Distribution of Inflation Impact: 
The Recent Experience in Central America and Mexico

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I. Introduction
In October of 2008, even in the presence of the largest financial crisis since the great depression, 60 percent of the households on earth experienced inflation above 10 percent. The US financial crisis and its contagion will create a recession worldwide that should reduce the inflationary pressures in the short run. However, in the resolution of such crisis, central banks are printing currency as we have never done in the past. Needless to say, the recovery should be accompanied by a rise in inflation again; and the problems that seem to have plagued our recent past, are bound to reappear two years from now.

The recent inflation has a particular characteristic that makes it different from previous episodes – it is mainly in food prices. Indeed, in the last 10 decades, in the world, the average inflation in food was almost always lower than the inflation in services, except during wars and the past 5 years. In fact, because inflation has been concentrated in food and energy it has had a severe distributional impact. So much that in countries such as Panama, where a very high growth rate has occurred in the past couple of years, unprecedented in the last couple of decades, still finds the incumbent party in a contested election. The reason? Very simple, inflation has been particularly unfair.

The purpose of this paper is to document the distributional impact of recent inflation in a region where inflation is likely to have a significant political and social effect. The paper documents first the very large differences that exists in consumption baskets and then documents the differences in inflation across the countries and income groups.

One important question we address in the end is what should governments do, and can do about this issue. For instance, is this a problem to the central bank? If so, what it can do? Or is this just a problem that fiscal policy should take care of? In fact, a very reasonable reaction to the issues highlighted here is that the inflation in wheat and oil that the world has just witness is a change in relative prices, and central banks should not react to those – supply side relative

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price changes. We come back to these points at the end of the paper arguing that if there are inefficiencies, such as price stickiness, then central banks should at least be aware of the distributional impact they produce, and the distributional impact that choosing their target causes.

Section 2 describes the nature of the problem using aggregate data for Central America. Section 3 describes the micro data used and studies the problem of distribution caused by the different consumption baskets. Section 4 presents the results for each country. Section 5 concludes with some policy lessons.

II. The distribution problem: A Simple Example

As was highlighted by Deaton (1998), when consumers have heterogeneous consumption baskets, and prices have heterogeneous inflation rates, the inflation rate faced by each agent is not the same as the one summarized by the CPI. This is intuitively obvious. The second point, however, is a little bit more sophisticated. When agents also have income inequality, the CPI basket is biased toward the basket of the riches percentiles. The reason is that the CPI is computed based on total expenditures as opposed to expenditure shares. To clarify this second intuition, let us proceed with an example.

Assume there are two types of agents in the economy, equally populated. Assume there are two types of goods: food and services. Finally, assume that their expenditure shares are as follows

<table>
<thead>
<tr>
<th>Expenditure Shares</th>
<th>Food</th>
<th>Services</th>
</tr>
</thead>
<tbody>
<tr>
<td>Agent 1</td>
<td>70</td>
<td>30</td>
</tr>
<tr>
<td>Agent 2</td>
<td>30</td>
<td>70</td>
</tr>
</tbody>
</table>

Clearly, if there are the same numbers of agents in each group the average expenditure share in the economy – based on expenditure shares – is 50-50. Indeed, if the two agents have the same income (let’s say 100), the aggregate expenditures in food and services are 100, and therefore, the CPI defined as the weights in the aggregate expenditure basket also puts weights 50-50. Notice however, that if income is unequal the basket defined from the expenditures is different as to the average of the expenditure shares. For example, assume that agent 2 has an income of 1000 while agent 1 has income of 100.

<table>
<thead>
<tr>
<th>Expenditures</th>
<th>Food</th>
<th>Services</th>
</tr>
</thead>
<tbody>
<tr>
<td>Agent 1</td>
<td>70</td>
<td>30</td>
</tr>
<tr>
<td>Agent 2</td>
<td>300</td>
<td>700</td>
</tr>
<tr>
<td>Total</td>
<td>370</td>
<td>730</td>
</tr>
<tr>
<td>CPI Weights</td>
<td>33.6%</td>
<td>66.4%</td>
</tr>
</tbody>
</table>
In this case, the total expenditures on food are only 33.6 percent of the aggregate income. In fact, the higher the inequality, the closer is the CPI basket to the basket of the richest.

