

Economics II

Inflation, Part II



INVESTICE DO ROZVOJE VZDĚLÁVÁNÍ

COST-PUSH INFLATION, SUPPLY SHOCKS AND OUTPUT LEVEL. METHODS OF INFLATION TREATMENT

The aim of the lecture is to deepen and develop knowledge essence of inflation, whose resources are on hand to aggregate supply, to clarify the effects of inflation and the possibility (methods) of its treatment.

Content:

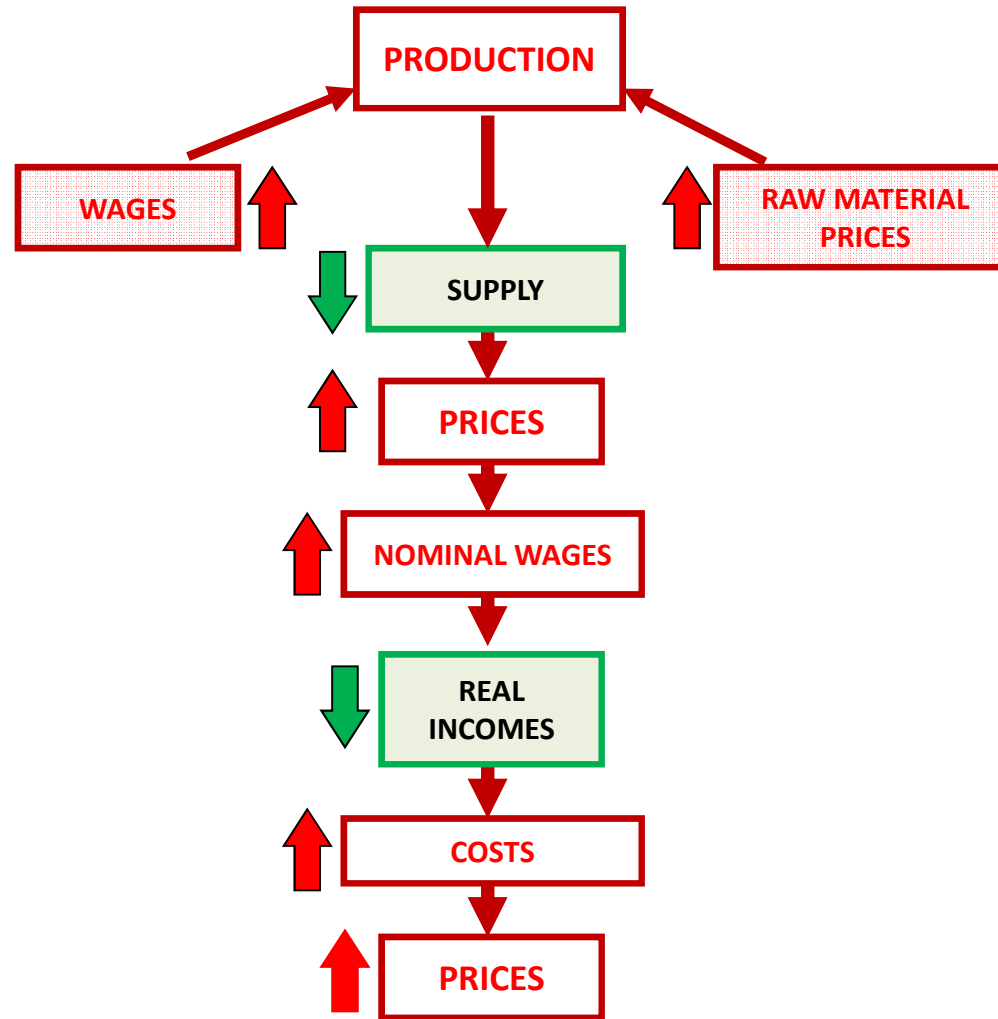
- ❖ Introduction
- ❖ Cost-push inflation
- ❖ Methods of inflation treatment, dezinflation
- ❖ Conclusion – summary, list of tasks for students



