

Growth with price stability -- an elusive goal

There are serious limitations to the effectiveness of domestic policies to contain inflation and simultaneously accelerate growth in an open, especially import-dependent, economy. Policy measures should, therefore, primarily focus on providing succour to the poor who are hit hard by inflation.

MIRZA AZIZUL ISLAM

As a poor country, Bangladesh attaches high priority to acceleration of growth. The 2008 election manifesto of Awami League envisages a growth rate of 8 percent by 2013 and 10 percent by 2017. The finance minister's budget speech of 2009-10 reaffirms this target. The high rates of inflation in FY '07 and FY '08 put a sharp focus on price stability.

The first among top five priorities identified in the aforementioned manifesto relates to reduction and stabilisation of prices. No quantified target has been specified in this case. The budget speech implicitly endorses the objective of price stability and talks about ensuring increased supply of consumables through international trade, ensuring competitive environment in the market and protecting consumers' rights by adopting legal measures.

However, there are severe limits to policy actions to contain inflation and simultaneously accelerate growth. At the cost of repeating the simple, well-known proposition it should be emphasised that inflation involves upward movement in the overall price index. Therefore, forces operating both on demand and supply side influence its movement.

The positive components of aggregate demand in an economy are private con-

sumption, private investment, government expenditure and exports of goods and services. The acceleration of growth in Bangladesh demands substantial increase of all these components. At the present low level of per capita income, private consumption expenditure is largely devoted to essential items despite visibly rapid increase in use/consumption of luxury items such as expensive automobiles, air-conditioners and pricey flats. Moreover, most people consider consumption as the barometer of welfare.

There is a paramount need for increasing investment in Bangladesh in order to accelerate growth. The present investment-GDP ratio in Bangladesh is about 24 percent whereas in fast growing China and India the ratios are about 45 percent and 36 percent respectively. The average annual growth of gross capital formation in Bangladesh during 2000-2007 period has been 8.6 percent as against 13.4 percent in China and 15.1 percent in India.

Bangladesh is also a country with undesirably low government expenditure. Among 44 Asia-Pacific countries listed in Asian Development Bank's Asian Development Outlook 2008, Bangladesh had the unenviable second lowest position in terms of ratio of central government expenditure to GDP. Even leaving aside the investment component of government expenditure for meeting the



Keeping a hold on prices.

grossly deficient infrastructure (particularly transportation, energy, education, health, water resources, rural development), an elected political government will remain under irresistible pressure to increase expenditure on social protection net, welfare services and various subsidies.

The last positive component of aggregate demand is exports. It would be patently insensible to bring about a reduction in merchandise exports as a means of curtailing aggregate demand with a view to exerting a benign influence on price stability. The same observation holds with respect to remittances.

The above paragraphs explain why curtailment of aggregate demand is not much of a policy option if acceleration of growth remains an overriding objective.

Supposing that the government takes the politically unpalatable decision to sacrifice some growth, would the reduction in aggregate demand achieve the desired result in terms of price stability?

There are at least two reasons why the result is likely to be disappointing. First, in an open, import-dependent economy, domestic prices are largely determined by international prices.

The variations in aggregate demand would cause corresponding variations in the level of imports, not the price level.

It may be recalled that in a comparatively less import-dependent Indian economy, aggressively contractionary monetary policy did not have much beneficial impact on inflation in 2008.

Second, contractionary monetary and

fiscal policies to contain aggregate demand may have an adverse impact on domestic supply conditions through reduction in import of raw materials, intermediate goods and capital machinery, as well as aggravation of infrastructural bottlenecks. It should be noted that much of production-related infrastructure (energy, transportation etc.) is provided by the government in Bangladesh.

In 2008, I pressed the above arguments forcefully in several rounds of discussion with IMF, who eventually yielded to the logic and did not insist on contractionary demand management policies.

