

Some Recent Developments in Macro-economics and Their Implications for Inflation : Empirical Evidence from India

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Quarterly data for India for the period 1973 to 1983 support the existence of an 'Expectation Augmented Phillips Curve'. Our results contradict the hypothesis of the New-classical economists that unanticipated money growth leads to a sudden jump in price level and subsequently only to output growth. We have, on the other hand, found much empirical support for the Buffer-stock approach to money. In India for this period there is much evidence for the 'Imported Inflation'. It appears that small but continuous exchange-rate depreciation during the period of study for India has not led to inflation.

The empirical implications of the recent macro-economic theories on inflation are not only interesting in themselves and for policy formulations but also useful for the future courses of the theoretical and empirical work in macro-economics. We are also empirically examining the conventional excess-demand model of inflation of the expectation augmented Phillips Curve on the one hand, and the money supply - inflation models on the other hand, and adding some structural variables to both types of inflation models like the import prices, food price-index etc., for Indian data. Needless to mention one cannot expect to claim to the econometric rigour of putting the foregoing two models as exactly competing hypothesis of inflation, and therefore if one is correct, then the other is not necessarily a misspecification. The econometric reason is that the proxy for excess activity variable and the excess money supply variable can be correlated to some extent.

One of the limitations of testing the aggregate models of inflation, viz., the excess activity and Phillips Curve variety, to the Indian economy is that the organised and unorganised sectors of the economy are aggregated together, and the Phillips Curve hypothesis may not be applicable to the unorganised sector of the economy.

The money supply model of inflation, is to empirically test the implications of the recent theoretical controversies of the effect of the anticipated and unanticipated money supply-changes on inflation, between new-classical economists and the Buffer stock approach economists.

The plan of the paper is as follows :

Section I surveys the implications of the recent theoretical issues in macro-economics between new-classical school and the Buffer stock approach.

Section II deals with the literature on the modelling of inflation incorporating the exchange-rate depreciation.

In Section III, the empirical models, results and conclusions are given.