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DETERMINANTS OF INFLATION: EVIDENCE FROM ASEAN-5 COUNTRIES

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MASTER OF ECONOMICS
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DETERMINANTS OF INFLATION: EVIDENCE FROM ASEAN-5 COUNTRIES

By

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A dissertation submitted to
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Universiti Utara Malaysia
In Fulfillment of the Requirements for the Award Master’s Degree of Economics
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Abstract

Topic involving inflation has generated an enormous volume of literature and heated debate in recent years. It is important to study inflation because the consequences of inflation is terrible. By explaining inflation, different school of thought view the contrast cause and have different policies for fighting inflation. This study examines the relationship between selected independent variable towards inflation and theory that can explain inflation in ASEAN-5 countries using panel data analysis. This study used panel data spanning from year 1990 to 2014. A panel data approach was used to straighten out the time invariant country-specific effect and to reveal the relationship between the important variables across time. The results presented that fixed effect model was appropriate over the random effect models in this inflation model studied. Interestingly, the variables, namely wages, import, interest rate and gross domestic product were found to be significant determinants of inflation in ASEAN-5 countries. But, only money supply found to be insignificant by explaining the inflation in this sample of study. Based on these results, this study support the Post Keynesians view of inflation and several policy implications and recommendations were suggested.

Keywords: Inflation; ASEAN-5 countries; Fixed Effects Model; Random Effects Model, Post Keynesians
Abstrak


Kata kunci: Inflasi; negara ASEAN-5; Model Tetap Kesan; Model Kesan Rawak, Post Keynesians
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This thesis is dedicated to them.

Thank you.
Table of Contents

Permission to Use ..............................................................................................................................i
Abstract ..............................................................................................................................................ii
Abstrak ................................................................................................................................................iii
Acknowledgement ...............................................................................................................................iv
Table of Contents ...............................................................................................................................v
List of Tables ......................................................................................................................................viii
List of Figures ......................................................................................................................................ix
Glossary of Terms ..............................................................................................................................x
List of Abbreviations ..........................................................................................................................xi

CHAPTER ONE: INTRODUCTION .................................................................................................1
1.1 Background of study ....................................................................................................................1
  1.1.1 Inflation in ASEAN-5: An Overview .................................................................................2
1.2 Problem Statement .....................................................................................................................6
1.3 Research questions .....................................................................................................................9
1.4 Objectives of study ..................................................................................................................10
1.5 Significance of study ...............................................................................................................10
1.6 Scope of the study ...................................................................................................................11
1.7 Organization of study ..............................................................................................................12

CHAPTER TWO: LITERATURE REVIEW .....................................................................................13
2.1 Introduction .................................................................................................................................13
2.2 Concept and Measurement of Inflation ..................................................................................13
2.3 Theoretical Review of Inflation ...............................................................................................15
  2.3.1 Post Keynesians Theory of Inflation .............................................................................15
  2.3.2 Demand-Pull Theory ......................................................................................................18
  2.3.3 The Quantity Theory of Money .....................................................................................19
  2.3.4 Monetary Theory of Inflation .........................................................................................20
  2.3.5 Structural Inflation Theory .............................................................................................20
  2.3.6 Rational Expectations Revolution .................................................................................21
  2.3.7 New Neoclassical Synthesis (NNS) ...............................................................................22
  2.3.8 New Political Macroeconomics of Inflation .................................................................23
2.4 Method Used for Analyze Determinants of Inflation ..............................................24
2.5 Previous Empirical Findings ................................................................................26
2.6 Concluding Remarks ............................................................................................30

CHAPTER THREE: RESEARCH METHODOLOGY .................................................31
3.1 Introduction ..........................................................................................................31
3.2 Theoretical Framework .......................................................................................31
  3.2.1 Post Keynesian Model of Inflation ...............................................................32
  3.2.2 Monetary Theory of Inflation .......................................................................34
3.3 Hypothesis Statement .........................................................................................34
3.4 The Model ............................................................................................................35
3.5 Variables and Measurement ...............................................................................37
  3.5.1 Consumer Price Index (CPI) ......................................................................37
  3.5.2 Wages ..........................................................................................................37
  3.5.3 Money Supply Growth ................................................................................38
  3.5.4 Gross Domestic Product (GDP) ..................................................................38
  3.5.5 Real Interest rate .........................................................................................39
  3.5.6 Import .........................................................................................................39
3.6 Data Collection ....................................................................................................40
3.7 Method of Analysis ..............................................................................................40
  3.7.1 Pooled Ordinary Least Square (POLS) Regression Model .........................41
  3.7.2 Fixed Effects Model ....................................................................................42
  3.7.3 Random Effects Model ..............................................................................43
  3.7.4 Panel Granger Causality Test ....................................................................43
3.8 Specification Test of the Model ..........................................................................44
  3.8.1 Fixed Effect Hypothesis Testing ................................................................44
  3.8.2 Random or Fixed Effects Model ................................................................45
  3.8.3 Breusch-Pagan Lagrange Multiplier (LM) Test ..........................................45
3.9 Concluding Remarks ...........................................................................................46

