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MARKET RELATED INFLATIONARY FACTORS AND THE PURCHASE OF CONSUMER PRODUCTS IN NIGERIA.

By

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Abstract

Inflation and social welfare have remained a twin issue in any political landscape. The correlation between them is borne out of the fact that economic products available in the market are produced based on cost inputs transmitted into the value of finished goods. When inflationary factors persist, the costs of input increase resulting in expensive products and services. A trend of this nature reduces the purchasing power of the consumer and invariably his or her welfare. Government policies have been observed to have far reaching effect on the catalytic effect of inflation in the economy through active monetary policies or a lack-lustre attitude towards investment both internally organized or through foreign direct investment (FDI). Environment- wide impact of inflation cannot be overemphasized, as it has a gamut of negative effects across societal values such as education, women and child labour, diseases, conflicts, riots, and other anti- social disruptions. It was also observed that a veritable paradigm of modern marketing strategy is equally abused and short lived by inflation, as persistent price rise reduces the relationship between the buyer and the seller because of the attendant risks and uncertainty in the market place.

Keywords: Inflation, Welfare, Prices, Costs, Consumers, Government, Nigeria.

INTRODUCTION

A growing number of concerns about the purchasing power of consumers in developing countries in order to afford a quality standard of living have been linked to the deleterious effect of inflation. Inflationary trend depicts a situation occasioned by a persistent rise in the general price of goods and services. Goods and services constitute the products that make life worth a living. Quality products which can only be affordable at favourable price is the only guarantee for quality living and welfare.

In Nigeria, consumer products are essential assets, provisions, and other items needed to make life comfortable and are meant to be used for further production of other goods and services for sale. However, these items are not easily affordable due to the incessant price increases that have direct impact on the value of purchasing power of an average consumer.

Moreover, the cause of most price increases can be attributed to the import oriented economy that has come to characterize the country Nigeria, over the years due to its non-productive status among developing as well as developed countries.

In order to purchase these basic commodities, the seller has to embark on importation which requires the purchase of scarce foreign exchange since these items of comfort are produced overseas in developed countries like Japan, United States, United Kingdom and recently the inundation of mass marketing encroachment by the Asian tigers of the emerging economies like India, Malaysia, Hong Kong, and China into the Nigerian market with little or no policy on standardized products or mutual trade balancing.

Inflation plays an informational role in the determination of prices which tends to reduce welfare because it erodes the information in current prices about future prices. Prices have an informational role: a consumer cares about a price not only because it determines how much he currently pays but also because it is a signal of another variable much more related to price charged as related costs (Ball & Romer, 2003).

In the case of essential commodities like fuel for domestic and vehicular use in Nigeria, the informational role of price accompany a proportional dimension which usually results to panic buying of these products as sellers tend to hoard supply when they perceive inkling that government is likely to increase pump price or reduce petroleum subsidy.

During this period, the prices of items generally tend to head towards the sky, welfare is short-lived, economic transactions become expensive and the political atmosphere tensed even though government's position in the end usually prove such information as mere rumour peddling.

Future prices, which matter to consumers in long-term relationships, are a natural example of a variable for which current prices are a signal.

Relationships of long term nature matter a lot to marketers as a paradigm approach to competitive sustenance. When a relationship between a customer and producer of products is occasioned by constant price changes, it reduces the element of trust and commitment required in a relationship. If this occurs, uncertainty and relationship risk occur leading to customer's dissatisfaction and eventually switching behaviours.

Carlton (1982) emphasizes that agent who operates outside of thick markets use the information contained in market prices. For example, sellers of a customized products use the prices of similar standardized products to guide their own price setting. Vertically integrated firms compare the costs of internal input suppliers with market prices for the inputs to determine whether production is efficient or not.

When inflation adds noise to prices, they become less useful signals in these settings. Price variability benefits consumers because it creates opportunities for substitution toward low-price goods. A similar result holds for markets in which consumers search across sellers; in this case, price variability benefit consumers by raising the returns to search (Kohn & Shavell, 1974).

In deciding whether to enter a relationship, potential customers use a firm's current price as a signal of the prices it will charge in the future. When inflation causes relative prices to vary, it reduces the information about future prices in current prices and

when inflation reduces the informativeness of prices, the results are simply higher markups and more mistakes about which goods to purchase.

