

Lesson 1: Inflation

Student Guide Pages: 71-72

Lesson Objectives: By the end of this lesson, your students should be able to:

- Explain what inflation is
- Explain why not taking any risk is, in fact, a risk

Lesson Summary:

Inflation is a rise in the cost of goods and services. As labor and raw materials costs go up, stuff becomes more expensive, and your dollars are worth less every year. This is inflation.

Deflation is the opposite. It happens when prices drop, typically because there is a drop in demand. No one wants a horse and buggy anymore! Sometimes it is because the price to produce the product drops. Computers are a great example of a product that has enjoyed deflation.

If you are only in super-safe investments, you are losing money to inflation. Not taking a risk is actually a risk. At least some of our investments need to outpace the inflation rate.

Review Questions:

- The lesson talked about net return. What does that mean?

Answer: Remember, we invest to get a return on our money. A *net return* factors in anything that eats away at that return, namely inflation. If we earned 10 percent last year but inflation was 4 percent, our net return is 6 percent.

Homework Assignment:

Tell your students to research how the inflation rate is calculated every year, then discuss it as a class.

Class Activity:

Discuss, as a class, how the inflation rate is calculated.

Answer: The Bureau of Labor Statistics (BLS) calculates the inflation rate by monitoring the published prices of over 80,000 items, divided into 200 different groups. These are referred to as the *market basket*.

Basically, the BLS watches the change in price for all the items in the basket and averages those changes into one number, the *consumer price index* (CPI). The CPI is typically used to help inflation rate calculations.

Believe it or not, there are many ways to calculate an inflation rate. Another is the *cost-of-living index* (CLI), which includes factors like cuts in government programs or increases in taxes.

Additional Information:

www.bls.gov: The Bureau of Labor Statistics calculates the inflation rate.

Fun Facts:

Share these facts with your students regarding inflation to hammer home the power of inflation concept:

- In 1980, a new house cost \$68,714. In 1989, it was \$120,000.
- In 1980, the average income per year was \$19,170. By 1989, it was \$27,210.
- In 1980, a gallon of gas was \$1.19. By 1989, it dropped to 97 cents. This is a rare example of deflation, prices going down. Prices are temporary, because we all know gas is certainly higher now!
- In 1980, a new car was \$7,210. In 1989, it was \$15,400.

Notes: _____

