Stagflation

Description

Theme:

- In June 2022, the world bankâ€™s latest report warned about the increasing risk of global stagflation.

What is stagflation:

- Stagflation is a scenario in which both inflation and unemployment rate are high.
- Till the 1970s, it was believed that inflation (increase in prices) and unemployment are inversely proportional. Because, if the unemployment rate is high, common people have low purchasing power, and hence the demand for goods reduces, thereby the prices will either reduce or stay constant. When the unemployment rate is low, most people will have jobs and common people will have money to spend, and hence demand increases, thereby the prices.
- In general, if inflation is high in any country, the central bank of that country raises interest rates. Then borrowing becomes expensive. So, people and companies will spend less money and thereby the demand for goods decreases and as a result, prices will decrease. But as a consequence of this, companies cut jobs to survive and hence the unemployment rate will increase.
- In the 1970s, a few countries including the US, and the UK faced high unemployment rates and high inflation at the same time. This situation is named â€˜stagflationâ€™ (stagnant economic Â growth + inflation). This is a tough situation for the economy because low or stagnant economic growth cannot create jobs, and steps to reduce inflation will further worsen the unemployment issue.

The present situation worldwide:

- The covid pandemic has severely impacted the global supply chains and caused the global economic slowdown. As the world economy is trying to recover, high oil prices along with Russiaâ€™s invasion of Ukraine are increasing the risk of slow global growth and stagflation.

How to control stagflation:

- Raising interest rates to reduce demand can reduce inflation and will also increase unemployment rates. It can lead to a global recession. But this will be better than reducing the unemployment rate and further increasing inflation because, in the long term, the high inflation will cause an increase in the unemployment rate and the economy can collapse.
- Increasing supply to meet the demand can also help in reducing inflation and hence controlling stagflation. For example, increasing oil supply by investing more in its production can reduce oil prices globally. A decrease in fuel prices can reduce the commodities prices as transportation costs reduce.

Conclusion:

Stagflation is a scenario in which both inflation and unemployment rate are high. This is a tough situation for the economy because low or stagnant economic growth cannot create jobs, and steps to reduce inflation will further worsen the unemployment issue. Stagflation can hit world's poor hard. So, governments should protect vulnerable population through welfare schemes.

Your Turnâ€¦

What are your thoughts on 'stagflation'? Express your point of view through the comment section below. And subscribe to our blog to read answers to the trending GD topics.

References:

- **Explained | How are fears of stagflation impacting markets?**
- **What is stagflation? Hereâ€™s why it matters and what you should know.**
- **Stagflation? There are big differences between the 1970s and today**
- **What is stagflation, and should we be worrying about it?**