Impact Of The Us Federal Reserve's Actions On The Indian Economy

---

Table of Contents

Abstract 2
Introduction 2
What is the Federal Reserve Bank? How does it function? 3
Historical analysis of Federal Reserve monetary policies 5
Effects of the Federal Reserve Bank's decisions on the developing economies over the years 7
India's monetary policy over the years 10
Impact of US Federal Reserve Decisions on Indian Economy 12
Conclusion 15
Recommendations 16
References 17

Abstract

The US Federal Reserve has hiked its interest thrice since the start of 2023. The Fed has indicated that it would continue to increase its interest rate to curb inflation. However, these aggressive interest rate hikes harm the Indian economy. This paper analyzes the nature of US Federal Reserve policies and recent developments. The paper also looks at the impact of the Fed policies on other developing countries and attempts to link it with the Indian economy. Finally, the paper analyzes the effects of the Federal Reserve's actions on the Indian economy from different dimensions and briefly looks at the way forward.

Introduction

The initial motive of any central bank is to achieve the critical goal of maintaining balance in the economy. The parameters that require attention while defining the monetary policy include stable prices, optimum level of employment (hypothetically, every country aims at achieving a cent percent employment), and a good proportion of investments in the economy. As it is generally known, the monetary policy of an economy is primarily determined by its central bank. Monetary policy is closely linked to maintaining price stability and keeping inflation under control. The monetary policy influences the exchange rates of an economy. [1] The value of an economy changes according to changes in the interest rate. Hence, a central bank framing a monetary policy does not limited to just the domestic economy itself. It has got its effect on the global setup as well. That is the reason there have been historical pieces of evidence of developing countries having the policy shocks of the changes in macro variables in developed countries. When the interest rates fluctuate, the aggregate demand changes and impacts the production of the firms and industries. More than that, it has an impact on the financial markets of the country, as people's expectations change accordingly, and they react to what we call a market trend. However, we are not arguing that it had only a negative impact. Policy changes in developed countries may also boost the market in developing economies. The reasons any central bank makes specific changes in the monetary policy

[1] https://www.imf.org/en/About/Factsheets/Sheets/2023/monetary-policy-and-central-banking

have been looked after in the first paragraph of the introduction. We must understand the critical difference between the monetary policy of developed and developing countries is the rate of growth they have to maintain. Developed countries have already achieved a specific growth rate, which essentially qualifies them as a developed economy. Hence, their job is to maintain a constant growth rate and keep inflation under control, not more than 2 %. In developing countries, there is always a trade-off between maintaining a high growth rate and controlling inflation simultaneously. This is why we find the inflation rate regularly adjusted to 4-5% in developing countries. The point of this statement is that there is always a paradoxical situation in framing monetary policies in developed and developing countries.

These features are commonly present not only in the policies formulated by the US Federal Reserve Bank and the Reserve Bank of India but also in the policies of most of the developed countries. The US Federal Bank considers the following motives while framing a particular monetary policy. First and foremost is to set an economic policy for the economy as a whole. The second being to take a brief account of regional economies and financial conditions and predict changes. The third and most important motive is to reach out to the public and convey the decision taken by the central bank. Considering the fact that the United States is a developed country, the Federal Reserve Bank has always tried to maintain a steady growth rate, keeping the inflation rate in control. The main aim of the Fed has been to control the price rise and its effects on the savings in the economy. This paper aims to analyze the impact of the Fed Reserve's actions on the Indian economy. At first, it is essential to understand the journey of the US Federal Reserve Bank and the history of decision-making in determining macroeconomic policies.[2]

What is the Federal Reserve Bank? How does it function?

