Estimating Inflation Rates of Import-Concentrated Commodities

M. G. Mortaza and Naima Farah

Abstract

This note provides estimates of inflation rate of import-concentrated commodities and their contribution to overall inflation in Bangladesh. The results suggest that the Bangladesh economy has been experiencing higher inflation of import-concentrated commodities especially of food items indicating the dominance of higher food prices in the international market in raising recent inflation in Bangladesh. The contribution of inflation of import-concentrated food commodities has also been large as estimates of pass-through of import-concentrated inflation rates to overall inflation exceed unity. The results highlight the importance of anti-inflation measures using both fiscal and monetary policies that ensure long-run food security and thereby reduce reliance on food imports.

1. Introduction

The Bangladesh economy has been experiencing a persistent and high level of inflation over the last eight consecutive years starting in FY01. While the general inflation rate (12-month moving average) was 1.94 percent in FY01, the corresponding rate stood at 9.94 percent in FY08. These inflation rates have mostly been dominated by higher price of food commodities, especially since FY04. Interestingly, recent inflation in Bangladesh has been in line with global trends, as recent trend of global inflation is upward, especially since the beginning of 2007 and the intensity of Bangladesh inflation has also deepened since then. While inflation rate (point-to-point) in January 2007 was 5.94 percent, the corresponding rate soared to 10.04 percent in June 2008. The rising trend in domestic inflation in line with global trend shows that recent domestic inflation is fed by higher commodity prices in the international market (Mujeri et al. 2008). The higher pass-through effect of international commodity-specific prices to the domestic prices is also recognized, essentially depending on higher consumption and lower production of those commodities (Mortaza and Rahman 2008). Higher domestic prices in the backdrop of global increase in commodity prices requires assessment of the role of inflation in import-concentrated commodities to total inflation so as to formulate appropriate monetary and fiscal policy measures.

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2 For example, during FY01-FY03, the contribution of food inflation to overall inflation was less than 50 percent, which stood at 69.9 percent in FY04 and 73.0 percent in FY08. See Mortaza and Hasnayen 2008.

3 According to International Financial Statistics (IFS), International Monetary Fund (IMF), the average world inflation rate in 2001 was 4.07 percent. Though the corresponding rate declined to 3.58 percent in 2004, it soared to 5.63 percent, on average, during January-June 2008.
In estimating inflation rates of import-concentrated commodities, it is important to find out the links through which domestic inflation may be affected by imports or higher prices of commodities at the international market. Since a large portion of final consumption goods and services in Bangladesh are, either directly or indirectly, based on imports, it is expected that higher prices of those goods in the international markets may directly transmit to the domestic prices unless there are strong substitutes of those goods in the domestic market.\(^4\) Even if there are strong substitutes of imported commodities, higher inflation of commodities in the international market may push up prices of domestic substitutes of those commodities if the supply is fixed in the wholesale market and the demand increases due to higher prices of imported commodities. Moreover, if the prices of imported inputs are used in the production of final domestic commodities, the production cost will increase and eventually, the prices at the farm gate level and the ultimate selling price will increase as well. Thus prices of import items may have differential impact on final consumer prices in the domestic market and call for estimating the role of imported inflation to overall domestic inflation.

This note identifies the role of prices of import-concentrated commodities in overall inflation in Bangladesh by computing inflation rates of import-concentrated commodities in Bangladesh and draws some policy implications.

2. Theoretical Background

In an open economy, transmission of trading partners’ inflation to the domestic economy is one of the aspects how domestic inflation may be fuelled up. In fact, recent inflationary period of Bangladesh is mostly explained by a surge in prices of commodities at the global market on which Bangladesh is highly dependent for final consumption. And as a small open economy and a net importer of food commodities, the Bangladesh economy needs to accept higher prices of world food commodities. Similar trends have also been observed in the case of non-food commodities as large amount of capital machinery and raw materials for some leading exporting industries such as ready-made garments (RMGs) in Bangladesh are also imported from abroad.

