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THE IMPACT OF INFLATION ON THE PURCHASING POWER OF INDONESIAN SOCIETY

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Abstract

Inflation is one of the important economic indicators that can affect the social and economic conditions of society. A general and continuous increase in the prices of goods and services reduces the real value of money and consequently decreases people's ability to obtain goods and services. This study aims to analyze the effect of inflation on the purchasing power of Indonesian society, explain the mechanism linking changes in the price level to consumption capacity, and identify factors that may strengthen or reduce the impact of inflation on purchasing power. The study uses a descriptive qualitative method with a literature-study approach. Data and information are obtained from relevant sources concerning inflation, household income, household consumption, prices of goods and services, and government and Bank Indonesia policies. The review indicates that inflation generally has a negative relationship with purchasing power. When prices increase while nominal income does not rise proportionally, real income declines and households tend to reduce the quantity or quality of goods and services consumed. However, the impact of inflation differs across groups and is influenced by income level, consumption patterns, type of employment, wage changes, savings, debt, and the types of goods experiencing price increases. Therefore, stable inflation control and policies that improve household income are important to maintain the welfare of Indonesian society.

Keywords: Inflation, Purchasing Power, Real Income, Household Consumption, Price Stability

INTRODUCTION

The economy of a country is not free from various problems that can affect the level of community welfare. One of the economic issues that often attracts the government's attention is inflation. Inflation is a condition when there is a general increase in the prices of goods and services that continues over a certain period. Inflation is an economic phenomenon that has wide-ranging impacts. Price increases not only affect the production costs of companies but also the ability of the community to meet their living needs. When the prices of basic necessities, transportation, education, health, energy, and various other needs rise, the community requires greater expenditure to obtain the same goods and services.

The problem becomes more serious when price increases are not accompanied by a balanced increase in income. For example, a person who previously earned Rp3,000,000 per month may have been able to meet certain needs with that income. However, if the prices of goods and services increase while their income remains the same, the quantity of goods and services they can purchase will decrease. The condition indicates a decrease in real income. Nominal income is the amount of money received by an

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individual, while real income reflects the purchasing power of that income in buying goods and services. Thus, people may experience a decline in purchasing power even if their nominal income remains unchanged.

The purchasing power of the community is an important component in the economy because household consumption plays a significant role in economic activity. If the purchasing power of the community decreases significantly, the demand for goods and services may slow down. This condition can then affect the turnover of business actors, company production, job opportunities, and economic growth.

Indonesia, as a country with a large population, faces challenges in maintaining price stability while also improving the welfare of its people. Excessively high inflation can put pressure on low-income groups because a large portion of their income is used to meet basic needs. On the other hand, controlled and stable inflation can create a healthier economic environment. Price stability provides certainty to the community and business actors in carrying out consumption, investment, and production activities.

Therefore, the study of the impact of inflation on the purchasing power of the Indonesian people is important to understand how changes in price levels can affect the welfare of society and how economic policies can be used to mitigate the negative impacts of inflation.

LITERATURE REVIEW

Inflation

Inflation is a condition when there is a general and sustained increase in the prices of goods and services. An increase in the price of one or two types of goods alone cannot necessarily be called inflation if that increase does not have a broad impact on the overall price level.

Inflation causes the real value of money to decrease. With the same amount of money, people can obtain fewer goods and services compared to before.Inflation is usually measured using changes in price indices, one of which is the Consumer Price Index (CPI). The CPI reflects changes in the prices of goods and services consumed by households. In simple terms, the inflation rate can be calculated using the formula:

$$Inflation = [(CPI\ current\ period - CPI\ previous\ period) / CPI\ previous\ period] \times 100\%$$

Types of inflation

Inflation can be classified based on its severity and causes. Based on the severity:

1. Light inflation, which is inflation with a relatively low rate of price increase and is still manageable.
2. Moderate inflation, which is a price increase that begins to exert pressure on economic activity and the purchasing power of the public.

