# Fighting the Effects of Inflation

By Haris Gazdar

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IJAZ Nabi's insightful article (Dawn, July 8) has opened a timely discussion on the direction of economic policy and the options that must be imagined. Pakistan's political business cycle has come round again — and as ever the bill for the generals' and bankers' party is post-dated.

The public outcry against dearness, however, must not be used as an alibi for another ineffective and devastating round of IMF-sponsored 'stabilisation'.

Pakistan's overall economic performance has less to do with domestic management than it does with the foreign policy environment. But showing that we have our priorities right will encourage the right sort of help.

The current chaotic state of global finance has invalidated the existing orthodoxy in macroeconomic management. If the IMF formula of stabilising economies by forcing them to adhere to deficit-GDP ratio targets was arbitrary before, it is completely unjustifiable now. The crisis triggered by subprime lending in the US was caused by cheap cash. The solution found by 'prudent' and 'responsible' monetary authorities in rich countries was to loosen monetary policy further. This means more cheap cash for investment banks to fuel speculative bubbles in international commodities markets. The G-8 summit acknowledged speculation as a key source of commodity price spirals, but did little else.
Asian economies in the meanwhile are being counselled to engineer domestic recessions through tighter monetary policies — all this in the vain hope that it will contain inflation which is actually being driven by cheap cash and loose financial regulation in Wall Street. This would be an unjust way of achieving stability in commodity markets. Force impoverished Asian economies to slow down their growth and hence their demand for commodities while letting the real culprits, the speculators and

their regulators, off the hook. A similarly unjust approach was found three decades ago when the IMF encouraged oil-importing developing countries to sustain their economies through the 1970s oil price shock by borrowing Eurodollars held by the oil exporters. This helped the rich countries out of a recession, enriched the banks and the elites in Africa and South America, but at the severe cost of working people and political stability in those countries.

The current IMF recipe — let's not call it prescription — is not only unjust. It is also ineffective. It is about fighting inflation as the mother of all evils at the expense of everything else. The working person's pain at rising prices might leave some in government feeling that the IMF brew is just the joshanda that is needed. Let us be very clear: it is not.

Domestic stabilisation cannot significantly reduce inflation at this stage. In fact, secondary wage and price inflation are necessary if the burden of exogenous price shocks is to be shared more equally than it has been. In an economy where 62 per cent of the workforce consists of 'own-account' workers, wage and price inflation are closely correlated. Yes, the government and the central bank must be more vigilant against speculators in particular sectors, reduce some market frictions and increase others. All of that will take some managing. But it will only help to control temporary shortages and domestic price spirals. National governments cannot control speculative bubbles in global markets.

What can and must be done, however, is to protect people from the effects of inflation. This means things like workfare, income support and even quantitative rations. The chaos in the world economy, led as it is by the financial markets, is likely to force Asian economies to demonetise more aspects of their social provision. Quantitative rations would be one way, others would be school meals and basic commodity coupons.
Slashing untargeted subsidies on energy and food is correct, but it becomes defensible if comparable budgetary allocations are set aside for social protection. Budget deficits and monetary sources of domestic inflation will have to be tolerated, at least for a while. And as Ijaz Nabi points out, our "friends" abroad have to help — particularly those that have done quite nicely out of the oil windfall, and have probably contributed to the windfall by themselves investing in oil futures. It is also as good a time as any to ask about the famous democracy dividend. But it is not just about money. The challenge ahead is to put in place credible social protection measures that will allow working people to see off the hangover of the generals' and bankers' party. Credibility is the key. For most interventions this means good targeting. Workfare or an employment guarantee programme, which incidentally was part of the PPP election manifesto, has the

virtue of being self-targeting. Anyone prepared to work at a basic wage is

guaranteed a job at that wage.
Cash grants require careful administrative targeting of beneficiaries and the key to success is that the selection criteria must be simple and intuitive. Quantitative rations are not targeted — they cover everyone but only a small part of their consumption needs — and the machinery has to ensure that everyone gets one ration and no one gets two. The most effective, perhaps, is feeding children through schools. It is self-targeted because only children get it, it directly protects nutritional entitlements, and it is inarguable that all children ought to be well fed.
None of the above sounds like easy work but then no one said life was going to be easy. Arguing that the government cannot and should not try to fight inflation has a sting in the tail, which is that government can and must work harder to fight the effects of inflation. If Pakistanis see and experience social protection that is effective and transparent, they will forgive the government inflation