

Inflation and Deflation

What Makes Money Important?

1. It's a **Medium of Exchange**.

Money is valuable because it is accepted in the buying and selling of goods and services. Money makes trading easier than it would be with barter.

2. It is a **Store of Value**.

Money is a way of storing wealth. If you work today, you can get paid in money and wait to spend it in the future.

3. It is a **Measure of Value**

Money can be used to state how much things are worth. The value of goods and services can be expressed in money prices to allow for easy comparisons

Characteristics of Money

- Portability
- Durability
- Divisibility
- Stability in value



What is inflation?

- **Inflation is:**

- A sustained increase in the average prices of all goods and services in the economy.

Prices are influenced by money supply: more money = higher prices

- Can be caused by greater consumer demand or greater production costs
- Usually coincides with an increase in wages (**cost of living**)

- **Inflation is not:**

- An increase price in one or a few goods or services
- Supply and demand can impact price but not be due to inflation

What causes inflation?

- **Demand Pull:** consumers demand more than the economy can produce (shortages) so businesses raise prices
- **Cost Push:** labor asks for more money so businesses have to raise prices
- **Wage Price Spiral:** high prices force workers to ask for higher wages so producers raise prices
- **Fiscal and Monetary policy:** These may also impact the amount of money available to be spent, but we'll talk about that later.

What is Deflation?

- Identified as continuously falling prices/wages for well over a year and is not a decrease price in one or a few goods

Money Supply: less money = lower prices

- Is usually caused by a sustained decrease in wages
- Is usually accompanied by sustained periods of falling production, unemployment, and limited capital investment (wealth).

Consumer Price Index

- Consumer Price Index (CPI)
 - Measurement used to determine inflation and deflation where the prices of over 200 categories of consumer goods and services are accounted throughout the month.

