1 Gallon of Gasoline

1 Bag of Apples

$$\text{Price}_{\text{gas}} = \text{Price}_{\text{apples}} = \$2$$


$1

$P_{gas} = 3\ P_{apples} = 1$

Prices Change


$2


$2


$3

1 Gallon of Gasoline

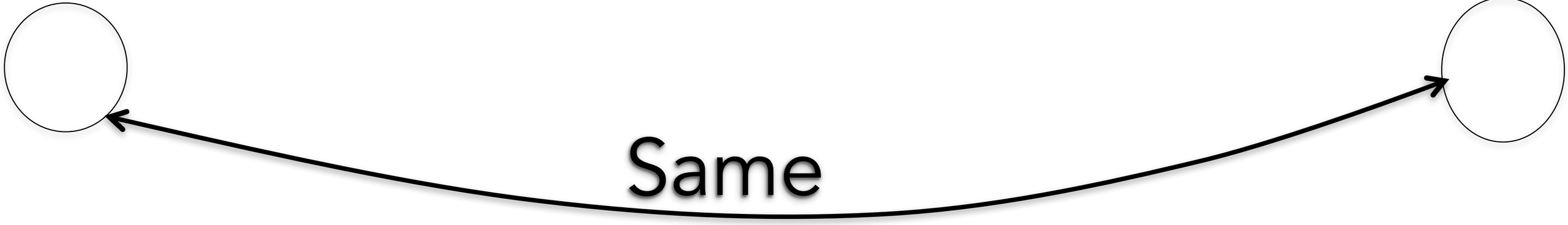
1 Bag of Apples

Cost of Basket

(1x$2)+(1x$2)= $4

Cost of Basket

(1x$3)+(1x$1)= $4


Same

Zero Inflation

1 gallon of gas costs now 3 bags of apples

Relative Prices changed:

Mistake # 2: Confusing Inflation with changes in Relative Prices

The apple farmer blames inflation but his loss is due to a change in relative prices

Mistake # 2: Confusing Inflation with changes in Relative Prices

$Price_{gas} = Price_{apples} = \$2$

1 Gallon of Gasoline — 1 Bag of Apples

The apple farmer blames inflation but his loss is due to a change in relative prices

$P_{gas} = 3\ P_{apples} = 1$

1 Gallon of Gasoline — 1 Bag of Apples

Zero Inflation

Relative Prices changed:

1 gallon of gas costs now 3 bags of apples