Welfare effects of the relative-price variability arising from inflation are depressing. If demand is not linked across periods, relative-price variability raises consumer welfare by creating opportunities for substitution toward low-price goods. On the other hand, relative-price variability causes costly variability in firms' sales, giving firms a strong incentive to reduce variability through more frequent price adjustments and in a long-term customer relationships in contrast, the inflationary effect reduces consumer welfare by reducing the informativeness of prices with little effect on firms because sales remain stable. Thus, long-term relationships explain both why relative price variability reduces welfare and why firms allow variability to occur through infrequent adjustment. (Ball & Romer, 2003).

The relative-price variability arising from inflation potentially harms both the suppliers who set prices and sell goods and the customers who purchase the goods. It is not plausible, however, that the losses to price setters are large.

Price setters have a simple means of stabilizing relative prices: they can adjust nominal prices frequently to keep up with inflation. Since the costs of such price adjustment often appear small, the amount of relative-price variability that suppliers permit must not impose large costs on them. Any major costs of price variability must fall on consumers (Ball & Romer, 2003). Firms sell a good to consumers who participate in the market for two periods as firms differ in their costs of production, and consumers differ in their tastes for the good. As aggregate price level rises steadily, firms adjust nominal prices every two periods; thus, a firm's relative price alternates between a higher level when it adjusts and a lower level when it does not. When a consumer enters the market, he meets a firm, observes its current price, and chooses whether to buy the good or not. Other major components of consumer outlay which record substantial higher rates of price increases include household goods and other purchases, clothing, accommodation and transportation.

Ranney (1981) and Schwab (1983) find that an increase in the rate of anticipated inflation may have differing effects on the size of

the house purchased, depending on the current mortgage market conditions, the financial constraints facing the household, and the level of inflation.

The present work is therefore intended to critically examine the effect of inflationary factors and how it affects consumers' buying behavior with respect to basic household welfare needs in Nigeria. Hence, this study is initiated to contribute to other aspects of consumer purchases and inflation from the perspective of household product purchase behaviour by consumers.

STATEMENT OF PROBLEM

Inflation has been acknowledged as a ruling parameter for the direction and informative factor for present and future prices. The higher the rate of inflation, the higher the prices of products and services, and vice versa. Household products are a toast for social welfare and a show of comfort and achievement in the basic standard of living of an average Nigerian. These products usually include televisions, household musical sets; example compact disc players and stereos, video players, and accompanying accessories.

Between 1990 and 1995 in Nigeria, the prices of these products rose astronomically that an average Nigerian could not afford the brand new types. This resulted in enabling marketers resorting to the importation of second-hand version most of these products commonly referred in the local parlance as "tokunbo". Therefore, considering the importance attached to the ownership of these products in a home, the effect of prevailing inflationary rate on the ability of consumers to purchase and own such ego-boosting and comfort signatures for the home becomes a thing of immense consideration.

Theoretical and empirical work suggests that an increase in the rate of anticipated inflation affects housing demand in two offsetting ways. First, an increase in inflation lowers the real after-tax user cost of housing due to the treatment of mortgage interest payments and imputed rental income. Secondly, the liquidity constraints that characterize the mortgage market become more binding as inflation, and so the nominal mortgage interest rate, increase. The constraints that prevent the household from borrowing against future income - the non-negativity constraints on wealth - may

be particularly effective in limiting housing demand (Aim & Follain, 1984)

It is widely accepted that the pursuit of price stability is primary to long-run growth and development and should be concern of every economy. One of the reasons for this is the high varying inflation rate which has social and economic shocks on the economy as a result of its negative effect on price stability, savings and investment factors such as changes in money supply, lagged changes in money supply, credit to government by the banking system, government deficit expenditure, industrial production, and food price indices are variables that jointly explained inflationary tendencies in Nigeria (Odusanya & Atanda, 2010).

They also identified increase in government expenditure financed by monetization of oil revenue and credit from the banking system as predictors of expansion of money supply in Nigeria which consequently, with a lagged-in-effect contributed immensely to inflationary tendencies.

Similarly, they opined that when the money supply growth increased substantially, inflation also accelerated and on the other hand, the decline in the monetary growth rate in 1994 in Nigeria led to a consequent decline in inflation rate.

