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Structural Drivers of Inflation in South Asia: Crisis and Continuity in the 2020s Global Economy

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Abstract

South Asian countries have gone through a high inflation rate since 2020, triggered by the COVID-19 pandemic and later followed by the war between Russia and Ukraine. While inflation is mostly a macroeconomic phenomenon explained through the money supply in the economy or the demand side factors, this paper primarily focuses on long-term structural vulnerabilities in South Asia that fuel the high inflation rate in this region. The primary objective of this paper is to find out how different structural problems in South Asian countries have influenced the high inflation trend during the 2020s. Three countries from South Asia, Sri Lanka, Pakistan, and Bangladesh, are used as case studies to compare inflation patterns in different countries in this region and the role of these structural weaknesses in the high inflation rate in each country, to offer a deeper understanding of the long-term macroeconomic problem like inflation in the developing countries.

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List of Abbreviations

ADB	Asian Development Bank
CPI	Consumer Price Index
FPMU	Food Planning and Monitoring Unit
FY	Fiscal Year
GDP	Gross Domestic Product
GNP	Gross National Product
IMF	International Monetary Fund
IOM	International Organization for Migration
MPC	Monetary Policy Committee
MSES	Micro and Small Enterprises
NAIRU	Non-Accelerating Inflation Rate of Unemployment
QTM	Quantity Theory of Money
SAARC	South Asian Association for Regional Cooperation
USD	United States Dollar
WGI	Worldwide Governance Indicators
WTO	World Trade Organization

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Chapter 1: Introduction

"Inflation," one of the most underlying economic concepts, often indicates the chronic increase of the price level of different commodities, generally in a certain period. Flemming defined the inflation rate as the proportionate changes of general price levels in an economy over a given period (Baranzini and Cencini, 1996, p. 22). Besides, Renowned Economist Milton Friedman compared inflation to a disease that can destroy the whole society (Chen, 2022, P.2). Inflation is a global macroeconomic phenomenon that significantly affects the economic development of individual countries, especially emerging and middle-income countries, by reducing economic activities among people. Though a moderate inflation rate is inevitable, a high one can hinder economic growth. According to a report by the Federal Reserve Bank of Dallas, there are generally four types of costs of monetary inflation, including inflation increasing money-holding cost that raises banking and information costs for future trade; sellers need to cut down their marketing costs along with decreasing their investment and workforce count; high inflation creates uncertainty in future trades and inflation negatively impacts the production costs and outputs (Rogers & Wang, p. 44).

However, the International Monetary Fund published a working paper in 2000 using threshold regression where they claim that, the critical point of inflation for industrial countries was estimated to be 1-3% whereas for developing countries 7-11% above this level the economic growth of a country negatively affected[1] (Senhadji & Khan, 2000, p. 2). The data provided by the IMF shows that developing countries have higher inflation expectations [2]than developed or industrial countries due to different economic dynamics and structural challenges like lack of fiscal sustainability, lack of transparency in central banks, financial openness, etc (Ha, Kose and Ohnsorge, 2019, p. 224). However, Inflation has a significant impact on developing countries, especially the rising food prices, high living costs, external debt, currency devaluation, uncertainty in investment, etc as a large portion of the population lives in poverty, they keep their assets in cash and heavily depend on wage income, social benefits or pensions (Ha, Kose and Ohnsorge, 2019, p. i5). Food and energy prices are more

[1] Threshold analysis is a statistical technique used to identify the specific point of variables at which it shows a different outcome occurs for any economic aspect.
[2] This term means what people believe will happen to prices in the future. If they expect prices to go up, they might spend more or demand higher wages now, which can cause inflation to rise.

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volatile than other consumer products in these developing countries due to poor infrastructure, supply constraints, and external shocks. Over the past few years, during and after the pandemic in 2019, global inflation peaked at its highest level after 2011 due to continuous lockdowns, supply chain disruptions, poor labour market conditions, and surging commodity prices, followed by the ongoing Russia-Ukraine war since 2022. This high inflation rate has also become an inevitable concern for South Asian countries due to their substantial dependency on imports of petroleum energy and essential food items to satisfy growing demands.

South Asia, which is one of the fastest-growing regions with flourishing large economies like India, has encountered challenges in maintaining a stable commodity price over the preceding years. Several countries in this region showed a peak in the inflation rate during the 2020s. Though the area is going through high economic growth, such as nearly 6% in 2024 according to the World Bank (Chung, 2024), the countries are facing challenges like income inequality, low purchasing power, poverty, political instability, debt crisis, unemployment and social unrest and violence due to high and unstable commodity prices and inflation. For example, in Bangladesh, the cost of primary crops has increased by 15-20% in 2024, causing social and political unrest throughout the country as people working in different sectors are engaging in strikes and protesting on the road by demanding high wages as the living and food expenses have raised in significantly in past few years become a concern for labour groups and middle or low-income families (Abdin, 2024).

The global pandemic and geopolitical tensions are not the only contributors to the inflation peak in this region throughout the 2020s, though they have played a significant role. Accompanied by specific monetary or fiscal policies like the overflow of money supply, exchange rate volatility, low interest rate, tax cut, debt, etc., several structural challenges stimulate the inflation trends in South Asian countries due to their unique social, environmental, economic, or political characteristics. These factors directly affect the production cost, supply chain, and use of resources, significantly impacting this region's high commodity prices.

South Asian region plays a significant role in the global political economy due to the presence of India, the sixth largest economy of the world, the diplomatic engagement of the US and China, two superpowers with South Asian countries like India or Bangladesh, the

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geographical location, the export-led growth strategies and interest of foreign investors (Ganguly and O'Donnell, 2022, pp. 470-482). Countries like India, Pakistan, Sri Lanka, and Bangladesh are the key players in global trade and investment sectors like IT, textiles, and pharmaceuticals, significantly impacting global commodity prices. So, studying South Asian economic crises like high inflation is vital for regional stability and global prosperity. Though there are several studies on the causes of high inflation and volatility in South Asia, there is a gap, as most of the studies are primarily based on the significance of monetary policy or fiscal policy inadequacies, overlooking the critical expectations of long-term structural factors. This can be better explained by the view of Dagum, who claimed that inflation usually originates from a combination of economic, social, and political causes (Madito, 2021, P. 73-78). Hence, traditional macroeconomic models often fail to capture all these structural challenges. So, this study will contribute to bridging the gap by comprehensively analyzing these structural factors causing inflation in the South Asian economy.

This paper aims to delve into the structural factors that have affected the unstable inflation rate of South Asian countries from 2020 to the present. Many South Asian countries went through several economic turmoils during this period due to the changing nature of global economic trends and national economic policies, political instability, natural disasters, and operational bottlenecks. The current fluctuations in fuel and food price inflation rates in these countries are a growing concern. They significantly impact the global economy by disproportionately affecting many people and aggravating economic inequality. Due to South Asia's diverse socio-economic structure, including high population growth, poverty, social stratification and caste, political instability, etc., the traditional economic theories often fall short when dealing with the inflation dynamics in this region as they are mostly limited to monetary and fiscal gaps.

The inflation dynamics in South Asia also need a more in-depth analysis of the long-term structural vulnerabilities, including aspects like supply-side constraints, institutional weakness, labour market rigidities, etc, to fully recognize the drivers of high inflation and its volatility in this region. Therefore, the key purpose of this study is to ascertain the underlying structural factors that drive inflationary trends in the South Asian region by focusing on some South Asian countries as case studies, which are primarily vulnerable to inflation volatility since 2020. To provide an extensive analysis of inflation dynamics in this region, the study seeks to provide valuable insight into the underlying factors of Inflation in South Asia by

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answering some primary questions like **"What were the key structural factors contributing to the inflation peak in South Asia in the 2020s?", "How do structural factors in South Asia challenge traditional inflation theories, demonstrating the insufficiency of a single theoretical framework in explaining the region's inflation dynamics?"**

To answer these questions, the study delves into both theoretical and empirical South Asian analysis using the historical lens and case studies. Three countries from South Asia, Bangladesh, Sri Lanka and Pakistan will be used as case studies accompanied by references from other South Asian countries as these countries have been confronted with high inflation rates and inflation volatility in recent years due to complex structural obstacles such as recent political instability inside these countries, inefficient infrastructure, their dependency on agriculture, high population growth and so on. Through a critical discussion of traditional inflation theories like the Quantity Theory of Money, Keynesian theories, Demand-pull, Cost-Push theories, and others, the study will emphasise the limitations of these conventional theories to capture the inflation scenario in this region fully.

The paper will make an exceptional contribution to the study of GPE as it will help the readers understand South Asia's unique and challenging economic environment. The diverse political economy of this region provides a complex instance for policymakers to scrutinize the underlying causes of inflation in developing countries. By analysing the inflation dynamics in South Asia, this study will help to offer valuable insight to promote economic stability globally. The findings of this paper will be a crucial component in the study of traditional macroeconomic theories of inflation, as they causally overlook the structural challenges of the developing world. Most of the time, economists, policymakers, or international organisations try to frame the developing world in a common framework without considering the individuality of each country, causing policy failures and economic instability. Considering the divergent structural challenges, the study will provide a context-sensitive approach to global Inflation dynamics.

The study used the "Quantitative Descriptive Analysis" methodology (QDA), which is primarily based on quantification and measurement. Herbert Stone and Joel L. developed the analytical method for quantifying results using a scientifically rigorous procedure and producing direct, generalizable outputs (Kemp, Hort and Hollowood, 2018, p. 288).

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Descriptive analysis mainly focuses on the statistical summarisation of the primary features of a data set. It is a non-experimental study approach that describes a situation, population, or phenomenon without testing a hypothesis, instead focusing on data collections like observations or surveys to quantify and then summarize (Mursa et al., 2025). However, the quantitative method has been used in this study to compare and analyze the inflationary trends in South Asia since 2020 by using secondary data collected from reliable resources such as IMF, World Bank, Asian Development Bank and Central Banks databases of Individual countries, primarily focusing on the inflation rates and volatility in different periods. The study used descriptive techniques to analyze the data, including cross-country comparison, time series analysis, and changes in mean and percentages. The internal validity has been ensured in this study by comparing countries with similar structures. However, external validity faced limitations as it solely focused on a single region, South Asia, and countries were chosen based on data availability.

The study unfolds in the following manner. In the introductory chapter, I consider the conceptualisation of “Structural Factors” by providing a short analysis of the definition of structure and structural factors in social science and economics, as it is crucial to understand the concept before going into an in-depth analysis. Later, I provided a glimpse of historical events related to inflation in South Asian countries in the 21st century, starting from 2000. a detailed literature review by considering the previous research focusing on global perspectives on inflation trends in developing countries. Understanding the prominent ideas of inflation plays a vital role in answering the research questions. In the 2nd chapter, I will outline and expand my theoretical foundations for the study by illustrating some critical theories of inflation that have been used for years to understand the underlying causes of inflation in different situations, along with some gaps in those theories.

The 3rd chapter will focus on the empirical analysis of structural challenges that drove the inflation peak in South Asia in the 2020s by analysing the case studies from Bangladesh, Sri Lanka, and Pakistan, providing a comparative analysis among those countries considering both local and global factors. The 4th and final chapter will concentrate on some of the traditional inflation theories by critically analysing their relevance and applicability in the context of South Asia. This chapter will also include policy recommendations and strategic aims to control high inflation dynamics and their fluctuations in developing countries.

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Understanding the structural factors

The term “Structure” was derived from the Latin word “structura”, referring to “fitting, building, or placing together”, which was introduced by Karl Marx and Emile Durkheim in the studies of social science during the 19th century (Patomäki, 2021, p. 18). The term is widely used in social science and economics, holding different meanings to demonstrate the arrangements and interconnectedness of various components of a society and economy. In economics, structure refers to the system in which other economic activities are arranged, such as market resources, production system, or distribution of resources. These are the compositional arrangements of a society, which include sectoral distribution of labor, patterns in government finance, trade, agricultural industry ratio, etc. In contrast, in social science, “structure” refers to the mechanisms of society that carry out the functionality of society. Social science often refers to structure as the stable patterns of social relations, including social institutions, classes, power relations, etc., which exist independently. According to Anthony Giddens, structure is the rules and resources of a society that guide the social practices over time (Giddens, 1984, p. 25). According to Ashley, social structure refers to a set of organised social institutions and institutional relationships that work to form a society.

Besides, Karl Marx, in his book Capital Vol 1, claims that “the economic structure works as a real basis which raises the political and juridical superstructures by influencing some definite social forms of thought” (Patomäki, 2021, p. 18). That means the economic structure isn’t solely market-based; rather, it identifies the underlying social relations for producing and distributing wealth. He also mentions the class structure of the society. Karl Marx's class structure is widely used as a component of broader economic activities that identify the position of people in a production system as owners and laborers. In neo-classical theory, the term structure is used as composition, specifically the quantity of market units or the involvement of the public in a market economy (Patomäki, 2021, p. 20). It usually refers to the arrangements of markets, the number of firms, the competition level, etc, which are evident in the discussion of market structures or monetary or fiscal frameworks. According to the neo-classical theorists, structure is more of a functional arrangement in an economy and less about power struggle among different social groups.

However, the term “Structure” in the study of inflation was brought into light by Prebisch in Latin America, as the structuralist view of inflation is still used as a primary policy tool of

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inflation (Madito, 2017, p. 15). The concept of structural factors in inflation was introduced 40 years ago as a part of economic outcome, and these factors indicate the aspects that don't change with the financial cycle; they are substantially constant or enduring (Totonchi, 2011, p. 460). These structural factors are persistent and deeply embedded aspects that shape a country's financial performance and growth. Identifying all structural factors, both economic and social, proves challenging as they aren't directly observable and vary from country to country. Still, some common categories of structural aspects may include market structure, supply/demand side factors, socio-economic factors, or institutional factors of an economy, which are explained here. These factors are indicated as structural, not only because they influence the inflation rate, but also because they are persistent and often deeply embedded in a social and economic system, which shapes the inflationary dynamics over time.

Initially, the market structure of economics deals with the competitive nature of the economy, which significantly impacts consumer prices and the welfare of the entire market, from monopoly to perfect competition. It determines how organisational behaviour and market competition influence economic outcomes. Similarly, the supply and demand side structural factors determine the ability of a firm to supply the goods or services to balance with the consumer demand side for proper utilisation and production of those products (Harland, 2024, p. 1). The supply-side structure deals with the units of the sub-parts of firms and organizations that work for resource procurement, operation, and distribution of products and services (Harland, 2024, p. 1). The suppliers sell the raw materials of production or service to the intermediate or final consumer for manufacturing and distribution. On the other hand, demand-side structural factors deal with the overall frameworks of behaviour and purchasing power of consumers, along with other elements that tackle the market demands for products and services (Firat & Hao, 2023, p. 11).

Moreover, the socioeconomic structure of a country links the social arrangements and economic stratification within a country that may include a class system, wealth distribution, social group connectivity, and different economic activities within a society. The term "socio-economic" is defined as a holistic approach where competitive behaviour is considered as a fraction of human behaviour focusing on the need for societal sources for effective market functioning that are influenced by emotions, social bonding, beliefs, mortality, expectations and other human needs (Ashford, 2004, p. 2). Along with the socio-economic factors, the institutional structural factors help to provide a solid framework within an economy by

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shaping an individual’s or organization's behaviour. According to Geoffrey M. Hodgson, institutions are recognised as the stuff of social life that matters significantly in the societal realm (Hodgson, 2006, p. 2). The institution works to structure social interaction by establishing social rules and norms (Hodgson, 2006, p. 18). Institutions can be formal or informal, including governance, healthcare, education, financial institutions, etc. Understanding these structural aspects of an economy is unavoidable, as they play a significant role in shaping inflation trends in a country, especially in developing countries.

