



**Today
Lender lends
\$1,000**

**Borrower
must pay
back \$1,000**

CPI = 1000

CPI = 105

**Lender needs
\$1,050 to buy a
full basket**



Full Basket

Lender must protect for Inflation!

Cost = \$1,000

Cost = \$1,050

Tonorrow



Full Basket

**Borrower
pays back
only \$1,000**

**Borrower
pays back
only 95% of
what s/he
borrowed**

95%
Basket



Borrower **wins**, **lender** **loses**

Lender must protect for Inflation!

CPI = 100
Today

CPI = 105
Tomorrow

Borrower **wins**, lender loses
full basket



Cost = \$1,000

Borrower
pays back
only 95% of
what s/he
borrowed



Cost = \$1,050

**To protect from inflation, lender
must charge **interest****