

COMMODITY TAXATION - ANTIINFLATIONARY: MYTH OR REALITY

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INTRODUCTION:

Inflation is a global phenomenon in present day's time. There is hardly any country in the capitalist world today, which is not afflicted by the specter of inflation. It is an account of this that the phenomenon of inflation has widely attracted the attention of the economists all the world over, but despite that there is no generally accepted definition of the term 'inflation'. Different economists have offered different definitions of inflation.

For the layman to understand the term 'inflation' is as a sizeable and a rapid increase in the general price-level. Inflation in the popular mind is generally associated with rapidly rising prices, which cause a decline in the purchasing power of money. Neo-classical economist regarded it as a destroying disease born out of lack of monetary control whose results undermined the rules of business, creating havoc in markets and financial ruin of even the prudent. But now a day's inflation is recognized as a self-perpetuating and irreversible upward movement of prices, caused by an excess demand over capacity to supply there we see that important symptom of inflation may be rising of prices but every increase in price may not be said as inflation. It can be rightly said that inflation is caused by a combination of four factors i.e. the supply of money goes up the supply of other goods goes down, Demand for money goes down, and Demand for other goods goes up.

Almost every one thinks inflation as evil, but it isn't necessarily so inflation affects different people in different ways it also depends on whether inflation is anticipated or unanticipated. If the inflation corresponds to what the majority of people are

expecting (anticipated inflation), then we can compensate and that cost isn't high and if it is unanticipated there arises the problem.

It is often said that like tuberculosis inflation passes through three stages. In the first stage, the rise in prices is slow and gradual. In this stage, it is comparatively easier to check the inflationary rise in the prices of goods and services. But if inflation is not effectively checked in the first stage then like tuberculosis it enters into the second stage. Inflation, in second stage, becomes a serious headache for the government. The prices of goods and services now start rising much more rapidly than before. The government finds it difficult to keep the rising price-level under check. In the second stage, it is not possible to eliminate inflation completely, but if the government takes effective steps, it may be possible to prevent a further rise in the price-level. In the third stage, inflation assumes alarming proportions. In this stage, inflation degenerates into hyper-inflation or runaway inflation. The prices of goods and services now start rising almost every minute and it becomes impossible for the government to check them. The entire economy of the country is seriously disrupted. Finally, the government is compelled to resort to demonetization of the currency.

The above three stages of inflation can be illustrated with the help of an example. In the first stage, the prices do not rise in the same proportion in which the supply of money increases. In other words, the prices rise in a proportion less than that of the increase in the supply of money. For example, if the supply of money increases by 10%, the prices rise by 5% or even less than that. In the second stage, the prices rise exactly in the same proportion in which the

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supply of money increases. In other words, if the supply of money increases by 10%, the price-level also goes up exactly by 10%. In the third stage, the prices rise in a much greater proportion than the increase in the supply of money. In other words, if the supply of money increases by 15% or even more.

India is a fast growing economy and has the potential to compete with the other big economics of the world. However, a growing population, increasing inflation, political instability, need for infrastructure *development & many other issues are causes for concern for the Indian economy.* Infact, these issues are prevailing the growth of the Indian economy to a considerable extent. Out of these factors the impact of inflation that is felt across all sections. Inflation has direct impact on the lives of the people in the country. People's capacity to buy goods and services is effected by the inflation rate in the country.

An underdeveloped economy has to bear an impact of inflation during its economic development, especially when the process of growth happens to be at a rapid pace. Infact, the risk of inflation is, inherent in the very process. The level of investment required to break through the vicious circle of low income- low savings has to be on a large scale, and it is not always possible to meet that investment expenditure from taxation and current savings of the community alone. A certain amount of credit creation to finance the investment activity thus becomes nearly inevitable, and the resulting frictions and pressures get reflected on the general and sectoral price levels, though the degree of their impact varies in different sectors, as for example, in investment and consumption goods sectors and with in the latter with respect to some particular commodities. Thus by increase in national income, output and employment may, on the whole be said that inflation directly and & indirectly promotes the process of economic development in the country.

JUSTIFICATION OF THE STUDY:

Now a days it has been seen that there is continuous rise in the prices of commodities. Inflation percentage had increased to 13% in mid 2008. The Government had tried hard to curtail the percentage and it had succeeded too. Recently it has been seen that the percentage rate has gone down to 5.6%. Government had applied fiscal and monetary measures and direct method to have control on the rate of inflation.

