



Full Length Research Article

THE IMPACT OF MONETARY POLICY ON FOOD FUEL AND CORE INFLATION

***Merlin Juliet, D.**

Department of Economics, Madras Christian College, Chennai 59, India

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ABSTRACT

The widely talked about problem in our country “ Inflation” has been thoroughly analyzed also with various jargons such as CPI ,WPI, PPI, core inflation and headline inflation by experts. In order to find out the root cause for the rise in prices or fall in the purchasing power of currency or the reasons for people’s constant struggle to fulfill their desires, analysis is still going on at different levels. Are the factors coming from demand side or supply side is a question which is yet to be answered. Will the monetary policy work or the fiscal policy be effective is always a puzzle. This paper aims at looking at the problem with a different perspective taking time series data on inflation in India from January 2013 to April 2015 to learn the causal relationship between various inflation rates and the headline inflation.

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INTRODUCTION

A very basic problem for a country like ours where there is quite a big proportion of population living below poverty line is the persistent rise in prices. Even if people get the very basic essentials such as food at a subsidized rate through public distribution system there are many more goods and services which come under the category of essentials these days. So to maintain a reasonable standard of living, one needs a substantial real income to see that the means and ends meet .As the real income is very less they are constantly at debt trap and vicious circle of poverty. To give a solution to this social menace,monetary authorities tried various stabilization policies but in vain. So, deep analysis is done by the statistical organizations and the banking sector by checking the basket of goods to identify the trouble maker. Consumer price index consists of food, beverages, tobacco, health ,education, transportation, communication ,entertainment, housing ,fuel and light, clothing and footwear .Headline CPI inflation means the number we get from combined data of above mentioned categories. Core CPI = Headline inflation –(food and fuel components). Headline CPI and Headline WPI measure the total inflation within the economy including commodities such as food and fuel, the prices of which are more volatile due to seasonal fluctuations and international conditions where as core inflation which is known as personal

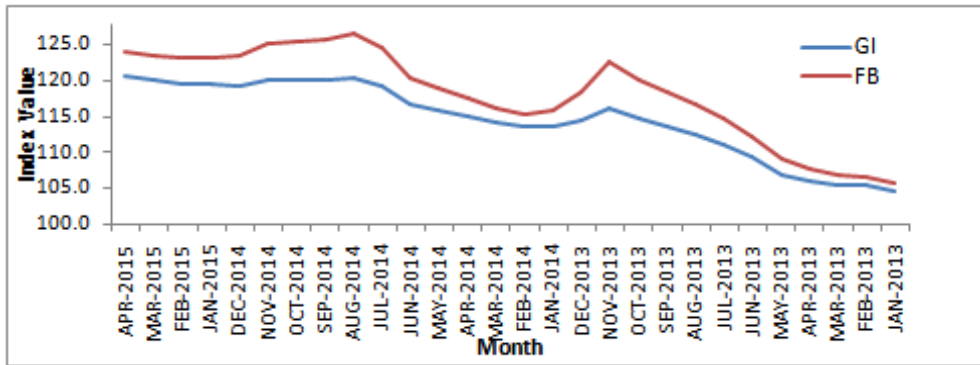
consumption expenditure index excludes primary articles such as food and fuel groups. This non food manufacturing goods index gives a better picture about the working of manufacturing units in an economy.The manufacturing units depend on the banking sector for financial assistance and so the effect of monetary policy instruments can be studied through the variations in the core inflation rates before and after the implementation of monetary stabilization policies. The demand for food beverages is inelastic but the supply is elastic because it depends mainly on the nature. The mismatch between the demand and supply leads to price rise for these commodities. The only option to control food inflation is to boost supply. Monetary policy instruments such as CRR and Repo cannot make any impact on food inflation. Fuel and light also has inelastic demand because there are no substitutes and there is always supply shortage. Most of the time the prices of those products are determined by the government taking welfare into consideration and so they are not market prices but subsidized administered prices. The other components of CPI like Housing, Paan- tobacco-intoxicants, clothing, and miscellaneous (communication, transportation, personal care and household operational expenses) can have some impact of monetary policy instruments because the providers of these products will have huge banking operations. Through financial assistance by the banks, supply bottlenecks can be avoided and price can be regulated. According to Engel’s Law of consumption the proportion of income spent for food and other essential commodities will fall as income rises and the

