

OPTIMIZING INFLATION POLICIES IN THE REPUBLIC OF MOLDOVA

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Abstract:

The successful anti-inflationary policy of the state is an important condition of its economic growth. For supporting sustainable economic development, the state creates economic policy, so that it provides it with an anti-inflationary direction. Selected by the government system of actions in conditions price inflation and depreciation of money form an anti-inflationary policy. Thus, the state anti-inflationary policy is a set of measures carried out by state bodies to control inflation by regulating the monetary and other sectors of the economy. The author reveals aspects of inflation in Republic of Moldova economy and suggests anti-inflationary measures as a means of exerting comprehensive impact on the reasons behind inflationary processes.

Keywords: inflation, sustainable economic, inflationary processes, anti-inflationary policy.

JEL Classification: C32, E31

Introduction

Anti-inflationary policy as an element of government regulation is a set of macroeconomic stabilization measures. These measures aim to regulate the movement of money and achieve a balance between the commodity market, the financial market and the labor market. Anti-inflation policies are varied, depending on the criteria that are taken into account in their construction: the intensity and meaning of the process; the methods and tools used; inflation anticipation; agreed socio-economic doctrine. These policies aim to return to a state of monetary stability, to keep prices within reasonable limits, often with the aim of reducing unemployment. Regardless of the criterion or criteria taken into account, the policy or policies act either from aggregate demand (following its restriction) or from aggregate supply (following its growth). In connection with the approached problem, it is opportune to come with some clarifications on the concept of inflation, existing in the economic literature, among which we will mention the following:

1. In the conception of J.M. Keynes inflation is generated by a surplus of demand for goods and services to which the economy cannot respond. The phenomenon translates into a slow rise in prices, after which, if the initial momentum is maintained, the rise in prices becomes chronic, turning into inflation [4, p. 158];
2. The Romanian economist Victor Slavescu considers that whenever monetary signs are created and put into circulation on the market, over the real needs of production and exchange of economic goods and services, so many times we will find ourselves in front of an abnormal, artificial monetary situation. , called inflation [1, p. 253];
3. In a modern vision, Costin C. Kiritescu conceives inflation as having a much wider scope, it is a notion related to the money supply in circulation, an objective phenomenon, which does not exclude its conscious use, the immediate cause is the economic and financial disorganization reflected in the growth of the money supply in circulation at a faster pace than the growth of production [5];
4. According to the Dictionary of Economics, inflation is defined as a phenomenon specific to periods of economic crisis, consisting in the depreciation of paper money in circulation as a result

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of either issuing a mass of money over the real needs of circulation, or reducing the volume of production and circulation goods, which leads to a decrease in the purchasing power of money [3].

Description of the problem

Contemporary inflation, understood as structural, monetary-material imbalance, is generated by the following causes:

- the increase of the money supply through the excessive issuance of money signals generates inflation through money;
- excess solvent demand has the effect of inflation due to excess demand;
- insufficient supply, in the sense that the increase in revenues (especially wages) is not offset by an increase in the production of goods and services which is the result of supply inflation;
- substantial increase of credit and, implicitly, the excess of nominal demand for consumer goods determines the inflation through credit;
- the increase of costs through the convergent actions of all economic actors in the direction of price increases determines the inflation through costs;
- causes that are outside the market, the existence of strong monopolistic, oligopoly and administrative-bureaucratic structures, etc. whose action leads to structural inflation;
- the variation of the nominal salary is considered by the American economist J. K. Galbraith a main cause of inflation that leads to the increase of the labor costs, and therefore, to the inflation through wages;
- the specific changes of the nominal wage, of the productivity of the production factors and / of the profit rate are considered by the neo-Keynesian economists, causes of inflation. They distinguish the causes of inflation in relation to time: short-term inflation and long-term inflation;
- the increase of international prices for raw materials, fuel, energy, etc., the effect of which is imported inflation [7, p. 36].

Often in a national economy there is self-aggravation or self-maintenance of inflation, which is explained by the reaction of economic subjects to rising prices:

1. The population increases the demand for goods, anticipating the increase of prices;
2. The population depreciates the currency, anticipating the loss of purchasing power;
3. Economic agents increase their raw material reserves, anticipating the increase of prices;
4. Economic agents decrease the offer, anticipating the increase of prices [Cocriș].

