Indian Economy · GS - III

Examine how monetary tightening by the US Federal Reserve influences global commodity prices, capital flows and emerging market economies.

EXAM YEAR	PAPER	SUBJECT
DAILY PRACTICE 19/11/2026	GS - III	Indian Economy

MARKS	WORD LIMIT
15	~250 words

Answer Hint

Federal Reserve policy, interest rate differential, US dollar appreciation, Treasury yields, gold and commodity prices, capital outflows, exchange rate volatility, imported inflation, emerging market vulnerabilities, policy response.

Model Answer

Introduction

The monetary policy decisions of the US Federal Reserve have significant global consequences because the US dollar and American financial markets occupy a central position in the international financial system.

Transmission to Global Markets

- **Commodity prices:** Higher US interest rates and Treasury yields increase the opportunity cost of holding non-yielding assets such as gold, potentially depressing bullion prices.
- **Dollar appreciation:** Higher returns on dollar-denominated assets attract global capital, strengthening the dollar and putting downward pressure on dollar-priced commodities.
- **Capital flows:** Investors may shift funds from emerging markets towards relatively safer and higher-yielding US assets, causing capital outflows.
- **Exchange rate pressure:** Emerging market currencies may depreciate, increasing the cost of imports, particularly crude oil and essential commodities.

- **Financial stability:** Higher global borrowing costs can increase debt-servicing burdens and weaken investment.

Implications for India

India may face imported inflation, rupee depreciation and volatility in foreign portfolio investments. However, lower international gold and commodity prices can provide some relief to import costs.

Policy Response

India needs prudent monetary management, adequate foreign exchange reserves, diversified trade and investment partnerships, and strong macroeconomic fundamentals to manage external shocks.

Conclusion

US monetary tightening demonstrates the interconnectedness of global financial markets. Emerging economies must strengthen domestic resilience while maintaining flexibility to respond to international monetary developments.

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