Module : English

Level : 3rd year LMD

Branch : Accounting and taxing

Lecture Three : Inflation

- **What is inflation ?**

Inflation is defined as a sustained increase in the general level of prices for goods and services in a country, and it is measured as an annual porcentage change. Under conditions of inflation the prices of goods and services rise over time. Put differently, as inflation rises every Dollar you own buys a smaller percentage of a good or service.

Inflation= Prices rise and the value of money falls down (you have inflation when the prices rise, and alternatively when the value of money falls).

- **What are the causes of inflation ?**

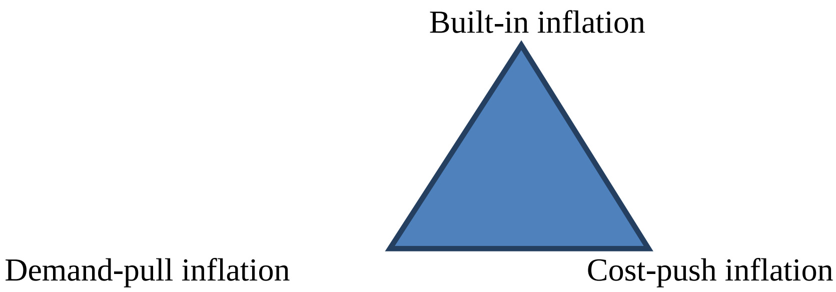
A great deal of economic literature was concerned with the question of what causes inflation and what effect it has. There are different schools of thought as to the causes of inflation :

1) **Keynesian view :** proposes that changes in money supply do not directly affect prices, and that visible inflation is the result of pressures in the economy expressing themselves in prices.
2) **Unemployment :** the connection between unemplyment and inflation was since 19th C and continue to be drawn today. The unemployment rate generally only affects inflation in the short-term, but not the long-term. In the long-term the velocity of money is far more predictive of inflation than low employment.
3) **Monetarist view :** they believe that the most significant factor influencing inflation or deflation is how fast the money supply grows and shrinks. They consider fiscal policy, or government spending and taxation as effective in controlling inflation.

4) **<u>Austrian view :</u>** it stresses that infltion is not uniform over all assets,goods, and services. Inflation depends on differences in markets and on where newly-created money, and credit enter the economy.

❖ <u>What are the types of inflation ?</u>

Robert.J Gorden stated that there are three major types of inflation, what he calls « The triangle Modal »



- ✓ **<u>Demand-pull inflation :</u>** is caused by increases in aggregate demand due to the increased private and government spending.
- ✓ **<u>Cost-push inflation</u>** : Also called ‘ Supply shock inflation’.It is caused by a drop in aggregate supply. This may be due to the natural disasters, or increased prices of inputs.
- ✓ **<u>Built-in inflation :</u>** is induced by adaptive expectations, and is often linked to the’ price or wage spiral’. It involves workers trying to keep their wages up with prices (Above the rate of inflation) and firms passing these higher labour costs on their customers as higher prices leading to a « vicious circle ». this type reflects events in the past, and so might be seen as hangover inflation.

<u>Activity :</u> Explain the following quotations :

a) The monetarist Milton Fired man stated :’ Inflattion is always and everywhere a monetary phenomenon.’

b) Ludwing Von Mises claimed :’ Inflation should refer to an increase in the quantity of money that is not off set by a corresponding increase in the need of money, and that price inflation will necessarily follow’.