Methodology and data sources

Theoretically, the most consistent criterion for measuring the inflationary process is the absolute and relative gap between the nominal solvent demand and the real supply of material goods and services. Both sizes must be considered as aggregates on the scale of countries' economies. Absolutely, the amount of inflation would consist in the difference between the absolute nominal demand and the real supply of goods that economic agents can offer and that they actually put up for sale. Relatively, the process is measured as a percentage ratio between the absolute difference shown and the mass of the real supply of goods. Relative quantities, in turn, can be expressed in indices. Based on the respective indices, one can appreciate the meaning of the evolution of the inflationary process (ascending, descending, constant). Inflation can be measured by several indicators. The most important of these are:

1. Consumer price index (CPI) - is an economic indicator, which measures the overall evolution of the prices of purchased goods and service tariffs used by the population in a certain period (called the current period) compared to the previous period (called the period of base or reference). The CPI is intended to measure changes in the dynamics of the general level of prices for products and services purchased for consumption by households in the country. The CPI measures the general

trend of consumer prices over time. Everything consumers buy has a price, this price can vary over time, and consumer price indices are intended to measure these changes. The CPI measures average inflation based on household spending on shopping cart items. The components of this basket and their share in total expenditures are determined by the National Bureau of Statistics on the basis of surveys conducted on households in the Republic of Moldova.

2. Production Price Index (PPI) - measures the evolution of prices in the stages before final consumption, respectively the prices of raw materials, semi-finished products and finished products before being delivered to the market.

3. General Price Index (PGI) - measures the evolution of all prices in the economy, respectively both the prices of goods consumed by households and the prices of goods entering production processes. This is the most general way to measure inflation.

4. GDP deflator - shows the evolution of the average price level of all goods and services included in GDP, and is calculated as the ratio between nominal GDP and real GDP. The difference between the PGI and the GDP deflator comes from the different structure of goods and services that are included in each of them. If the GDP deflator is calculated on the basis of goods and services produced within the country, the general price index is calculated taking into account the imported products. [2, p. 281].

Next, we present the dynamics of consumer price indices for the years 2015-2019. We determine that the consumer price index has a downward trend during this period, so in 2015 it was 109.7%, 2016 - 106.4%, 2017 - 106.6%, 2018 - 103.0%, 2019 - 104, 8%. Within the elements of consumer prices, it is observed that the largest increase in prices is attested for foodstuffs, which form the most important part of a person's consumer basket. The only exception is 2015, when the increase in prices for non-food goods was higher, due to the depreciation of the national currency. In 2019, the following increases were registered for the CPI components: food products - 7.61%, non-food products - 4.19%, services - 1.47% (figure 1).

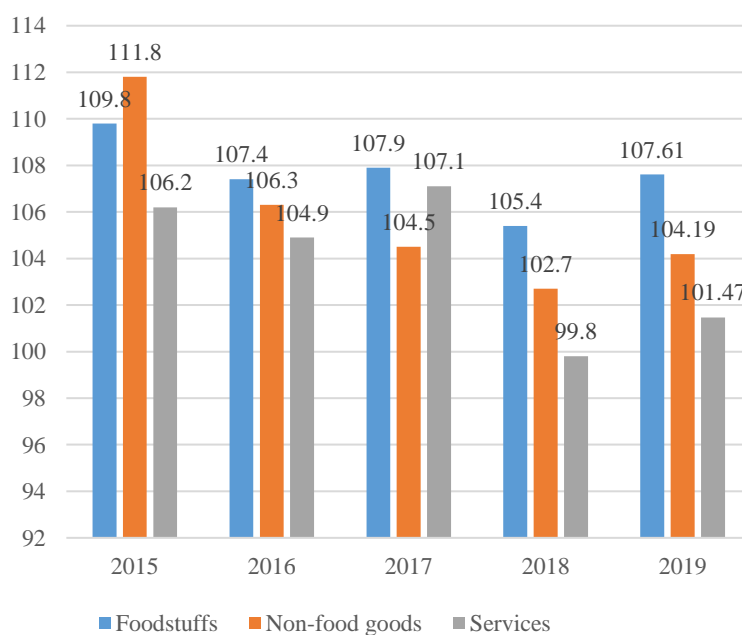


Figure 1. Elements of the consumer price index,%

Source: developed by the author based on [9]

During 2019, the annual rate of food prices recorded a sharp upward trend, which was mainly determined by the increase in contributions from the groups "fresh fruit", "meat, meat preparations and preserves", "Potatoes", "milk and milk products" and "milling products". The increase in prices for fresh fruits and potatoes was determined by a more modest harvest for these products, caused by unfavorable weather conditions in the summer of 2019. It should be noted that during 2019 inflationary pressures were recorded from processed goods. The increase in prices for these product categories was generated by the increase of production costs (wage costs, raw materials,

electricity, depreciation in annual terms of the MDL/USD exchange rate), but also as a result of a positive aggregate demand.