Before the Fed Reserve was established, the United States had its central bank in 1791. It was much of a commercial bank performing the primary functions of accepting deposits and granting loans. The bank purchased securities and also issued bank notes. The fact that it was a

---

[2] https://www.newyorkfed.org/aboutthefed/history_article.html

nationwide bank and the governor was appointed by the government it could be considered the federal bank of the country. The bank failed to gain the trust of the people. Its existence came to an end with a margin of votes falling against renewing its charter in 1811. In 1816, a bill was passed to bring the charter of the second central bank of the US. The only difference was that it had more capital than the earlier central bank. The bank functioned for several years but did not have any federal regulations to operate with a central banking authority. National Banking Act passed in 1863 gave power to national charter banks to issue bank notes. The office of the controller of currency was set up. At the end of the 18th century, the second central bank, too, couldn't function properly as the American economic structure grew immensely and became more complex due to the growth of industries. There were constant fluctuations due to business cycles and rigid currency. Finally, in 1893, depression hit the economy, and the banking system collapsed.

At the start of the 19th century, 1913, the Federal Reserve Act was created, which provided for the establishment of a Federal Reserve Bank. Currently, the US Fed is the most powerful banking institution in the United States. [3]. The US Fed frames the country's monetary policy. The headquarters of the US Federal Reserve Bank are located in Washington, DC. The Fed operates in 12 US states. The power is shared by a seven-member board of governors, which is led by the Fed chairperson appointed by the president. The Fed has 12 regional bank presidents, of which five are included in the larger portion of the Fed Open Market Committee (FOMC). The Open Market Committee is responsible for adjusting the interest rates and controlling or expanding the money supply. The main reason for maintaining the interest rates is the 'dual mandate' set by the Fed. It aims at achieving stable prices and full employment. The Fed chairperson is the spokesperson or mediator who deals with Congress and the FOMC.

The Fed generally uses the following tools to control inflation. These include open market operations, discount rate, reserve requirements, and the federal funds rate.

---

[3] https://www.cfr.org/backgrounder/what-us-federal-reserve#:~:text=It%20is%20responsible%20for%20managing,purchases%20to%20boost%20financial%20markets

Open Market Operations [4]

The open market operations involve purchasing and selling government securities in the market by the country's central bank. Before the 2008 global financial crisis hit the US economy, these operations were used to balance out the Federal funds rate to adjust the money supply.

Discount Rate[5]

The Discount rate is the interest rate charged on the loans received by the commercial bank by the Regional Federal Reserve Bank. Usually, there are three types of loans offered. The primary, the secondary, and the seasonal credit. These loans are fully secured. The loans are lent at similar discount rates at all the regional reserved banks.

Reserve Requirements[6]

The reserve requirements are the amount of reserved cash banks need to keep with them. As authorized by the Federal Reserve Act, the board of members establishes specific ranges of reserve requirements to set up the monetary policy. It is laid on certain types of deposits and liabilities. The reserve amount is determined by applying reserve requirement ratios provided by the board rules.

Federal Funds Rate

The Federal funds rate is the interest rate at which the commercial banks lend and borrow their excess reserves from each other. The FOMC determines it by conducting meetings periodically. It influences short-term loans deposits of the customers.

We shall now look at a historical analysis of monetary policies designed by the Fed in the context of some important time frames ranging from the 1990s to 2018.

---

4 https://www.federalreserve.gov/monetarypolicy/openmarket.htm#:~:text=Open%20market%20operations%20(OMOs)%2D%2D,Open%20Market%20Committee%20(FOMC).

5 https://www.federalreserve.gov/monetarypolicy/discountrate.htm

6 https://www.federalreserve.gov/monetarypolicy/reservereq.htm

Historical analysis of Federal Reserve monetary policies

The actual recessionary period for the US economy was 1999 to 2009. In 1999, the Asian economies were hit by a wave of business cycles. It was the decade where the US exports were mainly towards the eastern countries.[7] The devaluation of currencies reduced demand for the products of the United States. As a result, there was a huge trade deficit in the economy.

Moreover, the devaluation meant that the Asian countries started producing their own goods and substituting them for exported commodities. Due to the fall in the value of other currencies, there was a rise in the dollar price compared to other currencies. These trade deficits naturally resulted in overproduction, putting the economy into recession. The unemployment rate was under control, but the number of new jobs created was reduced, and a more significant portion of them were in industries offering jobs with low wage rates. The first impact of global imbalance was on the financial sector of the U.S. economy. The profit levels of corporate stocks came down as risk-averse investors, both domestic and international, withdrew their investments.

