



KAMARAJ IAS ACADEMY
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INFLATION IN INDIA AND ITS IMPACTS ON INDIAN ECONOMY

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Introduction

Inflation refers to a sustained rise in the general price level of goods and services in an economy over a period of time, leading to a decline in the purchasing power of money.

In India, inflation is primarily measured through the Consumer Price Index (CPI), with the Reserve Bank of India (RBI) targeting an inflation band of $4\% \pm 2\%$ under the Flexible Inflation Targeting (FIT) framework.

Current scenario in India

Retail Inflation (CPI-Based)

- July 2025: India's annual retail inflation dropped to 1.55%, marking the lowest level since June 2017 and falling below the RBI's target range of 2–6%

Food Inflation (CFPI-Based)

- April 2025: Food inflation plunged to 1.78%, the lowest since October 2021. It sharply declined from 2.69% in March

Overall view

- Inflation has moderated significantly, with CPI dipping to multi-year lows and food price inflation showing marked easing.
- The downward trend is broad-based, affecting both rural and urban areas, backed by better supplies and favorable base effects.

Retail inflation in India slipped to 1.55% in July 2025, the lowest since June 2017, and below the Reserve Bank of India's comfort band of 2-6%, primarily led by a contraction in food prices.

Headline Inflation: Year-on-year inflation rate based on All India Consumer Price Index (CPI) for the month of July, 2025 over July, 2024 is 1.55% (Provisional). There is decline of 55 basis points in headline inflation of July, 2025 in comparison to June, 2025.

DEFINITION	CAUSES
Demand-Pull Inflation	
Occurs When Demand Is Greater Than Supply, Leading To Higher Prices	Increased Spending, Investment, or Government Expenditure
Cost-Push Inflation	
Results From Rising Production Costs, Leading To Higher Prices	Labor Strikes, Natural Disasters, or Geopolitical Events
Built-in Inflation	
Arises From Expected Price Increases, Causing Higher Prices and Wages	Historical Trends and Psychological Factors
Hyperinflation	
Extreme Inflation With Rapidly Accelerating Price Increases	Expansion of Money Supply or Loss of Confidence in Currency

Impacts of Inflation in the Indian Economy

1. Erosion of Purchasing Power

- Rising prices reduce the **real income of households**, especially the poor and middle class.
- *Example:* In **2023–24**, food inflation (tomatoes, onions, cereals) led to higher household expenditure burden, hitting rural families hardest.

2. Impact on Savings and Investment

- High inflation discourages savings (as **real returns** decline) and distorts investment decisions.
- *Example:* With CPI inflation averaging **5.4% in 2023**, small savings schemes (like PPF at ~7.1%) barely protected real returns after tax.

3. Wage–Price Spiral

- Workers demand higher wages to compensate for inflation, increasing production costs further.
- *Example:* Higher **MSP hikes and wage revisions in MGNREGA** added cost-push pressures in agriculture and services.

4. Impact on the Poor & Inequality

- Inflation is regressive—it hits the poor disproportionately as they spend more on essentials (food & fuel).
- *Example:* **Food inflation at 6–7% in early 2024** worsened nutritional insecurity among low-income groups despite NFSA subsidies.

5. Impact on Government Finances

- Moderate inflation helps reduce the **real burden of public debt**, but high inflation worsens fiscal deficit due to subsidies.
- *Example:* Rising **fertilizer and LPG subsidies (2023–24)** widened fiscal pressures.

6. Impact on Monetary Policy & RBI Mandate

- Persistent inflation forces RBI to tighten monetary policy, affecting growth.
- *Example:* In **2022–23**, RBI hiked repo rate cumulatively by **250 bps** to control CPI above 6%; but by **2025**, inflation fell to **1.55% (July 2025)**, below RBI's tolerance band, giving room for easing.

7. External Sector Impact

- Higher inflation reduces India's **export competitiveness** and may worsen **Current Account Deficit (CAD)**.
- *Example:* High domestic inflation in 2022–23 coupled with elevated crude oil prices widened India's CAD to **2% of GDP**.

8. Impact on Growth & Employment

- Very high inflation creates uncertainty, discourages investment, and slows growth (stagflation risk).
- *Example:* Post-COVID period (2021–22) saw **sluggish job recovery** despite high inflation, raising concerns of stagflation.

Measures that can be possibly taken to Control Inflation in the Economy

Inflation control requires a calibrated mix of monetary, fiscal, and supply-side policies. While RBI manages demand through monetary policy, the government must tackle structural and supply bottlenecks to ensure sustainable price stability.

1. Monetary Policy Measures (RBI)

- **Repo Rate Hikes / Tight Liquidity** - To reduce money supply and demand-pull inflation.
- **Cash Reserve Ratio (CRR) / Open Market Operations** - Absorb excess liquidity.
- **Inflation Targeting** - RBI operates under **4% ± 2% CPI band**; in **July 2025, inflation fell to 1.55%**, showing effective control.

2. Fiscal Policy Measures (Government)

- **Rationalising subsidies** to avoid fueling demand artificially.
- *Example:* Reduction in fertilizer subsidies in 2024–25 Budget to cut fiscal slippage.
- **Tax adjustments** on fuel, essential items to ease cost-push pressures.
- *Example:* Union Govt cut **excise duty on petrol & diesel (2022)** to reduce inflation.
- **Targeted cash transfers** instead of universal subsidies to avoid excess demand.

3. Supply-Side Management

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- **Buffer stock release** from FCI to cool food inflation.
- *Example:* Govt released wheat & rice under **Open Market Sale Scheme (OMSS) in 2023–24** to check cereal prices.
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- **Export restrictions** to stabilise domestic prices.
- *Example:* Ban on **non-basmati rice exports (July 2023)** to control domestic rice inflation.
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- **Imports liberalisation** for short supply items.
- *Example:* Duty-free imports of edible oils and pulses (2023–24).

4. Structural Measures

- **Agricultural reforms** ? Better storage, cold chains, and logistics to reduce wastage-driven inflation.
- **Energy diversification** ? Reducing dependence on imported crude oil (which fuels imported inflation).
- *Example:* Push for **biofuels and renewable energy** under National Green Hydrogen Mission (2023).
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- **Market reforms** ? Strengthening e-NAM, digital platforms for transparent price discovery.

5. Administrative & Regulatory Actions

- **Anti-hoarding & anti-profiteering laws** to prevent artificial scarcity.
- **Price monitoring cells** to track essential commodities.
- *Example:* **Department of Consumer Affairs (2023)** monitored onion and tomato prices daily to intervene quickly.
- **GST Council adjustments** ? Rationalising GST on essential items to avoid inflationary impact.

Conclusion

Inflation in India is not merely an economic statistic but a developmental challenge that directly affects household welfare, fiscal health, and macroeconomic stability. While moderate inflation is considered a sign of growth and helps reduce the real burden of debt, persistent high or volatile inflation undermines savings, widens inequality, and erodes public trust in institutions.

to ensure that inflation remains low, stable, and predictable, we should foster inclusive and sustainable economic growth.