## Subject Index

- Capital: factors influencing user cost of, 201-20; impact of tax system on user cost of, 231-32; variation in user cost of, 211
- Capital flows, international: imperfect mobility of, 257, 260–63; open economy inflation-induced, 246–51, 264; taxinflation distortion of, 4
- Community Salary Survey (CSS), Federal Reserve Bank of Cleveland, 279–84
- Consumption: effect in Spain of inflation on, 103-11; effect of German tax system-inflation interaction on, 57-67; effect of inflation-induced capital flows, 246-57; effect of lower inflation on, 220-23; inflation effect on intertemporal allocation of, 12-26; with inflation in United Kingdom, 144-57; in Sidrauski model of welfare effect, 181-83. See also Revenue; Saving
- Consumption, retirement: effect of inflation in Spain on, 103–5; effect of inflation on, 13–19; with inflation in United Kingdom, 144–50; overlapping generations model for Germany, 82–88; price in relation to inflation rates, 15–19
- Convergence equations: to assess long-run impact of inflation, 315–16, 318–19, 342; estimation of inflation's effect, 321–25; estimation with individual country effects, 325–32; model of growth and inflation correlation, 319–21

- Data sources: for analysis of inflationconsumption behavior in United Kingdom, 145–46; in assessing inflation's distortions, 135; Community Salary Survey (CSS), 279–84; evidence for effect of inflation on OECD economic growth, 321, 325, 342
- Deadweight losses: changes from reduced inflation, 223–25; from demand for U.S. housing services, 26–35; in German tax system—inflation interaction, 57–67; from inflation-induced capital flows, 246–51; of inflation in open and closed economies, 253–57; model of distortion of consumption causing, 13–26, 41–42; triangles and trapezoids resulting from, 2, 10, 134
- Debt service: cost in United States, 11–12; with reduction of inflation in Spain, 122; related to inflation in Germany, 72–73; related to inflation in United Kingdom, 169–70; related to inflation in United States, 35–36
- Disinflation: cost and benefits of, 2, 9–10; costs in Germany of, 49–56; costs in Spain of, 97–103; costs in United Kingdom, 137–44; differences in gains related to tax rules, 3; Howitt's rule, 77–78; optimal rate in Germany, 79–80; optimal rate of, 77–79. See also Sacrifice ratio
- Economic and Monetary Union (EMU) convergence criteria, 95

- Economic growth: Balassa-Samuelson effect, 337; causality tests of impact of inflation on OECD, 332–38; correlation between inflation and, 4–5, 319–25; evidence of inflation's effect on, 4–5, 134–35, 317–19
- Economic shocks: response of economy to, 332–33; response of government to, 11; in Spanish economy, 101
- Efficiency: effect of inflation in open economy on, 246–57; effect of inflation on efficiency channel, 317; effect of tax distortions on, 2
- Feldstein trapezoids. See Trapezoids Fiscal channels, Germany, Spain, and United Kingdom, 180–81
- Fisher effect: in closed and open economies, 204–7; correlation of nominal interest rates and inflation rate, 17, 236–37, 242–46; German interest rates and price effects, 60; modified, 237; in open and closed economies, 253–55; tax-adjusted, 202, 204–7, 211, 215, 219f, 221f, 222f; on worldwide saving and investment in open economy, 238–46
- Harberger triangles. See Triangles Household behavior: with change in inflation rate, 10; nonsavers, 23–24. See also Consumption; Saving
- Housing, owner-occupied: demand in Germany for, 67–70; demand in Spain for, 3, 111–19; inflationary distortion of demand in United States, 26–32; mortgage interest relief in United Kingdom, 157–65 Howitt's rule, 77–78
- Income: inflation's impact on OECD per capita, 331–32; tax on investment, earned, and retirement, 21–26
- Income tax: effect of inflation on, 15–19; indexation of capital income, 43; treatment of owner-occupied housing, 26–32
- Indexation: as alternative in Germany to price stability, 66; in Spain, 102; of U.K. capital gains tax, 140, 171; of U.S. tax system for inflation, 6, 10
- Inflation: aggregate relationship between unemployment and, 296–97; convergence equations, 315–16; cost of servicing national debt with reduced, 35–36; costs of high levels of, 317; cost to shift to price

