

## SALIENT ASPECTS OF INFLATION AND GROWTH IN SELECTED COUNTRIES\*

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## ABSTRACT

*This paper comments on the figurative problems of inflation and growth, and the character of its trade-off, a topic which was the subject of heated numerous studies in developed countries. As a problem of external shocks, the unexpected procedures produce an extra point of their relationship. The observation of evidence in several level of country experiences and various periods should provide a useful comprehension and complement to the wide analysis of these problems. Some lessons obtained from the specific economic indicators reflect to general aspects of the subject under the role of price taker, inflexibility output supply and passive money which make the unexpected changes explore persistently to the character of this problem in general for many countries.*

## 1 – INTRODUCTION

The beginning of the seventh decade of this century demonstrated the significant effects of oil price crisis and late on the world recession, as the external shocks, in the development of prices and income specially in the non-OPEC developing countries. And for this reason, growth processes of these countries should address itself explicitly to the problems of open economies or deal directly with the balance of payment problems. By the way, due to these exogenous shocks to their economy, those countries adopted various policy measures in response to them. Obviously, it is possible to consider the effects of these shocks through the role of domestic level of excess demand which affects the structural change of balance of payments. The consequence of this swing will reflect to the domestic rate of monetary expansion and this will influence the domestic price level and capital movements<sup>1</sup>. Nevertheless a detailed study of the seventh decade relatively could not arrive at any conclusion with respect to trade-off between inflation and growth.

## 2 – OVER VIEW OF INFLATION AND GROWTH FROM THE SELECTED COUNTRIES

High rate of inflation and a dragging economic growth are the most serious problems that the developed and non-OPEC developing countries face nowadays. It is clear that this phenomenon is related with the external shocks, it can be seen that the degree of problems varies within a country itself not to say the least when it comes to consider the relationship among countries. Therefore, better explanation for trade-off should be considered from various countries and from many periods. In turn, fifteen countries had been selected and so as to represent differences in the character and the extent of external shocks as well as in the forms of relationship between growth and inflation<sup>(\*)</sup>. And selected periods would be during 1958 to 1978, as sufficient to capture their fluctuations by external shocks. The rates of inflation and economic growth of countries under study were calculated from their variation of price and quantity indices respectively, their data for the year 1976 had been taken as the basis.

This was due to the available data on the International Monetary Fund.

Graphs 1.1 to 1.16 show in terms of three-year average, correlation between inflation and growth in each countries sampled during two decades. Initially for the world economy (graphs 1.1 and 1.1.A) had shown its inflation rate relatively constant during 1958 to 1968 with the annual average rate of 4.4 per cent. This level began to increase clearly from the commencement of seventh decade, which also was the starting period of increasing price of petroleum. Anyway, in terms of growth cycle, this period had been considered as the "boom" period of world economy<sup>2</sup>. Even at the increasing world rate of inflation, around 40 per cent, as one part of the effect of oil price crisis, the boom period was able to interpret the structure of inflation as a real phenomenon. The period after, 1974 to 1978, had been considered as the period of world recession, and besides the oil crisis became particularly effective. The world inflation rate had been increasing at an accelerated rate about 80 per cent of the former period or more than 100 per cent excluding oil crisis. From

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(\*) Fifteen selected countries had been separated to two main groups and four sub-groups as following, firstly the non-OPEC developing countries which were combined by one european country – Portugal, latin american countries – Argentina, Brazil, Chile, Colombia, Mexico, Peru and Uruguay – and asian countries – South Korea and Thailand; secondly the developed countries – Israel, Italy, Spain, the United Kingdom and the United States.

graph 1.1.A, at the accelerated rate the trade-off world inflation and growth became negatively related. And also, consequently, the extreme exogenous shocks through the rapid acceleration of domestic inflation, had adverse effects on the growth rate of the countries in general. This observation expressed obviously for the countries which had higher increasing rate of domestic inflation than others, for example, in case of latin american countries and Israel. However, this negative trade-off also confirmed relatively in the seventh decade for countries which had suffered less elevation in their rates of domestic inflation – such as in case of developed countries and Thailand. Therefore, this gives a reasonable view about the importance of external shocks in their internal economy.

Obviously, on table 1, from the expression of the coefficients of degree of openness and the current account deficit, column 1 and 2 respectively, their values gave broad conclusions on the raising significance of external sector over the rest of the economy.

