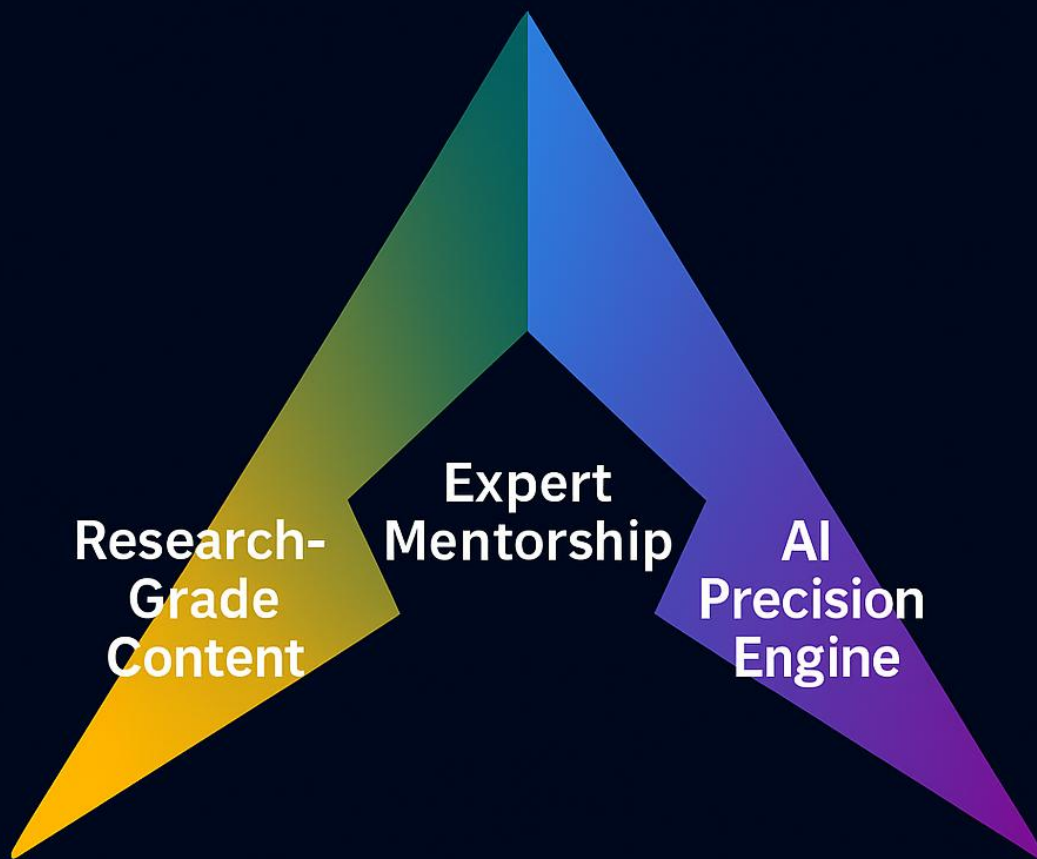


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GS Paper III: Economics

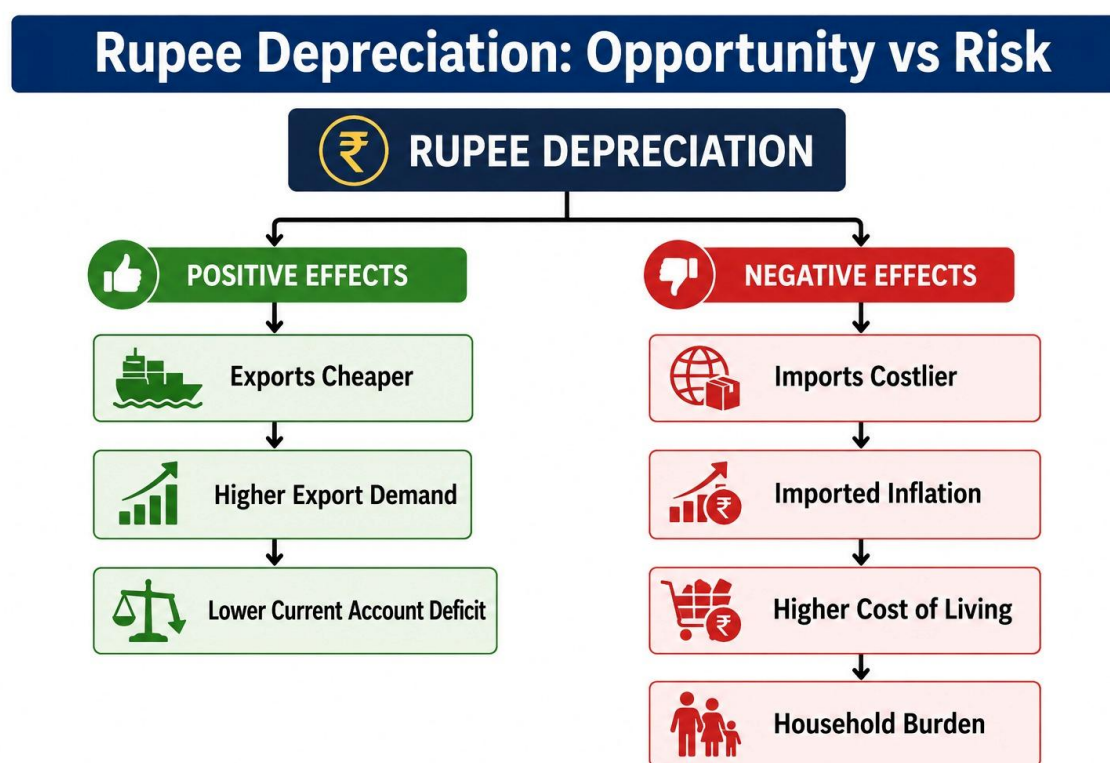
1. Rupee Depreciation and RBI Intervention

a. Introduction

The sustained depreciation of the Indian rupee, with the currency closing near 97 rupees per US dollar, has revived an important debate in India's external sector management. The central question is whether the Reserve Bank of India should allow the rupee to find its own market-determined level or intervene to prevent further decline.

This issue is significant because the exchange rate is not merely a financial market variable. It influences inflation, exports, imports, investor confidence, external debt, foreign exchange reserves and overall macroeconomic stability. Therefore, rupee depreciation must be understood not only as a currency movement, but also as a reflection of India's external sector vulnerabilities and policy choices.

This makes the issue important for understanding how India balances market-based adjustment with the need for macroeconomic stability.



b. Conceptual Background

- **Meaning of Rupee Depreciation:** Rupee depreciation refers to a fall in the value of the rupee against the US dollar. When the rupee depreciates, more rupees are required to buy one dollar. For example, if the exchange rate moves from 90 rupees per dollar to 97 rupees per dollar, the rupee has weakened.
- **Current Account Deficit:** A current account deficit occurs when a country's import payments exceed its export earnings and other current receipts. In such a situation, depreciation can theoretically help by making exports cheaper for foreign buyers and imports costlier for domestic consumers.