***Corresponding author: Merlin Juliet, D.,**
Department of Economics, Madras Christian College, Chennai 59,
India.

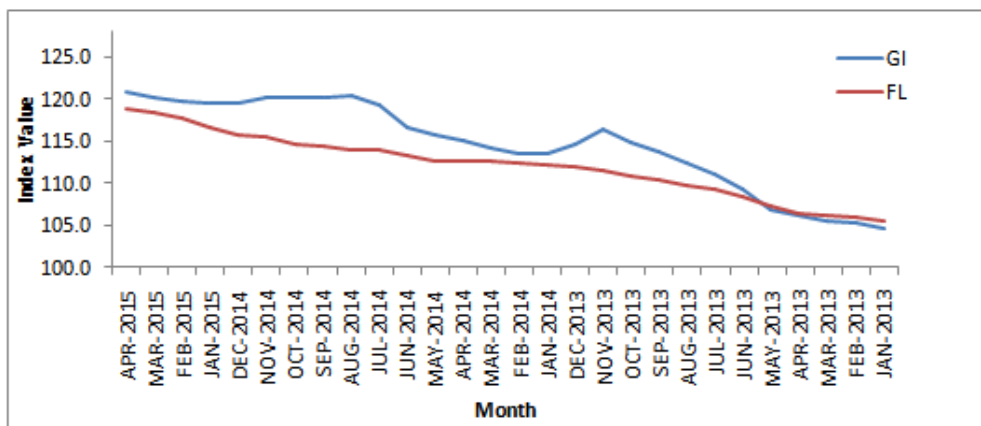
proportion of income spent on durables and not-so- essential commodities and services will rise.

Based on this law, the weights assigned for food items is reduced and weights for housing and household operational