Notice that at least two baskets can be defined in this example: the expenditure based basket (the usual one for the CPI) and the plutocratic basket (the one that averages out expenditure shares). The difference between the plutocratic and the expenditure based is that the first one eliminates income differences and averages out individual expenditure shares, while the second one computes the basket from aggregate expenditure shares.

There is an important discussion in the literature which basket is appropriate. See Deaton (1998) and Ley (2002) among many.

The purpose of this paper is not to indicate what governments of countries should do. The purpose is to highlight what they are doing. The idea is to present a picture of how the situation in Central America is today with the hope that these arguments will become a topic of conversation in the future.

What happens if the number of individuals is not the same in the different income groups? Still the bias exists. For instance, assume that there are 10 times more agent 1’s than agent 2’s. The plutocratic basket assumes the income of all agents is the same and computes the average over the individual expenditure shares. In this case, the weight on food is 10*70+1*30/11 which is 66.4 percent. On the other hand, if agent 2 is ten times richer than agent 1 the expenditure based basket puts a weight on food equal to 50. Again, the basket of the CPI is 50, which is closer to the weight from the rich (30) than what the plutocratic basket would put (66.4). In this example we can define an additional basket – the one from the median citizen – which in this case would put a weight on food equal to 70. It is the case, not only in this example but actually in the data, that the plutocratic basket is less favorable to the poor than the median basket; while the CPI basket is the least favorable of all.

III. CPI baskets
With this example at hand, let’s proceed to the data. We collected the micro CPI data from Mexico, Guatemala, Honduras, El Salvador, Nicaragua, Costa Rica, Panama, and Republica Dominicana. For all countries (except Panama and Republica Dominicana) we have 10 years of monthly prices of all the goods used for the construction of the CPI. On average, each country has 300 items that range from basic food to services.

We also collected average income and expenditure shares for 10 deciles in all these countries. The first step is just to show the differences in expenditure shares and income impact the basket that the CPI is representing. For expositional simplicity we concentrate on food versus non-food expenditures in this section.

Figure 1 shows the expenditure share on food by deciles for all the countries. The deciles are in the horizontal axis, and 1 is the poorest decile. Notice that the differences are dramatic. In the case of Honduras, the poorest decile consumes around 80 percent of their income on food,
while the richest dedicates less than 35 – a swing of more than 45 points from the poorest to the richest!

For instance, Costa Rica, which is the country in the region with the smallest aggregate expenditure on food, the poorest dedicate almost 40 percent of their income to food, while the rich spend close to 5. Again, a tremendous swing in expenditure shares from the different income groups. In fact, for every country in our data, the differences between deciles 10 and 1 are bigger than 30 percent for all of them!

Additionally, not only the differences across income groups within countries are interesting, but also across the differences across countries. Concentrating on the median decile, the largest food expenditure share is found in Honduras with 75 percent, and the smallest in Costa Rica with 25 percent. Guatemala is also very close to 70 percent, while the rest of the countries are have expenditure shares of their median citizens between 40 and 50 percent.

![Expenditure Shares on Food](image_url)

**Figure 1:** Expenditure Share on Food by Deciles and Countries

One important caveat in Figure 1 numbers is that this is the expenditure on food not taking into account that poor deciles in general supply part of the food they already consume.

In Figure 2, we adjust the initial shares by the proportion of self-consumption. As can be seen, the differences are smaller than in Figure 1 – which is a simple reflection that poorest families consume a larger share of food that is produced at home. Nevertheless, the differences between the expenditure share from the poor to the richest is still large; close to 30 to 40 percent differences in most countries.

In terms of inflation – which is the purpose of this paper – it is not clear which of the two we should take. The reason is that the price is the opportunity cost of the self consumption, and
therefore, their basket is increasing at that speed regardless. In any case, notice that even after adjusting for self-production the differences still very large across countries and deciles.

**Figure 2: Expenditure Share Adjusted by Self Consumption on Food by Deciles and Countries**

The next step is to concentrate on income differences. In Figure 3 we present the income of each decile relative to the poorest one. The left axis is in logs. Notice that for most countries, the highest decile is close to 10 times richer than the poorest. The countries have significant differences in income. The most equal country has the richest 10th percentile being 4 times richer than the poorest, while the most unequal country the richest is 30 times richer.

**Figure 3: Income relative to poorest decile**
Figure 3: Income differences relative to first decile.

Not coincidentally the numbers we used in the simple example in section 2 are of the same order of magnitude we observe in the data. Therefore, the bias we discussed in the previous section is possibly of the same order of magnitude in this data. This is our next step. We are interested in answering the following question: which decile does the CPI represents? Which one does the plutocratic based index represents?

