WHY DO WE DISLIKE INFLATION?
by Stefanie Stantcheva (Harvard)

Discussion by
Yuriy Gorodnichenko
UC Berkeley and 🇺🇦
BENEFITS AND (NON-)COSTS OF INFLATION

Textbook (Mankiw, Blanchard, etc.)

Costs
  Price dispersion
  Menu costs
  Shoeleather cost
  Unfair tax treatment
  General inconvenience
  Arbitrary redistribution

Misperceptions (non-costs)
  Inflation reduces real wage

Benefits
  Inflation reduces unemployment
**Benefits and (Non-)Costs of Inflation**

<table>
<thead>
<tr>
<th>Textbook (Mankiw, Blanchard, etc.)</th>
<th>Households</th>
</tr>
</thead>
<tbody>
<tr>
<td>Costs</td>
<td></td>
</tr>
<tr>
<td>Price dispersion</td>
<td></td>
</tr>
<tr>
<td>Menu costs</td>
<td></td>
</tr>
<tr>
<td>Shoeleather cost</td>
<td></td>
</tr>
<tr>
<td>Unfair tax treatment</td>
<td></td>
</tr>
<tr>
<td>General inconvenience</td>
<td></td>
</tr>
<tr>
<td>Arbitrary redistribution</td>
<td></td>
</tr>
<tr>
<td>Misperceptions (non-costs)</td>
<td></td>
</tr>
<tr>
<td>Inflation reduces real wage</td>
<td></td>
</tr>
<tr>
<td>Benefits</td>
<td></td>
</tr>
<tr>
<td>Inflation reduces unemployment</td>
<td></td>
</tr>
</tbody>
</table>
## Benefits and (Non-)Costs of Inflation

<table>
<thead>
<tr>
<th>Textbook (Mankiw, Blanchard, etc.)</th>
<th>Households</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Costs</strong></td>
<td></td>
</tr>
<tr>
<td>Price dispersion</td>
<td>✗</td>
</tr>
<tr>
<td>Menu costs</td>
<td>✗</td>
</tr>
<tr>
<td>Shoeleather cost</td>
<td>✗</td>
</tr>
<tr>
<td>Unfair tax treatment</td>
<td>✗</td>
</tr>
<tr>
<td>General inconvenience</td>
<td>✗</td>
</tr>
<tr>
<td>Arbitrary redistribution</td>
<td>✗</td>
</tr>
<tr>
<td>Misperceptions (non-costs)</td>
<td></td>
</tr>
<tr>
<td>Inflation reduces real wage</td>
<td>✗</td>
</tr>
<tr>
<td><strong>Benefits</strong></td>
<td></td>
</tr>
<tr>
<td>Inflation reduces unemployment</td>
<td></td>
</tr>
</tbody>
</table>
# Benefits and (Non-)Costs of Inflation

<table>
<thead>
<tr>
<th>Textbook (Mankiw, Blanchard, etc.)</th>
<th>Households</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Costs</strong></td>
<td></td>
</tr>
<tr>
<td>Price dispersion</td>
<td>✓</td>
</tr>
<tr>
<td>Menu costs</td>
<td>✓</td>
</tr>
<tr>
<td>Shoeleather cost</td>
<td>✓</td>
</tr>
<tr>
<td>Unfair tax treatment</td>
<td>✓</td>
</tr>
<tr>
<td>General inconvenience</td>
<td>✓</td>
</tr>
<tr>
<td>Arbitrary redistribution</td>
<td>✓</td>
</tr>
<tr>
<td><strong>Misperceptions (non-costs)</strong></td>
<td></td>
</tr>
<tr>
<td>Inflation reduces real wage</td>
<td>✓</td>
</tr>
<tr>
<td><strong>Benefits</strong></td>
<td></td>
</tr>
<tr>
<td>Inflation reduces unemployment</td>
<td>✓</td>
</tr>
</tbody>
</table>
WHAT CAUSES INFLATION?

