



INFLATION

What is stagflation and why do policymakers worry about it?

Stagflation

Stagflation is the combination of economic **stagnation**—higher unemployment and slowing economic growth—and rising **inflation** happening at the same time.



It's an unusual pattern of economic conditions because inflation typically increases in times of strong, not weak, economic growth.

Stagflation can result when a severe negative shock hits the “supply” side of the economy, sharply increasing the price or reducing the availability of a crucial product. It's rare. The last major case in the United States occurred in the mid-1970s, when global crude oil prices surged, triggering widespread rises in other prices and fueling inflation of more than 12 percent and unemployment that peaked at 9 percent.

If it's rare, why do economists and monetary policymakers worry so much about it?

Because stagflation is hard to combat with the usual policy tools.



Federal Reserve policymakers typically address slower economic growth or higher unemployment by cutting interest rates.

But cutting interest rates can lead to higher inflation.

On the other hand, the Fed typically responds to higher inflation by raising interest rates.

But raising interest rates can slow economic growth and increase unemployment.

The Fed pays close attention to economic data and carefully weighs risks to the outlook for inflation and employment when setting interest rates in order to promote our two goals, stable prices and maximum employment.

