

It's Baaack: The Surge in Inflation in the 2020s and the Return of the Non-Linear Phillips Curve

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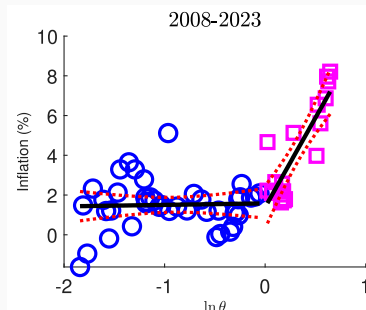
Discussion: Stéphane Dupraz

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*The views expressed do not necessarily represent those of the Banque de France or the Eurosystem

Best case to date for overheated labor market & convex PC view of 2020s inflation

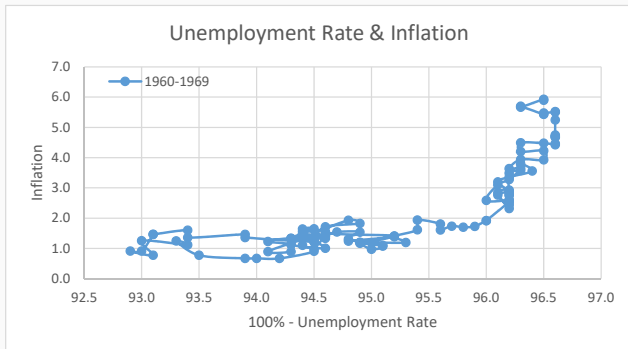
1. **Empirics:** Evidence of non-linearities from (inflation \sim tightness) regressions



2. **Model:** S&M with DNWR, but also non-standard employment agencies
3. **Policy Implication:** Easy way up but so also easy way down, \neq 1970s

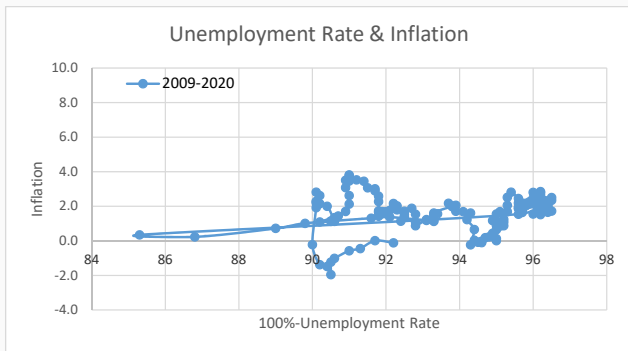
Comment #1: What Would a Convex PC Skeptic Have Said in 2019?

Arguably, s/he remembered the 1960s



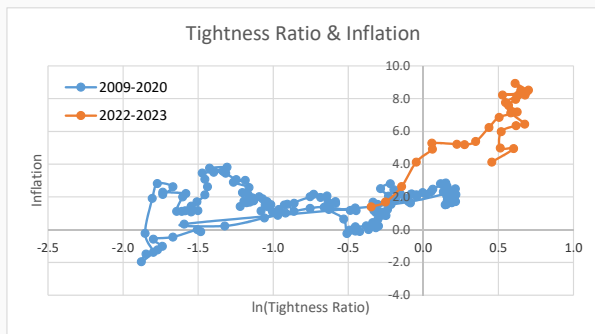
Comment #1: What Would a Convex PC Skeptic Have Said in 2019?

Ex ante in 2019: could argue it's ok to relax about convex PC nowadays
→ Unemployment was 3.5% in 2019 with inflation barely on target

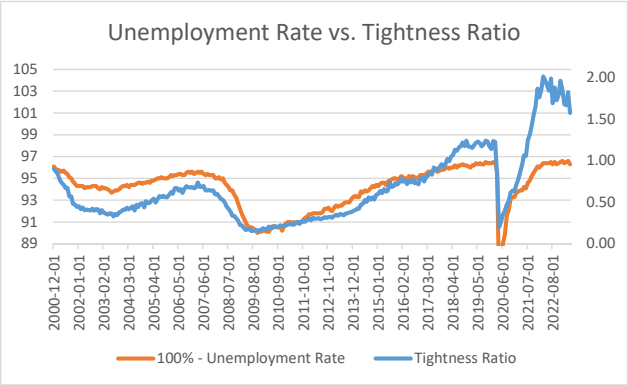


Comment #1: What Would a Convex PC Skeptic Say?