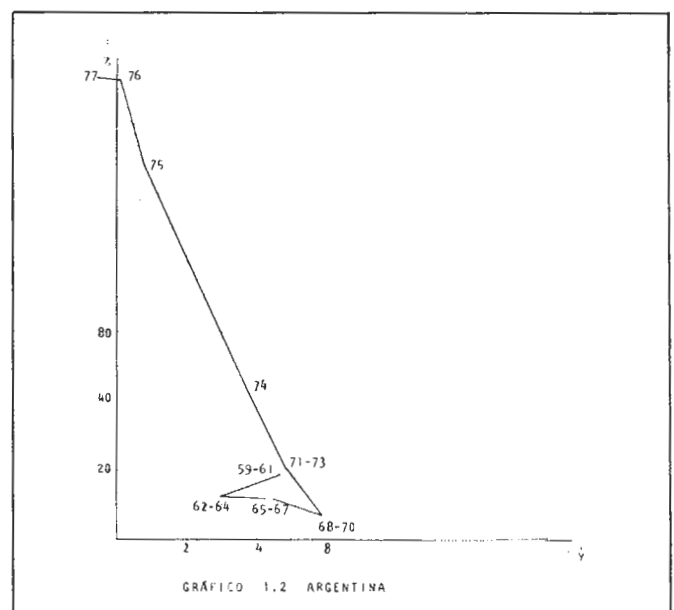
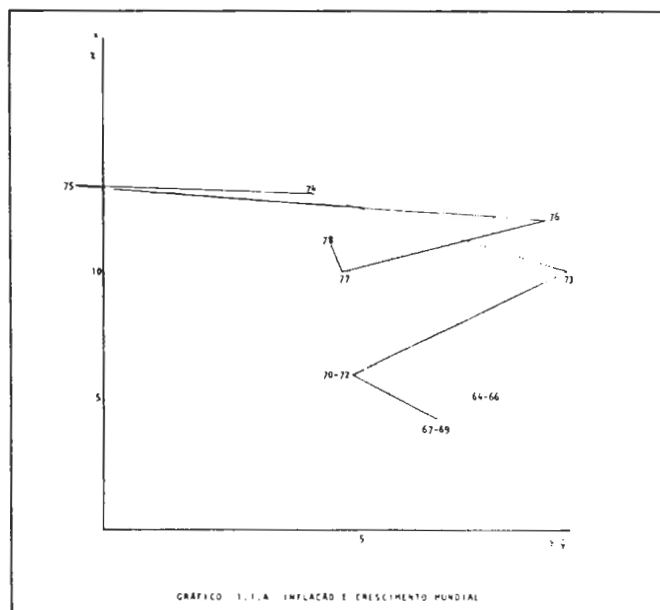
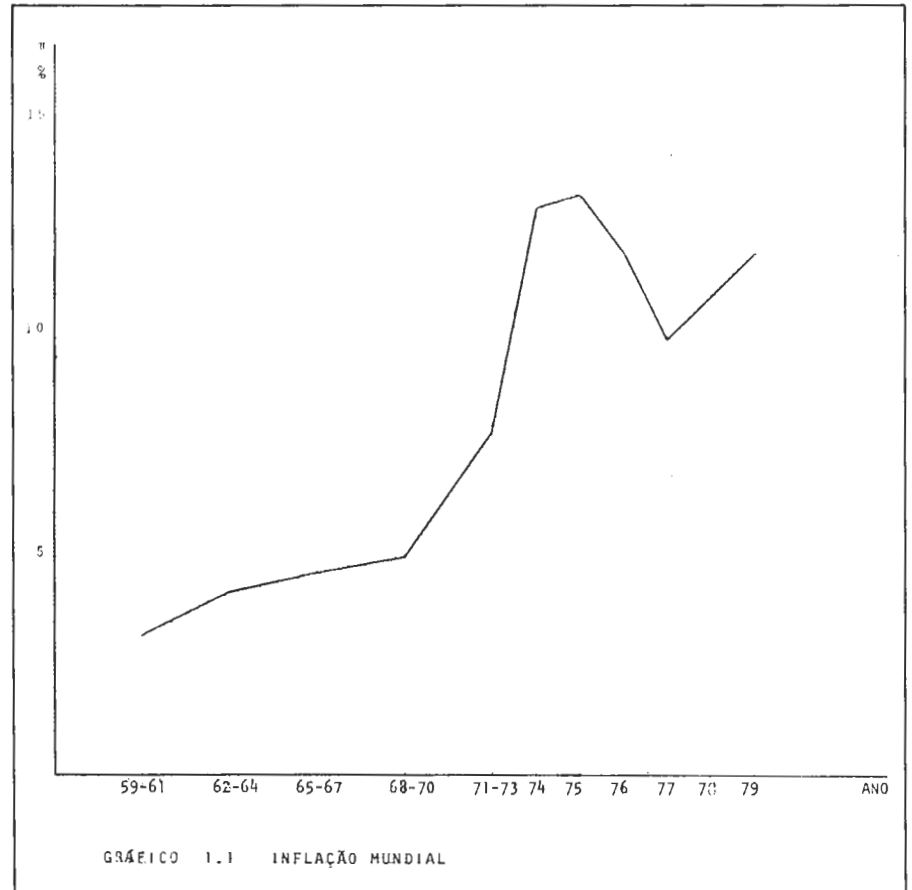
Besides with the high rate of monetary growth, this provokes an explosion of internal rate of inflation principally for the countries which usually had explosive rates of domestic inflation.