Consequently, in 2000-2001, the Federal Reserve reduced the interest rate to tackle inflation and boost up the domestic demand.[8] In 2004, the interest rates were relatively lower; the idea was to make people spend more. The Fed consistently hiked the interest rates from 2004 to 2006 17 times. The sole motive of this move was to increase the consumption and domestic demand for the commodities so that unemployment could be reduced. On the contrary, it cut the interest rates to almost zero to rescue the economy from the 2008 economic crisis.

Below are the changes in interest rate and the target range of interest rate:

Year	Change in Interest Rate	Target Values
2001	-25 to -50 basis points	2-6%
2002	-50 basis points	1.25%
2003	-25 basis points	1%
2004	+25 basis points	1.25-2.25%

[7] https://assembly.state.ny.us/Reports/White99/EconReport/econreport.html
[8] https://www.cfr.org/media/60562/modal?anchor=timeline-60562

2005	+25 basis points	2.5-4.5%
2006	+25 basis points	4.5-5.25%
2007	-25 to -75 basis points	4.25-4.75%
2008	-100 to 75 basis points	0,0.25-1%

(Changes in federal Funds rate by Federal Reserve Bank between years 2001-2008[9])

The global financial crisis started with a fall in prices in the housing market of the US economy. The housing market took a massive turn from 2007 to 2008 prices. The sharp price fall failed in mortgage industries, which lent loans. A substantial amount of firms entered bankruptcy. The largest loan company in the US entered bankruptcy, which was the starting point of the global impact of the financial crisis. The financial markets of various countries were under tremendous stress till September 2008. The Federal Reserve Bank had the massive task of reviving the economy. The interest rates were at an all-time low, and the loans were lent at almost zero interest rates. The Fed opted for quantitative easing and announced extensive purchasing of the securities. In 2009, the United States government announced a stimulus package of $ 787 billion. The post-revival policies of the Fed for the decade 2011-2020 have been stringent in maintaining steady interest rates. The Fed kept interest rates at a lower value (near zero) till 2015. After that, they raised it by only 25 basis points per year until 2019, when the inflation was just above the margin. The Fed then announced a cut in the interest rates. The Fed was forced to cut its interest rates during the pandemic period, and the interest rates were lower until the last quarter of 2021. Since then, the Fed has increased its interest rates to curb inflation. These interest hikes are continuous and have taken more remarkable strides. The interest hike after the pandemic has been the highest-ever hike approved by the Fed since 2000.

[9] https://www.bankrate.com/banking/federal-reserve/history-of-federal-funds-rate/

Effects of the Federal Reserve Bank's decisions on the developing economies over the years

The former governor of the Reserve Bank of India, Mr. Raghuram Rajan, criticized the Fed's policies in 2014. He stated that the decisions taken by the Federal Reserve impact emerging markets and, thus, the motive behind the determination of policies and changing macroeconomic variables should be announced publicly. The decisions should also align with the changes in the outside world. The US Federal Reserve had historically low-interest rates on its road to economic recovery. This poured investments into emerging economies. But the time when the Fed decided to wind down its bond-buying program and hike the interest rates, the investors pulled out from the emerging economies. As a result, the markets in the developing economies suffered due to a change of interest rates by the central bank of a developed economy. The critical question that arises here is: do the financial decisions of a developed country affect the economic conditions in developing countries? There is enough to accept this doubt. Developing countries' markets are linked to developed countries' market conditions. We will begin with the global perspective and narrow it down to India. In the global context, there have been spillovers of Fed reserve policies. The US monetary policy affects the other emerging markets through capital inflows and the credit lent to these markets. These effects are often referred to as policy shocks. A hostile policy shock from the US economy leads to a credit boom in the other markets as the capital will flow towards these markets from the US economy. This leads to a banking or equity market crisis as the increased lending capacity reduces the credit quality. On the other hand, the favorable monetary policy could have positive spillovers to the emerging economies as they contract the excess quantity of credit being poured into the economy. However, if this contraction is sudden without prior intimation, the capital outflows can be quick, leading to a brief economic stoppage and a crisis.

