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High Inflation Risk And Growth Rate

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ABSTRACT

This paper examines the causal relationship between high inflation and economic growth in Turkey. While talking about economy, The growth in the economy sounds positive but as inflation word, the citizens most of the time do not have an idea how it can be and how would it influence on the people in the market. The inflation and economic growth are the basic keys of purchasing power of individuals, organizations and the government and if there is one in the market the other one would not be. Here we can easily say that there is a negative relationship between these two terms and the basic purpose of this study is to determine the relationship by the literature review methodology. In the study the academic studies have been researched for defining the terms and the relations. Also, the effects of these terms to people and the producers have been determined. As seen from the daily life, the inflation is a cause and reason of financial crisis and the individuals' money power decreases day by day with the inflation. The study does not have an interview or a questionnaire application for the proof of the literature results and this has been accepted as the limitedness of the study.

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Introduction

In daily life everyone has to satisfy its needing for continuing to their life in their standards such as buying food, clothes, education and health services etc. but every day the price of these needs change because of the influence of pricing mechanisms of the market. Sometimes the prices of them decrease or this can be thought as the purchasing power of money increases or sometimes the amount of bought things decrease with the same money. Every period in the economy such as day, week, month or year, the prices should be compared to each other for seeing the growth of the economy and the growth of it is stays loyal to the inflation, risks, production, investments, interests etc.

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In this study the relationship between the inflation risk and the economic growth has been determined by the literature review and as guessed they are the elements of economy but they have negative effect between each other. The growth means higher purchasing power of the companies, government and the individuals and higher investments and low credits and depts. But the inflation means the decreasing purchasing ability and the value of the money, increasing unemployment and prices. The inflation causes more inflation and the growth brings more economic growth.

From the literature review we can see that the inflation in a country is one of the most important market determinants for the local and foreign enterprisers and if there is high inflation the investigation would be rare or none and this would cause unemployment, poverty, difficulty on reaching to the basic needs and making policies in the world. The economy is the basis of a country in every condition in the global world. For prestige and being the investor center, increasing the life standards, the production should continue. Inflation means foreign-source dependency and in process this would be more dangerous for the country than wars.

Methods

Model In this study, basic concept explanations have been carried out and articles of important and current researchers of economics discipline have been examined. In these articles, information about the interaction in economic growth figures in high inclusion environment was compiled. In the study conducted in the form of a field survey, the effects of financial crises on growth rates and the effects of disruptive effects on inflation figures and their reflection on society were investigated and the main findings were compiled in tables and graphs.

1. Definition of Risk

The risk means a probability of damage and in the finance science risk means "the probability that an actual return on an investment will be lower than the expected return. Financial risk is divided into the following categories: Basic risk, Capital risk, Country risk, Default risk, Delivery risk, Economic risk, Exchange rate risk, Interest rate risk, Liquidity risk, Operations risk, Payment system risk, Political risk, Refinancing risk, Reinvestment risk, Settlement risk, Sovereign risk, and Underwriting risk" (Business dictionary, 2018).

Economically risk is most of the time related with the amount of sales and the amount of costs. Both of them are based on the market and its elements' balance. For example with high inflation the production costs would be high for a company such as energy raw material and tax. For not decreasing the total profitability, the price for selling the product would be increased by the company but the value of money of the consumers would be decreased and the consumers would not buy the product as much as before. This is a huge risk for every kind of good and service producer and by the inflation, the process told here would be a vicious cycle. By this reason, the financiers like huge companies or banks would not want to be in this kind of unbalanced market because of the losing liquid risk (Garcia and Werner, 2010; Visconti, 2012).

While talking about the inflation and rates this means that we are talking about the macroeconomic risks. In every market there is a risk premium and if the inflation are high this means that this is an unbalanced economy and the risk is high for the investment. The risk premium grades of a market shows the potential damage to the investment and liquid money.

