The causes and the effects of the inflation

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Abstract: *The inflation represents the result of the economical, monetary and socio-political factors seeing through the inter-conditioning and simultaneity of its action having as functions: the elimination (revalorization) of the superadded capital, the profit's-dimension and the redistributions of the national income in favor (disfavor) of one category or another of producers or consumers.*

That is why, the measures of the economical politics that are promoted must target first of all the minimum reduction of the distortions, of the inequities and the sacrifices paid for these situations, taking a good care for the big number of the consumers.

Key words: inflation, hyperinflation, disinflation, budgetary deficit, monetarism, unemployment.

1. The form of the inflation

The word inflation comes from the Latin "inflare" which means to exaggerate. As economical phenomena inflation seems to appear for the first time around 1300 in France during Phillip The Beauty reign. Because he was needed financial resourced for the war with England, after he spent all his money, he recourses to the monetary emission, which serves him for his purposes. The first explanation about the inflationist phenomena has as basis the quantitative theory of the money. This explanation was possible because it is determined by two essential factors: the movement of the monetary gold and the agricol production modification.

Inflation has a long story, which evolved during the centuries with unequal intensities and sense changing.

The inflationist phenomena has appeared for the humans since the beginnings under different forms, which have affected in some ways the right course of the economical, social and political life.

In the specialty literature the inflation has as a definition: the general raise of the prices when the buying power of the market actors (including the population) is decreased. Or the prices of the goods and of the services are rising, the quantity of currency (real and in cont) rise and the buying power for a monetary unit decrease.

Inflation is the process of significantly and persistent rise of the prices' level. Inflation represents a state of economic disequilibria where the existent monetary mass in the economy overwhelm the real necessary of currency going to a generalized rise of the prices and to the buying power decrease of the money. Not only rise of the money means inflation. Inflation is, first of all, a monetary phenomenon, being related to the abundance of money over the real needs of the economy, determined by the decreased goods and services offer.

Generally, the quantitative theory is considered as the classical or neoclassical theory of the inflation. (The wells known classical economists were: Adam Smith (1723-1790), David Ricardo (1772-1823). The neoclassical term is referred to the L. Walras (1843-1910), A. Marshall (1842-1924) and A. C. Pigou (1877-1959) writings). In the frame of the neoclassical theory, the quantitative theory plays a different part from those played in the frame of the classical theory.

When Spain discovered the New World and the gold started to flow form Mexico and Peru, in the entire Europe have been recorded prices increase. There were more money in the circulation but the same quantity of real goods, so the money worth less and the goods more.

This type of experiences has determined the economists to see a mathematical relation between the quantity of active money, the goods prices and the quantity of products goods. This relation was called *the trade equation*, because it tried to explain the goods exchange in a free economy. Irving Fisher (1920) perfected the equation taking also into consideration the speed of the money.

The quantitative theory explains the report between the monetary quantity and its value, a larger active quantity reduces the value of the monetary signs (increasing the goods prices) as the active quantity reduces as its value rises and the prices of the goods are reducing.

Inflation is a negative phenomenon, which affects the economy on both long and short terms. On short term, denudes the buying power of the currency and through this affects especially the most vulnerable citizens, those with fix incomes. On long terms, inflation discourages the investments and inhibits the economical growth.

On long term, the inflation is presented in every economy. The phenomenon cannot be totally controlled and at the same time it is not advantageous for everyone. Those who anticipate correct the evolution of the inflation can always find ways to become rich in spite of the other who cannot.

A conception regarding the explanation of the inflation refers to the monetary theory[1]. The monetary thinking appears from the quantitative theory of money, but its area is beyond that. Karl Brunner introduced the term "monetarism" in 1968.

In the monetarists works (Milton Friedman, Karl Brunner, A. Meltzer, H.G. Johnson, D.E.W. Leidler, M.J. Parkin and others) the leading part was played by the inflations

[1] **Elena Pelinescu,** *"Monetarismul – abordare teoretică și aplcații. Cazul României"*, în Anale, Institutul Național de Cercetări Economice, Academia Română, INCE, CIDE, București, 2001, p.45-70.

explanations.

Inflation is a monetary phenomenon. In 1970, Friedman said: "Inflation is everywhere and always a monetary phenomenon…and can be determined only by a rapid raise of a money quantity than of a production".

A rapid raise of monetary mass will develop a prices raise. It is true that the monetary aggregates are not a perfect indicator to describe the state of an economy, but on the long terms the relation between money and prices will remain intact. Moreover, this relation is analyzed in the studies done by the European Central Bank, which demonstrates that the dynamics of the monetary mass contains information referred to the inflation. Economical history is full of examples in which those agents working with the implementation of the economical and monetary politics had been ignored the signs given by the monetary mass. The Great Crises from 1929-1933, the hyperinflation from 70's, the financial collapse from Japan in 80's and the Asian crises from 1997. All these crises were preceded by rapid raise of the monetary mass. We can introduce the idea that between the monetary mass and the inflation there is a direct relation.

Monetarism sustains that the market economy equilibrium can be done, almost automatically, using an official control of the active monetary mass.

Because of the importance that Friedman and his disciples allowed to the monetary politics, their economical thinking became known as the "monetary school". It can be defined as an economical school that provides the importance of changing from the real production and the price's level.

Milton Friedman, mentor of Chicago School, recognizes the need to use a governmental measure rational limited required by the economy recover at a certain point. State must not interfere in the domains and problems that the free market can successfully resolve. It must intervene only when and where, without his support, the problems cannot be resolved.

Monetarists believed that the market economy functioned in every condition but recorded success only when it is left alone.