Common Structural Factors Driving Inflation in Developing Countries

The structural theorist claimed that structural challenges play a complex role in studying inflation, especially in developing countries. According to some scholars, structural rigour along with anomalies and bottlenecks has an immediate effect on the supply-chain efficiency, production cost, and use of economic resources, shaping the inflation trend of countries (Ahmad, Kuldasheva, Ismailova, Balbaa, Akramova, & Ul Ain, 2024, pg 2). However, in most developing countries, external factors accompanied by supply-side bottlenecks, including production and distribution constraints, play a crucial role in price instability in the economy. The rising prices of traditional culprits of an economy- oil and food, along with rising gas prices and global distributional limitations, pushed the national economy of developing countries into high inflation trends throughout the decades.

Historically, the supply chain bottlenecks influence the intermediate products in the global commodity market by providing upward pressure in import and production prices (Bańbura, Bobeica, & Martínez Hernández, Year, p. 7). Inadequacy in global shipping capacity or shipping equipment shortage, along with rising prices of commodities, can lead to inflationary pressures in local markets in developing countries when a significant portion of the economy depends on imported energy and products. Though Keynes mainly focused on demand-side factors as the causes of inflation, modern Keynesians also support the idea that supply constraints primarily drive cost-push inflation. During the era of the COVID pandemic, modern Keynesian Joseph Stiglitz claimed that the post-COVID inflation was mainly driven by supply-side constraints (Stiglitz and Regmi, 2022). However, neo-classical

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economists used to argue that external shocks or supply-side constraints, etc, are typically temporary phenomena; they don't have any long-term impact on inflation.

Besides supply-side shocks, labour market rigidity harms inflation trends in developing countries. New Keynesian economists developed the idea of nominal price rigidity in the labour market, causing inflation. According to the New Keynesians, nominal wages are generally sticky and cannot be adjusted immediately, which slows down the adjustment of wages during an economic shock (Dixon, 2009, p.17). So, the firm cannot immediately increase wages if there is a high demand for labour during an economic boom. As a result, the production cost increases due to the mismatch between labour demand and wages to fill the gap, and the production costs increase the product price to maintain the firm's profit (Dixon, 2009, p.18). Again, the worker asks for higher wages due to high product prices, which continues the circle of inflation due to this wage-price spiral in the market. On the other hand, the neoclassicism theories believe in the market clearance approach, where markets are always flexible for price adjustment to ensure equilibrium in the market (Friedman, 1968, pp.11–12).

However, the characteristics of the labour market in developing countries are quite different from those in developed countries, as the former consists of an ample supply of unskilled workers with high informality and minimum wages (Caballero, Chui, Kohlscheen, & Upper, 2023, p. 4). In addition, the demographic features of developing countries, like a fast-growing population with high dependency on agricultural sectors, influence high supplies of low-skilled workers with very low wages, limiting the purchasing power of workers and affecting the inflation trends in the developing world. Furthermore, fiscal deficits [3]and high public debts in developing countries were significantly blamed for the high inflation rate and slow economic growth of countries throughout the 19th century (Easterly & Schmidt-Hebbel, 1993, p. 211).

A narrow and inequitable tax base, causing high fiscal deficit or debt pressures driven by high levels of informality, weak tax institutions, and political resistance, can force the government to print and increase the money supply in the market, causing high inflation in developing

[3] A fiscal deficit happens when a government spends more money than it earns through taxes and other revenue sources. This gap is often filled by borrowing or printing more money

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countries. In "Monetarist Arithmetic", Sargent and Wallace claimed that fiscal deficits and inflation have an affirmative relationship if monetized, though the relation is conditional (Easterly and Schmidt-Hebbel, 1993, p.212). However, it seems blurry as governments tend to fill the gap either by borrowing or printing more money. Besides, in his book "*The Deficit Myth* (2020)" Stephanie Kelton, a modern monetary theorist, argued that the size of the fiscal deficit in a country doesn't pose a threat of inflationary pressure; rather, the economy's capability of absorbing the excess money spending matters more (Kelton, 2020, p.64). So, it doesn't matter whether the deficit is too small or too large; only the capacity of production matters in inflation.

In contrast, the structural theorist views fiscal deficits as one of the key drivers of high inflation in developing countries, as these are not a short-term policy failure rather show a narrow tax system and long-term institutional weaknesses. Especially in the post-coronavirus pandemic, the budgetary deficit became a fundamental reason for high inflation in the developing world due to the lack of the government's capacity to take necessary steps to reduce public debts and control the high inflation rates caused by failures in fiscal policies. Likewise, a working paper published by the International Monetary Fund in 2005 claimed that the inflation trend of an economy is highly influenced by the differences between its features fiscal and monetary policies and one of the key structural feature leads to this problem is determined by substantially its government's abilities of tax collection (Aisen & Veiga, 2005, p. 3). According to the Optimal Taxation Theory, the government optimally balances the inflation tax and output taxes, supported by the structuralist view that determines the causes of inflation in developing countries (Aisen & Veiga, 2005, p. 5).

Some political scholars also claim that a good government preferably a democratic one with an independent central bank can keep the inflation rate low in a country as they are bound to maintain transparency in the check and balance mechanism and proper implementation of rules of law can ensure the autonomy of the central bank (Ho, Nguyen, & Nguyen, 2021, p. 379). Structuralists emphasise that the role of political instability and poor government structure leads to supply bottlenecks[4], tax avoidance, and production failure, which are recognized as deep institutional fragility leading to a high inflation rate.

[4] These are points in the supply chain where goods get delayed or stuck, like port congestion or factory shutdowns. They reduce supply and push prices up.

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Keynes also talked about the active role of the state during a crisis in implementing active monetary policies and managing aggregate demand to avoid events like the Great Depression. However, neo-classical economists believe political instability can't lead to high inflation unless it causes monetary mismanagement (Sargent and Wallace, 1981, p.2). Besides, the neo-classical economists supported the idea of an independent central bank. A country's central bank supervises the exchange rate. It controls the interest rate by increasing it to stabilise the price, so it should operate without any political influences to maintain transparency and price stability in the market (Wachtel and Blejer, 2020).

Furthermore, according to a working report by the IMF, demographic changes will be a key factor in the future economic landscape (Yoon, Kim & Lee, 2014, p. 4). Demographic changes significantly impact the labour market decisions, saving and investment behaviour, and aggregate supply and demand of a country. IMF claims that population ageing can reduce the aggregate demand in an economy as consumption behaviour changes at the same time, which helps to keep the price low., still, at the same time, it affects the supply of effective labour in the market, creating inflation pressure in the economy (Yoon, Kim & Lee, 2014, p. 19). Keynesians and Post Keynesian economists also discussed the relationship between demography and inflation.

According to Keynes, the population growth increased the aggregate demand for new capital (Palley, 1996, p.469). When aggregate supply overemphasises aggregate demand, product prices go upward, causing economic inflation. Though monetarist or classical economists found no direct connection between population growth and inflation. On the other hand, high population growth creates pressures on natural resources and unskilled labour, along with challenges to the transparency of institutional frameworks, which can cause inflation in the economy. For example, in countries like Japan and Korea, demographic changes have a tremendous impact on economic growth, fiscal positions, inflation, asset prices, and investments (Yoon, Kim & Lee, 2014, p. 21). So the high population growth may contribute to high inflation when the economic capacity of a country outpaces the production capacity, infrastructure, and food security.

Lastly, exchange rate volatility negatively affects price stability, especially in developing countries. In import-oriented economies, exchange rate stability is crucial in shaping inflation

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dynamics (Uçar, 2024, p. 144)—the structuralist and new structuralist theorists were greatly concerned about currency depreciation [5]due to structural trade deficits or import dependency, as a driver of inflation in developing countries. However, short-term currency depreciation can cause inflation if combined with structural weaknesses like commodity dependence. The raw materials for the production system become expensive due to currency depreciation (Mulwa, 2013, p.14). The cost of imported goods and production costs rise when the currency depreciates, increasing the price in the domestic market, creating market uncertainty and inflationary pressure in sectors like rents or wages. Besides, according to the monetarist, the only reason why the exchange rate volatility should be monitored is that the major countries' monetary policy changes frequently without any predictions can cause trouble for the other countries as asset holders to predict the future price and change their policies accordingly (Humphrey, 1977, p.3). However, developing countries impact the supply chain; they often depend on advanced economies for capital and certain consumer goods. As a result, exchange rate fluctuation directly influences cost and price levels, leading to price instability and inflation pressures for those countries (Uçar, 2024, p. 146).

However, inflation is a multifaceted issue that could be driven by plenty of structural factors. According to the structuralist school of Inflation, the bottlenecks and inelasticity on the supply side can be the root of inflation in most developing countries (Madito, 2021, p. 73-78). Besides, conflicts among trade unions and higher wage demands through strikes by the employees can pressure the firms, and the government can lead to high inflation (Madito, 2021, p. 73-78). Again, Allianz SE, a German-based Global Financial Service Company, discovered five structural factors that drive inflation over a more extended period, including demographics, deglobalization, decarbonization, digitalization, and debt (Allianz Research, 2023, p. 6). Some of these factors are closely related to the inflation dynamics in South Asia. So understanding these structural factors is indispensable for analysing the causes of inflation vulnerability in South Asian countries.

[5] Currency depreciation means a country's money loses value compared to others, like the US dollar. This makes imported goods more expensive, often leading to higher prices at home

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History of Inflation Vulnerability in South Asia

South Asia is a region of divergent economies. India, Pakistan, and Bangladesh, the three largest economies of this region, have seen growth and poverty reduction for the past few years. In contrast, India is gradually increasing its presence in the world economy as the largest democratic country in the world, with around 1.32 billion people (International Monetary Fund, 2023). Countries like Sri Lanka, Nepal, and Bhutan have had mixed economic performances. According to the latest South Asia Development Update 2025, the growth of this region will be the fastest of the others in the upcoming two years, and the growth will be expected to be 6.1% in 2025 (World Bank, 2024).

The economy of this region is driven mainly by India, as a large amount of labour is in technology industries, and it has a great presence in the agriculture and industrial sectors. Countries like Bangladesh and Sri Lanka are the largest exporters of textiles and ready-made garments in the European Union and the USA. However, most of these countries are net importers of commodities and energy resources to dispatch the finished goods to the world market. Besides, the Maldives and Bhutan’s economies are driven by a strong tourism sector. The Maldives is a country of 1200 coral islands, and the other is a country with the immense natural beauty of the Himalayan Mountains. Moreover, remittance plays a significant role in every country's economic growth in this region.

Despite these promising growth projections, a few domestic and external aspects have increased the risk of fragile economic conditions held by persistent structural changes in this region. The World Bank Vice President for South Asia, Martin Raiser, claimed that the economic growth of South Asia remains promising in the short run, but the fragile fiscal policies, along with natural calamities, seem like a dark cloud over the region in the long run (World Bank, 2024). Some global factors, like poor financial conditions coupled with recent trade disputes, prove a drawback for the South Asian economy as well (Nabi et al., 2010, p. 16).

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Moreover, the countries of South Asia struggle to maintain price stability because of their rapidly growing population and divergent economic sectors. During 2000, the economic condition of most South Asian countries remained stable while the inflation rate varied across the countries. According to the Global Economic Prospects provided by the World Bank, the region's inflation rate was nearly 9.3% throughout the decade, slowing down economic growth (Acharya & Miah, 2021, p. 1). In preceding periods, the enduring inflation rate in India was 7.5%, but a significant moderation was noticed amid 2000, when the inflation rate rose from 5.2% to 5.5% from the first half to the last half of 2000(Mohanty, 2011, p. 1442).

On the other hand, Bangladesh experienced heavy infrastructural and agricultural damage due to the major flood in 1998, consequently, the country faced a sudden increase in consumer price inflation rate from 2.6% in 1996 to 7% in 1997 (U.S. Department of State, 1999, pg-1). Moreover, Sri Lanka underwent multiple upward modifications in consumer prices in 2000 due to direct or indirect influences of specific state policies, often called "administered prices". The diesel and kerosene prices increased by 86% and 77%, respectively, causing an annual price increase of 6.2%, according to a report of the “Colombo Consumers' Price Index” (Central Bank of Sri Lanka, 2000, p. 3). Compared to Sri Lanka, other South Asian countries, such as Pakistan, Nepal, and Bhutan, had a stable and declining inflation trend following the year and beyond.

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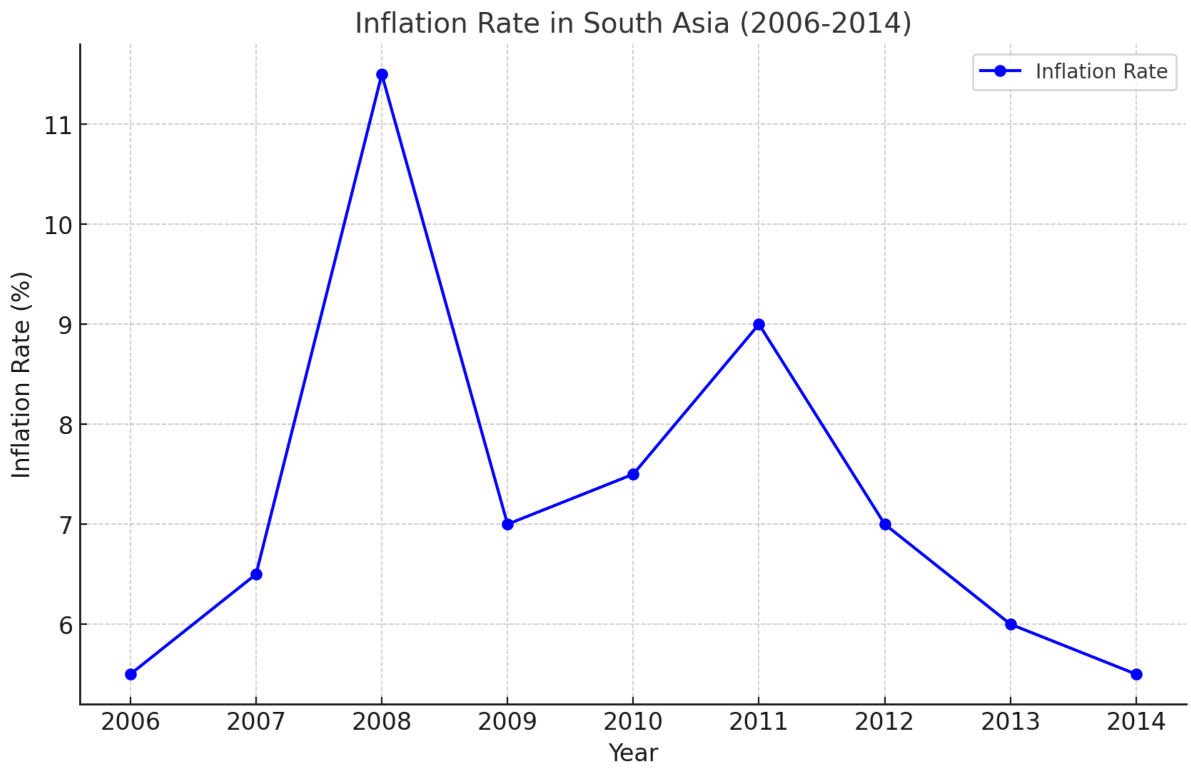

Source: Data from World Bank Group

However, the global financial crisis struck the South Asia region when it was already going through the "Twin Shock" due to rising fuel and food prices since 2004 (Shabbir, 2011, p. 35). According to the World Bank, the overall inflation in South Asia increased from 7.2% in 2007 to 11.5% in 2009 and then decreased to 10.3% in 2011 (World Bank, 2023). The price of fuel in the world market has endured an upward trend since 2004 and peaked in 2008 at 300%, while the food price ascended in 2006 and peaked at 175% in 2008 (Shabbir, 2011, p. 35). These twin shocks hit the South Asian economy from a different level than other regions of the world due to its extreme dependency on fuel and food imports as a result, this region lost a huge percentage in its annual GDP growth between 2003 to 2008. According to data from the World Bank, India and Pakistan, the two supreme economies of South Asia imported 66.67% and 80% of their crude oil respectively over the year 2006-2008 due to growing demand and limited oil production along with the increasing price in global markets (Shabbir, 2011, p. 37). The food price inflation also rose to an elevated stage as in between 2007-08, the price of rice and wheat, two staple foods of the region increased by 74% and 130% correspondingly imposing substantial pressure on the poor households who usually

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spend one-third of their income on food items in an extended family structure (Shabbir, 2011, p. 38).

