

## **A Comparative Analysis of the Effects of Output and Inflation Volatility on Economic Growth**

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### **Abstract**

Historical data do not show the relationship between inflation and output the way it is highlighted by the Philips curve. However, the absence of such relationship notwithstanding, there is permanent volatility tradeoff between inflation and output. Since the late 1980s monetary policy has been putting more weight on price stability considering it as prerequisite for long run sustained economic growth. This also shows that policy makers assume output volatility to have lesser harmful effect on long run growth as compared to inflation volatility. However, there is no empirical evidence available in the literature on the validity of this assumption. Absence of such evidence motivates this study to estimate and compare the effects of inflation and output volatility on economic growth. Therefore, this study aims at estimating these effects using panel data spanning 1990 to 2020 for upper, middle and lower income countries. The categorization of countries is based on World Bank ranking while time period is selected on the basis of regime shift from economic growth to price stability. Fixed Effect Model has been used to estimate the effects of both volatilities on economic growth. The choice of model is based on time invariant characteristics of countries that must be controlled to make error term independent of the explanatory variables. The results show significant negative effect of output volatility on economic growth even after controlling the effect of inflation volatility. This evidence suggests policy makers to care about output volatility along with price stability to sustain long run growth.

**Keywords:** Output Volatility, Inflation Volatility, Economic Growth

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