Classical approach to tame inflation

Classical case of inflation generally entails increasing or decreasing inflation targets, based on liquidity crunch or glut, to arrest targets meant ideal in the 1-2 % range. Targeting inflation based on the changes of the repo rates, increases or decreases liquidity and hence tame inflation to be kept under targets. Here are a few cases that can happen, based on current inflation.

Current inflation levels at WPI level	Status of liquidity	Changes made in the repo rates	Expected Inflation	Case
3 - 7%	*Liquidity increases*	*Interest rate is decreased*	*Expected inflation lowers*	*Normal*
2 - 3.5%	*Liquidity decreases*	*Interest rate is the same*	*Expected inflation remains the same*	*Special*
0.5 - 1.0%	*Liquidity decreases*	*Interest rate is increased*	*Expected inflation increases*	*Rare*
2 - 3%	*Liquidity increases*	*Interest rate is the same*	*Expected inflation increases*	*Corrective*
-1.5 - -0.5%	*Liquidity increases*	*Interest rate is increased*	*Expected inflation increases*	*Deflation*
2.5 - 4.5%	*Liquidity decreases*	*Interest rate is the same*	*Expected inflation decreases*	*Possible likely*
2 - 3%	*Liquidity increases*	*Interest rate is decreased*	*Expected inflation remains the same*	*Classical case*

However, there are some cases where repo rates need not change to arrest inflation all at once. Here are a few approaches.

1. Increase in public spending, mostly related to public expenditure and increase of disposable income, adds to inflationary pressures at a considerable rate. The difference in CPI and WPI at a macro level, actually determines real inflation by Current inflation = Weighted(CPI, WPI) – Correlation (WPI, CPI). The macro equation can be I = 2/3*WPI + 1/3*CPI – 0.647*Co-Relation(WPI, CPI) + Constant.
2. Inflation is also seasonal, where stocking before the arrival of monsoons can reduce a lot of consumer priced inflation. Emergencies can also increase food prices, where stocking is necessary for monsoon led agriculture based economy.

3. Reduction of prices through an efficient public distribution system is an enhance factor. Also, driving prices with low cost and fresh items necessary to keep an inflation check can enhance meeting of targets.
4. Collaborating with the states to keep regional inflation under control for the states accepting rise in food grains and pulses, where stockists can work on increasing the necessary supply under statutory norms, can lessen pressures for inflation.
5. The macroeconomic views related to SLR and CRR, namely arresting of liquidity is of lesser consequences to tame the aggregate of macroeconomic indicators. Correcting SLR and CRR does not bore well for central banks which tame inflation based on liquidity rise.
6. Overall, $I = GNP – GDP – A + S$, where gross national product is determined by the aggregate of the goods and services, minus inflation caused loss, actually determines the correct inflation level. Here, an increase of aggregate determined by the market forces by counting an increase of services and goods can actually tame inflation. ‘S’ denotes surplus of goods and services injected by changing repo or interest rates, at a gross and macro level.
7. The rise of oil prices, if any, form a considerable part of inflationary miss, which can be adjusted by the introduction of metros and electric or hybrid vehicles, which run on electricity and petrol.
8. Local agricultural products can actually be made accessible to corporate institutions like Walmart, Big Bazzar and Reliance Fresh, where affordable everyday prices bring down inflationary targets by introducing vegetables and fruits, including groceries at low prices. Certain macro economic factors as the prices of oil, pulses, rice, wheat, food grains, clothing for brands under the money market reduces or increases the inflation. Basic food items, including necessary items need a very affordable approach keeping sourcing norms locally at around 30-50%.
9. Affecting circulation in the money market, until 2.5-4% of increase of inflation at a macro level does not generally trigger arresting liquidity at a macro level, by reducing interest rates. Changes in the repo rates do not imply a change in the interest rates for the banks, or a bull whip affect that is spread on.
10. To increase money at an aggregate level, which defines freedom of variable allowances from the tax burden, actually reduces disposable income, which affects the consumer led economy and helps the middle-class driven economy a thrust for savings.