In what follows we are going to create “fake” CPI baskets using the information we have so far. The reason why these are “fake” CPI baskets is because we are considering only consumption from citizens. We are not including investment and government consumption. In other words, the basket we will construct will have weights on food that are much larger than the real ones (investment and government consumption have weight of almost zero on food and beverages). However, for the purpose of this paper we do not want to contaminate the conclusions about which deciles the CPI basket represents by shifting the weight because government consumption is biased toward services.

Using the income of each decile and their respective baskets we construct three indexes. First, the median basket is just taking the consumption basket of the median citizen (the average of deciles 5 and 6). Second, the plutocratic basket is the simple average across all deciles – which in general does not coincide with the median because basket distributions are skewed. Third, the “fake” CPI basket is obtained by computing the implied consumption from each decile and then aggregating for the country.

Figure 4: Weight on food of the different baskets.

In Figure 4 we present the weight on food that each basket allocates. The basket identified as “average expenditures” is the plutocratic. Notice that for all countries the CPI puts a lower
weight on food than the plutocratic. In turn, for all countries except Panama, the plutocratic basket assigns lower weight than the median basket. The differences between the last two are small, but still are significant for some countries.

An alternative perspective of these differences is to try to compute which percentile does the CPI basket targets. In other words, assuming that the differences in the expenditure shares evolve smoothly across deciles we can compute which percentile has the closest basket to the one the CPI or the Plutocratic indexes are capturing. Of course an assumption required is that the share moves smoothly from one percentile to the other. Under that assumption, in Figure 5 we present the implied percentile capture by each index. The purpose is to compare the basket to the median citizen’s basket – i.e. how far it is from the median?

Only two lines are presented. The top line corresponds to the percentile targeted by the CPI, the lower schedule is the percentile from the plutocratic basket. We do not show the line for the median because it is a flat line crossing at 50 percent.

Notice that for all countries the CPI baskets reflect agents that belong to percentiles above the 70 percent. For countries such as Honduras, Guatemala and Costa Rica the basket is closest to percentiles above 80 percent! Very importantly these numbers will be exacerbated when government consumption is included. The reason is that investment and government expenditures have an even lower share on food than the rich. The best countries in our sample are Mexico and Republica Dominicana which are targeting the 70th to 75th percentile – i.e. their CPI baskets correspond to the 70th to 75th percentiles.

Figure 5: Implied deciles targeted by the expenditure based index (CPI) and the expenditure shares based index (plutocratic).
One feature from this figure that is worth highlighting is that the plutocratic index helps move the target toward the median citizen, but does not goes all the way. For Honduras and Guatemala the plutocratic index is still closest to the 70th percentile. For the rest of the countries, however, it is between the 55th and 60th percentiles. In this dimension the best country is Panama with a weight closest to 50.

One important aspect that is worth repeating: what we call “best” in the previous discussion is in terms of comparing the basket of the inflation index to the one from the median consumer. Where “best” here is not a value judgement in terms of what countries should do, but a measure of how close the basket from the median is. Again, this is just reflecting a fact: what the countries ARE doing; and not necessarily an indication of what they SHOULD be doing. We leave this discussion to the final section where other dimensions of the distributional characteristics of the prices are further explored.

IV. Country Results

The previous section has discussed how the heterogeneity in income and consumption baskets affects the “target” that the CPI is capturing. In this section we use the micro data to measure how these differences have affected the different deciles in Central America.

We study several dimensions. First, average yearly inflation; in Latin America food has increased much faster than services and other items – which means that the poor, who have a higher weight on food, will suffer higher inflation. The question is how much higher.

The second aspect we study is the volatility of the basket. Food and energy in general are more volatile prices and because the poor have a larger share of their expenditures in these products we would like to measure how much volatile those baskets really are. This is extremely important because clearly the poor have less ability to insure their real income. Hence, this volatility is more likely to be welfare detrimental than for the agents that are able to insure against inflation.

Finally, we study the degree of stickiness of each of the baskets. Modern optimal monetary policy analysis (see Aoki (2001), Benigno(1999), and Woodford(2003)) have highlighted that, other things equal, central bankers should put a higher weight on those goods that have higher degrees of stickiness. The reason is that sectors in which prices are flexible monetary policy movements are going to be irrelevant because prices will adjust rapidly. In fact, this is a common explanations why central banks want to define “core” inflation and eliminate form the index the flexible prices, and the prices that are driven mostly by supply side shocks.