- **Capital Outflows:** Capital outflows refer to the withdrawal of foreign investment from the domestic economy. These outflows may occur due to higher returns abroad, global risk aversion, domestic uncertainty or expectations of further currency depreciation.
- **Imported Inflation:** Imported inflation occurs when costlier imports raise domestic prices. This is especially important for India because the country depends on imports for crude oil, fertilisers, edible oils, electronic components and several intermediate goods.
- **RBI Intervention:** RBI intervention refers to the use of policy tools, including foreign exchange reserves, to reduce excessive instability in the currency market. The purpose is not necessarily to defend a specific exchange rate, but to prevent sharp and disorderly movements.

These concepts provide the foundation for understanding why rupee depreciation can have both corrective and destabilising effects.

c. Why Depreciation Is Not Always Negative

- **Corrective Role of Depreciation**
A weaker rupee is not automatically harmful. In theory, depreciation can help correct external imbalances. When the rupee weakens, Indian goods become cheaper for foreign buyers, which can support exports. At the same time, imports become more expensive, which may reduce import demand. Together, these effects can help narrow the current account deficit.
- **Argument for Market-Based Adjustment**
This is the main argument in favour of allowing the rupee to find its market-determined level. If the exchange rate is artificially supported for too long, it may hide underlying weaknesses in the external sector and delay necessary adjustment.
- **Natural Adjustment Process**
Therefore, some degree of depreciation can be part of a natural correction process, especially when it reflects trade fundamentals and broader balance of payments pressures.

