



PIDE-Inflation Expectations Survey

Vol. 2, No. 4/2010

According to PIDE inflation expectations survey experts are expecting high inflation and high unemployment and stagnant growth during the current financial year. Current stance of monetary policy is considered as ineffective to control inflation. The results of inflation expectations survey reveal that vast majority of the respondents expect much higher inflation than the current year target (9.5 percent). According to the respondents, persistent high inflation, reformed GST, policy credibility and law and order situation are the major factors driving high inflationary expectations.

1. Introduction

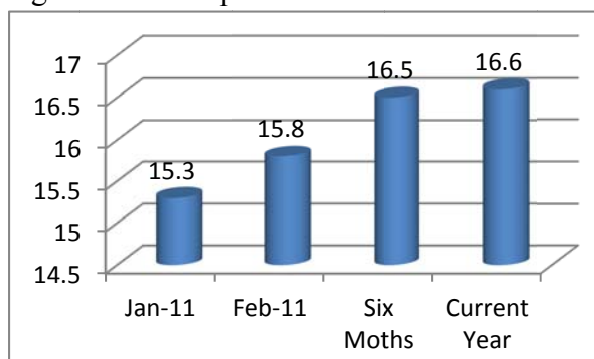
Price stability is considered as the prime objective of the Central Bank. High inflation reduces welfare and growth by reducing investment and productivity growth. Currently Pakistan's economy is facing serious problems of high inflation, high budget deficit and low economic growth. Increasing tendency of government borrowing from SBP to finance the deficit and proposed implementation of reformed GST are feeding the public expectations about future prices. Reduction in inflation expectations take a long time to occur with a track record of good performance of the important indicators of the economy.

2. Inflation Expectations

Based on the PIDE Inflation Expectations Survey, conducted in December 2010 inflation expectations remain high. Respondent's expectations about inflation are 15.3 percent

for the month of January 2011 and 15.8 percent for the month of February 2011. Majority of the respondents indicate that on average 16.5 percent is the expected rate of inflation for the next six months and 16.6 percent for the current year (Figure: 1). Moreover, in view of 97 percent respondents inflation will be higher than target rate of 9.5 percent set by the authority for the current year.

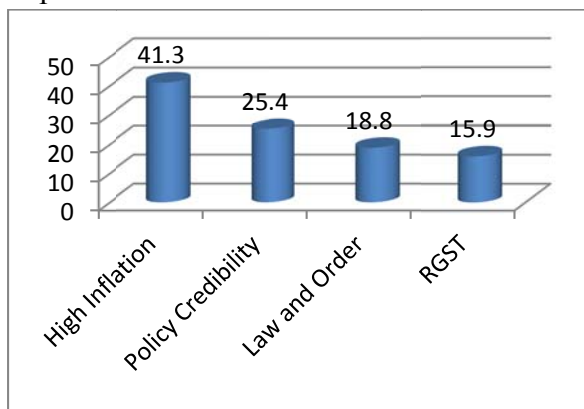
Figure: 1 Expected Rate of Inflation



High inflationary expectations are due to persistence of high inflation, policy

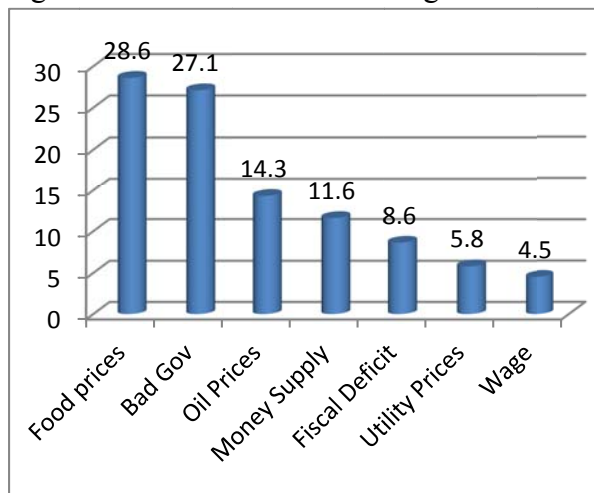
credibility and law and order situation prevailing in the country and reformed GST. As shown in figure 2, according to 41.3 percent respondents persistent high inflation is the major cause of high inflationary expectations followed by policy credibility (25.4 percent), law and order situation (18.8 percent) and 15.9 percent consider the introduction of R-GST as an important factor for high inflationary expectations.