On the supply side, the two sources of supply are imports and domestic production. As regards to the former, Bangladesh being a small country in the global market cannot exert any influence on the import price level through domestic policy measures. As regards to domestic production, the most important item is food grain, the price of which carries nearly 60 percent weight in the estimation of consumer price index (CPI) -- the most widely used measure of inflation. As in the case of aggregate demand, it can be argued that in an import-dependent economy, the variations in domestic supply (meaning shifts in supply curve) would bring about changes in the level of import, not in domestic price level.

In the very short run, there may be some benign impact because marginal farmers who do not have much of holding capacity may be forced to sell at low prices immediately following the harvest.

Eventually, however, price will veer toward import price level, import being the only alternative option for consumers. The recent increase in the price of rice

despite two successive bumper boro harvests illustrates this reality. The situation may change if the country becomes a surplus producer. However, even in that case, outward smuggling, if export is not officially allowed, would tend to bring about parity between international and domestic price level.

In light of the above, I recently undertook a simple regression analysis using import price index and food grains per capita production index as the explanatory variables for consumer price index over the last 9-year period. In both simple and log-linear forms, a statistically significant, high and positive coefficient of import price index is found. One percent change in this variable causes 0.94 percent change in CPI. In contrast, the coefficient of food grains production index turns out to be statistically insignificant.

The above analysis suggests that there are severe limits to the effectiveness of domestic policies to contain inflation while trying to accelerate growth. It is not, therefore, surprising that successive governments in Bangladesh have been pursuing expansionary fiscal policy and accommodating monetary policy. The justification for providing subsidies to food grain production arises from the need to reduce dependence on import, not from its impact on the price.

However, it is well known that inflation hits the poor hardest. It is, therefore, essential that the government maintains or even expands social protection net till acceleration of growth brings about a sharp reduction in poverty. Successive governments of Bangladesh have also actively pursued this approach.

Mirza Azizul Islam, Ph.D. is former Adviser to the Caretaker Government, Ministries of Finance and Planning.

Will scrapping of election create new complications?

Certainly, under Karzai social and economic progress is discernible, but a weakening and corrupt administration, likely non-cooperation from Dr. Abdullah and his supporters, and combating the ever-increasing threats of the insurgents pose bigger challenges for him.

ZAGLUL AHMED CHOWDHURY

HAMID Karzai has been declared president of Afghanistan for the second term following scrapping of the run-off elections by the Election Commission. This set at rest all speculations about the presidential polls in a country which is already in tatters through war and internal strife.

The run-off election for a new president was scheduled for November 7, but the challenger, former foreign minister Dr. Abdullah Abdullah, withdrew from the second round of voting fearing a repeat of the "massive malpractices" that marred the elections on August 20. This leaves the election without any significance since the run-off polls was between two top candidates only. The Election Commission said that it was scrapping the balloting since the challenger had withdrawn, and declared Karzai as the automatic winner.

The curtain has now fallen on a tumultuous chapter in the present Afghanistan surrounding the presidential elections that raised a lot of dust over the last several weeks because of a variety of reasons -- mainly allegations of massive fraud in the voting in favour of the incumbent president Karzai. But questions will obviously be raised whether this denouement of the much-awaited and much-talked about Afghan presidential election will help strengthen democratic edifice and attain stability for the trouble-torn nation.

The United Nations and Western allies of Kabul were also convinced that the polls were not free and fair even though Hamid Karzai was insisting otherwise. Because of intense pressures from home and abroad, the president had announced that the embattled nation would have second round of polls on November 7. Indeed, the decision was welcomed since the August 20 voting was largely seen as having been influenced by the administration and supporters of the incumbent president.

His main rival, Dr. Abdullah Abdullah

had been clamouring for the run-off polls,

charging the president of large-scale irregularities in the balloting. Initially, Dr. Abdullah also expressed readiness for contesting the run-off polls but backed out later, citing fears of the "same experience" of August 20 polling. That decision came somewhat as a surprise as Western nations and the United Nations were keen for the second round of balloting.