By this reason other countries' global companies would have to plan more carefully while they are entering to the market. Being careful means being more expensive in this market because the real returns of the investment would be hard and slow and this means impairment. For protecting the companies from the economic crisis in a market the investors would search for alternative places (Reiser, 2014).

2. Definition of Inflation

Inflation can be defined as a kind of pricing mechanism of goods and services but here we should say that it is not the only influencer of the price and the purchasing power. It is based on the interests, rates, production capacity and ability, population and the politics. Most of the time because of a shock in the economy effects on the interests, investments and production and the amount of goods and the services in the market decreases and this causes a raise in the prices. This raise means buying problems of raw materials, needs of people, less production and less employment. In this kind of unbalanced quotation, the investors, producers, banks and the people would afraid of spending their habits and this also influences on the prices. The changed prices can be caused from the inflation and they also can create the inflation. So here we can easily say that every element of the economy has a relationship with the other (Sağlam and Sönmez, 2017; Sever and Mızrak, TY).

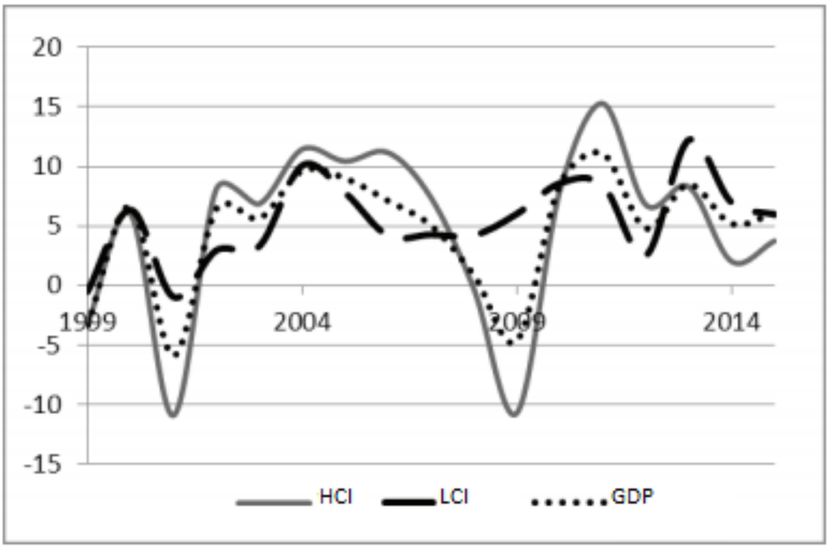
Inflation is a description of the continuous raise of the prices in a market (Poedjıyo, 2014). It means that unbalanced and distrusted economy and in a market which is influenced by the inflation this means the buying power of local money decreases day by day. The raise of the price should be felt by every instrument of the market for calling a raise "inflation". The speed of raise shows the rate of inflation and the prices of the goods and services increases continuously with the inflation (Oner, 2010).

Labonte describes inflation as a continuous decrease on value of money in a market/country and the author says that there may be several causes of inflation. The economic crisis in all around the world showed that the inflation and economic crisis are both their causes and there is a two-sided relationship between these notions. The money, growth and other economic policies of the government or the central bank can be the basic cause of the inflation and these directly effects on the economic relationship of the different markets/countries. An alternative view comes in several versions. They have in common a belief that the major upward pressure on prices comes from activities which would produce a fall in real output. The production decrease means less goods for selling and less money for the producers. Less good means higher prices and this causes less purchasing power. The decrease of purchasing power means increase on unemployment, raw material, stocking, logistics and other flows prices and these problems again causes inflation (Labonte, 2011).

3. Definition of Growth and Economic Growth

Growth is the enlargement, increase of the success and development. In the economy, the growth is possible with the financial development according to the economy theory so for understanding the growth first of all we should clarify how the financial development can be possible. The economic growth and development have been debated for centuries especially after the industrialization and the importance of the subject has been increased with the globalization because of the relationship of the economies of countries.

