

Inflation and monetary policy

Business



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Zero Inflation Inflation is concerned with the rise in the price in the goods and services in a local economy, which reduces the buying power of the individuals. For many governments, inflation is considered as a sign of economic development. At the same time, governments set up limits, where as inflation percentage exceeding a predetermined level will cause serious threats to the economy.

Many factors are considered to be the main cause of inflation. The worst cause of extreme rise in inflation is observed when governments attempt to print excess amount of money in order to recover the already increased inflation. Resultantly, they end up becoming another cause of prices getting even higher. Consequently, inflation gets even higher. Among other causes, rise in production costs, and excessive international lending and borrowing. Governments aim to controlling inflation as their primary economic concern, and do help the domestic economy through various means to inflation rise but at a controlled pace. Most of the countries believe in zero inflation phenomenon, but the economic history suggests that inflation leads to the economic development. Therefore, the countries tend to make the policies which make inflation rise but at a controlled pace, so as to create a balance between zero inflation scenario and worst inflation causes. Additionally, most of the economists believe that the inflation should be relatively low, but they do not rule out the possibility of inflation completely wiped out of an economy. This means they do desire the inflation to be the integral part of the economy, and tend to avoid the state of zero inflation. Therefore, most of the economists do have the consensus about inflation of x% rather than that 0%.

The Federal Reserve must understand the inverse relationship between

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inflation and unemployment, i. e. rising inflation will cause lesser unemployment. This has been represented through 'Phillip's curve', which suggests that the zero inflation case would consistently cause the unemployment levels to rise. There has historically been observed to be a stable relationship between high but controlled inflation and lesser unemployment rates.

During 1950s in US, the economists were of the opinion that positive inflation rate was enviable. This period was also noted as a stable one as the economy experienced an inverse relationship between unemployment rates and inflation. On the other hand, the economists suggested that a case of zero inflation will cause the unemployment rates to get higher. In this scenario, the economists started searching for the middle approach instead of implementing zero inflation policies as the middle approach would balance the unemployment rates to a minimum level, where the economic development is also achieved at a desirable rate due to rising but controlled inflation.

It can therefore be argued that the Federal Reserve should not opt for the zero-inflation policy as it would result in the unemployment levels to rise as was the case in 1970s and 1980s in USA. The Federal Reserve should rather aim for controlled inflation which should be set by the economists considering the economic circumstances facing the country, but it must be kept sure that the inflation rises must also be limited.

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