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A STUDY ON INFLATION TRENDS IN INDIA AND ITS CAUSES

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Abstract: The problem of inflation is also a significant economic phenomenon that has effects on individuals as well as the economy in general. It decreases the buying power of money and brings in uncertainty in financial decisions. Governments turn to such instruments as fiscal policy to regulate inflation by cutting the amount of money spent by people or raising taxes. Demand-pull inflation is a situation whereby there is greater demand in the goods and services than the supply that is available hence causing the prices to skyrocket. The research is premised on the secondary data retrieved through journals, websites, and reports. It seeks to learn the trends of inflation in India, its key causes, and the effects that it has on the stability of the economy. The research is useful in understanding further about inflation and how it can be used in financial decision-making.

Keywords: Inflation, Economic Uncertainty, Consumer Price Index (CPI), Wholesale Price Index

1. INTRODUCTION

Inflation is a persistent rise in the price of goods and services in a certain duration of time. The increase in price will mean that money will be valuable and individuals will be able to purchase less using the same sum of money. The inflation is a significant indicator of the economic situation in a country. The inflation will be a significant factor in influencing the economic policy in a developing country such as India.

The average inflation is said to be healthy since it motivates people to spend and invest. Nevertheless, high inflation may lower the savings and uncertainty, and it may deteriorate individuals and companies. On the same note, low inflation can reduce the pace of economic growth to very low levels.

In India, the Consumer Price Index (CPI) is used as the primary indicator of inflation. The reserve bank of India (RBI) manages inflation by using the monetary instruments like the repo rate and reverse repo rate. Fiscal policies serve the other purpose of stabilizing prices by the government. Inflation in India varies with time because of the variables such as fuel prices, supply situations and the happenings in the global economy.

2. BACKGROUND OF STUDY

The problem of inflation has never been insignificant either to the developed or developing nations. It is a mirror of the rise in cost of living and it influences financial planning of individuals and business. The inflation in India has been experiencing various phases in the form of internal and external influences.

Due to globalization, inflation is no longer a problem that is affected by domestic factors. Crude oil prices, exchange rates, and world economic situation are some of the international factors that contribute significantly. As an illustration, when the cost of fuel goes up, transportation and production costs go up consequently leading to high prices of goods.

The recent occurrences such as the COVID-19 pandemic were influential on inflation. It upset supply chains, production, and cost increments causing price variations. Inflation is also affected by the policies of the governments, the taxes, and the monetary policies. Hence, the stability of inflation rate is beneficial to the economic growth and stability.

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3. Objective of the Study

- To understand the causes and effects of inflation
- To identify the risks of inflation in India due to domestic and global factors
- To study how inflation changes due to different economic conditions

4. REVIEW OF LITERATURE

In the literature, studies that specifically analyse the tail risks of inflation are still very rare (Banerjee, Contreras, et al., 2020; López-Salido and Loria, 2020). However, a few research over the past ten years have examined the dynamics of inflation quantiles. Wolters and Tillmann (2015), for example, look at how distinct quantiles persist in the conditional distribution of inflation. In the instance of South Africa, Gupta, Jooste, and Ranjbar (2017) discover stronger inflation persistence for larger quantiles. In a study of 12 OECD countries using the quantile regression approach, Tsong and Lee (2011) demonstrate unequal convergence of inflation to long-run value. This finding is consistent with relevant literature on convergence. They discover that positive shocks converge slowly to the long-run level and are more enduring than negative shocks. Uganda likewise exhibits comparable empirical data (Anguyo, Gupta, and Kotzé, 2020).

Iddrisu and Alagidede (2020), for example, use quantile regression to explain food inflation and its various determinants, including economic growth, inflation in the price of food globally, monetary policy, etc., for South Africa. This is just one of many studies that have focused on different determinants of inflation in a quantile regression framework.

Lahiani (2019) investigates how crude oil prices are distributed across several US price quantiles.The idea of inflation at risk is comparable to value at risk (VaR), which refers to the extreme quantiles for a given degree of probability in financial risk management. A comparable metric, known as Growth at Risk, is also available for economic growth among macroeconomic factors (Prasad et al., 2019).

In their examination of advanced economies, Lopez-Salido and Loria (2020) specifically derived the conditional distribution based on quantiles. Emerging economies were added to the analysis by Banerjee et al. (2020), who also assessed the conditional density. Their research reveals that nations with IT exhibit relative inflation risks that are moderater than those in non-IT countries.

When Banerjee, Mehrotra, and Zampolli (2020) simulate the COVID-19 pandemic's effects, they discover that emerging economies face greater upside and downside risks from inflation, while advanced economies face greater downside risks. In contrast to past studies that employed quantile regression to analyse the quantiles of inflation and their dynamics, the development in deriving the conditional distribution based on quantile is a novel contribution in the works mentioned above. These analyses emphasise, in particular, how various shocks affect the inflation tail risks. In our research, we extend the analysis previously stated for India and look at some country-specific characteristics to explain the dynamics of inflation tail risks.