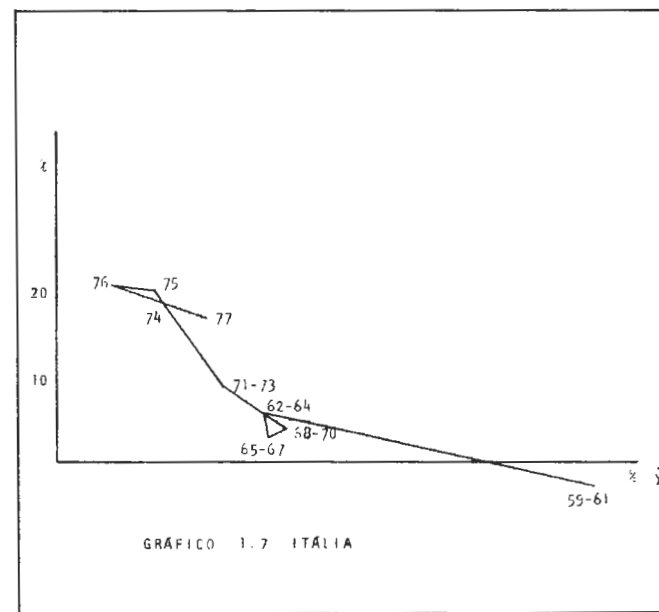
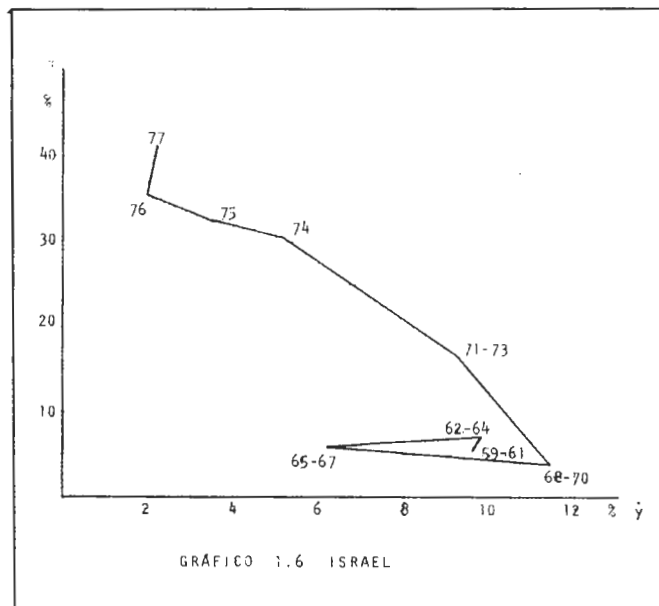
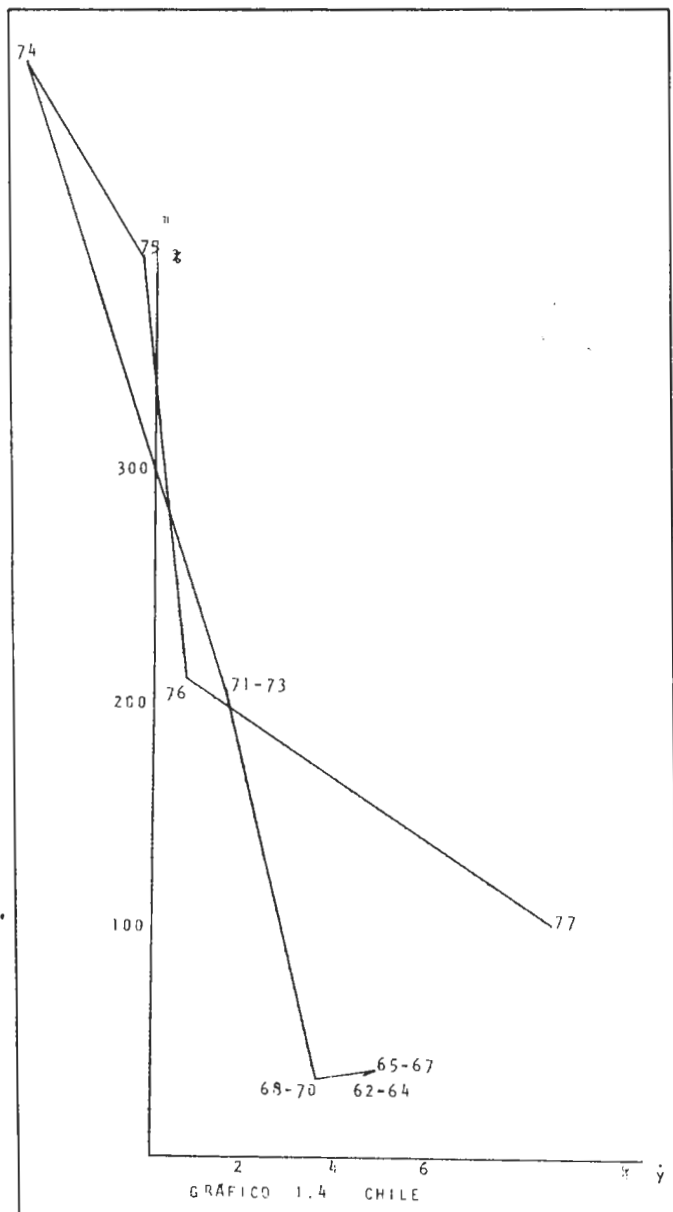
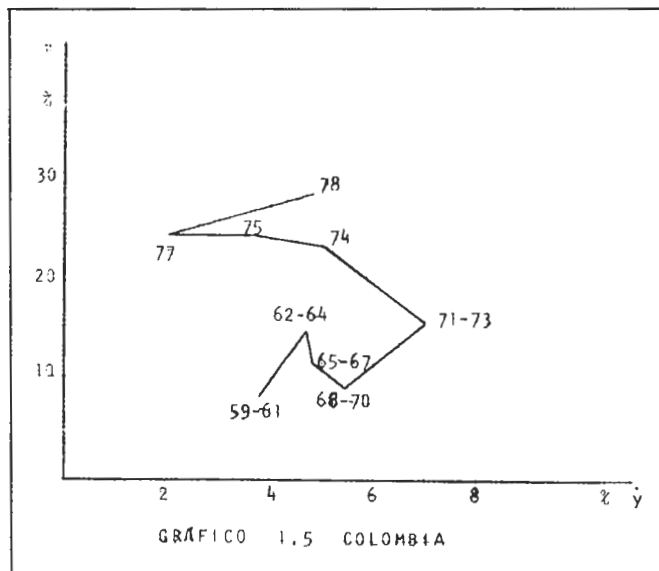
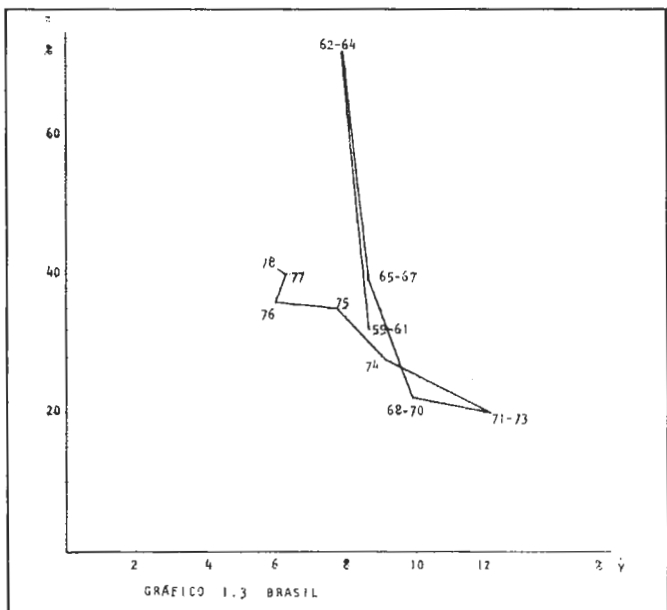
From the observations of inflation and growth including some specific estimates had shown a negative relation of trade-off principally during the period which existed the problem of external shocks and increasing