2. The cauze of the inflation

The causes of the inflation are defined differently in the economical literature. These points of view could be framed in two groups: I. Adepts of the monetary inflation and II. Adepts of the nonmonetary inflation.

The first conception has at the basis of the inflation factors that act around the monetary circulation and especially it's mass. This conception corresponds to the classical explanation of the inflation, which has seen the cause of the inflation in the abundance of monetary mass irrespective to the currency forms that compose it, that attracts the price rise- explanation given by Davanzati and especially Jean Bodin in XVI century and carried on by the Chicago School through Milton Friedman.

Milton Friedman makes a distinction between the immediate causes and long term causes of the inflation. On ling term, it is considered as immediate cause of the inflation the rapid raise of the monetary mass than the production raise. The question is: where this raise comes from?

The answer given by Friedman reflects the monetary conception regarding the inflation:

a) The first cause is the government wish to spent more than it collects, to rise the public expenses without rising the tax, without benefits the supplementary incomes.

b) The second cause of inflation is the government wish to reduce the unemployment and to assure "full occupancy", which gave birth to the politics with the same name. If the government raises the public expenses to create job placements the inflation appears.

c) The third cause mentioned by Friedman is the wrong politics of the Central Bank. So, the Central Bank, wishing to maintain the interest rate for certain limits, it raises the monetary mass and it provokes inflation, which develops the growth of the interest more than if it wouldn't require the monetary mission. The raise of the interest discourage the private investments and its reduction stimulates the income reduction a well being phenomenon known as eviction effect.

For the contemporary supporters of this conception, the control of the inflation must be realized through pressure measurement over the monetary mass, reducing it with the help of some restrictions of the credit and interest domain.

Taking into consideration the period of the First World War and what followed – the irreversible break down of the gold etalon from all over the countries at the same time with other changes in the economical mechanisms – especially after the Second World War- it marked an important accenting of the inflationist phenomena and a very powerful raising of the prices slowed down in the 90's. Under this situation, the quantitative theories over the currency, the monetary explanations of the inflation were no longer efficient and that is why, the analyst attention was drawn more upon the real processes of great depth, non-monetary.

The non-monetary causes are:

- The solvent demand pressure face to the economy capacity (global offer) stays;
- The production cost pressures, following the continuum rise of the prices' factors, especially of the salaries (as an effect of the union's pressure);
- The psychological factors which determine the transactional participants to take cover measures for inflation at the previous level rate – salary and prices rise.

Among the deep causes of the inflation we can find: the disturbance of the supply and demand report, where we can have either an excess demand or an adverse supply.

3. The effects of the inflation

Some economists believe that the moderate inflation can be accepted by the contemporary society, and others, especially the monetary economists, which share the same point of view as the International Monetary Fund, discourage the inflation by recommending stable prices and salaries. The monetarists consider the inflation as a scourge, a malady harmful for the society, a public enemy.

We must distinct between the impact of a moderate inflationist process and that of an excessive inflation escaped over the macroeconomic control.

Some effects generate by inflation.

a. Inflation has as effect the diminishing of currency's buying power.

b. Inflation distributes the existent wealth and modifies their meanings.

c. Inflation affects negative the uses of the economical resources of the society, because are neglected activities of great importance for the achievement of a general economic equilibrium.

d. The inflationist rise of the prices diminishes the life level of the employed, pensioners with fixed and reduced incomes.

e. Inflation stimulates general unbalance for the national economy; the economic instability does not encourage the productive investments but contrary, it stimulates the speculative ones.

f. Inflation has an impact over the external economic relations, especially for the states with unconvertible currency.

g. Hyperinflation leads to the decay of the civil society in general; stimulating the middle class poverty, it undermines the impose system, generates corruption and degradation of the social institutions.

As conclusive, by its effects, inflation was and still is a negative phenomenon. That is why; the society tries to elaborate anti- inflationist strategies to adhere at the accomplishment process of slowing down the inflation (disinflation)

4. Who is responsible for the romanian inflation?

The state is responsible for the inflation. Governs declare that the inflation is a scourge which must be eradicate. The state is not out the inflationist game. Anticipating the prices raise, raising the taxation, raising the social contribution rate, the state revives deliberately the prices raise.

The banks are also responsible. The banks lent the industry and the private. It receives and manages their deposits. The interest rate collected followed the prices dynamics.

The Romanian National Bank took the decision to increase the monetary politics interest by 50 base points, from 7% to 7,5% and to leave unchanged the levels of the minimum compulsory reserves, both for the foreign currency liabilities (40%) and those in Ron (20%), of the banks to save as much as possible in the battle against inflation.

The Romanian Central Bank Governor launched a warning for the government: " Do not pull off this economy because it's broken! We cannot have salary and pension raised and the reduction of the taxation at the same time, we must develop a priority list".

The acceleration analyzed at the annual rate level of the inflation was generated in 70% by the volatile prices, the annual dynamic reached in September 2007 outrun by 10,9 % the value from the middle of the year. The determinant factors include on one hand, the tension induced by the drought of the vegetables and fruits market- not only internal, but also regional-, and on the other hand, the base effect associate to the abundant harvest of the previous year. A favorable influence exerted the deceleration by 1,9% of the annual raise rate of the fuel price (to –0,7%) where the recent tendency of increasing the price of petrol on the international market have not yet produced significantly movements on the internal market.

Conclusions

Contemporary inflation represents a structural unbalanced monetary-material, which expresses the gold convertible money's depreciation and of those unconvertible in general and the length and generalized rise of the prices that can be identified as an existence in circulation of a monetary mass that overcomes the economy needs.

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