Inflation has become a household topic of discussion in Nigerian families and the press alike as its effects penetrates more deeply into the nation's life due to prevailing increase in prices.

Persistent increases in prices are among the most prevalent economic problem in Nigeria as well as Africa. Considering the urban, rural and combined consumer price index in Nigeria, all components of price index rose at generally higher rate than previous years. The index for food dominated the increase in the aggregated index for most periods. This could be due to the fact that inflation has a general effect on farm economy compared to any other sector since the agricultural sector is highly volatile, with most of its outputs being perishable and with a high potential to pass on input cost increases directly into higher output prices in other sectors of the economy (Obasi, 2007).

The structuralists explanation for long-run inflationary trend in developing countries include the following factors; structural rigidities, market imperfection and social tension, relative inelasticity

of food supply, foreign exchange constraints protective measures, rise in demand for food, fall in export earnings, hoarding import substitution, industrialization, political instabilities (Onwioduokit, 2002).

Monetarists opine that "inflation is always and everywhere", hence prices tend to rise when the rate of inflation in money supply is greater than the rate of increase in real output of goods and services (Johnson, 1973).

On the other hand, imported inflation arises from international trade where inflation is transmitted from one country to the other, particularly, during periods of rising prices all over the world (Anyanwu, 1992). This is particularly true of today's feature of a global village with super highway information, economic, political, and cultural diffusion leaving no one unscathed as is still the case of the grueling effect of the global financial crises since 2008.

Ojameruaye (1988) noted that inflation is usually the result of the interplay of many factors. For instance, in most developing countries, including Nigeria, poor and inadequate tax programmes makes government unable to generate enough revenue leading to the pursuance of the policy of financing government expenditure by creation of money becoming inevitable. This invariably results in liquidity glut within the economy, a precursor of inflation.

In some cases natural consequences such as the drought which tends to hit some part of the world creates a supply crisis, thereby aggravating the upward trend in food prices.

Moreover, the huge jump in energy prices and rising environmental and political concerns force many countries to seek alternative sources. In Nigeria, the concern for a steady power supply for industrial and domestic capabilities has been a daunting task to several governments with threatening alarm by former president Musa Yar'adua to declare a state of emergency in the power sector. The inability of government to generate adequate and sustainable power supply for the economy has contributed in more gravely consequences to the excruciating effect of inflation on the economic activities especially the real sector with the resultant high cost of production and increased prices of goods and services. The increased costs paradoxically does not complement in terms of increased wages and salaries resulting in the gross diminution of the purchasing

capability of the ordinary consumer and by far implications for marketing activities.

The high inflation rate has therefore become not only a concern in the industrial and emerging market economies but to the general economy of the nations. In addition, this general rise in prices constitutes one of the factors responsible for the poverty generally in household and business concerns (Ayinde, Olatunji, Omotesho, & Ayinde, 2010).

LITERATURE REVIEW

Theories of Inflation

There are many theories of inflation, namely demand- pull, cost – pull, structural, monetary and imported inflation.

The demand- pull paradigm suggests that the inflation occurs when aggregate demand for goods and services is greater than the aggregate supply, such that the resultant excess cannot be satisfied by running down the existing stocks, diverting supplies from the export market to the domestic market, increasing imports or postponing demand.

The cost-push views attribute inflation to a host of non-monetary supply- oriented influences of shocks that raise costs and consequently price. In recent time, this school of thought has attributed inflation to such random non-monetary shocks such as crop failures, commodity shortages and increase in the price of oil (Onwiodukit, 2002).

The cost pull school suggests that inflation arises from increase in the cost of production, rising wages from trade union activities and embodies a sociopolitical view (Anyanwu, 1992).

Monetary inflation, as observed by Kiat (2008), occurs with the characteristics of for instance when monetary policy presents the impossible problem where trade-offs must be done in order to maintain economic stability thereby anchoring this on two prime factors of inflation autonomy and exchange rate variability.

On the other hand, imported inflation arises from international trade where inflation is transmitted from one country to the other, particularly, during periods of rising prices all over the world (Anyanwu, 1992).

Effects of Inflation

Persistent increases in prices are among the most prevalent economic problems in Nigeria as well as Africa. Considering the urban, rural and combined consumer price index in Nigeria, all components of price index rose at generally higher rate than previous years.

