Inflation Expectations and Firm Decisions: New Causal Evidence

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We use a unique design feature of a survey of Italian firms to study the causal effect of inflation expectations on firms' economic decisions. In the survey, a randomly chosen subset of firms is repeatedly treated with information about recent inflation (or the European Central Bank's inflation target) whereas other firms are not. This information treatment generates exogenous variation in inflation expectations. We find that higher inflation expectations on the part of firms leads them to raise their prices and reduce their employment.

(joint with Yuriy Gorodnichenko and Tiziano Ropele (Bank of Italy))