Research paper

Forum: 2nd committee – Economic and Financial
Issue: Using different economic approaches to decrease inflation
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Background

In early 2021, global inflation began to spike. Various possible causes include pandemic-related financial and monetary stimulus, supply shortages (including chip and power shortages), price hikes, and Russia's invasion of Ukraine in 2022. A debate arose as to whether inflationary pressures were temporary or persistent. Many countries are experiencing their highest inflation in decades, and central banks are responding with increasing interest rates. Some economists argued that upon emerging from the COVID-19 recession consumers significantly shifted spending to goods compared to services. This shift placed stress on supply chains such that the supply of goods could not meet demand, resulting in price increases.

Current state

While most countries saw a rise in their annual inflation rate during 2021 and 2022, some of the highest rates of increase have been in Europe, Turkey, the United States, and Israel. In Mexico, for example, annual inflation increased to 8.2% in July 2022, the highest rate in more than 20 years. Similar upward trends are observed in Brazil, Colombia, Egypt, Indonesia, and South Africa. Growth in the world's three largest economies—the United States, China, and the European Union—is weakening, with significant spillovers to other countries. At the same time, rising government borrowing costs and large capital outflows are exacerbating fiscal and balance of payments pressures in many developing countries. In July, the euro fell below dollar for first time in 20 years, mainly due to fears of energy supply restrictions from Russia. In August, Eurozone inflation hit 9.1%, the highest ever since the creation of the euro in 1999. Some regions in Europe faced public discontent and strikes due to the inflation surge. In September the ECB raised the interest rate for a second time in the year to 1.25%. Inflation in many large developing economies has also accelerated and is now generally well above the comfort zone of the central banks. The impact of rising living costs is much higher in the least developed countries with a large share of their population already living in poverty. The food crisis will likely increase the number of people living in extreme poverty.

Concerns

Soaring energy and food prices are hurting the lower-income consumers in developed economies and most people in developing economies, with consumer confidence hitting a record low in July, falling even below the level at the beginning of the pandemic.

A potential total shutdown of Russian gas during the upcoming winter could lead to severe energy shortages and likely push Germany, Hungary, and Italy into recessions.

Food prices remain close to record highs, surpassing levels seen during the global food crises of 2007-2008 and 2010-2012, which sparked worldwide protests, particularly in Africa. A recent agreement between Ukraine and the Russian Federation to allow the resumption of grain exports from Ukrainian ports provided some relief, but its duration remains uncertain, and the conflict still weighs on Ukrainian agricultural production. The war is also contributing to high energy prices, which will affect forthcoming harvests as farmers cut back on sowing and planting given the high cost of running farm equipment, transportation, and fertilizer. For example, food insecurity has intensified in Ethiopia, Nigeria, and South Sudan. A few developing countries are implementing or considering food export restrictions (e.g., India, Indonesia, Malaysia), which in turn will raise the cost of food imports for others.

Possible solutions

- Support for local producers
- Contractionary monetary policy
- Providing support to low-income population

Terms

- *Inflation* - the rate of increase in prices over a given period of time.

Inflation is typically a broad measure, such as the overall increase in prices or the increase in the cost of living in a country.

- *Contractionary monetary policy* - type of monetary policy that is intended to reduce the rate of monetary expansion to fight inflation. The policy reduces the money supply in the economy to prevent excessive speculation and unsustainable capital investment.

Main countries involved

- Russia
- United States
- Germany
- China
- Eurozone countries

Links

https://www.un.org/development/desa/dpad/publication/world-economic-situation-and-prospects-september-2022-briefing-no-164/
https://tradingeconomics.com/country-list/inflation-rate