But if use the tightness ratio, inflation appears (mostly) as a move along a convex PC



Comment #1: What Would a Convex PC Skeptic Say?



Comment #1: Convincing a Convexity Skeptic

- **So hinges strongly on u vs. θ debate for assessing labor market overheating**
 - e.g. Furman Powell (2021) vs. issues vacancy data (measur., sector. realloc.)
- **Can argue 2022 in itself proves tightness is a better predictor of inflation**
 - But shift PC interpretation not absurd either, if go beyond energy/food prices
 - Relative-Price changes, supply side beyond oil (commodity prices, shortages)
 - Relative-Price changes, demand side (Peloton ®, Guerrieri et al. 2021)
- **Begs the question: Why tightness-PC convex but unemployment-PC not?**
 - Unemployment-PC was convex in the 1960s
 - Unemployment-PC was convex between 1861 and 1957 in UK (Phillips 1958!)

Comment #1: Convincing a Convexity Skeptic

- **Can model account for convex θ -PC but non-convex u -PC**
 - Can model account for the difference between 2019 and 2023?
→ Same u but different θ and different π ?
 - Can model account for the difference between 1960s and post-2000?
→ Both PC convex in 1960s vs. using tightness matters post-2000?
- **Can standard S&M features of the model account for this?**
 - In baseline S&M, u and θ closely tied together
 - Bar shifts in Beveridge Curve (matching efficiency)
 - Bar changes in separation
- **Do novel features of the model help with this?**
 - Model adds to S&M both DNWR and novel employment agencies
 - DNWR alone can explain convex PC (Benigno Ricci 2011!)
 - Agencies charge a fee γ_t^b proportional to wages; implies

$$w_t^{flex} = \frac{\gamma_t^c}{\gamma_t^b} \frac{1}{m_t} \theta_t^\eta$$

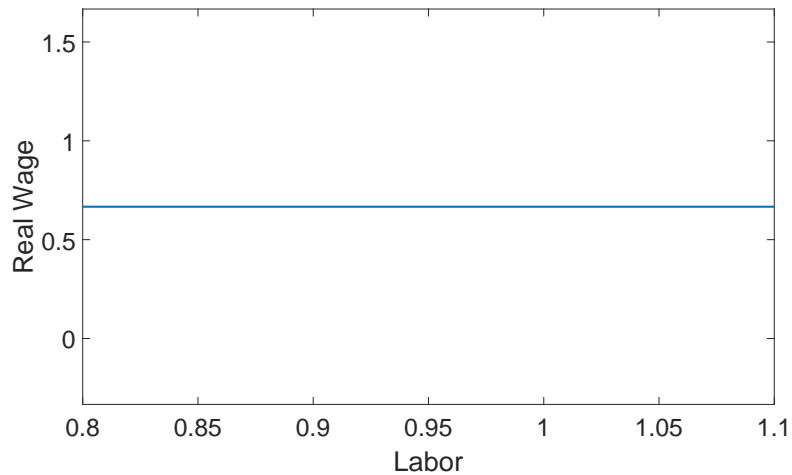
- Do employment agencies help with θ -PC versus u -PC?