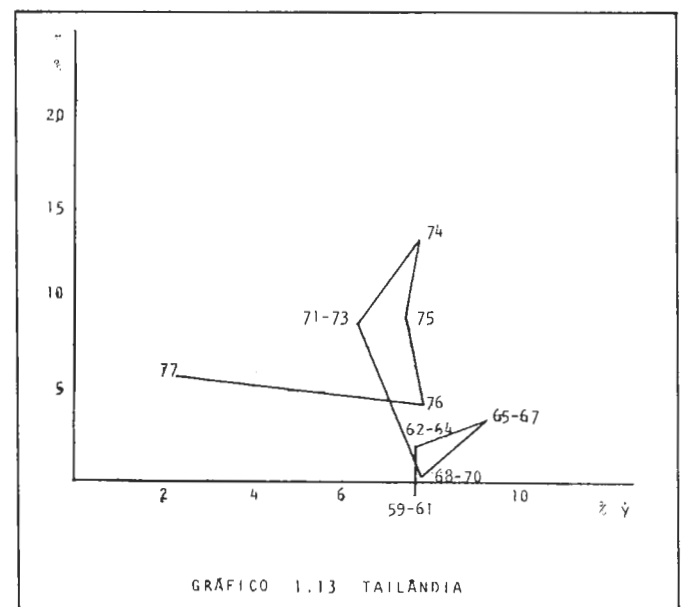
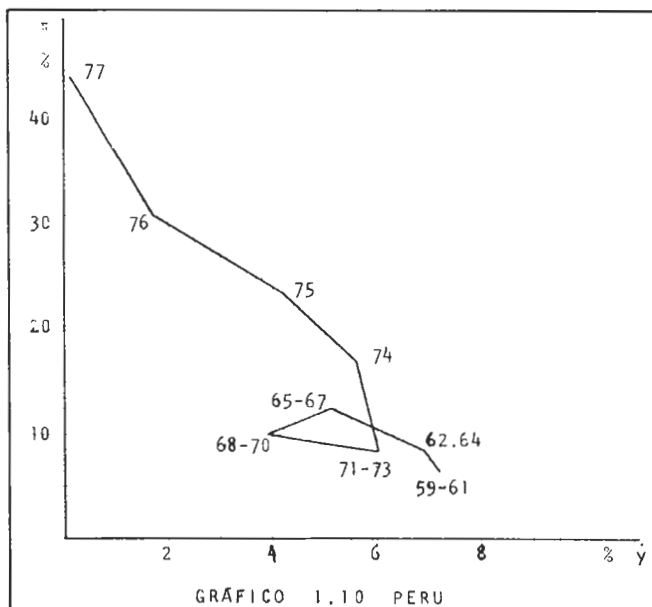
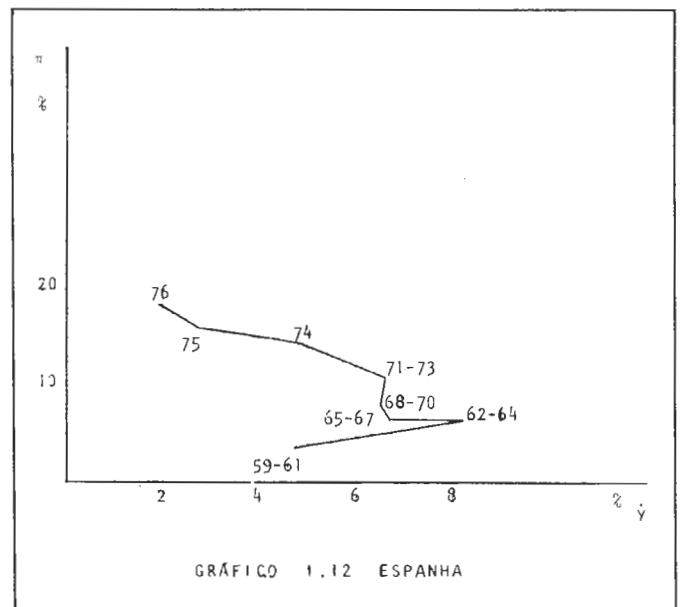
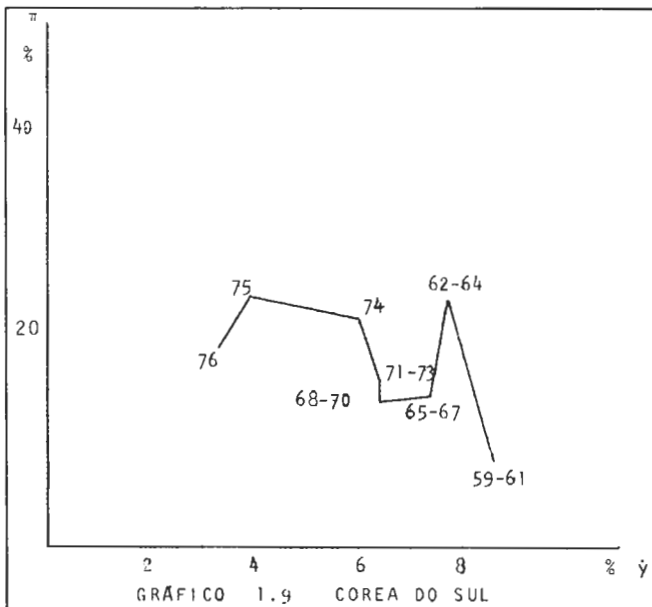
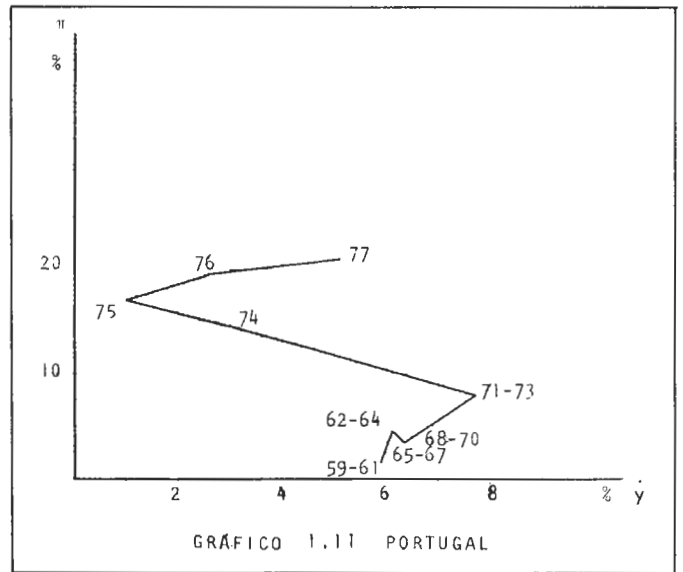
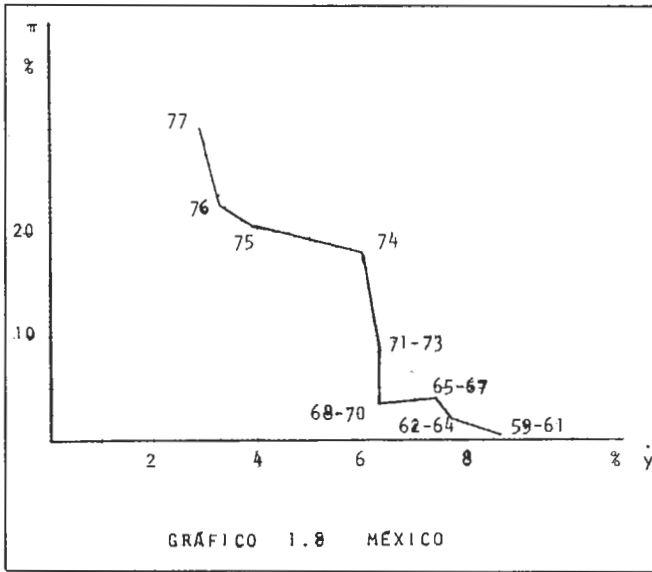
degree of openness. Anyway, this analysis seems contrary to description of economic literature under the well-known Phillips' curve. However, with the increasing degree of openness, this turns to be impossible to analyse the trade-off only under the context of closed economy. On the other hand, under the development of economic paradigms about this relationship such