The transmission of trading partners’ inflation to the domestic economy can be both direct and indirect. In the direct way, higher prices of imported consumer goods and inputs may quickly transmit to the domestic economy. However, domestic inflation and higher prices of imported commodities and raw materials are connected in several ways. First, domestic inflation of final consumer goods may increase directly due to higher prices of those items at the international market. It is expected that higher prices at the production level in abroad due to higher prices of inputs such as oil and labor, may increase the prices of final products in abroad and the imports of those commodities to the domestic market will eventually increase the consumer

\(^4\) While, in Bangladesh, the ratio of total imports of goods and services to total private consumption expenditure was 26.4 percent in FY03, the ratio reached 37.0 percent in FY08. See BBS 2008.
prices at the domestic market. Lower agriculture production in abroad due to natural disasters such as drought or the increase of use in cropland for other production purposes may create a situation of excess demand among countries, which can have a positive shock on prices of those commodities in the international market and eventually will push the domestic consumer prices to go up. The higher freight charge or higher transportation cost of imported items due to higher prices of oil may add to the final consumer prices in the domestic market. In a similar fashion, higher tariff rate on imported items will put an upward pressure on the selling price in the domestic market.

In the indirect way, for example, if China’s inflation rate is higher than in Bangladesh, then it is rationale for traders to take advantage of price differentials, or arbitrage. Arbitrage will increase the demand for tradable items in Bangladesh, and hence raise domestic prices (Taslim and Chowdhury 1995). Moreover, higher price of imported inputs for domestic export sector may increase the price of exports. A rise in export price directly improves the earnings of the exporters which will result in increased expenditure and will cause a demand-pull type of inflation. An improvement in export earnings also may encourage the exporters to import more raw materials from abroad for their production and the resulting outcome will be a further rise of inflation.

One may term the above as structural inflation and stress on structural rigidities of the economy as the principal cause of inflation (Jhingan 1997). The process starts with the increase in non-agricultural incomes at the initial phase of development accompanied by high growth of population that tends to increase the demand for goods. More specifically, as the demand for agricultural goods rises with their domestic supply inelastic, prices of agricultural goods rise. The output of these goods doesn’t increase with the pace of their price rise due to a defective system of land tenure and other rigidities in the form of lack of irrigation, finance, storage and marketing facilities, and bad harvests. As imports in large quantities are hampered due to foreign exchange constraints and the prices of imported products are relatively higher than their corresponding domestic prices, the process pushes the domestic price level to rise.

In another indirect channel, prices of domestic substitutes will increase due to higher prices at the international market, mainly due to two reasons. First, if the supply of that commodity is fixed in the wholesale market, the demand for domestic substitutes will increase due to higher prices of imported commodities. Second, the production of substitute goods may take a long period which will put pressure on demand of existing availability of those commodities. The resulting effect in either of the above cycles is higher prices of domestic substitutes of imported commodities.

Thus, trading partners’ inflation may have differential impact on domestic inflation and may fuel up domestic inflation. At the aggregate level, the channel through which the effect of international price changes is reflected in domestic inflation is the direct relationship between consumer price index (CPI) and import price index (IPI). If commodity prices at the

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5 Usually higher prices of final consumer goods are observed in the case of food items as food items are imported for final consumption purposes and higher prices of imported inputs are observed in the case of non-food items.
international market rise, it will be reflected in IPI and consequently will affect domestic CPI. However, this note identifies indirect channels as well – higher input price or substitution effect – through which imported price may affect domestic prices. Thus we call the underlying estimated inflation rates as ‘inflation rates of import-concentrated commodities’ rather than ‘imported inflation.’

3. Data Analysis

The theoretical background of imported inflation allows us to draw a relationship between inflation rates of countries from which Bangladesh imports and domestic inflation in Bangladesh. It may be argued that current domestic price pressure is due to higher prices of final commodities and inputs in the importing countries of Bangladesh.