The core inflation rate in 2019 was 5.6%, similar to the CPI during 2019, core inflation remained on an upward trend, being fueled by the increase in aggregate demand. During October-December 2019, the core inflation index was 6.47%, up from the same period of 2018 by 3.8 pp. However, there is a decrease in the core inflationary pressure on the CPI towards the end of the year, an impact ameliorated by the appreciation of the real exchange rate of the national currency against the main reference currencies. The upward trend in the annual core inflation rate since the beginning of the year has been fueled by the maintenance of a high level of aggregate demand as well as rising prices in the subcomponent sectors, such as clothing, food, education and so on. [6, p. 29].

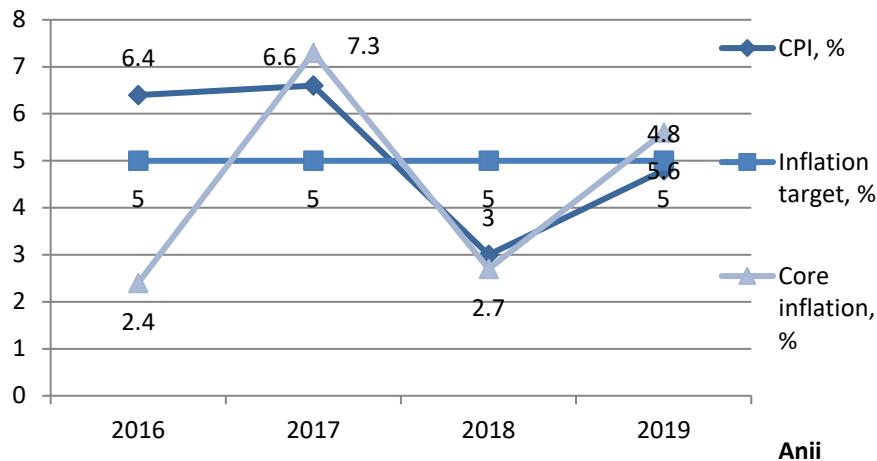


Figure 2. CPI and core inflation dynamics
Source: developed by the author based on [8]

The decreasing trend of core inflation, as it results from the data of figure 2, in 2018 was determined by the appreciation of the national currency against the main reference currencies as well as by the decrease of inflationary pressures from the CPI components. However, during this period, core inflation was also subject to inflationary pressures from the prices of its subcomponents, such as those for cigarettes and tourism services. The CPI compared to core inflation is higher in 2016 and 2018, while in 2017 core inflation exceeds the CPI by 0.7 pp. It is worth noting that this measure of inflation excludes the transitory effects on the CPI and largely reflects the inflationary pressures associated with excess demand. Core inflation continued to fall in the target range for more than a year.

The annual growth rate of industrial production prices in 2019 was 1.8%, which represents an increase in the growth rate by 1.4 pp. compared to the value of the respective indicator of the previous year. The acceleration of the growth rate of industrial production prices was supported by the increase of costs in the manufacturing industry which has a maximum contribution, fueled by the increase in energy and agricultural raw material prices. Prices for agricultural products increased at a fast pace at the end of 2019 both on international markets and domestically; the tendency was accentuated in the last case also by the dependence of the local agriculture on the climatic conditions. The annual index of prices for agricultural products was 3.8% compared to the previous year. A easing of inflationary pressures was visible in the case of fuel prices (whose annual rate decreased in 2019 by 4.57 percentage points to 2.3%), amid the downward trend in international oil prices and the appreciation of the real exchange rate. national currency against the main reference currencies [6, p. 30].

