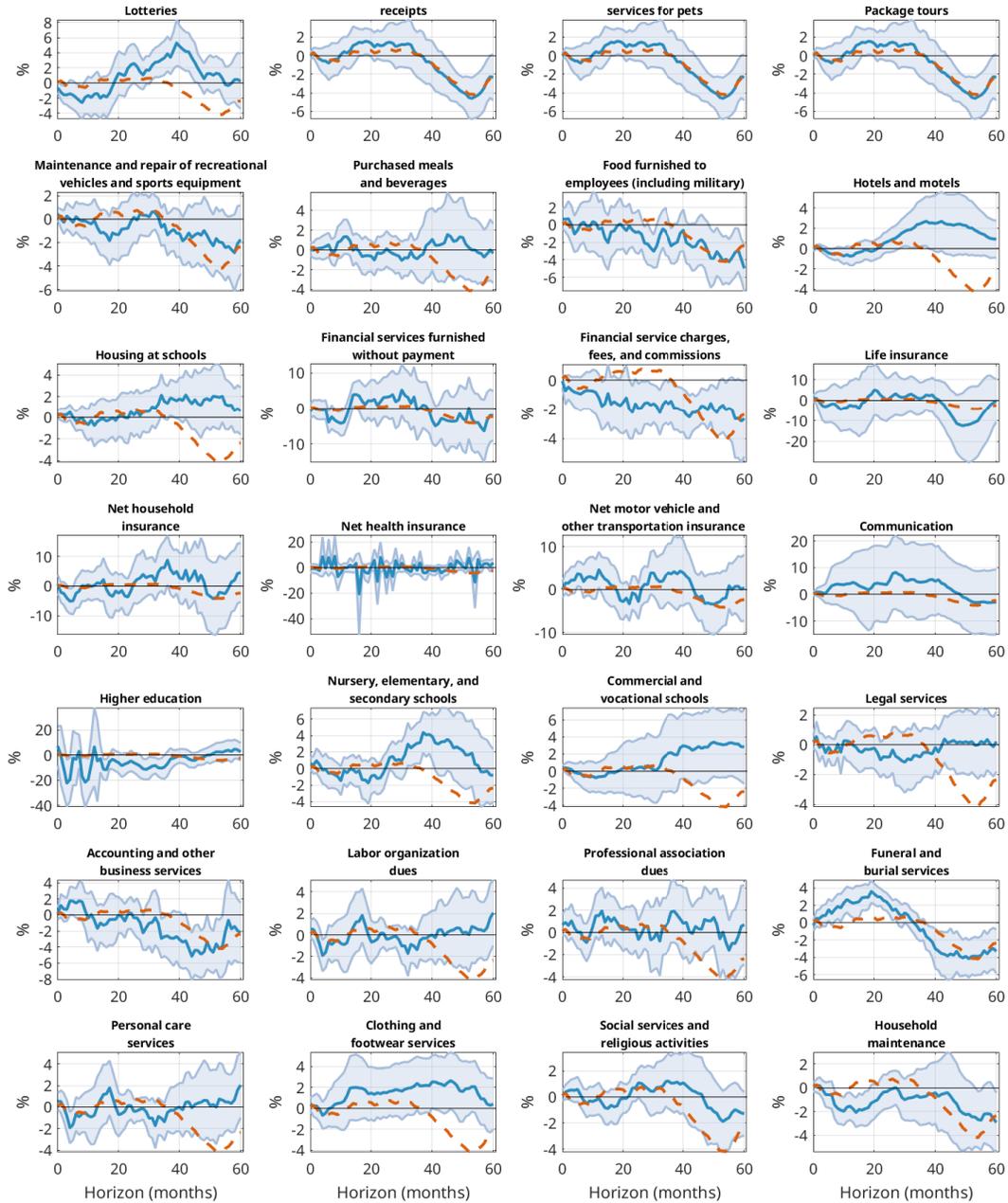
**Notes.** IRFs estimated using local projections using the identified monetary policy shocks of [Aruoba and Drechsel \(2023\)](#). This figure repeats Figure 3 but for series 29–56 at level 5\*.