The index for food dominated the increase in the aggregated index for most of the periods. This could be due to the fact that inflation has a general effect on farm economy compared to any other sector since the agricultural sector is highly volatile, with most of its outputs being perishable and with a high potential to pass on input cost increases directly into higher output prices in other sectors of the economy (Obasi, 2007).

Other major components of consumer outlay which record substantial higher rates of price increase include household goods and other purchases, clothing, accommodation and transportation. There is a fixed cost of establishing a customer relationship with a seller. This assumption leads to long-term relationships; in equilibrium, a consumer buys either in both periods of life or in neither, despite the fluctuations in prices (Ball and Romer 2003).

Afolabi (1999) pointed out that the effect of inflation could be described as either creeping or hyper inflation depending on the dimension it takes at a particular time period in the economy. According to him, a creeping inflation which portends a mild effect on the economy is natural to stimulate production and economic growth. On the other hand, a hyper rate of inflation which is the opposite of the creeping inflation is a situation where prices escalate to an unreasonable level in the economy whereby the value of money virtually becomes useless.

In analyzing the effect of inflation on the purchase behavior of housing, Ranney (1981) and Schwab (1983) find that an increase in the rate of anticipated inflation may have differing effects on the size of the house purchased, depending on the current mortgage market conditions, the financial constraints facing the household, and the level of inflation. In contrast, Wheaton (1982) demonstrates that inflation always increases housing demand, even in the presence of borrowing restrictions that require wealth to be non-negative. However, he assumes that the household may continuously borrow

against the capital gains on the house. Housing cost is also associated with inflationary trend with respect to prevailing interest rate applicable to the marketing of housing units thereby inferring that interest rate is associated with cost-push inflation type.

The high inflation rate has therefore become not only a concern in the industrial and emerging market economies but to the general economy of the nation. Ayinde, Olatunji, Omotesho, & Ayinde (2010) equally indicated that, this general rise in prices constitute one of the factors responsible for the poverty generally in household and business concerns

Effect of Inflation on Consumers' Welfare

A substantial body of literature opined that inflation that affects the basic necessities of the common man is counter to good economic policy. Basic needs like food and shelter especially in developing countries constitute the main agenda of governments and when they become unaffordable due to inflation the value of welfare is eroded and people live in despair.

According to Ahmed (2008) he explained that there are several reasons the effects on food consumption, and welfare more generally, may have been quite serious, at least for certain types of households and that is first; the share of household expenditure spent on food is high, suggesting that welfare is sensitive to food price changes.

Secondly, little food production takes place in the cities, thus higher food prices do not raise urban incomes as agricultural production is absent there. Urban households are not in a good position to produce for own consumption, another notable difference compared to rural households. This reflects the nature of live in a city like Lagos in Nigeria where the majority of the residents are preoccupied with small, medium, and large business undertakings in entrepreneurship and large corporations almost round the week without any reasoning for even subsistence food production. The growing trend is the sale of available land portions for the purpose of housing development occasion by the quest for freedom from the pressure of shylock landlords. These leave the utilization of available land in a landscape of scrambled substandard properties occupying arable lands. Thirdly, there is no formal insurance mechanism for this

type of shock. (Ahmed, 2008). This would have been provided in Nigeria if only for the continued existence of the erstwhile marketing board.

There has been a longstanding debate about whether income or consumption expenditure should be used to measure household welfare. In the context of developing countries, using consumption measures appears to be favoured over using income measures, because income is often underreported and in many cases, volatile and difficult to remember (Deaton, 1997).

Macroeconomic volatility as measured by inflation, exchange rate, debt service ratio and unemployment may affect level of welfare. For example, it is well known that the level of unemployment impacts the rate of welfare. An increase in unemployment will first impact those marginal low skill, low wage workers that are the prime candidates to fall into poverty (Deutsch and Silber, 2005).

According to Fabiosa and Jensen (2002), cited in Odior and Fadiya (2011), macroeconomic shock will have impact on the level of household welfare via low private consumption expenditure and inflation may also affect measure of welfare if the income of low income families responds slowly to increases in the price level.