For 2018, we attest a considerable decrease of the prices in the industry, which also generated the reduction of IPPI from 3.3% to 0.4%. This evolution was generated by the decrease of the prices for the products delivered on the external market to -0.4%, as well as on the domestic one to 0.8%. In the first half of 2017, the annual rate of prices in the industry registered a slightly upward

trajectory, and later, starting with September, it recorded a downward trajectory. In December, the annual rate of prices in industry was 2.3%, being 1.7 pp. lower than in August 2017 and by 0.5 p.p. that of December 2016. The annual rate of the industrial production price index (IPPI) recorded, during 2016, a downward trajectory, thus, in December 2016, it was positioned at the level of 2.8 percent or 6, 3 percentage points lower than in December 2015. This evolution was influenced by both the dynamics of prices for products delivered on the external and domestic market.

The economic reality attests to the fact that there is no universally valid anti-inflationary solution, each country, depending on its needs, applies the tactics it considers most appropriate, taking into account the nature of inflation, its speed of propagation, its consequences, the type of economy, internal and external socio-political conjuncture, etc.

Among the theoretical approaches of anti-inflation programs we should highlight the concept of "supply economy", which makes it possible to address the additional inflation-related unemployment (which is characteristic of countries with economies in transition) (Table 1).

Table 1

Characteristic features of the "supply economy"

Comparison parameters	Characteristics
Purpose	Impact on aggregate supply
Touch methods	Measures that have a positive effect on current production: - improving the efficiency of the use of production factors; - improving the efficiency of resource allocation by reforming the financial system, the public sector, the labor market, etc .; - developing competition by eliminating trade restrictions, reducing subsidies; - reducing the "fiscal tax" by reforming the fiscal system - reducing the number of taxes, reducing tax rates, increasing the amount of tax benefits. Measures for a long-term increase in production growth: - stimulating savings and investments (transfer of savings to investments); - stimulating the entry of foreign capital in the economy; - creating new technologies; - changes in the field of education (support programs for employment, professional retraining, etc.) etc.
Deficiencies of conception	Fiscal incentives can only increase production in the long run. A reduction in taxes can lead to an increase in consumption and an increase in aggregate demand, exceeding the increase in aggregate supply (which can lead to an increase in inflation and a budget deficit). The return on the additional investment will not be received immediately. In practice, it is difficult to determine when tax rates have reached a critical value, therefore, when tax reforms are carried out, it is likely to make mistakes that involve a budget deficit, etc.

Source: developed by the author

However, in the countries of Western Europe and America, considerable experience has been gained in counteracting inflationary processes, indicating the opportunity for the combined use of short-term and long-term policies as shown in Table 2.

Table 2

The main features of short and long term anti-inflationary policy

Characteristics	Short-term policy	Long-term policy
Objectives	1) reducing the budget deficit. 2) temporary reduction of inflation by: - expanding the aggregate supply without increasing the aggregate demand; - decrease in demand with constant supply	- reimbursement of the inflationary expectations of the population; - reducing the budget deficit. - regulation of the monetary circulation process. - weakening of external factors
Solution methods	- privatization of state property. - mass sale of shares of new enterprises. - providing taxes and other benefits to real sector enterprises. - imported goods. - increase in interest rates on deposits (increase in savings rate)	- changing consumer psychology. - raising taxes and reducing government spending. - establishing strict limits on the annual increase of the money supply. - short-term government loans abroad to finance the budget deficit

Source: developed by the author

Today, a major problem is to combat inflationary expectations, these expectations, which are formed on the basis of ideas about previous inflation (adaptive expectations), lead to the phenomenon of inflationary inertia, when inflation continues to rise even in the absence of supply shocks and a deviation of unemployment from the natural level. According to the theory of rational expectations, economic agents form their expectations based on all available information, which is not limited to past experience. It is assumed that the loss of the state in the fight against inflation can be reduced if a plan for the implementation of the relevant policy is announced in advance (before the formation of inflationary expectations), as long as private actors have confidence in the effectiveness of this policy.

Theoretically, in order to counter inflation, the method of "shock therapy" recommended by monetarists can be used, allowing the rapid reduction of inflation with the help of a narrow monetary policy. To balance this method, the state can use the policy of gradualism, which is a method of gradually reducing inflation through a combination of demand reduction measures and supply stimulus measures as shown in Table 3.

Table 3

Distinctive features of the "shock therapy" method and the policy of gradualism		
Comparison criteria	Shock therapy method	The policy of gradualism
The term of manifestation of a positive effect	The method is designed for a rapid decrease in inflation	The method is designed for a gradual, slow, gradual decrease of the rate of inflation
Applied measures	Monetary measures: - large-scale liberalization of the economy; - price exemption; - cessation of the economic activity of the state; - strict limitation of the increase of money supply; - balancing the budget by reducing social programs	Active state regulation: - supporting the most important industries; - fiscal incentives for business; - partial regulation of prices; - creating a market infrastructure
Shortcomings	Adherence to the method leads to an increase in unemployment, to a sharp decrease in the living standard of the population.	The state's anti-inflationary programs are long-term.