The financial development means there is an ease on the payments and there is liquid in the market. In a growing economy the investors will have high income and profit and the total savings of individuals and the organizations would be high. If there is development in the economy this means that there is a cooperativeness between the government and the investors. The policies of the government and the central bank are successful and low interest rates. In growth economies, there is a balance in the market and the income per capita increases every economic period (Sağlam and Sönmez, 2017). The balance brings investments and the investments in a market directly effects on the economic growth:



Graph 1. Relationship Between Gross Domestic Product, High Capital Intensity and Low Capital Intensity

Graph one shows the high capital intensity and low capital intensity in the Turkish market from 1999-2004. For seeing the relationship of economic growth and the investments; the graph can be checked. As seen when the HCI is down, the GDP decreases (Göcen, 2017).

The positive growth of the economy shows that there is higher living standards, quality and mass production, an increase of the national income per capita, high education and decrease on unemployment. The positive growth is raise in the production of goods and services. In a growing economy there are many job and investment opportunities and the health, education and other basic living standards of the population becomes higher. Here we can say that the growth can be positive, zero or negative. The positive growth as guessed means development. Zero growth means balance in the economy and no surprise and no development but in this age with high increase and development of technology and relationship between the economies of all around the world, it can be thought as risk of negative way. The negative growth as thought from its name causes financial crisis, high inflation and risks (Haller, 2012).

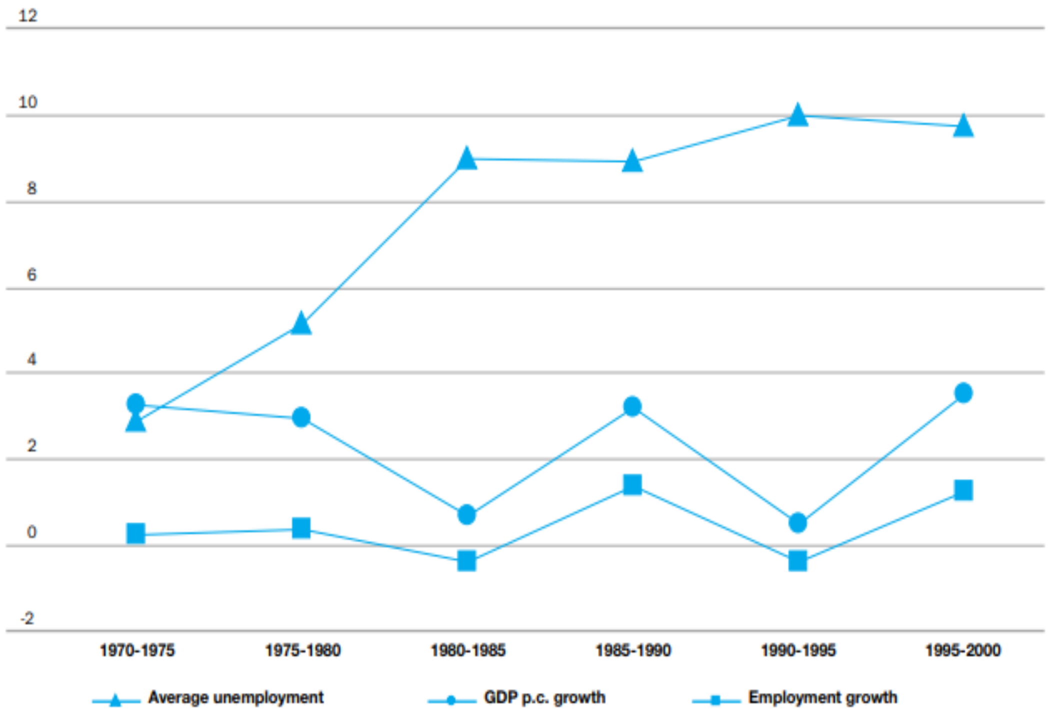
i. For example better health and qualified education means better economy. Higher levels of income reduce infant mortality and this helps population to grow up.

ii. Primary and secondary school enrolment rates are positively associated with higher levels of per capita income. This shows the importance of education for the families and their ability for sending their children to school. In undeveloped countries the children most of the time cannot go to school, they should work or cannot reach to the schools because of high travelling costs. Again, Educational outcomes such as test scores and the rates at which children repeat a year's schooling or drop out of school are significantly affected by per capita income.

iii. Life expectancy is clearly positively related to the level of per capita income, according to cross-country evidence. Higher standards cause higher education and health, higher human rights and higher production.

