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What are deflation and reflation?

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WHAT DOES IT MEAN?

Deflation is negative inflation, in that the general price level is on a decline. Put simply, it means things keep getting cheaper.

Reflation, on the other hand, means a stop or a reverse of a deflationary situation. In other words, it means a situation where prices stop falling and may start to increase slightly.

WHY IS IT IMPORTANT?

Deflation may not be good news. In a deflationary environment, most people will postpone their purchasing decision in the hope that the items they intend to buy will be cheaper in the future. When fewer people purchase goods and services, the businesses which produce them will perform poorly. They may go out of business or cut cost by reducing manpower, which means many people will lose their jobs.

People who lost their jobs will cut spending and the vicious circle continues. As a result, the economy may slow down or even contract.

Deflation will also make past borrowings difficult to repay. Imagine that you borrow $300,000 to buy an HDB flat.

When prices fall in a deflationary environment, the price of your flat will also fall.

However, your debt of $300,000 does not go down with the price of your flat. Hence, central banks of countries that suffer from deflation will have to implement economic strategies to try to reflate the economy.

IF YOU WANT TO USE THE TERM, JUST SAY:

After a long period of deflation, the central bank has finally succeeded in reflating the economy.

• The writer is an associate professor of the department of finance at NUS Business School. The opinions expressed are those of the writer and do not represent the views and opinions of NUS.