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THIS IS WHAT HAPPENED TO THE NEXUS BETWEEN INFLATION AND OIL PRICE AMONG SOME DEVELOPING COUNTRIES — A MACROECONOMIC ANALYSIS

ASIM K. KARMAKAR¹ & SOVIK MUKHERJEE²

Abstract

The recent rounds of recession have renewed the fears of consumer price inflation. Theoretically, as oil is used as a direct input for many consumer items it will lead to higher prices for some goods and services. Historically, the “pass through” effect of oil price shocks was very evident during the seventies but disappeared somehow in the eighties. Interestingly, empirical research, however, has not always predicted that oil price shocks leads to a general rise in the price level. In this backdrop, the research question is how variations in global oil prices impacts domestic inflation in a panel data set-up of thirty emerging and developing countries including India, Pakistan and China during the period from 2000 to 2016. The results show that a rise in the global oil prices leads to an impact on domestic price inflation. Interestingly, we find some asymmetric impact of oil price shocks for Asian and non-Asian countries. The impact of monetary policy has been significant and as a result the oil price shock has declined over the years in the post-globalization era which is something momentous given the current situation.

Key words : oil price, structural shocks, inflation, monetary policy, fiscal policy

JEL Classification: E58, O11, N15

I. Introduction

OPEC was formed on September 14, 1960 with five founding members : Saudi Arabia, Kuwait, Iran, Iraq and Venezuela. The current membership of 14 nations also includes Qatar, Indonesia, Libya, the UAE, Algeria, Nigeria and Ecuador. Its original purpose was to try and obtain higher prices for oil sold to the “seven sisters”: ESSO, Royal Dutch Shell, Anglo-Persian Oil Company, SoCal, Gulf Oil and Texaco, which were the major oil companies that dominated production, refining, and distribution at that time. By 1970, oil had begun to exert considerable control over production by its members and this in turn, had a significant influence on the market price for crude oil.

1.Assistant Professor (Stage III),Department of Economics,Jadavpur University, Kolkata.

2.Lecturer in Economics,Department of Commerce ,Shri Shikshayatan College, Kolkata