A report by the Asia-Pacific Development Journal claimed that countries are more vulnerable to issues like supply-side shocks during a financial crisis, which mostly depend on agriculture, net oil importers, and dealing with infrastructural inefficiencies (Goyal, 2010, pg-12). The economic crisis of 2008 hit the South Asian economy with rising inflation and volatility rate (Goyal, 2010, pg-12). Besides, factors like high currency depreciation, reduced foreign investment due to the global crisis, and rising fiscal deficits in national economies also contributed to high commodity and energy prices during that time.

According to a report by the Asian Development Bank, India and Sri Lanka were mostly affected by the global crisis in 2008 as the net capital outflow along with financial accounts were lowest in these countries which were $1.1 billion and $0.3 billion in Sri Lanka and $4.3 billion and $5.3 billion in India (Carrasco, Hayashi, & Mukhopadhyay, 2010, p. 4). In Sri Lanka, the increased price of food grains in the world market was pushed toward the consumers, causing double-digit inflation throughout the years of the financial crisis, but in India. However, the food prices inflation was lower but relentless as local support systems prevented the sellers from decreasing the price in domestic markets, though prices fell in international markets. Despite this, in 2009, some countries like Bangladesh and Sri Lanka started to recover as they prevented high currency depreciation; still, Nepal, India, and Pakistan held a high inflation rate of 8-10% till 2013 (Goyal, 2010, pg-31). Furthermore, the South Asian countries went through some structural changes in the post-crisis period, including a sharp decrease in agricultural share while noticing a gradual increase in manufacturing industries in the South Asian economy which helped to carry out a moderate inflation rate in most of the countries from 2014 till 2020 the outbreak of corona worldwide.

Literature Review

According to Fischer & Modigliani, inflation has both positive and negative impacts on an economy, depending on different structures of public and private institutions by adapting to the ongoing inflation and fully anticipating the upcoming (Sepehri and Moshiri, 2004, p. 191). Where low and moderate inflation increases the flexibility in the consumer market and

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expedites the labour market, high inflation can negatively affect the resource allocation, increase uncertainty, and may force firms or households to cut off their productive resources. There is always a controversial relation between inflation and economic growth, for rich countries those have high development and economic growth, the effect of inflation in optimization in price flexibility is higher than the poor countries those are dependent on the export of few primary products and agricultural items with more fragile trade unions than the rich countries (Sepehri and Moshiri, 2004, p. 193).

Many emerging and developing countries went through moderate inflation during the 1970s-80s, and some economies faced hyperinflation during the late 1980s to early 1990s (Asfuroğlu, 2021, p. 485). Cardoso and Helegwe in the monetarist-structuralist debate claimed that there are three main determinants of inflation in developing countries include: cost-push elements, money creation and fiscal imbalances, where first two determinants were recognized by the monetarist and cost-push factor played role in structuralist view during 1950 to 1960 (Edwards, 1993, p. 2). According to structuralists, inflation in developing countries is driven by structural imbalances in the production system and distribution process, along with agricultural constraints and inefficiencies in the agricultural sectors (Owuor and Ghabon, 2024, p. 7). Craven claimed that inflation isn't always an interplay between supply and demand; rather, it's influenced by structuralist characteristics (Owuor and Ghabon, 2024, p. 8).

Structuralists found two different types of elements in inflation: one is autonomous, and the other is propagation; autonomous signifies the shocks that infringe the system and initiate inflation, and propagation deals with how the system responds to the shocks (Argy, 1970, p. 80). Besides, Sek examined how oil prices affect the local consumer price in Malaysia and found that high fluctuations in oil prices in local and global markets have a long-term impact on price inflation and influence consumer, producer, and import prices (Owuor and Ghabon, 2024, p. 9). Scholars use a variety of methods to identify the structural factors that cause inflation in developing countries. For example, Mukhtar, Jehan, and Bilquees attempted research in Pakistan to identify a relation between trade openness and inflation in a developing economy, where they confirmed a positive and substantial relationship of price inflation with trade openness (Mukhtar, Jehan, and Bilquees, 2019, p. 47-68). Chhabra and Alam also investigated a positive nexus between trade openness and inflation by conducting

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research on the Indian economy as a structural challenge (Chhabra and Alam, 2020, pp. 79-90).

Besides, Menon claimed that an increase in the exchange rate has a direct impact on domestic prices, especially in countries that are heavily dependent on imports of finished or intermediate goods and energy supply (Menon, 1996, pp. 105-115). McCarthy scrutinised the impact of oil price on consumer price index and producer price index for six commercialised organisations for OECD countries, where it was found that exchange rate volatility has limited influences on consumer prices but a greater impact on imported prices (McCarthy, 2007, pp. 511-537). Tugral and Bari examined the asymmetrical relation between inflation and the exchange rate in Turkey and later reported that the exchange rate and inflation hold a non-linear relationship by moving together in the long run (Tuğral and Bari, 2021, p. 114).

Furthermore, in the 2008 global financial crisis, several researchers found that external and internal debt have a direct link with the economic decisions of a country. A large portion of external debt in developing countries that are facing balance of payment imbalances is financed by the IMF to achieve sustainable global growth and impose macroeconomic policies and three-year programs on structural reforms (SAP). Khan, Nawaz, and Hussain claimed that these structural reform programs in Pakistan caused inflation (Khan, Nawaz and Hussain, 2011, pp. 1450-2275). Again, Karakaplan examined the relation between inflation with external debt in 121 countries and reported that debt has less inflationary impact in well-developed economies and financial markets and vice versa (Karakaplan, 2009, pp. 203-217).

However, Mallik and Chowdhury examined the impact of inflation in four South Asian countries including Bangladesh, Sri Lanka, Pakistan, India and ended with two points; first the inflation rate and inflation sensitivity highly influence the economic growth changes the economic growth more than the economic growth changes the inflation rate (Patra and Sahu, 2012, p. 11). According to some scholars, the financial environment of South Asian countries is vulnerable to inflation; excessive import reliance for food and energy has a direct impact on the inflation rate of South Asia along with population trends, labour market conditions, and the unemployment rate (Ahmad et al., 2024, p. 11).

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Chapter 2: Theories of Inflation

Quantity Theory of Money

The root of the quantity theory of money was derived from classical economics, proposed by David Hume in the early 18th century. However, the monetarist school became popular and vigorously promoted the theory in the 20th century. Milton Friedman, the dominant representative of the Quantity theory of money, believed that when the growth of the money supply outweighs the growth of output, then inflation takes place in an economy (Su et al., 2014, p. 1). It shows a long-term relationship between prices and money and claims that inflation is mainly driven by money growth in the long run. In macroeconomics, a country's money and inflation variables always have a direct link with each other. The commodity price level, consumers' real income, and the interest rate of a country represent the effects of money supply in an economy (Su et al., 2014, p. 2). It also affects the price levels of domestic products and people's income trends. The relation between money supply and inflation is essential to consider as it influences the effectiveness of monetary policy decisions in preventing future high inflation in a country.

According to the quantity theory, money is vital in deciding inflation trends. David Hume constituted the relationship between money supply and price level changes (Aslan and Korap, 2007, p. 94). Fisher constructs a mathematical model, $M V = P Y$, to show the relationship between the money supply and inflation (Aslan and Korap, 2007, p. 95). Here, M stands for money supply, V for velocity of income, P for general price level, and Y is the aggregate output, which overall expresses the idea that, in a given period, the economic transaction volume is proportional to the agreed-upon output growth of an economy. According to Bittaye (2021), the QTM is driven by the following hypothesis:

- ➔ The quantity of money supply fundamentally drives inflation in an economy.
- ➔ Money supply is an exogenous process.
- ➔ Different variables, such as interest rates, nominal income, and so on, function to regulate the demand for money.
- ➔ In the long term, the formality of injecting money is not essential in an economy.

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- ➔ Different non-monetary factors like capital productivity or time rate determine the interest rates.

The quantity theory of money has been challenged by Keynesian economics as it applies to the long run because the price is always sticky in the short run, so it's not possible to hold a direct relation between money supply and price hikes (Bittaye, 2021, p. 50). John Maynard Keynes developed the income-expenditure study, which is an alternative approach that emphasized the correlation between investment and nominal income, the transformative nature of money velocity, the role of aggregate demand and interest rates in the study of inflation, and the asymmetrical relation between money supply and economic growth. Keynes didn't entirely reject the relation between money supply and inflation instead he claimed that the amount of money does not have a direct or stable link to prices since velocity and production were not constant but rather extremely changeable, in contrast to what was believed at the time (Bittaye, 2021, p. 51). Keynes argued that the idea of the quantity theory of money was too simplistic to understand the changing nature of money velocity and production quantity in an economy, as money can be held for a more extended period during a crisis moment causing low velocity or the production might be low or high based on the market need.

Post-Keynesian theorists argue that money supply is an endogenous factor determined by the credit creation by the commercial banks, not directly controlled by the central banks (Nayan et al., 2013, p.49). So, the money supply in an economy adjusts based on the credit demand, which can grow based on the needs of a specific economy, so this is not a direct cause of inflation. Instead, the money supply in an economy increases the aggregate demand, especially in the investment-driven sectors, which pushes businesses to fuel their economic activity. When demand outpaces the supply, it can lead to higher prices. The central bank can indirectly control the money supply in an economy based on the needs and interest rates (Nayan et al., 2013, p.49). Besides, throughout the last four decades, central banks of different countries, like the European Central Bank or US Fed officials, rejected the idea of considering money supply to measure inflation, as the instability of money velocity makes it an unrealistic metric to measure inflation. During the global financial crisis, the inflation rate seemed to be low, though many unconventional policies on monetary factors were granted (Castañeda and Cendejas, 2023, p. 3).

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Demand-Pull Theory of Inflation

Demand-pull inflation theory is a prominent theory defining the causes of inflation in a market economy. According to the demand-pull theory, consumer aggregate demand for different goods and services causes inflation in an economy when the aggregate demand outweighs the aggregate supply. The contradiction between supply and demand, where consumer demands increase pressure on supply output capacity, increases the prices in the market disproportionately, causing inflation (Jain, Sharma, and Kumar, 2022, p. 2981). However, the root of demand-pull theory was mainly derived from the idea of prominent economist John Maynard Keynes. Still, later the theory was expanded by Keynesian economists such as Richard Musgrave and Alvin Hansen (Totonchi, 2011, p. 459).

They identified aggregate demand as the source of inflation at the full employment level, as the consumption, government spending, and investments comprise the aggregate demand (Totonchi, 2011, p. 459). The increased aggregate demand could be driven by a few factors, such as low interest rates, a booming economy, or growing consumer confidence. Keynes established a model to express the demand-pull theory, where he found that a sudden rise in aggregate demand, along with price rigidity, can push the price level upward when the economy is at its full capacity, as they are unable to increase production to meet the increased aggregate demand. The rapid inflationary trends depend on the larger gap between the aggregate demand and supply. Keynesians also argued that aggregate demand is boosted when the money supply increases in the economy, as it lowers the interest rates.

According to the demand-pull theory, when consumers have more money, they are willing to spend high amounts to buy limited stock products, which leads to inflation, especially during periods of economic growth. The most common causes of demand-pull inflation include:

Gap in Real Output: A country's Inflation rate is highly influenced by the gap between its actual and potential output, known as the real output gap. When an economy crosses its potential output, the demand for goods and services outpaces the supply, leading to a high inflation rate.

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High Government Expenditure: Extensive government spending can result in high inflation, as it stimulates demand, pushing up commodity and service prices. Total government spending has a direct impact on the high inflation rate.

Increased imports: Imports and inflation are directly linked. When a country expands its import capacity, it increases its dependency on foreign commodities, which raises the prices and costs of imports, causing inflation (Okon, Eke, and Morgan, 2023, p.36).

However, demand-pull theorists claim that when unemployment declines, inflation rises in an economy, and the unemployment rate is driven to its minimum, creating an inflationary gap due to an increase in wages and prices.

Despite being widely accepted, the demand-pull theory has been criticised for its oversimplified view on the rise or fall of price due to aggregate demand. Fritz Machlup, a economist of Austrian School criticize the demand driven explanation and claim that in a traditional market economy, the price of commodities rises naturally in a perfect market as it is the mechanism to enhance prices to maintain stability due to rising aggregate demand; the producer does not decide to enhance the value of products and services (Machlup, 1960, p.127). In a modern economy, prices aren't lifted by any invisible hand but rather by proper formal managerial decisions, which he recognised as "rules of Thumb" (Machlup, 1960, p.127).

As a rule of thumb, the prices are determined by administrative decisions, giving less consideration to aggregate demand and more to production or supply bottlenecks. The demand-pull theory fails to explain the high prices of products due to rising demand when the rule of thumb is observed by the producers, sellers, or trade unions globally, taking into consideration the rising cost of labour and production, so that the excess demand will not be enough to increase the prices. That's how the cost push theory of inflation challenges the idea that increased aggregate demand causes high inflation. It claims that even a low or stable demand can lead to high inflation due to the rise in production costs, for example, the 1970 oil price crisis was mainly fueled by the high production costs due to geopolitical tensions, despite having a stable demand (McNeill, 2018, pp. 93–106).

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Cost-Push Theory of Inflation

Cost-push theory offers a fundamental contribution to the new economic paradigm. This theory was initially proposed to show the relationship between wage growth and price, and how wage growth affects the price range of products and services, leading to inflation. Cost-push inflation is usually driven by wage and profit increases by trade unions and employers, respectively (Totonchi, 2011, p.460). Cost-push inflation occurs when the total cost in a production system increases due to disruptions in the supply of goods and services. When the costs of production increase, the owners of the firms try to impose extra costs on consumers by increasing the price of food and services. In a Keynesian economy, cost-push inflation is a structural manifestation that deals with supply-side market power. The origin of cost-push inflation can be found in both Keynes's General Theory and Robinson's Post Keynesian Theories (Cristiano, 2023, p.225). Though Keynes was primarily focused on the demand-side factors, the development of cost-push theory is mainly driven by the Post-Keynesian economists.