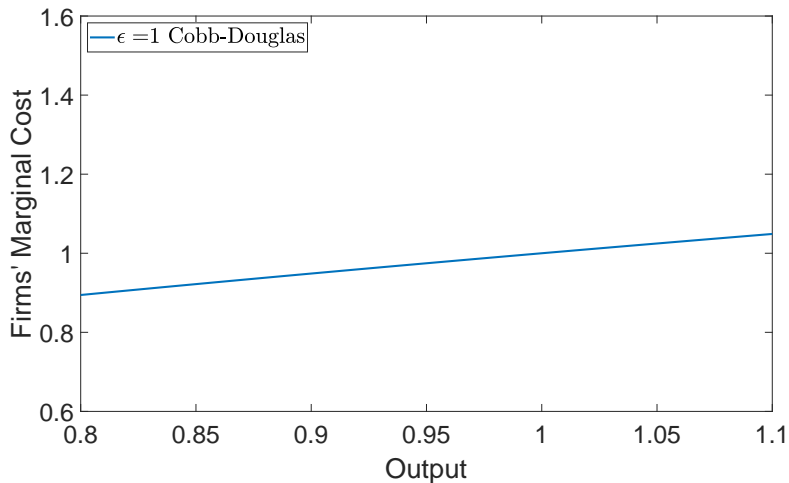
Comment #2: Labor Shortages vs. Something Else Shortages?

- **One alternative view: Shifts in PC from relative price changes**
 - On demand side: goods/services, Peloton ®
 - On supply side: shortages/bottlenecks (ships, chips, etc.)
- **But “Bottlenecks” is also just another word for Convex Phillips Curve**
 - Labor Shortages = Labor Bottlenecks → Convexity in PC
 - Something Else Shortages = Something Else Bottlenecks → Convexity in PC?
- **Can account for return of convex PC even if labor shortages not main driver**
 - CES with labor and Something Else S : $Y = (\alpha S^{1-1/\epsilon} + (1 - \alpha)L^{1-1/\epsilon})^{\frac{\epsilon}{\epsilon-1}}$
 - Say, fully fixed supply of S (but little elastic supply is enough)
 - Say, infinitely elastic supply of labor (to make things even sharper)
 - Getting rid of all search frictions with their potential non-linearities

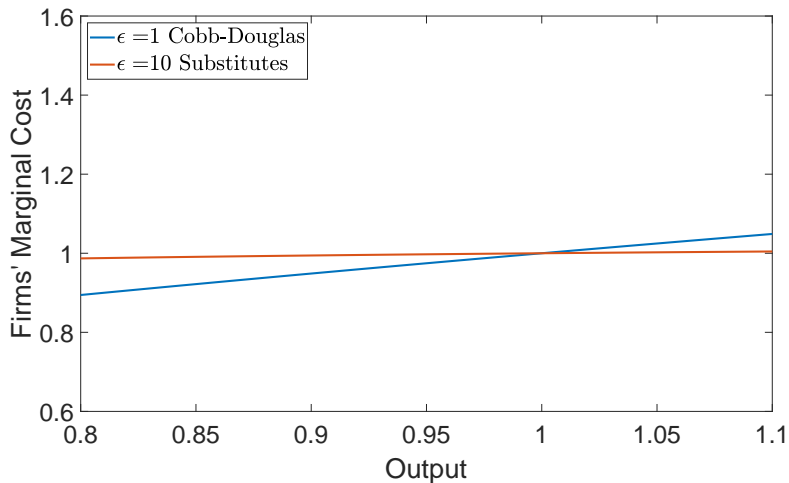
Bottlenecks/Convexity: Something Else Shortages



