

*Bill Watkins*

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Most people are concerned about potential inflation, but deflation is the immediate worry. It is easy to see why the concern for inflation. Big deficits and big increases in the monetary base usually lead to inflation.

However, inflation is not inevitable. For inflation to occur, increases in the monetary base have to be translated to an increase in money supply. This is the money multiplier that we teach in elementary macro-economics, and it depends on bank lending, something that is just not happening. Even if the money supply increases, velocity declines could offset the inflationary impacts.

We are seeing an alarming increase in deflation around the world. The BBC reported today that Japanese prices have fallen 8.5 percent in the past year. Prices have also been falling in Germany, Spain, Britain, Ireland, and Switzerland.

It is virtually impossible to imagine a recovery if the United States slips into deflation. So far, we've had small increases in prices. Let's hope that continues.