# Analysis of the Factors that Influence the Inflation Rate in Sri Lanka

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**Abstract**: One of the main problems encountered by the people around the world is inflation and its effects. Not only Sri Lanka but also many well-developed countries are affected by the effects of inflation. In this study, the factors affecting the inflation rate in Sri Lanka were examined using the multiple linear regression approach. The main objective of the study was to investigate the most influential factor affecting the rate of inflation in Sri Lanka and to determine the relationship between the inflation rate and the identified factors. For this study, budget deficit, oil price, interest rate, exchange rate, and gross national income were considered as the explanatory variables, while the inflation rate was considered as the response variable. The data were obtained from Government Fiscal Operations, Macrotrends, and Trading Economics websites for the period from 1987 to 2021. In this research, a multiple linear regression model was fitted to identify the factors that affect the inflation rate in Sri Lanka. Additionally, the best subset regression method was employed to find the best subset multiple linear regression models. Based on the best subset of regression, the results have found that budget deficit, oil price, interest rate and gross national income have a significant effect on the inflation rate, while exchange rate does not have a significant effect on the inflation rate, budget deficit, oil price, interest rate and exchange rate have a positive correlation with the inflation rate, while gross national income has a negative correlation with the inflation rate.

**Keywords**: Budget deficit, Exchange rate, Inflation rate, Interest rate, Multiple linear regression, Oil price.

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