as the role of rational expectations of the New Classical School and the concepts of non-market-clearing theorists these still are incapable of appreciating the analysis in reality.

Under the concept of unisolated economy, the concepts of inflationary and growth problems would be explained favourably on the basis of the attractive features of the open economy.







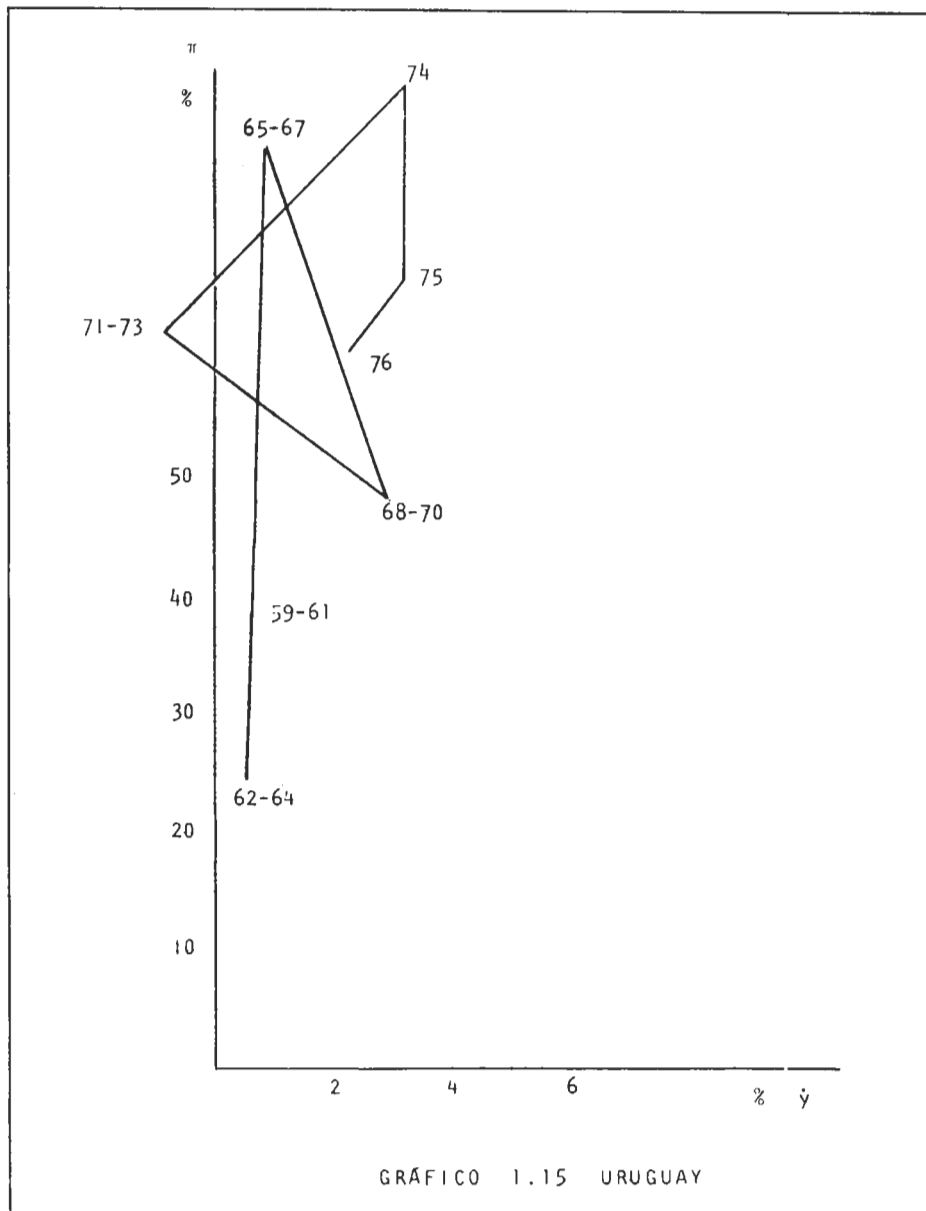
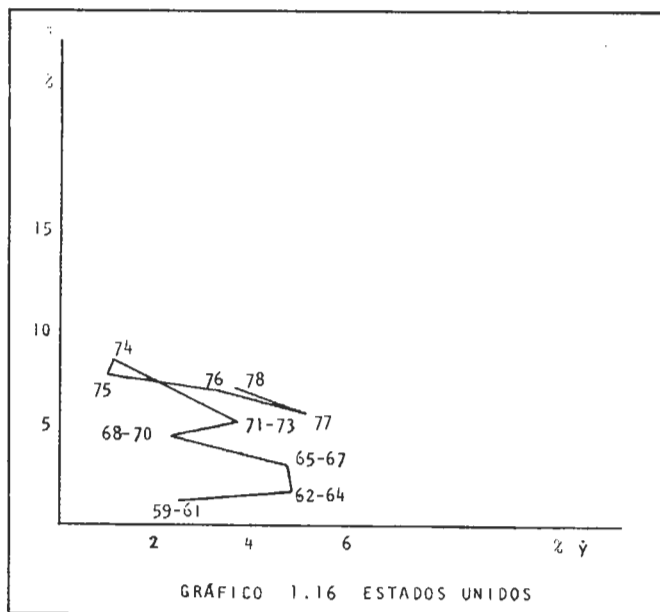
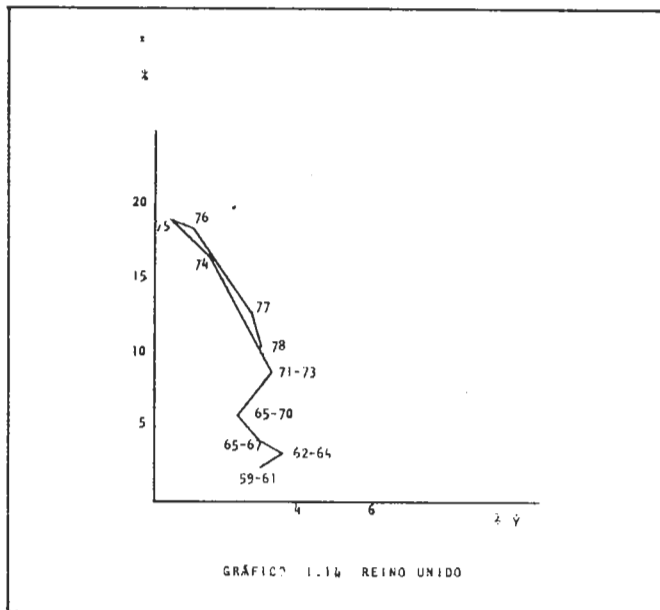