<table>
<thead>
<tr>
<th>Importing countries</th>
<th>Share in total import (%)</th>
<th>Inflation rate (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Average (FY04-FY07)</td>
<td>2001</td>
</tr>
<tr>
<td>India</td>
<td>15.37</td>
<td>3.68</td>
</tr>
<tr>
<td>China</td>
<td>14.43</td>
<td>0.47</td>
</tr>
<tr>
<td>Kuwait</td>
<td>7.33</td>
<td>1.66</td>
</tr>
<tr>
<td>Singapore</td>
<td>7.25</td>
<td>1.00</td>
</tr>
<tr>
<td>Japan</td>
<td>4.78</td>
<td>-0.80</td>
</tr>
<tr>
<td>Hong Kong</td>
<td>4.63</td>
<td>-1.61</td>
</tr>
<tr>
<td>Korea, R. of</td>
<td>3.67</td>
<td>4.04</td>
</tr>
<tr>
<td>Thailand</td>
<td>2.50</td>
<td>1.64</td>
</tr>
<tr>
<td>U.S.A.</td>
<td>2.46</td>
<td>2.83</td>
</tr>
<tr>
<td>Malaysia</td>
<td>2.33</td>
<td>1.42</td>
</tr>
<tr>
<td>Germany</td>
<td>2.30</td>
<td>1.98</td>
</tr>
<tr>
<td>Indonesia</td>
<td>2.23</td>
<td>11.47</td>
</tr>
<tr>
<td>Saudi Arabia</td>
<td>2.10</td>
<td>-1.12</td>
</tr>
<tr>
<td>Bangladesh</td>
<td>...</td>
<td>1.94</td>
</tr>
</tbody>
</table>

Note: For Bangladesh, inflation rates refer to fiscal year. The data for 2008 is until June 2008.
Source: IFS, IMF and Import Payments, BB

Table 1 provides the inflation rates of major importing countries of Bangladesh during 2001-2008. In particular, inflation rates of two biggest importing countries of Bangladesh, i.e., India and China, have been soaring significantly in recent times, putting upward pressures on the prices of consumer goods in Bangladesh. In China, the consumer price inflation jumped to more than 8.0 percent, on average, in the first half of 2008, from 1.0 percent in early 2006, while in India, the consumer price inflation accelerated to more than 7.7 percent in June 2008. Producer and consumer price inflation measures in East Asian countries Asia have increased noticeably since early 2007, largely driven by soaring food and energy prices. Surging food and energy prices coupled with strong economic

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6 The listed 13 countries cover 71.4 percent of Bangladesh’s total import.
7 In China, the consumer price inflation jumped to more than 8.0 percent, on average, in the first half of 2008, from 1.0 percent in early 2006, while in India, the consumer price inflation accelerated to more than 7.7 percent in June 2008.
8 Headline inflation in these economies rose sharply from mid-2007, when annual inflation ranged between zero and 2.5 percent, to between 3.7 percent and 7.5 percent in May 2008.
expansion have also pushed up prices across these countries (ADB 2008). At the same time, higher inflation rates are also observed in Kuwait and Saudi Arabia which are the two biggest crude oil exporting countries to Bangladesh. A consistent and rising inflation is also observed in Bangladesh since FY01. Thus a significantly positive shock of global inflation, especially higher inflation rates of importing countries of Bangladesh, may have influenced domestic inflation in Bangladesh.

**Food and non-food inflation**

Higher inflation rates in importing countries of Bangladesh may affect domestic inflation rates on the basis of its concentration with respect to location and commodities. In the case of location, it is expected that in the rural areas, the prices of imported commodities will be higher as compared with those in the urban areas.