Dr. Abdullah might have sensed that the run-off polls were unlikely to give a verdict in his favour. Besides, the visit to Kabul by UN Secretary General Ban Ki Moon might have also given him the signal that Karzai had international support despite allegations against him of corruption and mal-administration. The message was probably that Karzai has steered the country through difficult times since the drastic change of the Afghan scenario, and he is needed for coming years as the country is still grappling with myriad problems.

The outcome of the presidential elections hung in the balance for several weeks and it seemed that incumbent President Karzai was heading for the victory in the disputed voting. Unofficial results showed Karzai was ahead of his nearest rival and secured more than the required 50 percent of the secured votes, avoiding a run-off election in the French style. But the whole exercise was embroiled in uncertainty because of allegations of massive rigging and malpractice, which reduced the otherwise important election to a controversial event.

The presidential elections, the second since a sea-change took place in the political landscape following the toppling of the Taliban regime in 2001, was billed as a development that was expected to strengthen the democratic edifice of a country whose history of recent decades is replete with violent developments. The country witnessed presence of foreign troops in large number in contrasting circumstances on one hand and infighting among various groups in a typical milieu of the Afghan scene on the other.

The presence of foreign troops is nothing new in the country. The troops of the former Soviet Union remained in the country in the eighties to support the leftist Kabul government against their Islamic opponents aided by the United States and other Western countries. The Soviet troops left the embattled Afghanistan after ten long years without succeeding in their task.

It is the United States that threw its entire weight behind the Islamic forces against the Soviet-backed Kabul government. Paradoxically, it sent troops to Afghanistan several years later to fight broadly the same Islamic forces -- albeit more radical and militant in nature. Certainly, the dispatch of the American and other western soldiers to Afghanistan in the aftermath of 9/11 in the United

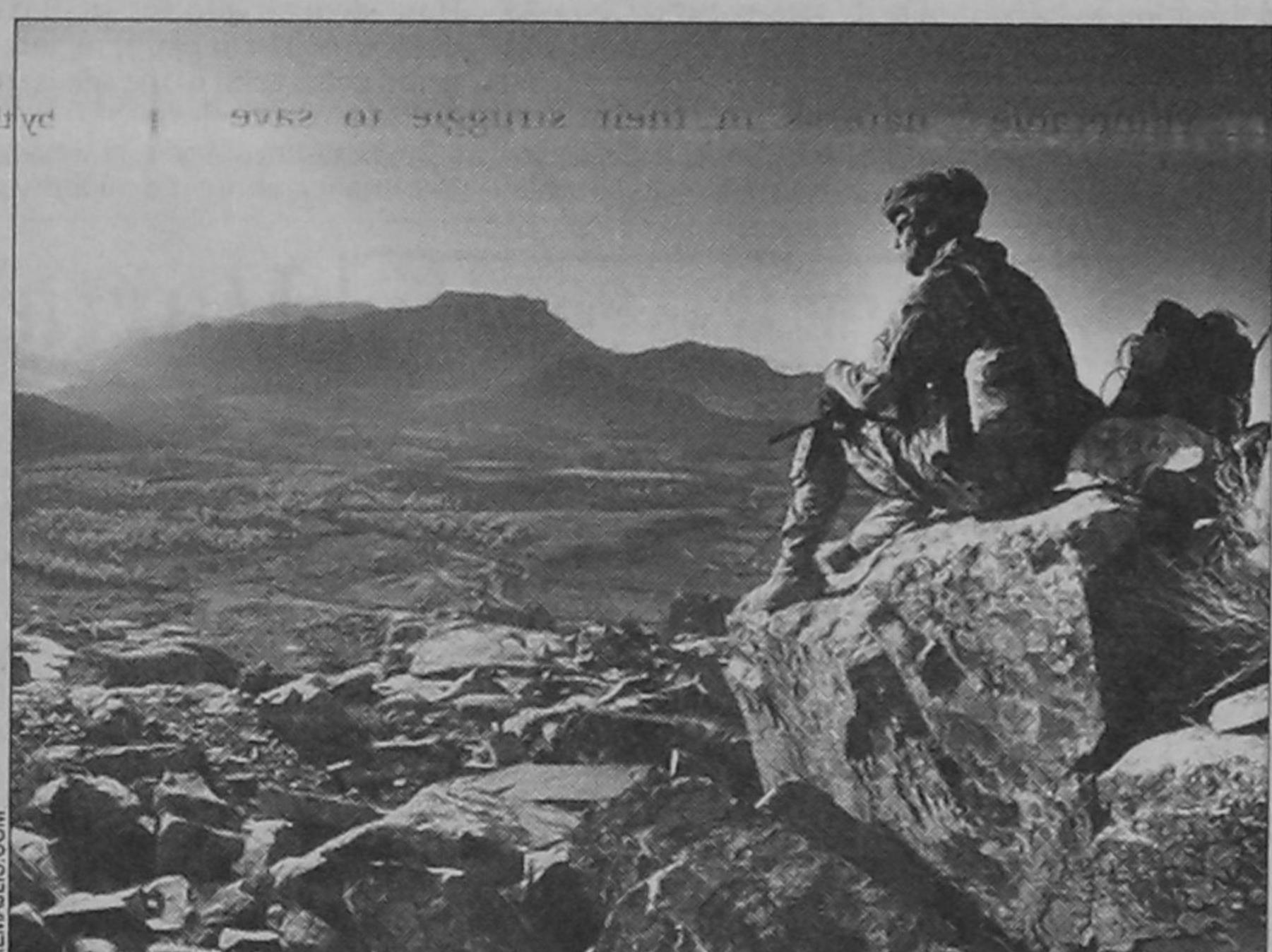
States was largely seen as justified, and the soldiers still remain in the trouble-torn country. More than one lakh soldiers are now fighting the opponents of the Karzai government as peace and stability still elude the nation.

