Firming up Price Inflation

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We use data from a large panel survey of UK firms to analyze the economic drivers of price setting since the start of the Covid pandemic. Inflation responded asymmetrically to movements in demand. This helps to explain why inflation did not fall much during the negative initial pandemic demand shock. Energy prices and shortages of labor and materials account for most of the rise during the rebound. Inflation rates across firms have become more dispersed and skewed since the start of the pandemic. We find that average price inflation is positively correlated with the dispersion and skewness of the distribution. Finally, we also introduce a novel measure of subjective inflation uncertainty within firms and show how this has increased during the pandemic, continuing to rise in 2022 even as sales uncertainty dropped back.

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