M. Friedman: “Inflation is always and everywhere a monetary phenomenon”
WHAT CAUSES INFLATION?

M. Friedman: “Inflation is always and everywhere a monetary phenomenon”
WHAT CAUSES INFLATION?

M. Friedman: “Inflation is always and everywhere a monetary phenomenon”

Panel A: Reasons for inflation/disinflation

Source: Salle et al. (2023)
HOW DO PEOPLE VIEW INFLATION?

- Stagflationary
  - High inflation is associated with bad economy
HOW DO PEOPLE VIEW INFLATION?

- Stagflationary
  - High inflation is associated with bad economy

- Partial equilibrium
  - Inflation reduces purchasing power
HOW DO PEOPLE VIEW INFLATION?

- Stagflationary
  - High inflation is associated with bad economy

- Partial equilibrium
  - Inflation reduces purchasing power

- Zero-sum game
  - Inflation as a conflict
HOW DO PEOPLE VIEW INFLATION?

- Stagflationary
  - High inflation is associated with bad economy

- Partial equilibrium
  - Inflation reduces purchasing power

- Zero-sum game
  - Inflation as a conflict

- Personalized blame
  - “Biden”, “Putin”, etc.
HOW DO PEOPLE VIEW INFLATION?

- Stagflationary
  - High inflation is associated with bad economy

- Partial equilibrium
  - Inflation reduces purchasing power

- Zero-sum game
  - Inflation as a conflict

- Personalized blame
  - “Biden”, “Putin”, etc.

- Politics strongly colors the interpretation
  - Opposition blames the government
BUT FIRMS ARE DIFFERENT FROM HOUSEHOLDS
BUT FIRMS ARE DIFFERENT FROM HOUSEHOLDS

Elon Musk (October 20, 2022): “There's more deflation than inflation.”

CPI inflation in October 2022 (according to the BLS): 7.8%
**But firms are different from households**

Managers in New Zealand: Source for inflation expectations

<table>
<thead>
<tr>
<th>Source for inflation expectations</th>
<th>Importance of information source (5 = extremely important; 1 = not important)</th>
<th>Average score</th>
<th>Share of “extremely” and “very important”</th>
</tr>
</thead>
<tbody>
<tr>
<td>Family and friends</td>
<td></td>
<td>2.12</td>
<td>0.06</td>
</tr>
<tr>
<td>Employees &amp; colleagues</td>
<td></td>
<td>1.88</td>
<td>0.08</td>
</tr>
<tr>
<td>Customers &amp; suppliers</td>
<td></td>
<td>1.68</td>
<td>0.04</td>
</tr>
<tr>
<td>Gas prices</td>
<td></td>
<td>4.14</td>
<td>0.76</td>
</tr>
<tr>
<td>Personal shopping experience</td>
<td></td>
<td>4.42</td>
<td>0.88</td>
</tr>
<tr>
<td>Government agencies</td>
<td></td>
<td>1.74</td>
<td>0.00</td>
</tr>
<tr>
<td>Business associations</td>
<td></td>
<td>1.82</td>
<td>0.00</td>
</tr>
<tr>
<td>Media</td>
<td></td>
<td>3.54</td>
<td>0.54</td>
</tr>
<tr>
<td>Professional forecasts</td>
<td></td>
<td>2.42</td>
<td>0.20</td>
</tr>
</tbody>
</table>

Source: Kumar et al. (2015)
POLICY IMPLICATIONS
POLICY IMPLICATIONS

- Objectives and tradeoffs
  - Standard NK macro: \( \text{var}(X_t) + \omega \times \text{var}(\pi_t) \) but struggle with \( \omega \gg 1 \)
POLICY IMPLICATIONS

- Objectives and tradeoffs
  - Standard NK macro: $\text{var}(X_t) + \omega \times \text{var}(\pi_t)$ but struggle with $\omega \gg 1$
  - People want $\omega \gg 1$
POLICY IMPLICATIONS

- Objectives and tradeoffs
  - Standard NK macro: \( \text{var}(X_t) + \omega \times \text{var}(\pi_t) \) but struggle with \( \omega \gg 1 \)
  - People want \( \omega \gg 1 \)