One of the fundamental causes of cost-push inflation is the rapid increase in money wages over labour productivity (Totonchi, 2011, p.460). These types of inflation are often driven by high raw material costs, rising wages of labour, etc. For example, due to the boost in oil prices in the market, production costs rise, which are transferred to consumers by increasing fuel prices, causing inflation in other sectors like food and textiles due to high transportation or production costs. During a cost-push inflation, the aggregate demand remains constant, but the cost of production increases, which forces businesses to raise their price to hold the profit margin. Some other causes of cost-push inflation may include:

Supply constraints: The performance of the agricultural and manufacturing industries has a direct impact on inflation. Obstacles in the farming sectors and supply-side constraints can lead to high commodity prices and inflation.

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Exchange rate volatility: Inflation can be caused by frequent changes in nominal exchange rates. A high depreciation in the rate of domestic currency compared to foreign currency can increase the price of different imported goods and services.

High unemployment rate: Inflation is impacted by the employment rate of an economy. A rising unemployment rate can reduce demand by decreasing the purchasing power of the buyers and can lead to high inflation (Okon, Eke and Morgan, 2023, p.37).

Natural Disaster: Natural disasters like floods, droughts, or earthquakes can cause unexpected damage to the production system and disrupt the production chain. The disruptions can lead to a higher production cost, which may force the business to raise its prices.

New Government Policies or Changes in Previous Policies: Changes in government policies or the application of a new policy can raise a business's cost by requiring it to compensate. These changes drive companies to increase their prices to keep up with production costs, which may lead to inflation.

However, some macroeconomic thinkers identified cost-push inflation as less credible. The traditional cost-push theory was also rejected by post-Keynesian economists like Sidney Weintraub. They highlighted the importance of aggregate demand and the elasticity of the money supply in inflation (Egle, 1961, p.218-231). When the aggregate demand decreases, the prices will automatically fall until the overall price returns to its previous level. The New Keynsian American Economists Robert J. Gordon, in his study of inflation in the US and other countries, found no direct link between inflation and the wage-push theory claims that the cost-push theory can be a hypothesis to explain the wage rates, still, it can not be recognized as a theory of inflation or money growth as higher wages do not always lead to higher price (Batten, 1981, p. 25). Again, Ludwig von Mises criticizes the idea of cost push saying that an increase in production cost isn’t enough to lead to high inflation unless accompanied by an increase in money supply (Mises, 1949, pp. 419–420).

Conflict theory of inflation

In 1974, the British Communist Party published a magazine named ‘ Marxism Today’ where they claimed that, at that time, inflation was usually caused by distributional conflicts

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between the workers and the capitalists (Mitchell, Wray, and Watts, 2019, pp. 260-261). According to Pat Davine, due to structural predisposition and enhanced bargaining power by the workers, inflation broke out during the mid-1970s, and later it slowed down economic development (Mitchell, Wray, and Watts, 2019, pp. 260-261). Despite having a vulnerable market share and pricing method, large oligopolistic enterprises engaged in non-price competition using their price-setting power. Generally, the conflict theory of inflation is linked with class conflict, such as the wage-price spiral, but it is also applicable to other situations as well. An example can be drawn from the tug-of-war among the nations that consume and produce oil. If the producing countries raise their price once and the consuming countries react by adding more price to that, then the producing country may increase its price a second time.

R.E. Rowthorn developed his conflict theory of Inflation from the Idea of Karl Marx's class struggle between workers and capitalists (Cachanosky and Ocampo, 2024, p. 9). According to Rowthorn, Conflict is a capitalist phenomenon that concerns every aspect of economic life (Rowthorn, 1977, p. 215). Conflict can influence the price level by impacting the money and distribution of income, and monetary factors have no direct influence on inflation. Rowthorn drew a chain model to show the relationship between inflation and conflict: money -demand -conflict -prices (Rowthorn, 1977, p. 215). Money plays a vital role and influences economic activity, but this is not the only independent variable. Money and demand have a direct complex link where a change in the money supply changes the demand and expenditure. Demand has a direct influence on both conflict and prices, especially on the bargaining power of the working-class people. The monetary policy controls the demand and expenditure and influences the wages and prices in a market economy.

Post Keynesians have highlighted the gaps in the conflict theory, claiming that conflict theory can be an explanation but cannot be the only cause of inflation (Palley, 2024, p.40). There could be multiple causes of inflation, including rising demand, structural and supply-side factors, the role of financial and monetary factors, etc. The workers must have the right to demand a wage increase, and historically, there are trade unions that fill the bridge between workers and owners by bringing them to the negotiating table, giving them guidelines, and offering them authority to impose a unionisation threat for management to consider strongly. In the past thirty years, the absence of strong labour organisations and the flexibility in the

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market have weakened the explanation of conflict theory as the cause of inflation (Palley, 2024, p.41).

Nicolas Cachanosky, an Austrian School Economist, also views conflict theory as a societal threat. According to Cachanosky, conflict is a natural phenomenon of every society, so the existence of conflict in a society doesn't push the price high as people are fighting for scarce resources naturally (Cachanosky, 2024). He reminds us of the situation in Latin America, under Marxist beliefs of class conflict, where the political parties used conflict to create economic instability. Cachanosky finds that conflict theory exacerbates economic instability in a country rather than helping alleviate it. He is also concerned about the idea of government control in the economy and private property suggested by the conflict theory, which can undermine the growth of a country.

Structural Theory of Inflation

Structural inflation arrived in economic discussions and policies almost 40 years ago to show the effects of different structural factors in inflation (Totonchi, 2011, p.460). These structural factors help realise how different economic diseases like inflation destroy economic stability and the root causes of this destruction. This theory is based on the equation that the price-output and the production cost are equal, and the total cost of production can be separated into immediate inputs, total wages, and gross profits (Kim, 2023, p. 4). Due to the globalisation of the process of production, wage-led inflation is taking place despite having strong economic growth in many countries. The structuralist theory emphasises variable markup as there is a possibility of differences in real profit and desired profit due to supply shocks, and it also emphasises the role of real income in determining inflation, which is slightly ignored by post-Keynesians or mainstream economists (Kim, 2023, p. 4). As gross profit share and wage share have a negative relation, there is always a conflicting view between the workers and the producers on distributing the income properly, which can lead to inflation based on social conflict.

Import price plays a significant role in structural inflation. Early structuralist thinkers defined external shock as the key driver of inflation and the conflict over distribution as the mechanism of propagation (Noyola Vázquez, 1956, p. 603-648). Global factors like oil shocks or commodities' super cycles impinge on inflation development. Exchange rate

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volatility, primarily the domestic currency depreciation, fuels these external shocks. The countries mostly suffering from conflicting claims are more vulnerable to permanent inflationary pressure due to temporary currency exchange shocks.

Many advanced economies are going through deflationary pressure due to the globalisation of the production system and the increase of external dependency since the collapse of the Bretton Woods system (Kim, 2023, p. 5). Structuralist thought mainly applies to developing countries' economies, where structural constraints are more vulnerable due to market imperfections, imperfect economic knowledge, disequilibrium, and rigidities of the supply and demand side of the economy. Two major constraints in developing countries are agricultural and exchange rate of foreign currencies bottlenecks, where agricultural constraints mostly occur due to institutional defects, and foreign exchange rate constraints due to slow development in export sectors and high import dependency (Taslim, 1982, p. 26).

However, the structural theory of inflation has been criticised by monetarist supporters, claiming that the structuralists sharply ignore the role of money while discussing the causes of inflation. During the structuralist-monetarist debate that took place in Latin America in 1960, economist Campos claimed that all structuralists become monetarists in the short run while in the long run, the monetarists turn into structuralists (Boianovsky, 2012, p. 41). Celso Furtado designed a three-year plan to tackle Brazil's inflation, where he suggested managing fiscal deficits, which is called a monetarist approach by Campos because the fiscal deficit is a key monetary phenomenon (Boianovsky, 2012, p. 41). Fiscal deficits, often financed by printing money, cause inflation in economies. Besides, some economists believe that structuralism failed to provide a theoretical explanation of non-food prices' downward rigidity. Besides, structuralism fails to explain aggregate demand or inflationary expectations, so many scholars think this model fails as an inflation theory (Wachter, 1979, p. 233).

Chapter 3: Empirical Analysis of Key Structural Drivers of Inflation in South Asian Countries from 2020 to 2024

This chapter discusses the key structural drivers from both local and global levels that drive the high inflation rate and volatility in South Asian countries in the 2020s, especially after the

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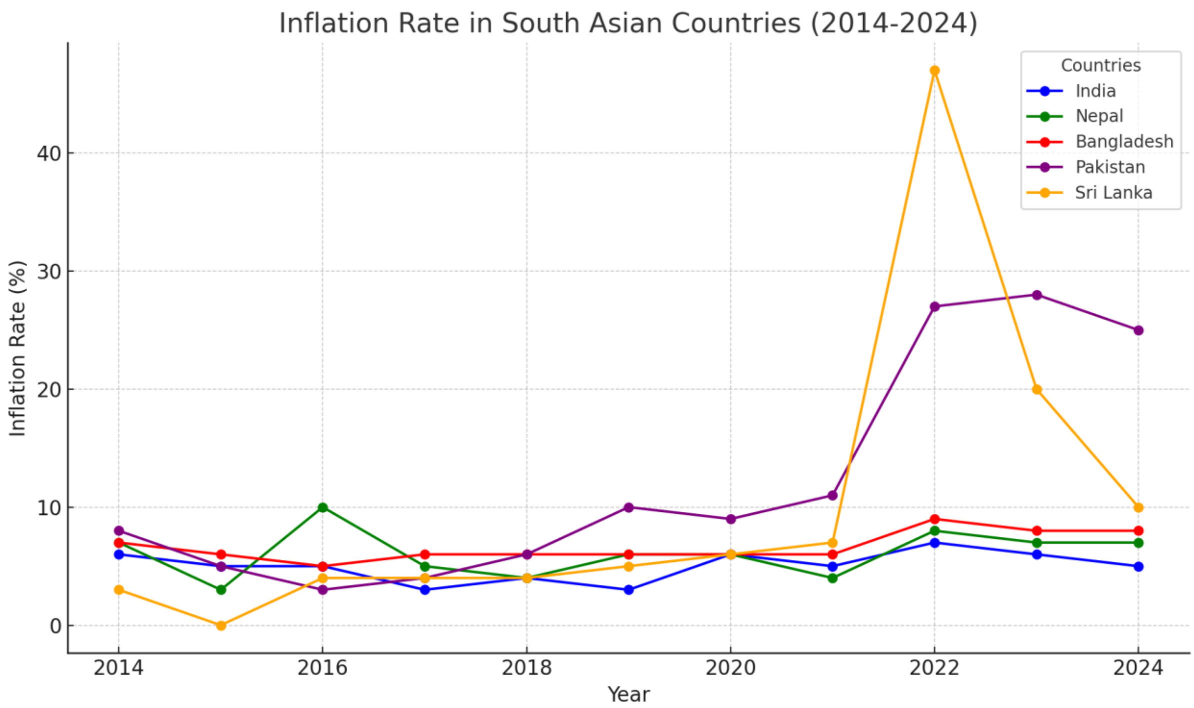
COVID-19 pandemic. A focus will be given on three case studies- Bangladesh, Sri Lanka, and Pakistan- to show how South Asian countries faced inflationary pressure during the 2020s, not only as an aftermath of the global shock but also due to a dynamic interconnection between the local structural vulnerabilities and universal instabilities.

Inflation Trends in South Asia in the 2020s

In 2020, an economic report from the World Bank claimed that South Asia was going through its worst-ever recession (Narayanan et al., 2023). India, the largest economy in the region, exceeded its monthly inflation in food prices by over 10% (Dovonou & Xie, 2023, p. 2). On March 23, 2020, India went under a national lockdown due to the rapid spread of coronavirus nationwide causing a vast economic downturn, especially in the service industry collapsed by 90% and the unemployment rate rose from 8% in mid-March to 23.4% in April 2020 (Younus, 2021, p. 5). India's large production capacities of agricultural products and government subsidies to economic sectors made it less vulnerable to inflationary shock than the other countries of the region, such as Bangladesh, Pakistan, or Sri Lanka, due to their heavy reliance on global food and energy markets.



Source: Data Source IMF

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In Bangladesh, the first COVID case was reported on 8 March 2020, and the country was put under strict lockdown on March 26, 2020 (Younus, 2021, p. 9). Remittances that play a vast role in Bangladesh's economy decreased to $1.29 expected to decline 25% at the end of the year and over a million workers from the garment industry, the largest export sector of the country laid off as the orders declined by 80% in 2020 (Younus, 2021, p. 9). Food inflation was more vulnerable than non-food inflation throughout the pandemic, and it showed volatility in the inflation rate rose from 5.79% in November 2019 to 6.02% and then again dropped to 5.52% in December 2020 (Ahamed, 2021, p. 26). The government declared $8.6 billion in economic aid, along with other international organisations like the IMF, World Bank, and Asian Development Bank providing $732 million, $1 billion, and $500 million in funding, respectively (Younus, 2021, p. 10).

In addition, Pakistan experienced a rise in commodity prices from 8.5% in April 2020 to 11.1% in April 2021, due to the spread of the coronavirus, the rise of global commodity prices, and supply-side disruptions (Ministry of Finance, 2021, p. 141). The prices of non-perishable food items like poultry, staple foods, and non-alcoholic beverages mainly increased by 16%, whereas the price of wheat, the main food group of Pakistan, increased by 24% in 2021 (Ministry of Finance, 2021, p. 143). Besides, oil prices increased by 51% in the FY20/21 due to the high price in the global market and growing demand in industrial sectors (Younus, 2021, p. 149). On the other hand, in Bhutan, the inflation rate was moderate, with a rise of 8.1% in FY2020/21, an increase of 3% from 2019 (World Bank, 2021, p. 4). On the other hand, the Maldives showed a different scenario, the inflation rate declined by -1.59 % as the country received huge relief from the COVID-19 pandemic. Furthermore, in Sri Lanka, both the food and non-food group inflation increased from 9.8% in June 2021 to 11% in July 2021 and from 2.9% in June to 3.2% in July 2021, correspondingly due to the continuous lockdown (Department of Census and Statistics, 2021, p. 3).

However, the post-pandemic years from 2022 to 2024 are more hazardous for some South Asian countries due to structural challenges. For example, the inflation rate in Sri Lanka reached a peak of 69.8% in September 2022, which decreased to 16.5% in 2023 and 3.0% in 2024 due to some structural shocks like extreme currency depreciation, external debt crisis,

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and institutional weakness etc (World Bank, 2025). Both in Sri Lanka and Pakistan, during the year 2022, food inflation peaked at 84% and 36%, respectively, while the inflation in the energy and transportation sectors was over 100% and 60%, respectively (Dovonou & Xie, 2023, p. 2).

