Is Food Inflation Taking A Bite Out Of Growth?

Twenty-Third Corporate Economic Briefing

17 April 2018
Lower Lobby, Plaza 2
Parkroyal Hotel, Kuala Lumpur

MALAYSIAN INSTITUTE OF ECONOMIC RESEARCH

Is Food inflation taking a bite out of growth?

Many participate in the debate surrounding the rising cost of living, either supporting the economic reforms initiated by the present Government to transform our economy, or attacking it. The Strategic Reform Initiatives (SRIs), the second critical component of the Economic Transformation Programme (ETP) is much maligned and unappreciated by many. Several of the least popular SRIs are namely the Goods and Services Tax (GST), implementation of Minimum Wages, subsidy reforms and rationalization and finally the implementation of the Competition Act.

Anecdotal evidence seems to suggest that there is an overall increase in costs associated with reform initiatives. However, is this really the case or is there more than meets the eye?

A closer examination of the Labour Market will reveal the importance of human capital as average salaries generally coincide with labour productivity. High value-added economic activity and higher productivity levels are necessary to raise average wages. This could be achieved through the promotion of high value-added economic activities and through attracting quality investments, particularly in the knowledge-intensive industries.

Metrics and Economic Indicators

One metric that is a reflection of the living standard of a country is the "Engel coefficient." It is an application of Engel's law, which is an observation in economics stating that as income rises, the proportion of income spent on food falls, even if absolute expenditure on food rises. A low Engel coefficient indicates a higher standard of living.

Price stability implies avoiding both prolonged inflation and deflation. Inflation is a rise in the in the general price level of goods and services in an economy over the long run resulting in a decline in the value of money and purchasing power. Whereas, deflation is a decrease in the general price level of goods and services over the long run.

Price stability is one of the primary goals of central banks. Some central banks monitor core inflation rather than headline inflation. Core inflation is a measure of inflation that excludes the rate of increase of prices for certain volatile components in price indexes.

Focusing on core inflation can help prevent a central bank from responding too strongly to transitory movements in inflation, as it provides signal about persistent movements in inflation, which is important for the conduct of monetary policy.

Among the impact of high food prices are: increased poverty, possible worsening of malnutrition, depletion of the productive assets of the poor and reduction in the utilisation of education and health services.

Policy Matters

The immediate policy responses of the Federal Government aim at reducing the negative impact of high and volatile food prices on the lives of the poor in a timely manner, which could translate into sustainable policies that mitigate the adverse impact of high and volatile food prices on poverty.

In the long run, it would mean supporting broad-based growth in productivity and market participation in agriculture to ensure an adequate supply response, as part of a sustained improvement in food supply.

One such move is targeted food subsidies; and targeting is key, simply because across-the-board food price subsidies are generally the least desired option. They can be regressive, they distort relative prices and market functioning, and they usually cost more than other options. Politically speaking, once established, they can be very difficult to eliminate.

During boom times, in the absence of subsidies, one can expect there to be abnormally high inflation. However, this is not the case, as subsidies act to buffer sudden price spikes and dampen erratic price fluctuations.

If one were to look at food items with fine details. Fruits and vegetables and fish as well are influenced by weather conditions, market imperfections, to name few. Dairy products, milk and meat are examples of imported items, which in turn is influenced by exchange rate, distribution and marketing cost etc. Granular data analysis is the key to explain these volatile prices. Consumption patterns and share of food in household expenditure, income and substitution effects need to be examined.

In Malaysia, stabilisation of food prices is achieved via three means: subsidies, control of prices and control of supply. Subsidies are meant to help the poor and to stabilise prices from price shocks. In addition, subsidising the production of certain goods helps promote domestic industries. However, there is always a lag time for these price adjustments to take effect. In short, the adjustment is neither proportionate nor instantaneous.

Many believe that subsidies do more harm than good because they act against the functioning of an efficient market. Subsidies raise the important issue of inequity and regression: it is the tax-paying citizens who have to ultimately foot the bill.

This is the dilemma faced by any government wishing to help its poorest citizens to have affordable goods and services. This noble objective can only be achieved at the cost of weaker economic growth.

The deployment of subsidies is also accompanied by one unintentional consequence – richer citizens who could afford to pay the market price of goods are now able to gain more from these subsidies. Subsidies also mask the true cost of scarcity, as industries tend to overproduce to meet the artificial demand that they create. This encourages wastage that, along with growing government budget deficits, will impair national competitiveness.

The bigger picture

This brings us to the question as to how policymakers react to inflation. Should they behave like fire-fighters or should they be more proactive and less reactive instead? It is noteworthy that even George Soros, the infamous speculator, believes that left to their own devices, markets tend to overcorrect themselves.

In the final analysis, when facing with the spectre of inflation/deflation, what are the proactive measures to be observed by policymakers or should the question instead be, in the first place: “Are there any real strategies?”

MIER's Corporate Economic Briefing is a forum for discussing these and other issues of concern to the Malaysian economy. We will be presenting the results of the first quarter 2018 Business Conditions and Consumer Sentiment Surveys during the briefing. The results of MIER's other four industry surveys covering automotive, residential property, retail trade and tourism will also be presented.

Targeted at senior management and industry captains, the briefing provides a platform for frank discussions and debates. Come join us and keep abreast of the latest happenings in the Malaysian economy. Attendance is limited and will be on a first-come, first-served basis.

PROGRAMME

Tuesday, 17 April 2018

Time	Agenda
08.30 a.m. – 09.00 a.m.	Registration
09.00 a.m. – 10.30 a.m.	23rd Corporate Economic Briefing by Emeritus Professor Dr Zakariah Abdul Rashid Executive Director, MIER
10.30 a.m. - 11.00 a.m.	Q & A
11.00 a.m. - 11.30 a.m.	Refreshments
11.30 a.m. - 12.30 p.m.	Special topic: **Decomposing household expenditure on food items – establishing how much households spend on food and beverage** by MIER Researcher
12.30 p.m. - 01.00 p.m.	Q & A
01.00 p.m. - 02.00 p.m.	Lunch (Chatz Brasserie Coffee House, Lower Lobby)

Registration Fees : RM530.00 each for MIER Members
Inclusive of 6% GST

RM636.00 each for Other
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REGISTRATION FORM

TWENTY-THIRD CORPORATE ECONOMIC BRIEFING
17 April 2018
Lower Lobby, Plaza 2
Parkroyal Hotel, Kuala Lumpur

PARTICIPANT'S DETAILS

Name	
Designation	
Organisation	
Address	
Contact Person	
Tel No.	
Fax No.	
Email	

REGISTRATION FEE (Inclusive of 6% GST)

Full conference registration fee includes presentation materials, refreshment and lunch

MIER Members	Others
❑ **RM 530.00**	❑ **RM 636.00**

All registration must be received by MIER no later than **13 April 2018**. Cancellations and refunds will not be made after that date. However, substitution will be allowed if made at least 72 hours before the Conference.

RSVP: Pn Isnani Bt Ismail and Pn Nur Faizah Bt Bakri (603) 2142 0091/5895/5897 Fax: (603) 2141 0131, Email : secretariat@mier.org.my

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