- stability from, 38; distortion of demand for money, 32-35; distortion of demand for owner-occupied housing, 26-32; effect on allocation of capital, 223-25; effect on consumption of lower, 220-23; effect on cost of owner-occupied housing, 26-35; effect on domestic and foreign investment incentives, 239-46; effect on efficiency in open economy, 246-57; effect on occupation and employer wage components, 285; effect on tax distortions, 2, 10; effect on user cost of capital, 211-22; evidence of effect on economic growth, 4-5, 134-35, 317-19; impact on OECD growth, 325-38; model of effect on large-firm wage setting, 275-79; negative effects of, 317-18; net impact of effects on labor market, 297-99; targeting of, 344-45; triangle and trapezoid distortions, 2, 10. See also Disinflation; RPIX inflation, United Kingdom; Trapezoids; Triangles
- Inflation, Germany: welfare gain from reduc-
- Inflation, Spain: gain from reduction in, 3; relation to unemployment (1964–95), 97–99
- Inflation, United Kingdom: gain from reduction in, 3-4; house prices with, 157; RPIX inflation, 136
- Inflation rate: benefit of zero, 73–75; effect in OECD countries, 316; effect of differences on capital flows, 235–36; effect of high, 2; effect on revenues, 21–22; EU annual, 96; excess burden associated with, 47; G-7 countries (1963–95), 48; Howitt's rule, 77–78; optimal, 48; for price stability in United States, 1; relation to price of retirement consumption, 15–19; sacrifice ratio as cost to correct, 47
- Inflation-tax interaction: in closed and open economy, 236–46; effect on international capital flows, 4; in Germany, 3, 56–79; trapezoids in, 173–74; in United Kingdom, 3–4, 144–57; in United States, 2–3
- Interest rates: effect of capital inflows on, 237–38, 242; Fisher's hypothesis related to inflation, 17, 60–63, 236–37; obeying Fisher effect ( $dr/d\pi = 1$ ), 239, 242–57
- Investment, business: effect in open economy of inflation on, 239–46; effect of corporate taxes on incentives for, 209–10; ef-

fect of inflation on, 317–18; effect of inflation on user cost in open economy, 213–19; foreign direct investment, 263–64; relation to inflation in United Kingdom, 173–75

Labor market: inflation's cost and benefit impact, 273–74, 297–304, 309–10; low inflation's cost and benefits to, 275–80; wage adjustment under high and low inflation, 284–96; wage data for occupations, 280–84

MIRAS. See Mortgage interest relief at source (MIRAS), United Kingdom

Monetary policy: Bundesbank targeting strategy, 51–52; Federal Reserve goal for, 1, 6–7; goals of future European System of Central Banks, 95–96; implications of inflation's effect on OECD countries, 344–46; inflation targeting, 344–45; price stability as target for, 47; related to inflation in Germany, 49–50

Money demand: effect of reducing inflation on, 32–35; Harberger analysis, 70–71; related to inflation in United Kingdom, 165–69; related to seigniorage in Germany, 70–72

Mortgage interest relief at source (MIRAS), United Kingdom, 157–65, 171–72

OECD countries: causality tests of inflationgrowth correlation, 332–38, 343–44; estimated long-run cost of inflation, 325–32; estimation of inflation's effect on growth, 4–5, 321–38, 343; inflation rate (1963– 95), 48

Okun's law, 53, 79, 81, 99, 134, 197–98 Open economy: efficiency consequences of inflation, 246–57; Fisher effect with taxation, 238–39; interaction of inflation and taxation in, 236–46

Phillips curve. See Unemployment
Price stability: absolute, 11; advantages of,
5-6, 10-12; benefits in Germany of,
56-79; benefits in Spain for policy
of, 103-11, 122-25; cost of going from
low inflation to, 2; estimates of German
tax system-inflation interaction on, 6367; as goal of European System of Central Banks, 95-96

Revenue: with reduction in inflation, 10, 120; from seigniorage, 11, 32–35, 120–22; from taxes with change in inflation, 10; welfare effect of changes in, 22–23

Revenue effect: of domestic inflation on foreign economy, 257, 259t; on housing with move to price stability in United Kingdom, 163–65; of inflation in open economy, 251–52; of inflation on housing subsidy, 30–32; from lower inflation in Spain, 116–19; of lower inflation rates on, 21–22; with move to price stability in United Kingdom, 152–57; of reduced demand for money in United States, 34–35; of reduced money demand in Germany, 71–72; with rise in capital stock in United Kingdom, 175–76; of tax treatment for German owner-occupied housing, 70

RPIX inflation, United Kingdom, 136, 140

Sacrifice ratio: defined, 47, 316; empirical estimates for, 54–55; estimated for Spanish economy, 97–103; as measure of cost of disinflation, 193–94; for OECD countries, 53; Okun gap, 53, 79, 81, 99–100; output and unemployment, 53–54; related to reduced inflation in Germany, 49–56; in United Kingdom, 137–44

