

**INFLATION AND ECONOMIC GROWTH NEXUS
IN EGYPT**

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IN EGYPT

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ABSTRACT

The moderate and stable inflation rates are promoting important factors in the development process of a country, and hence economic growth. Moderate inflation supplements return to savers, enhances investment, and therefore, accelerates economic growth of the country. This paper empirically explores the present relationship between inflation and economic growth in the context of Egypt. Using annual data set on real GDP and CPI for the period of 1980 to 2010, an assessment of empirical evidence is acquired through the co-integration and error correction models. Further, it explores a policy issue of what is the threshold level of inflation for the economy using the threshold autoregressive models. The empirical evidence demonstrates that there exists a long-run and a short-run relationship between inflation and economic growth. In addition, the estimated threshold model suggests 15 percent as the threshold level (i.e., structural break point) of inflation above which inflation adversely affects economic growth.

Keywords: Inflation, Economic Growth, Granger Causality, Threshold level of Inflation

ABSTRAK

Kadar inflasi yang sederhana dan stabil adalah faktor penting kepada proses pembangunan negara, dan pertumbuhan ekonomi. Inflasi sederhana mendatangkan pulangan pendapatan kepada ke simpanan, meningkatkan pelaburan, dan dengan itu, mempercepatkan pertumbuhan ekonomi negara. Kajian ini empirik meneroka hubungan antara inflasi dan pertumbuhan ekonomi dalam konteks negara Mesir. Dengan menggunakan data tahunan KDNK benar dan indeks harga pengguna (IHP) bagi tempoh 1980 hingga 2010, penilaian diperolehi melalui kaedah co-integration dan model pembetulan ralat. Ia menerokai isu dasar iaitu apakah tahap ambang inflasi bagi ekonomi dengan menggunakan model paras ambang autograsi. Bukti empirik menunjukkan bahawa wujud hubungan jangka panjang dan jangka pendek antara inflasi dan pertumbuhan ekonomi. Di samping itu, anggaran dari model paras ambang mencadangkan 15 peratus sebagai tahap ambang (iaitu, titik perubahan struktur) inflasi dimana inflasi yang melebihi paras ini akan menjejaskan pertumbuhan ekonomi.

Keywords: Inflasi, Pertumbuhan Ekonomi, disebabkan Granger, tahap Ambang Inflasi

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TABLE OF CONTENTS

PERMISSION TO USE.....	i
ABSTRACT.....	ii
ABSTRAK.....	iii
ACKNOWLEDGEMENTS.....	iv
TABLE OF CONTENTS.....	v
LIST OF TABLES AND FIGURES.....	vii

CHAPTER ONE

BACKGROUND OF THE STUDY

1.1 Introduction.....	1
1.2 Problem Statement.....	5
1.3 Research Questions.....	6
1.4 Objectives of the Study.....	7
1.5 Hypothesis of the Study.....	8
1.6 Significance of the study.....	8
1.7 Scope of the study.....	9
1.8 Organization of the Study.....	9

CHAPTER TWO

REVIEW OF RELATED LITERATURE

2.1 Introduction.....	11
2.2 The Economy of Egypt.....	11
2.3 Historical Trends of Inflation and Economic Growth in Egypt.....	12
2.4 Review of previous Studies.....	18
2.4.1 Theoretical studies.....	18
2.4.2 Empirical studies.....	22

CHAPTER THREE	RESEARCH METHODOLOGY	
3.1 Sources and Classification of Data		37
3.2 Theoretical Framework		38
3.3 Model Specification		39
3.4 Method of analysis and measurement		40
3.4.1 Estimation Co-integration and Error correction model		40
3.4.1.1 Unit Root Test		41
3.4.1.2 Co-integration		46
3.4.1.3 Error correction model		47
3.4.2 The Granger causality test		48
3.4.3 Estimation Threshold of Inflation TAR method		50
CHAPTER FOUR	EMPIRICAL ANALYSIS	
4.1 Descriptive Analysis		52
4.2 Empirical Results and Finding		54
4.2.1 Test for unit roots		54
4.2.2 Co-integration test result and Analysis		57
4.2.3 Error Correction Mechanism		58
4.2.4 Granger Causality Test		60
4.3 Threshold Model Estimation		61
CHAPTER FIVE	CONCLUSIONS AND POLICY IMPLICATIONS	
5.1 Conclusion of empirical results		64
5.2 limitation of study		66
5.3 policy implication		67
REFERENCES		69

LIST OF TABLES AND FIGURES

Figure 2.1 : inflation and real GDP growth rate in Egypt.....	14
Figure 3.1 : The Conceptual Model of the Economic Growth.....	38
Figure 4.1 : GDP Descriptive Statistics	53
Figure 4.2 : INF Descriptive Staistics	54

Table 2.1 : Description of Inflation and GDP Growth (1981/82-2009/10).....	14
Table 4.1 : Descriptive Statistics.....	53
Table 4.2 : Augmented Dickey – Fuller (ADF) Stationarity test at Levels.....	55
Table 4.3 : Phillips-Perron (PP) Stationarity test at Levels.....	55
Table 4.4 : Augmented Dickey – Fuller (ADF) Stationarity test at First Difference.....	56
Table 4.5 : Phillips-Perron (PP) Test Stationarity test at First Difference.....	56
Table 4.6 : Results of Johansen’s Cointegration Test	57
Table 4.7 : Error Correction Model Test Result	59
Table 4.8 : Granger Causality Tests Result.....	60
Table 4.9 : Estimation of inflation threshold model at $K = 5$ - $K = 16$	62

CHAPTER ONE

BACKGROUND OF THE STUDY

1.1 Introduction

The relationship between inflation and economic growth is one of the most important issues in economy. It becomes issue of debate among the macro economists, policy makers and central monetary authorities. Specifically the bone of contention is that whether inflation is necessary for economic growth or it is detrimental to growth. Basically the rate of economic growth depends primarily on the rate of capital formation and the rate of capital formation depends on the rate of savings and investment. Therefore, whether inflation affects economic growth depends on whether it affects savings and investment (Kanchan and Chandan 2011).

The link between inflation and growth remains a controversial one in both theory and empirical findings. Originating in the Latin American context in the 1950s, the issue has generated an enduring debate between structuralists¹ and monetarists. The structuralists believe that inflation is essential for economic growth, whereas the monetarists see inflation as detrimental to economic progress. There are two aspects to this debate: (a) the nature of the relationship if one exists and (b) the direction of causality. Friedman (1973: 41) succinctly summarized the inconclusive nature of the relationship between inflation and economic growth as follows: “historically, all possible combinations have

1) **Structuralism** is an approach to the human sciences that attempts to analyze a specific field as a complex system of interrelated parts.

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