

Inflationary Expectations and Demand for Per Capita Real Balances : Evidence from the Indian Economy.

M. S. Trivedi

1. INTRODUCTION

In another paper by the present author, along with some simpler models, a wealth adjustment model of demand for money function with permanent income and anticipated rate of inflation as its arguments was tested with Indian data. The study was based upon annual data covering the period between 1951-75 (Trivedi M.S., 1980a, 1980b). The specific objective of the study was to assess the empirical performance of various models in which expected rate of inflation was specified as the opportunity cost variable in place of conventionally used interest rates, prevailing in the organized capital markets. The demand variable employed in that study was the total real stock of money - undeflated by population - and the expectational variables were operationalised by utilising the geometric distributed lag scheme.

The present study is a continuation of the earlier study. It attempts to test the previously tested models in *per capita real terms*. The purpose is to ascertain to what extent the major empirical findings of the earlier study are corroborated or modified when the tests are implemented on the basis of per capita data.

Obviously, defining and testing the macro money-demand relation in per capita real terms involves an implicit *a priori* restriction that the demand for nominal stock of money is homogeneous of degree one in measured price level and population. In the previously mentioned study related with the total real stock of money, one of the problems encountered was the relatively closer R^2 s, yielded for various specifications and to that extent it was found difficult to assess the comparative empirical performance of various models, with sufficient confidence. This particular difficulty was found to be especially significant in discriminating between the empirical performance of the permanent income version of the money demand function relative to the measured real income version, though evidence of indicative nature could be collated which pointed to the