

Answer on Question #44605 – Economics – Macroeconomics

How can the high rate of inflation in a developing country like Uganda be solved?

Solution

There is no doubt that inflation is detrimental to development. During times of inflation, both the consumers and the firms are adversely affected. In fact, inflation can directly cause an increase in the poverty incidence of a country and indirectly cause higher unemployment rates. There are several proposed methods in order to solve the problem of inflation. Basically, these solutions require government intervention. Gone are the days when the prices and the flow of the economy is left to the market forces. This view, which is advocated by Adam Smith, is no longer applicable to the contemporary setting especially with the advent of increasing globalization among countries. The role of the State according to Adam Smith is supposed to be confined into three functions. The first function is that it must defend a country against attacks. The second function is that it must establish an administration of justice. The third function is that it must provide for collective benefit projects. All these three functions are still relevant and pertinent nowadays but certain functions have to be added in order for the state to become effective. This is especially true in the case of inflation, which can be solved through government intervention.

In order to solve inflation, the government can resort to various acts. The government can regulate the transfer of foreign currency reserves. The government can impose restrictions in the transfer of foreign currency reserves outside of the country. This will be able to lessen inflation because the depletion and reduction of the foreign currency reserves will be prevented. Another act that the government can do to solve the problem of inflation is to lift certain import controls. By lifting import controls, a country is able to increase the supply of certain products and services since more foreign products will be able to enter the domestic market of a country. This will result to the balancing of supply and demand.

The government plays a significant role in the development of the economy and in the fight against inflation. Therefore, it is imperative to allow the government to perform regulatory acts that will prevent or eliminate inflation.