However, this positive role of depreciation holds mainly when the movement is gradual and aligned with fundamentals. The situation becomes more serious when depreciation is sharp, continuous or driven by speculative pressures.

d. Why Sharp Depreciation Can Be Risky

- **Risk of Currency Instability**
The problem arises when depreciation is sharp, continuous or driven by speculative capital outflows rather than trade fundamentals. In such a situation, currency movement may create instability instead of adjustment.
- **Self-Reinforcing Cycle**
If investors expect the rupee to fall further, they may withdraw more funds from Indian markets. Such withdrawals increase demand for dollars, which weakens the rupee further. This can create a self-reinforcing cycle of depreciation and capital outflows.
- **Difference Between Weak Rupee and Falling Rupee**
There is an important difference between a weak rupee and a falling rupee. A weak but stable rupee may support exports. In contrast, a continuously falling rupee can increase uncertainty. Foreign buyers may delay purchases if they expect Indian prices to become cheaper later. Indian importers may rush to buy dollars in advance, fearing further depreciation. This can increase pressure on the currency market.

Thus, the real policy concern is not depreciation itself, but disorderly depreciation that damages confidence and creates macroeconomic instability.

e. Impact on Inflation and Households

- **Imported Inflation Channel**

Rupee depreciation can worsen inflation through the import channel. India imports a large share of its crude oil requirement. It also depends on imports for fertilisers, edible oils, electronic components and several industrial inputs. When the rupee weakens, these imports become costlier in domestic currency terms.

- **Impact on Production and Essential Goods**

Higher import costs raise transport, production and distribution expenses across the economy. Costlier crude oil can affect fuel prices, freight costs and the prices of many essential goods. Costlier fertilisers can increase agricultural production costs. Costlier intermediate goods can affect manufacturing competitiveness.

- **Unequal Social Burden**

The burden of imported inflation is socially unequal. Poorer households spend a larger share of their income on essentials such as food, fuel, transport and basic services. Therefore, a sharp fall in the rupee can indirectly hurt low-income groups more severely.

This shows that exchange rate management is not only a financial sector issue. It also has direct implications for household welfare, inflation control and inclusive growth.

f. External Sector and Capital Flow Concerns

- **Dependence on Volatile Portfolio Flows**

The rupee's depreciation also raises a larger concern about India's dependence on volatile foreign portfolio investment. Foreign portfolio flows can enter and exit quickly depending on global interest rates, risk appetite and investor sentiment. If domestic financial stability depends heavily on such short-term flows, the exchange rate becomes vulnerable to external shocks.

- **Impact of Global Financial Conditions**

For example, when interest rates rise in advanced economies or when global investors become risk-averse, funds may move out of emerging markets. This can weaken emerging market currencies, including the rupee. Such pressures may not always reflect India's domestic fundamentals, but they can still affect India's currency, reserves and financial markets.

- **Need for Stable Capital**

This highlights the need to attract more stable forms of capital, especially foreign direct investment, long-term infrastructure finance and patient capital linked to manufacturing and technology.

Therefore, exchange rate stability depends not only on RBI intervention, but also on the quality and durability of capital inflows.

g. Limits of RBI Intervention

- **Role of RBI:** The Reserve Bank of India has an important role in preventing excessive volatility. However, intervention has limits. If the RBI sells too many dollars from its foreign exchange reserves to defend the rupee, reserves may decline. This can reduce India's external buffer and affect market confidence.
- **Risk of Artificial Support:** Artificially supporting the rupee for too long can also delay necessary external sector adjustment. If the exchange rate does not reflect underlying economic conditions, imports may remain artificially cheap and exports may lose competitiveness.
- **Correct Objective of Intervention:** Therefore, the objective should not be to defend a particular exchange rate level. The better approach is to prevent disorderly depreciation, reduce speculative volatility and maintain confidence in macroeconomic stability.