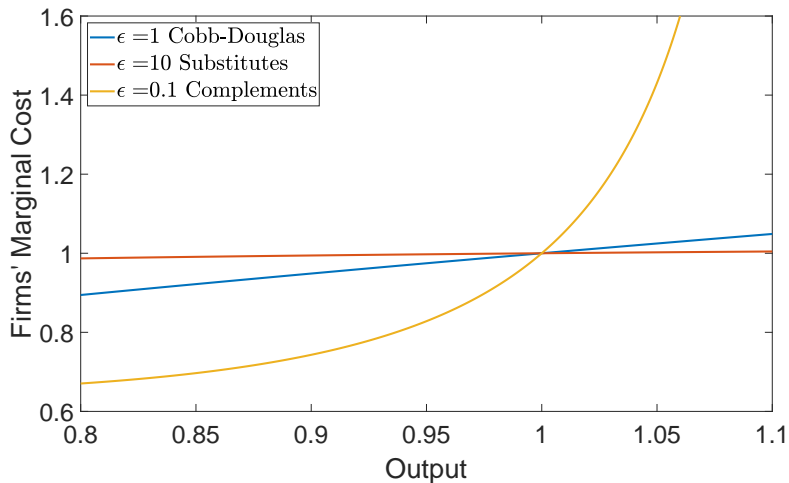
Bottlenecks/Convexity: Something Else Shortages



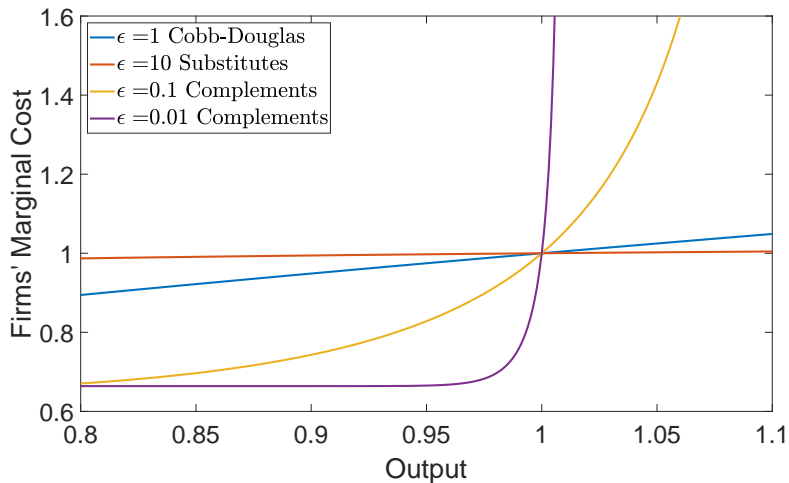
Bottlenecks/Convexity: Something Else Shortages



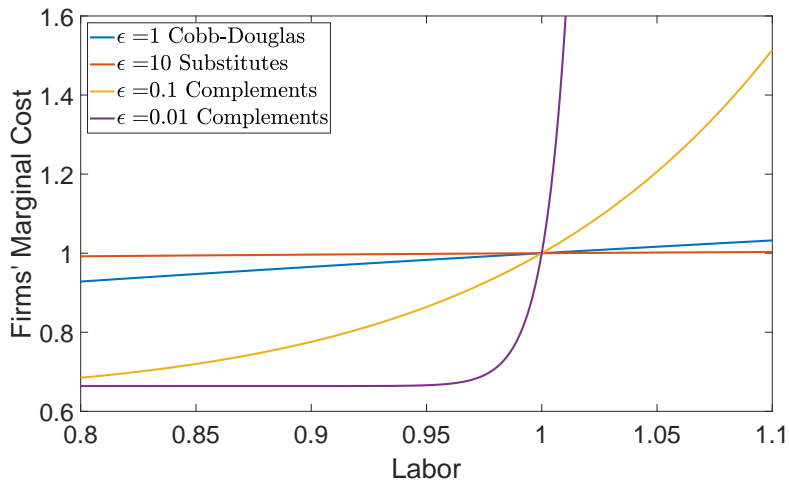
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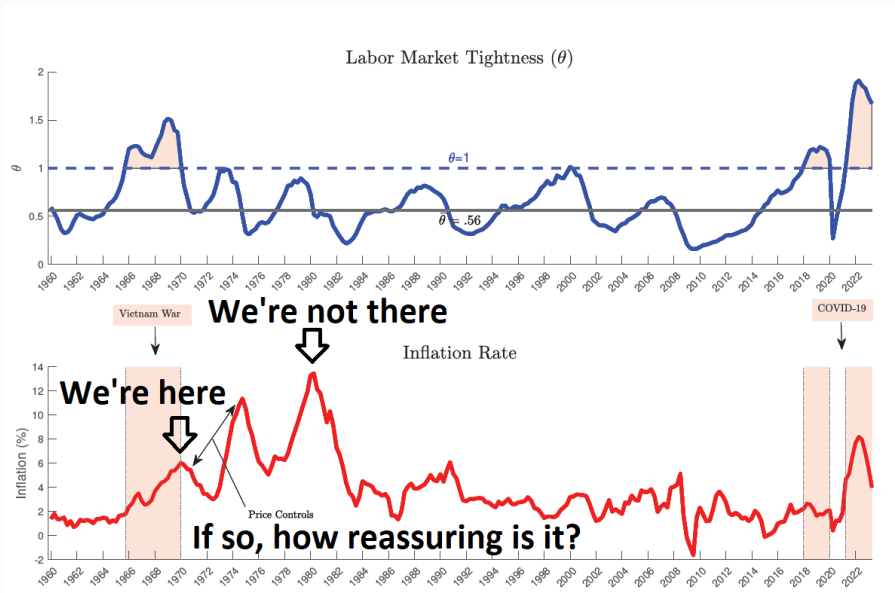