Figure2: Factors Responsible for Inflationary Expectations



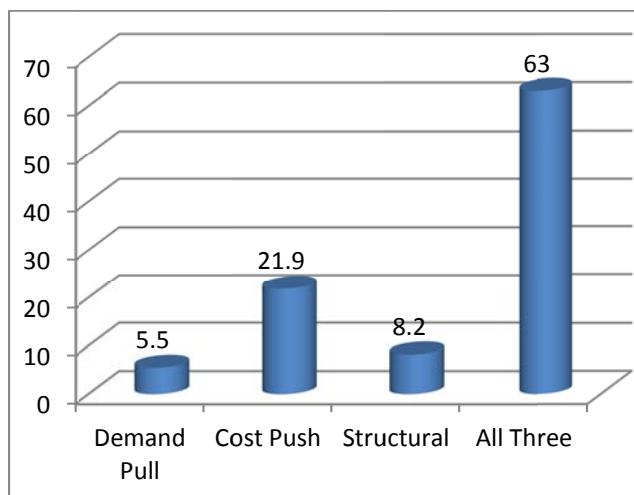
Among the important factors responsible for current inflation it was indicated that food prices (28.6 percent) followed by bad governance (27.1 percent) and oil prices (14.3 percent) are the main causes of the high inflation. Utility prices, fiscal deficit, money supply, international inflation, wages, property prices and gold prices are also considered as driving forces for high inflation.

Figure 3: Causes of High Inflation



In response to the question about nature of current inflation, 21.9 percent respondents believe that it is cost push inflation while 5.5 percent says it is demand pull inflation. In view of 63 percent all three i.e. demand pull, cost push and structural reasons are behind the current price hikes. (Figure 4)

Figure 4: Nature of Current Inflation

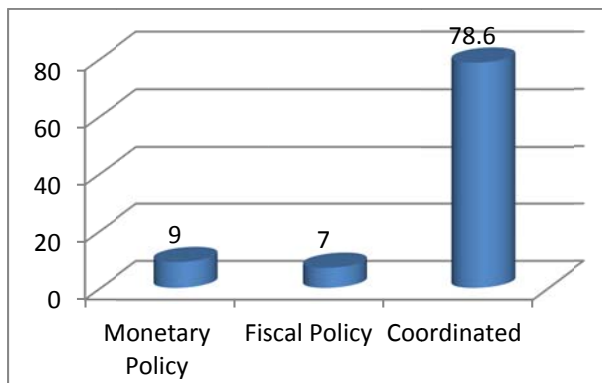


3. Monetary &, Fiscal Policies and Interest Rate

Inflation expectations play a vital role in setting and conducting monetary policy in modern times. Inflation expectations reflect the credibility of the monetary authority's commitment to the objective of price stability. The effectiveness of monetary policy is likely to be greater if inflation expectations remain anchored. A persistent rise in expectations causes the heightened inflationary pressures, so monetary authority needs to understand how inflation expectations are formed.

Survey results indicate that current monetary policy practiced by SBP to control inflation is ineffective. Vast majority of the respondents (78.6 percent) suggest that both monetary and fiscal policy should be used simultaneously to control inflation rather than rely only on monetary policy. In response to the question about the suitability of current policy rate (14 percent) to control inflation, vast majority of expert clearly indicate that it is not suitable to control inflation in Pakistan. Current monetary policy rate is considered to be higher by 60 percent of the respondents (Figure 5).

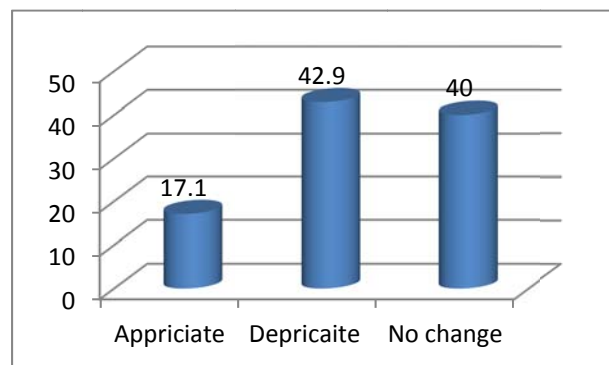
Figure 5: Effectiveness of Monetary and Fiscal Policies



4. Exchange Rate

About 42.9 percent respondents think that the value of domestic currency will depreciate in the month of February, while 17.1 percent expects that it will appreciate and 40 percent say that it will remain same. For the next six months, 18.8 percent of the respondents expect the exchange rate to appreciate whereas, 65.2 percent predict that it will depreciate and the remaining are of the view that there will be no change in it. All these observations show that majority of the respondents are of the view that exchange rate will depreciate in the future.

