THE
News Today

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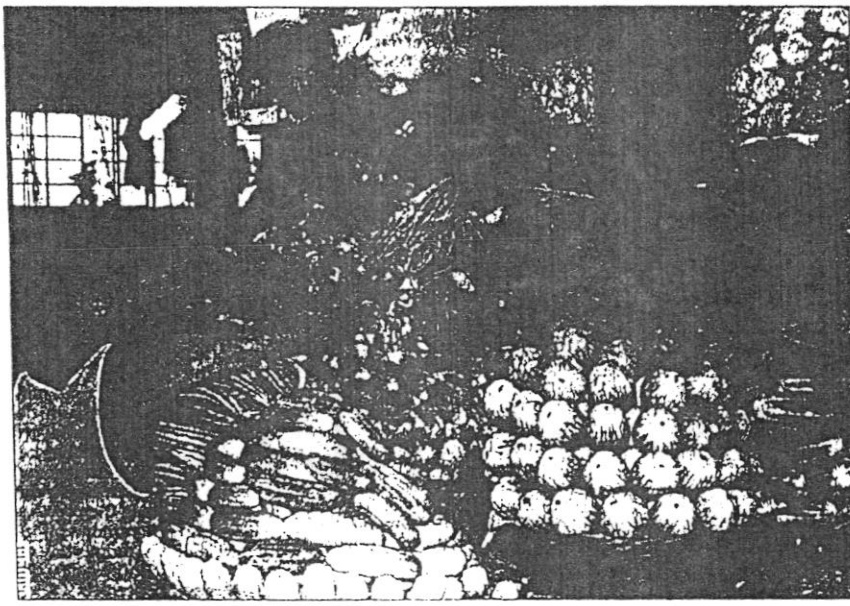
Dhaka Tuesday November 13, 2007 Kartik 29, 1414 Zil Quada 1, 1428

Fighting inflation

International inflation has had a severe impact on inflation in Bangladesh moving from a double digit- towards a galloping inflation of 20% or over, which is a stagflation,

writes **Dr M Azizur Rahman**



In recent decades, inflationary environment of Bangladesh has been characterized by price instability. Prices used to be rising slowly and predictably. However, very recently international inflation has had a severe impact on inflation in Bangladesh moving from a double digit- towards a galloping inflation of 20% or over, which is a stagflation - high level of unemployment and low level of economic growth. Analysis shows that inflation has adverse impact on the real economy including redistribution of income and wealth among different groups.

Stagflation is fairly a high rate of inflation even when we have a slow rate of economic growth, lower level of output and income, lower production of goods and services with a high unemployment and idle-capacity. Usually, stagflation occurs when we have a cost push inflation, or a higher inflation due to increase in the cost of production or import prices of goods and services including those of intermediate goods that are used in production.

Higher inflation and higher unemployment are going together, the main cause of which is the higher cost of production. Higher cost of production is attributed to higher prices of energies and oil since the U.S. invasion to Iraq four years ago. Oil price used to be $6 per barrel during 1973, which is $ 92 per barrel in this month of October/2007.

The rate of GDP growth remaining substantially too low to accept may be from 2% to 4% for the next decade from now. Due to higher price and decreased competitiveness, exports from our Apparel Sector has decreased by 24%. The foreign investment in Bangladesh has already decreased significantly for a reason of political instability. Consumers are losing their purchasing power.

The economic stage of stagflation has been complicated this year by flood, river-erosion, rainfall and drought and crop damage. The political instability has been added as one among the few significant reasons for lower economic growth. The engine of production and supply of goods and services and manufacturing business have lost its confidence in investment in the present regime for a severe move for anti-corruption. Stakeholders or investors are simply scared for being caught probably for their black money to invest. What is really happening is that attempt of anti-corruption is too quick and too hard to cure the economy, and cure is getting worse than its disease. We have to have a device to provide a better treatment not by killing the patient. Otherwise, the economy may be in more trouble. We may not be able to avoid a possibility of an economic crash. Hopefully, the Government is thinking of Truth Commission to rescue the loss and help grow the business and the economy not by killing the business. This might be a good idea.

Fighting inflation has become a priority. In order to fight the inflation the following strategies are suggested:

The usual remedy of a cost-push inflation is to control the increase of prices and income through a policy, which will control the social pressure to raise wages, and the ability of the producers and suppliers to increase prices. A market intervention to lower the pressure for wage increase and control of prices will temporarily suppress the inflation, which is also beyond our control. Because this is a world wide increase in prices due to higher prices of energies. Import prices of intermediate goods, have also increased in the exporting country. Import prices of many essential goods from foreign countries and India in particular including food and related items, fabrics and female dresses of three-pieces and saries have increased. Therefore, lowering prices are beyond our control. Suppressing the claim of wage increase would be very inhuman as the wage level is already too low for the workers to afford essential goods. Consumers have already lost their purchasing power significantly, which have greatly increased the social and political concern.

Concentration on supply-side to increase productivity may be the last hope to fight the recent inflation. Technological improvement and innovative discovery for production and supply can decrease the cost of production for a given output or can increase the output with the same or similar amount of input. All these will tend to [illegible] crease the price.

Additionally, the government would have to [illegible] dies for the produ[illegible] sential goods inc[illegible] item. We do not inc[illegible] rate since it is not [illegible] pull inflation but [illegible] crease the coverage of [illegible] ment by each and every [illegible] of taxable income to [illegible] the tax revenue [illegible] Government. We al[illegible] decrease tariff, and [illegible] import quota, if an[illegible] tial consumer go[illegible] termediate items [illegible] prices reasonab[illegible]

The other s[illegible] in this major imp[illegible] try is that our exch[illegible] too low to afford [illegible] goods and [illegible] Government should think of a fixed exchange rate at a relatively high level, which might help the consumer to afford imported goods to some extent.

As mentioned above, consumers' purchasing power has substantially decreased. Purchasing power of the consumer will have to be increased so as to enable them to buy their essential goods and services to meet their basic needs in life. Since this is more of a cost push than a demand pull inflation, we do not reduce the government expenditure to purchase of goods and services by reducing the budget deficit, money supply and hire purchase. Rather, we need to take an expansionary economic policy by increasing budget deficit or money supply or both and not increasing the tax rate, so that this policy will directly and indirectly increase the consumer's purchasing power, domestic consumption and domestic private investment. Increased burden of Government loan will be taken care of in a gradual fashion.

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