As the current inflation period is dominated by soaring food prices, it is clear that food inflation will be higher than non-food inflation. The 12-month CPI inflation rates of food and non-food items show significant differences (Figures 1 and 2). While the average food inflation was 1.38 percent compared with the nonfood inflation rate of 3.04 percent in FY01, food inflation reached to 12.28 percent in FY08, even widening the gap from the nonfood inflation rate of 6.32 percent. The gap between 12-month average food and nonfood inflation further expanded in July 2008, as food inflation rose to 12.50 percent and nonfood inflation to 6.13 percent.

![Figure 1: 12-Month CPI Inflation (Food)](image1)

![Figure 2: 12-Month CPI Inflation (Non-food)](image2)

The significant differences in the commodity-specific inflation rates between rural and urban areas are also observed over the same period. For example, during FY01, average food inflation was 1.18 percent in rural areas and 1.89 percent in urban areas; while, in the case of nonfood inflation, the rates were 3.83 percent in rural areas and 1.13 percent in urban areas. In July 2008, average food inflation stood at 12.20 percent in rural areas compared with 13.21 percent in urban areas. In the case of nonfood category, rural areas experienced an inflation
rate of 6.23 percent in the same month while the rate was 5.84 percent in urban areas. This shows that, in general, urban people face a higher rate of food inflation relative to rural population, while the rural people experience a higher rate of nonfood inflation relative to their urban counterparts.

4. Methodology and Estimation

The consumer price index (CPI) measures the changes in prices of goods or services acquired or utilized by households for consumption purposes in a particular period and CPI inflation measures the changes of CPI between a given period of time, usually a year. However, in the estimation process of general CPI, it is not mentioned whether commodities are imported or domestically produced. Thus, the usual CPI index stands as the following:

\[
CPI_{L,t} = 100 \sum_{i} w_{i0} \left( \frac{P_{it}}{P_{i0}} \right)
\]

where, \( P_{it} \) is the price of product \( i \) at time \( t \), and \( w_{i0} \) is the proportion of total expenditure attributed to product \( i \) at time \( 0 \). The inflation would be the percentage changes of this CPI between two periods of time. However, in an attempt to separate the domestically produced inflation from imported inflation, the underlying inflation can be divided into two components, one that reflects domestically generated inflation and one that mirrors imported inflation:

\[
\text{Inflation} = \text{weight} * \text{domestic inflation} + (1-\text{weight}) * \text{imported inflation}
\]

where, weight is the domestic inflation’s share of total inflation. Thus the imported inflation can be estimated from the following CPI:

\[
ICPI_{L,t} = 100 \sum_{i} w_{i0} \left( \frac{P_{it}}{P_{i0}} \right)
\]

where, ICPI is the imported CPI, \( P_{it} \) is the price of imported product \( i \) at time \( t \), and \( w_{i0} \) is the proportion of total expenditure attributed to imported product \( i \) at time \( 0 \). However, this note considers not only the commodities that are imported from abroad, but also the commodities for which the imported raw materials are required. And inflation rates of import-concentrated commodities can be found from the estimation of the following CPI:

\[
ICCPI_{L,t} = 100 \sum_{i} w_{iC0} \left( \frac{P_{iCt}}{P_{iC0}} \right)
\]

where, ICCPI is the import-concentrated CPI, \( P_{iCt} \) is the price of import-concentrated product \( i \) at time \( t \), and \( w_{iC0} \) is the proportion of total expenditure attributed to import-concentrated

\[9\] This is Laspeyres index of consumer prices; though there are other indexes as well such as Paasche CPI and Fisher CPI. However, the Bangladesh Bureau of Statistics (BBS) uses Laspeyres index in estimating CPI inflation rates in Bangladesh.
product $i$ at time $0$. The percentage changes of CPI between two periods of time will give the inflation rates of import-concentrated commodities in Bangladesh.