This makes RBI intervention useful as a stabilising tool, but not as a substitute for deeper external sector reforms.

h. Policy Balance Required

- **Need for Balanced Exchange Rate Strategy:** India needs a balanced exchange rate strategy. The rupee should be allowed to adjust to genuine market conditions, but excessive volatility must be managed. This balance is essential because both extremes are risky.
- **Risks of Both Extremes:** A rigidly defended rupee can exhaust foreign exchange reserves and weaken export competitiveness. On the other hand, unchecked depreciation can create inflationary pressure, capital market instability and external debt concerns.
- **Role of RBI and Government:** The RBI's role, therefore, is to smooth volatility, prevent panic and ensure orderly market functioning. At the same time, the government must address structural weaknesses through export promotion, import diversification and stronger domestic production capacity.

Thus, the exchange rate question requires coordination between monetary management, fiscal policy, trade strategy and industrial policy.

i. Way Forward

- **Prevent Disorderly Movements, Not Defend a Fixed Level:** The RBI should continue to intervene when currency movements become disorderly, but it should avoid defending an artificial exchange rate level. Intervention must aim at reducing excessive volatility rather than fixing the rupee at a politically convenient number.
- **Strengthen Export Competitiveness:** India must strengthen export competitiveness through better logistics, trade facilitation, lower transaction costs, quality infrastructure and production-linked manufacturing. A weaker rupee alone cannot boost exports unless domestic firms are globally competitive.
- **Reduce Essential Import Dependence:** The country should reduce dependence on essential imports by diversifying energy sources, promoting renewable energy, building strategic reserves and encouraging domestic capacity in critical sectors such as electronics, fertilisers and industrial inputs.
- **Encourage Stable Capital Inflows:** India should also encourage stable capital inflows, especially foreign direct investment, instead of relying excessively on short-term portfolio flows. Stable investment linked to manufacturing, infrastructure and technology is less vulnerable to sudden withdrawal.
- **Coordinate Monetary, Fiscal and Trade Policies:** Monetary, fiscal and trade policies must be coordinated to contain imported inflation. For example, fiscal measures can cushion vulnerable households, while trade policy can ensure adequate supply of essential commodities.
- **Maintain Strong External Buffers:** Finally, India must maintain strong external buffers through adequate foreign exchange reserves, prudent external borrowing and careful monitoring of short-term debt obligations.

A durable solution therefore requires not only currency market intervention, but also structural strengthening of India's external sector.

Conclusion

The rupee should not be rigidly defended at any specific level, because exchange rate adjustment is a normal part of external sector management. However, unchecked depreciation can create inflationary pressure, financial instability and loss of investor confidence.

A balanced approach is therefore necessary. India should allow market-based adjustment while using RBI intervention to prevent speculative volatility and disorderly currency movements. In the long run, exchange rate stability will depend not only on RBI action, but also on export competitiveness, stable capital inflows, lower import dependence and strong macroeconomic fundamentals.

Thus, India's exchange rate policy must combine flexibility with stability, allowing the rupee to adjust while preventing panic-driven and self-reinforcing depreciation.

