

Inflation as a distributive conflict. Few policy recommendations.¹

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The monetary explanation of inflation (i.e.: too much money searching for too few goods, according the famous definition of Milton Friedman) has shown a number of failures. Just to look at the most recent facts in Europe, after the sovereign debt crisis, the ECB increased the stock of money (M1) by about 123% (since 2011 until November 2023, with a peak by 150% in August 2022), while consumer prices (HICP) rose by 30% and the volume of European supply (whose dynamics is approximated by real GDP) only by 14%. Thus, apparently two thirds of money growth have had no effect on prices (has the circulation speed of money dropped by about 90%?).

Nevertheless, the ECB is fighting against the ongoing inflation by reducing the money stock and increasing interest rates, as if the main cause of prices surge was an excess of aggregate demand. Surprisingly, the latter strategy seems to be at odds to what Christine Lagarde, president of ECB, recognised during the ECB Forum on Central Banking in Sintra last June: “unit profits contributed around two-thirds to domestic inflation in 2022, whereas in the previous 20 years their average contribution had been around one-third. This in turn led to the shocks feeding into inflation much more quickly and forcefully than in the past.”

Coherently, European inflation should be contrasted by curbing profits rather than aggregate demand, as pointed out also by a former central banker, Ignazio Visco (2023), who wrote recently: “only the coherent and cohesive action of monetary, fiscal and [...] incomes policy may counter inflation successfully.”

There is no doubt that monetary restriction is going to curb inflation in the end, since it drives the economy into a recession or stagnation intentionally, which lessens the pressure of demand on prices, nevertheless, the cure could be worse than the disease. Furthermore, ongoing slowdown carries over likely negative outcomes on employment, human capital and accumulation in the future, via hysteresis effect. For instance, a paper by Stockhammer and Sturn (2012) found that the effect of monetary restriction on employment was substantial even after 5 years in 40 recession episodes in 19 OECD countries, from 1980 to 2007 (i.e.: before the Great Recession): on average, an increase of one base point of real interest rate makes the ratio between the changes of actual unemployment and the NAIRU raise by about 0.3 base points.

What is more, virtually no inflationary process has left relative prices (including productive factors' remuneration and international terms of trade) unchanged. It follows that inflation mainly covers up some redistributive process in favour of agents with a stronger market power (typically: corporations, professionals, countries producing raw materials and other key commodities) at the expense of weaker agents (typically: less qualified workers, pensioners, industrial countries). If this is the case, monetary restriction helps (or accelerates) relative income changes (i.e.: the true source of inflation) and holds back real growth and employment. As a consequence, inflation hits labour twice: because of the loss of real wages and larger unemployment.

Interpreting inflation as a distributive conflict (or a sharp change of relative prices) dates back at least from the Rowthorn's (1977) contribution. Morlin (2022) provides a survey on this topic and Pianta (2023) analysed the Italian case.

An income policy may dampen the impact of inflation on weaker national agents, also stopping either a possible wage-price or a profit-price spiral. Industrial and antitrust policy may reduce the market power of national stronger agents, opposing the profit-price spiral pointed out also by Ms. Lagarde.

¹ I gratefully acknowledge my debt to Roberto Schiattarella for most ideas reported here. Of course, the responsibility for remaining mistakes and is only mine.

At European level, stronger antitrust regulation could help to reduce extra-profits in many markets (energy, commodities, drugs, financial services, etc.). Enforcing a European minimum tax on multinational companies may stabilize and reduce profits. Also, common procurement for key commodities (such as those enacted for vaccine during the pandemic and the AggregateEU platform established for natural gas) may attenuate shocks on international markets. In any case, a stricter regulation of key commodity markets within EU is necessary to avoid new speculative sunspots. Bottlenecks and excessive dependency from non-EU countries in key sectors (e.g.: energy, food, raw materials, technology, some low value added key industries) should be lessened through appropriate common European industrial policies.

In the short run, there is another measure which may hamper inflation: improving the awareness of consumers. D'Elia (2005) shows as firms seize consumer's rent by setting different prices in oligopolistic market exploiting asymmetric information, thus disseminating information about "fair prices" may slow down price increase, since cuts search costs for consumers, reducing their information disadvantage.

Inflation must be curbed because hits mainly weaker (and likely poorer) economic agents, particularly employees and pensioners. Nevertheless, inflation is seldom a monetary phenomenon, thus monetary restriction does not reach the former objective (and possibly worsen and make permanent the effects of inflation) and is a purely symptomatic treatment. Income and antitrust policies may be effective because front the very roots of inflation (i.e.: a conflict on income distribution) directly. Industrial policy should reduce the dependency of Europe from key commodities and services (particularly energy, micro-electronics, some semi-finished industrial goods) to prevent bottlenecks and external shock. For instance, European institutions should enact some policy tools such as a common procurement for key commodities and a stronger regulation of commodity markets. Also, reducing consumers' information disadvantage on prices may help to slow down inflation.

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