

3

5

You lend \$100,000 at 9% Nominal interest in 2024 to be repaid in 2025

CPI = 210

2024

You guess
Inflation will
be 5%

CPI = ?

2025

You earn

$$\text{Interest Income} = 100,000 \times 0.09 = \$9,000$$

Tax on interest income is 25%



Tax you owe

$$\$9,000 \times 0.25 = 2,250$$

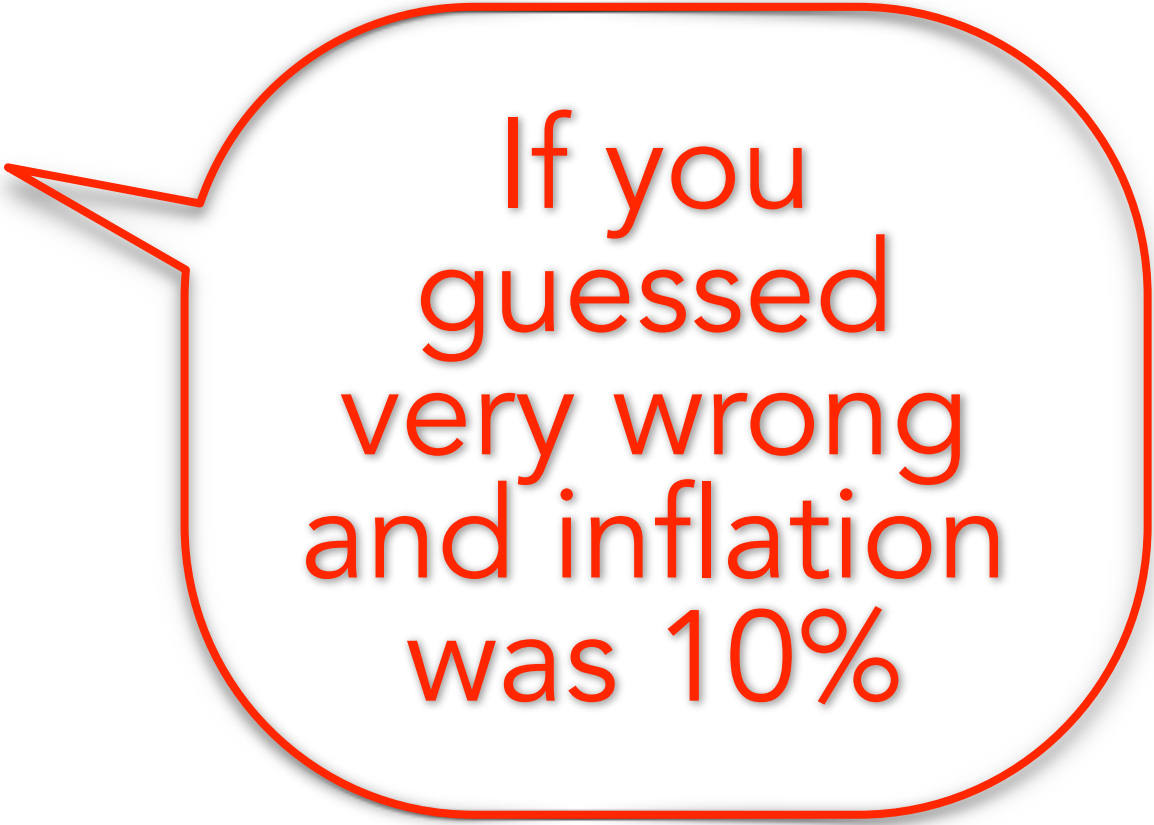


You earn

$$\text{Real Interest rate} = 9\% - 10\% = -1\%$$

$$\text{Real Interest Income} = 100,000 \times (-0.01) = -1,000$$

Even though in **Real** terms you incurred a **\$1,000**
loss the government still makes you pay **\$2,250!**



If you
guessed
very wrong
and inflation
was 10%

Inflation imposes an **unfair** tax on Interest Income

CPI = 210
2024



CPI = ?
2025

If you
guessed
very wrong
and inflation
was 10%

Inflation imposes an **unfair** tax on Interest Income

You earn

Interest Income = $100,000 \times 0.09 = \$9,000$

Tax on interest income is **25%**

Tax you owe

$\$9,000 \times 0.25 = 2,250$

You earn

Real Interest rate = $9\% - 10\% = -1\%$

Real Interest Income = $100,000 \times (-0.01) = -1,000$

Even though in **Real** terms you incurred a **\$1,000 loss** the government still makes you pay **\$2,250!**

Capital Gains