Estimation

Following the above methodology, the commodities in the CPI basket are divided into two broad groups, both in rural and urban areas. One is for domestic-concentrated commodities and another one is for import concentrated commodities. In Bangladesh, to get the national CPI inflation, CPI is constructed separately for rural and urban areas with detailed prices for 215 commodities and services (106 food and 109 non-food) in rural areas and 302 items (113 food and 189 non-food) in urban areas. In terms of weights, rural CPI has a higher dependency on food category (by nearly 13 percentage points) than non-food category and urban CPI has higher dependency on non-food category (by nearly 2 percentage points) than food category, implying higher food dependency at the national level. However, in an attempt to estimate CPI inflation rates of import-concentrated commodities, this note considers the detailed prices of 101 commodities and services (37 food and 64 non-food) in rural areas and 159 items (45 food and 114 non-food) in urban areas. The remaining weights are 55.3 percent in rural areas and 45.6 percent in urban areas. The commodity-wise disaggregated data on CPI have been collected from BBS and information on imported items has been taken from Annual Import Payments 2006-2007 of the Statistics Department, Bangladesh Bank. Using above information, the estimated results of rural and urban inflation of import concentrated commodities are presented in Tables 2 and 3.

Rural inflation

The quarterly inflation rates of import-concentrated commodities in rural areas are provided in Table 2 during FY06 - FY08. The point-to-point (p-t-p) inflation rates of import-concentrated commodities was significantly higher in the first half of FY06, around 12.1 percent in December 2005; which however slowed down in the second half of FY06. The inflation rates of import-concentrated commodities continued to decline until the first half of FY07 and reached 4.2 percent in December 2006 and then started to rise since the beginning of 2007. The inflation rate of import-concentrated commodities continued to soar up in FY08 and increased from 14.5 percent in September 2007 to 22.0 percent in June 2008.
One interesting observation is that import-concentrated inflation rates (p-t-p) of non-food items dominated over food items in FY06 and FY07; however the situation reversed in FY08. While import-concentrated inflation rate of non-food items has been decreasing over the period, the corresponding rate in food items (p-t-p) has significantly jumped up in FY08 and climbed to 33.9 percent in June 2008. The assertion that can be made from this analysis is that import-concentrated inflation rates in rural areas are comparatively higher when food inflation outweighs non-food inflation significantly. Similar trends in the case of food and non-food items are also observed when inflation rates are estimated on the basis of moving average (MA). In this case, general inflation rate increased from 7.98 percent in September 2006 to 19.07 percent in June 2008, while food inflation increased from 6.26 percent in September 2006 to 27.18 percent in June 2008.

*Urban inflation*

In the case of urban inflation, the trend of inflation rates, both p-t-p and MA, of import-concentrated commodities are similar to those in rural areas (Table 3). That is, import-concentrated inflation rates were higher in the beginning of FY05, then a declining trend is observed until end of 2006; however, the rates started to increase since the beginning of 2007.
Table 3: Inflation of import-concentrated commodities in urban areas

<table>
<thead>
<tr>
<th></th>
<th>Point to point</th>
<th></th>
<th></th>
<th>Moving average</th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>General</td>
<td>Food</td>
<td>Non-food</td>
<td>General</td>
<td>Food</td>
<td>Non-food</td>
</tr>
<tr>
<td>Sep-05</td>
<td>8.93</td>
<td>10.43</td>
<td>7.47</td>
<td>8.36</td>
<td>7.69</td>
<td>9.03</td>
</tr>
<tr>
<td>Dec-05</td>
<td>9.07</td>
<td>9.02</td>
<td>9.12</td>
<td>7.49</td>
<td>6.57</td>
<td>8.43</td>
</tr>
<tr>
<td>Mar-06</td>
<td>7.33</td>
<td>5.65</td>
<td>9.04</td>
<td>7.71</td>
<td>7.39</td>
<td>8.03</td>
</tr>
<tr>
<td>Jun-06</td>
<td>7.81</td>
<td>5.80</td>
<td>9.85</td>
<td>8.39</td>
<td>8.65</td>
<td>8.13</td>
</tr>
<tr>
<td>Sep-06</td>
<td>7.82</td>
<td>7.66</td>
<td>7.99</td>
<td>9.29</td>
<td>10.80</td>
<td>7.78</td>
</tr>
<tr>
<td>Dec-06</td>
<td>6.24</td>
<td>6.34</td>
<td>6.14</td>
<td>7.12</td>
<td>15.44</td>
<td>8.04</td>
</tr>
<tr>
<td>Mar-07</td>
<td>9.84</td>
<td>11.46</td>
<td>8.24</td>
<td>13.57</td>
<td>19.38</td>
<td>7.79</td>
</tr>
<tr>
<td>Jun-07</td>
<td>9.75</td>
<td>11.24</td>
<td>8.28</td>
<td>14.66</td>
<td>22.76</td>
<td>6.56</td>
</tr>
</tbody>
</table>

