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Inflation and Income Distribution after the Pandemic

In the wake of the 2008 crisis, inflation remained below 3 percent. The surge in international inflation above that level during the Covid-19 pandemic has attracted attention not only from economists and economic policymakers but also from working people, who feel its immediate impact in their pocketbooks when purchasing the goods and services included in the basic food basket, an indicator used in Mexico to calculate the National Consumer Price Index (INPC), which in turn is used to measure inflation.[1] Subtracting inflation from the nominal wage gives us the real wage, which is devalued by price increases, driving down purchasing power and the relative share of wages in national income.

The explanation of the relationship between inflation and income distribution can be approached from the structural micro-fundamentals of inflation to the determinants of macro-distribution, without ignoring the political and social factors that shape the relationship. Aside from the industrial and sectoral composition of added value, the relative wage or labor share depends on price premiums and the relationship between unit wage costs and commodity prices. Aside from the industrial and sectoral composition of added value, Y (Wages, W, plus Gross Benefits, B), the relative wage or labor share, W´= W/Y, depends on price premiums and the relationship between unit wage costs and commodity prices. An increase in the price premium, commodity prices, or production costs will be reflected in a lower value of W´, which indicates a reduction of the relative wage share due to the increase in

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commodity prices in relation to wage costs. Here, W' represents the relative standardized wage share over time, which measures changes in that wage share after accounting for structural changes, such as price increases and industrial concentration.

After dividing the numerator and the denominator by W, commodity price increases in relation to wage costs will be reflected in a lower value of W´.

W' reflects a reduction in wages due to the increase in commodity prices in relation to wage costs. Here, W' is defined as the standardized wage share over time, which measures changes in that wage share after accounting for structural variations, such as price *increases* and industrial concentration. Industrial concentration leads to the formation of large oligopolies, where large companies that fix prices influence the industry price, and other vendors in the industry will be forced to move in the same direction because the composition of the price depends on the mean price. Therefore, the company that sets the price premium can set it at a level higher than it would be in the absence of high industrial concentration,[2] which reflects an inflationary increase under the conditions of a modern capitalist structure, where the state –by means of an active income-expenditure policy– can counter the negative effects of inflation on real wages and income distribution.

Inflation and Global Income Distribution

Global inflation fell from its highest level in the first decade of the twenty-first century (9 percent in 2008) to its lowest level midway through the second decade (1.5 percent in 2015).[3] From that point, prices began trending upward and inflation was expected to reach 9.5 percent in 2022. Thus, prior to the pandemic and the war in the Ukraine, global inflation had already been on an upward trajectory starting in 2015. This can be explained by rising economic growth rates resulting from increased spending on capital accumulation, expressed in higher real spending on gross fixed capital formation, which went from US$18.8 billion in 2015 (at constant 2010 prices) to US$21.04 billion in 2019.

In the four years preceding the pandemic, we also see the phenomenon of the Phillips curve, in which a higher rate of inflation correlates with lower male and female unemployment, given that inflation rose from 1.4 percent in 2015 to 2.2 percent in 2019, and female unemployment went from 5.8 percent in 2015 to 5.5 percent in 2019, while male unemployment fell from 5.5 percent in 2015 to 5.3 percent in 2019. Although we saw a steeper slope in inflation starting in 2020, as a result of the economic contraction caused by the pandemic, the negative economic effects of the war between Russia and Ukraine, which have paralyzed economic activity and employment and produced inflationary pressures worldwide, are unquestionable since both are important exporters of commodities, and the war has driven up energy and food prices.

As forecast by the OECD, in 2022 the global economy was expected to be weakened drastically with 3.3 percent economic growth, below the initial estimate of 4.5 percent.[4] The inflation forecast for 2022 was nearly twice the previous estimate. Rising inflation is reducing real income, further concentrating income distribution to the detriment of living conditions for households. In the case of the United Kingdom, despite having reported a reduction in the Gini coefficient from 39.6 in 2000 to 33.2 in 2012, with rising inflation, real wages have fallen 2.9 percent in 2022. Germany has presented a trend toward greater concentration of income since 2000, reporting a 28.9 Gini coefficient, which rose to 31.7 in 2018, with real wages losing 2.6 percent in 2022.

Canada and the United States

Inflation in the United States and Canada has remained below 3 percent. Bucking the global trend, North America presented very low inflation rates even during the 1994

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and 2008 crises, the worst of modern capitalism; however, since 2020, in Canada and the United States inflation has risen by more than 3 percent.[5] Such low inflation notwithstanding, real wages in these two countries have fallen. For 2022, losses were 6 percent in the United States and 2.1 percent in Canada. This situation has been reflected in both countries' income distribution. Canada reports the best income distribution levels, with a lower Gini coefficient than the United States. In the two decades of the twenty-first century, Canada reported a Gini coefficient below 34, fluctuating between 32.7 and 33.8. In contrast, the United States has shown a growing tendency toward income concentration, starting in 1974 with a Gini coefficient of 35.3 and reaching 41.5 in 2019, despite government welfare policies like Medicaid, the Children's Health Insurance Program (CHIP), the Supplemental Nutrition Assistance Program (SNAP), unemployment insurance, etc.

Mexico

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Also significant in this context are efforts by the administration of Andrés Manuel López Obrador to mitigate inflation through direct intervention in price fixing with business leaders in the country, with whom it has reached an agreement not to raise the prices of their products, and to increase the minimum wage without affecting prices. Also, it is important to consider measures to improve income distribution and public welfare with strategies to guarantee employment, education, healthcare, and public welfare through programs like Youth Building the Future, a policy of social spending to boost income, and financial aid for students and the elderly, which, taken together, work to maintain and increase available income, reducing the negative effects of inflation on income distribution and laying the foundation for economic growth and employment.

Notes

1 To identify the volatility of changes in the prices of products in the basic market basket, institutions devoted to statistics have divided the general INPC into core and non-core. The former consists of the increase in prices for a subset of goods and services in the INPC, the amounts of which are not dictated by administrative decisions, seasonal [variations], or high volatility, and includes subindices for goods and services. Goods include processed foods, beverages, tobacco products, and other consumer goods; services include housing, education (tuition), and other services in the basic market basket. The non-core index is comprised of unprocessed farm products, energy, and government-authorized rates. The prices of this kind of inputs may present abrupt changes due to unforeseen events like wars or natural and climatic phenomena such as drought, flooding, pests, etc., that affect agricultural products. It also includes the prices of products traded on international markets like wheat, corn, rice, etc., and government rates like property tax, gasoline, public transport, water, etc. See World Bank, "Inflation, Consumer Prices (annual %)," 2022, https://data.worldbank.org/indicator/FP.CPI.TOTL.ZG.

2 See George R. Feiwel, *Michael Kalecki: Contribuciones a la teoría de la política económica* (Mexico City: FCE, 1981), pp. 126-129.

3 World Bank, "Inflation, Consumer Prices (Annual %)– United States, Canada," 2022, https://data.worldbank.org/indicator/FP.CPI.TOTL.ZG?view=chart&locations=US-CA.

4 Organization for Economic Co-operation and Development (OECD), "Building a Resilient Recovery. Emerging Stronger from the COVID-19 Pandemic," in "Better Policies for Better Lives," 2022, at https://www.oecd.org/coronavirus/en/.

5 World Bank, "Inflation, Consumer Prices…", op. cit.

6 Banco de México, "Portal de inflación. Sistema de Información Económica (SIE)," https://www.banxico.org.mx/tipcamb/main.do?page=inf&idioma=sp.