Besides, in Bangladesh, the inflation rate rose from 7.48% in 2022 to 9.74% in 2023 to 11.66% in 2024 (Bangladesh Bank, 2024, pg.1). Furthermore, another large economy, Pakistan, also experienced high inflation volatility. According to the State Bank of Pakistan, in October 2022, the national inflation rate was 26.6%, increasing to 36.42% in April 2023 (Bokhari, Ali, and Hussain, 2022, p. 6). These volatile inflation rates show South Asia's vulnerability to an unstable economic landscape. The latter part of this paper will focus on the root causes of inflation trends in South Asian countries by giving attention to the roles of different structural factors in this developing region.

Global Structural Drivers of Inflation (External shocks)

During 2021-22, the global inflation increased dramatically by nearly 6.4% more than the inflation rate at the end of the global financial crisis in 2010, which was almost 4.3% (Jałtuszyk, 2022, p. 10). The COVID-19 pandemic affected more than 200 countries of the world by hitting nearly 90 trillion economies globally, downgrading the global economic growth from -4.5% to -6.0% due to the worldwide lockdown policy (Fatima, Maqbool and Maqbool, 2022, p. 611). The advanced economies faced more economic downturns as their GDP growth rate decreased from 1.7% in 2019 to -4.2% in 2020, compared with the emerging economies, whose GDP growth declined from 3.6% in 2019 to -1.7% in 2020 (Vieira and da Silva, 2024, p. 2). Even the inflation rate in the United States reached 8% at the end of 2022, which is the highest point since the 1980s (Brooks, Orszag and Murdock III, 2024).

Though the economies in the global North started to see recovery since 2020, the global South economies failed to recover as most of the countries are solely dependent on trade, so in 2020, they faced a negative growth of around -0.9% (Fatima, Maqbool and Maqbool, 2022, p. 612). The South Asian countries have also been going through the vulnerability of COVID-19 along with the war in Ukraine that has shaken the economy, causing disruptions, and the commodity price inflation rose to its peak level (already discussed in the

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background). Here are some major global structural obstacles that have fueled the high inflation rate during the 2020s in South Asian countries:

Global Commodity Price Shock

Global commodity prices change frequently in tandem, especially during an economic downturn. The COVID-19 pandemic during 2020-22 led the world economy into a recessionary period, which later became a global shock. Compared with the previous recessions and economic turmoil, this time, the rebound of commodity prices was faster for all types of commodities. Energy prices during 2020 declined faster than any other time, especially oil prices recorded the highest one-month decline in April 2020 as the oil demand plummeted by nearly 8% due to travel bans and recession, later on it was rebounded nearly 50% within three months and surpassed its pre-crisis price within a year (Kabundi, Vasishtha and Zahid, 2022, p. 199). Besides, the prices of natural gas and coal rose to high records due to demand and supply disruptions in 2021, whereas the price of agricultural products declined in 2020 but sharply increased in 2021 and was driven by the higher demand from China, especially for animal feed and the high price of energy (Kabundi, Vasishtha and Zahid, 2022, p. 199). The intensified fluctuations in commodity prices shocked the global commodity market.

Even though the price shock had occurred as a short-term phenomenon, it proved to be a long-term structural challenge for developing economies like South Asia, as these countries lack production capacities and are heavily dependent on imported energy and food. All South Asian countries are deficient in liquid fuel and import crude oil. For example, India, the fastest-growing economy of South Asia, became the world's 3rd largest oil importer in 2017/18 after China and the USA, which imported 220 million tons of crude and refined oil (Alam et al., 2018, p. 28). Besides, Pakistan imports 70% of its energy, like crude oil and petroleum products (Alam et al., 2018, p. 29).

Only India, Bangladesh, Sri Lanka, and Pakistan have their own oil refinery, so the other countries are forced to import refined oil from global or regional markets. Besides, South Asian countries are also net importers of staple foods, agricultural products, and raw materials for textiles. In 2022-23, Bangladesh imported 4.93 million metric tons of food

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grains from the global market (FPMU, 2024, p.1). The rise of food prices globally due to the production and supply bottlenecks during lockdown increased the cost of rice, wheat, and other primary foods in the local South Asian Market. The global commodity price shock affected the import sector of South Asian countries and caused high inflation rates for a long time, even when the other regions started to recover.

Global Supply Chain Disruptions

Supply chain disruptions globally have a historical relation with domestic price rises, as the price changes brought by international trade also affect the trading nations globally.
The world faced a massive disruption in the global supply chain in the aftermath of COVID-19, along with the devastating effects of the Russia-Ukraine war. According to a Global Supply Chain Pressure Index report, the supply chain disruptions started in April 2020 and peaked in their maximum level by December 2021 (Diaz, Cunado, and Perez de Gracia, 2024, p. 1). The war between Russia and Ukraine has shaken the commodity price as Russia is one of the biggest energy exporters, while Ukraine is a major exporter of agricultural products. The massive disruption in maritime disruptions disconcerted the world trade as 80% of trade internationally is conducted by sea (Diaz, Cunado and Perez de Gracia, 2024, p. 2). The global supply chain disruptions due to COVID and the war in Ukraine undermined the local economy in developing economies, notably the South Asian economy, especially the industrial sectors of South Asia, which have been brutally damaged, which has led to inflation, food insecurity, and fiscal imbalances.

The pandemic particularly affected our countries' textile and apparel industries, as giant countries like the USA or the European Union were severely affected, and they closed the import of textiles and apparel. South Asian countries, the top exporters of textiles and ready-made apparel, closed their apparel industries due to fewer orders of ready-made garments from Western countries. Besides, the producers in these countries had to bear production delays and higher production costs. Those factories wouldn’t be able to recover from the loss for a long time, even till now, as the buyers were unwilling to pay for the orders. Agriculture and fish industries in South Asian countries, notably in Sri Lanka, were also severely affected and saw negative growth (Karunathilake, 2020, p. 569).

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The South Asian region heavily depends on imported fertilisers. For example, in 2023, India imported 70.42 Lakh of Urea fertiliser worth 2.6080 billion USD (Ministry of Chemicals and Fertilisers, 2024). The price of these fertilisers increased due to the global supply chain disruptions, making it unaffordable to the farmers and causing a decrease in agricultural production and high food inflation in the local market. Furthermore, the situation also affected the tourism sectors and the remittance flow, especially in Nepal and Sri Lanka, which are heavily dependent on revenue streams (Yousuf and Shafiur, 2024, p. 890). The pandemic, followed by the war, also affected the trade and investment sectors in South Asia due to uncertainty, which led to a decline in investors' sentiment and hindered the economic growth of the region. South Asian countries are highly dependent on foreign investment. As they couldn't meet their production demand, it caused a rise in commodity prices for a prolonged period in the local market and the weakening of local currencies.

Global Financial instability and currency devaluations

Foreign currencies are used in international exchange markets to trade different products and transactions. Hence, any unexpected changes in cash flow affect the entire economic system. A change in the currency exchange value can impede the cash flows in the global market. Some economists say, "A devalued currency might trigger a Speculative assault in the reformed equilibrium exchange rate because other nations' trade competitiveness is diminished" (Gunay, 2021, p. 2). The 2020s, during and after the era of the Global Pandemic and War, brought a global economic shock that surpassed the 1999 Asian and 2008 global financial crises. The situation created a massive change in the demand and supply of currencies for trade and investment around the globe.

Later, the countries faced a high fluctuation in the exchange rate of their currencies against the US dollar. According to Devpura, the exchange rate volatility has a close relation with the global oil prices; he examined the data from the Euro-US dollar exchange rate since January 1 to November 30, 2020, and found out that the cost of oil has a direct impact on the foreign exchange rate (Olaifa, Oyetayo, and Olubiyi, 2023, p. 104). The crude oil price crashed during the time of the pandemic due to the lowest demand, which was one of the causes that affected the foreign currency exchange rate globally. High exchange rate volatility led by

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trade disruptions, low investments, remittances drop, etc, increased the demand for foreign currencies, and the currency lost its value.

Currency devaluations have both short and long-term impacts on developing economies. When research was carried out by Beakal Tafesse over Ethiopian economy through media mediation analysation analysis during 2019, they found that a exchange rate devaluation can cause lower export-import, lower real GDP and higher inflation rate in an economy (Tafesse, 2019, p. 35). The South Asian countries went through the same consequences of currency devaluations in the 2020s, as these countries need to use foreign currencies like the US dollar or the Euro for their trades and transactions. For example, during the year 2020-21, the Indian currency devalued significantly in terms of the US dollar, which resulted in a decrease of foreign reserves in India from USD 577554 billion to USD 540724 billion between 2021-22 (Shravan, 2022, p. 3657).

The rapid fluctuation in local currency against the US dollar influenced the inflation rate and the export and import of the Indian economy. The inflation rate rose from 4.8% in 2020 to 6.2% in 2021 (Government of India, 2022, p. 188). In Sri Lanka, the scenario was worse than in India. Before 2020, for the past 21 years, exchange rate exhibited annual fluctuation ranges used to be 3% to 5% yearly, that climbed up to 15% in 2020-21 which increased the cost of imported goods to 188.18 points and decreased the foreign reserves, as a result Sri Lanka's inflation rate rose to 45.3% in May 2022 (Khandre, 2022, p.142). Other South Asian countries, such as Bangladesh, Pakistan, Nepal, etc., experienced high inflation due to high currency devaluations and exchange rate volatility in the 2020s.

Local Structural Drivers of Inflation

The global pandemic and the war between Russia and Ukraine since 2020 have shaken the world economy, and South Asia is no exception to this global economic crisis. Since the end of 2021, when the world economy started rejuvenating, the region has remained vulnerable to inflationary shocks due to its homegrown structural vulnerabilities. Some countries like Bangladesh, Sri Lanka, or Pakistan continuously face inflationary pressures and high inflation volatility rates due to their weak domestic fundamentals, which are also affecting the

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other countries in this region and worldwide. Here are some local structural aspects that are forcing the high inflation rate in South Asian countries throughout the 2020s:

Rapid Population Growth

Country	Population (Thousands)
Afghanistan	41454.76
Bangladesh	171466.99
Bhutan	786.38
India	1438069.6
Maldives	525.99
Nepal	29694.61
Pakistan	247504.49
Sri Lanka	22037.0
South Asia (Total)	1951539.83

Population of South Asian Countries (2023) — Source: World Bank

South Asia is a region of 1.5 billion people, representing nearly a quarter of the world's population and remaining one of the most populous regions in the world (Australian Centre for International Agricultural Research, 2021). The rapid population growth in South Asia decelerates the economic growth of the region by increasing the poverty rate, creating a high supply of low-skilled workers, and overburdening the educational system. Besides, the high population growth also negatively impacted the region's food supply by creating high demands for staple foods and deteriorating food security. According to a report from the World Bank, since 2000, the working-age population has been declining in South Asia, the ratio was 59% in 2023 whereas it is more than 70% in other developing regions and declared South Asia is the only region where the ratio decreased in last two years (Chung, 2024).

The weak employment conditions challenge the socioeconomic environment in South Asian countries by restraining the growth of businesses and firms in recent years (Chung, 2024). Besides, the rapid population growth forced the countries to take financial assistance from external resources to meet the growing needs of their people, which has burdened the countries with heavy debt, causing an extreme debt crisis and high inflation trends as governments increased the interest rate to balance the fiscal deficit policies. An example can

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be taken from the Debt Crisis in Sri Lanka in 2022. Furthermore, high population density increases the pressure on infrastructure supply like transportation, housing, electricity, and health, in South Asian countries during the 2020s, causing reduced productivity and increased operational costs for firms.

During the coronavirus pandemic, South Asian countries were fighting to feed the 1.5 billion people as food and fuel were more expensive due to supply chain disruptions in the global market. The large demographic pressure also affected the urban infrastructure as more people were migrating from rural to urban areas in search of work, and many people lost their jobs, so the unemployment rates in different South Asian countries were at their peak. The inflation in the housing markets also rose in the major cities.

Institutional Fragility, Corruption, and Political Instability

Weak institutional structure and a high level of corruption are two main causes of underdevelopment in South Asia. The administrative nature of South Asian countries is mostly derived from the pre-colonial culture of a fusion of politics with administration, lack of elected governance, dominance of the state over the economy, trade, and production, and subordination of states and private capital (Jabeen, 2007, p.10). According to the Worldwide Governance Indicators (WGI) 2015, provided by the World Bank, which usually measures the institutional quality and good governance of states all over the world based on six indicators, such as political stability, rule of law, voice or accountability, effectiveness of government, regulatory control, and corruption control; South Asian countries except Bhutan got a negative score which usually proved the poor government structures, high corruption and weak institutions of those countries (Javed, Padda and Akram, 2018, p.115).

The public sector's corruption and institutional weakness fuel inflation in South Asian countries by undermining economic stability, reducing public trust, and hindering policy implementation. In post-COVID times, when the economic crisis and hyperinflation took place in Sri Lanka, corruption in the public sector played a crucial role. Some weak government policies, like investment in infrastructure with foreign debts, misuse of public funds, and some scam activities by governance officials, pushed the country into high inflation. For example, the sugar tax scam in Sri Lanka that cost a loss of 15.9 billion in taxes

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in 2020, though the price of sugar did not decrease, created a revenue gap forcing the government to print money to fulfilll the gap caused an upward trend of inflation (Committee on Public Finance, 2023). The economies of India, Bangladesh, and Pakistan have also been facing structural challenges due to high corruption among government officials and weak institutional frameworks.

Besides, Political instability has been considered a destructive issue that hinders a country's economic performance. International Country Risk Guide claimed that political instability or violence within an economy can be led by internal conflicts (Murshed et al., 2023, p.2). Again, it is argued that the anti-government demonstrations held in unstable political situations can hamper the economic activities of a country, often leading to high commodity prices, a drop in investment, a decline in national savings, and so on. Compared to other developing regions, South Asia has a long history of political uncertainty and frequent cabinet changes, causing policy uncertainties and economic unrest throughout the region. The economy of a country is deeply linked to political stability because unstable political institutions hamper investment opportunities and economic growth. According to Barro, the number of violent occurrences by the political parties and military coups affects the level of economic growth of a country (Anwar et al., 2024, p. 12).

Political instability also leads to frequent changes in economic policy, volatility, and macroeconomic performance. Alesina et al. examined 113 countries from 1950 to 1982 to clarify the relation between weak governing systems and low GDP growth, where it showed that countries that faced low GDP growth had a history of government collapse (Aisen and Veiga, 2011, p. 3). The high level of political instability and government weakness leads to a high inflation rate, disrupting long-term economic policies and shortening the government's prospects. The South Asian region can be identified as a critical one where most of the countries have had a history of political instability and weak governance. Six among the eight countries of South Asia, except Maldives and Bhutan, have been facing unstable political situations and conflicts for a long time (Rathnayake, 2022, p. 186).

Political instability and a weak governing structure disrupted the development process of South Asian countries, which has been identified as a structural problem.
Throughout the 2020s, the South Asian countries went through different political turmoils became one of the prominent structural factors for the high inflation rate in those countries.

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While India became successful as one of the largest democracies in the world, its neighbours, Pakistan and Bangladesh, failed to establish themselves as democratic countries. India, which is now under the Bharatiya Janta Party, is facing constant challenges in terms of regional conflicts, religious and social unrest, and economic reforms. Besides, its neighbouring country, Pakistan, faced an economic crisis due to political unrest between ruling parties in 2022, where its GDP fell from over 1600 US dollars to 1500 US dollars from June to September 2022 (George, 2023). Mahmood Azidand Siddiqui analyzed the relationships between political instability and economic growth in Pakistan and found out that the continuous change in governing system in Pakistan affected the GDP growth of the country and the autocratic regimes performed better than the democraties in terms of economic growth as the former one were more stable than the later (Anwar et al., 2024, p. 13). The inflation rate rose to 30%, the highest in 47 years, due to supply constraints, corruption, and weak fiscal policies, followed by natural calamities like floods (case study 1).