3. Severe inflation, which causes major disruptions to the economy.
4. Hyperinflation, which is a very high and uncontrollable price increase.

Based on the causes:

1. Demand-Pull Inflation
   Inflation that occurs due to an increase in aggregate demand faster than the economy's ability to provide goods and services.
2. Cost-Push Inflation
   Inflation that occurs due to rising production costs, such as the prices of raw materials, energy, transportation, and wages.
3. Imported Inflation
   Inflation influenced by the rise in prices of goods from abroad, changes in exchange rates, or increasing international commodity prices.

Purchasing power

Purchasing power is the ability of the public to acquire goods and services using their income or economic resources. Purchasing power is closely related to real income. The higher the real income, generally the greater a person's ability to meet needs. Conversely, if the prices of goods and services rise faster than income, the purchasing power of the public will decline.

Nominal income and ral income

Nominal income is the amount of money received by an individual over a certain period. Meanwhile, real income indicates the purchasing power of that income to buy goods and services. In simple terms:

$$\text{Real Income} \approx \text{Nominal Income} / \text{Price Index}$$

For illustration, if a person's income increases by 5%, but the price level increases by 8%, then the increase in income may not necessarily improve welfare. In real terms, the ability to purchase goods and services may actually decrease.

Inflatin and PURCHASING POWER

The relationship between inflation and purchasing power can be explained through the concept of real income. When inflation rises:

Prices of goods and services rise → cost of living increases → real income decreases → consumption ability decreases → purchasing power weakens.

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However, this relationship is not always the same for all segments of society. Those whose income increases faster than inflation may still be able to maintain or increase consumption. Conversely, groups whose income remains the same or only increases slightly will be more vulnerable to a decrease in purchasing power.

METHOD

Type of research

This research uses a qualitative descriptive method with a literature study approach. This approach is used to analyze the relationship between inflation and the purchasing power of the community based on economic theory and relevant research and publications.

Data sources

The data used in this research is secondary data obtained from various sources, including:

1. Central Statistics Agency (BPS).
2. Bank Indonesia.
3. Ministry of Finance of the Republic of Indonesia.
4. Ministry of National Development Planning/Bappenas.
5. Economic books and scientific journals.
6. Relevant research publications.

Data collection techniques

Data collection was conducted through documentation studies and literature studies by means of:

1. Identifying theories regarding inflation.
2. Examining the concepts of purchasing power and real income.
3. Analyzing data on price and consumption developments.
4. Comparing results of previous research.
5. Connecting theory with the economic conditions of Indonesia.

Data analysis techniques

Data is analyzed descriptively through several stages:

1. Collecting relevant information.
2. Grouping information by theme.
3. Identifying the relationship between inflation and purchasing power.
4. Analyzing the impact of inflation on consumer consumption.

5. Drawing conclusions based on the study results.

RESULTS AND DISCUSSION

Inflation Conditions in Indonesia

Inflation is one of the economic indicators that always receives attention because it relates to the cost of living for the community. Changes in inflation in Indonesia can be influenced by various factors, both domestic and international. These factors include food prices, energy prices, transportation costs, the exchange rate of the rupiah, production conditions, distribution of goods, public demand, and changes in global commodity prices. The food component plays an important role because food is a primary need for households. Increases in the prices of rice, cooking oil, eggs, meat, vegetables, and other commodities can exert significant pressure, especially on low-income households. In addition to food, energy prices can also have a cascading effect. Increases in fuel or energy prices can raise transportation and production costs. Business actors may then pass on some of these cost increases to the prices of goods and services. Thus, inflation is not just a matter of rising prices of a single item, but can become a phenomenon that affects various sectors of the economy.

The Impact f Inflation on the Purchasing Power of Society

In general, inflation has a negative impact on purchasing power if the increase in prices is higher than the increase in people's income. As a simple example:

A worker has an income of Rp4,000,000 per month. If the prices of goods and services increase by an average of 10%, while the worker's income remains at Rp4,000,000, then the worker's real ability to purchase goods and services decreases.

