

THE IMPACT OF PETROLEUM PRICES ON FOOD AND NON-ALCOHOLIC BEVERAGES PRICE INDEX IN SRI LANKA

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From an economic point of view, inflation is the process of continuous rising of price level of goods and services in an economy over a period of time in a country. In Sri Lanka, petroleum is an essential intermediate resource in the production process and it plays a significant role in the economy of the country. According to recent statistics, more than 40% of our country's gross income is being spent on fuel import, transportation and production of thermal power. However, impact of petroleum prices on prices of food and non-alcoholic beverages has not been studied after 2004. Therefore, this study has analysed the indirect impact of monthly oil prices on monthly food and non-alcoholic beverages prices during the period from 2008 to 2013. Price index of Food and nonalcoholic beverages was obtained as a subgroup of the Colombo Consumer Price Index (CCPI) which was published by the Department of Census and Statistics (DCS).

First difference of log transformation series was used to make the series stationary and make the variances more homogeneous. It was found that log oil prices does not Granger cause to log food and non-alcoholic beverages price index. Co-integration test confirmed that there is no long run permanent relationship between these two series. However, error correction model was used to determine the short run relationship between above two series. It was confirmed that about 0.1% of disequilibrium was corrected each month by changes in log of food and non-alcoholic beverages price index and about 36% of disequilibrium was corrected each month by changes in log of oil price. The results obtained in this study will be beneficial for various stakeholders in decision making. Furthermore, the methodology used in this study is recommended as an effective tool to measure the indirect impact of current changes in fuel prices on future inflation.