The same year, in 2022, Sri Lanka, another South Asian country, had faced the negative impact of high political instability in the economic growth as the country was structed into a debt crisis due to the policy fluctuations as the economic decisions had not been taken with sufficient deliberation causing insistences in policies within the government functions (Rathnayake, 2022, p. 188). Sri Lanka went through the worst crisis in 73 years, facing an unexpected level of inflation, high currency devaluation, and sociopolitical unrest. Scholars claimed that political uncertainty and weak institutional structures mainly drove the economic crisis in Sri Lanka in 2022 (case study 2). Two years after the Sri Lankan crisis in 2024, Bangladesh also went through a massive, unstable political environment due to anti-government demonstrations by the general public to throw out the fascist regime after 17 years. All these incidents show the persistent struggles of South Asian countries due to a weak governance structure affecting the economic activities by disrupting policy making and investments, triggering capital outflows resulting in currency depreciation, high import costs, and driving high inflation in the region.

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Agricultural constraints

In developing countries, agriculture and food security are crucial in economic development and sustainability. South Asia is an agriculturally driven region where half of its population is solely dependent on agriculture for their livelihood, especially in rural areas where employment is high in the agricultural and farming sectors (Australian Centre for International Agricultural Research, 2021). Though the region contains only 5% of global farming land, the farmers of South Asia have been providing food for almost 20% of the population of world. Despite heavy dependency on agriculture, the growth in the agricultural sector is slow, with low-income levels, which affects the productivity and poverty rate in South Asian countries. The slow growth is driven by some natural causes like climate change, soil degradation, or floods, along with poor infrastructure and transportation, lack of modern technologies and education, and trade restrictions or high tariffs.

The slow growth in agricultural sectors is causing the high price of staple foods like rice and wheat in South Asia, that have a large impact on poverty as it has a direct connection with food security. According to a report published by the Asian Development Bank, a 10% increase in food prices in South Asia can drive 64.5 million more people below the poverty line (Dev, 2013, p. 10). The high food price also affects the small farmers who sell their surplus during harvest season at a low price and later buy food and commodities at a high price, so the situation becomes worse for these small farmers as well. Besides, high food prices also decrease economic activities like business, investment, and savings in developing countries like Sri Lanka or Pakistan, as people spend a large share of their income on food.

The climate challenges and the pandemic worsened the agricultural situation in South Asia and hampered food and nutritional security. Since 2020, South Asian countries have been facing dual challenges: one is due to natural calamities, and the other is due to supply chain disruptions and uncertainty in production as a result of the pandemic and war as global agriculture is interconnected. South Asian countries are more vulnerable to these challenges due to their large population, weak infrastructure, lack of pure water and sanitation, and limited social protection. For example, in 2022, the damage caused by floods in Pakistan was

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nearly US$14.9 billion; it lost GDP of US$15.2 billion, and compensation needed for rehabilitation is around US$16.3 billion (Ministry of Finance, Government of Pakistan, 2023, p.281).

Besides, the pandemic broke out in a harvest season, so farmers were unable to take their crops to the market, causing a chaotic environment in the agricultural sector in South Asia, which became more harmful due to the ban on cross-border trade in the region. For example, the food prices in Afganistan increased by 30% when Pakistan cancelled all cross-border trades with Afganistan in March 2020, though it resumed in June 2020, but the country has to pay an additional amount of US$15,000 to navigate in Karachi port, which has created a huge loss in Afgan economy and high commodity price in local markets (Rasul, 2021, p.5). The impact of agricultural constraints on South Asian inflation trends during the 2020s is substantially greater than in many other developing economies due to poor mechanisation, high intensity of agrarian labour, and limited farm equipment and facilities.

A large share of informal Economies

The informal economy[6] refers to the economic activities that are not governed by any law and are not included in Gross National Product (GNP). Unstructured economic and institutional activities drive the informal sectors without any stable working hours or protections and are not subject to any tax systems. The informal sector may include temporary or part-time work, outsourcing, childcare, working in the tourism sector, etc. The emergence and impact of large informal economic sectors in developing countries is a mostly debated issue for policymakers, as the production of primary commodities in agriculture and animal husbandry is mostly included in the informal sectors (Mughal and Schneider, 2020, p.8). According to an estimate published by the Asian Development Bank, more than 90% of MSES (Micro and Small Enterprises) are included in the informal economic sector; even in South Asia, it is 80%-90% (Timilsina, Rahut and Embuldeniya, 2024).

Substantial Trade Openness

[6] The informal economy includes jobs and businesses that aren't registered with the government—like street vendors or home-based work. These often lack job security and legal protections.

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The trade openness generally demonstrates the unification of different economies in this globalised era. The global trading system offers diversification of products at the lowest prices by allowing each country to produce those products in which they are efficient. In South Asia, most of the countries are highly dependent on international trade and have a low self-sufficiency level. According to the report of World Integrated Trade Solutions by the World Bank, in 2023, the total imports of South Asian countries were 837,568,067.64 thousand US$ and exports were 498,504,299.56 thousand US$, resulting in a negative balance in trade of -339,063,768.07 thousand US$ (World Bank, 2025). Within the South Aian region, India is the strongest player in the global supply chain, and it ranked 5th in terms of importing primary goods, components, and different parts in 2023, according to the World Bank.

In 2022-23, another South Asian country, Bangladesh, imported 92453 million US$ and exported 56623 million US$, also showing a negative trade relation, which is the same for other South Asian countries as well (Bangladesh Bureau of Statistics, 2024, p.9). The high import dependency of foods, raw materials, and energy of these South Asian countries has caused inflationary pressure in these countries since 2020. When the global supply chain disruption took place during the COVID-19 pandemic, South Asian countries were unable to import essential commodities from the global market. The import declined by 15.4% in 2020, and shipping costs increased due to border closures, which caused high commodity prices in local markets in South Asian countries. The currency depreciation also affected the trade openness to push the inflation rate high, especially in countries like Pakistan and Sri Lanka, which faced high currency depreciations in 2020-21, as it increased the import costs and intensified inflation pressures, which is usually known as import inflation.

Case Study 1: The Worst Economic Crisis in Sri Lanka (2021-22)

Sri Lanka, a beautiful island in the South Asian region bordering the Indian Ocean, is one of the largest economies based on the tourism sector earnings in the area. Before the COVID-19 pandemic, the economic growth of Sri Lanka had an average rate of 4.8% annually for the past six decades (Athukorala, 2024, p.165). It took six decades for Sri Lanka after independence to become a middle-income country to low-income in 2007, and later on, after

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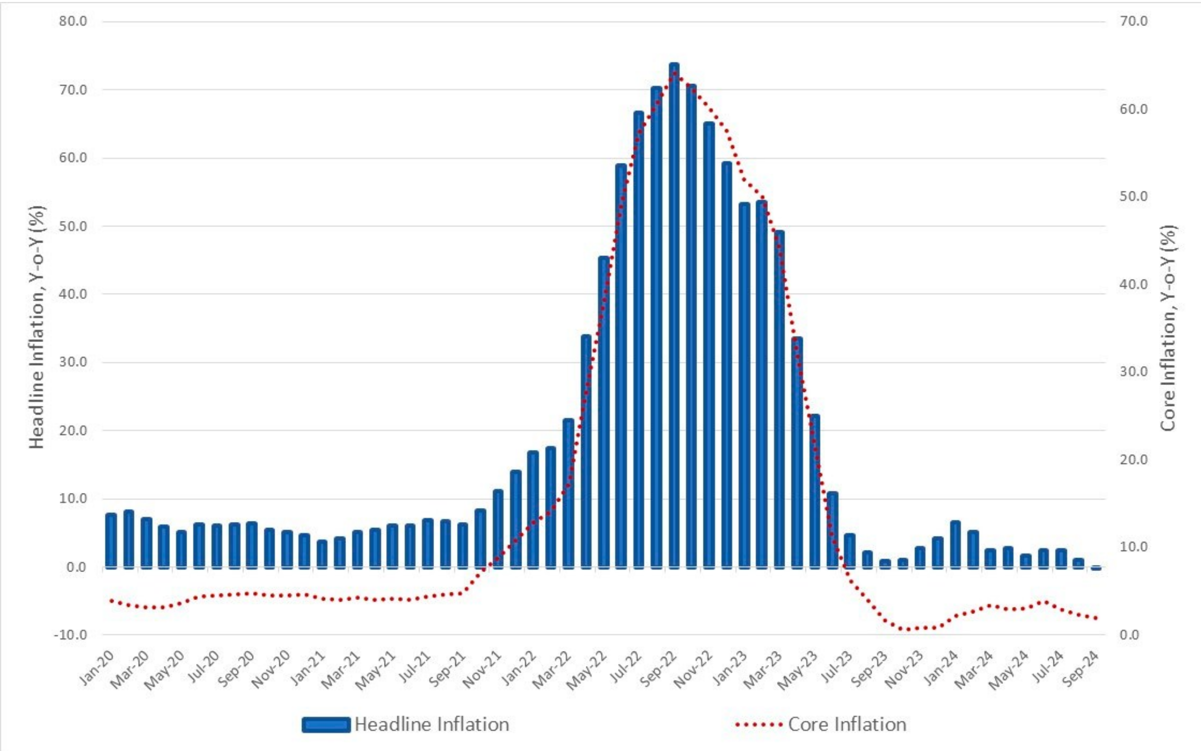
12 years, it became an upper-middle-income country in 2019. The annual average GDP growth in Sri Lanka from 2015 to 2019 was 3.7%, which declined to 0.4% in 2020 due to the pandemic (Athukorala, 2024, p.165). However, Sri Lanka was struggling with its worst-ever economic crisis in mid-2021. The inflation rate rose to its highest level between October 2021 to June 2023 and faced hyperinflation between June 2022 and March 2023 when the inflation rate remained above 50% consistently, even in September 2022 it rose to a peak at 73.6% (Ekanayake and Dissanayake, 2024, p.1).



Source: Data Source from Central Bank of Sri Lanka

The above graph shows that both the core and headline inflation rates have been above 10% since July 2023. According to the Central Bank report, in December 2022, the inflation rate declined to 59.2%. The process of disinflation has continued since 2023 and gradually reached nearly 5% in July 2023.

Now the question is, what were the main drivers of hyperinflation in Sri Lanka during that time? The Central Bank of Sri Lanka claimed that policy errors and some exogenous factors triggered the inflation rate in Sri Lanka. For example, the country became vulnerable to local and external shocks due to its failure to control fiscal and external reserves, along with the shock of the COVID-19 pandemic. At the beginning of 2022, Sri Lanka went through

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economic challenges due to ineffective microeconomic policies, followed by prolonged deficits in budgets and imbalances in external accounts, which affected the country's foreign reserve. The situation created extensive pressure on countries' Balance of payment, which resulted in a weak and volatile exchange rate, declining economic activities, and inflation (Weerasinghe, 2023, p.8).

In addition, Sri Lanka faced a high rise of public debt when the current government, led by Rajapaksa, cut out the essential taxes, leading the country into difficulty in financing the imports of basic items such as food, fuel, and medicine in 2019. Due to the tax shrinking, Sri Lanka was continuously borrowing from local and international banks and financial institutions at high interest rates to finance imports. Later on, the country asked for assistance from the IMF. However, in 2021, the foreign reserves in Sri Lanka fell significantly, and the country expressed its failure to repay the external debts, falling into a debt trap. Again, the government's decision not to devalue the currency led to high currency depreciation and a sharp increase in the inflation rate.

Besides the macroeconomic policy failures, the unstable political environment and lack of institutional transparency fuelled the economic crisis of Sri Lanka. According to some scholars, the financial crisis in Sri Lanka was the long-term consequence dragged by the civil war. The internal conflicts in Sri Lanka, especially with the religious minorities and militarisation in eastern and northern provinces, created a chaotic situation in Sri Lanka during 2010-19, which forced the country to get back into the era of civil war (Santhirasegaram, 2023, p.47).

The centralised government of Sri Lanka increased the military expenses by cutting down the social benefits for the people in the 2022 budget, where the defence ministry of Sri Lanka received its highest allocation than in previous years, which was around 373 billion Sri Lankan Rupees (Santhirasegaram, 2023, p.48). Besides, the government was reportedly accused of corruption and financial intransparency by weakening the institutions. People started to protest against the government in the streets and demanded the resignation of President Rajapaksa in April 2022. The government used forces like the police, military, and blocked social media to stop people.

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On May 9, the president declared a state of emergency, killing five people and injuring several, and the same day, the prime minister resigned. After 2 months in July, President Rajapaksa resigned and later fled the country as protestors occupied the presidential house (Human Rights Watch, 2023). The unstable political environment was one of the primary drivers of the economic crisis and hyperinflation in Sri Lanka, as it disrupted the flow of capital, reduced investments, and led to divestment from the global financial market. Again, governments' failure to implement proper monetary or fiscal policies and continuous protests and blockades disrupted the country's supply chain system, pushing the inflation rate higher.

The new Sri Lankan government implemented some policies to fight the high inflation. The Government of Sri Lanka took some fiscal policies, like decreasing the expenditures of the government, freezing the recruitment process, and not filling the vacancies etc. Besides, monetary policies like reimposing individual taxes that were abolished in 2019 and increasing the corporate taxes, etc, are initiated by the government (World Bank, 2023). The government also implemented structural reforms to regain stability in macroeconomic policies and initiated debt restructuring discussions with the international creditors. Though the Sri Lankan government was successful in reducing the inflation rate in the midst of 2023, but progress was slow due to structural weaknesses, and the stability in macroeconomic structure remained fragile and volatile.

Case Study 2: Economic Crisis in Pakistan 2023

Pakistan went through a tremendous economic crisis in 2023 due to high inflation, the rise of current account and fiscal deficits, a downgrade of economic growth, and debt default. The country was under slow economic growth of about 1.9% in the 2019 fiscal year, which declined by 0.4% in the 2020 fiscal year due to COVID-19 (George, 2023, p.2). Later on, the GDP growth rate in Pakistan declined from 6.2% in 2022 to a contraction of -0.2% in 2023 (Asian Development Bank, 2025). According to the annual report from the Finance Division of the Government of Pakistan, the average CPI inflation recorded in 2023 was 28.2% in the June-July period, which was around 11.00% in 2022 at the same time (Government of Pakistan, 2023, p.117). The inflation rate became highly volatile till 2024, and it decreased to 4.9% in December 2024 (Haider and Bokhari, 2024, p.5).

