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II საერთაშორისო სამეცნიერო კონფერენცია

გლობალიზაციის გამოწვევები
ეკონომიკასა და ბიზნესში

შრომების კრებული

**Ivane Javakhishvili Tbilisi State University,
Faculty of Economics and Business**

The 2nd International Scientific Conference:

**Challenges of Globalization in
Economics and Business**

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CHALLENGES OF GLOBALIZATION IN ECONOMICS AND BUSINESS

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Challenges of the Inflation Targeting in Low-Income Countries

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The inflation index fails to fully reflect the expectation of the population in low-income countries. Some of the commodity groups fail to reflect the problem of the low-income population. Under these conditions, a logical question arises concerning the kinds of problems which might occur when the main goal for a central bank's monetary policy is only to retain price stability, which is known as inflation targeting.

Keywords: inflation, inflation targeting, imflation, agflation, munflation.

A consumer basket in different countries is rather balanced and covers all of the products required by an ordinary citizen. However, the majority of these commodity groups fails to reflect the problem of the local population as well as for other developing and, especially, poorer countries. In particular the price dynamics whether it decreases or increases on expensive alcoholic beverages, furniture, recreation and entertainment, and hotel and restaurant services are of no importance. Consequently, we can conclude that the abovementioned basket fails to adequately reflect the expenditures of average (poorer) consumer.

Under these conditions, a logical question arises concerning the kinds of problems which might occue when the main goal for a central bank's monetary policy is only to retain price stability. This is known as inflation targeting. Ignorance of the importance of the national currency exchange rate rather painfully affects a wider group of the population and business which ultimately increases both fear and uncertainty (Anguridze, Charaia, Doghonadze, 2015).

Beginning from 1967, New Zealand experienced a stretch of high inflation lasting for more than two decades (the average annual inflation was 15% and it peaked at 20%) (Sherwin, 1997). In 1984, the Reserve Bank of New Zealand issued an act under which the desired maximum inflation level was set for the monetary policy which paved the way for the so-called inflation targeting. By doing this, New Zealand was the first country in the world to renounce the internationally recognized priority of the monetary aggregates and exchange rate (e.g. Archer, 2000; Brash, 2002). By 2006, there were 25 inflation targeting countries (Mishkin, Schmidt-Hebbel, 2007) with the number growing to 62 by 2017 (CBN, 2017).

Central banks employing inflation targeting frequently justify their decisions to do so and state that they have reached not only their desired target (price stability) but have also contributed to stable economic growth such as, for example, was announced by Canada's central bank (Bank of Canada, 2006). The fact that the average inflation level was comparatively low in both developing and developed countries utilizing inflation targeting is proven by research studies (Mishkin, Schmidt-Hebbel, 2007; Vega, Winkelried, 2005).

However, inflation targeting does have serious opposition (Snooks, 2008). For example, Joseph Stiglitz, the Nobel Prize winner in Economic 2001, is almost confident that this system will be changed because the central banks of developing economies are incapable of managing their inflation which is frequently imported (Stiglitz, 2008). In the opinion of Jeffrey Frankel, inflation targeting died and central banks have not yet decided what new commitment monetary policy should be given in order to become a new hope for stability (Frankel, 2012).

The Bank for International Settlements resists inflation targeting which, in most cases, runs counter to financial stability (BIS, 2010; Jones, 2016). Inflation targeting does not take into account the financial cycle and thus produces an excessively expansionary and asymmetric monetary policy (Weber, 2015). It is noteworthy that inflation targeting creates

a great deal of questions. A major argument in favor of inflation targeting – that it has contributed to a decline in inflation since the early 1990s – is questionable at best. From the 1980s on, the inflation trend was already on the decline where globalization and China's integration into the world economy – and not inflation targeting – have probably been the most important reasons for the drop (Weber, 2015).

For an adequate reflection of the reality in developing and mostly poorer countries, other indices must also be used together with the inflation index. For countries where import exceeds export by several times, it should be clear that calculations must be made not only by the traditional inflation index but also according to their consumer basket made up exclusively of imported goods and services. Such an index can be called *imflation* which is a combination of two terms – "import" and "inflation" (Charaia, Papava, 2017).

If targeting parameters also include imflation together with ordinary inflation, then central banks will need to adequately respond to the issue of national currency devaluation in order to prevent price increases of imported goods on the domestic market owing to the particularly large volume of import.

In some cases neither inflation nor the imflation index will meet the goal of assessing price dynamics in those spheres important for the poorer population, especially in developing countries. As is well known, agrarian inflation (or the growth of average prices for agricultural products) or the *agflation* index, becomes more and more popular in economics. The term "agflation" is relatively new and its introduction is associated with the substantial increase in the prices for fruit, eggs, grain and other commodities in 2006-2007 (Chorafas, 2016). The agflation measurement is very important in developing and, especially, poorer countries which are characterized by permanent increases in foodstuff prices like in India (Suryanarayana, 2008).

Many studies have proven that the agflation index is higher and rather more important in developing countries where food products constitute about half of the total consumer basket: Russia – 50%, Azerbaijan – 50%, Armenia – 50%, Tajikistan – 57% and Turkmenistan – 60%, in contrast to developed Western countries: USA – 15% and Eurozone countries – 18%.

It is noteworthy that agflation is not only a problem for developing economies. This is evidenced by the challenges experienced by the new EU Member States (the ten Eastern European countries which joined in 2004) (IMF, 2008).

As is also well known, food inflation is not only higher, more instable, shows great volatility and lasts longer than non-food inflation, it also needs more time to adapt to new reduced prices which is unlike the process of price increases (EPRC, 2012). Given that the population in poorer countries gives special attention to how prices of food products, medication and utilities (mainly water, electricity, sewage, gas and other fuels) fluctuate, the statistical indicator adequately reflecting these prices should be calculated.

Hence, we propose a new statistical indicator, *munflation*. This new term comes from the first letters of the English words – medication, utilities and nutrition (Charaia, Papava, 2017).

The respective parameters for medication, utilities and food products from the consumer basket should be used for a munflation calculation. Food products prices are also used for the agflation calculation.

The issue of the possibility of extending the existing inflation targeting practice and studying the indicators of imflation, agflation and munflation in developing and relatively poorer countries, together with the inflation index, is the subject for a separate study.

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ინფალაციის თარგეთირების გამოწვევები დაბალშემოსავლიან ქვეყნებში

ვახტანგ ჯარაია

ასოცირებული პროფესორი
ბიზნესისა და ტექნოლოგიების უნივერსიტეტი

ვლადიმერ პაპავა

პროფესორი
თბილისის სახელმწიფო უნივერსიტეტი

რ ე ზ ი უ მ ე

ინფლაციის იდექსი და მისი თარგეთირება სულ უფრო მეტად კარგავს აქტუალურობას და მასთან ერთად ნდობასაც, განსაკუთრებით კი დაბალშემოსავლიან ქვეყნებში. სამომხმარებლო კალათაში შემავალი პროდუქტების გარკვეული ნაწილი ვერ ასახავს მოსახლეობის ფართო ფენების ინტერესების სფეროს. ამ პირობებში ლოგიკურა იბადება კითხვა, თუ რამდენად ადეკვატურია ცენტრელური ბანკების მონეტარული პოლიტიკა ინფლაციის თარგეთირებასთან დაკავშირებით.

საკვანძო სიტყვები: ინფლაცია, ინფლაციის თარგეთირება, იმფლაცია, აგფლაცია, მანფლაცია.