

Macro Roundup Article

Headline: [A Major Shock Makes Prices More Flexible and May Result in a Burst of Inflation or Deflation](#)

Article Link: <https://www.nber.org/papers/w31025>

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Tweet: Robert Hall argues that a substantial rise in the volatility of costs can free the prices of a significant fraction of goods and services prices from the grip of New Keynesian "zone of inaction." @NBERpubs

Summary: The basic idea of this paper is that a substantial rise in the volatility of costs and other determinants of prices can completely free the prices of a significant fraction of goods and services from the grip of New Keynesian stickiness, when the volatility of cost rises. There is a critical configuration of the model such that at lower values of the of the cost volatility, the price is a constant over time—resetting never occurs, except possibly to bring the price into the zone of indifference at the beginning of time. The surprising implication of this investigation is that an increase in the volatility of cost that leaves the average level of cost unchanged can trigger a near collapse of price stickiness. The next section of the paper presents an empirical analysis demonstrating a large increase in cost volatility around the time of a burst of inflation during and after the pandemic, followed by a reversal.

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Primary Topic: Inflation

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