This means that the Rp4,000,000 that could previously be used to meet certain needs no longer has the same purchasing power after prices have increased. This condition can be illustrated as follows:

Inflation increases

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Prices of goods and services increase

↓

Household expenditures increase

↓

Real income decreases

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↓

Purchasing ability decreases

↓

Purchasing power of society decreases

The Impact of Inflation on Consumption Patterns

A decrease in purchasing power can lead to changes in the consumption behavior of society. Some changes that may occur include:

1. Reducing the consumption of non-essential goods
   People tend to reduce purchases of items that are not primary needs, such as entertainment, recreation, electronics, clothing, or certain consumer products.
2. Shifting choices to cheaper products
   People can switch brands or types of products to alternatives that are priced lower.
3. Reducing the quantity of purchases
   If someone previously bought five units of a certain item, a price increase may lead them to buy only three or four units.
4. Reducing savings
   Some households may use savings to maintain consumption when income cannot keep up with rising prices.
5. Changing spending priorities
   Spending on basic needs, education, health, transportation, and housing can be prioritized over secondary or tertiary needs.

The Impact of Inflation on Low-Income Community Groups

Low-income community groups tend to be more vulnerable to inflation. This is because a large portion of their income is used to meet basic needs. For example, low-income households allocate most of their income to food, housing, electricity, transportation, and other basic needs. When the prices of these necessities rise, the room for adjusting expenditures becomes smaller. In contrast, high-income households generally have more options to adjust consumption and have larger financial reserves. Thus, the same inflation rate can have different impacts on different groups of society.

The Impact of Inflation on Business Actors

Inflation affects not only consumers but also business actors. When the prices of raw materials increase, the production costs for companies may also rise. To maintain profit margins, companies may raise selling prices. However, if the purchasing power of the public is declining, price increases can lead to a decrease in demand for products. Business actors then face a dilemma between:

Raising prices → margins are maintained but demand may potentially decrease. or

Maintaining prices → demand remains relatively stable but profits may decrease.

This situation shows that inflation can create a chain effect in the economy.

Inflation and Economic Growth

Low and stable inflation generally can coexist with healthy economic activity. However, excessively high inflation can disrupt economic activities because:

1. Production costs increase.
2. Business uncertainty is increasing.
3. Public purchasing power is declining.
4. Household consumption may weaken.
5. Investment may be delayed.
6. Business planning is becoming more difficult.

If public consumption experiences a significant decline, sectors that rely on domestic consumption may face pressure.

Factors Affecting Purchasing Power Besides Inflation

Inflation is not the only factor that determines the purchasing power of the public. Some other factors are:

1. Income Level

   The higher the income, the greater the ability of the public to meet their needs.
2. Wage Level

   Wage increases that are in line with or higher than inflation can help maintain purchasing power.
3. Job Opportunities

   People with stable jobs and income tend to have better consumption capabilities compared to those without stable income.
4. Prices of Basic Necessities

   Changes in food, energy, transportation, and basic needs prices significantly affect household consumption capacity.
5. Interest Rates

   Changes in interest rates can affect borrowing costs and consumption or investment decisions.
6. Government Policy

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Subsidies, social assistance, social protection programs, wage policies, and price controls can influence the purchasing power of the community.

Government Strategies to Maintain Purchasing Power

The government can use various policies to mitigate the impact of inflation on the community.

1. Maintaining Food Price Stability
   The government needs to ensure the availability and smooth distribution of food supplies.
2. Increasing Production
   Increasing agricultural productivity and other production sectors can help maintain supply.
3. Improving Distribution
   Efficient distribution can reduce price disparities between regions.
4. Social Assistance
   Social assistance can help vulnerable groups when price pressures occur.
5. Monetary Policy
   Bank Indonesia plays an important role in maintaining the stability of the rupiah and inflation through monetary policy.
6. Strengthening Employment
   Increasing job opportunities and labor productivity is important for improving community income.
7. Fiscal Policy
   The government can use fiscal policy to maintain economic stability while protecting vulnerable groups in society.

