

# Inflation Notes

- 1  **Inflation**  
Rising prices
- 2  **Inflation & Purchasing power**
  - Inflation: General increase in prices
  - Purchasing power: Ability to buy G & S
  -

As inflation goes up, Purchasing Power goes down!
- 3  **Calculating Inflation**
  - Price Indexes

Measurement that shows how the average price of a given group of goods changes over time

  - Market Basket

The 'given group of goods' measured by a price index
- 4  **CPI: Consumer Price Index**
  - CPI calculated by the BLS
  - It is the Price Index used to calculate America's Inflation rates
  - 8 Categories (see pg 343)
- 5  **Inflation Rate**
  - Percent change in the CPI from one year to the next
  - Shows average price changes
  - Uses a 'Base Year' (1982-1984)
  - Base Year is what all prices are converted to
- 6  **Causes of Inflation**
  - Quantity Theory of Money
    - More Money in System, higher inflation
    - Too much money in system causes *Hyperinflation*
  - Aggregate Demand Changes
  - Aggregate Supply Changes
- 7  **AD and AS**
  - Aggregate Demand:  
Demand for G & S for the entire economy (Macro, not Micro)
  - Aggregate Supply  
Supply of all goods for an economy (Macro, not Micro)
- 8  **Shifts in AD or AS cause Price Level changes, which can be Inflation or Deflation**
- 9  **AD RULES!!!**
  - Most Changes are due to changes in AD
  - 
  - AD is the more powerful force!!!
- 10  **Effects of Inflation**
  1. Reduces Purchasing Power
  2. Reduces Income
    - You get a 5 % pay raise
    - Inflation is 3 %
    - Your REAL pay raise (adjusted for inflation) is 2 %
    - Those on fixed incomes hurt most!
      - No pay raises!!!
      - Inflation erodes their money!
- 11 
  3. Effects Interest Rates
    - You get a loan at 10 % interest
    - Inflation is 4 %
    - The REAL interest is 6 %
      - Higher inflation helps the borrower
      - Higher inflation hurts the Loaner