We describe how each country looks like in these three dimensions. The results for every country are summarized in six figures. The top left panel shows the evolution of the price level for each basket. Time is measured in the horizontal axis and the baskets have been normalized to have a price of one for the first observation. In this figure we present the price level of each decile as well as the evolution of the price of the food basket and the non-food basket. The baskets were computed using the actual consumption shares
The top right figure shows the annualized inflation for each decile relative to the inflation from the richest decile (the 10th). We also present the inflation of the CPI and the Plutocratic index. On the horizontal axis the deciles and baskets are depicted. The vertical axis is the inflation rate in percentage terms. In this figure we present the inflation differentials for the baskets computed using the consumption shares, and the baskets computed using the self-production adjusted consumption shares.

The two mid figures measure the degree of stickiness in the baskets. The horizontal axis in both figures depicts each income group (plus the implied CPI and Plutocratic baskets). The left mid panel is the stickiness by decile and for the CPI and Plutocratic indexes. The different baskets are depicted in the horizontal axis and the probability that prices remain constant in two consecutive months is measured on the vertical axis. We compute for every basket the unconditional probability that items have the same price in two consecutive months, relative to the total number of items that actually have two consecutive prices. See Bills and Klenow (2004), Gopinath and Rigobon (2008), and the references there in for a description of this procedure to measure stickiness.

The right mid panel just computes the ratio in the degree of stickiness of each basket relative to the degree of stickiness in the CPI basket.

Finally, the last two figures document the volatility of monthly inflation. The panel on the left computes the standard deviation of the monthly inflation in each basket, while the figure on the right computes the variance in each social group relative to the richest percentile. In the figure on the left we present both the consumption shares and the consumption shares adjusted by self-production results, while the figure on the right only measures the relative variance for the consumption share.

With this overall explanation to the figures, we proceed to summarize briefly the results for each country.

The organization of countries is geographical – from north to south.

A. Mexico
Mexico is an interesting case to start with. First, the inflation differences between the rich and the poor are not extremely large. As can be seen from the second panel, the poorest suffer just 0.2 percent more inflation a year than the rich when we compute the inflation using the total consumption baskets. If we use the adjusted consumption basket these differences are less than 0.05, and it is the 4th percentile the one that actually suffers the most inflation – and its differential is only 0.12 percent. What is even more important is that these differences occur for inflation rates for the aggregate that are greater than 10 percent a year.

In other words, in a relatively high inflationary environment, the differences between rich and poor in Mexico are very small.

Stickiness is also an interesting dimension in Mexico. Mexico is by far the least sticky country in our data set. Notice that on the third panel, prices have a probability to remain constant of 4
percent for other items, and 0 for food prices. In other words, in the case of food, prices change every month, while in the case of other goods they change relatively frequently. This implies that the differences in the stickiness of the baskets across deciles is very small in absolute terms.

In relative terms these differences are very large, mainly because the denominator is very close to zero. In other words, looking at panel 4 we notice that the degree of stickiness of the poor is 20 percent smaller than the stickiness in the basket of the rich. But this 20 percent is from a base of only less than 4 percent.

Finally, we concentrate on the volatility of the inflation rate across the different income groups (panels 5 and 6). As expected, given what we have discussed already for Mexico, the
differences are extremely small. In panel 5 we can see that the volatility of the poor has a volatility of 12.2 percent, while the rich suffer 12.0 percent. In panel 6 we show the differences in relative terms, and even though the poor have a larger volatility than the rich, the variance only increases in 0.8 percent. In terms of volatility, the plutocratic index represents the 6th percentile, while the CPI is close to the 7th one.

One immediate conclusion of this analysis is that Mexico, targeting the CPI, plutocratic basket, or any of the baskets of the income groups is likely to produce similar macro effects. In this country the outcome of monetary policy and its impact on the economy are going to be almost identical irrespectively if the CPI or the Plutocratic basket is used.

B. Guatemala
The case of Guatemala is different from the Mexican case.

First, inflation across the deciles is much larger for the lower ones. For example, from all the deciles between 1 and 6 the inflation is 0.6 percent higher than the richest one; where the average inflation of the rich is 6.5 percent. This means that 60 percent of the households have an inflation that is 10 percent higher than the richest decile. Furthermore, the poorest deciles have one more point of inflation a year than the richest. In other words, in Guatemala, the poorest have lost one percent of real income a year more than the richest.