GS Paper III: Environment

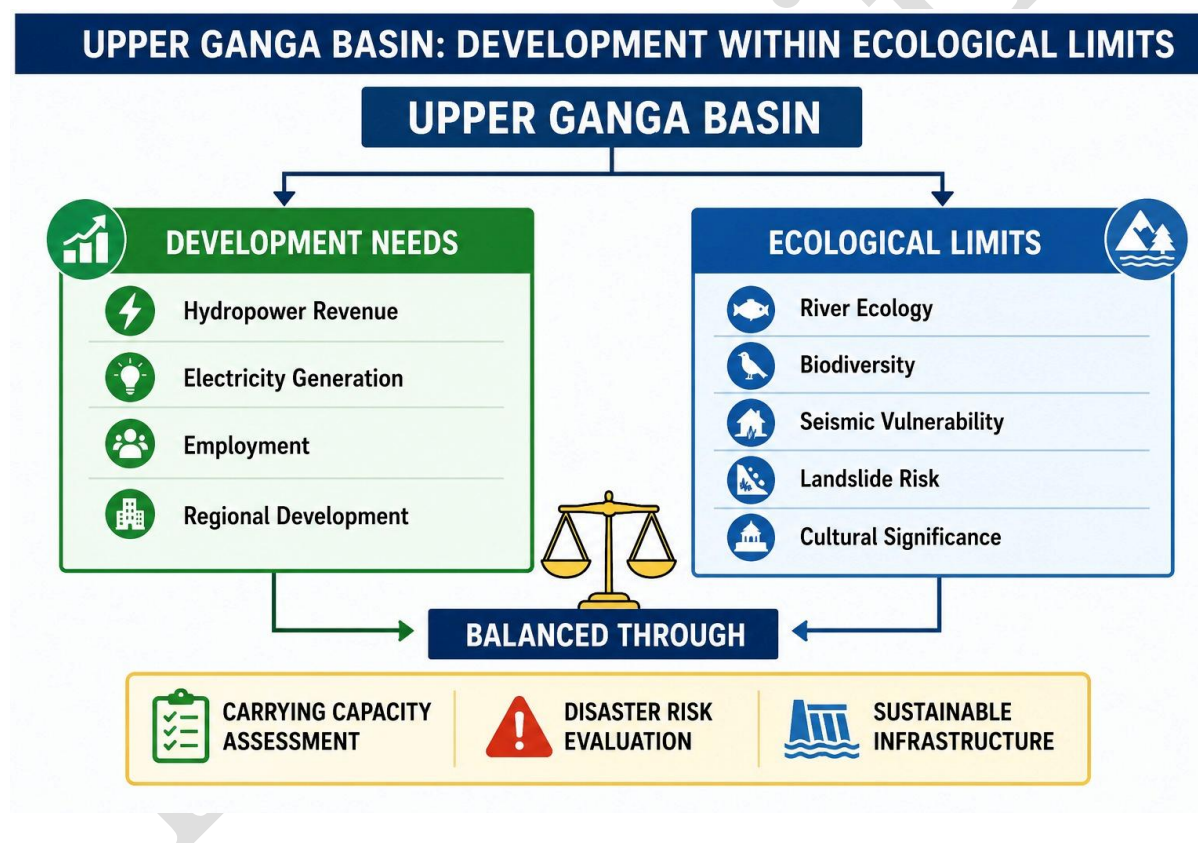
2. No New Hydroelectric Projects in the Upper Ganga Basin

a. Introduction

The Union Government has informed the Supreme Court that it is not in favour of new hydroelectric projects on the Alaknanda and Bhagirathi rivers, the two headwater streams of the Ganga. This position is significant because it comes after more than a decade of debate on hydropower development in Uttarakhand, especially after the 2013 Kedarnath disaster exposed the ecological and disaster-related vulnerabilities of the Himalayan region.

The issue is not merely about hydropower generation. It concerns the larger question of how development should be planned in fragile mountain ecosystems where rivers, glaciers, slopes, forests, settlements and cultural landscapes are closely interconnected. The upper Ganga basin is ecologically sensitive, geologically unstable, culturally sacred and hydrologically important. Therefore, infrastructure planning in this region requires a cautious and science-based approach.

This makes the issue important not only for environmental protection, but also for understanding sustainable infrastructure planning in the Himalayas.



b. Background of the Issue

- **Post-2013 Judicial Scrutiny**
After the 2013 Kedarnath disaster, the Supreme Court directed scrutiny of existing and proposed hydroelectric projects in Uttarakhand. Environmental and forest clearances for new projects were frozen, and expert bodies were asked to examine whether such projects could aggravate disaster risks and ecological damage.
- **Expert Committee Findings**
The Ravi Chopra Expert Body concluded that most proposed hydroelectric projects would adversely affect biodiversity in the upper Ganga basin. Later expert committees examined wider concerns such as cumulative impact, carrying capacity, glacial movement, seismic vulnerability and socio-economic consequences.
- **Upper Ganga Basin as Sui Generis**

The Union Government has now argued that the upper Ganga basin is *sui generis*, meaning that it is one of a kind. This description reflects the basin's unique combination of biodiversity, geological fragility, cultural significance and hydrological importance.