Saving: effect in open economy of inflation and taxation, 239–46; effect of German tax system-inflation interaction on, 57–67; effect of inflation-induced capital flows, 246–57; effect of inflation on, 12–26; with inflation in United Kingdom, 144–52; relation to inflation levels in Spain, 103–11; U.S. and U.K. ratios (1990), 150–51

Seigniorage: as advantage of inflation, 11; loss with reduction in inflation, 32–35, 120–22; in relation to demand for money in Germany, 70–72; in relation to demand for money in Spain, 119–22; in relation to demand for money in United States, 32–35

Tax, corporate: effect on user cost of capital, 209-10

Tax Reform Act (1986): depreciation schedules, 231; investment tax credit, depreciation, and corporate tax rate under, 208, 226-27 Tax revenue. See Revenue

Tax system: distortions caused by, 2, 10; effect of differential taxation, 223–25; effect on user cost of capital with inflation, 201–13; impact on user cost of capital, 231–32; indexation for inflation, 6, 10; reform proposals to gain price stability, 6; role in model of inflation's effect on consumption, 12–26, 41–42. See also Inflation-tax interaction

Tax system, Germany: effect on consumption and saving, 57-67; interaction with inflation, 56-79; treatment of owner-occupied housing, 67-70

Tax system, Spain: effect with inflation, 103-11; treatment of owner- and nonowner-occupied housing, 111-16

Tax system, United Kingdom: advanced and mainstream corporation tax, 146; differences in, 3-4; effect of interaction with inflation, 144-57; incentives in mortgage interest relief, 157-63

Tax wedge: with inflation-induced capital flows, 246-47; Spain, 106; United Kingdom, 144, 148, 171, 173-75

Trapezoids: in analysis of money demand in Germany, 70–71; in analysis of U.K. business investment-inflation interaction, 173–74; deadweight loss of inflation, 2, 10, 59, 135–36; to measure welfare effect of price stability, 79, 81–82, 135–36

Triangles: from deadweight loss of inflation, 2, 10, 134; Harberger's deadweight loss of taxation, 58–59, 135; to measure welfare effect of price stability, 79, 81–82, 134–36; welfare benefits in United Kingdom, 172

Unemployment: aggregate relationship between inflation and, 296–97; effect of inflation on downward wage inflexibility, 42; German sacrifice ratio related to, 52–56; with low U.S. inflation, 5–6; related to disinflation in United Kingdom, 141–44; relation in Spain to inflation (1964–95), 97–99; with shift to price stability, 5; simulated effects of inflation-induced wage adjustment on, 299–302

Wage adjustment, large-firm: analysis of variance (ANOVA), 284-85; from Commu-

nity Salary Survey (CSS), 280–84; comparison among studies of inflation-induced, 302–4; density in high- and low-inflation years, 285–87; model of inflation effect on, 275–79

Welfare effect: comparing move to price stability in Spain and United States, 125-30; cross-country comparison with 2 percent inflation cut, 191-93; discounting gains, 9; with distortion of demand for money, 33-34, 119-22; gain from move to price stability, 2-3, 10-11; gain from negative rate of inflation, 6-7; gain from reduced distortion of demand for housing, 27-31; gain from reduced intertemporal distortion, 14-21; gain from reducing rate of inflation, 2, 9–10, 12t, 22–23, 36–38; Howitt's rule of choice of inflation rate, 77-78; of inflation in open and closed economies, 246-58; losses related to allocation of consumption, 12-26; loss from inflation and tax distortions, 2, 38; of lost seigniorage, 32-35; of reduced distortions in consumption, 103-11; related to costs of government debt service, 35-36, 72-73; related to demand for money, 70-72; Sidrauski model applied to Germany, Spain, and United Kingdom, 181-91; of U.K./U.S. tax and inflation distortions, 135-38. See also Deadweight losses

Welfare effect, Germany: gain from reducing inflation, 3; of price stability, 57-67; tax system-inflation interaction, 57-67

Welfare effect, Spain: demand for money distortion, 119–20; gain from reducing inflation, 3; gains related to housing demand, 111–16; of moving to price stability, 122–25

Welfare effect, United Kingdom: consumption and saving with move to price stability, 154-57; gain from reducing inflation, 3-4; of inflation, 144-57; of inflation distortions on money demand, 165-69

Welfare gains. See Welfare effect
Welfare loss. See Welfare effect
Welfare programs: effect of lower inflation on,
12t, 36–38, 41