The following table shows the capital outflows of developing countries

	Capital Flight[1] (1)	External Debt (2)	Ratio of Capital Flight to Total External Debt (1) ÷ (2)	External Claims[2] (3)	Ratio of Capital Flight to Total External Claims (1) ÷ (3)
1978	47.30	113.70	0.42	71.62	0.66
1979	64.14	141.76	0.45	92.17	0.70
1980	75.41	179.06	0.42	119.41	0.63
1981	85.16	224.26	0.38	134.16	0.63
1982	99.95	261.30	0.38	142.57	0.70
1983	123.77	285.70	0.43	164.13	0.75
1984	136.43	301.05	0.45	182.52	0.75
1985	147.54	311.60	0.47	199.70	0.74
1986	152.67	326.39	0.47	210.30	0.73
1987	180.62	349.75	0.52	233.73	0.77
1988	184.01	360.43	0.51	239.14	0.77

Sources: World Bank, *World Debt Tables*, various issues; International Monetary Fund, *Balance of Payments Yearbook*, various issues; and IMF staff estimates.

[1]Data refer to *net* capital flight, that is, the unrecorded stock of capital outflows less the unrecorded stock of capital inflows. For methodology used, see fn. 6 in text.

[2]The stock of external claims is defined as the net stock of recorded claims on nonresidents other than direct investment plus the net stock on unrecorded claims of residents.

(Source: IMF Report on Risk and Capital Flights in Developing Countries [10]).

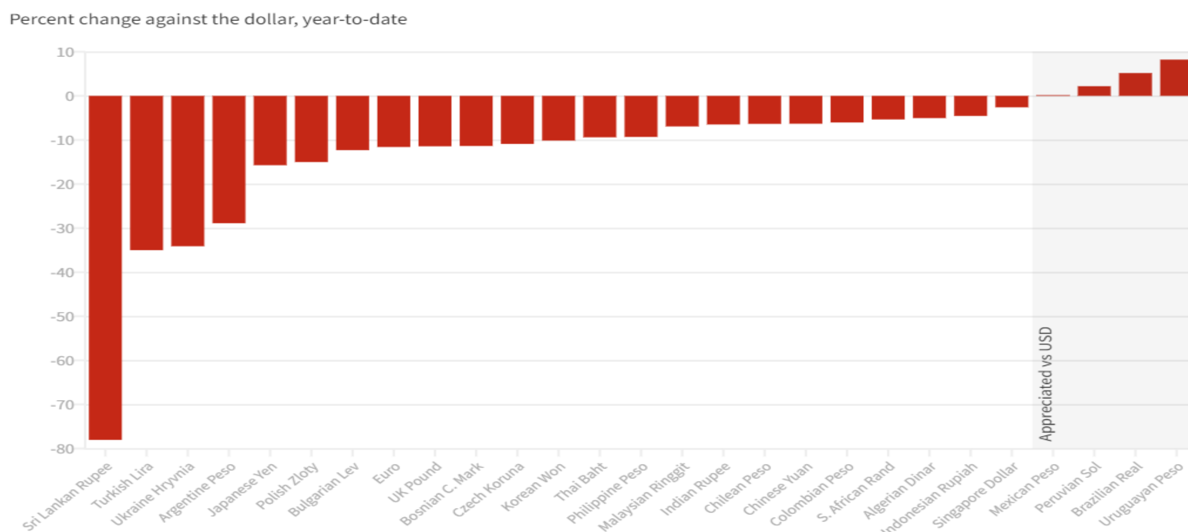
It can be noted from the above given time series data that the capital outflows of developing countries have risen after the 1975 oil price shocks. The prominent reasons behind this include:

1. The Macroeconomic policy changes in the other countries.
2. The number of foreign deposits and the dependency on foreign currency.
3. Less capital control in the domestic market.