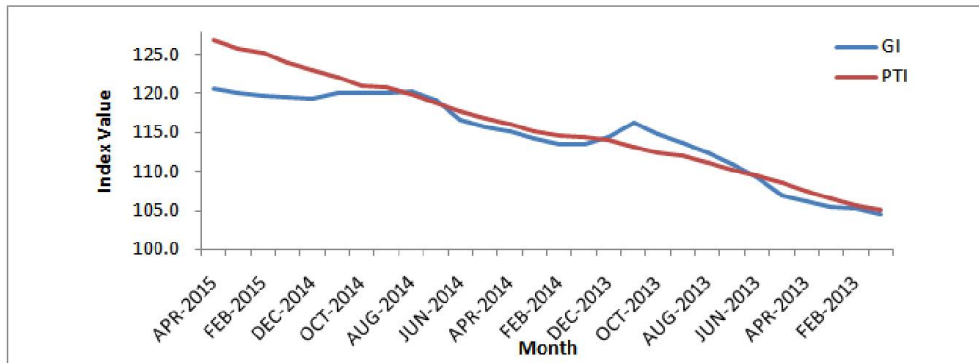
General Index (CPI) & Food and Beverage



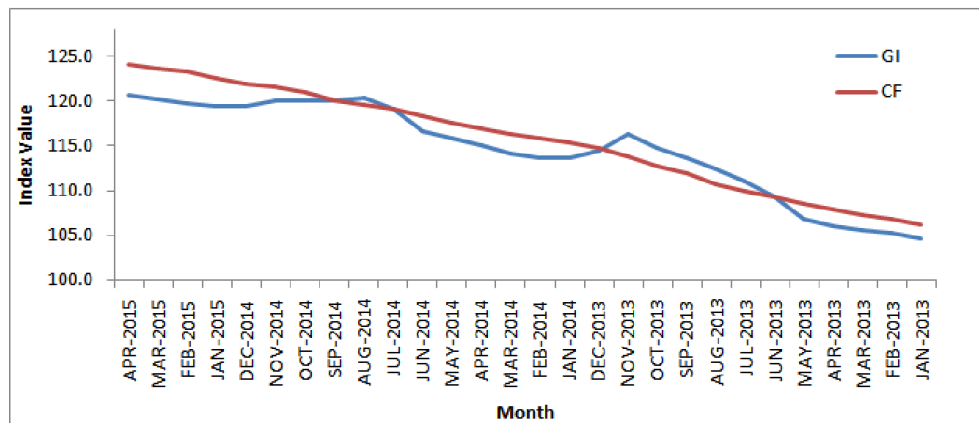
General Index (CPI) and Fuel and Light



General Index (CPI) and -Pan Tobacco and Intoxicants



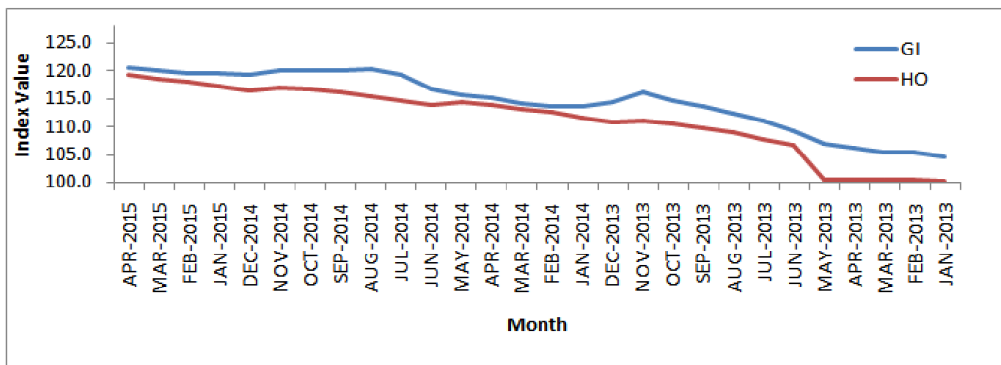
General Index (CPI) and Clothing and footwear



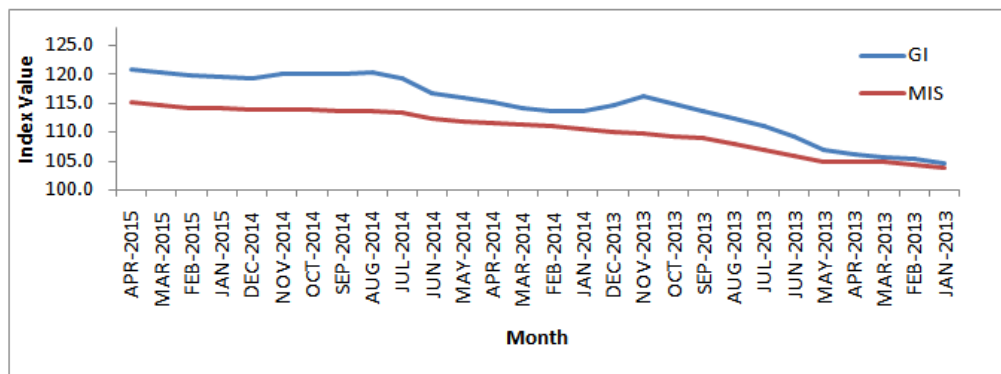
services have been increased in the recent past indicating that India is in the development path. The percentage of income spent on food should come down drastically so that the weights assigned to food items compared to other commodities is very low hence food inflation can disappear. Core inflation can be easily managed through stabilization policies. This is possible only when the per capita income of the rural poor reach a reasonably good level. Total rate of growth of national income or total GNP will not be a sufficient condition!

coal. This WPI is also known as Headline WPI inflation. Core WPI inflation means WPI of non-Food manufacturing industries (ie) Core WPI =Headline WPI-(Primary+ Fuel+ manufactured food products). As most of these products covered under Core inflation are dealt by manufacturers, traders and distributors who have huge transactions with banks, monetary policies can make impact on WPI inflation. Regression results for WPI and the components.

