

SUMMARY

This study is an attempt to find empirical model to forecasting monthly inflation in Pakistan. A class of Box-Jenkins ARIMA models has been tried with and without explanatory variables. The sample is restricted to most recent observations. The best fitted model consists of AR and MA parameters together with real effective exchange rate (reer) and nominal effective exchange rate (neer) as explanatory variables. The forecasts have been made within the sample and out-side the sample. The forecasts are found reasonably accurate.

In Chapter 1, causes of inflation, determinants of inflation and measure to sustain inflation have been discussed. Historical review by computing average and standard deviation for different periods is discussed. To show the changes in food, non-food inflation and core inflation during different years, bar chart has been used. Different methods of computation of inflation rate and the use of CPI in computing different economic indicators are discussed as well.

In chapter 2, Literature Review is given. A number of studies have been made for forecasting inflation rate in different economies by applying different methodologies. The methodologies and conclusions drawn by different researchers have been discussed.

In Chapter 3, models identification, testing and validation have been discussed. Different statistics like Akaike Information Criteria (AIC), Schwarz Information Criteria (SIC), Theil Inequality Coefficient (TIC), Root Mean Square Error (RMSE) have briefly discussed.

In chapter 4, data analysis and interpretations has been given. Test of stationary has been applied at level and at first difference by consideration the possible log transformation as well. The results of different possible models and their validity have been stated. The best possible model by using explanatory variables and without explanatory variables has been stated.