

**ANALYSING THE IMPACT OF MONETARY POLICY ON
FOOD PRICE DYNAMICS IN INDIA**

INIYAN A

*A project report submitted in partial fulfilment of the requirement for the
award of the degree of*

MASTER OF ARTS

IN

FINANCIAL ECONOMICS



May 2025

MADRAS SCHOOL OF ECONOMICS

Chennai- 600025

ABSTRACT

Food Inflation plays an important role in driving the headline inflation in emerging economies like India, it therefore becomes important to understand how monetary policy adjustment influence food prices. This study investigates the effectiveness of monetary policy in managing food price inflation in India, with a focus on both aggregate and disaggregated food subgroups, using monthly data from January 2014 to December 2024. Using a Factor-Augmented Vector Autoregression (FAVAR) model, the analysis incorporates 30 comprehensive set of macroeconomic and financial variables to capture the complex transmission mechanisms of monetary policy shocks, proxied by changes in the Weighted Average Call Money Rate (WACR). The findings reveal that while contractionary monetary policy induces a statistically significant short-term decline in aggregate food inflation, as measured by the Consumer Food Price Index (CFPI), this effect is transitory, with inflation rebounding within 6–12 months possibly due to supply-side rigidities. At the disaggregated level, non-perishable subgroups like cereals and spices exhibit only moderate responsiveness to monetary tightening, while perishable subgroups, including milk, eggs, meat, and vegetables, show minimal or statistically insignificant responses, driven by biological production cycles, perishability, and fragmented supply chains. The study advocates for a coordinated policy approach, integrating disaggregated inflation monitoring, supply chain reforms, and fiscal measures to enhance food price stability, household welfare, and to address India's evolving inflation dynamics.

Keywords: Monetary policy, Inflation Targeting, FAVAR, Food Inflation