The US monetary policy affects the financial sector in three ways: bank leverages, capital flows, and credit lent. It is evident from the studies that the countries with direct exposure or more significant liabilities to the US dollar tend to have more significant reactions to the policy changes in the US economy. Excess exposure to the dollar is a prominent reason for financial instability in the countries. Looking at the trade values over the years, we find that the exchange rate plays a significant role. As the developing economies are not price makers or deciders, they settle their transactions in dollars. Hence, a substantial dollar value against relatively weaker domestic currency restricts the economies from importing critical raw materials such as oil, metals, lubricants, etc. As a result, the stronger the dollar gets, the more the domestic currencies of developing countries

[10] https://www.elibrary.imf.org/display/book/9781557752055/ch04.xml

depreciate. This is why we observe the fall of some major currencies when the dollar's value rises. The following graph shows the percentage change of currencies against the US dollar.



(Percentage change of currencies of countries against dollar[11])

The above figure shows the percentage change of currencies concerning changes in the dollar value. It is visible that most of the developing countries' currencies have depreciated as the interest rates rose. The Fed Reserve's decision to aggressively raise interest has led to high demand for the dollar. Thus, the dollar has strengthened against the currencies of other countries. The other problem most developing countries face is maintaining a steady growth rate. To maintain foreign investments, they are compelled to raise the interest rates, but this will increase the cost of borrowing and hamper the production of the country. Now, we move to analyze India's monetary policy over the years.

India's monetary policy over the years

India's monetary policy has evolved from six to seven stages until now. In the initial phase of policy, pre-independence, India was under the Bretton Woods regime, where the Indian Rupee was first pegged to British sterling and then to the US dollar. However, the working of the Reserve Bank of

---

[11] https://blogs.worldbank.org/voices/three-ways-strong-dollar-impacts-emerging-markets#:~:text=Yes%2C%20imports%20are%20more%20expensive.of%20the%20issues%20detailed%20here.

India was started in 1935.[12] The RBI Act of 1934 provided the foundational principles or framework of the monetary policy. As mentioned above, the initial aim of the monetary policy was to maintain uniformity with the British currency sterling through open market operations. The bank rate and the cash reserve ratio were the helping tools used to hold the parity. The main concern was constant inflationary pressure due to the agricultural nature of the economy and frequent supply-side shocks to the economy.

From 1949 to the 1980s, the monetary policies were in sync with the five-year plans in the post-independence era. The economy moved towards a planned economic development, but it should be noted that the external forces had a more significant influence over the interest rates determined. Two decades post-independence saw excessive state control. The idea was to make the economy self-reliant. The decade of 1970 to 1980 was challenging with circumstances such as the war in 1971, oil price shocks, and the breaking of the Bretton Woods conference in 1979. The main issue was maintaining credit availability even under inflationary pressure. Constant inflationary pressure from the 1980s and budgetary deficit led to monetary policy tightening. After liberalization, the more significant focus of the policy was on stabilizing the economy and integrating the money market with other markets. The passing of the FRBM Act in the year 2003 brought a fiscal balance. A mix of policy instruments were used to maintain inflation and growth rate. The target value for inflation was 5.4%. The multi-disciplinary approach was a success to a greater extent, but it only lasted until the global economic crisis of 2007-08. The post-crisis period came with high inflation and low growth rates coupled with the challenges posed by the decision of the US Fed to stop purchasing the assets. The RBI decided to keep inflation at the center to curb these challenges. From peak inflation of 11% post-crisis to 6 to 5 % in 2016, the RBI successfully kept inflation in check. 2017 onwards, the inflation rate was kept flexible. While reviewing the monetary policy, the expert committee highlighted the importance of price stability while targeting higher growth. However, over the years, it must be noted that India's monetary policy has always been linked with global financial market developments. May it be the breaking of Bretton Woods,

[12] https://www.rbi.org.in/commonman/english/Scripts/speeches.aspx?Id=3161

which provided the base to set money supply as the factor for forming monetary policy. However, the lesson was soon learned during the 1990s economic crisis. Another prominent example is inflation-targeting monetary policies adopted by many developing countries around 1990 to 2000s, which took India 16 years to adopt. Still, in the meantime, India also used the multidisciplinary approach. From the above analysis, it can be understood that India matured quickly after the 2000s decade, particularly after the global financial crisis. The second important thing is the inflation-targeting policy design adopted shows the concurrent efforts taken by the RBI to manage the growth-stability tradeoff. It also signifies that India has kept learning through its mistakes. Now, we analyze the impact of changes in Fed Reserve rates on the Indian economy.