**Figure E.3: IRFS TO MONETARY POLICY TIGHTENING: DISAGGREGATION LEVEL 5\* (3/5)**



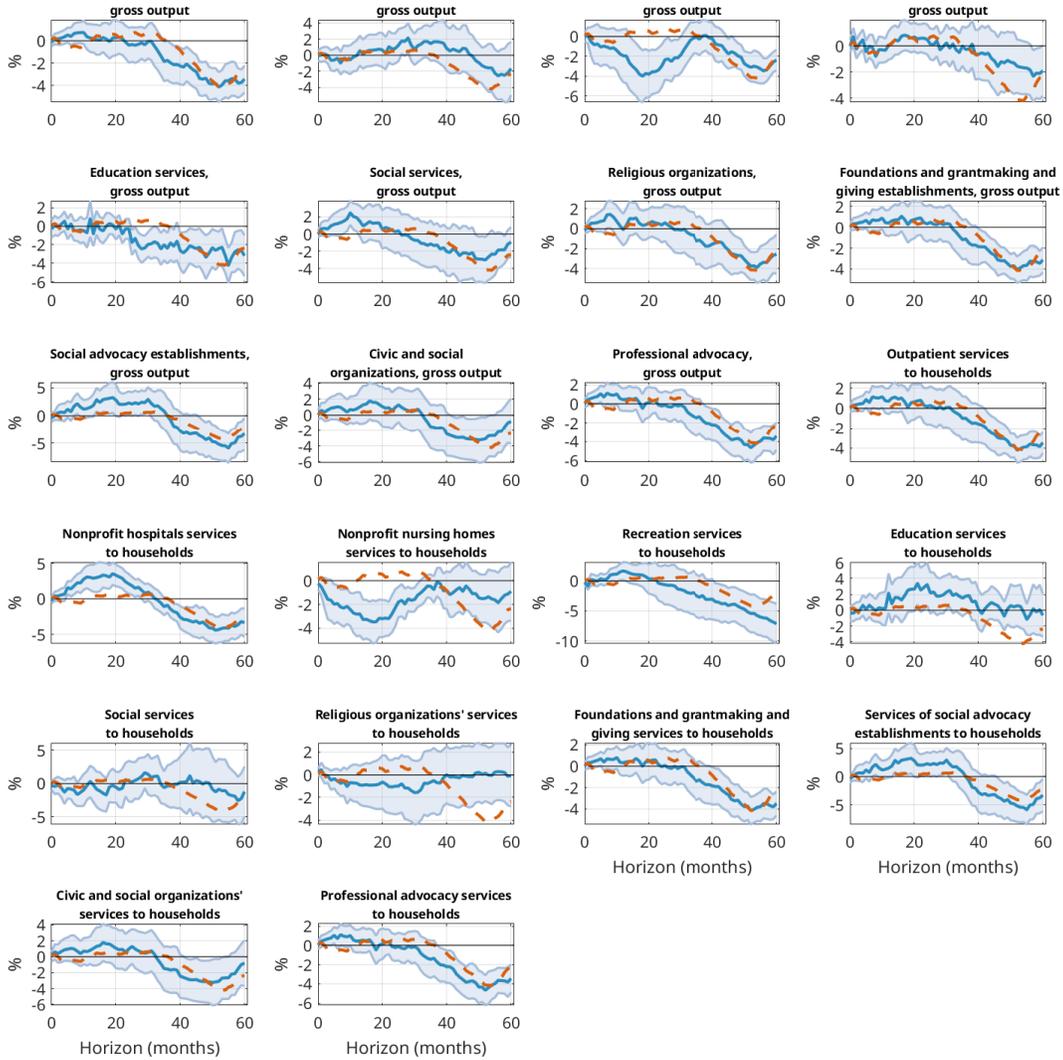
**Notes.** IRFs estimated using local projections using the identified monetary policy shocks of [Aruoba and Drechsel \(2023\)](#). This figure repeats Figure 3 but for series 57–84 at level 5\*.

**Figure E.4:** IRFS TO MONETARY POLICY TIGHTENING: DISAGGREGATION LEVEL 5\* (4/5)



**Notes.** IRFs estimated using local projections using the identified monetary policy shocks of [Aruoba and Drechsel \(2023\)](#). This figure repeats Figure 3 but for series 85–113 at level 5\*.