Definitely, Karzai has been the key figure in the Afghan imbroglio for the last several years, and has spared no efforts in leading the country through an extremely tough phase. But his presidency has also seen his countrymen getting disenchanted with him on a variety of matters, like rise of corruption in the higher echelons of the administration. Besides, violence and resistance to the government and its supporters do not seem to be slackening, causing frustration in the people.

Abdullah Abdullah is an experienced person, familiar with the nitty-gritty of Afghan politics and characteristics as he was involved in different crucial phases. He was active during the Soviet-influenced period, being close to legendary guerrilla commander Shah Ahmad Mosood, who later also fought the radical Taliban. Abdullah is also known to different countries, being the foreign minister, and is widely seen as being largely successful in his job. He is a Tajik and from the south while Karzai is from north, with influence over the Pashtuns.

Their rivalry centering the elections has also created undesirable tension between the south and the north among the ruling circles. A run-off election would have further widened this rift and increased acrimony. The supporters of Afghanistan were clearly worried about such a development and now must be heaving sigh of relief over the "dignified back-out" of the challenger.

The United States and its allies have great stakes in Afghanistan, and have tried to minimise the differences and acrimony, centering the elections, among the anti-



Back to square one?

Taleban base. That is exactly what they have done in the last several days, following a flurry of negotiations with Hamid Karzai, his main challenger, and other relevant quarters.

President Barack Obama, who is under pressure from military commanders and Republicans to dispatch more troops to Afghanistan to fight the Taleban, congratulated Karzai for winning a second five-year term in office but called for curbing corruption and working for a healthier society in Afghanistan, which has received billions of dollars as assistance in the last few years. French President Nicholas Sarkozy and other Western leaders echoed the same.