Impact of US Federal Reserve Decisions on Indian Economy

The impact of US Federal Reserve decisions on developing countries has been described above. India has faced similar issues against US Fed Reserve policies as any other emerging market. The impact is on mainly three types of markets: the Goods market, the money market, and the equity market. We will examine the money and equity markets first and then discuss the former. The table below shows values regarding currency value, exchange rate, inflation at consumer prices, and inflation according to the GDP deflator.

Year	Currency Value to USD	Official Exchange Rate Local currency to USD	Inflation (Consumer Prices) Annual % change	Inflation (GDP Deflator) Annual % change
2021	74.50	73.92	5.1	8.5
2022	80.36	78.60	6.7	8.3

(Source: World Bank Indicators[13])

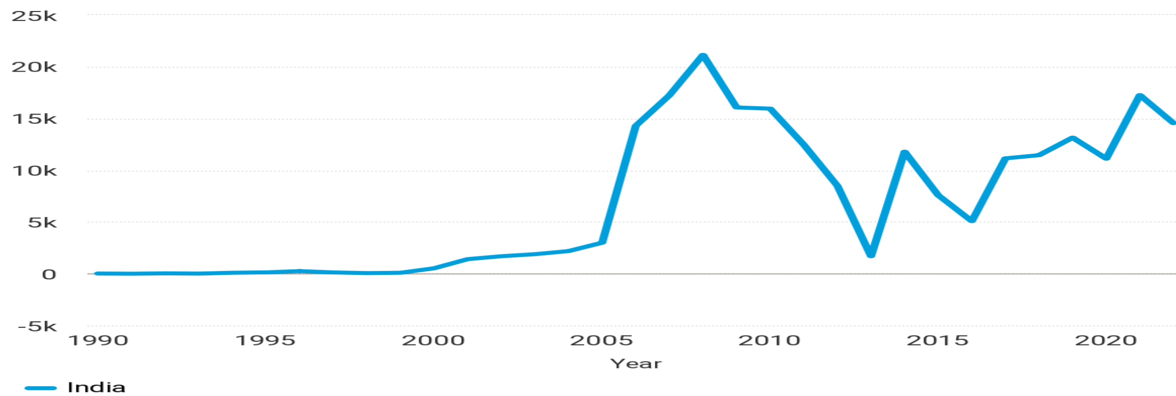
The difference in interest rate of US Fed Reserves has been positive since the first quarter of FY2022. The direct impact can be seen on the currency value of INR (Indian National Rupee) as the currency has depreciated compared to the US dollar. In 2021, the dollar accounted for INR 75.

[13] https://wdi.worldbank.org/table/4.16#

At the end of 2022, the Rupee slipped to INR 80, which further increased to 80.96, almost tending to ₹81. It is predicted that with further increased interest rates by the US Fed, the Indian Rupee is expected to fall by another ₹1. The depreciation in the currency consequently increases the exchange rate. The exchange rate has risen to ₹5 in just one year. Thus, this has affected the prices of consumer goods as the import cost increased with the increase in the exchange rate. The inflation has increased roughly by 1.5%. Hence, it can be seen that the impact of change in interest rates by the US Fed reserves directly affects the currency market of the Indian economy. A weaker rupee also makes the debt costlier for many companies taking credit from sources abroad. Repayment of domestic credits also gets costlier as the RBI hesitates to cut the interest rates to keep the attraction towards foreign investments. Thus, companies do not get any relief on the EMIs.

The Indian equity market has been highly reactive over the years[14]. Especially being a market in developing countries, it has shown more excellent responsiveness towards external economic actions. The Indian equity market has a history of higher reactivity towards the US Fed decisions. The depreciation in the Rupee has forward linkages here towards the returns on the investments in the Indian stock market. A comparatively weaker rupee reduces the returns on the investments. There is a large amount of capital outflows from the Indian markets due to these low returns. A hike in interest rates by US Fed reserves attracts investors over high treasury yields. On the contrary, the rate cuts will act in the favour of the Indian equity market.

