

Accepted Manuscript

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Paola Boel

PII: S0165-1889(18)30088-5
DOI: [10.1016/j.jedc.2018.02.011](https://doi.org/10.1016/j.jedc.2018.02.011)
Reference: DYNCON 3565

To appear in: *Journal of Economic Dynamics & Control*

Received date: 14 July 2017
Revised date: 19 February 2018
Accepted date: 22 February 2018

Please cite this article as: Paola Boel, The Redistributive Effects of Inflation and the Shape of Money Demand, *Journal of Economic Dynamics & Control* (2018), doi: [10.1016/j.jedc.2018.02.011](https://doi.org/10.1016/j.jedc.2018.02.011)

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The Redistributive Effects of Inflation and the Shape of Money Demand*

Paola Boel[†]

Abstract

I quantify the distributional effects of expected inflation in a sample of OECD countries using a microfounded model of money where agents differ in their consumption risk, against which they can insure using money and government bonds. The model is calibrated using harmonized wealth microdata from the *Luxembourg Wealth Study*. I find that the inflation tax is progressive for low inflation levels, but it becomes regressive as inflation increases. Cut-off points vary across countries and depend on discount factors and heterogeneity in consumption risk across agents. Moreover, I find that the magnitude of inflation's distributional impact depends not only on wealth distribution but also, and importantly, on the curvature and height of the money demand curve. Indeed, a higher and less elastic money demand leads to more regressive effects of inflation, thus implying such effects are not necessarily stronger in a country with a more unequal wealth distribution.

Keywords: Money, Heterogeneity, Calibration, Welfare Cost of Inflation

JEL codes: E4, E5

*I thank Julián P. Díaz and Sam Schulhofer-Wohl, as well as seminar and workshop participants at the Chicago Fed, the Atlanta Fed, the SAET and SMYE Meetings, Sveriges Riksbank, the Federal Reserve Board and Università L. Bocconi. This paper was previously circulated under the title “The Redistributive Effects of Inflation: An International Perspective.” The opinions expressed in this article are the sole responsibility of the author and should not be interpreted as reflecting the views of Sveriges Riksbank.

[†]Sveriges Riksbank, Research Division, SE-103 37 Stockholm, Sweden (e-mail: paola.boel@riksbank.se)

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