The Price Stability-Important Lever within the Economy

Maria Mirabela Florea Ianc
"Constantin Brancusi" University of Târgu Jiu ,Faculty of Economics
mariamirabela04@gmail.com
Loredana Ciurlău,
„Constantin Brâncuşi" University of Târgu Jiu, Faculty of Economics
lciurlau@yahoo.com

Abstract

One of the biggest problems that have confronted the authorities, whether fiscal, monetary, either along the time is represented by the generalised increase in prices (inflation), which is why it is not considered good at the level of an economy, because it is presented as a nominal increase of PIB, namely the erosion of the economy as a whole, not least, to generate macroeconomic imbalances

The inflation creates pressure not only on monetary plan, and the plan as general economic, political and social. This, in addition to generating a sharp decline in savings, discourages investment and favors moving the capital in assets that generate real revenue.

Key words: stability, authorities, problems, economy
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1. Introduction

Benefits of price stability in the economy and the costs associated with inflation or deflation, are always closely linked to money and its functions.

So it can be said that in a world without money, respectively in a barter economy, the costs associated with the exchange of goods and services, such as information, search and transportation costs would be very high. Money always increase the efficiency of trade, thereby contributing to the welfare of all citizens.

The money always plays an essential role in modern economies. Certainly, no exaggeration to say that "money makes the world go round" and that modern economies could not function without money (Stavre John – Gabriel, 2014)

It would therefore be useful to define money in general terms. Money can be considered a very special good that fulfills some basic functions. Money should serve mainly as a medium of exchange, store of value and unit of account. For this reason, it is often said that "money is what I do."

The money plays one of the most important roles in the economy, because through them all and to make transactions and exchange market.

2. The importance of price stability

One of the biggest problems faced Authority, either monetary or fiscal, over time is the creţterea in general prices (inflation), which is why it is not considered good for the economy because Growth is presented as nominal PIB or erosion of the whole economy, and not least, generating macroeconomic imbalances. (http://www.insse.ro)

The inflation was created pressure not only on monetary plan, and the plan as general economic, political and social. This, in addition to generating a sharp decline in savings, discourages investment and favors moving the capital in assets that generate real revenue.

Lately, and especially in recent years more and more countries have opted for inflation targeting, for macroeconomic policy orientation towards ensuring price stability.

The great influences on the stability of prices in the economy has The inflation and deflation So in principle, **inflation** is defined as a general increase in prices of goods and services on a long time, which leads to lower value of money and thus power their purchase. The opposite of inflation is **deflation** that unlike inflation that occurs when the general price level falls over an extended period.

In the absence of inflation or deflation, we can talk about price stability if, on average, prices neither increase nor decrease but stay stable over time.

Price stability is generally defined by the European Central Bank's Governing Council, as an annual pace of increase in the Harmonised Index of Consumer Prices for the euro area of below 2%.

For an understanding of this phenomenon more obvious can imagine a shopping cart filled with various products, the price of this basket is checked periodically by calculating growth, and in rarer cases decreasing annual prices. If the price increase is less than 2% have, according to the quantitative definition of price stability.

So the objective of the European Central Bank and the Eurosystem is to keep prices stable, that is to maintain inflation rates below but close to 2% over the medium term.

Within the Central Bank is carrying out two types of analyses in order to be able to see what is the level of inflation rate: (Elena Bojeţeanu, Bucharest, 2011)

- the monitoring of a series of factors, such as increased economic and oil prices, factors that could lead to further increases in the short term
- the pursuit of money circulation in the economy because they could cause an increase in prices in the medium and long term

Another thing which makes the European Central Bank is to set interest rates. With the higher interest rate will be lower demand for money which leads to a price stability over time, establishing customer trust and facilitating savings and investments; companies invest more than your economy grows creating default your new jobs.

One very important thing is that you have to distinguish between variations in the prices of any goods or services deemed to be individually and the general level of prices. Frequent changes of individual prices are relatively normal market economies, even when prices are stable as a whole. Modification of the conditions for the application and/or offer different goods or services considered individually, leads inevitably to price variations.

In an tough economy there are millions of individual prices. These prices are subject to continuous, reflecting essentially changing demand and supply of goods and services and thus indicat a relativity individual goods and their respective services. Clearly, it is neither feasible nor desirable for all these prices to be considered, but neither appropriate for only some of them to be analyzed because it may not be representative of the general price level (Elena Bojeţeanu, Ana Simona Manu Razvan Stanca Victor,2011)

3. Consumer price index

In most countries there is, or using a simple approach and judicious in terms of measuring inflation, using the so-called "price index for consumer (CPI) because in fact, the consumer price index, which measures price changes in consumer goods and services is not the only price index in an economy. Another index a similar economic importance is the Producer Price Index. This index measures changes in the selling prices, while operated by producers of goods and services.

