W E L C O M E

MONETARY ECONOMICS

Demand pull inflation

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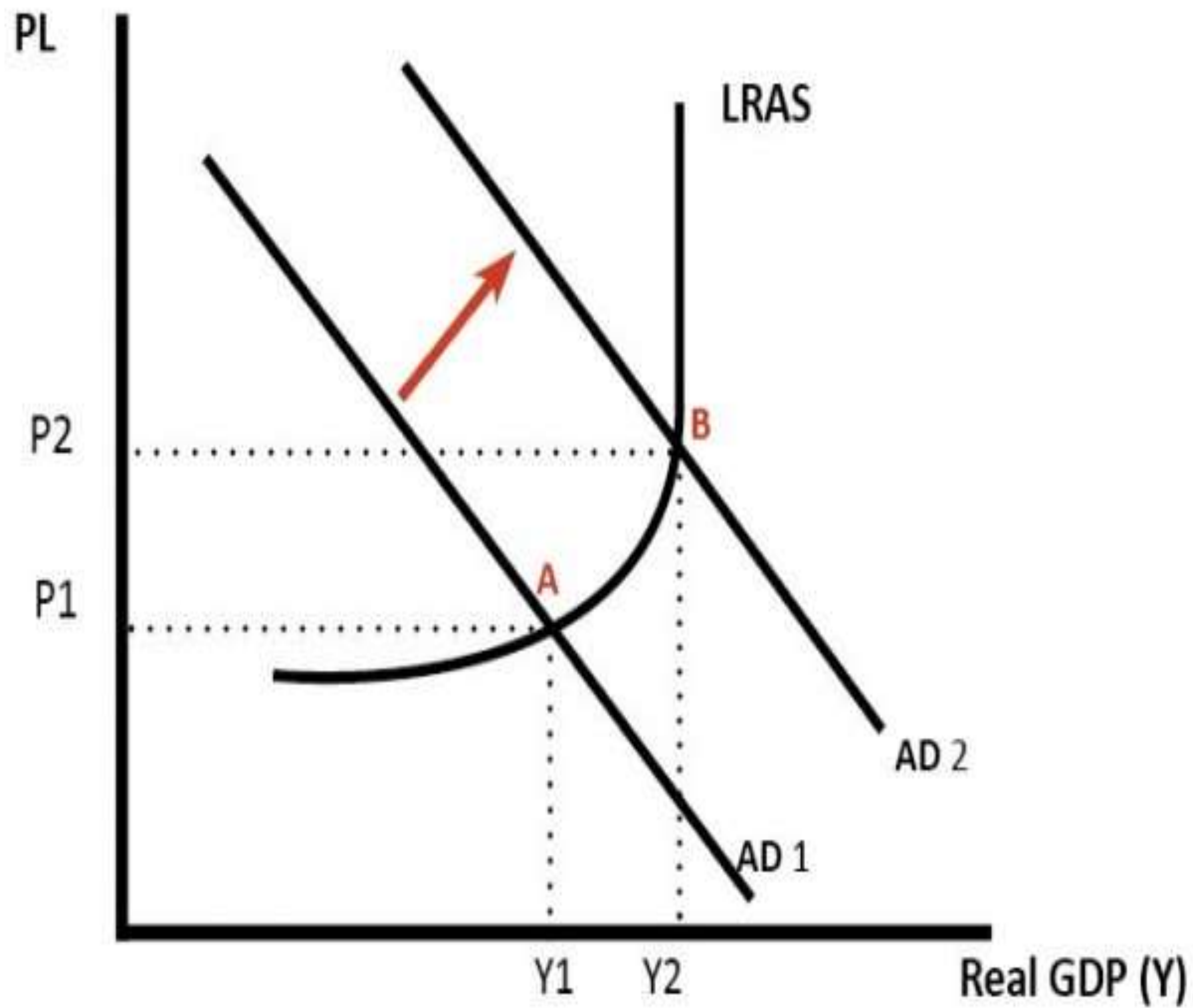
DEMAND – PULL INFLATION

- Demand-pull inflation is a period of inflation which arises from rapid growth in aggregate demand. It occurs when economic growth is too fast.


PL
LRAS
P2
B
P1
A
AD 2
AD 1
Y1
Y2
Real GDP (Y)
www.economicshelp.org

- If aggregate demand (AD) rises faster than productive capacity (LRAS), then firms will respond by putting up prices, creating inflation.

- Inflation – a sustained increase in the price level.

- Demand-pull inflation – inflation caused by AD increasing faster than As.

Demand pull inflation means

- ✓ Excess demand and ‘too much money chasing too few goods.’
- ✓ The economy is at (or ver close to) full employment/full capacity.
- ✓ The economy will be growing at a rate faster than the long-run trend rate.
- ✓ A falling unemployment rate.

Demand – pull inflation occurs

- If aggregate demand is rising at 4%, but productive capacity is only rising at 2.5%; firms will see demand outstripping supply. Therefore, they respond by increasing prices

- Also, as firms produce more, they employ more workers, creating a rise in employment and fall in unemployment. This increased demand for workers puts upward pressure on wages, leading to wage-push inflation.