Alem and Söderbom (2011) in a study conducted on households in Ethiopia found that households with low levels of assets, and households headed by a casual worker, were particularly adversely affected by the food price inflation with a contrasting result suggesting that education plays at most a small role for the ability of households to cope with food price inflation. Similarly, household demographics appear to play a limited role in the same context.

Government Policy and Inflation

It is widely accepted that the pursuit of price stability is primary to long-run growth and development and should be concern of every economy. One of the reasons for this is the high varying inflation rate which has social and economic shocks on the economy as a result of its negative effect on price stability, savings and investment factors such as changes in money supply, lagged changes in money supply, credit to government by the banking system, government deficit

expenditure, industrial production, and food price indices are variables that jointly explained inflationary tendencies in Nigeria (Odusanya and Atanda, 2010).

They also identified increase in government expenditure financed by monetization of oil revenue and credit from the banking system as predictors of expansion of money supply in Nigeria which consequently, with a lagged-in-effect contributed immensely to inflationary tendencies.

Onwioduokit (2002) noted that it is in the opinion of Ojameruaye (1988), that inflation is usually the result of the interplay of many factors. In most developing countries, including Nigeria, poor and inadequate tax programmes makes government unable to generate enough expenditure; hence the pursuance of the policy of financing government expenditure by creation of money or deficit financing especially for capital projects development and employment becoming inevitable. This invariably results in liquidity glut within the economy, a precursor of inflation.

Similarly, when the money supply growth increased substantially, inflation also accelerated. On the other hand, the decline in the monetary growth rate in 1994 in Nigeria led to a consequent decline in inflation rate. The relative-price variability arising from inflation potentially harms both the suppliers who set prices and sell goods and the customers who purchase the goods.

As part of the macroeconomic objectives of government, the level of inflation in a country and its control is of concern to governments. Inflation can be caused by excessive money supply, insufficient supply of goods and services, excess demand over supply, droughts and crop failure. These concomitant effects results in societal distributive injustice having its toll on fixed income earners, a reduction in the propensity to save, and to far reaching extent, an enormous erosion in the value of money and its functions (Afolabi, 1999).

Effect of Inflation on Foreign Direct Investment (FDI)

Developing countries, especially Nigeria, has strong desire for foreign investment in their countries. Omankhanlen (2011) observed that in most developing countries there is the dearth of capital for investment which has affected the economic situation of

these nations. He indicated that, in order to ameliorate the situation, various governments of these nations have now focused much attention on investment especially foreign direct investment which will not only guarantee employment but will also impact positively on economic growth and development.

According to Ayanwale (2007) the relationship between FDI and economic growth in Nigeria is yet unclear, and that recent evidence shows that the relationship may be country and period specific implying a further study on their relationship. Developing countries economic difficulties do not originate in their isolation from advanced countries. The most powerful obstacle to their development comes from the way they are joined to the international system (Omankhanlen, 2011)

A stable economic policy and political policy that can provide a conducive economic environment that will help to attract FDI inflows into the country is desired. However, Kiat (2008), observed that the characteristics of monetary policy presents the impossible problem where trade-offs must be done in order to maintain economic stability thereby anchoring this on two prime factors of inflation autonomy and exchange rate variability.

The cost of foreign exchange or exchange rate in Nigeria is high due to a low level of the country's foreign reserves and a demand-pull string of inflation occasioned by an unwholesome demand for foreign made products since they are not produced locally even though they are in high demand.

Foreign direct investment (FDI) is a major component of capital flow for developing countries, its contribution towards economic growth is widely argued, but most researchers concur that the benefits outweigh its cost on the economy. (Musila & Sique, 2006). McAleese (2004) opines that FDI embodies a package of potential growth enhancing attributes such as technology and access to international market. Other literature suggests that, the host country must satisfy certain preconditions in order to absorb and retain these benefits.

According to Omankhanlen (2011), FDI is needed to reduce the difference between the desired gross domestic investment and domestic savings and attracting and encouraging more inflow of foreign capital. Foreign direct investment consists of external

resources including technology, managerial and marketing expertise and capital. All these generate a considerable impact on the host nation's productive capabilities. The success of government policies of stimulating the productive base of the economy depend largely on her ability to command adequate amount of FDI comprising of managerial, capital and technological resources to boost the existing production capacity. Although, the Nigerian government has been trying to provide conducive investment climate for foreign investment, the inflow of foreign investments into the country have not been encouraging.

