Impact of Stagflation on Markets

What is the issue?

Authorities worldwide are trying to formulate appropriate set of policies to ensure that the current inflation is cooled without triggering a recession.

What is stagflation?

- Stagflation is characterized by slow economic growth and relatively high unemployment (economic stagnation) and at the same time accompanied by rising prices (inflation).
- Stagflation was first recognized during the 1970s when many developed economies experienced rapid inflation and high unemployment as a result of an oil shock.
- Stagflation led to the emergence of the **Misery Index** which is the simple sum of the inflation rate and unemployment rate.
- The **Phillips curve** states that inflation and unemployment have an inverse relationship.

The Misery Index measures the degree of economic distress felt by everyday people, due to the risk of joblessness combined with an increasing cost of living.

What has sparked the latest concerns about stagflation?

- **Covid-19**- The outbreak of the Covid-19 pandemic and the curbs imposed to contain the spread of the virus caused the major recent economic slowdown worldwide.
- **Fiscal and monetary measures**- The measures taken to address the downturn, including substantial increases in liquidity in most of the advanced economies fuelled upsurge in inflation.
- **Ukraine war**- The ongoing war in Ukraine following Russia's invasion and the consequent Western sanctions on Moscow has caused a fresh supply shock.

What lies ahead?

- We've been hit by historically large inflationary shocks since the pandemic.
- There's a need to look the economy that's coming out the other side to find price stability.

References

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