

The Causes and Consequences of Inflation and the Role of Central Banks in Achieving Price Stability

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Introduction

The purpose of this thesis is to examine the causes of inflation and the influence of monetary policies. The study will explore the consequences of inflation, including its effects on the economy and society. Also, research will investigate how central banks manage inflation what actions and policies they use in order to manage the inflation and prevent the danger that inflation can cause.

Inflation is a critical issue that shapes the global economy, with direct impact on individuals, businesses, and governments. Often economic growth leads to moderate inflation, but both deflation and high inflation can harm the economy. Inflation has wide consequences, affecting the cost of living, income distribution, and investment decisions. On the other hand, deflation can lead to economic stagnation and increase unemployment, both of which pose long-term threats to price stability.

Therefore, it is essential to maintain healthy inflation, balancing supply and demand to help ensure price stability without negative effects on the economy.

Meanwhile, this study will draw on research, including Blanchard and Johnson (2013), 6th ed., Pearson Education, which analyzes the causes and effects of inflation, as well as the role of central banks in managing it.

Nowadays, central banks play a crucial role in controlling inflation and maintaining economic stability by special techniques, including monetary policy tools like interest rates, open market operations, and inflation targeting. By managing inflation, central banks aim to maintain stable

financial markets and decrease financial risks before it occurs, which is essential for fostering growth and enhancing public confidence in the national currency.

CONCLUSION

This study examined the effects of inflation on individuals' financial behavior and their perception of the central bank's role in maintaining price stability. Based on the responses of 105 participants, several key conclusions were reached. Almost all respondents (over 99%) noticed a significant increase in the prices of essential goods such as food, housing, and transportation, confirming that inflation directly reduces purchasing power and affects daily life. Most participants reported changing their spending habits by prioritizing necessities and reducing luxury consumption. About half of the respondents (50.5%) attributed inflation to excess demand and weak policy measures, while others mentioned rising production costs and global economic instability. This reflects a reasonable level of public awareness of the main drivers of inflation. Furthermore, 73.3% believed that an annual inflation rate between 2% and 3% supports stable economic growth—consistent with international monetary standards. The majority (79%) expressed confidence in their central bank's ability to control inflation, and more than 80% agreed that transparency and communication from monetary authorities enhance public trust. These findings underline the importance of credibility and openness in economic policy.

A smaller portion of respondents expressed uncertainty or limited confidence in the effectiveness of monetary policy, suggesting that some individuals may not fully understand how central bank measures influence inflation. This highlights the need for continued public education and outreach to improve economic awareness and strengthen trust in policy actions. Finally, inflation was found to affect not only finances but also mental and social well-being. Many participants reported stress and reduced life satisfaction as their income failed to keep pace with rising prices. Overall, the study confirms that inflation is both an economic and social challenge.

Maintaining moderate inflation, strengthening communication, and increasing public awareness are essential to achieving long-term economic and social stability.

RECOMMENDATIONS

- Central banks should continue applying transparent and data-driven monetary policies to maintain moderate inflation rates.
- Regular communication about policy goals and interest rate changes can strengthen public trust and reduce uncertainty among citizens.
- Monetary authorities are encouraged to enhance financial education programs to help individuals better understand how inflation develops and how central bank actions influence prices. Improved awareness can increase confidence in monetary measures and reduce misconceptions.
- Governments should coordinate fiscal and monetary policies more effectively to avoid contradictory actions that could intensify inflation. This includes managing public spending responsibly and limiting unnecessary deficits.
- Social protection programs should be expanded to support low- and middle-income groups most affected by rising prices, particularly in essential sectors such as food, housing, and energy.
- Public campaigns should encourage individuals to adopt responsible financial habits such as saving, budgeting, and investing in stable assets. These behaviors can help mitigate the personal effects of inflation and improve financial resilience.
- Economic policymakers should focus on achieving a sustainable balance between growth and stability by keeping inflation around the optimal rate of 2–3%. This ensures continued development without eroding purchasing power.
- Future studies are recommended to include larger and more diverse samples or to compare perceptions of inflation across different countries. Further research could, also explore the long-term social and psychological consequences of persistent inflation.