CHAPTER FOUR: RESULTS AND DATA ANALYSIS ........................................47
4.1 Introduction ..........................................................................................................47
4.2 Results of Panel Data Analysis ..........................................................................47
List of Tables

Table 4.2 Panel Data Estimation of ASEAN-5 Countries ....................................................48
Table 4.3 Specification Tests .............................................................................................50
Table 4.4.1 VIF Test for Determinants of Inflation .............................................................52
Table 4.5 Pairwise Granger Causality Test Results .............................................................54
List of Figures

Figure 1.1.1 Inflation Rate across ASEAN-5 Countries..........................................................3
Figure 3.2 Determinants of inflation......................................................................................32
Glossary of Terms

ASEAN-4:
Indonesia, Malaysia, Philippines and Thailand

ASEAN-5:
Indonesia, Malaysia, Singapore, Philippines and Thailand

M2 (Money supply):
M1 + narrow quasi – money

G-7 (Group of Seven Developed Countries):
Canada, France, Germany, Italy, Japan, United Kingdom and United States
# List of Abbreviations

<table>
<thead>
<tr>
<th>Abbreviation</th>
<th>Full Form</th>
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<tbody>
<tr>
<td>ADF</td>
<td>Augmented Dickey-Fuller</td>
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<tr>
<td>ASEAN</td>
<td>Association of Southeast Asian Nation</td>
</tr>
<tr>
<td>CPI</td>
<td>Consumer Price Index</td>
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<td>ECM</td>
<td>Error Correction Model</td>
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<td>FEM</td>
<td>Fixed Effect Model</td>
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<tr>
<td>FMOLS</td>
<td>Fully Modified Ordinary Least Square</td>
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<tr>
<td>GDP</td>
<td>Gross Domestic Product</td>
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<tr>
<td>GNP</td>
<td>Gross National Product</td>
</tr>
<tr>
<td>G-7</td>
<td>Group of Seven Developed Countries</td>
</tr>
<tr>
<td>GST</td>
<td>Goods and Services Tax</td>
</tr>
<tr>
<td>IMF</td>
<td>International Monetary Fund</td>
</tr>
<tr>
<td>M2</td>
<td>Money Supply</td>
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<tr>
<td>MAS</td>
<td>Monetary Authority of Singapore</td>
</tr>
<tr>
<td>OLS</td>
<td>Ordinary Least Square</td>
</tr>
<tr>
<td>OPEC</td>
<td>Organization of Petroleum Exporting Countries</td>
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<tr>
<td>POLS</td>
<td>Pool Ordinary Least Square</td>
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<td>PPI</td>
<td>Producer Price Index</td>
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<td>REM</td>
<td>Random Effect Model</td>
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<td>WPI</td>
<td>Wholesome Price Index</td>
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<td>VAR</td>
<td>Vector Error Correction</td>
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<tr>
<td>VECM</td>
<td>Vector Error Correction Model</td>
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<td>VIF</td>
<td>Variance Inflation Factor</td>
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CHAPTER ONE
INTRODUCTION

1.1 Background of study

Persistent and substantial increasing in general level of prices has worrying impact. This situation has widely attracted the attention of the economists all over the world. Whitney (1982) define inflation as a “sustained increase in average prices”. Issue involving inflation has generated a huge volume of literature and heated debate in recent years. It is crucial to study inflation because the effect of inflation is terrible.

Generally the inflation rate has an impact to world economic growth of the country whether negative or positive impact. This inflation rate and world economic growth have been fluctuating. A case study of Tanzania indicated that inflation has an negative impact on economic growth (Kasadi & Mwakanemela, 2013). Whereas, Shahbaz (2013) confirms there is co-integration among economic growth, terrorism and inflation in Pakistan. Rises in inflation and economic growth raises a terrorist attack and terrorism in Pakistan.

By utilizing panel regressions, Rousseau and Wachtel (2002) found finance growth relationship in inflation threshold. Studies states that, disinflation is positive effect related to financial depth on growth. However, studied inflation threshold done by Thanh (2015) found inflation and growth has an inversely relationship.

Based to this several studies on inflation, issue of inflation still on discussing within the researchers in different context because once inflation occurs, it creates problems
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