Indian Economy · GS - III

Rising inflation often compels central banks to tighten monetary policy, but higher interest rates can also slow economic growth. Examine this trade-off in the Indian context, with reference to the Reserve Bank of India's inflation-targeting framework.

(150 words Marks: 10)

EXAM YEAR	PAPER	SUBJECT
Daily Practice 12/10/2026	GS - III	Indian Economy

MARKS	WORD LIMIT
10	~150 words

Answer Hint

Rising inflation erodes purchasing power and threatens stability, while rate hikes curb demand but raise borrowing costs. Supply-side measures and calibrated monetary tightening can balance inflation control and growth.

Model Answer

Inflation refers to a sustained increase in the general price level, which reduces the purchasing power of money. In India, the Reserve Bank of India (RBI) uses monetary policy to maintain price stability while keeping growth considerations in view.

The report warning that inflation could reach 7% highlights the risks posed by rising crude oil prices, food costs, currency depreciation and inflation expectations. If inflationary pressures persist, the RBI may increase the repo rate to make borrowing costlier, moderate credit growth and reduce excess demand.

However, monetary tightening involves a trade-off. Higher interest rates can increase EMIs, discourage private investment and consumption, and slow economic growth. Moreover, rate hikes may not immediately resolve

supply-side inflation caused by expensive oil or food shortages.

Therefore, India needs a balanced approach involving calibrated monetary tightening, improved food supply chains, strategic energy management and fiscal prudence. Coordination between monetary and supply-side policies is essential to control inflation without imposing excessive costs on growth and employment.

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