

Discussion of  
“Inflation and Inequality”  
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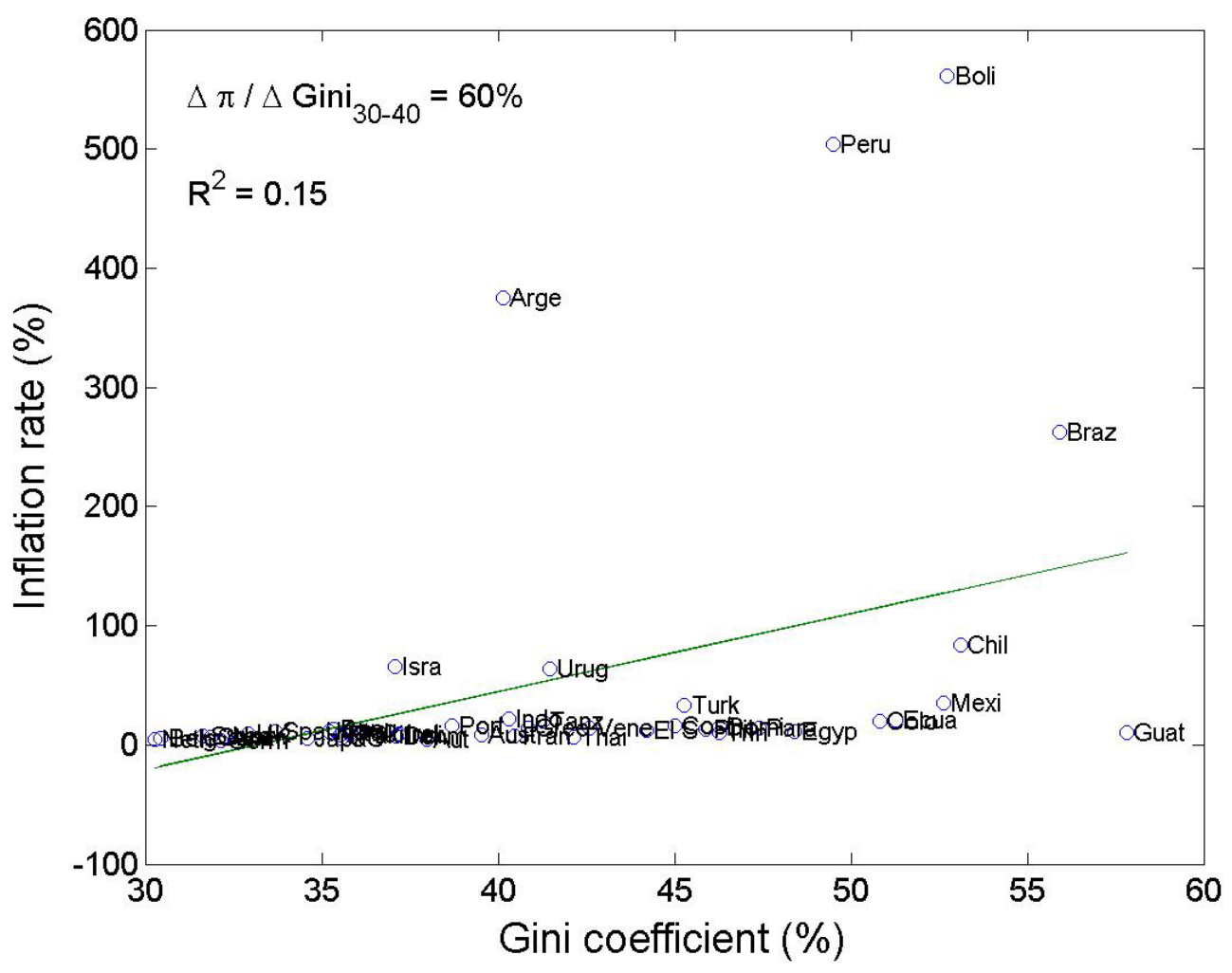
AEA meetings, 2002