Notice that the comparison between the expenditure based baskets and the adjusted by self consumption ones are very similar.

Turning our attention to the degree of stickiness the probability that prices are fixed for the food in Guatemala is 2 percent, while other prices have a probability of being constant of 12 percent. There is a large and significant difference in the degree of stickiness of these two types of goods, and therefore, not surprisingly, the degree of stickiness of the different baskets moves significantly across income deciles. It fluctuates from 4 percent for the lowest deciles to 8 percent for the highest.

Finally, the difference in volatility of each of the baskets is large. For instance, the standard deviation of the inflation of the poorest is 5.5 percent, while it is 4.1 percent for the richest one. In other words, this represents almost 35 percent higher volatility (as shown in Panel 6).

The ratio is reduced when the expenditures are adjustment by self-consumption. Nevertheless, the variance is 25 percent higher for all the deciles between one and five.

Notice that the plutocratic index has the same volatility as the 6th percentile, while the CPI’s volatility is between the variance of the 8th and 9th percentiles.
C. Honduras

The third country we study in detail is Honduras. Notice in Panel 1 that Honduras did not experience the inflation differentials the other countries in the region had. In fact, for the first seven years of the data, the inflations of food and services where so close that even though agents have different weights in their baskets there are no major differences across them. It is only in the last couple of years where it can be seen that food has started to increase at a faster pace than services.

The average inflation is indeed larger for the richest group in the society. This result is very similar to the inflation differentials in the US (see Broda and Romalis (20XX)); and similar to the inflation differentials in the Nordic countries (see Ehrmann, Fratzscher, and Rigobon (2008)).
Regarding the stickiness and volatility, however, Honduras looks very similar to the other countries in the region. The basket of the 1st decile is less sticky than the basket of the richest deciles. In fact, the stickiness of the rich is close to 25 percent, while for all the deciles between 1 and 6 the stickiness is less than 15 percent.

In terms of volatility, Honduras presents one of the most dramatic differences in our sample. Notice that the variance of food products is close to 6.5 percent, while it is just above 4.0 percent for other products. These products are clearly negatively correlated because for the 10th decile the variance is smaller than the services one. The poor have a much larger variance. Panel 6 shows that it is 60 percent higher!
Finally, the plutocratic index has similar volatility to the 6\textsuperscript{th} percentile, while the CPI has a variance that is between the 9\textsuperscript{th} and the 10\textsuperscript{th} percentile. In other words, stabilizing the variance of the CPI is actually stabilizing the variance of the highest percentiles, which is a small fraction of the variance of the lowest ones.

**D. El Salvador**

The patterns of inflation, variance, and degree of stickiness for El Salvador look very similar to the results from Guatemala. In the case of El Salvador it is important to mention that the differentials in inflation – for a dollarize economy – are very large. In other words, 0.35 percent inflation differentials is a very large difference across the income groups.
Stickiness moves from 30 percent to 40 percent by moving from the 1st to the highest decile. Finally, the volatility exhibits the same patterns as before – although here the coefficients of variation are quite large.

In terms of volatility, the plutocratic index has volatility between the 5th and 6th deciles. While the CPI's variance is similar to the 8th percentile.

**E. Nicaragua**

Nicaragua, is a very interesting case. Its inflation is very large and different across the deciles. Indeed, in the same order of magnitude as Guatemala. However, stickiness in Nicaragua is extremely low and almost identical for all groups. This is what we should have expected in a high inflation country.
Additionally, also in line with a high inflation country, the volatility of inflation is relatively large. The volatility is 8 percent for the lowest decile and 6 percent for the highest; in relative terms, it is 35 percent larger for the lowest decile.

In terms of volatility the plutocratic index has the volatility of the 6th percentile while the CPI reflects the variance of the 8th percentile.

**F. Costa Rica**

Costa Rica is a country with mild inflation differentials, even though the average inflation in the country is relatively large. This is in contrast with the previous countries where large inflation usually leads to large differentials. And these small differences across groups occur even though food has had much larger inflation than non-food – as can be seen in the first panel. One possible explanation for the differences is that in Costa Rica the food consumption is relatively low.

Before proceeding, it is important to mention that in Costa Rica, we do not have the information on self consumption on food. Hence, all our conclusions are from the straight consumption shares.

