Daily Mains Practice Answer 9-09-2026

Q. What is Flexible Inflation Targeting (FIT)? Examine its effectiveness in maintaining price stability in India. (10 marks, 150 words)

Directions: Intro------Effectiveness in maintaining price stability + Limitations-----Conclusion.

Introduction:

Define Flexible Inflation Targeting (FIT).

India formally adopted FIT in 2016, with the RBI mandated to maintain CPI inflation at 4%, with a tolerance band of 2%–6%.

Main Body

Effectiveness in maintaining price stability

- Provides a clear nominal anchor – 4% target has made monetary policy more predictable, transparent and credible for price expectations.
- Inflation has moderated – India's formal inflation-targeting regime helped bring inflation down from high levels and also contributed to greater predictability in monetary policy.
- Inflation Expectations (Mixed Outcome) – FIT and the 4% target helped make inflation expectations more stable, especially before the pandemic, whereas Indian households often expect higher inflation than RBI forecasts.
- Balances inflation and growth – During economic downturns, FIT permits monetary easing rather than mechanically prioritising inflation; hence, it provides greater flexibility.
- Strengthens institutional accountability – The MPC's committee-based decision-making, inflation forecasts & failure-accountability mechanism improve transparency and credibility.
- Phillips Curve appears weak – Meaning higher interest rates may have limited impact on inflation.
- Tight monetary policy can reduce growth and employment without a proportionate fall in inflation. Thus, the inflation–growth trade-off is weak in India.
- Repo-rate transmission – Higher policy rates increase borrowing costs, discourage credit-financed consumption and investment, and reduce aggregate demand, which can subsequently moderate inflation.

Limitations

- Weak Phillips-curve relationship.
- Household inflation expectations remain elevated.
- Food and fuel shocks are largely supply-driven.
- Monetary-policy transmission has lags.
- Tight policy can impose growth/employment costs.

Conclusion:

Give a balanced conclusion and suggest some way-forward measures.