RECENT GLOBAL INFLATIONARY TRENDS AND THE ROLE OF CENTRAL BANKS IN DEVELOPING ECONOMY (INDIA)

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Most of the developing countries have been subject during the recent years to inflationary pressures of various degrees of intensity. As a rule, these pressures emanate from attempt by one or more sectors of the economy to secure a larger share of the total product. The primary motivations of such attempts are the desire of other public sector or the private sector, or both, to undertake additional investments and to put the burden of the required additional savings on the other sector. However, the attempts of any one sector, once made effective, tends in terms to induce defensive reactions of other sectors that want to maintain their share in the total product, not only for investment but also, especially on the part of the government and of wage and salary earners, for consumption. These defensive reactions usually intensify the inflationary pressures.

Asian economic growth is slowing as weaker global demands dents exports, but accelerating inflation across the region is expected to pile pressure on Central Banks to tighten policy. China is on track for its sixth straight year of double-digit growth in 2008, but momentum will probably slowdown in nearly a decade. Meanwhile, China's consumer prices in 2008 will probably rise at the fastest pace in more than a decade, extending a policy dilemma for Chinese leaders as they try to balance the risks from slower economic growth with higher inflation. "Inflation will remain as a pressing issue", said Wong Jianhui, an analyst at South west Securities in Beijing. Economists forecast slower gross domestic product growth this year in 11 of the 12 economies in the Asia-Pacific, excluding Japan. Thailand's economic growth is seen bucking the trend, accelerating to 5 per cent from 4.8 per cent in 2007-08 solid exports under pinned by rice sales - help the economy defy expectations of a slowdown amid political uncertainty.

India's economic growth is expected to slow to 7.6 per cent in 2008-09 (April-March) as inflation forces the central bank to tighten policy, while South Korea's growth could slip to a 3 year low of 4.5 per cent in 2008. The Asian Development Bank has said it expects growth in the region's economies, excluding Japan to ease to 7.6 per cent in 2008 from 8.7 per cent last year as exports slow due to weaker demand from the United States. But Asia's exports remain resilient due to rising demand from other emerging markets, reflected in solid trade surplus in such countries as China, Indonesia, Taiwan and Malaysia, Indonesia's annual average inflation this year is seen accelerating sharply to 11.2 per cent from 6.6 per cent in 2007. India's annual inflation is expected to rise to 11 per cent in fiscal year 2007-08. That far exceeds the 6 per cent in a previous poll conducted in March 2007 and now 4 per cent rate recorded in 2009. Inflation is accelerating across Asia, driven by surging food and oil prices, posing threat to economic growth. Central Banks in Indonesia, the Philippines, Taiwan and Vietnam and India have raised interest rates in last year (2008), but analysts believe they remain behind the curve as inflation expectations rise and firms try to pass on higher costs to consumers." GoI, like other governments all over the world is fighting inflation, We have taken fiscal, monetary and administrative measures and we are willing to take more measures" said Indian Finance Minister. Inflation as measured by the whole-sale price index has become a cause of measure concern ever since it crossed 9 per cent in March 2008, and since then it has been steadily rising without respite. Owing to its wide coverage of commodities and frequently available data, the whole-sale price index is the most commonly used measure of inflation in India. However, it excludes services and non-tradable commodities. Further it only measures headline inflation.

It is important to distinguish between headline inflation and core inflation. Headline inflation includes the entire set of commodities in the general price index, in this case, the whole-sale price index. Core inflation does not take into consideration commodities that have volatile prices, for example food and fuel. It follows that supply shocks that arise from a poor crop yield or hikes in international prices of fuel while lead to increases in headline inflation. In contrast, core inflation would not be affected by these shocks. In India and most other developing countries, food articles are significantly weighted in the price index. As such, a measure of core inflation may not provide a complete picture of the price scenario. Inflation in 2007-08 and in the current fiscal so far has been driven mostly by price increases of manufactured products followed by primary articles and then the fuel price.

So, the Indian economy has experienced robust growth since 2003-04 to date. However, while the first three years in this period showed moderate inflationary pressures, the last two years have experienced relatively high inflation. In terms of whole-sale prices, inflation began to firm up mid 2006- 07 mainly due to (i) an increase in the prices of wheat, pulses and edible oils because of the shortfall in domestic supply relative to demand and firm international prices; and (ii) an increase in prices of international crude The R.B.I, continued to follow its policy of gradual withdrawal of monetary accommodation in order to be able to stabilize using inflationary expectations. This in addition to an enforcement in the availability of wheat, pulses oils and fiscal and supply-side measures put into place by the government of India helped contain inflation. This decelerating trend continued into 2007-08 until Dec. 2007 and increased sharply thereafter.

Increases in prices of food and non-food primary articles as well as manufactured products also affected to the economy and the whole-sale price index inflation (in the current fiscal year 2008-09) has consistently been above 7 per cent mark and touched a three and a half year high of 8.24 per cent in the week ending May 24, 2008 on account of increases in food, metal products and industrial fuel. In order to combat the inflationary pressures, the government has taken a number of measures which became successful to control over it in 2009.There is no easy policy response to the present inflationary crisis but there are critical differences between what should be done for food and for oil and what should be done in short-run and the long. For basic food, there is no alternative to shielding poor consumers from the market price rise. Some experts have remarked how this is all a matter of supply and demand and if Government do not interfere in the market, the price rise will bring a supply response, which will cause inflation to level out. That ma be true. But markets pay no heed to grinding poverty. There would be starvation deaths before such a market process fully works itself out. The state needs to intervene even though, in the long run, and state should invest heavily in agricultural sector to boost productivity and allow for the free flow of food between regions and also in an out of the nation, in response to market incentives. On oil, continuing to shield consumers from the global price rise is not sustainable policy. It is causing unmanageable fiscal strain and by keeping the demand for fuel artificially high, it is distorting markets which will soon hurt the economy's growth. Prices will have to be raised, even though will hurt consumers in visible ways, hurt in itself is unavoidable given the global situation. While some subsidy for end-use goods, such as basic good, education and health, is unavoidable in a nation of as much poverty as ours, subsidies in general are a bad idea. They distort prices and get subverted by corporations and the rich and seldom reach the needy. In a strange way, this crisis can be an opportunity. Faced with rising costs, corporations in industrialized nations are struggling to protect their profits. India needs to work on a war-footing to cur bureaucracy, increase efficiency and attract international business. This will help stave off the immediate crisis, create unemployment and yield large, long-run benefits.