THANK YUO

Inflation: Causes, Effects, and Implications

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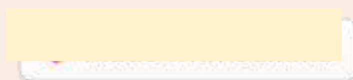
Inflation:

- Increase in price but not accompanied by the increase in production
- First defined by neo-classical economists
- Galloping rise in prices as a result of the excessive increase in the quantity of money
- A persistent and appreciable rise in the general level of prices - Shapiro



Factors Influencing Inflation: Demand-Pull and Cost-Push

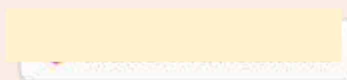
Inflation can be driven by demand-pull forces, where increased spending and consumer demand outpace supply, or by cost-push forces, where increased production costs, such as wages or raw materials, lead to higher prices.

Demand-Pull

Increased consumer spending, government spending, or investment can lead to higher demand, pushing up prices.

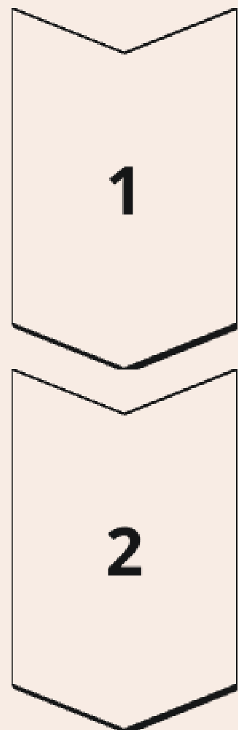
Cost-Push

Rising input costs, such as wages, energy prices, or raw materials, can push up prices.



The Inflation-Unemployment Trade-Off: The Phillips Curve

The Phillips Curve suggests a trade-off between inflation and unemployment: lower unemployment may lead to higher inflation and vice versa.



Low Unemployment

High demand for labor, leading to wage increases and potential inflation.

High Unemployment

Lower demand for labor, potentially leading to lower inflation but higher unemployment.

Monetary Policy and Inflation Control: Tools and Strategies

Central banks use monetary policy tools to manage inflation, such as adjusting interest rates, controlling the money supply, and setting reserve requirements for banks.

1. **Interest Rates**

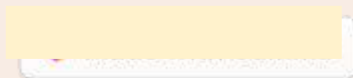
   Raising interest rates makes borrowing more expensive, potentially reducing spending and inflation.

2. **Money Supply**

   Controlling the money supply, such as through open market operations, can influence the availability of credit and spending.

3. **Reserve Requirements**

   Altering reserve requirements for banks can influence the amount of money available for lending.



Fiscal Policy Measures to Address Inflation

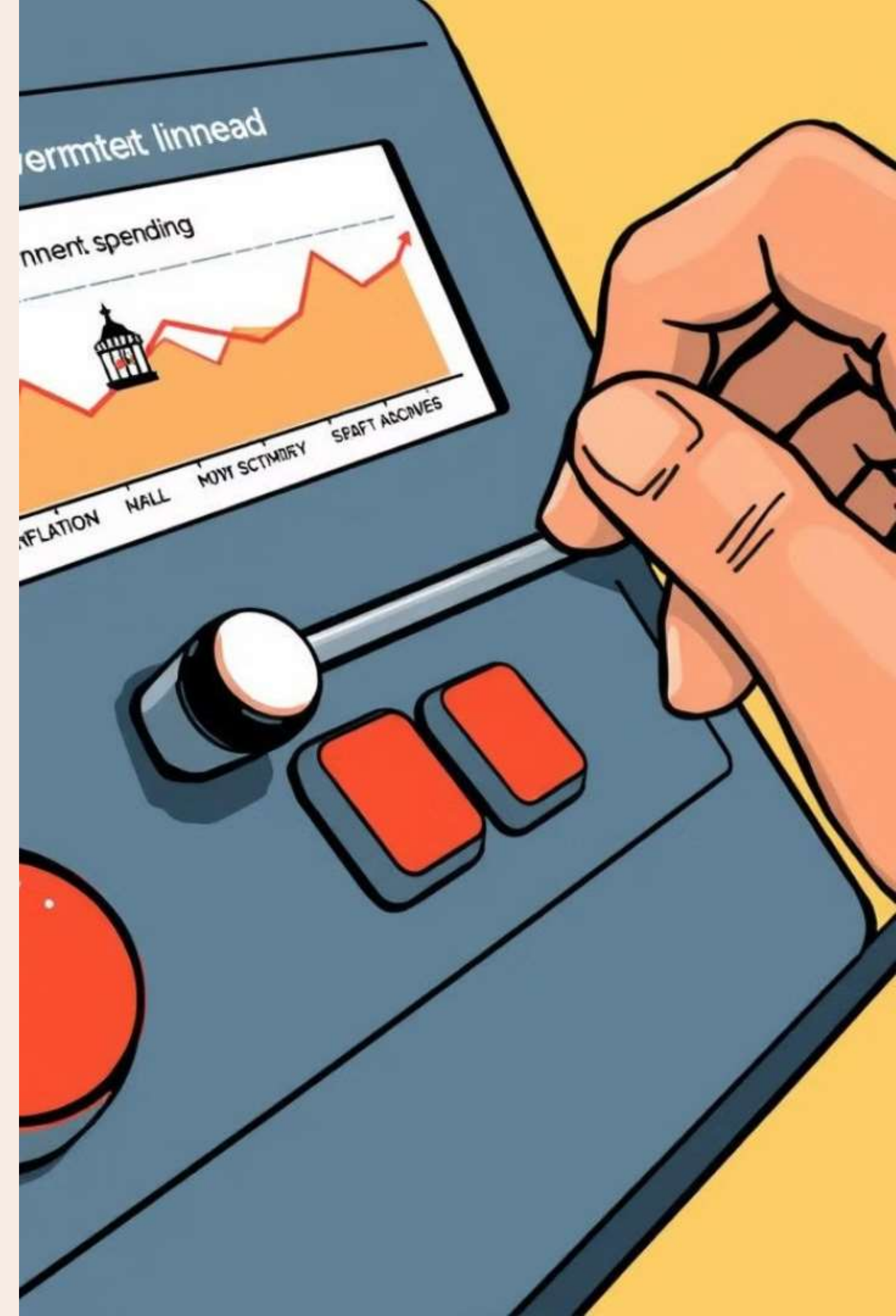
Governments can use fiscal policy to control inflation, such as by increasing taxes or reducing government spending to lower aggregate demand.

