

## Prices and Monetary Management

It is well recognized that inflation in India is a structural as well as a monetary phenomenon. In the short term, localised demand – supply imbalances in wage goods, often due to seasonal variations in production – coupled with market rigidities and regulatory failures have supported inflationary expectations that have resulted in a more widespread impact on the consumers than the initial inflationary impulse. In the medium- to long-term, the movement and outcome of monetary aggregates such as the money supply and reference interest rates of the financial systems have influenced aggregate demand and

consequently changes in price levels in the economy. The latter considerations and the influence of global commodity prices on the domestic prices have become more important with the opening and growing integration of the Indian economy with the rest of the world. Indeed, the fiscal 2007-08 has demonstrated this facet of the economy more than ever before. With huge surge in capital inflows, the liquidity management with its underlying implications for inflation has been a major challenge for the policymakers. This chapter brings together an analysis of developments on prices and monetary management in 2007-08.