

Inflation, Relative Price Variability and the Markup: Evidence from the United States and the United Kingdom

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Abstract

This paper links two separate empirical literatures on inflation, relative price variability (*RPV*) and the price-cost markup. Measures constructed from annual and quarterly data for the US and UK are used to examine the nature of the relationships among these variables. The results show that two long-run relationships can be identified from the data: a negative relationship between inflation and the markup and a positive relationship between inflation and *RPV*. We eliminate the possibility that inflation is a proxy for *RPV* in the inflation-markup relationship and show systems estimates to be superior to single-equation estimates.

Keywords: inflation, price setting, relative price variability, cointegration.

JEL Classification: C32, E31.