INVESTICE DO ROZVOJE VZDĚLÁVÁNÍ



Cost-push inflation

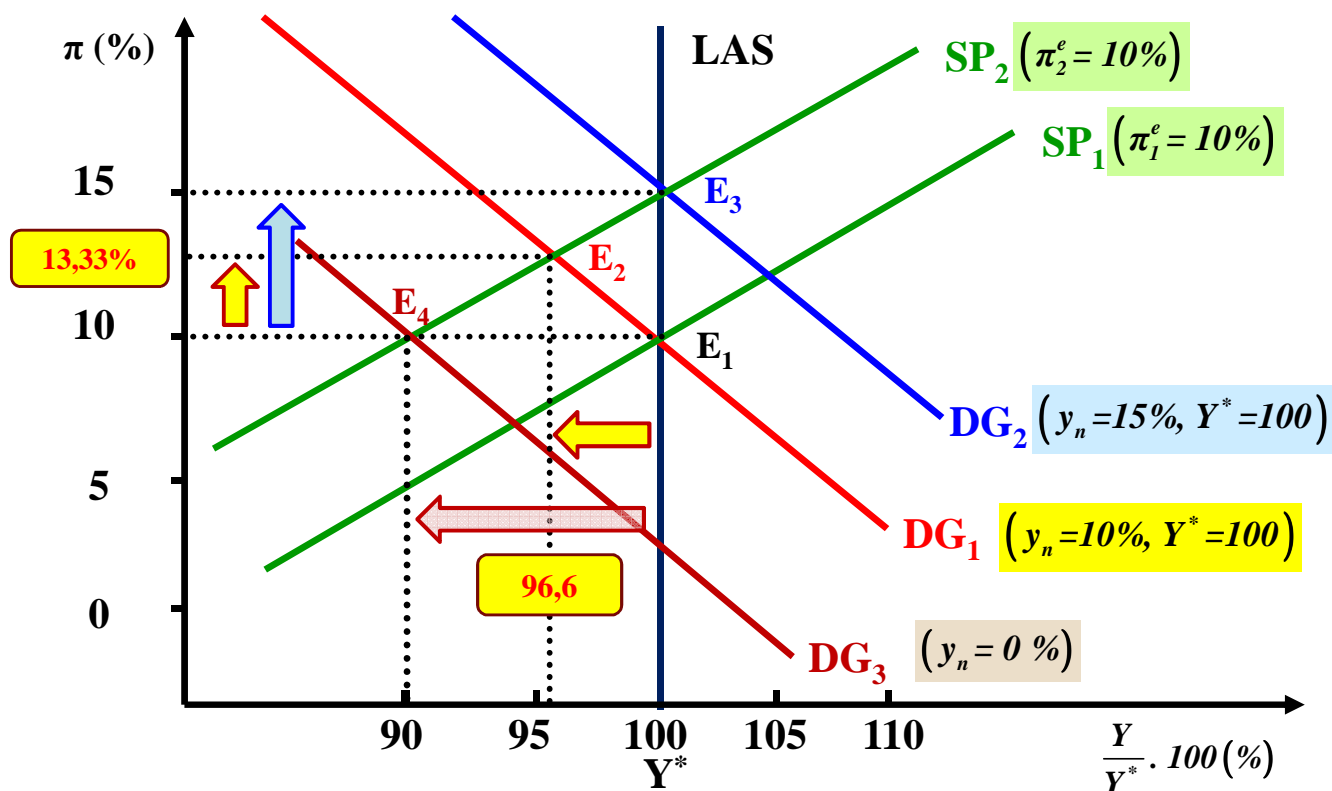


Negative supply shocks, cost-push inflation and output rate

Neutral policy in response to adverse supply shock keeps the growth rate of nominal output unchanged.

Accommodative policy eliminates the influence of negative supply shock decline in production and unemployment.

Suppressive policy leads to complete suppression of the adverse effect of the inflation shock, i.e. the inflation rate remains at the starting position of the economy.

