BHARAT SCHOOL OF BANKING
INFLATION

Suppose, you lived in **"peace"** (in context of your **spending**) in the year **2010,** when you bought vegetables or fruits (or any other **commodity**) in **much less price** (than present). But at present i.e. in **2015**, the **prices** of the same things have **gone up** which means you have to **spend** much more, than you used to spend in **2010**. This phenomenon is known as **Inflation**.

And if the **government** thinks that the year **2010** was **"ideal"** year to compare the **prices** with, then the year can be determined as **base year** (fixed by government; and generally **changes** with trends in economy throughout periods of time)

For example, if in **2010** (suppose fixed as base year), the price of **potato** was **Rs. 20 / kg**, but the price has **increased** significantly throughout the period, becoming **Rs. 25 / kg** in **2015**. Then the **inflation** would be simply **(25 - 20) / 20 x 100 % = 25 %**

Note carefully, we **cannot** have a **clear picture** of overall **inflation** by taking **only one commodity.** But then, we **cannot** even take **all commodities** (millions!) to measure **inflation**. Therefore, it is **logical** to take few (say **400 or 600,** only a figure) most used and important **commodities** in **market** to measure **inflation**.

Also note that the **price** of **commodities** can be **less than** the **base year.** then it will be known as **Deflation** (opposite of **Inflation**).

Stages of Inflation

Depending on the **intensity** of **inflation**, we can have several stages -

- **Creeping Inflation - (slow) - 2 - 4 %** inflation
- **Trotting Inflation - (moderate) - 4 - 10 %** inflation
- **Galloping Inflation - (fast) - 10 - 20 %** inflation
- **Hyper Inflation - (very fast) - more than 20 %** inflation

Types of Inflation

Inflation can occur for several reasons, hence there are several types of inflation -

- **Demand-Pull Inflation -**
  This type of inflation occurs, when the total **demand** for **goods** and **services** exceeds the **available supply** in the market (meaning more goods needed, but limited stock). As an effect, **prices** of those **commodities** increase. It is also known as **Excess-Demand Inflation.**
- **Pricing Power Inflation -**
  This type of inflation occurs, when **business houses or industries increase prices** of **commodities** to increase their **profit margin** significantly. Generally, they have few or no **competitors** in their market segment, making their business into **monopoly**. It is also known as **Administered Price Inflation** or **Oligopolistic Inflation.**
- **Cost-Push Inflation -**
  This type of inflation occurs, due to the **increase in prices of raw materials, wage** of employees, etc.

making the **ultimate product** more **costly**. For example, price of **car** will rise, if the price of **raw materials** to make a **car** increases.

- **Sectoral Inflation -**
  This type of inflation occurs in a **sector**, due to the rise in **prices** in another **sector**, on which the sector is **dependent** on. For example,