

CPI = 200CPI = 2102009 → 2019

210 - 200 $--- \times 100 = 5\%$ Inflation = 200

Suppose you lend \$100,000 (one full basket) at zero interest in 2009 to be repaid in 2019

Loan = 100,000

The borrower returns = 100,000





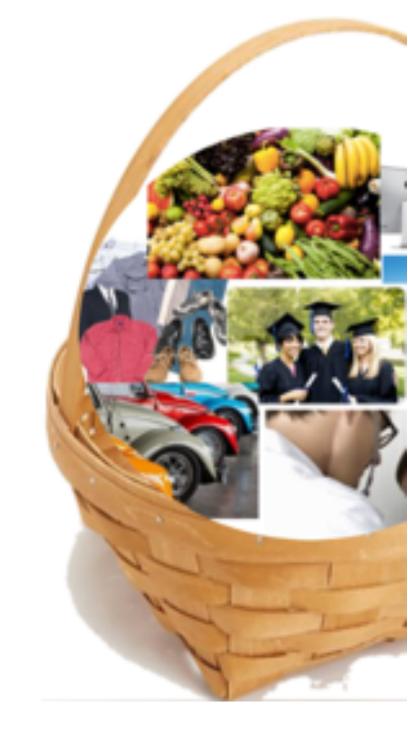
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5% inflation means that the
basket in 2019 costs 5% more:
$100,000(1.05) = $105,000
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\$105,000

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$100,000 does not buy a
full basket. It only buys:
(100,000/105,000)x100 ~
```

95% of the basket ...

The borrower returns less than what he borrowed



Lenders must protect from inflation by charging interest

95% of the basket

CPI = 200

2009

Inflation =
$$\frac{210 - 200}{200} \times 100 = 5\%$$

Lenders must protect from inflation by charging