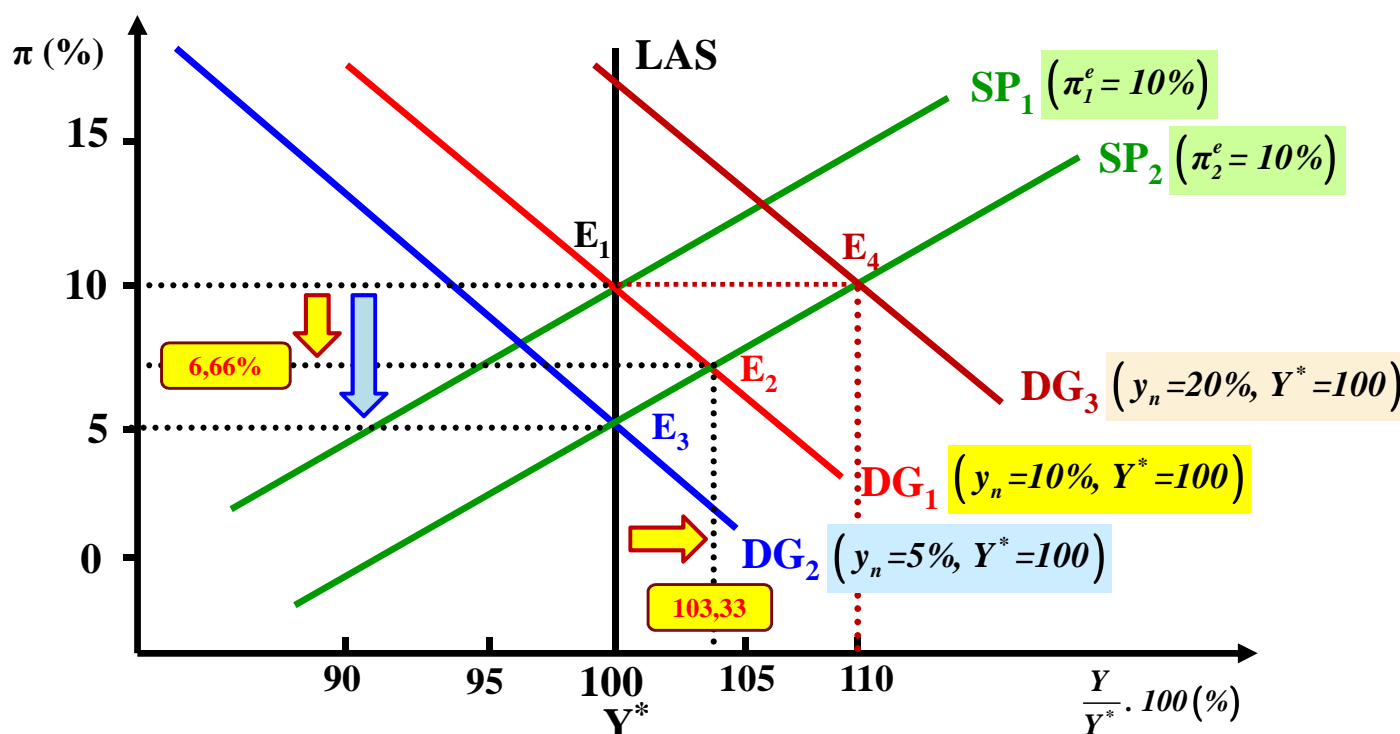


Positive supply shock, inflation rate and output growth rate

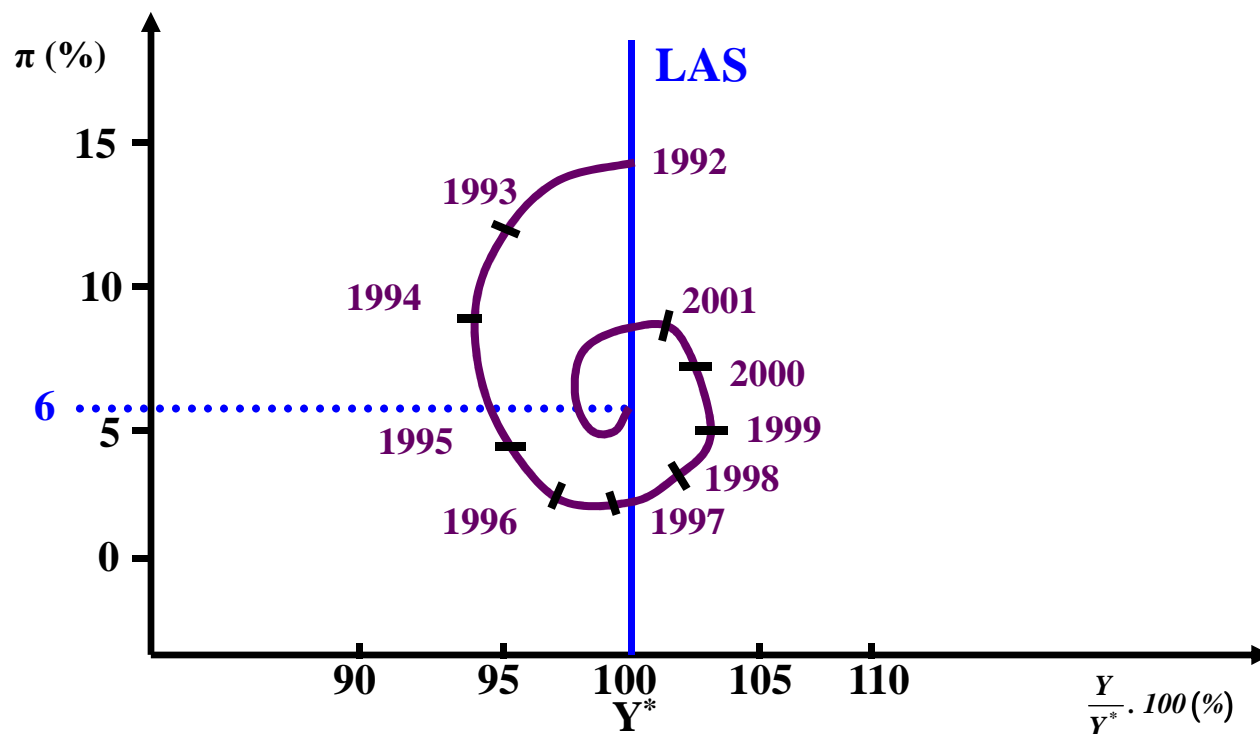
Neutral policy: AD growth rate does not change, a positive supply shock will reduce inflation and increase the output growth rate

