

How to fight inflation

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 decrease the price. Additionally, the government would have to give subsidies for the production of essential goods including food item, writes **Dr M Azizur Rahman**

IN THE recent past, inflationary environment of Bangladesh used to be characterised by price stability. Prices used to rise slowly and predictably. However, very recently international inflation has had a severe impact on inflation in Bangladesh, which has already reached the double digits and is now inching towards a galloping inflation of 20 per cent or over, which is 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 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 US invasion to Iraq four years ago. Oil price used to be \$6 per barrel during 1973, which is about \$100 per barrel now.

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 of being caught probably for their black money to invest. What is really happening is that the anti-corruption activism is too quick and too hard to cure the economy and the cure is getting worse than the 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 the possibility of an economic collapse.

The rate of GDP growth remaining substantially too low to accept – may be from 2 per cent to 4 per cent for the next decade from now. Due to higher price and decreased competitiveness, exports from the apparel sector have decreased 24 per cent. Foreign investment in Bangladesh has already decreased significantly because of political instability. Consumers are losing their purchasing power.

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

The usual remedy for 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 worldwide 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 saris 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. As mentioned before, consumers have already lost their purchasing power significantly, which has 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 decrease the price. Additionally, the government would have to give subsidies for the production of essential goods including food item. We do not increase the tax rate since it is not demand-pull inflation but we can increase the coverage of tax payment by each and every citizen of taxable income to maximise the tax revenue of the government. We also need to decrease tariff and increase import quota, if any, for essential consumer goods and intermediate items to keep their prices reasonably low.

The other significant reason in this major importing country is that our exchange rate is too low to afford the imported goods and services. The 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 cost-push than demand-pull inflation, we do not reduce the government expenditure to purchase 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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