When using the consumer price index, considering only purchasing patterns of consumers to identify goods and services that they buy habitually and which can be considered implicitly as to some extent representative of the average consumer in her economy. These include not only the items they purchase everyday buyers (eg bread and fruit), but also durable goods (for example such as cars, computers, washing machines, etc.) and frequent transactions (such as rents). (Costica, I. 2005):

The registration of these items in a "shopping list" and weighting them according to importance in consumer budgets leads to the creation of what is known as "basket" (https://www.ecb.europa.)

The consumer basket is the fact that these goods are weighted according to the share they hold in final monetary expenditure of households and in practice, the weights in the basket are reviewed regularly to reflect changes in consumer behavior.

An army of "control price" checks each month the prices of these items in various outlets. Subsequently, the costs of this basket are then compared over time, which allows for a series for the price index. The annual rate of inflation can then be calculated by expressing the change in the costs basket today as a percentage of the costs of the identical basket in the previous year. (https://www.ecb.europa)

But still however, changes in the price level, identified by such a basket only reflect the situation of a consumer "average" or representative. But if a person's buying habits differ substantially from the average consumption pattern and thus the consumption basket underlying the index, it is possible that this person may experience a change in the cost of life different from that suggested by the index. Therefore, there will always be people who experience an "inflation rate" highest in terms own basket in t imp others will perceive the contrary, a "lower individual rate of inflation". In other words, the inflation measured by the index is only an approximate measure of the average situation in the economy.

We could illustrate the above with a simple numerical calculation. Suppose that a representative market basket of the yearly expenditure of teenagers is 100 pieces of hamburger, 50 soft drinks, ten drinks with acid and a scooter.

Table No. 1. Measuring inflation - example

	Amount	Price -Year 1	Price -Year 2	Price -Year 3
Hamburger	70	7 lei	8 lei	6 lei
Fizzy drinks	100	5 lei	4 lei	7 lei
Non-acid drinks	50	4 lei	6 lei	5 lei
scooter	1	100 lei	150 lei	200 lei
The cost of the consumer basket		1290 lei	1410	1570
Price index		100	110	122

Source: my interpretation

The total cost of the basket can then be calculated by multiplying the quantities by the respective prices and adding the results. It is easy to see that between the first and second year, the cost of this basket of goods has risen from 1290 RON to 1410 RON, or by 10%. Between the first and the third year was recorded an increase in the cost of 1290 RON to 1570 RON, the equivalent of 20%.

Price index is another way to express this. To compute the price index, the cost of the market basket in any period is divided by the cost of the consumer basket in the base period, and the result is multiplied by 100. In the table above, year 1 is the base period. So, the price index for year 3 is:

$$\textbf{Price index} = (P3/P1) \times 100 = (1570/1290) \times 100 = 121{,}70 = 122$$

The price index tries to give an overview of the evolution of a large number of prices. But as the example shows, the price index may rise despite some prices actually declining.

However for various reasons, any attempt to express the overall change -a number of prices presents some difficulties.

It may be observed first that, an existing basket becomes, over time, increasingly and less representative and me, as consumers increasingly tend to replace more expensive goods for cheaper ones. So if the weights are not adjusted, index variation may lead to a slight overestimation of growth "true" price. Second, changes in quality are sometimes difficult to incorporate into the price index.

In the event that quality of a product improves over time and the price also rises, some variation in price is due to the improved quality. Price increases due to quality changes can not be regarded as giving rise to inflation, as it does not reduce the purchasing power of money. Changes in quality are commonplace over long periods. (Stavre John – Gabriel, 2014)

From all discussed it may be noted that price stability supports higher living standards by helping you have the information above explains why inflation and deflation are generally undesirable phenomena.

Indeed, there are substantial disadvantages and costs related to inflation and deflation. Price stability prevents these costs and brings significant benefits to all citizens. There are several ways in which price stability contributes to achieving high levels of economic prosperity, such as a high employment of labor.

So price stability supports higher living standards by helping it has to:

Reducing uncertainty about general price developments and thereby improve the transparency of relative prices

- reducing risk premiums in interest rates associated with inflation included
- avoiding unnecessary hedging operations
- reducing the distortive effects of taxation systems and the social security
- increasing the benefits of holding cash
- prevent the arbitrary distribution of wealth and income
- financial stability

Therefore price stability enables the public to easily identify changes in the prices of goods relative to other goods ("relative prices"), bearing in mind that such changes are not concealed by fluctuations in the general price level.

Otherwise maintaining price stability, central banks contribute to broader economic goals

4. Conclusion

The main objective, natural and otherwise, of a country and especially central banks is to keep prices stable. Price stability is defined as an annual pace of increase in the Harmonised Index of Consumer Prices for the euro area of below 2%.

Any monetary policy regime is based around a nominal anchors, defined as intermediate target to achieve specific objectives.

Each economy is built on its way, with its customs and monetary policy must adjust to these features, otherwise be rendered meaningless.

Benefits of price stability and the costs associated with inflation or deflation, are closely linked to money and its functions

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