

I. SOME VIEWPOINTS ON INFLATION

1. Recession, unemployment and inflation are common phenomena in the world economy. So fighting against them is always the main concern of both economists and governments. However, there are different viewpoints on these problems. As for the inflation, antagonists of the quantity theory of money argue that the inflation occurs because the stock of money far exceeds the demand of goods circulation, the paper money loses its value in comparison with gold, with the result that the prices of goods rise. In the inflation time, prices rise faster than wages, with the result that the real income of laborers is reduced and the unbalanced development becomes more serious. Argument of these economists is based on studies of three basic problems:

Firstly, analyses of the ratio of paper money and gold coins in circulation.

Secondly, in relation between the needed stock of money in circulation and total value of goods supplied, the latter is considered as a base, that is, the total value of goods supplied determines the amount of money in circulation, not vice versa.

Thirdly, the law of money circulation requires that the amount of money in circulation should equal the needed stock of money. If the amount of money in circulation is bigger than the needed stock of money, the inflation will occur.

According to this viewpoint, the main cause of the inflation is the way of putting money in circulation.

Exponents of the quantity theory of money argue that the inflation is an increase in the general level of prices in an economy that is sustained over a period of time. In other words, the inflation is an increase in the general level of prices because the demand increases over time faster than the supply capacity of the economy, with the result that the money supply is increased.

These economists study the inflation based on the following ideas:

Firstly, the lawful money, as a medium of exchange, will have a higher value than it is of other uses, because the value of money is higher than its production cost. The value of money is estimated according to its purchasing power.

Secondly, the paper money has no value in itself but it has value when it is put in circulation as a means of exchange. Its value depends on, and is in inverse proportion to, the amount of money in circulation, that is, the more the money in circulation,



INFLATION: THEORETICAL ASPECTS AND REALITIES

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the lower the value of a monetary unit. An decrease in value of a monetary unit will make the general level of prices increase.

Thirdly, in the relation between the needed stock of money and prices of goods and services supplied, the prices are subjected to the amount of money, thus, when the money supply increases the general level of prices will increase accordingly.

Fourthly, the main cause of the inflation is either the pull of demand or the push of cost.

The demand-pull inflation is caused by a level of demand in excess of the supply potential of the economy, with the result that the general level of prices rises. The cost-push inflation is caused by increases in factor input costs which pushes up prices even in periods when natural resources are not fully exploited (an increase in wage, for example).

We can see that different economic schools all agree that increases in general level of prices are signs of the inflation. But there are also basic differences between them in ways of explaining the causes of inflation and increases in the general level of prices. (increases caused by inflation or by other factors)

2. In spite of these differences, all these economists agree that the inflation is considered as undesirable because of its adverse effects on the economic growth. So the inflation rate must be kept low. But how low will the inflation rate be considered as reasonable? Economists of various schools have given two different answers to this question.

The first group of economists argue that the price control is the best basis for the fast economic development in the long run. This argument maintains that the inflation deforms the price system and make the people fail to perceive changes in a particular price based on changes in the general level of prices. Therefore, factor inputs will be unreasonably allocated and ineffectively used.

The inflation can also make investors fail to predict exactly the prices in future, thus, the inflation encourages investment in businesses of quick profit and discourages investment in long-term projects. Based on these arguments, they say that any inflation rate above 0% could lead to unrest and ineffectiveness.

In the second group, an increasing number of economists think that the current problem of all economies is the recession, not the inflation. They argue that "a bit of inflation" is what the economy needs to reduce the burden of debts, thereby developing

the production. They think that, if the unrest is caused by the inflation, then the amplitude of the inflation is more important than the inflation rate itself. According to them, the inflation rate of 0% on average fluctuating between - 5% and + 5% will produce the same effects as the inflation rate of 10% on average fluctuating between 5% and 15%. So they believe that "a bit of inflation" is healthy, and will act as a lubricant that could make prices and wages change effectively, or they think that, the cost for reducing inflation rate to 0% is bigger than the cost of inflation itself. They come to a conclusion that policy makers need not eliminate the inflation but had better stabilize the inflation rate in order to make price forecast easier.

