

# Commodity and Oil Price Fluctuations, Macroeconomic Performance and Challenges for an Emerging Economy: The Indian Experience

by

**D. TRIPATI RAO**

Professor, Business Environment Area, Indian Institute of Management, IIM Road  
Lucknow-226 013, India, E-mail: [tripati@iiml.ac.in](mailto:tripati@iiml.ac.in) & [dtripatirao@yahoo.com](mailto:dtripatirao@yahoo.com)

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**SAURABH GOYAL**

Assistant Commissioner, Income Tax Department, Ministry of Finance, Government of India,  
New Delhi, E-mail: [sontygoyal@gmail.com](mailto:sontygoyal@gmail.com)

## Abstract

Commodity and oil price fluctuations have significant bearing on domestic macroeconomic performance and challenges macroeconomic policy making of an emerging economy. The paper explores the impact of non-energy commodity and oil price fluctuations on domestic macroeconomic variables such as, output, inflation and real exchange rate in India; being a natural candidate for whom commodity and oil constitutes sizeable imports. The empirical analysis carried out through Vector-Error Correction Model (VECM) for the post-liberalisation period 1991-2014 clearly points out that commodity and oil price shocks have a significant impact on the variation of output and prices accounting for real exchange rate adjustment as well as the role of a developed financial market (private credit). The real exchange rate adjusts to commodity and oil price shocks accounting for foreign exchange reserves and financial markets (private credit). The impulse response functions indicate that one standard deviation shock in commodity and oil prices persists for over three to eight quarters over domestic prices and output. While these results points out for lessening the commodity and oil imports through a series of medium- and long-term structural-cum-policy reform measures, in the immediate it also lends for a role of intervention by monetary authority (central bank) in pursuit of inflation targeting. Conjointly, pursuance of countercyclical fiscal policy to stabilize domestic output and prices in short run are called for.

**Keywords:** Commodity prices, oil price, output variation, real exchange rate, vector-error correction model, impulse response function, central bank intervention

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