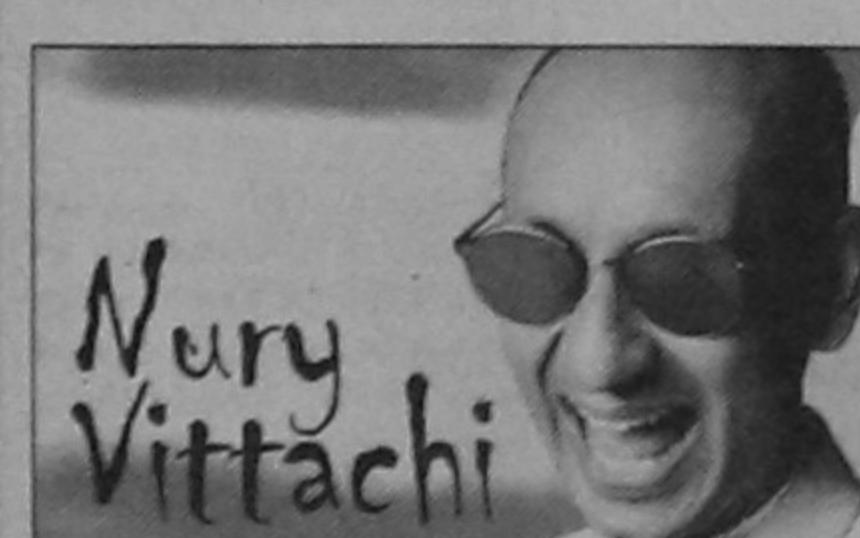
Karzai is now faced with the greater challenge of delivering the goods and can ill-afford failure, particularly on two fronts -- corruption and effective fight against the Taleban. In his first speech after being announced as the president for the new

term, he vowed to eradicate corruption and also offered the olive branch to the Taleban, who, however, are unlikely to respond to his gestures.

The severity and complexities of the Afghan tangle are such that Karzai is entering a more crucial and difficult phase. Certainly, under him social and economic progress is discernible, but a weakening and corrupt administration, likely non-cooperation from Dr. Abdullah and his supporters, and combating the ever-increasing threats of the insurgents pose bigger challenges for him. It remains to be seen how he really confronts this situation after becoming president again, which may remain questionable as far as the legitimacy of the election is concerned.

Zaglul Ahmed Chowdhury is a senior journalist and analyst of international affairs. Editor@thethedailystar.net

The crime writer's secret



When we sat down at Oliver's Super Sandwiches, he explained that he had been commissioned to write a crime screenplay by an Asian movie house and needed advice from someone with experience in the genre.

"Congratulations," I said. "You seem well on the way to making crime pay."

He gave an uneasy smile. "Yeah, but there's a problem. The commissioning editor says there must be no crime involved."

Ah. Got it. What he meant was that some or all of the money for the movie was coming from a state film commission.

Here's a trade secret. Why are Asian films not successful internationally? Most people think it's because they are

rubbish. In fact, this is true. They are rubbish in many cases. But there's another reason: state film commissions in Asia have secret rules. No crime in crime stories. No ghosts in ghost stories. No corrupt officials in settings where corrupt officials can be found wall-to-

wall. This makes film-making an interesting challenge. What edge-of-the-seat action-adventure stories do you like to see? Exciting, successful action stories inevitably feature embezzlement, treachery, gun-running and the usual type of murderous activity which passed for "office politics" in some of the school boards I've sat on.

Writers are stuffed. In the classic suspense model, crimes are solved by maverick detectives who have just been told by their chief: "You're off the case: hand in your badge."

Asian Film Commission model:

think that even suggesting that "crime exists" is going too far.

In Singapore, crime stories are not forbidden, but budgets are low and fear of authority is high. Screenwriters tell me that they don't have the cash to build sets of police stations or jails, and can't get access to real ones without full co-operation with the authorities.

Result: no negative portrayals of authority figures.

Classic crime-writer model: Detective says to his junior, "Remember. Evil often emerges where some people might least expect it: from slick, rich, smiling, successful individuals who make up the elite."

State Film Commission model:

Detective says to his junior, "Remember. The elite are sinless and trouble

comes from foreigners and other minority groups."

This makes it difficult for people on the Eastern side of the planet to create the next Godfather or Scarface.

This is an industry secret, so it's strictly between you and me, dear reader.

But I've often thought that one-day filmgoers will suss it out, realising that certain countries never produce films dealing with subjects such as government corruption.

Or maybe not. All filmgoers with taste are in the movie house next door, watching All The President's Men.

With me.

Pass the popcorn.

Visit our columnist at www.vittachi.com