As a concluding remark Omankhanlen (2011) suggests that given the Nigerian economy resource base, the country's foreign investment policy should move towards attracting and encouraging more inflow of foreign capital. This is necessitated by the government's two principal objectives of; the desire for economic independence and the demand for economic development.

Mwillima (2008) describes foreign direct investment as investment made so as to acquire a lasting management interest (for instance 10% of voting stocks) and at least 10% of equity shares in an enterprise operating in another country other than that of the investor's country.

Foreign Direct Investment can also depict an investment made by an investor or enterprises in another enterprise or equivalent in voting power or other means of control in another country with the aim to manage the investment and maximize profit. This investment involves not only the transfer of fund but also the transfer of physical capital, technique of production, managerial and marketing expertise, product advertising and business practice with the aim to make profit (Omankhanlen, 2011).

Olaniyi (1998) in his study observed the impact of direct foreign capital on domestic investment to ascertain its overall contribution to the enhancement of domestic savings capacity in Nigeria. Empirical evidence from his study indicated that with his model of domestic savings and investment financing in Nigeria, the results confirm that domestic savings is by far more relevant in determining investment growth than foreign capital inflows in Nigeria and at best, foreign capital only serves as a complements to domestic savings stock.

Community Environmental-wide Effects of Inflation

Easterly and Fischer (1999) present evidence from a variety of sources including subjective assessments of the importance of inflation on the community indicating that inflation matters more to the poor than the rich, who are presumably in a better position to protect their living standards.

Community Environmental Effects (CEE) impacts according to them, are felt not just by individual households, but by whole communities; as traditional ties and networks and other forms of social capitals are disrupted because of economic hardship, integration, and the emergence of fault times between different ethnic, religious, or racial groups.

There is evidence from several countries that social capital can be damaged during crises emanating from inflation. Households respond to these shocks in various ways. Consumption patterns change in response to price change, production levels change across sectors and employment pattern change. Children are pulled out of school and sent to work; people turn to informal sector jobs. In some cases, poor women increase their labour force participation in response to a decline in the income of the main household earner.

They also observed that the situation might lead to a reduction in the nutritional intake of babies or pulling of children out of school which can have permanent effects on their future learning and income earning abilities. Malnourished mothers are more likely to give birth to low-birth-weight children, who in turn are more likely to suffer from poor health.

Ferreira, F., Prennushi, G. & Ravallion M. (1999) study also show that evidence from rapid social assessments conducted in Thailand, the Philippines, Indonesia and Cambodia, and survey in Korea, Indonesia and Thailand confirming that the poor responded to the effects of inflation in ways which will affect their long-term well being. These according to them include youngsters being taken out of secondary schools and sent to work, health care is delayed or foregone, with increased risks of epidemics of communicable diseases, malnutrition spreads, and productive assets being sold. There is also anecdotal evidence of reverse migration from the cities to the country side or urban-rural strange migration trend. Their observation also indicated that, in Nigeria, the acquisition of

education was dampened both by a reduction in the rate of enrollment in primary school and a smaller share of people continuing on to higher levels of education (Ferreira & Keely, 1999).

CONCLUSIONS/RECOMMENDATIONS

Inflation has remained an economic and social burden to contend with by both the government and the individuals. An inflationary trend of any type affects both trading and welfare factors. The accelerating effect of inflation erodes values across board both internally and externally.

It has been examined from the study that the deleterious shocks of inflation affects the poor more than the rich as the rich are presumably in a better position to protect their living standards.

It is equally noted that, relative-price variability causes costly variability in firms' sales, giving firms a strong incentive to reduce variability through more frequent price adjustments.

The adjustments in prices create relational risks and uncertainty between the marketer and the consumer as the element of trust and commitment is mutually impaired and welfare short-lived.

A major suggestion is that government through its monetary and other economic policies should be conscious of inflationary triggers such as its policy on extra budgetary demands, and deficit financing and to realize that any policy that will in the long run impede negatively on societal long run expectation of the citizens' welfare which can be evidenced by their ability to purchase essential products and services is a betrayal of the social contract.

Therefore, all efforts to sustain quality welfare through affordability of quality products and services should be encouraged by all investible means including through direct inflow of foreign investment that will enliven the economy.

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