OBJECTIVES OF THE STUDY:

1. To analyze the various methods of control on inflation.

2. To examine that commodity taxation is anti inflationary or not.

METHODOLOGY OF THE STUDY:

The present paper is based on Primary as well as Secondary Data. The Primary Data are collected through observations; experience, discussions and opinions of experts and Secondary data are collected from different sources like Newspapers, magazines, journals and published reports of Government of India. Some latest data related to subject are also collected through Internet. The related data are analyzed according to the needs of study. This study systematically covers prices, goods and services and distribution of commodities. Commodity taxation is anti-inflationary, is it myth or reality. Finally, on the basis of this study, conclusions and some suggestions are offered.

ANALYSIS OF VARIOUS METHODS OF CONTROL ON INFLATION:

Price rise has become a problem for the Indian economy and to control the price rise some measures has to be taken. These measures can be classified as monetary measures, fiscal measures and direct measures.

A. Monetary measures, which can be used to control inflation, can be raised as follows-

1. **Bank Rate:** This is the very traditional method to control the inflation; by raising the bank rate, bank borrowings are discouraged, this will minimize the bank credit. Bank also raises their bank rates on deposits this will lead to more savings in bank.
2. **Open Market Operation (OMO):** By selling securities the central bank reduces the amount of cash held by the banking system. When bank purchases securities there is a flow of cash into the coffers of the central banks as a result of which cash base commercial banks support credit becomes narrower.
3. **Reserve Ratio:** Another measure is to increase the reserve ratio, when this amount in large quantity is kept for reserve then much lesser amount is left to support the credit.
4. **Selective Credit Control:** Another measure can be by making very stiff conditions before the customers who extends loan from the bank for purchasing durable goods and bank also reduces the borrowing capacity of traders.

B. In the fight of inflation fiscal measures also play a vital role; this can be done through following ways-

1. **Increasing Tax Rates:** By increasing tax rates on selected commodities as well as imposing new taxes these things will reduce the purchasing power from customers. To cut personal consumption expenditure the rate of personal, corporate and commodity taxes should be levied but the rate of taxes should not be high as to discourage savings, investment and production. Tax system provides larger incentives to those who save, invest and produce more. This method are bound to be effective in controlling inflation by increasing the supply of goods within the country, the government should reduce import duties and export duties.
 2. **Increase in Savings:** Another measure is to increase savings on the part of the people. This will tend to reduce disposable income with the people and hence personal consumption expenditure. But due to rising cost of living people are not in the position to save much voluntary.
 3. **Reduction in unnecessary expenditure :** This measure would be by reducing the unproductive expenditure. It has been also seen that in some developed states, large expenditure is done on a number of commodities and commissions functioning under different ministries. The number of such commodities and commissions if curtailed or minimized then the expenditure incurred would be less.
 4. **Public Debt:** At the same time it should stop repayment of public debt and postpone it to some further debt till inflationary pressure are controlled within the economy
- C. Another method that could be applied is direct measures:**
1. **Wage Policy:** An appropriate wage policy can be an effective weapon to control inflation. Trade unions can play a very important role in making it possible for the government to follow a rational wage policy.
 2. **Importing Commodities:** To improve the supply position government can import essential commodities which will control the prices of domestic prices but this could be possible in developed countries only.

3. To increase production: The following measures should be adopted to increase production:

- A. One of the foremost measures to control inflation is to increase the production of essential consumer goods like food, clothing, kerosene oil, sugar vegetable oils etc.
- B. If needed, raw materials for such products may be imported on preferential basis to Increase the production of essential commodities.
- C. There should be made efforts to increase productivity.
4. **Price control:** Price control means fixing an upper limit for the prices of essential consumer goods. There are maximum prices fixed by law and anybody charging these prices is punished by law.
5. **Rationing:** It aims at distributing consumption of scare goods so as to make them available to large number of consumers. It is applied to essential consumer goods such as wheat, rice, sugar kerosene oil, food oil etc. There should be stabilization in prices of necessary goods and also ensure distributive justice.

For the effective control there should be a coordination of both monetary and fiscal measures so that effective results could be achieved.

STEPS TAKEN BY RBI TO TACKLE INFLATION:

It includes a rise in repo rates (the rates at which banks borrow from the RBI), a rise in Cash Reserve Ratio and a reduction in rate of interest on cash deposited by banks with RBI. The RBI's measures are expected to suck out a substantial sum from the banks. In effect, while the economy is booming and the credit needs grow, the central bank is tightening the availability of credit. The RBI also buys dollars from banks and exporters, partly to prevent the dollars from flooding the market and depressing the dollar indirectly raising the rupee.

DOES THE COMMODITY TAXATION ANTI-INFLATIONARY?

