

## **Inflation Dynamics in India: P-Star Approach**

**Nandini Sud**

Panjab University, India  
nandinisudd@gmail.com

### **Abstract:**

The P-Star model puts together long-run determinants of price level based on the classical QTM and short-term changes in current inflation. In this approach, along with the output gap, velocity gap is also taken into consideration for price-level determination. P-star is defined as the price level which is consistent with current money supply and equilibrium in goods and financial markets. Deviations of actual price from P-Star indicate the amount of price adjustment which has not yet materialized and can help predict future movements in the price level. The study aims to examine the validity of the P-star model in India by estimating fourteen models using competing measures of inflation (GDP deflator and WPI) and output (real GDP and IIP) by analysing annual and quarterly data from 1980-2019. All the variables will be tested for stationarity and thereby suitable econometric models will be estimated and requisite diagnostic tests will be conducted. Further the forecasting ability of the models will be tested to arrive at the best P-star model for India. Section I will explain the concept of P-Star model and lay down a historical perspective of inflation in India. Section II will provide review of literature. Section III will describe the data and methodology. Section IV will enunciate the empirical results. Section V will conclude and provide policy recommendations.

**Keywords:** Inflation, Econometric Model, Money Velocity

**JEL Codes:** E31, E37, E41