

Labor Contract: "Employer will increase workers' salaries **by** CPI Inflation"



Employer

To avoid a drop in **real** salary, the **nominal** salary
must increase by inflation



Employee

Nominal Salaries remain
the same

If prices drop with the same
nominal salary, workers get an
increase in their **Real** Salary



The CPI
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Employee

We **do not** calculate the CPI correctly: **New Goods Bias**