To understand that if commodity taxation is anti inflationary or not there must be a glance on causes of inflation. In India the reason for increasing rates of inflation are increase in demand and fall in supply causes rise in price, a growing economy has to pass through inflation, lack of competition and advance

technology (i.e. increase cost of production and ultimately there is rise in price), defective monetary and fiscal policy, hoarding (when trader hoard goods with intention to sell later at high price), weak public distribution system, increase in population and decrease in production etc. To have an eye on these factors government had to make measures for it in which one good source is of taxation, government tax because major source of income can be achieved like revenue tax, wealth tax, service tax, commodity tax etc from which the amount (revenue) collected is used for the welfares like infrastructures, roads, schools etc. are made for which government is accountable. It is major sources of revenue to generate funds from public. Here it can be seen that there is a recycle of inflow and outflow of money from government to public and vice versa. It is necessary only in developing countries like India and could not be seen in developed countries as there is no need of making capital expenditures.

It is believed that inflation is closely associated with deficit financing, which means that fresh notes and coins are circulated in the economy, which causes an extra quantity of money. Another aspect of price rise in the general level is inelasticity in the supply of goods and services. More production could be made if the existing supply is completely utilized and if additional production is not build in time there would be an excess of demand over supply leading to increase in inflation in the economy. This situation can be minimized by either curbing the demand or by augmenting the supplies or by both simultaneously. For curbing the demand is to take away the excessive purchasing power in the hands of the people all immediate stoppage of fresh additions to the supply of purchasing power out of deficit financing is a very essential condition to control inflation.

Another aspect is to tax heavily on non-essential investment projects in the private sector and directly eliminate such projects from the public sector. This can be improvised by making essential investment to those industries that cater to the basic needs of the people so that an anti- inflationary allocation can be made. Commodity tax decreases the capacity of purchasing power of people and at the time of inflation seller charges the highest price for the commodity. So commodity taxes are fiscal measure and by themselves would not be said as anti-inflationary. One another reason for inflation is the time lag between the investment and the fruition of the investment i.e. gestation period. This gap is to be cut down and it is

possible only when investment be made on quick yielding projects.

Sales and excise taxes are in all likelihood typically shifted forward in the form of higher commodity prices. Their anti-inflationary influence arises from their effect in reducing real purchasing power by raising commodity prices relative to factor incomes. Unlike other price increases, this type does not have a spiraling effect because it does not generate additional income. Sales and excises have some relative advantage over income taxes so far as inflation control is concerned. They place a heavier relative burden on persons spending high percentages of their incomes and compel them to reduce consumption. They give some incentive to spend less and save more. In addition some persons may tend to spend the same dollar sum, including tax elements, as before. If persons attempt to maintain their old consumption levels of goods and services, they increase their tax liability by so doing. On the other hand, much of the greater anti-inflationary advantage of the sales and excise taxes will be lost if they generate wage increases. The sales and excise taxes may also offer some limited advantage from the standpoint of production incentives, but this can easily be exaggerated. The principal objections to the sales and excise taxes are equity ones; the levies conform much less closely to accepted standards of equity in taxation than the income tax. Sales and excise taxes, as well as the income tax, are greatly inferior to the expenditure tax as anti- inflationary measures, and the latter is more equitable than the commodity taxes.

CONCLUSION:

After critical analysis it has been seen that commodity tax is really anti-inflationary or not. Hence, we have concluded that commodity tax is not anti-inflationary because it is entirely unable to control on inflation, although taxation what ever may be income tax, wealth tax, service tax, commodity tax etc. it is a fiscal measure of control on inflation but government of India having a major source of income is by imposing various taxes and also collect large amount of revenue from public. The important question arises that how to manage capital expenditure from which funds? Simply, we can see that government have incurred capital expenditure from revenue, which was collected from taxation. This things inflow and outflow of cash from government to public and vice versa. The commodity tax is not able to

control on inflation due to above reason. Thus, it is clear that commodity taxation is not anti-inflationary. It is a myth it is not a reality because capital expenditure is essential for economic development. This expenditure cannot be ignored otherwise all the economic system would collapse in developing countries like India. Now we can say that capital expenditure may be curtailed but cannot be ignored. At last we conclude that we manage men, men manage things, managing men is equipping them, empowering them and inspiring them for excellence.

SUGESIONS:

In order to have control on inflation there should be curtails on government capital expenditure and that should be also utilized in a productive work or affairs from which income can be raised. Another remedy would be to increase production in an effective manner so that there would be balance of demand and supply of goods and services. Other monetary and direct

measures should not be ignored as to achieve good results to check on inflation. In developing countries there should not be too much of control on inflation as this will hinder the progress of the country but inflation must be within a limit and easily digestible.

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