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Macro Roundup Artcile

Headline: Fiscal Influences on Inflation in OECD Countries, 2020-2022

Article Link: https://www.nber.org/papers/w31838

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Tweet: Robert Barro and @Francesco_Bia find that 40-50% of pandemic-era OECD government financing came from the effect of unexpected inflation on the real value of public debt, consistent with the fiscal theory of the price level.

Summary: We show for a sample of 21 economies—20 non-Euro-zone OECD countries and an aggregated version of 17 Euro-zone countries—that headline and core inflation rates in 2020-2022 responded positively to a theory-motivated government-spending variable. This variable includes cumulated increases in spending-GDP ratios divided by the pre-pandemic level of the debt-to-GDP ratio and by the average duration of the outstanding debt. In contrast, across 17 Euro-zone countries, differences in the government-spending variable do not generate significant differences in inflation rates. We also find in the sample of 21 economies that, while positive and statistically significant, the coefficient that gauges the response of the inflation rate to the scaled measure of government spending is significantly less than one, the value predicted when all of the extra spending is "paid for" through surprise inflation. The point estimates of coefficients of 0.4-0.5 suggest that 40-50% of the extra spending was financed through inflation, whereas the remaining 50-60% was paid for through the more conventional method of intertemporal public finance that involves increases in current or prospective government revenue or cuts in prospective future spending. Related: What We've Learned About Inflation and Fiscal Arithmetic and the Global Inflation Outlook and When Will There Be No More Excess Savings Left?

Primary Topic: Inflation

Topics: Academic paper, Database, Fiscal Deficits, Fiscal Policy, GDP, Government Spending, Important!, Inflation, Monetary Policy, Very Important, Weekly

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