Source: Authors’ calculation

A few interesting points can be observed if one compares rural and urban inflation rates of import-concentrated commodities. First, in the case of general inflation, the volatility of inflation rate in rural areas is much higher than that in urban areas. This is mainly due to higher volatility in inflation rate of import-concentrated food commodities in rural areas than that in urban areas. This explains seasonality of food production in rural areas, shortage of food supply in rural areas due to natural disasters, and higher prices of food commodities in the international market. Second, while inflation rate of import-concentrated non-food items has been declining in rural areas, the corresponding inflation rate in urban areas is relatively stable. This is more likely to be the outcome of lower weights of these items in rural areas and lower expenditure on import-concentrated non-food items by the rural people. Third, inflation rate of import-concentrated items is higher in rural areas than that in urban areas, mainly due to higher food inflation rate of import-concentrated items in rural areas. Though inflation rate of food items in rural areas (12.5 percent) is lower than that in urban areas (13.2 percent), the situation is opposite in the case of import-concentrated inflation rates. This is due to the substitution effect of imported commodities. Usually, there is less availability of substitution commodities of imported food items in rural areas and thus rural people have to face higher prices of imported commodities. However, lower prices of domestically produced food items may force the overall inflation rate in rural areas to go down. On the other hand, urban people have more access to substitute commodities of imported food items and thus experience a lower food price. However, they have to face higher prices of domestically produced food items due to higher transportation cost of food commodities from rural to urban areas and higher producer prices at the domestic level, which force the overall food inflation rate in urban areas to go up compared with rural food inflation.
National inflation

Until August 2007, non-food inflation rates (MA) of import-concentrated commodities at the national level were higher than the corresponding food inflation rates (Figure 3). Afterwards, the situation is reversed and both increased at similar pace. It is interesting to note that non-food inflation rate of import-concentrated commodities slightly declined in FY07-FY08. Thus it is clear that overall inflation rate of import-concentrated commodities during FY07-FY08 have been dominated by corresponding food inflation rates.

Pass-through of inflation of import-concentrated commodities

The estimation of inflation rate of import-concentrated commodities allows us to estimate the pass-through of import-concentrated commodities to overall inflation in Bangladesh during FY07 and FY08 (Table 4). The pass-through is defined as the ratio of import-concentrated inflation to overall inflation, considering corresponding weights in estimation. The estimated values confirm that the pass-through of imported inflation to overall inflation in Bangladesh has been increasing with higher contribution of import-concentrated food items than non-food items. The contribution of non-food inflation of import-concentrated commodities to overall inflation has been declining over the period. The trends are similar in both rural and urban areas. However, it is important to note that the pass-through of inflation of import-concentrated commodities is higher in rural areas than that in urban areas, mainly due to higher rural and food weights in the calculations.
Table 4: Pass-through of inflation of import-concentrated commodities