Source: developed by the author

Due to these circumstances, most states are trying to reach a moderate level of inflation. Some countries are trying to control the processes that take place by using adaptation measures.

The adjustment policy is based on the application by the subjects of the market economy of the different methods of adjusting the inflation, allowing to take into account the losses that occur by compensating them. An anti-inflationary policy, in turn, is a strategy for actively combating inflation. Adaptation policies (as well as anti-inflationary policies) can be accompanied by different types of monetary reforms: cancellation, denomination, devaluation and revaluation.

Table 4

Distinctive features of anti - inflationary policy and adaptation policy

Comparison criteria	Adaptation policy	Anti-inflationary policy
Objective	Control of the adapted processes and adaptation to them	Achieving moderate inflation
Essence	Strategy for adapting to inflationary processes	Active inflation strategy
Methods	Income indexation compensation	The set of methods depends on the type of anti-inflationary policy
Applied techniques	Income indexation, taking into account the dynamics of a predetermined index. Adjusted wage inflation. Contracting only for the execution of short-term projects. Looking for additional sources of income Attracting external sources of financing: shares, leasing, factoring. Changes in profit policy, etc.	Regulation of direct and indirect prices. Limiting the level of annual price increases for certain goods and services. Introducing restrictions of the central bank on increasing the money supply and lending volume. Increasing the discount rate of required reserves. Reduced fees. Implementation of government securities on the open market, etc.
Deficiencies	The time interval between the time of the price change and the payment adjustment. Inability to escape inflation	Each type of state anti-inflationary policy has its own disadvantages.

Source: developed by the author

Results obtained

When choosing a particular model of anti-inflationary policy, the Government should take into account the full range of state-specific circumstances. This leads to the idea that in world practice there are two ways to solve problems:

- a tough fight against inflation at state level;
- introduction of a complex of adaptation measures.

Adherents of recognized economic schools - keynesianism [7] and neoclassicism [4] identify as the main objective of the program to overcome inflation the research of the impact on the actual demand of economic agents as presented in the table 5.

Table 5

Typology of government anti-inflationary policies

Characteristic features of the state's anti-inflationary policy	The Keynesian approach	The neoclassical approach
The goal	Impact on actual demand	
The main directions	Active fiscal policy: - use of the tax regulation function; - handling government expenditures.	Monetary policy, which is carried out through the central bank: - changing the value of money in circulation; - changing the interest rate.
Regulatory methods used in excess of demand (recovery)	Increasing the tax burden. Reducing government spending	Deflationary measures: - increasing the interest rate on loans; - reducing the volume of money in circulation
Results	Reducing demand, reducing inflation	
Possible negative consequences	Limiting the increase of production, increasing unemployment, the possibility of stagnation and crisis in the economy	The negative consequences are less because the impact on the economy is indirect and more flexible.
Regulatory methods applied in conditions of insufficient demand (recession)	Reduction of the tax burden (mainly for low and medium income beneficiaries)	Reducing interest rates on loans. Increase the amount in circulation
Results	Stimulating demand, expanding production, reducing inflation	
Possible negative consequences	The use of budgetary methods can, on the contrary, strengthen inflationary processes (confirmed by international experience)	Stimulating economic growth and artificially maintaining jobs leads to a loss of control over inflation.

Source: developed by the author

Conclusions

Researching the relationship between inflation and its indicators of appreciation leads to the conclusion that controlling inflation should be one of the main objectives of economic policy in a developing economy. It is true that, in itself, rapid economic development can cause inflationary pressures. Therefore, one of the issues that needs increased attention from the authorities in a developing economy is the implementation of an effective anti-inflationary policy.

The main objective of anti-inflationary policy is to bring the growth rate of money supply in line with the short-term growth rate of the mass of goods (or real GDP) and the volume and structure of aggregate supply with the volume and structure of long-term aggregate demand.

In conclusion, we would like to mention that inflation is reflected in all areas of social and economic activity of society, so we mention that ensuring price stability and maintaining a low inflation rate is the most important objective of the National Bank of Moldova.

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