The central bank attempted some avenues forward impairing the efficiency of the central banking in less developed countries like India. The experience of these countries reviewed suggest that governments are perhaps not as universally the principle source of inflation as often seems to be supposed. Nor is the actual, and much less the potential, scope of an anti-inflationary monetary policy quite so limited as is frequently. The more significant is central bank credit to the private sector as a primary expansion factor, the greater will be the possibility of preventing cronic inflation through monetary measures. It follows that the realization of a stabilizing, or, of the government is the primary expansion source, an at least partially compensating policy, requires the removal of obstacles. The most important obstacle seems to be unwillingness of the monetary authorities to exercise greater restraint upon the private sector. If monetary authorities are reluctant to exercise a greater measure of restraint in their credit policy because they believe that a highly elastic supply of credit is conductive to an acceleration of economic development, the lessons of experience may gradually tend to induce change in views.

So far as unwillingness to enforce sufficiently serve anti- inflationary measures is due to apprehensions regarding the short-run output effects, of a restrictive credit policy, it may be more difficult to induce a greater degree of restraint. For a less developed country in which the foremost policy objective is not only absolute but also relative economic growth; underutilized production capacity will be socially less tolerable than in an advanced economy where the stability of full employment objectives tend to take priority over growth objective. It may, therefore, be difficult to persuade monetary authorities to contract credit or even to freeze it, when, for instance, output and income in the agricultural sector fall on account of exogenous factors, like a crop failure or depressed export markets, since such policy may result in underutilized capacity.

In their day-to-day decisions on credit policy, specially in respect to rediscounting, central banks are likely to be more concerned with the immediate effects of their decisions on output than with the long-run effects on propensities (to save, to invest, to hold money etc.) and the structure of the financial system. In less developed countries, those long-run effects will, however, determine the scope for monetary policy in the future. Therefore, an important, although perhaps unorthodox, field of what may be called long-run monetary policy may lie in activities that aim at changing these proper and the structure of the monetary and financial system. Such attempts often conflict with short-run policies. Other related measures are encouragement of specialized saving institutions and the extension of bank control over the investment policies of non-bank financial intermediant. If such long-run policies succeed in changing saving, investment and as: holding habits in the "right" direction, some reasons for the reluctance central banks to apply restrictive measures to commercial banks and to private sector will gradually disappear. One particular aspect of long-run monetary policy may need specie attention. 'The extent to which credit can be expanded without inflation, other things being equal will be greater when income velocity declines than when it remains constant or even increases long-run policy may, therefore, aim at reducing velocity by, say, lengthening payment periods and encouraging the holding of money. On the other hand, it has also been noted that the efficiency of short-run monetary policy will be raised when the public, including banks, can be induced to hold financial assets and to use means of payment less liquid than money. This will reduce the scope for credit expansion without inflation' but it will permit greater credit extension by financial institutions outside the monetary system, i.e. from sources other than the central bank and commercial banks.

In spite of institutional limitations, monetary measures could, as equired very recently in India, have succeeded in preventing continuous inflation. Central bank action could have reduced the rate of inflation. The stentlally most effective restrictive tool would have been greater restraint in central bank rediscounting for banks and the private sector. The unwillingness the monetary authorities to use restrictive tools more vigourously is due to apprehensions regarding the output effects of a reduction in the 3 of credit expansion and of a reduction in the volume of credit. There are indications that in most of the countries including India reviewed gradual change in the legal and institutional framework were : followed a more determined implementation and restrictive money measures. In addition, further improvements in the efficiency of money policy in still predominantly agricultural economies may depend on the e) to which the present inflexibility of credit policy can be reduced. This requires the growth of capital markets and credit institutions outside monetary system.

CONCLUSION

It has been said that inflation is the most regressive form of taxatii as it effects the poor and vulnerable sections of society. In the Indian conte> it is the unrecognized, without the benefit of trade union or political patronage who suffer the worst effects of inflation. Inflation dampens exports by making; our products expensive and conversely, makes imports attractive. Inflation leads to recession, as people with fixed income set apart an increasing share of their income to meet the growing costs of essential commodities, leading very little expenditure on non-essential items. The production of such items has to be curtailed leading to shutdowns and recession.

Reserve Bank of India assisting in controlling inflation through monetary measures such as quantitative and selective credit controls and by manipulating the Cash Reserve Ratio (CRR) and the Statutory Liquidity Ratio SLR). On the other side, the mechanism of Public Distribution System ensures availability of essential commodities for the poor. This helps to maintain price levels. Foreign inflows need to be sterilised by the R.B.I, by withdrawing from regulation an equivalent amount of rupees either through open market teration or through regulating bank credit. The country's inflation rate fall low 3.7 per cent, the lowest in 13 months raising hopes of further fall in the interest as policy makers group for options to maintain growth amid a sharp / down in the world economy. A cut in the rate - at which the central lends to commercial banks appears a possibility.

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