Name ______________________ Date ____________

Flocabulary

What Is Inflation? - Answer Key

Use the text to answer each question below.

1. To track the impact of inflation on consumers, government agencies regularly conduct surveys of households to learn how much people are spending on different things. The goods and services included in these surveys are collectively referred to as a “basket of goods.” If you take the cost of this basket of goods and compare it to that of a designated reference year, you get the consumer price index (CPI). The percentage change between the two figures represents the amount of inflation during that time period. By measuring the price of a predetermined and unchanging selection of items like a basket of goods, economists can more accurately assess living costs and track their fluctuations over time. The basket of goods approach also reflects the relationships between different parts of the economy. Rising fuel prices, for example, may affect your grocery bill because producers are forced to pay more to ship their products. Regulators and lawmakers often consider these connections in order to predict how policy changes in one industry may impact others.

The government monitors inflation by {}.

✔ **A.** surveying households about their living costs

The text states, “To track the impact of inflation on consumers, government agencies regularly conduct surveys of households to learn how much people are spending on different things.”

B. sending a free basket of goods to every household

C. tracking the cost of a different set of items each month

D. focusing on only one economic sector at a time

2. Between January 2020 and June 2024, consumer prices in the US rose by about 21%. This is due in large part to the economic changes brought about by the COVID-19 pandemic. Supply chain disruptions resulted in shortages of food, fuel, medicine, and other goods, leading producers to raise prices. Millions of people lost their jobs, and afterward, some opted not to return to the labor force. Employers across industries were forced to raise wages in order to meet their hiring goals. Many hiked their prices in response. The federal government also spent billions of dollars providing business loans and direct payments to lower-income workers. Though these measures helped prevent an economic collapse, they dramatically increased the amount of money in circulation, thereby exacerbating inflation and lowering consumer purchasing power. As of 2024, inflation has returned to a normal rate of between 2% and 3% annually. But studies show that many Americans still feel living costs are too high. Experts say this may be because prices remain much higher than they were before the pandemic, even though inflation has subsided. Uncertainty about the future of the job market and a lack of affordable housing may also be contributing to people’s negative perceptions of the economy.

Which of the following contributed to inflation during the COVID-19 pandemic?

A. Staffing shortages

B. Supply chain disruptions

C. Federal monetary policy

✔ **D.** All of the above

The text states, “Supply chain disruptions resulted in shortages... leading producers to raise prices.” Additionally, “Employers across industries were forced to raise wages in order to meet their hiring goals,” and “Many hiked their prices in response.” Finally, “[Government policies] dramatically increased the amount of money in circulation, thereby exacerbating inflation.”

3. Policymakers can address high inflation in two key ways. The first is through monetary policy, or actions taken by a government's central bank. These policies are contractionary, meaning they're intended to reduce the money supply in order to stabilize the value of a currency. During periods of rapid inflation, the central bank of the United States, known as the Federal Reserve, may opt to raise interest rates. This makes it more expensive for consumers and businesses to borrow money from banks. With fewer people taking out loans and using credit, demand for goods and services may decrease, resulting in lower prices. The Federal Reserve can also require banks to have more cash on hand at a given time. This inhibits their ability to offer loans, thereby decreasing the amount of money in circulation. Another way that policymakers can curb inflation is through fiscal policy: a government's approach to taxation and spending. Tax hikes reduce the money supply by lowering consumer spending. They may also dissuade individuals and businesses from making speculative investments, which can lower the value of assets like property. Governments can also reduce the amount of money in circulation by temporarily limiting their own spending on things like infrastructure and welfare programs.

Which of the following is an example of monetary policy?

A. A legislature raising taxes

✔ **B.** A central bank raising interest rates

The text states that monetary policy is "actions taken by a government's central bank." For example, "During periods of rapid inflation, the central bank of the United States, known as the Federal Reserve, may opt to raise interest rates."

C. A legislature lowering government spending

D. A president promising to invest in infrastructure