ANALYSIS

Relationship Between Inflation and Purchasing Power

The relationship between inflation and purchasing power can be explained using a simple concept:

$$\text{Purchasing Power} = \text{Nominal Income} / \text{Price Level}$$

If the price level increases while nominal income remains the same, purchasing power will decrease. Conversely, if income increases faster than the price level, purchasing power can be maintained or even increased. Example:

Initial income = Rp5,000,000 Income increase = 5% New income = Rp5,250,000. If inflation during the same period reaches 8%, the increase in income is not enough to offset the rise in prices.

In simple terms, changes in real income can be approximated by:

$$\text{Real income growth} \approx \text{nominal income growth} - \text{inflation}$$

Therefore: $5\% - 8\% = -3\%$. This means that, by approximation, the real purchasing power of income has decreased by about 3%.

Inflation Does Not Always Have the Same Impact

It is important to understand that the impact of inflation varies. For example, if food prices rise significantly, the impact will be greater for households that spend most of their income on food. Conversely, someone with a higher income and a relatively smaller proportion of food expenditure may not experience the same pressure. Therefore, inflation analysis should not only look at national inflation figures but also consider:

- Income groups;
- Regions;
- Type of work;
- Consumption pattern;
- Wage changes;
- Prices of certain commodities.

Short-Term Impact

In the short term, inflation can cause:

1. Increased costs of household necessities.
2. Decreased consumption of non-essential goods.
3. Reduced ability to save.
4. Increased pressure on low-income households.
5. Rising production costs of companies.

Long-Term Impact

If high inflation persists in the long term and is not offset by income growth, the impact can be broader. Society may experience a decline in living standards, the ability to save may decrease, household investment may decline, and economic inequality may potentially increase. Therefore, price stability is one of the important conditions for maintaining sustainable economic growth.

Efforts To Improve The Purchasing Power Of The Community

To maintain and improve the purchasing power of the Indonesian people, policies are needed that not only focus on controlling inflation but also on increasing community income. Some steps that can be taken are:

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Increasing Labor Productivity

Improving the quality of education and skills can enhance labor productivity so that the community has the opportunity to earn better income.

Creating Job Opportunities

The government needs to encourage investment and the development of productive sectors that can create job opportunities.

Maintaining the Prices of Basic Necessities

The availability of food supplies and the efficiency of distribution must be continuously strengthened.

Providing Protection to Vulnerable Groups

Social protection programs need to be accurately targeted at the communities most affected by rising prices.

Encouraging MSMEs

Micro, small, and medium enterprises play an important role in providing jobs and income for the community. Support in the form of financing, training, digitalization, market access, and mentoring can help MSMEs increase productivity.

Improving Financial Literacy

The community needs to have the ability to manage finances, create budgets, control spending, prepare emergency funds, and engage in long-term financial planning.

CONCLUSION

Based on the discussion that has been conducted, it can be concluded that inflation has a close relationship with the purchasing power of the Indonesian people. The general increase in the prices of goods and services leads to a rise in the cost of living. If the increase in nominal income is lower than the inflation rate, the real income of the community will decrease, thus reducing their ability to obtain goods and services.

The impact of inflation is most felt by low-income communities because most of their income is used to meet basic needs. The rise in prices of food, energy, transportation, and other essential needs can reduce their ability to meet other needs. Inflation can also lead to changes in consumption patterns. People tend to reduce their consumption of non-essential goods, choose cheaper products, decrease the quantity of purchases, and change their spending priorities. On the other hand, the impact of inflation on purchasing power is not uniform. The extent of the impact depends on income levels, wage growth, consumption patterns, employment conditions, savings, and changes in the prices of consumed goods.

Therefore, keeping inflation low and stable is an important part of maintaining the purchasing power of the public. However, inflation control needs to be accompanied by policies to increase income, create jobs, enhance productivity, strengthen social protection, and empower MSMEs.

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