Bottlenecks/Convexity: Something Else Shortages

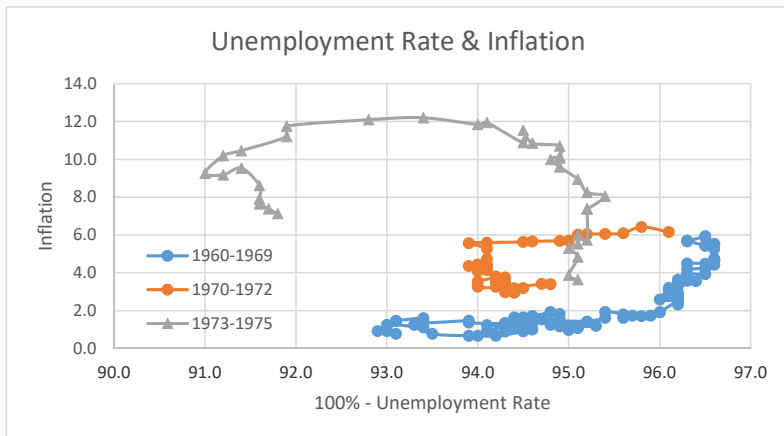


→ Can we empirically rule out this alternative account of the convex PC?

Comment #3: Different from the 1970s, but how different from the 1960s?



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- **Optimistic conclusion of the paper: Today is different from 1970s**
 - 1970s: PC shift from $\uparrow E(\pi)$ due to passive MP, hard to undo
 - Today: Convex part of PC, easy way up but also easy way down
- **But this narrative of the 1970s usually highlights 1960s as root of $\uparrow E(\pi)$**
 - *“Martin tried to exploit stable PC, encouraged by Samuelson and Solow”*
 - *“Paved the way for easy de-anchoring from oil-price shocks of 1974 and 1979”*
- **Paper actually highlights today similar to 1960s!**
 - Should we then worry we are replaying the 1960s, paving the way to the 1970s?
 - Will the 2025s be the 1970s?
 - De-anchoring after Lithium Price Shock of 2026 and Chilean Revolution of 2031?
 - Ending with Judy Shelton disinflation of the 2030s?
- **Or can we be optimistic this time will be different from the 1960-1970s?**
 - e.g. inflation expectations will remain better anchored
 - But if so why, if 2022 was comparable to 1960s, including wrt. convexity of PC?