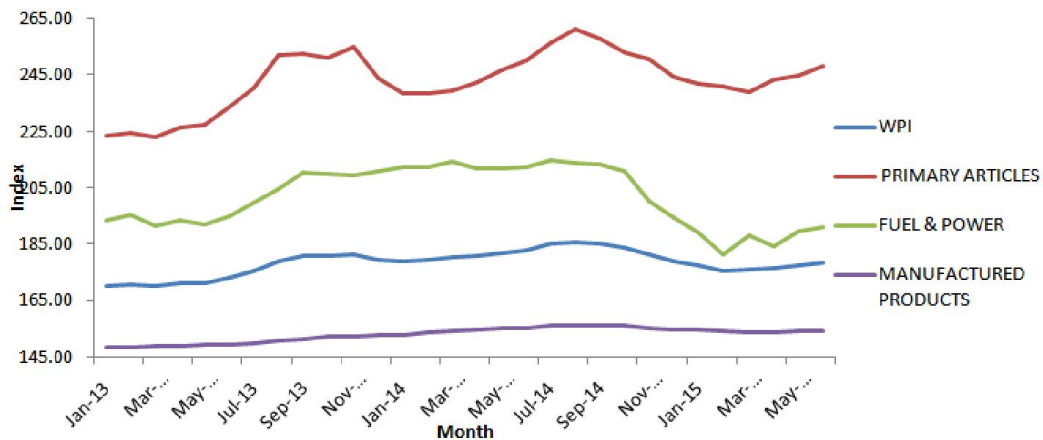
General Index (CPI) and Housing



General Index (CPI) and Miscellaneous



WPI and its Components



When it comes to WPI, the components are primary, fuel and manufactured products. Primary includes food, non-food articles and minerals. Manufactured goods include food, metal and chemicals products. Fuel includes oil, electricity, LPG and

Though the weights given and the number of primary products are low, the coefficient for the primary products (.466) is more when compared to the other two categories namely fuel (.356) and manufactured goods (.364). Nearly 50% change in WPI is

caused by primary products which are not directly under the control of the monetary policies. The graphical analysis on CPI and the graphical and statistical analysis on WPI reveal that the rise in price is mainly because of food inflation as core inflation is stabilized through stabilization policies.

Regression results for WPI and the components

Components	Beta	t value	sig value
Constant		-345	.733
Primary	.466	172.0	.000
Fuel and Power	.356	186.4	.000
Manufactured	.364	148.5	.000

The demand for food will keep on increasing and so fiscal and monetary policies should focus on the production of food products which is possible only if individuals and corporate involve themselves in large scale cultivation through mechanization, intensive and extensive cultivation. Banking services can come into picture only then to give financial assistance to those who are involved in production and marketing of agricultural produce. Agricultural sector should be dragged and included in the growth process.

To conclude, if the supply of agricultural products such as fruits, vegetables and protein products are increased to match the growing demand for these products, inflation can be curtailed to a very large extent. Agriculture sector being the backbone of our nation can heal the economy suffering from inflation.