<table>
<thead>
<tr>
<th></th>
<th>National</th>
<th>Rural</th>
<th>Urban</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>General</td>
<td>Food</td>
<td>Non-food</td>
</tr>
<tr>
<td>Sep-06</td>
<td>60.86</td>
<td>53.44</td>
<td>67.98</td>
</tr>
<tr>
<td>Dec-06</td>
<td>49.52</td>
<td>36.09</td>
<td>67.94</td>
</tr>
<tr>
<td>Mar-07</td>
<td>46.52</td>
<td>35.36</td>
<td>65.14</td>
</tr>
<tr>
<td>Jun-07</td>
<td>48.41</td>
<td>41.63</td>
<td>59.17</td>
</tr>
<tr>
<td>Sep-07</td>
<td>56.37</td>
<td>59.68</td>
<td>53.10</td>
</tr>
<tr>
<td>Dec-07</td>
<td>68.94</td>
<td>84.38</td>
<td>48.79</td>
</tr>
<tr>
<td>Mar-08</td>
<td>80.76</td>
<td>106.02</td>
<td>45.21</td>
</tr>
<tr>
<td>Jun-08</td>
<td>93.80</td>
<td>126.78</td>
<td>42.51</td>
</tr>
</tbody>
</table>

Note: The pass-through at the national level is weighted average of the pass-through in rural and urban areas.
Source: Authors’ calculation

5. Conclusions and Policy Implication

The analysis shows that recent inflation in Bangladesh has been dominated by higher prices of import-concentrated commodities, especially of food items. The dominance of import prices, especially in recent times, indicates the vulnerability of a small open economy, such as Bangladesh, to foreign inflation. Since the Bangladesh economy is a price taker in the world market, several policies at trade policy levels are important. For Bangladesh, tariff reduction has limitations due to its possible adverse impact on the overall revenue generation and on prices of domestic substitutes. More than 100 percent pass-through of import-concentrated food commodities reflects the limited availability of domestic substitutes and calls for expanding the availability of substitute commodities so that international prices cannot affect domestic consumer price levels so strongly. This also calls for appropriate policy actions pertaining to sustainable food production in the long-run, and easing up demand pressures adopting appropriate policies.

In the long-run, greater efforts are required to build a strong food security system by investing more in increasing agricultural productivity as the area of cropland is declining rapidly due to urbanization and other forces. Effective use of land must be ensured by using quality seeds, better production techniques, and taking steps against floods to ensure smooth agricultural production. In this regard, appropriate long-run fiscal measures are required in terms of higher expenditures on agricultural research, addressing issues pertaining to climate change on food security, and ensuring higher farm level prices to producers of agricultural commodities. The government can subsidize the import of agricultural inputs such as fertilizer and pesticides with the intention to stimulate domestic production of food and reduce reliance on imports.

At present, policy responses of the government with respect to trade policies are confined mostly to tariff reduction and import subsidy on food items in cases where importers are already regulated or imports are controlled by a few large suppliers. In this context, it is important to consider that these are short term measures and can be highly distortionary and higher food demand exacerbates adverse terms of trade effect of higher import prices (Ter-
Minassian et al. 2008). It is also important to consider the prices of exportables as higher prices of imported inputs can have adverse effect on the country’s international competitiveness which is important to compete with trading partners.

The role of Bangladesh Bank in this regard is important for encouraging the banking system to increase credit support to the agriculture sector rather than increasing the budgetary support to the government. The former is more supportive to higher agricultural production, higher employment generation, and is less inflationary, which are urgent requirements for ensuring macroeconomic stability. On the other hand, budgetary support to the government may have higher inflationary impact on the economy and the outcomes in regard to agricultural production are not clearly visible.

The estimation of import-concentrated inflation rate in the present note suffers from a few caveats. First, in the CPI, it is not clear whether a specific commodity is domestically produced or imported. In addition, no information is available on imported inputs that are used to produce domestic consumer goods. Thus the present analysis relied on the source of import data to derive the use of imported items in estimating the inflation rate of import-concentrated commodities. Second, the estimation may suffer from a limitation arising from low commodity concentration in estimating CPI. In reality, there are many imported commodities in the market which may affect domestic inflation but are not included in the CPI basket.

References