Tax Increases

Higher taxes can reduce disposable income, leading to less spending and potentially lower inflation.

Government Spending Cuts

Reducing government spending can lower overall demand and contribute to inflation control.



The Impact of Inflation on Economic Sectors and Individuals

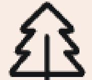
Inflation can have a significant impact on different sectors and individuals, affecting their purchasing power, savings, and investment decisions.

Consumers

Inflation reduces purchasing power, leading to a decline in the value of savings and increased costs for goods and services.

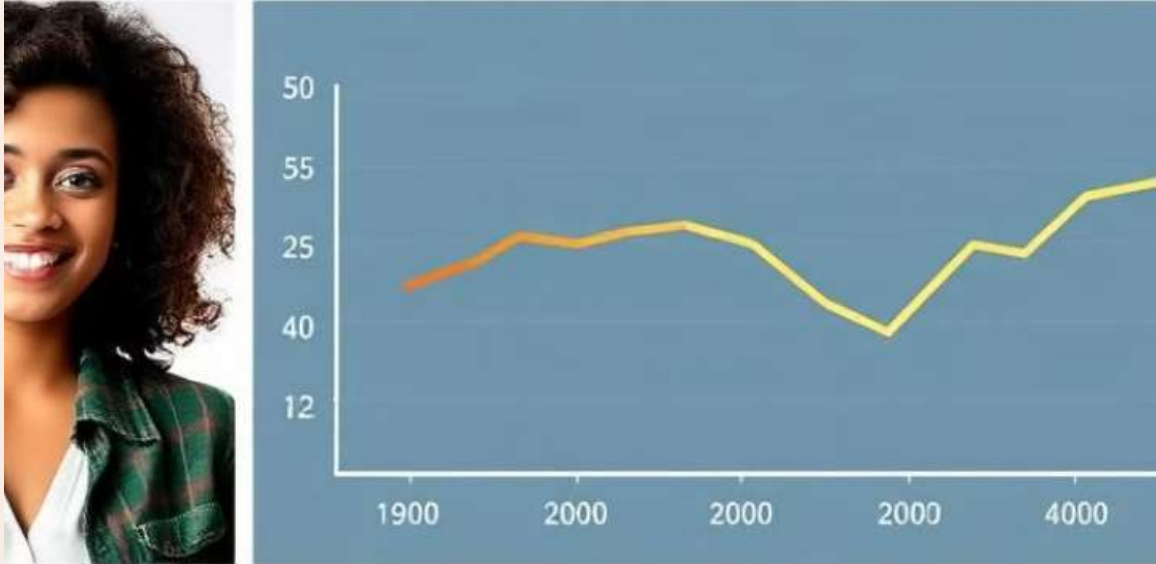
Businesses

Businesses face challenges in managing costs, planning for the future, and maintaining competitiveness.



Investors

Inflation can erode the real returns on investments, and it requires investors to adapt their strategies to account for inflation.



Conclusion :

Navigating the inflationary environment requires a proactive and adaptable approach, including understanding the underlying factors, monitoring economic indicators, and adjusting strategies accordingly.

1. **Monitor Economic Indicators**

   Closely follow inflation rates, unemployment data, and other key economic indicators.

2. **Review Financial Strategies**

   Adjust investment portfolios to account for inflation, consider inflation-protected securities, and seek professional financial advice.

3. **Focus on Value**

   Seek out value-priced goods and services, negotiate prices, and explore alternative options for reducing costs.