The economic growth is a complex phenomenon and for a better understanding the measurement of it can be investigated. *Economic growth supposes the modification of the potential output, due to the modification of the offer of factors (labour and capital) or of the increase of the productivity of factors (output per input unit). Some economists state that a rate of the GDP growth of 3% a year allows a rise of the potential GDP with 10% in three years and a doubling in 23 years. According to the "rule of 70", a rate of growth of 1% doubles the potential GDP over a period of seventy years* (Anyanwu Uchenna and Kalu Alexanda, 2015).

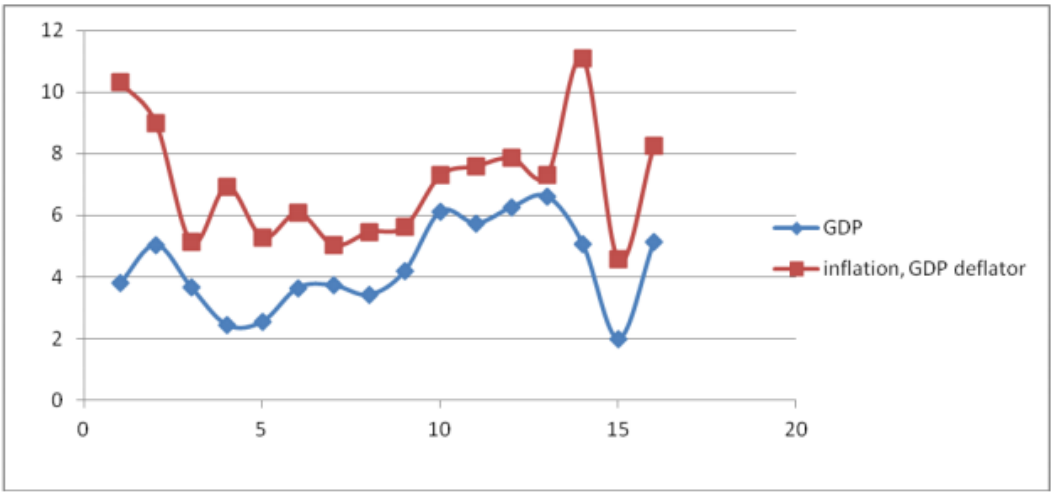
The economic growth and the development of production and the society has a positive relationship between each other. In a positive growing economy, there are always new possibilities for the investments and there are always high incomes and sales. While the financial standards are increasing in a growing economy there would not be inflation and high risk.



Graph 2. Relationship Between Employment, Unemployment, GDP

As seen from the Graph 2 (An example of European Countries between 1970-2000), when an increase happens on average unemployment, the GDP growth and the employment growth falls down (Wilson and Briscoe, 2004).

According to OECD the society is the basic function of the growth side. If the education is high and the population is young enough for working and production; this would help economy to be balanced and grow positively. But if the retirements is high or the qualified personnel is rare, the production would slow down and also the pension systems would not be effective. The positive link between growth and poverty reduction is clear. The impact of the distribution of income on this relationship – in particular, whether higher inequality lessens the reduction in poverty generated by growth – is less clear. Here we can easily say that if the society is qualified and working; this would decrease the poverty and increase the economic growth (OECD, 2013).



Graph 3. GDP-Inflation Relationship

Here we can say that the resources' usage effectiveness shapes the GDP in the countries and the GDP shapes the economic growth way and the inflation rates. The high inflation means negative economic growth and we see from the Graph 3, when the GDP goes down the inflation increases and this influences economy negatively (Tsegaye Mamo, 2012).