As said before, even though Costa Rica has large differences in consumption shares on food, and it has relatively large inflation, the impact of inflation across the different income groups is very similar. For instance, the degree of stickiness in Costa Rica moves from 12 percent for the poor to less than 20 percent for the rich. And inflation volatility is almost the same for all income groups. Costa Rica is one of the smallest differences in relative variance (see last two panels).

Very interestingly, the plutocratic index has the volatility similar to the 6th percentile, as does the CPI.
G. Panama

Panama, as Costa Rica, has had moderate inflation, but opposite to Costa Rica, has had relatively large impact across income groups.

Notice that the inflation differential is 1.8 percent more inflation for the poor per year. This is extremely large differences for a country with an average of 10 percent inflation a year. Regarding stickiness, the differences are small. The highest income has a probability of 35 percent, while the poorest is just above 25 percent. The differences in probability of prices changes are small for all. Finally, the volatility of inflation exhibits large differences across income groups. The poorest decile has 45 percent more volatility than the richest decile.

In terms of volatility the plutocratic index reflects the 5th decile, while the cpi represents the 7th.
V. Final Discussion: Targeting Inflation Targeting

Most countries in Central America do not have inflation targeting as their monetary policy regime; some are dolarized, some are not; some manage their exchange rates, some allow it to freely move; etc. Nevertheless, the detailed analysis of Mexico and Central America allows us to put into context some discussions about inflation targeting that have not received enough attention.

Several lessons can be extracted from the previous analysis.
First, it is clear that inflation in general will impact different groups in the society differently. One question that we have not analyzed in detailed is the following: does monetary policy have distributional impact? Likely yes. The second question is, how big? And if the answer to the second question is that indeed it is large, the next step is to ask whether or not central banks should care about it.

This paper does not pretend to analyze any of these questions but at least to pose them. The recent experience in Central America does highlight that inflation is very different across the income groups, and we have paid little attention to it.

Second, what does the theory says about these differences? There is a growing literature studying optimal monetary policy under heterogeneity; heterogeneity in terms of differences in degree of stickiness (Aoki), differences in degree of supply versus demand shocks (Woodford), differences in their capacity to insure risk, etc. That literature does not study (except for one paper, Benigno) what is the optimal policy regarding individuals heterogeneity.

Nevertheless, optimal monetary policy says that central banks should shift the weight of their “optimal basket” toward goods that are more sticky and that their movements are mostly driven by demand shocks. In fact, this is the rationale of several central banks to concentrate on core inflation. They argue that they cannot control the price of food and energy; and therefore they drop them from the index.

I believe there are several misconceptions about this operation that are worth highlighting. For example, the fact that a country cannot control the international price of oil does not say anything about the price of oil domestically – except for the US. Oil prices are denominated in dollars and therefore the domestic and the international price of oil in the US is the same. But that is not the case in Austria or Brasil and almost any other country. In fact, if the Central Bank decided they want to have a constant domestic price of oil they can perfectly do so by moving the exchange rate accordingly. This is probably not desirable, but the point I want to make here is that this “inability” to control oil prices or food prices is mostly a US “theme” or “mystery”, and not a reality to most countries. Monetary policy does have an impact in the domestic price of oil and food; and therefore it should be part of the objective function of the central bank.

The second aspect is to see monetary policy as the outcome of modern macro models where the central bank is maximizing the utility of its citizens. In this environment, how individuals are included in the aggregate utility function changes dramatically central bank’s operations. For instance, if each individual’s utility is included without normalization (similar to computing the CPI as we have done in the previous sections) the answer would be different if each individuals utility has its income normalized (as in the plutocratic index). And not only monetary policy would be different but the optimal target basket is also different.

This paper is not dealing with these problems. It has only highlighted the tremendous differences in stickiness, volatility and inflation across the income groups in several countries. As pointed out throughout the text, the disparities across countries vary. There are countries in which the differences in all dimensions are small – Mexico. And if we were to have the data for
Sweden I expect those differences to be even smaller. There are other countries, however, that suffer more inflation differentials, or larger stickiness differentials, or higher volatility differentials, or any combination of the three. These differences imply that agents will react differently to monetary policy shocks, and that monetary policy will have a distributional impact. It is clear that one possible response to these facts is simply to point out that central banks can do nothing about it. The other alternative is to take into account in the design of the policy its distributional impact.

This paper is pointing to the importance of the second dimension in the design of future monetary policy regimes.

VI. References