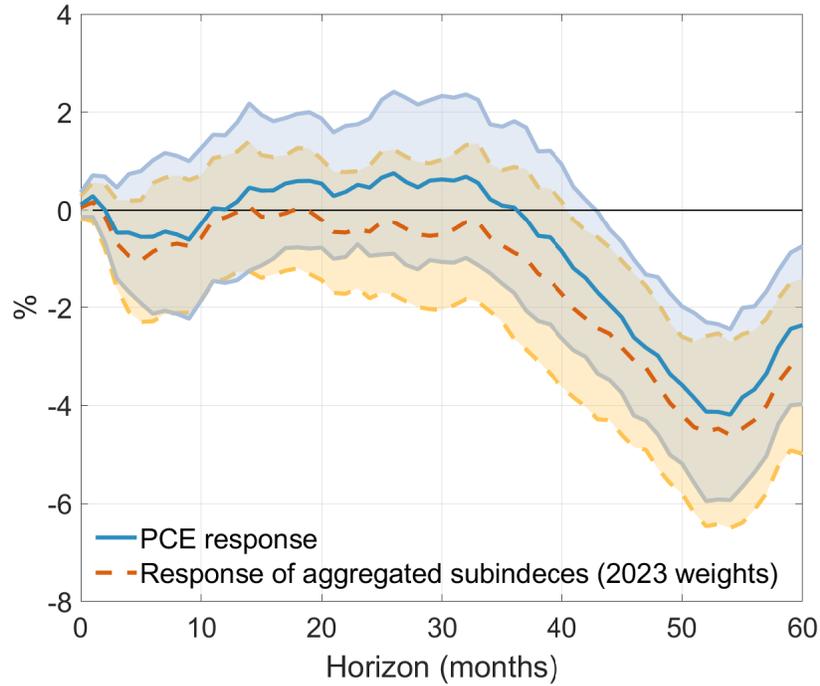
**Figure E.5:** IRFS TO MONETARY POLICY TIGHTENING: DISAGGREGATION LEVEL 5\* (5/5)



**Notes.** IRFs estimated using local projections using the identified monetary policy shocks of [Aruoba and Drechsel \(2023\)](#). This figure repeats Figure 3 but for series 114–136 at level 5\*.