Figure 6: Expectation about Exchange Rate for the Next 6- Month

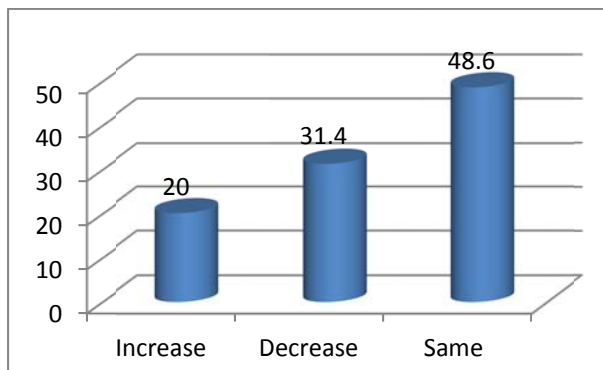


As far as unemployment is concerned, 59.2 percent respondents think that unemployment will increase in the next six months. In fact this rise in unemployment is expected to continue for the next twelve months according to 61.4 percent of the respondents.

5. Growth Rate

Majority of the respondents (48.6 percent) are expecting same growth rate in the coming six months, as compare to the current growth rate while 31.4 percent are expecting low growth rate in the coming six months. Remaining believe that it will increase (Figure 7).

Figure 7: Expectation about Growth Rate in Next 6- Months



When asked about the usefulness of government policies to enhance the growth majority of expert's indicate that current Government policies are not helpful for the enhancement of growth (79 percent)

Figure 8: Effectiveness of Government Policy for Growth.

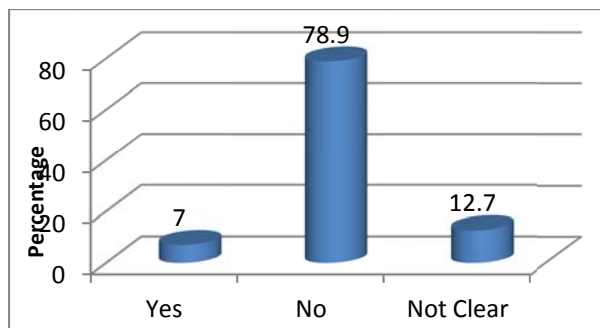
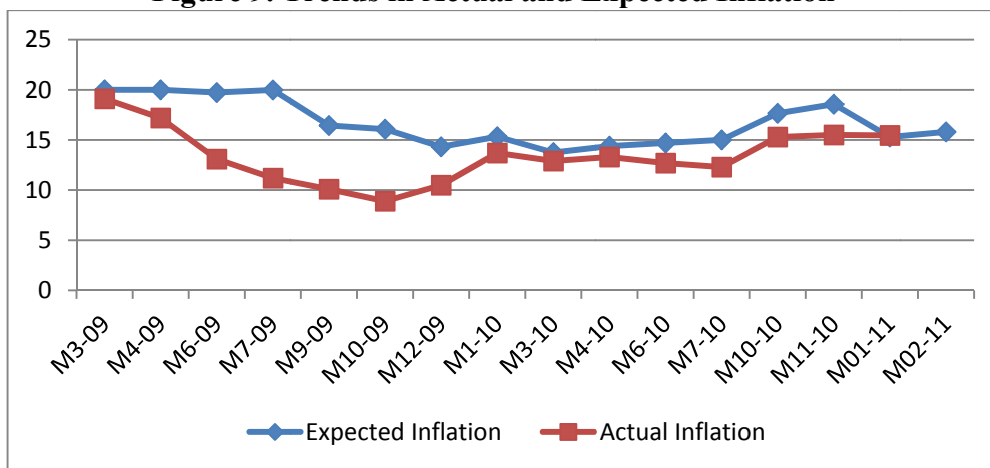


Figure 9. Trends in Actual and Expected Inflation



Note:

This report is the outcome of survey conducted by PIDE for the month of December 2010. Participants of the survey are economists and business men from all over the Pakistan.

Prepared by:

Dr. Abdul Qayyum (Registrar, PIDE)

Email: abdulqayyum@pide.org.pk

Muhammad Javid (Research Economist)

Kashif Munir (Staff Economist)

PIDE Inflation Expectations Survey

Pakistan Institute of Development Economics

P.O. Box 1091

Islamabad 44000, Pakistan

Tel. +92-51-9248051, Fax +92-51-9248065

This document is available at

www.pide.org.pk