Oligopolistic Competition, Price Rigidity, and Monetary Policy

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This paper investigates how strategic and heterogeneous price setting influences the real effect of monetary policy. Using a questionnaire survey to consumer-goods manufacturers and scanner data from supermarkets in Japan, we show that price changes by firms with large market share tend to be more frequent, larger in size, and have smaller dependence on competitor firms' price changes than those by firms with small market share. Then, we construct an oligopolistic competition model that incorporates sticky prices and asymmetry in terms of competitiveness and price stickiness. The model shows that the cross superelasticity of demand generates dynamic strategic complementarity, which decreases price adjustments and the real effect of monetary policy. Whether dynamic strategic complementarity for highly competitive firms is smaller than that for uncompetitive firms depends on models. Empirical results from Japanese data support the Hotelling model rather than the CES preferences model. The real effect of monetary policy substantially increases by the dynamic strategic complementarity as well as asymmetry in price stickiness.