

1

4

CPI = 210

2024



CPI = ?

2025

You lend \$10,000 (one full basket) at 7% interest in 2024 to be repaid in 2025

Loan = 10,000

The borrower returns $= 10,000(1.07) = 10,700$



\$10,000

Full Basket




Full Basket

5% inflation means that the basket in 2025 costs 5% more:

$$\$10,000(1.05) = \$10,500$$

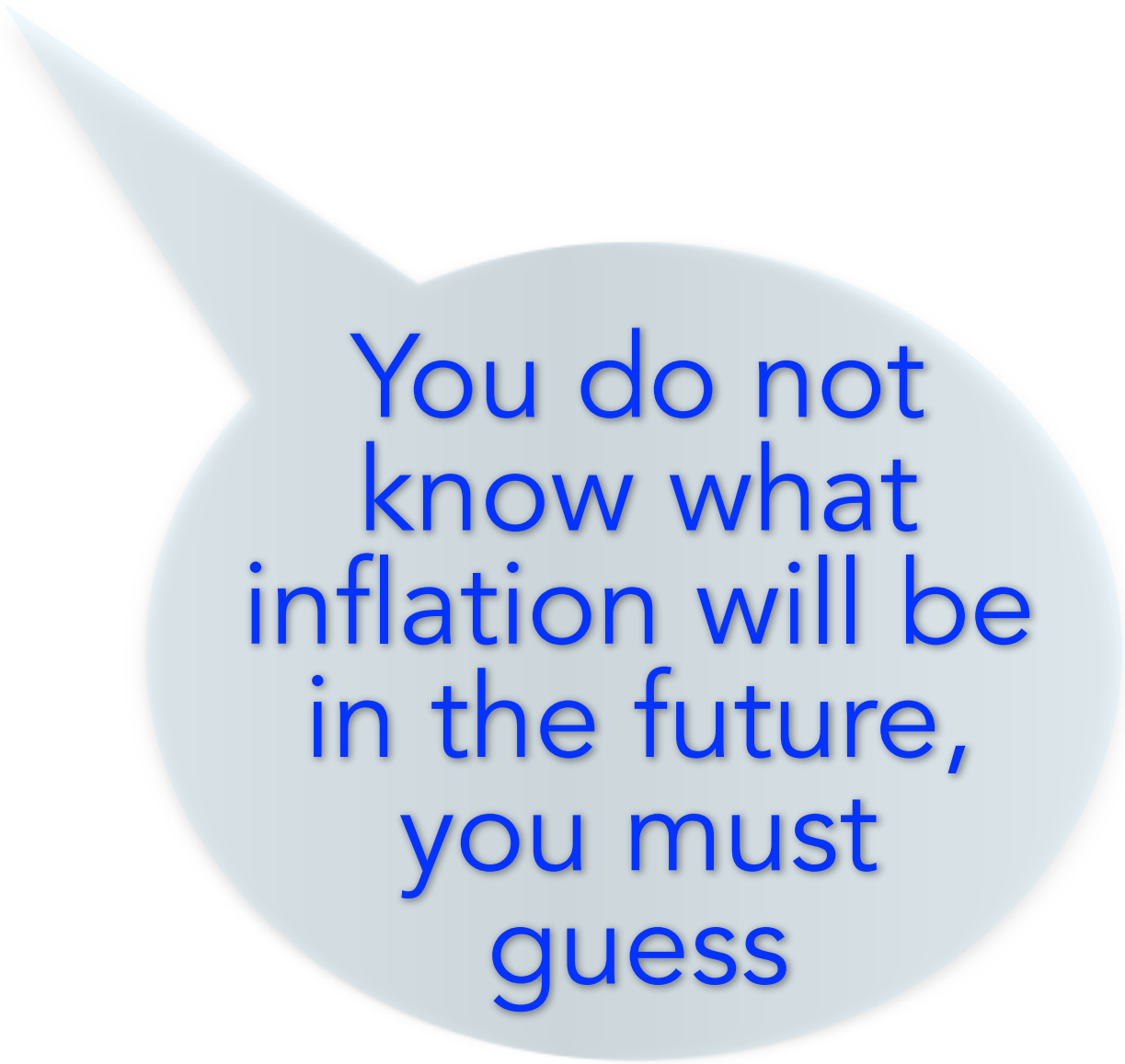
\$10,500

\$10,700 buys a full
basket with \$200 extra



The borrower returns
what s/he borrowed +
\$200 interest

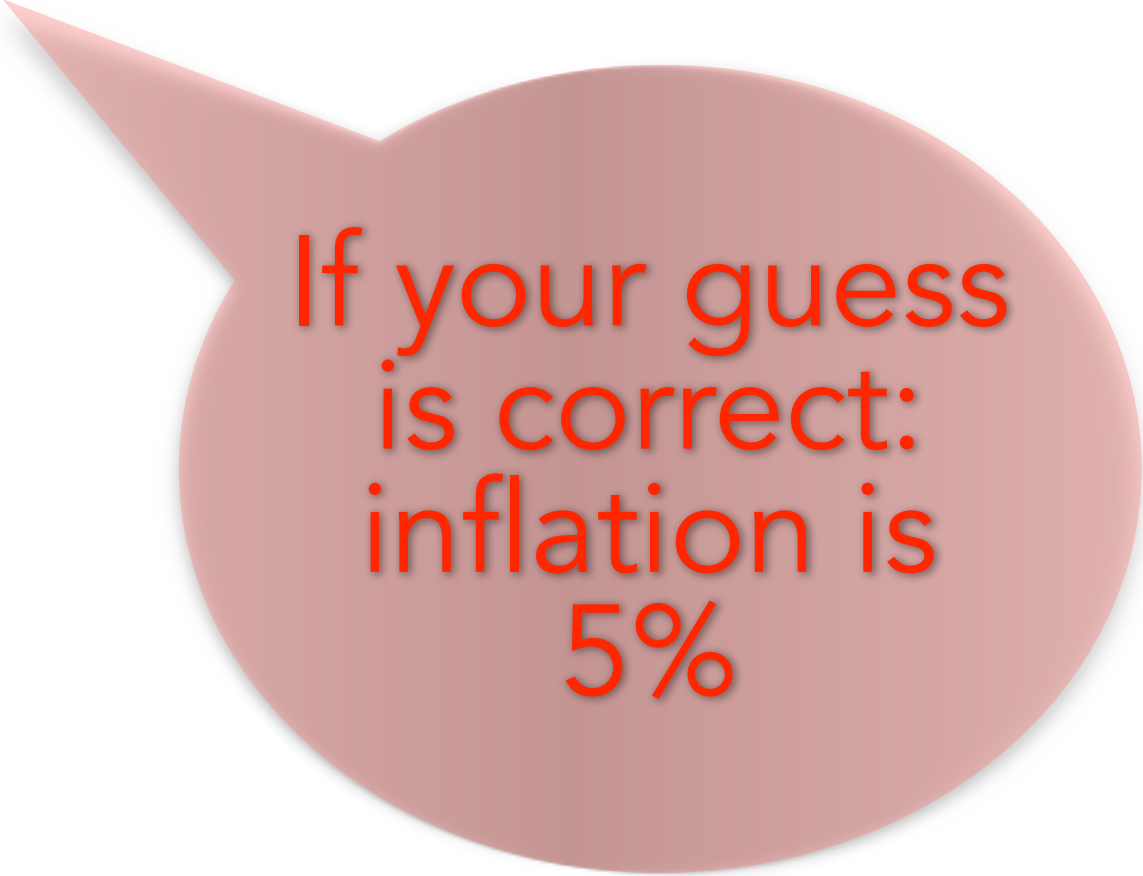
If lenders guess inflation correctly they are not hurt
by inflation



You do not
know what
inflation will be
in the future,
you must
guess



**You guess
Inflation will
be 5%**



If your guess
is correct:
inflation is
5%

CPI = 210

2024



CPI = ?

2025

If lenders guess inflation correctly they are not hurt by inflation



The borrower returns
what s/he borrowed +
\$200 interest

\$10,500



You lend \$10,000 (one full basket) at 7% interest in 2024 to be repaid in 2025

