Indian Economy · GS - III

Food-price volatility poses a challenge to India's flexible inflation-targeting framework. Examine the limitations of monetary policy in controlling supply-driven inflation and suggest complementary measures.

EXAM YEAR	PAPER	SUBJECT
DAILY PRACTICE 13/11/2026	GS - III	Indian Economy

MARKS	WORD LIMIT
10	~150 words

Answer Hint

Flexible inflation targeting, CPI inflation, food-price volatility, demand-side and supply-side inflation, repo rate transmission, agricultural supply chains, buffer stocks, monetary-fiscal coordination.

Model Answer

Introduction

India follows a flexible inflation-targeting framework under which the RBI aims to maintain CPI inflation at 4%, with a tolerance band of 2%–6%. However, food-price shocks can complicate monetary management.

Limitations of Monetary Policy

- **Supply-side constraints:** Higher interest rates cannot directly increase agricultural production or correct weather-induced shortages.
- **Limited transmission:** Food-price increases may persist despite monetary tightening.
- **Growth trade-off:** Excessive tightening can raise borrowing costs, weaken investment and slow economic activity.
- **Expectations:** Persistent food inflation can influence wage demands and broader price-setting behaviour.

Complementary Measures

The government should improve agricultural storage, cold-chain infrastructure and transport networks to reduce post-harvest losses. Timely market intelligence, calibrated buffer-stock operations and predictable trade policies can moderate price volatility. Better irrigation, crop diversification and climate-resilient agriculture can strengthen long-term supply.

Monetary and fiscal authorities must coordinate while preserving the RBI's operational independence.

Conclusion

Monetary policy remains essential for anchoring inflation expectations, but food-price stability requires structural agricultural reforms and responsive supply management. A coordinated approach can protect purchasing power without imposing unnecessary costs on economic growth.

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