According to many economists, an inflation rate of 2% or 3% per year is the best, and in fact, it has become a target for many governments.

II. REALITIES OF THE PROBLEM

1. In the relation between the inflation and economic development, the problem is that whether nation of high inflation rate will develop faster or slower than a nation of low inflation rate. Realities provide us with different answers. In the period between 1971 and 1991, the annual growth rate of Sweden was 1.1% although its inflation rate is the second lowest one among 20 surveyed countries, whereas Italy, Spain or Iceland had a higher growth rate in spite of their inflation rate of 10% up.

2. As for the relation between the inflation and unemployment, J.M. Keynes's argument about the use of inflation and budget expenditure for reducing unemployment and crisis levels has been applied by many Western countries successfully in decades after 1933. But in the 1960s, the inflation was widespread whereas unemployment and crisis levels couldn't be reduced. In the period between 1974 and 1991, countries with low inflation rate had the lowest levels of unemployment.

3. In the relation between the increase in money supply and the inflation rate, the realities proved that what happened was not exactly coincident with the theory. In 1990, in Vietnam, the money supply was increased by 73%, the inflation rate was 67%. In 1991, the money supply increased by 41%, but the inflation rate reached 66.4%. Anh in 1992 and 1993, the money supply increased by 70% to 80%, but the inflation rate decreased to 17.6% (1992) and 5.2% (1993). In Thailand, the money supply increased by 14.8% in 1990 compared with 1985, the money supply increased by 14.8% in 1990 compared



with 1985, the growth rate was 45.8% but the inflation rate was about 3.5% per year.

These facts show that theories of inflation are numerous but the realities of inflation are ever more varied. However, both theory and realities come to the same conclusion that the high inflation rate will produce adverse effects on the development. So all governments have to occupy themselves in keeping the inflation rate at single-digit level.

4. In Vietnam, the process of reducing and keeping the inflation rate at low level is considered as an outstanding achievement in the economic renovation. The following chart will show result of inflation control in Vietnam:

Increase of CPI (%)

Year	Increase of CPI (%)
1986	774.7
1987	223.1
1988	393.8
1989	34.7
1990	67.4
1991	67.6
1992	17.6
1993	5.2
1994	14.4
1995 (est.)	15.0

We see that the inflation rate has stayed at three digit level for many successive years. In 1989, it was reduced to the two-digit level for the first time. In 1993 particularly, the inflation rate decreased from 17.6% to 5.2% while the growth rate reached 7.2%. The Okum's argument that the GDP will reduce by 4% if the inflation rate decreases by 1% is proved wrong by this fact.

However, we haven't reduced the inflation rate to the expected level and we still have great difficulty in

forecasting the amplitude of the inflation rate in future. Just because of this unpredictability, many investors felt discouraged, the task of making policies on wage rate, interest rate and tax became more difficult. Thus, besides reducing the inflation rate to a single - digit level, we should keep this rate stable. In order to carry out this task, many studies show that we should map out appropriate fiscal and monetary policies, adopt flexible exchange rate, have great reserves and know when to intervene in the economy.

I would like to stress here the following points:

- We should accelerate the reformation in the economic structure and mechanism for economic management, thereby exploiting advantages of the market economy and national potentialities.

- Prices of essential goods and other goods and services monopolized by the Government should be stabilized.

- The CPI is the common sign of the inflation, but it is not always measured exactly because of mistakes in calculating methods. Furthermore, it doesn't reflect all changes in product quality.

- We should realize that controlling the inflation is not the target of the task of macro-economic management, but it's a way to create favorable conditions for economic development, that is, all macro-economic policies should aim at helping the economy develop stably and fast which is considered as the only target.

In short, we should use many instruments, take many measures, study many theories of inflation and test the value of these theories on realities in order to curb and control the inflation more effectively. ■