NEUTRALITY OF MONEY IN INDIA: A MYTH OR A REALITY

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ABSTRACT
The paper aims to study the causal relation between money supply, output, general price level and interest rate for India. The nature of the causal link has serious implications for the effectiveness of monetary policy and the monetary policy rule itself (which instrument should be used to achieve stabilization of output around natural rate and inflation around zero). To investigate the issue of neutrality of money in the context of Indian economy post liberalization, four variable vector autoregressive models is developed. Cointegration procedure is applied to determine whether the system is stable and to draw inferences about long run relationship. The empirical findings presented in this paper consistently show that evidence based on the post liberalization Indian experience indicate a close and reliable relationship between money and real economic activity.

KEYWORDS: Causal link, Cointegration, General Price level, Interest rate, Money supply, Output.

JEL CLASSIFICATION: C22, E40, E50

REFERENCES


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