- **Recent Himalayan Disasters**

Recent events such as the 2021 Rishi Ganga floods, Joshimath land subsidence and Dharali landslide have further strengthened concerns about the vulnerability of the Himalayan region. These disasters show that infrastructure decisions in the Himalayas cannot be treated as routine project approvals.

This background shows a clear evolution from project clearance debates to a larger concern about the ecological limits of infrastructure in the Himalayas.

c. From Project-Wise Clearance to Cumulative Risk Assessment

- **Need for Basin-Level Thinking**

The government's position reflects a shift from isolated project-wise clearance towards a broader cumulative ecological risk approach. In fragile mountain regions, the impact of a dam cannot be assessed only by examining that individual project. The combined effect of multiple dams, tunnels, roads, blasting operations and river diversions on the same river basin may be far more serious than the impact of any single project.

- **Ecological Impact of Hydroelectric Projects**

Hydroelectric projects can alter natural river flow, affect sediment transport, disturb aquatic biodiversity and change downstream ecological processes. When several projects are located in the same basin, long stretches of a river may become fragmented or diverted through tunnels. This can weaken the ecological character of the river and affect both local communities and downstream users.

- **Importance of Carrying Capacity**

Therefore, a basin-level approach is essential. It allows policymakers to examine whether the river system as a whole can bear additional infrastructure pressure without crossing ecological and disaster-risk thresholds.

Such an approach is especially important in the Himalayas, where ecological damage and disaster risks are closely linked.

d. Himalayan Fragility and Disaster Risk

- **Geological Vulnerability of the Himalayas**

The Himalayas are young fold mountains. This means that they are geologically young, tectonically active and still undergoing structural changes. Such mountains are naturally prone to landslides, earthquakes, slope instability and erosion. Climate change has added another layer of vulnerability by accelerating glacial melt, increasing the risk of glacial lake outburst floods and intensifying extreme rainfall events.

- **Infrastructure-Induced Risks**

In this context, conventional infrastructure models may not be suitable for the Himalayan region. Tunnelling, blasting, slope cutting, muck dumping, road widening and river diversion can disturb already fragile slopes. These activities may increase landslide risk, weaken drainage patterns and make settlements more vulnerable.

- **Lessons from Recent Disasters**

The 2021 Rishi Ganga floods demonstrated how sudden high-energy flood events can damage hydropower infrastructure and create severe downstream risks. Similarly, the 2023 Sikkim glacial lake outburst flood showed that upstream vulnerabilities in mountain regions can produce devastating downstream consequences. These events underline the need to integrate climate science, glaciology, seismic studies and disaster-risk assessment into every major infrastructure decision.

Therefore, Himalayan infrastructure must be planned as a risk-sensitive exercise rather than as a routine engineering project.

e. Development and Environment Dilemma

- **Development Needs of Himalayan States**

The debate also reflects the development and environment dilemma faced by Himalayan states. Uttarakhand seeks hydropower for revenue, electricity generation, employment and local development. For a mountain state with limited industrial options, hydropower appears to offer an important economic opportunity.

- **Wider Ecosystem Services**

However, ecological limits cannot be ignored. The Himalayan region provides ecosystem services that extend far beyond state boundaries. Its rivers support agriculture, drinking water, biodiversity, cultural practices and downstream economies across the Gangetic plains. Damage to these systems can impose costs that are far greater than the immediate benefits of electricity generation.

- **Appropriate Development Model**

The central question, therefore, is not whether development should stop. Rather, the question is what kind of development is appropriate for fragile Himalayan landscapes. Development in such regions must be guided by carrying capacity, disaster risk, ecological sensitivity and long-term sustainability.

This reframes the debate from “development versus environment” to “development according to ecological limits.”

f. Hydropower as Clean Energy: A Qualified Argument

- **Renewable Energy Value of Hydropower**

Hydropower is often described as a clean and renewable source of energy because it does not produce emissions in the same manner as fossil fuel-based power generation. However, in ecologically sensitive regions, hydropower can carry serious environmental and social costs.

