Convergence of Demand Pull into Cost Push Inflation in Indian Economy

Topic: 516A Financial Analysis
Author: Shri PRAKASH
Co-Authors: Sudhi Sharma

Inflation has been the perennial problem world over since times immemorial. But the Indian economy had been experiencing periodic inflationary pressures even before the problem became endemic in the developed countries. Besides, the genre of inflation in Indian economy is different from that of the developed economies. Reason is that inflation in Indian economy has not been a monetary phenomenon at any time. The economy had been experiencing famines due to periodic crop failures, resulting in the high rise in prices of agricultural goods in general and food grains in particular. The rise in food prices are accounted by sudden shortages of supplies of essential goods. Thus, inflation does not emerge in all sectors simultaneously which occurs due to exceptional rise in money incomes. The demand pull inflation in Indian economy is, therefore, not the consequence of increase in demand due to excess supply of money in the economy; the excess demand is the result of supplies falling short of demand for good and other agricultural goods, even though monetary incomes and quantities of demand might have remained constant. This feature of the economy has not changed much despite seven and half decades of the growth of the Indian economy and structural changes associated with growth.
The paper has evolved four input output models to empirically examine the problem in alternative ways and also to compare the results furnished by different models. The paper also focuses on the evaluation of the stability of elasticity coefficients of fix-prices with respect to the observed and hypothetical changes in flex prices in the economy.
Two of the four I-O models are integrated ones and rest two models are decomposed I-O models. Changes in flex prices are treated as exogenous to the system, though both flex price sectors (41) and fix price sectors (89) are an integral part of I-O models.
The thrust of the findings is that the monetary policy followed by India in recent years, which is patterned on the policy of developed economies, has been a failure to contain what to say mitigate inflation due to its irrelevance to the structural features of the economy and the root cause underlying inflation. Inflation in Indian economy is structural rather than monetary.

(1) Research Questions
1.1 Is Inflation in India is Monetary or Structural phenomenon
1.2 From which sectors Inflation originates in India
1.3 Is RBI following Policy which addresses the genesis of inflation in Indian Economy
1.4 What is the impact and spread of changes of flex/agricultural prices on fix/non agricultural prices
1.5 Is Demand pull Inflation necessarily a monetary phenomenon in economies like India
1.6 What is the degree and direction of responsiveness of fix prices to changes in flex prices

(2) Method Used:
2.1 Four Input Output Models- two are decomposed and two are integrated

(3) Data Used:
3.1 Input Output Table of CSO 2008
3.2 Data relating to flex prices of 20011, 2012 and 2013

4. Novelty of the research
4.1 The mechanism of conversion of demand into cost push inflation in Indian Economy
4.2 Estimation of coefficients of elasticity of fixed prices with respect to changes in flex prices
4.3 Evaluation of stability of point elasticity and their convergence to arc elasticity.