BHARAT SCHOOL OF BANKING
TYPES OF INFLATION

Reflation

If the **government** tries to **increase Inflation rate** to stimulate **economy**, then it will be known as **Reflation.** It can be done by -

- Increasing **money supply** to the market
- Reducing **taxes,** etc.

When **Reflation** is needed?
When the **economy** is in highly **deflated** state, i.e., in **Deflation,** where **price level** of commodities is too low, or **value of money** is too high (meaning you can **buy** a lot of goods with small amount of money!)

Disinflation

It is the opposite of **Reflation**. **Disinflation** process will be used by the **government,** if it tries to **decrease** the **Inflation rate** to recover the **economy** from a high **Inflation** state. It can be done by -

- Decreasing **money supply** to the market
- Increasing **taxes**, etc.

When **Disinflation** is needed?
When the **economy** is in highly **inflated** state, i.e., in **Inflation**, where **price level** of commodities is too high, or **value of money** is too low (meaning you can **buy** a small amount of goods with a lot of money!)

Note that **Reflation** and **Disinflation** are the process of **increasing** and **decreasing** the **Inflation rate**, respectively. But **Inflation** and **Deflation** are the **state** of **economy,** where the **price level** of goods are too high and too low, respectively.

For example, suppose **Inflation** of January is **5 %** (Inflation) and February is **4 %** (Inflation). Then you can say that the price is **disinflated** by **5 - 4 = 1 %,** but is still in **Inflated** state (in **Inflation**) in February.
Now suppose **Inflation** of January is **1 %** (Inflation) and February is -**2 %** (Deflation)**.** Then you can say that the price is **disinflated** by **1 - (-2) = 3 %**, and is in **Deflated** state (in **Deflation)** in February.

There are **two extreme** cases of **Inflation -**

- **Hyperinflation** - This is an extreme situation of **Inflation** in an economy, when the country experiences **very high price level** of goods (which is rapidly **accelerating**), and the real **value of money** is **very low** (which is rapidly **depreciating**).
  In this situation, people try to **hold foreign currencies** (e.g., USD), because their local currency has very low value.
- **Stagflation** - This is an extreme situation of **Inflation,** which is associated with **high unemployment** (stagnant inflation). It raises a **dilemma** for **government**, because reducing **inflation** will rise **unemployment**, while reducing **unemployment** will increase **inflation**.