- **Environmental and Social Costs**

Large hydroelectric projects may involve extensive tunnelling, blasting, road construction, forest diversion, slope cutting and changes in river flow. These interventions can affect biodiversity, fish movement, sediment transport, local water sources and the stability of mountain slopes. In some cases, local communities may face displacement, livelihood disruption and increased exposure to disaster risk.

- **Location-Specific Sustainability**

Thus, hydropower cannot be treated as automatically sustainable. Its environmental value depends on location, scale, design, cumulative impact and disaster-risk profile. In fragile Himalayan basins, even renewable energy projects must be examined through the lens of ecological limits.

This qualified understanding is essential because clean energy transitions must not reproduce new forms of ecological damage.

g. Role of Judiciary and Expert-Based Governance

- **Judicial Oversight**

The issue also highlights the importance of judicial intervention in environmental governance. The Supreme Court’s involvement ensured that concerns related to carrying capacity, biodiversity, river ecology and disaster risk were considered before further clearances were granted.

- **Institutional Weaknesses**

At the same time, the long sequence of committees and differing institutional opinions also reveal weaknesses in India’s environmental decision-making system. There is often a lack of clarity between the objectives of power generation, environmental protection, water resource management and disaster-risk reduction. This results in delays, uncertainty and fragmented governance.

- **Need for Risk-Informed Planning**

A stronger institutional framework is needed, where expert assessments are independent, transparent and binding in ecologically sensitive zones. Environmental governance must move from clearance-based decision-making to risk-informed planning.

This shows that the future of Himalayan development depends as much on institutional reform as on individual project decisions.

h. Way Forward

- **Adopt Basin-Level Cumulative Impact Assessment:** India should adopt a basin-level cumulative impact assessment for all major infrastructure projects in the Himalayan region. Such an assessment must examine the combined impact of dams, tunnels, roads, townships, tourism pressure and climate-related hazards on the entire river basin.
- **Declare No-Go Zones in Fragile Stretches:** Highly fragile stretches of Himalayan rivers should be declared no-go zones for large hydropower projects. This does not mean opposing all development, but recognising that some areas are too ecologically sensitive for high-impact infrastructure.
- **Strengthen Environmental Flow Norms:** Environmental flow norms must be strengthened to preserve river ecology and downstream livelihoods. Rivers should not be reduced merely to channels for power generation. Their ecological, cultural and hydrological functions must be protected.
- **Integrate Disaster-Risk Assessment:** All infrastructure planning in the Himalayas should integrate the risk of glacial lake outburst floods, seismic vulnerability, landslide susceptibility and extreme rainfall. Disaster-risk assessment should become a mandatory part of project design, approval and monitoring.
- **Promote Alternative Development Models:** Himalayan states also need alternative development models. These may include eco-tourism, decentralised renewable energy, payment for ecosystem services, climate-resilient agriculture, sustainable pilgrimage management and livelihood diversification. Such models can support local development without imposing excessive ecological stress.
- **Improve Institutional Coordination:** Finally, coordination must improve among institutions dealing with environment, power, water resources, roads, urban development and disaster management. Fragmented decision-making is especially dangerous in fragile ecosystems where one sector's project may increase another sector's risk.

A sustainable way forward must therefore combine ecological protection, livelihood security, disaster-risk reduction and institutional coordination.

Conclusion

The decision to oppose new hydroelectric projects in the upper Ganga basin underlines an important principle: clean energy cannot be pursued by ignoring ecological limits. In fragile Himalayan regions, development must be guided by carrying capacity, river ecology, seismic vulnerability and disaster risk.

A balanced approach requires protecting sensitive river basins while also supporting Himalayan states through safer and sustainable livelihood alternatives. The upper Ganga basin should therefore be seen not merely as a site for infrastructure, but as a living ecological and cultural system whose protection is essential for long-term environmental security.

In this sense, the issue represents a wider shift towards ecological prudence in Himalayan development planning.

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