## F IRF of reaggregated subcomponent data

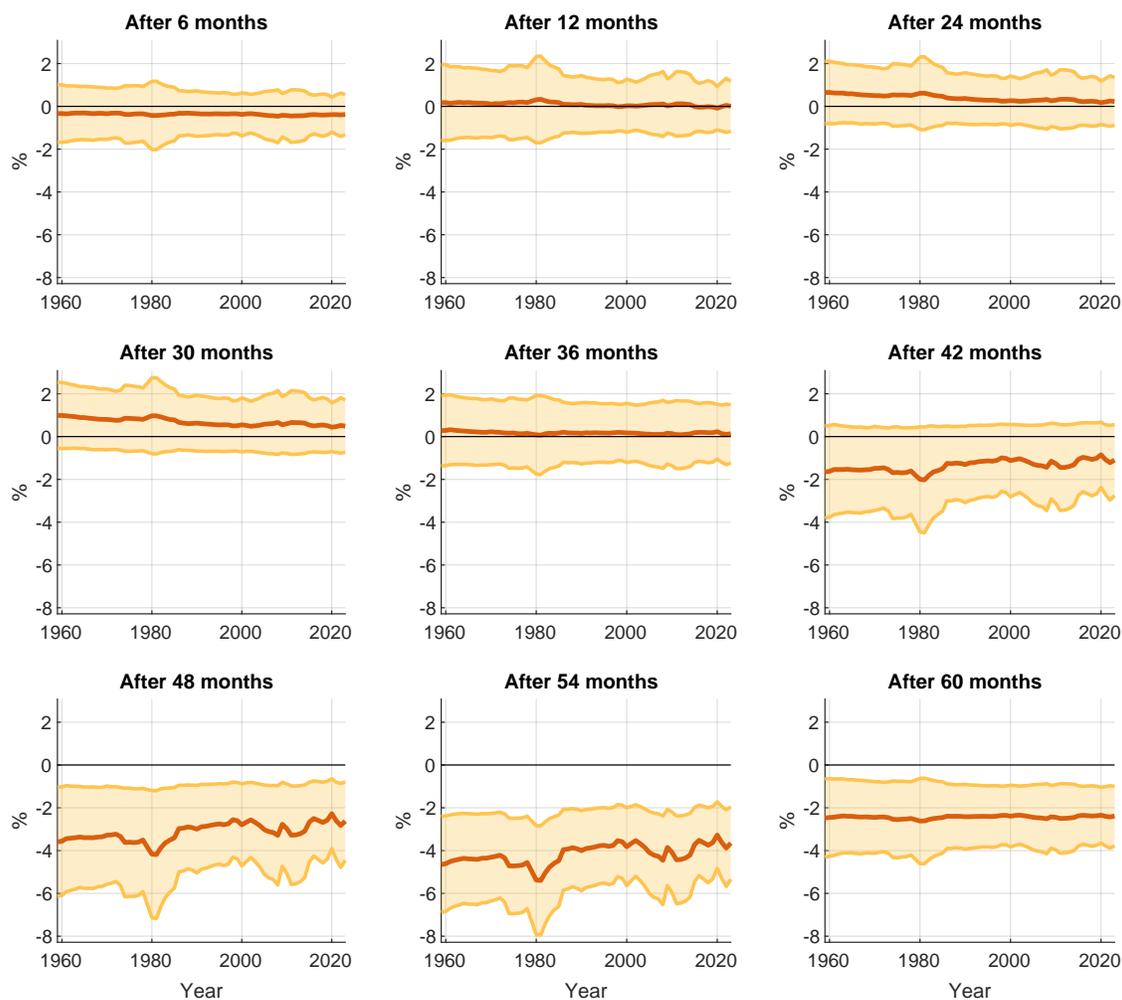
**Figure F.1:** COMPARISON OF PCEPI IRF WITH IRF OF REAGGREGATED SUBCOMPONENTS



**Notes:** Comparison of the PCEPI IRF (blue solid line) and the IRF of an index that we rebuilt using the data, rather than the estimated IRFs, of the level-3 subcomponents, using 2023 weights (orange dashed lines). The shaded areas represent 90% significance bands based on HAC standard errors

## G Re-aggregation using year-by-year weights

Figure G.1: UNPACKING THE IRF AGGREGATION THROUGH TIME

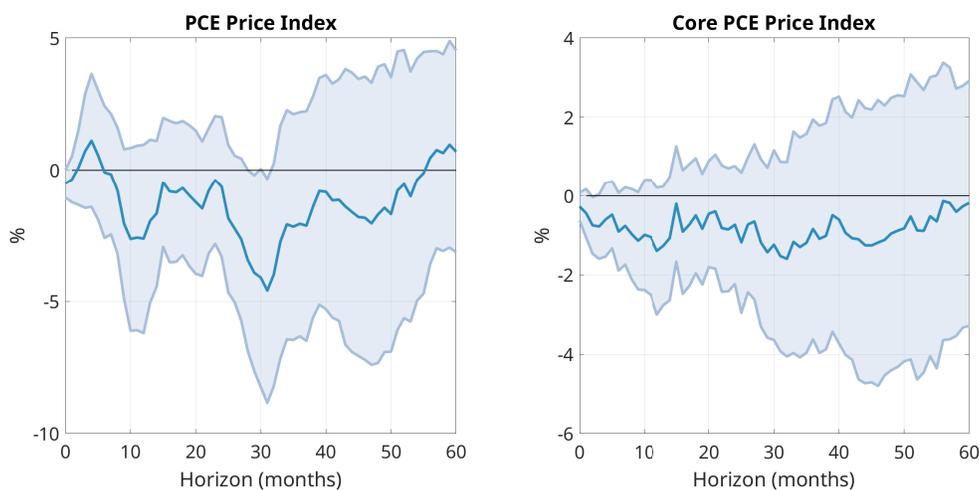


**Notes:** Re-aggregated Level 3 responses using year-by-year expenditure weights, for separate IRF horizons. The x axis shows the year used for re-aggregation and the different subplots correspond to different IRF horizon. The solid line corresponds to the points estimates and the shaded areas correspond to 90% significance bands based on HAC standard errors and accounting for cross-sectional dependence using SUR. These plots make clear that despite some meaningful changes in expenditure shares shown in Figure 8, the aggregated responses look fairly stable through time.

## H State-dependence and asymmetries

**Figure H.1:** EXPLORING STATE-DEPENDENCE AND ASYMMETRIES IN THE EFFECTS

(a) Interaction with dummy for above-median inflation periods



(b) Interaction with dummy for positive shocks



**Notes:** The IRFs in this figure represent the estimates of the coefficient on an additional interaction term that we add to the local projection for the headline and core PCEPI. In panel (a) we interact the monetary policy shock with a dummy variable that is one in above-median inflation periods and zero in below-median inflation periods. In panel (b) we interact the monetary policy shock with a dummy variable that is one when the monetary policy shock is positive and zero when it is negative.