REFERENCES

- Newspapers
- Websites
- Journalarticles

Appendix 1 CPI and its Components

Year	GI	FB	PTI	CF	HO	FL	MIS
APR-2015	120.7	124.0	126.9	124.1	119.2	118.7	115.1
MAR-2015	120.2	123.4	125.8	123.7	118.6	118.3	114.7
FEB-2015	119.7	123.1	125.2	123.3	118.1	117.7	114.1
JAN-2015	119.5	123.1	124.0	122.5	117.3	116.5	114.0
DEC-2014	119.4	123.6	123.0	122.0	116.5	115.7	113.8
NOV-2014	120.1	125.1	122.1	121.6	117.1	115.5	113.8
OCT-2014	120.1	125.4	121.1	121.0	116.7	114.7	113.9
SEP-2014	120.1	125.8	120.8	120.1	116.1	114.3	113.7

AUG-2014	120.3	126.6	119.9	119.6	115.5	114.0	113.7
JUL-2014	119.2	124.7	118.8	119.1	114.8	113.9	113.3
JUN-2014	116.7	120.4	117.8	118.3	113.9	113.2	112.3
MAY-2014	115.8	118.9	116.8	117.6	114.3	112.5	111.8
APR-2014	115.1	117.6	116.0	117.0	113.9	112.5	111.5
MAR-2014	114.2	116.1	115.2	116.4	113.2	112.5	111.3
FEB-2014	113.6	115.3	114.7	115.9	112.5	112.4	110.9
JAN-2014	113.6	115.8	114.5	115.4	111.6	112.2	110.6
DEC-2013	114.5	118.4	114.0	114.8	110.7	111.9	110.0
NOV-2013	116.3	122.6	113.1	113.8	111.1	111.6	109.7
OCT-2013	114.8	120.2	112.5	112.8	110.5	110.9	109.2
SEP-2013	113.7	118.3	112.0	111.9	109.7	110.5	109.0
AUG-2013	112.4	116.6	111.2	110.7	108.9	109.7	107.9
JUL-2013	111.0	114.7	110.3	110.0	107.7	109.2	106.9
JUN-2013	109.3	112.2	109.5	109.3	106.6	108.3	105.8
MAY-2013	106.9	109.2	108.6	108.5	100.5	107.4	104.8
APR-2013	106.1	107.7	107.5	107.9	100.5	106.5	104.8
MAR-2013	105.5	106.9	106.6	107.3	100.4	106.1	104.7
FEB-2013	105.3	106.6	105.7	106.8	100.4	106.0	104.4
JAN-2013	104.6	105.6	105.1	106.2	100.3	105.5	103.9

WPI and its Components

Month	WPI	Primary Articles	Fuel & Power	Manufactured Products
Jun-15	178.60	248.40	191.00	154.20
May-15	177.70	244.90	189.80	154.10
Apr-15	176.40	243.60	184.30	153.90
Mar-15	176.10	239.00	188.00	153.90
Feb-15	175.60	240.90	181.20	154.00
Jan-15	177.30	242.10	189.00	154.50
Dec-14	178.70	244.40	194.60	154.70
Nov-14	181.20	250.80	200.10	155.20
Oct-14	183.70	253.30	210.80	155.90
Sep-14	185.00	257.80	213.40	156.00
Aug-14	185.90	261.20	214.00	156.10
Jul-14	185.00	256.60	214.60	156.00
Jun-14	183.00	250.30	212.30	155.40
May-14	182.00	246.80	212.10	155.10
Apr-14	180.80	242.40	211.80	154.60
Mar-14	180.30	239.40	214.20	154.20
Feb-14	179.50	238.50	212.60	153.60
Jan-14	179.00	238.80	212.40	152.90
Dec-13	179.60	243.70	211.10	152.50
Nov-13	181.50	254.90	209.60	152.30
Oct-13	180.70	251.40	209.80	152.10
Sep-13	180.70	252.70	210.60	151.50
Aug-13	179.00	251.90	204.70	150.60
Jul-13	175.50	240.30	199.90	149.90
Jun-13	173.20	233.90	194.70	149.50
May-13	171.40	227.30	191.90	149.30
Apr-13	171.30	226.50	193.70	149.10
Mar-13	170.10	223.10	191.60	148.70
Feb-13	170.90	224.40	195.50	148.60
Jan-13	170.30	223.60	193.40	148.50