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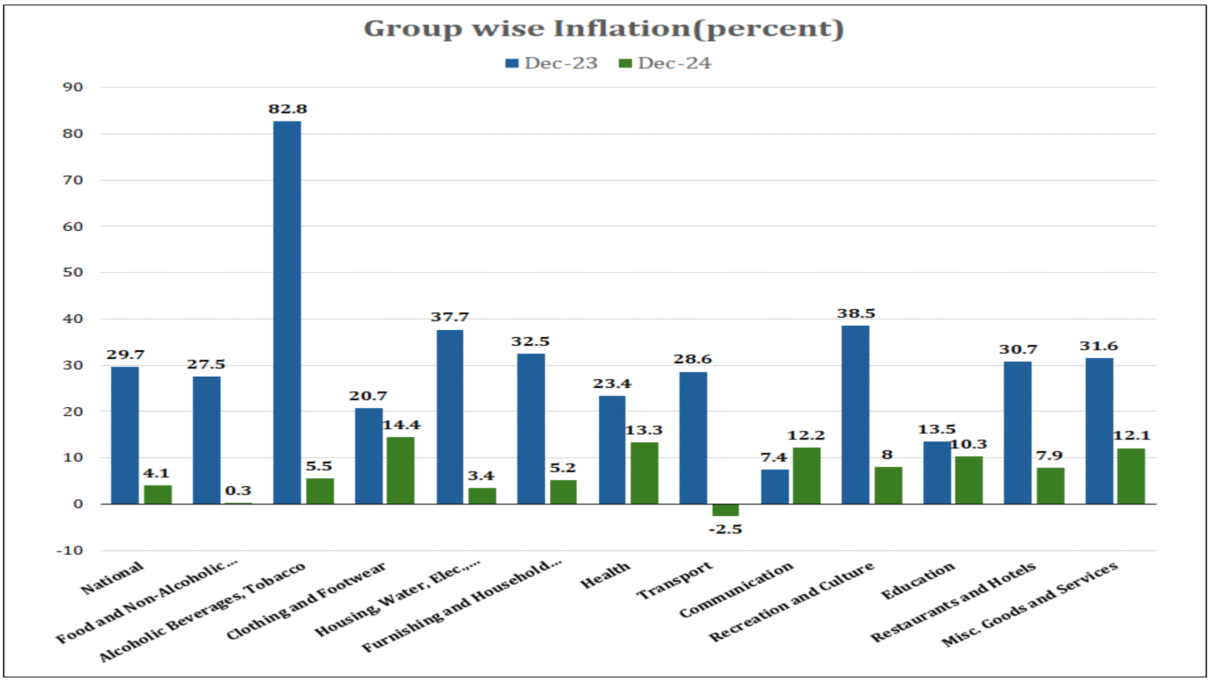

Source: State Bank of Pakistan

According to the graph, the highest rate of inflation in 2023 was in the Tobacco and alcoholic beverages, which was 82.8%, the inflation rate for food items was 27.5%, and for housing was 37.7%. A few structural causes drove the inflation trend higher in Pakistan throughout 2023. One of them was high trade deficits. Pakistan has gone through persistent trade deficits for the last few decades, as some structural bottlenecks prevent the country from becoming an export-oriented country. During the fiscal year 2022, the trade deficit peaked at USD 48 billion 2022, driven by exports totalling just USD 32 billion, causing a decline in the foreign reserves due to the low exports in the same year (George, 2023, p.3). Besides, the quantity of imports for machinery, metals, chemicals, and petroleum increased significantly even in 2022, Pakistan imported 80 billion USD due to increasing consumer demand, high oil prices, and the import of capital goods (George, 2023, p.2). Again, Pakistan is highly dependent on oil imports, around 80%, which amounted to around 17 billion USD in fiscal year 2022, making it highly vulnerable to the oil price shock globally. The high trade deficit and excessive dependency on imports, especially oil imports, affected the high inflation trend in 2022/23 FY, showing clear structural challenges such as limited industrial diversification, underdeveloped domestic production capacity in Pakistan.

Moreover, Pakistan has a long history of weak institutions and political instability, which has undermined the development of the country since its independence. The military government

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continuously ruled the country for more than three decades, and it is recognised as a failed state due to persistent political crisis by many scholars. In April 2022, the removal of Prime Minister Imran Khan and his government from power created a chaotic political situation among his followers. People marched on the road and demanded fair democratic institutions, as there were allegations of foreign interference and judicial bias (Hyder, 2023, p.07). The unstable political environment was also a big part of the economic crisis in Pakistan during 2022-23. Textiles and ready-made garments hold a significant share in Pakistan's export sector, and a large part of the population is aligned with the textile sector for their livelihood. Due to the political turmoil, a massive energy crisis arose, causing a considerable loss in the textile industry, many people lost their jobs, and the annual GDP growth rate fell from 6% to 5% (Ali et al., 2022, p.15). The political instability has worsened the situation since 2020, when Pakistan was already going through the shock of COVID-19, and later, the extreme flood in 2022 worsened the inflation rate in Pakistan.

Furthermore, Pakistan shares one of the largest sectors of informal economies globally, around 30-40%. This large proportion of the untaxed informal sector hinders the tax collection process of the government for the social and economic welfare of the country and affects the monetary and fiscal policies. An estimation shows that only 1% of the total population in Pakistan files tax every year due to the large informal sectors and tax avoidance flexibility driven by corruption and political influence (George, 2023, p.6). The monetary policies to avoid high inflation taken by the government used to be ineffective due to the government's inability to control the money supply and increase the interest rates, as most of the transactions occur in cash. The failure to allocate proper taxes also increased the fiscal deficits and forced the country to borrow from internal and external sources in 2022-23. According to the State Bank of Pakistan, the domestic debt was 38,810 Rs billion in June 2023, and international debt was 24,071 Rs billion, which were 47% and 24.4% of their GDP, respectively (Ministry of Finance Pakistan, 2024, p.150). The high debt from the Central Bank increased the money supply in the economy, and the value of the local currency went down due to external imbalances, pushing the inflation rate to a peak in 2023.

As a policy response, the State Bank of Pakistan increased the interest rates several times in the fiscal year 2022/23. To deal with the fiscal deficits, the government enhances its reliance on commercial banks to finance the deficits. In November 2022, the Monetary Policy Committee (MPC) increased the policy rate by 100 bps to set up a tight monetary policy

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(State Bank of Pakistan, 2023, p.43). Besides, the government increased the general sales tax and imposed taxes on purchasing luxury items and also reduced the subsidies on items like fuel or electricity production. In 2023, IIMF provided a standby arrangement for Pakistan, where the country secured 3 billion USD (State Bank of Pakistan, 2023). The government also tried to enhance the agricultural productivity of the country by implementing various projects and took strong initiative to stop black market exchanges of foreign currencies and smuggling. Though the policies helped the country decrease the inflation rate in Pakistan in the short term, the long-term inflation and macroeconomic stability couldn't be achieved due to structural weaknesses.

Case Study 3: Upward Inflation Trend In Bangladesh

Bangladesh is a small South Asian country with 160 million people living there. The economy of Bangladesh has been facing high inflation trends since 2022, which has slowed down the economic growth of the country, reducing the purchasing power, creating huge unemployment, and hampering the sustainable development of the country. Though inflation was a common problem globally during 2022/23 due to the aftershock of the COVID-19 pandemic and the Russia-Ukraine war, many countries started to recover as soon as possible. The inflation trend in Bangladesh showed a different scenario as the prices in Bangladesh continued to rise. In December 2024, it peaked at 10.8%, a high inflation rate according to the national standard (Liller and Parray, 2025). According to some scholars, the inflation in Bangladesh is driven by cost push or demand-pull factors, external influence, and inflation expectations (Sayed et al., 2025, p.26).

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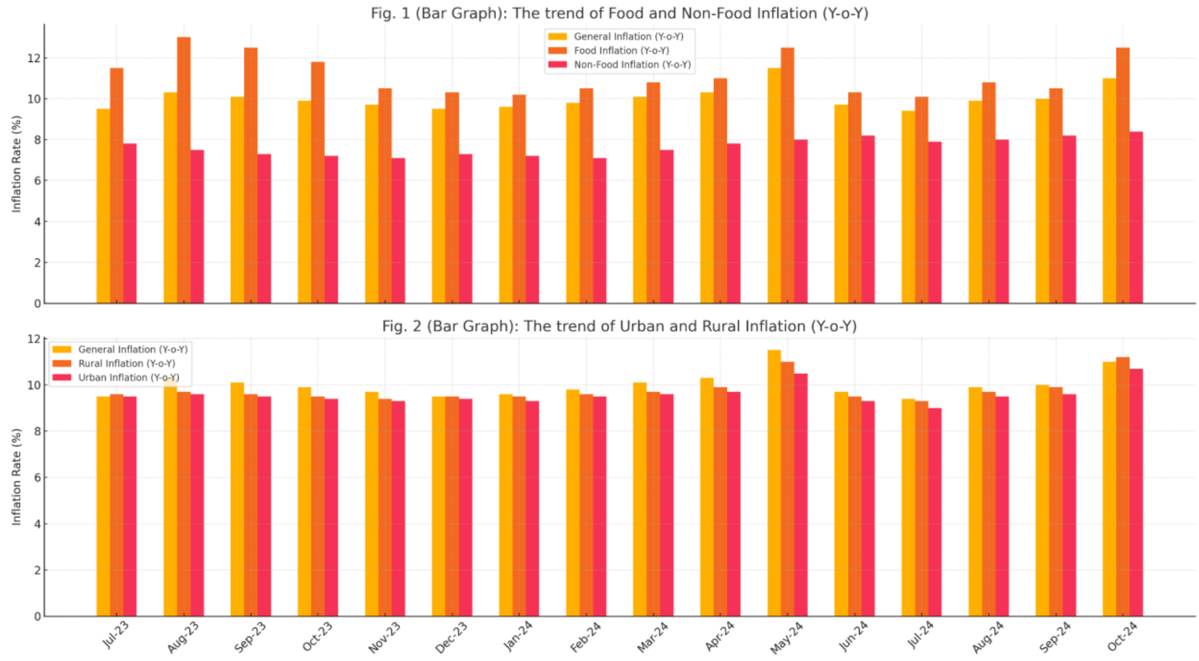

Source: Bangladesh Bureau of Statistics and Bangladesh Bank

Demand-pull inflation in Bangladesh is driven by extreme money supply, high government expenditure, and expansion of the economy, where the cost push is driven by the constraints on the supply side, such as high production cost and global price shock. Bangladesh is mostly affected by food inflation, as it primarily affects people's economic capability of buying food. The food inflation peaked at 14.10 % in July 2024, where rice and vegetables were the primary determinants (Sayed et al., 2025, p.30). Supply-side constraints were crucial at that time due to floods and political instability. The global supply chain disruptions due to the pandemic and war affected the inflation rate in Bangladesh. Bangladesh is a net importer of petroleum, raw materials for readymade garments, food grains, consumer goods and other capital goods. As a result, the global commodity and fuel price shock during 2021-22 increased the commodity price in the local market of Bangladesh.

Again, due to the process of strengthening the value of the US dollar worldwide, the foreign exchange markets came under significant volatility in 2022. The most powerful currencies like the pound, euro, Yen, and indian rupee have gone through a sustained decrease over time. The dollar’s value appreciated against the Euro by 13%, against the pound by 15%, and against the Yen by 20% in 2022 (Kumar et al., 2024, p.409). The value of the Bangladeshi taka also devalued significantly without informing the public about the depreciation, which created a discrepancy between the importers and exporters due to the value offered by the

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bank and the value exporters received. The situation was affected by the energy shortage and the high cost of energy and creating a huge gap in the balance of payment of the country, increasing the interest rates, and high commodity prices in the market.

Besides, like Sri Lanka and Pakistan, Bangladesh was also going through a political turmoil since July 2024, when all kinds of students were protesting on the streets for reforming the quota system in government job sectors, which later turned into an anti-government movement due to the killing of an innocent student by the government forces. The students, along with masses of people, protested by blocking the roads and government institutions for nearly one month. Because of the protest, fascist Prime Minister Sheikh Hasia resigned after 17 years and fled from the country. During the protest, the supply side of production was highly disrupted due to continuous strikes, blockades, and curfews imposed by the government to suppress the protest. The export sector, especially the ready-made garments and textiles, on which the export industry of Bangladesh is excessively reliant, came to a standstill, which badly affected the economy. Though the non-food inflation was lower than the food inflation, it rose to 10% in the first half of the year 2024 due to transportation blockage, rise of global fuel price, and depreciation of local currency (Sayed et al., 2025, p.30).

To reduce the inflation rate, the current interim government of Bangladesh decided to keep policy rate 10% and subdue the money supply by decelerating the growth of private sector credits by 7.3% at the end of 2024 to fight against the demand-pull inflation by controlling the money supply (Bangladesh Bank, 2025, p.3). Besides, the government-initiated measures to enhance regional trade to deal with the supply constraints and make imports low-cost. For example, Bangladesh started direct trade with Pakistan after 50 years by trading 50,000 tonnes of rice in 2025 (Reuters, 2025). The government decided to cut down the fiscal budget in 2025, the previous year, for the first time in its history, and reduce government expenditure to control the upward trend of inflation in Bangladesh. Bangladesh Bank expects the inflation rate to decline by 7-8 per cent in the second half of FY25 (Bangladesh Bank, 2025, p.1).

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Comparison Among the Case Studies

All three South Asian countries, Sri Lanka, Pakistan, and Bangladesh, went through structural challenges and a high inflation rate from 2021 to 2024. Though these countries share common drivers for high inflation during that time, some differences remain. However, all these countries are highly dependent on imports for petroleum, food grains, raw materials, and other commodities, which makes them vulnerable to external shocks like global supply chain disruptions or commodity price shocks during the post-COVID and Russia-Ukraine war era. For example, all these countries are net importers of petroleum oil, and almost 80% of petroleum is imported. As a result, when the oil price shock took place in the global market, the economies of these countries were severely affected, and the inflation rate rose significantly.

Another commonality these countries experienced during the 2020s was that institutional weaknesses led to political instability. All three of these countries underwent political turmoil, mass protests, and government changes, which created production supply constraints in the local markets, causing high inflation trends throughout the period. Besides, ineffective financial institutions, highly corrupt structures, high fiscal deficits, and weak fiscal and monetary policies worsened the situation. Besides, these countries share a large sector of the informal and untaxed economy, which limits the monetary and fiscal policy tools to battle the high inflation rate and government revenue collections. In the post-pandemic era, the informal economic sectors were badly affected due to high demand and a supply shortage, causing excessive pressure in the market and increased commodity prices.

However, Sri Lanka's inflation trends were extreme, peaking at 76.3% in September 2022, while Pakistan's average was 28.2%. On the other hand, Bangladesh's inflation rate during the peak was 10.08% in December 2024, which was a manageable level compared to the two other countries. The main drivers of the highest inflation rates in Sri Lanka were the instabilities in macroeconomic policies, currency depreciation, and supply shortage, whereas in Pakistan, the high inflation rate was mostly driven by natural disasters, external shock, or trade imbalances. In addition, both domestic and external challenges fueled the inflation rate in Bangladesh. Again, where Sri Lanka and Pakistan went through the economic crisis and

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high inflation trend immediately in the post-pandemic era, the high inflation started to hit Bangladesh lately, when most of the countries of the world had already started to recover from COVID-19 shocks.

In the policy response, all of these countries took different monetary and fiscal policies, like to cut down government expenditure, imposing or reimposing taxes, increasing the interest rate, etc. But Sri Lanka was more successful than Pakistan in controlling the inflation rate, as Pakistan faced more challenges due to its structural weaknesses, like an unstable political structure, weak institutions, etc. Bangladesh is still working on its monetary and fiscal policies to reduce the commodity price and bring economic stability by enhancing regional trades, limiting the private sector's credit and so on. When both Sri Lanka and Pakistan were drowned in both internal and external debt, and received external assistance, especially from the IMF, Bangladesh has taken a more proactive stance by seeking loans from the IMF, as Bangladesh isn’t currently as critical as Sri Lanka and Pakistan were.