Table 1. Comparison among countries, based on some specific economic indicators: during two decades (60/70)

Countries	Degree of Openness		Current Account Deficit over Gross National Product		Growth Rate of Money Supply		Growth Rate of International Reserve	
	60	70	60	70	60	70	60	70
Developed Countries								
Israel	0.61	0.99	-0.0500	-0.1215	15.23	25.43	22.22	23.67
Italy	0.29	0.43	0.0260	-0.0005	13.44	18.58	12.09	11.71
Spain	0.22	0.30	-0.0050	-0.0120	12.30	18.87	39.31	26.02
United Kingdom	0.40	0.51	-0.0029	-0.0215	2.89	12.69	2.57	53.83
United States	0.09	0.15	0.0043	0.0004	3.36	5.87	-2.98	-0.84
Developing Countries								
Portugal	0.48	0.55	-	-	7.55	14.50	6.35	1.81
Asia								
South Korea	0.24	0.59	-0.0273	-0.0586	26.93	31.04	16.65	39.56
Thailand	0.38	0.43	-0.0105	-0.0292	6.58	12.34	10.08	6.72
American Latin								
Permanent Inflation								
Argentina	0.18	0.17	-0.0089	-0.0126	28.98	114.79	33.37	55.64
Brazil	0.13	0.17	-0.0147	-0.0427	44.98	35.92	14.14	42.28
Chile	0.32	0.32	-0.0267	-0.0433	-	170.23	-	39.70
Uruguay	0.27	0.30	0.0018	-0.0203	46.28	53.80	0.28	8.83
Irregular Inflation								
Colombia	0.27	0.30	-0.0200	-0.0175	17.49	23.49	8.78	32.93
Peru	0.42	0.35	-0.0226	-0.0492	14.53	28.10	15.82	19.18
Recent Inflation								
México	0.21	0.19	-	-	7.55	19.68	3.43	10.29

### 3 - GENERAL ASPECTS OF LESSONS OBTAINED

As the character of openness involving widely to each economic regime, the analysis of inflation and growth would impute partially to the outside factors. On the ground of the data which had shown the acute problems of inflation and dragging growth facing several countries on the seventh decade, this is worthwhile to open some aspects of these problems and persuade more attention on the covariance between internal and external movements. A few things would undoubtedly stand out.

a) In the international economy, the countries in general play as "price taker"; therefore, the variation of external prices disturbs positively to their internal economic movements. With the degree of openness, worldwide rate of inflation gives differently multiple and accelerated effects to internal

movements. Therefore, there is a high variance in the distribution of worldwide inflation across the countries. The picture of import inflation would be clear to the recent inflation countries such as the developed and asian countries.

b) Inflexibility of domestic and export supply, is another essential element which intervenes in this generation of inflationary pressures. This usually is expressed in case of the developing countries.

c) In the high inflation countries as latin american countries, the rate of expansion in the money supply has been such as to outstrip any realistic possibility of growth of real domestic product supply. This indicates a passive behaviour of the monetary authorities.

As a period of inflation crisis which may or may not influence the economic growth, therefore, it is necessary to consider the origin of inflation and how

it affects an economic system as a time path. Precisely, for open economy, the role of imported inflation or transmission process is one constraint for growth process especially in the developing countries. However, no clear relationship appears to exist between the rate of inflation and the rate of development. The high inflation countries (Argentina, Chile, Uruguay) tended to stagnate, some of the low inflation countries (Mexico, Thailand) seem to be developing fast. For the others there is a mixed picture but it may be said tentatively that (1) where inflation coincided with rapid development, the latter can best be explained by other factors (absorption of foreign resources, improvement in terms of trade), than by the full utilization of capacity supposedly brought by inflation; (2) in recent periods the acceleration of inflation has coincided with a deceleration of development.

## RESUMO

*Análise do figurativo dos problemas de inflação e de crescimento e seu trade-off. Com o problema de choques externos, os acontecimentos exógenos afetaram extremamente suas relações. Uma observação empírica de vários países e vários períodos daria a compreensão mais útil e complementar a análises mais abrangentes de problemas. Alguns resultados obtidos de indicadores econômicos específicos refletiram aspectos salientes desse problema, tal como o papel de tomador de preço, a inflexibilidade da oferta de produto e a moeda passiva que produziram mudanças não antecipadas permitiram explorar persistentemente a característica desse problema em geral para vários países.*

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