In 2005, Daal et al. conducted research on the relationship in several developed and developing nations, including India. They discovered evidence for the Friedman-Ball and Holland hypothesis for India (negative relationship between inflation and inflation uncertainty). In a number of Asian nations, including India, Rizvi et al. (2009) discovered bi-directional causality between inflation and uncertainty.

With respect to India, Chowdhury (2014) uses the generalised autoregressive conditional heteroscedasticity (GARCH) model to uncover evidence in favour of this claim. Similar data on inflation and inflation volatility are graphically presented by Kundu, Bhoi, and Kishore (2018) at the sub-national level. While the monetary authority assigns weights temporarily to reduce its loss preference, inflation uncertainty is a key worry.

5. Statistical Data:

Table No: 1
India Inflation Rate
Consumer Price Index

Year	Inflating rate
2024	4.95
2023	5.65
2022	6.7

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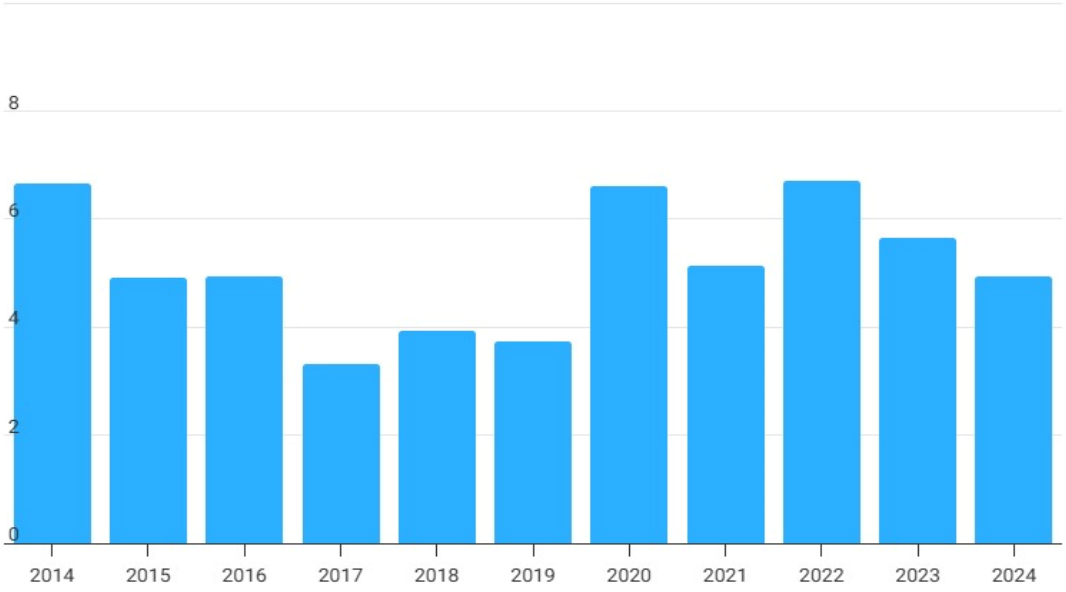
2021	5.13
2020	6.62
2019	3.73
2018	3.94
2017	3.33
2016	4.95
2015	4.91
2014	6.67

Source: https://www.macrotrends.net/global-metrics/countries/ind/india/inflation-rate-cpi

Figure No:1



Source: https://www.macrotrends.net/global-metrics/countries/ind/india/inflation-rate-cpi

6. FACTORS INFLUENCING INFLATION IN INDIA

Inflation in India is affected by several factors, which can be grouped into the following categories:

1. Demand Factors

When demand for goods and services is higher than supply, prices increase. This is common in situations where people spend more but production is limited.

2. Supply Factors

Shortage of goods due to poor agricultural output, natural disasters, or transport issues can lead to higher prices. Increased production costs also raise prices.

3. Domestic Factors

Weak financial systems and improper market structures can affect inflation. Changes in interest rates and money supply also influence price levels.

4. External Factors

Global factors such as exchange rates, import prices, and international market conditions affect inflation. For example, an increase in oil prices globally increases inflation in India.

7. FINDINGS

The study demonstrates that fiscal policy as well as the monetary policy are significant instruments that help to contain inflation. Inflation can be reduced through decreased public expenditure or raising taxes by the government. These will decrease the total demand in the economy.

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Monetary policy also has a major role to play. The central bank can cut down interest rates to decrease the number of borrowers and spenders which will aid the central bank in controlling inflation. The level of price also becomes stable when the demand is low.

There are cases that fiscal and monetary actions can be applied together in situations of high inflation. To illustrate, high demand in the economy can be well checked by ensuring that the government spending is reduced and the taxes are equally raised.

8. CONCLUSION

The effects of inflation are both good and bad in the economy. The moderate inflation is conducive to growth in the economy but high inflation is detrimental as it lowers the purchasing capacity in addition to creating some uncertainty. It also impacts the investment of long term in terms of lowering their real worth.

Hence, there is the need to sustain a moderate rate of inflation. Fiscal and monetary policies can be used in a proper manner to help in controlling inflation and equilibrate the economy. Inflation trend helps one to plan and make financial decisions.

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