Chapter 4: Theoretical Fragmentation in the Analysis of Inflation in South Asia

The inflation trends in South Asian countries during the 2020s demonstrate different scenarios due to the structural vulnerabilities embedded in the economy and some factors like an unstable political environment, a large sector of informal economy, high fiscal deficits, import dependency, etc can lead to deeper structural conditions like weak institutional structures, centralized governance, and externally dependent production systems. Due to these structural problems, traditional economic theories of inflation, like the Quantity theory of money, demand-pull or cost push theories, conflict or structural theories of inflation, etc., often failed to fully capture the causes and drivers of inflation in South Asia.

Inflation Beyond Money Supply (QTM)

The “Quantity Theory of Money” is a prominent theory of inflation in classical economics. The QTM claims that the price of goods and services in an economy is proportional to the supply of money, which means that when the money supply increases in an economy, it often

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may lead to inflation as it influences either the price level or make changes in the supply side of products, sometimes even both. Milton Friedman (1968), one of the prominent supporters of QTM, argues that inflation is always a monetary phenomenon. However, the sufficiency of QTM has been challenged in this chapter, as in South Asia, inflation isn`t always a monetary phenomenon (Su et al., 2014, p. 1). That means money supply isn't the single driver of inflation in South Asian countries, as they are equipped with some structural problems, as explained in the previous chapter. For example, in 2021-22, the global supply chain disruptions and commodity price shocks due to coronavirus and later on the geopolitical war between Russia and Ukraine played a vital role in the high inflation rate later in 2022-23 in South Asian countries, as these countries are solely import-oriented. The QTM ignores these external factors, often driving high inflation in developing economies like South Asia.

QTM argues that excessive money growth is the primary cause of inflation in an economy. However, there are periods in South Asia when the inflation rate remained high, even though the money supply was modest or controlled in the economy. For example, during 2022-23, Pakistan faced the highest inflation rate in previous decades despite operating under a tight monetary policy. Causes like Supply shocks or currency depreciation fuelled the high inflation in Pakistan rather than the money growth. Besides, QTM believes the velocity of money is often predictable, which usually fails in developing economies (Palley, 2003). In South Asian countries, the velocity of money changes frequently due to high informal sectors and underdevelopment in the financial sectors. QTM is the role of informal sectors where there are unrecorded transactions, unstable money velocity, and unpredictable relations between money supply and prices. As South Asian countries have a considerable informal sector where economic activities occur outside the banking and financial system, the QTM is insufficient to explain the complex inflation trends in this region.

In 2022-23 in Sri Lanka, the inflation rate peaked at its highest in its history and caused hyperinflation in the Sri Lankan economy. During this economic crisis, monetary mismanagement and external shocks drove the high inflation rate. Several structural weaknesses, such as fiscal deficits, currency depreciation, debts, supply-side bottlenecks, etc., contributed to the abnormal money supply in the Sri Lankan economy. The theory ignores these structural weaknesses in a complex economic situation like Sri Lanka. Also, the stability of money velocity was broken down in Sri Lanka as the consumers and investors lost

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confidence and became unsure about spending and investing in the Sri Lankan economy. The instability of velocity also challenged one of the core assumptions of QTM.

Inflation Not Just Demand Pressure

Demand-pull theory claims that Inflation occurs in an economy when aggregate demand exceeds the aggregate supply of goods and services. Demand-pull inflation is often caused by economic booms, technological advancements, and inflation expectations. This type of inflation breaks out in an economy when it is in a full-employment phase and people's purchasing power increases. However, in 2020 and onwards, when South Asian countries started to face rising inflation pressure, the core reason wasn't the rising aggregate demand but supply destruction that played the leading role. During the pandemic, when the global supply chain faced disruptions due to lockdowns and border closures, the price of commodity products increased sharply in South Asia, as these countries are highly dependent on imported items from the global markets. Besides, one of the core assumptions of demand-pull inflation is full employment (Palley, 2003; Blecker, 2002). However, during the pandemic and afterwards, the unemployment rate was highest in South Asian countries due to the slowdown of trade and business and the shutdown of many small or informal enterprises. This high unemployment rate contradicts the demand-pull inflation's full-employment scenario.

For example, during the economic crisis in Sri Lanka, many people lost their jobs, especially in the government sector. This impacted consumer behaviour as people were stuck on the necessities and cut all other expenses. A study found that 75% of households cut their basic consumption, like food, beverages, personal care, etc., in 2023, which reduced the total consumption from 6% to 2% before and after the crisis (Sooriyaarachchi and Jayawardena, 2023) . So, consumer spending and demand were reduced, but the inflation rate peaked at 69% in 2023 in Sri Lanka. The same happened in India and Bangladesh; both countries faced a high inflation rate despite having limited demand and consumer spending. These countries faced supply bottlenecks and structural vulnerabilities like poor infrastructure, fiscal deficits, political instability, etc., which drove their inflation rate to be high despite having a constant aggregate demand from consumers (Agenor & Montiel, 2015).

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Though many scholars claim that inflation expectations drive high prices in South Asian countries, consumers' and businesses' predictions of future high inflation in the economy cause an inevitable price rise by asking for higher wages or spending more. For example, in 2022-23, during the economic and political crisis of Pakistan, inflation expectations played a crucial role in worsening actual inflation when the currency highly depreciated and the global price shock caused high prices along with the internal political instability, people and businesses in Pakistan expected a higher future inflation. This inflation expectation led to an increase in aggregate demand that pressurised the supply side, which was already broken, causing higher inflation in Pakistan (Siraj,2023). However, though inflation expectations caused a short-term demand-driven price rise, supply pressures quickly overtook it. So the demand-pull theory partially failed to explain the causes of the high inflation scenario in South Asian countries during the 2020s.

More than Cost-push Forces

A cost-push inflation is usually driven by rising production costs, such as high wages or increased costs of raw materials. When increased production costs decrease the aggregate supply in the economy despite constant demand, the prices of products usually increase to cope with the high production costs to maintain the profit margin. Cost-push inflation offers a valid understanding of the causes of inflation during an external shock, but critics argue that it has oversimplified the inflation process by undermining demand-driven factors (Taylor, 2004; Blecker, 2002). However, during the 2020s, the high inflation rates in different South Asian countries have had many cost-push triggers, like supply chain disruptions and global price shocks. However, the real scenario is more complex and multifaceted. Though the supply side bottlenecks and currency depreciations between 2020 to 2023 contributed prominently to the production in the economy, causing inflation, some other factors were equally responsible. For example, in countries like Pakistan or Sri Lanka, some fiscal policies during the economic crisis, such as the high fiscal deficits, debt-fuelled infrastructure, withdrawal of subsidies, etc., caused immediate inflationary pressure in the economy.

Besides fiscal policies, structural vulnerabilities, such as high demographic pressure, weak institutions, corruption, and market inefficiencies, also played a significant role. For example, during the debt crisis in Sri Lanka, corruption and mismanagement in governmental

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institutions made the inflation trend more persistent, leading to hyperinflation due to policy failures. Besides, infrastructural weaknesses, a lack of proper transportation and technologies, such as cold storage or refrigeration, and poor harvest, caused high food inflation in countries like India and Bangladesh. A report shows that India loses around ₹44,000 crore of vegetables and fruits annually due to the 2024 inflation of vegetable prices, which contributed 66% to the food Inflation in India (Dhyeya IAS, 2024).

Moreover, high demographic pressure in South Asian countries also fuelled the inflation trends in South Asia, especially in countries like Bangladesh, Pakistan, and India. For example, during and after COVID-19, more people started to migrate from rural to urban areas, especially in the capital cities like Dhaka or Chattogram, due to job loss and unemployment, which created housing and real estate inflation mostly in these capital cities. The production costs don't solely cause these demands in the urban centres, but relatively poor institutional capacities to handle the migration, which puts a gap in the classical cost push theory (Aisen and Veiga, 2011, P.327–338). Besides, cost-push inflation usually ignores the monetary factors in inflationary trends. However, excessive money supply in some countries' economies also played a prominent role, along with other vulnerabilities, in pushing the inflation rate upwards. In Sri Lanka during the economic crisis, the government and central bank initiated monetary policies like increased money supply, lowering interest rates, quantitative easing, etc., which resulted in inflation expectations and later hyperinflation in the country. Eventually, it can be said that, though cost-push or supply-driven inflation was one of the key players of high inflation trends in South Asian countries since 2020, it wasn't the sole explanation that can take the whole limelight, as other structural vulnerabilities also exacerbate the complex phenomenon.

Inadequacies of the Conflict Theory of Inflation

The conflict theory of inflation claims that inflation occurs in a country due to inequality in income distribution among the different social groups (Rowthorn, 1977, p. 217). When workers claim high wages from firms, the firms usually raise the price of the products to maintain the same profit from the production, which creates inflationary pressure in the economy. Conflict theory mainly focuses on how power struggles among social groups lead to economic price increases (Aoki, 1981, p. 359). However, this theory has made limited

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contributions to explaining the inflationary trends in various South Asian countries since 2020, as there are other key drivers of inflation in the region. However, one of the key assumptions of conflict theory is the presence of a wage-push spiral [7]or strong trade unions. But in reality, South Asian countries are short of strong trade unions due to a large informal sector with a minimal presence of unions. So, workers in these countries struggle to bargain for a high wage, as most of them have no formal contracts or organizations to support them.

Besides, during the 2020s, inflation in South Asian countries was not driven by a wage-push spiral. Even during and after the pandemic, many sectors have faced a decrease in real wages due to economic downturn and production loss. For example, in Bangladesh, many garment industries halved their employees' salaries since the COVID-19 pandemic due to the global supply chain disruptions and decreased production. So, inflation wasn’t directly influenced by the wage demand of labour, as there was no visible response from the labour markets or trade unions. Though there are some small, isolated sectors where the conflict theory may be applied, it cannot explain the significant economic crises in South Asia, like in Sri Lanka or Pakistan. So, this time the inflation in South Asia is mainly driven by the supply shocks and structural rigidities rather than the conflictual demands among the different social groups.

Limitations of the Structural Theory

The structural theory of inflation is mainly applicable to the developing world. The structural theory claims that inflation in developing countries mostly occurs due to structural weaknesses that hinder the capacity of production and supply of commodities—the low productivity of developing countries is often driven by outdated technologies, poor infrastructure, or supply-side bottlenecks (Prebisch, 1950, p. 14). The inflation trends in South Asia are influenced mainly by the structural theory of inflation, as structural vulnerabilities like poor government, political instability, high demographic pressure, etc., primarily affected the high inflation rates in South Asian countries. Though the structuralists do not identify some factors, they still play a crucial role in the inflation history of South Asia. Structuralism theorists ignore the short-term monetary and fiscal factors that impact inflation in developing countries. For example, budgetary mismanagement and policy failures

[7] This happens when workers demand higher wages due to rising living costs. If companies meet those demands, they often raise prices to cover costs, causing a cycle of rising wages and prices.

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were crucial in Sri Lanka during the economic crisis. Besides, the Central Bank's decision to increase the money supply to deal with the foreign debt also caused inflation, which cannot be described directly through the structural theory.

Structural theory also overlooks the demand factors that can cause high inflation in an economy. For instance, the demand inflation caused by instant increased aggregate demand due to inflation expectation among consumers and firms for anticipation of unexpected price rise in Pakistan worsens the situation; these types of behavioural dynamics or cyclical volatility are usually uncharacterized by the structural theory of inflation. Besides, structural theory often claims that underdevelopment causes inflation in an economy. However, one of the key drivers of Inflation in South Asia during the 2020s is the global commodity price shock, such as the rising price of commodities in the worldwide market, like oil or food grain in the international commodity market increased the prices in local markets as these countries are highly dependent on imported product. On the other hand, structuralists mainly focus on the structural weaknesses in the local economy without emphasizing the global factors. Otherwise, the inflation trends in different South Asian countries are highly relatable to the structural theory of inflation, as these countries have been going through structural weaknesses for a long time, which have affected the economic growth and price stability in these countries.

Chapter 5: Conclusion and Policy Recommendations

The study examined the Structural Vulnerabilities of South Asian countries that fueled the high inflation trend and volatility in this region during the 2020s, especially after the COVID-19 pandemic and the Russia-Ukraine war. When the world was fighting with global supply-chain disruptions and commodity price shocks, the structural underpinning of the South Asian countries magnified the inflation trends to a prolonged period due to internal weaknesses. Even when the other parts of the world started to recover from the shocks, countries like Bangladesh, Pakistan, and Sri Lanka in this region continue to face high inflation due to institutional weaknesses, political instability, high demographic pressure, etc. The long-term fiscal deficits and external debt in these countries also constrained the long-

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term development in this region. The paper explored the deeper reasons behind the high inflation in South Asian countries from both a theoretical and an empirical perspective.

Many economic theories, like the Quantity theory of money, Keynesian demand-pull theory, cost push theory, Conflict theory, etc., have successfully explored the underlying causes of inflation in different parts of the world; still, the trends in South Asia are more complex and diversified than a single theoretical approach. fell short in explaining the overall high inflation scenario in these countries. Though the structural perspective helped identify some of the core internal vulnerabilities of these developing countries, it has limitations, like ignoring the monetary policies or demand factors that fueled the high inflation in this region. In this study, three South Asian countries, Pakistan, Sri Lanka, and Bangladesh, have been discussed as case studies as they represent the most vulnerable inflationary situation in this region since 2020. The long-term structural vulnerabilities in these countries threaten the global economic environment, as South Asian countries are directly linked to international trade and investments, so these structural deficiencies need practical solutions. Issues such as weak institutions, high population growth, global supply chain disruptions, etc., have played a vital role in the increasing inflation rate in these countries. To deal with these long-term structural vulnerabilities, short-term attempts are not enough; they need a long-term fix.

Policy Recommendations:

- ❖ South Asian countries need good governments and political stability to continue their growth and avoid inflation. Their first and foremost need is to take policy initiatives to improve government quality through transparency, the rule of law, the autonomy of the central bank, and anti-corruption schemes.
- ❖ Policies to promote regional cooperation, such as intra-regional trade, can help these countries deal with supply-side bottlenecks and global shocks. The South Asian Association for Regional Cooperation (SAARC) should be empowered to enhance regional cooperation among South Asian countries.
- ❖ Agriculture plays a vital role in the commodity prices of South Asian countries. Policies to intensify local agriculture will help decrease the dependency on imported staple foods, which will help reduce food inflation.

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- ❖ Besides, upgrading the infrastructure, roads, transportation, and technologies will help reduce production costs and increase aggregate supply according to demand. For example, improving the food storage systems will help countries maintain a stable market price during a crisis.
- ❖ Improving urban planning and housing in the big cities will reduce the pressure of high population growth and migration people from rural to urban areas. Promoting family planning, maternity health, and education programs will help with rapid population growth.
- ❖ Last but not least, investing in public productivity sectors like education, energy, or health and decreasing subsidies or excessive deficit financing will help to avoid future hyperinflation and debt crises like those in Sri Lanka and will promote each country's self-sufficiency.

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