Abstract: Inflation and Real Sectoral Output Shares

Economists have argued that an increase in inflation affects sectors unevenly and so induces a costly reallocation of resources across sectors. Previous studies have considered the effects of inflation on relative price dispersion because of its possible effects on resource allocation. However, they have not investigated inflation’s effects on the composition of output which changes in relative prices might alter. We examine the relationship between inflation and sectoral shares directly by using a dynamic panel model. This model also allows us to treat the possible endogeneity of inflation using instrumental variables. We find evidence that inflation changes shares in some sectors.