[14] https://groww.in/blog/us-fed-rates-impact-on-indian-stock-market



(Capital outflows of India 1990-2022[15])

The above figure shows the capital outflows of India from the 90s to 2022. The chart shows the reactivity of the Indian stock market to the Fed reserve rates. In 2005, we can see a peak of outflows. 2006 to 2008 were the three years when the Fed increased the interest rates by 25 basis points. The total capital outflows after the 2008 global financial crisis were $21,142 million. After covid too, when the US Fed started raising interest in 2021, the Indian market saw a rise in capital flows from 11000 million dollars in 2020 to 17000 million dollars in 2021, a $6000 rise was seen in 9 months span. This capital outflow is not just about the Indian investors but also results in a large amount of dollar flight. Hence, this is a dual problem for India as it causes shaky markets. The interest rate cuts by the US Fed cause foreign portfolio investors to run towards emerging markets like India. This causes a flood of investments, but the moment the Fed starts raising its interest due to expectations of high returns, the investors drop out of the Indian market and invest their money into the US market in bulk. This also increases the volatility of the currency.

Regarding the goods market, the Fed rate hike raises the import costs. Thus, it results in costlier imports of electronic items such as laptops, televisions, washing machines, mobile phones, etc. Above all this, it makes the import of crude oil more expensive for India. Despite the crude oil

[15] https://unctad.org/publication/world-investment-report-2023

prices hitting a decade-low, the cost of oil shipments had recently increased, making the oil imports costlier. As the Fed raises its interest, other essential institutions raise interest rates to attract investors. More expensive imports lead to reduced production and curb the profitability of the industries in the Indian economy. Amidst this rise, there is a slowdown in the global demand. Hence, this reduces the enthusiasm for the export of commodities. The merchandise exports in India have fallen by 22.02% by the second quarter of 2023. The Department of Trade and Commerce has stated that the steep decline in exports was due to a fall in demand from large markets such as the US and Europe.

The external debt of India rises sharply after the Fed's interest rates increased. According to data released by the RBI, India's external debt increased by $4.7 million towards the end of the second quarter. The debt has a larger share from non-financial institutions. Hence, there is an effect on the overall health of the economy. The infant industries and start-ups lack sufficient funding or credit. The start-up community has seen a decline in credit in FY2023 subsequently.[16] Currently, there are over 100 unicorn companies in India. The foreign funding has reduced by $15 billion in FY2023—however, the banking sector benefits from the high interest rates of the US Fed. As the interest in the US rises, they can lend at higher rates and thus increase their income from the higher returns than expected.

Recommendations

To revive the economy from the negative impact of the US Fed reserve rates, the RBI and the government may consider taking some essential steps.

1. Payment in rupees in international trade is a game changer for the Indian economy. Payment in the Indian rupee will not only reduce India's dependence on the US dollar but also increase the demand for rupees globally. This means the Indian currency will appreciate against the US dollar. Currently, India is trading in the rupee with 31 countries. In the

[16] https://timesofindia.indiatimes.com/business/startups/companies/indian-startups-faced-70-drop-in-funding-in-fy23-to-15-billion/articleshow/101853177.cms?from=mdr

future, India can look to expand repayment in rupees to some of the larger economies in the world.

2. The RBI may also look at diversifying the holding of other foreign currencies to reduce dependence on the dollar. It can hold more proportions of the Yen, Euro, etc.
3. The Reserve Bank of India can focus on domestic credit growth to reduce external debt. It can frame policies to avail credit at lower rates to producers. RBI could also consider increasing domestic consumption in response to the Fed rate hikes by introducing subsidies or tax reductions.
4. As a long-run measure, it is recommended that the government could reduce its dependence on crude oil and focus on renewable energy sources. The government has taken positive steps, launching the first hydrogen-based electronic vehicle.