Fabrizio Perri

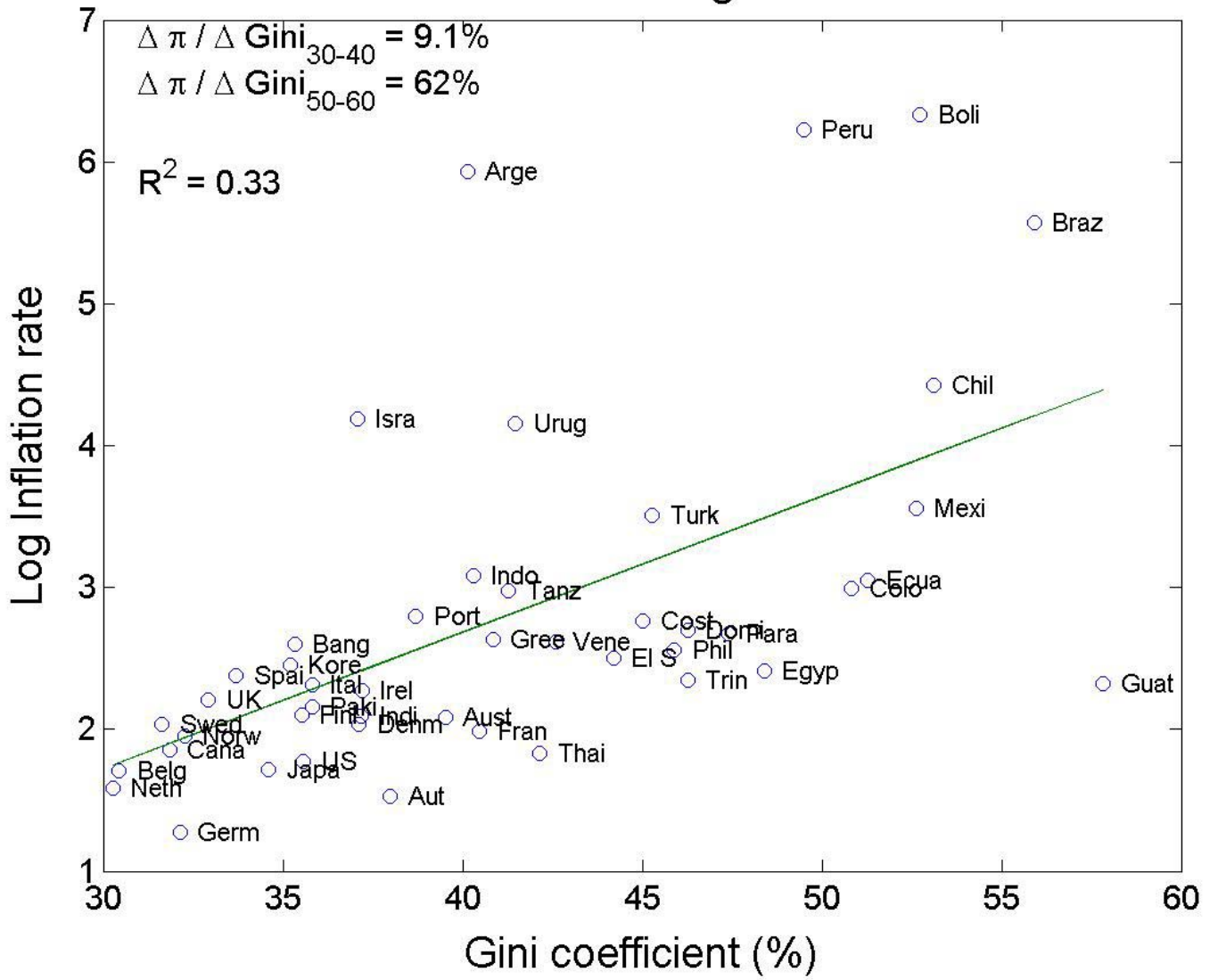
The empirical relation between inflation and  
inequality