4. High Inflation Risk and Growth Relation

High inflation is a kind of deterioration of balance of the instruments of payments because of any effect and it's the raise of the prices in a country or market. The economy faces with several problems if this balance would change because inflation can be described as a negative frame in the economy. Inflation risk periodically emerges as an extreme – albeit hardly perceived-event, to which infrastructural investments especially in developing countries are particularly vulnerable, creating disrupting agency costs among different stakeholders. For understanding the effect of inflation and for lessening the effect of inflation on the market the economy researches are continuing in all around the world. Because the inflation in a market such as a developing country depends on its economic growth but also it directly prevent the growth. For the investors being in such a market is risky because of losing the profit but also being out of this kind of market is losing the chance of huge amounts of sales because most of the time the inflation comes with stopping the local producing and production downturn is a financial chance for the developed countries being a super-state. But as seen, with the inflation risk, with investments or without investments, the local consumers have the huge damage. Their living standards and the value of their money would decrease so fast (Visconti, 2012).

High inflation risk means there is not effective policies of the government and the central bank of the country. The government and the central bank should always have an alternative plan for keeping the prices fixed and this may be done by mostly fixing the exchange rate. The risk in the economy always increases the exchange rate of the society and the organizations. The inspecting and expectations should be done and by looking the balance of the economy and the past. This should not be forgotten that the high inflation are often the result of lax monetary policy. If the money supply grows too big relative to the size of an economy, the unit value of the currency diminishes; in other words, its purchasing power falls and prices rise. This relationship between the money supply and the size of the economy is called the quantity theory of money, and is one of the oldest hypotheses in economics (Oner, 2010). In every market the inflation, exchange rate and the interest rates are interdependent and a change on one would change on the others and the change means economic risk (Poedjıyo, 2014).

Results

The incomes of the organizations and even the individuals are most of the time indexed to prevailing inflation rates. To the extent that revenues command a positive margin over costs, indexation widens economic marginality. The inflation increases the value of loans of the companies and the markets which are risky are most of the time dangerous for the organizations' economic sustainability (Vizconti, 2012).

Especially after 1980s, the economic growth, its ability and the factors influence on the economy are the main subjects of the researchers because of the globalization and repeated financial crisis. The results of the crisis and the researches showed that the financial crisis and the inflation has a positive relationship and the economic growth and the inflation has negative relation. If the growth is high this means that the market has the economic balance and low risk premium and the investments would be more and easy. The purchasing power and the production would be high and continuous (Yamak and Tanrıöver, 2009).

The inflation in a market causes different investment alternatives for the companies and in every kind of crisis the policies should have diffe4rent solutions but the production should be local for the economic growth and this is the necessity. The energy production and especially the agricultural power most of the time prevents the inflation because these are the basic parts of the raw materials and the basic need of the society. In a market where the energy and the agricultural products are local, the production would be in safe and most of the time it would be profitably for the companies. But if there is an external dependency on energy and agriculture, this means that the prices would be high during the inflation and the profitability and the purchasing power would directly be influenced (Yüksel, 2014; Poedjıyo, 2014; Labonte, 2011).

Because of these reasons, the countries which are still developing and facing with the high inflation risks and have unbalanced economies should find the ways for producing their own energies and develop the agricultural abilities. The people should be informed about using the local goods and especially the SMEs must be encouraged by the governments.

Discussing for future study

As seen from the literature high inflation means increasing prices but low buying ability and this causes decrease of living standards of the society. Exactly opposite, the low inflation and low risk can be possible by positive growing economy and this kind of economies let investors to have new opportunities, well-educated employees, high living standards and purchasing power. So here we can say that if there is inflation in a market the economy is not growing well enough . Econometric study could show that how much affected high enflation on economic groth rates for next study will be about that subject.

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