Desired inflation target

Source: Afrouzi, Dietrich, Myrseth, Priftis and Schoenle (2024)
POLICY IMPLICATIONS

- Objectives and tradeoffs
  - Standard NK macro: \( \text{var}(X_t) + \omega \times \text{var}(\pi_t) \) but struggle with \( \omega \gg 1 \)
  - People want \( \omega \gg 1 \)

- Central banks can use inflation to stimulate aggregate demand
  - Mario Draghi (2015): “When inflation expectations go up with zero nominal rates, real rates go down. When real rates go down, investments and the economic activity improves. That’s the reasoning [of QE].”
POLICY IMPLICATIONS

- Objectives and tradeoffs
  - Standard NK macro: $\text{var}(X_t) + \omega \times \text{var}(\pi_t)$ but struggle with $\omega \gg 1$
  - People want $\omega \gg 1$

- Central banks can use inflation to stimulate aggregate demand
  - Mario Draghi (2015): “When inflation expectations go up with zero nominal rates, real rates go down. When real rates go down, investments and the economic activity improves. That’s the reasoning [of QE].”
  - People can withdraw from consumption when inflation increases
POLICY IMPLICATIONS

- Objectives and tradeoffs
  - Standard NK macro: $\text{var}(X_t) + \omega \times \text{var}(\pi_t)$ but struggle with $\omega \gg 1$
  - People want $\omega \gg 1$

- Central banks can use inflation to stimulate aggregate demand
  - Mario Draghi (2015): “When inflation expectations go up with zero nominal rates, real rates go down. When real rates go down, investments and the economic activity improves. That’s the reasoning [of QE].”
  - People can withdraw from consumption when inflation increases

- Some policies rely on strong general equilibrium effects and sophistication
  - Price level targeting works when agents can iterate forward
POLICY IMPLICATIONS

- Objectives and tradeoffs
  - Standard NK macro: \( var(X_t) + \omega \times var(\pi_t) \) but struggle with \( \omega \gg 1 \)
  - People want \( \omega \gg 1 \)

- Central banks can use inflation to stimulate aggregate demand
  - Mario Draghi (2015): “When inflation expectations go up with zero nominal rates, real rates go down. When real rates go down, investments and the economic activity improves. That’s the reasoning [of QE].”
  - People can withdraw from consumption when inflation increases

- Some policies rely on strong general equilibrium effects and sophistication
  - Price level targeting works when agents can iterate forward
  - People have low level-\( k \) thinking
FUTURE WORK

- Publish data for researchers
  - 30+ minutes of survey time $\Rightarrow$ a lot of interesting material
  - Political polarization
  - Men vs. Women
  - How inflation expectations correlated with priorities & beliefs
FUTURE WORK

- Publish data for researchers
  - 30+ minutes of survey time \(\Rightarrow\) a lot of interesting material
  - Political polarization
  - Men vs. Women
  - How inflation expectations correlated with priorities & beliefs

- More surveys
  - Level of inflation vs. uncertainty about inflation
  - Quantify sensitivity (hypothetical questions?)
FUTURE WORK

- Publish data for researchers
  - 30+ minutes of survey time \( \Rightarrow \) a lot of interesting material
  - Political polarization
  - Men vs. Women
  - How inflation expectations correlated with priorities & beliefs

- More surveys
  - Level of inflation vs. uncertainty about inflation
  - Quantify sensitivity (hypothetical questions?)

- Develop theory consistent with how “the public” thinks about inflation
FUTURE WORK

- Publish data for researchers
  - 30+ minutes of survey time ⇒ a lot of interesting material
  - Political polarization
  - Men vs. Women
  - How inflation expectations correlated with priorities & beliefs

- More surveys
  - Level of inflation vs. uncertainty about inflation
  - Quantify sensitivity (hypothetical questions?)

- Develop theory consistent with how “the public” thinks about inflation

Terrific paper!