The political economy of inflation

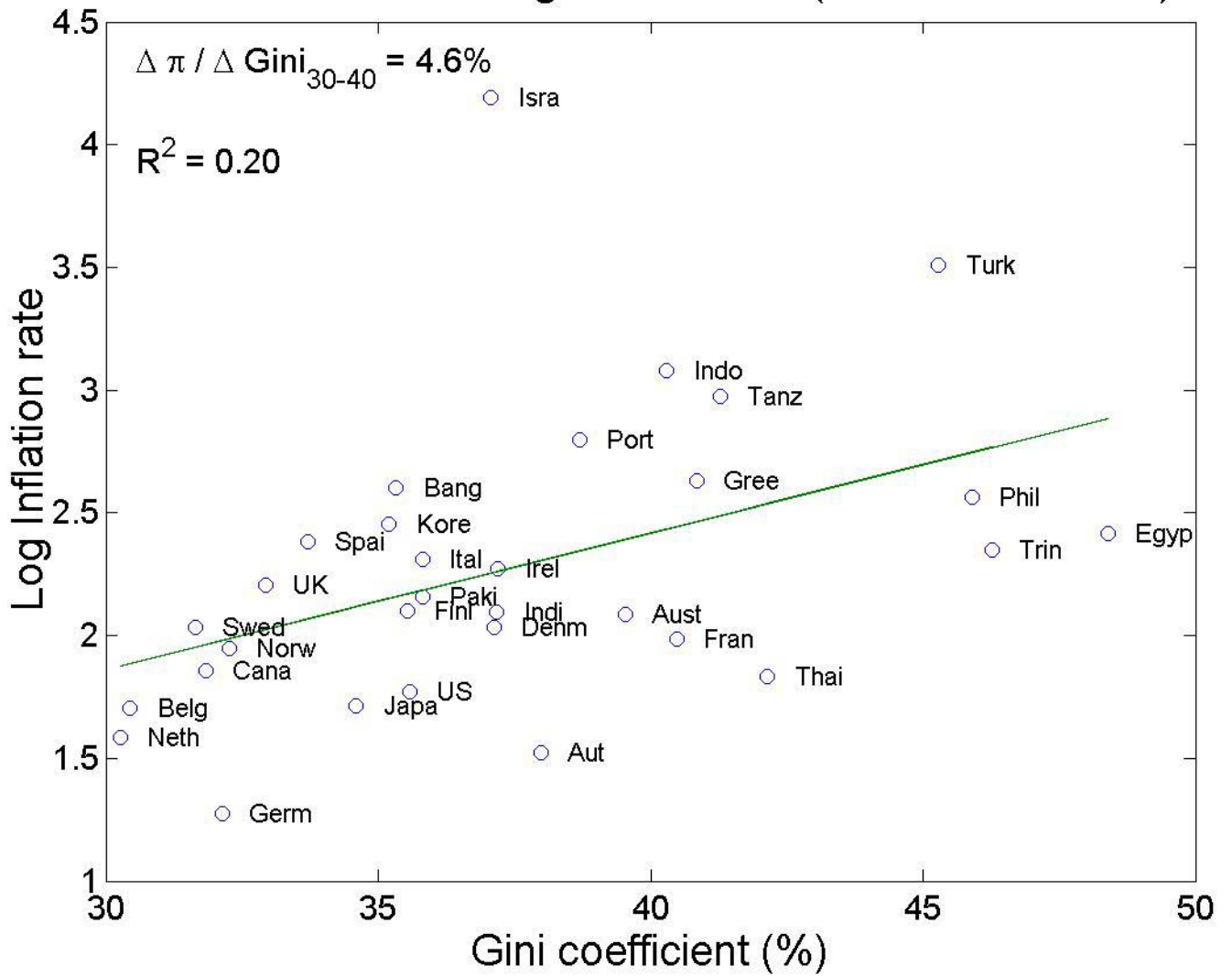
### Gini coefficient and Inflation rate



### Gini coefficient and log inflation rate



Gini coefficient and log inflation rate (Non LA countries)



Relation between inflation and inequality  
seem robust

(Dolmas, Huffman and Wynne, 2000 show  
that is also robust to panel analysis)

Strong evidence of non linearity. Societies  
with high level of inequality are more prone  
to hyperinflations.

# The political economy of inflation

Who loses the most from inflation?

In this paper the (income) poor use more cash and loses more from inflation. This weakens their bargaining position (because of the bargaining setup) and thus the bargaining outcome is that government spending is financed more through inflation (that is preferred by the rich)

Increasing income differences increases inequality improves the bargaining position of the rich and leads to more inflation

Implications of this approach

Suppose that greater inequality does not arise because of greater differences between rich and poor but simply because there are more poor people. Since a larger number of poor people would raise their bargaining position there would be a **negative relation** between inequality and inflation

Alternative Approach (Dolmas, Huffman and Wynne, CJE 2000)  
Income rich are also wealth rich, wealth is held in form of money and so the rich lose more from inflation

In this case more poor people would yield more inflation

## Key issues

To understand the political economy of inflation need to understand redistributive effects of inflation and consider inflation effects on wealth.

If 0 wealth no loss

If medium wealth: big loss

If large wealth: no loss

In this case the relevant variable that determines inflation would be the size of the middle class (consistent with historical evidence of hyperinflations) that does not coincide with inequality.

## Conclusions

Nice paper

Present new evidence on a surprisingly little documented fact

Political economy approach to inflation

Extensions: A model with wealth accumulation

- Can better address the redistributive effects of inflation
- Can address the reverse causation

Modelling CB independence as changes in the bargaining game. Also empirically the relation should be weaker for countries with independent central banks