

Deflation

Deflation is a general, economy-wide, fall in prices. Deflation is usually seen as bad and dangerous because once deflation rears its ugly head, it can become self-perpetuating. Debts are usually not indexed to deflation. Therefore, once deflation sets in, debts in real terms go up. This has a chilling effect on aggregate demand, which results in even more deflation.

Deflation is sometimes confused with disinflation. The two are not the same. Deflation is a general fall in prices. Disinflation is simply a fall in *inflation*. Disinflation is a slowing rate of inflation; it is not necessarily a fall in prices.