CHAPTER I

STATEMENT OF THE PROBLEM

1.1 Introduction
1.2 Reasons for the choice of the topic
1.3 Objectives of the Study
1.4 Uniqueness of the study
1.5 Research Methodology
1.6 Chapter Scheme of the Study
CHAPTER I
STATEMENT OF THE PROBLEM

1.1 Introduction:

There are very few topics in economics, particularly in macroeconomics, which have received greater or as much attention as the topic of inflation. This is primarily because it is the topic which touches the lives of people in all walks of life and all dispositions.

There is no single theory which explains the concept, origin causes and consequences of inflation. Economists and the propounded theories so far differ a great deal in this respect. Therefore, inflation is considered as a complex phenomenon.

In simple language, it is referred to a situation in which there is excess demand over supply, a situation wherein too much money chases too few goods, a situation wherein wages or costs chase prices and prices chase wages and costs or a situation of disproportionate increase in incomes of the people compared with the available output. It can be defined and described in variety of ways. It is however to be noted that price rise is called inflation only when it is general and sustained over a long period of time. In short, it refers to a persistent rise in general price level.

High inflation is viewed with concern and considered enemy number one because of its adverse socio-economic impact. In a developing country like India where poverty is a rule, it turns out to be disastrous, for it reduces the purchasing power of money, sends many people below poverty line, creates balance of payments problems, adversely affects savings, encourages investment in unproductive assets and thus derails the growth process and widens the inequalities
of income and wealth. The analogy of a hydra-headed monster is used to describe the bad consequences of inflation, with each head of the monster representing a bad consequence.

As far as India is concerned, inflation has been a chronic problem for long. It became more severe in the 1970’s and 1980’s with the excessive practice of deficit financing for achieving the developmental goals and finally culminated in the economic crisis of 1990-91. In the second half of the 1990’s and early years of new century, it however appears to have remained more or less subdued, which perhaps is the result of more autonomy being offered to the Reserve Bank of India in the conduct of monetary policy and the break-up of the fiscal-monetary nexus with the discontinuation of deficit financing in 1997. Similarly, it can be termed as the end effect of new economic policy adopted in 1991, which has helped to some extent correct the macro economic imbalances through reforms.

This research work is an attempt to analyze the historical trend in inflation in India, ascertain various causes of inflation, their relative importance in causing it, links of inflation with other macroeconomic variables etc. over a period of more than 70 years from 1935 to 2009. Originally though the period of this study was limited upto 2005, data until 2009 has been used and analyzed, as it is available. This study also makes an attempt to briefly review the policy options available and actually used by the government of India through RBI for keeping inflation under control.

1.2 Reasons for the choice of the topic:

Though there is enough literature available on the problem of inflation in India and its causes and consequences, no research work
has attempted a review of inflationary process in India for such a long period of time of over 70 years. Further, the available literature on inflation touches one or two aspects of inflation problem, whereas the present study endeavors to study as many dimensions of inflation as possible. The unique feature of the present work is that, it has divided the analysis of inflation in four stages defined by major historical events – namely

- Establishment of the RBI – 1935
- Nationalisation of the RBI – 1949
- Nationalisation of commercial banks – 1969

1.3 Objectives of the Study:

The objectives of the study are as follows:

1. To trace the changes in inflation over a period of seventy years.
2. To study the relationship of inflation with money supply, agricultural production and balance of payments related variables.
3. Identifying the contemporary factors leading to inflation and significant fall in inflation.

1.4 Uniqueness of the study:

The period of the present study, which starts with 1935 and ends at 2009 is a unique attribute of the study. However, it is to be noted that the study begins with the establishment of RBI and the end coincides with the completion of most of the financial sector reforms in India.
Moreover, the data used in this work has entirely been sourced from the available published material, so it is subject to the limitations which the published material carries.

1.5 Research Methodology:

The present study is largely a library work based on published official secondary data and theoretical literature. The secondary data used for the present study is mainly drawn from the following libraries.

2. Library of Chh. Shahu Institute of Business Education & Research, Kolhapur
3. Servants of India Society’s Library, Ghokhle Institute of Politics & Economics, Pune.
4. R. N. Godbole Chair Library, Shivaji University, Kolhapur.
7. Other sources accessible on internet.

The necessary secondary data is collected mainly from the following published work.

1. Budget documents published by the ministry of finance, Govt. of India.
2. Economic Surveys published by the ministry of finance, Govt. of India.
3. Reports on currency and finance published by Reserve Bank of India.
4. Monthly Bulletins published by the Reserve Bank of India.

5. Handbook of Statistics on Indian Economy, Reserve Bank of India.

6. Handbook of Monetary Statistics of India, Reserve Bank of India.

7. Volumes of History of Reserve Bank of India.


9. Archives of Economic and Political weekly.

10. Archives of Yojana.

The collected data is tabulated and graphed to suit the analytical purposes and is subjected to statistical techniques like percentage variations, averages, compound annual growth rate, correlation (simple and partial) and standard deviation.

In each of the chapter, the analysis of the data is divided into following historical stages.

1. Establishment of Reserve Bank of India (1935) to Nationalization of Reserve Bank of India (1949)


1.6 Chapter Scheme of the Study:

The study is divided into following chapters.

Chapter No. 1: Statement of the Problem.

This chapter underscores the need of this study along with the main objectives and statement of the research methodology adopted.
Chapter No. 2: Review of Literature.
This chapter reviews the available literature on the topic of inflation in India. The review covers books, collected volumes, reports, research articles in journals and other publications.

Chapter No. 3: Inflation Record of India (1935 to 2009)
This chapter presents the collected data on inflation in India in a chronological order as also in stages mentioned above, along with analysis of the same mainly in terms of the contributing factors.

Chapter No. 4: Money Supply and Inflation
This chapter documents the rate of Inflation, rate of increase in money supply and their interrelationship, in stages defined by periods mentioned above.

Chapter No. 5: Agricultural Output and Inflation
In this chapter, an attempt has been made to correlate agricultural and food grains production with food inflation and overall inflation measured on the basis of WPI.

Chapter No. 6: Inflation and BOPs
In this chapter, an attempt has been made to correlate the rate of inflation with the balance of payments related variables like imports, exports, trade account balance, exchange rate and foreign exchange reserves. Impact of major devaluations is also briefly outlined.

Chapter No. 7: Inflation and Policy
This chapter attempts to review the available policy options before the govt., monetary, fiscal and physical to control inflation. A brief reference is also made to actually used measures, particularly in the recent past.
Chapter No. 8: Conclusions and Policy Implications.

This chapter presents conclusions arrived at on the basis of this study and also specifies policy implications.