Accommodative policy: AD growth rate adjusts to the new (lower) rate of inflation.

Suppressive policy: AD growth rate must increase to maintain the previous price level.



❖ „Cold turkey“ method



Disinflation has resulted in a rapid decline in inflation.
The cost of this treatment is a significant decline in the actual product below its potential level, causing great loss of production and high levels of unemployment.
Recession is therefore deeper, shorter.

Methods of inflation treatment

Comparison of cold turkey and gradual method

Effects	Gradual method		„Cold turkey“ method	
Decrease in inflation rate	mild	long run	significant	short run
Decrease in production	mild	long run	significant	short run
Decrease in AD growth rate	mild	long run	significant	short run

Methods of inflation treatment, dezinflation

Cost-push inflation treatment

This kind of treatment requires:

- ✓ *weaken, respectively eliminate the causes of negative supply shocks;*
- ✓ *and seek (by the Government) on the formation and implementation of positive supply shocks.*

❖ Income policy

- ✓ *Wage and price control*

a) wage freezing

b) negotiations with trade unions

c) decrease in corporate taxes, firms involving

Experience with prices and wages control is not positive. Freezing of prices and wages excludes the market economy mechanism of resource allocation: changes in relative prices are a key mechanism for effective resource allocation.

References

1. MACH, M. Macroeconomics II for Engineering (Master) study, 1st and 2nd part. Slany: Melandrium 2001. ISBN 80-86175-18-9.
2. ŠTANCL, et al. Fundamentals of the theory of military-economic analysis. 1st ed. Brno: Monika Promotion, 2012. ISBN: 978-80-905384-0-5.
3. MAITAH, M. Macroeconomics in practice. 1st ed. Praha: Wolters Kluwer CR, 2010. ISBN 978-80-7375-560-1
4. WAWROSZ, P., HEISSLER, H., MACH, P. Facts in macroeconomics - professional texts, media reflection, practical analysis. Prague: Wolters Kluwer ČR, 2012. ISBN 978-80-7275-848-0.
5. OLEJNÍČEK, A. et al. Economic management in the ACR. 1st ed. Uherské Hradiště: LV. Print, 2012. ISBN 978-80-260-3277-9.
6. ROMER, D. Advanced Macroeconomics. 3rd edition. New York: McGraw-Hill/Irwin, 2006. 678 p. ISBN 978-0-07-287730-4.



INVESTICE DO ROZVOJE VZDĚLÁVÁNÍ



List of tasks for students

Exercise „**Cost-push inflation. Methods of reducing the inflation**“

1. Explain the causes of cost-push inflation, the nature of the negative supply shocks and discuss the impact of inflation on real production supplied.
2. Analyze the different types of macroeconomic policy reacting to negative supply shocks.
3. Explain positive supply shocks and their impact on inflation and the growth rate of production.
4. Analyze methods of inflation treatment, their pros and cons.



INVESTICE DO ROZVOJE VZDĚLÁVÁNÍ