Conclusion

The Indian economy is one of the fastest-growing economies in the world. India has achieved export-led growth in the past decade, and the overall movement of raw materials across the country has led to more outstanding production of goods and services in the economy. India's exports have shown immense growth in recent years. After the 1991 economic crisis, the Indian markets have stabilized, and the Indian rupee has been relatively less volatile. During the 2007-2008 global recession, the Indian market somewhat stabilized and could maintain the demand. Historically, India has been highly responsive to external changes. India, being a developing country, has had an impact on developed markets on its macroeconomic policies. In this paper, we have analyzed the impact of one such major developed economy on India and other developed economies. A famous saying is that 'when America sneezes, the world catches cold.' The world's largest economy, the United States, has significantly influenced several developing and developed economies and financial markets. The US Federal Reserve Bank uses a set of policies to maintain economic stability and a constant growth rate. There have been periodic shifts in interest rates by the Fed. These rate cuts or rate hikes impact developing economies in the short term. The impact is on three fronts: the currency, the financial, and the goods markets. The currency depreciates as the US hikes interest

rates and the exchange rate increases. The higher import cost raises inflation at consumer prices and affects the import of raw materials, consequently reducing the country's production. Regarding the financial market, we experience capital flights due to the investors' expectations. This reduces FDI and FII in the economy. The goods market faces a shortage of demand and, hence, a reduction in exports. However, the banking sector of developing economies experiences higher revenues due to lending at greater rates. The impact of the Fed interest rates is not all negative for India in the long term; when other central banks increase their rates to keep up with the Fed Reserve, the global demand for crude oil will come down due to low production. India, on the other hand, is looking to expand its production. Hence, it is predicted that India can import crude oil at a cheaper rate in FY2024. RBI has also maintained a steady repo rate, which it can reduce once the Fed stops aggressively increasing interest rates. This will release the inflationary pressure. The global demand for rupee will play a significant role in India's response to the Fed rate hikes.

References

1. McGrane, V. 2014, Indian Central Banker Raghuram Rajan Criticizes Fed; Bank Chief Says Fed Ignores Impact of Its Low Interest Rates on Emerging Markets, New York, N.Y.

2. McKinnon, R. 2015, "Hot Money Flows, Cycles in Primary Commodity Prices, and Financial Control in Developing Countries 1", Frontiers of Economics in China, vol. 10, no. 2, pp. 201-223.

3. Mohan, R. (2009). Working Paper No. 407 Global Financial Crisis: Causes, Impact, Policy Responses and Lessons. [online] Available at: https://kingcenter.stanford.edu/sites/g/files/sbiybj16611/files/media/file/407wp_0.pdf.

4. https://econ.msu.edu/repec/wp/ism_oct2018.pdf

5. https://www.sciencedirect.com/science/article/pii/S2214845014000167

6. https://www.federalreservehistory.org/essays/federal-reserve-history

7. Stefan Avdjiev & Valentina Bruno & Catherine Koch & Hyun Song Shin, 2019. "The Dollar Exchange Rate as a Global Risk Factor: Evidence from Investment," IMF Economic Review, Palgrave Macmillan; International Monetary Fund, vol. 67(1), pages 151-173, March.

8. https://www.bankrate.com/banking/federal-reserve/history-of-federal-funds-rate/

9. https://www.vox.com/2014/6/20/18079946/fed-vs-crisis

10. Paul, Biru Paksha. “GLOBALIZATION AND MONETARY-POLICY INDEPENDENCE IN INDIA.” The Journal of Developing Areas 46, no. 2 (2012): 205–11. http://www.jstor.org/stable/23215370.

11. Durdu, Ceyhun Bora and Martin, Alex and Zer, Ilknur, The Role of U.S. Monetary Policy in Global Banking Crises (May, 2019). FEDS Working Paper No. 2019-39, Available at SSRN: https://ssrn.com/abstract=3423245 or http://dx.doi.org/10.17016/FEDS.2019.039

12. Sawhney, Bansi & Kulkarni, Kishore & Cachanosky, Nicolas. (2017). Monetary Policy in India and the U.S.: Is the Taylor Rule Irrelevant? International Review of Business and Economics (IRBE). 1. 75-107.

13. https://www.imf.org/external/np/exr/ib/2000/062600.htm#II

14. https://www.ncbi.nlm.nih.gov/pmc/articles/PMC7309432/