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MONETARY POLICY AND RESERVE BANK OF INDIA

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ABSTRACT

Monetary Policy is the process by which the monetary authority of a country controls the supply of money, often targeting an inflation rate or interest rate to ensure price stability and general trust in the currency.
Monetary policy is the macro economic policy laid down by the central bank. It involves management of money supply and interest rate and is the demand side economic policy used by the Government of a country to achieve macro economic objectives like inflation, consumption, growth and liquidity.
The monetary policy of RBI is not merely one of credit restriction, but it has also the duty to see that legitimate credit requirements are met and at the same time credit is not used for unproductive and speculative purposes. RBI has various weapons of monetary controls by using them, it hopes to achieve its monetary policy.

1. INTRODUCTION

Monetary policy is the process by which the monetary authority of a country controls the supply of money, often targeting an inflation rate or interest rate to ensure price stability and general trust in the country. Further goals of a monetary policy are usually to contribute to economic growth and stability, to lower unemployment, and to maintain predictable exchange rates with other currencies.

Monetary economics provides insight in to how to craft optimal monetary policy.

2. MEANING OF MONETARYPOLICY

Monetary policy is the macroeconomic policy laid down by the Central Bank.
It involves management of money supply and interest rate, and is the demand side economic policy used by the government of a country to achieve macroeconomic objectives like inflation, consumption, growth and liquidity. Monetary policy is the process by which the government, central bank or monetary authority of a country controls (i) The supply of money, (ii) availability of money and, (iii) cost of money or rate of interest to attain a set of objectives oriented towards the growth and stability of the economy.

3. OBJECTIVES OF MONETARY POLICY

The objectives of monetary policy differ from country to country according to their economic condition.
Following are the main objectives of the monetary policy:

- Control of Inflation and Deflation:- Inflation and deflation both are not suitable for the economy. If the price level is reasonable and there is an adjustment between the price and the cost, rate of output can increase.
- Exchange Stability:- Monetary policy second objective is to achieve the stable foreign exchange rate. If the rate of exchange is stable it shows that economic condition of the country is stable.
- Economic Development:- Monetary policy plays very effective role in promoting economic growth by providing adequate credit to productive sectors.
- Increase in the role of employment:- Monetary policy another objective is to achieve full employment but without inflation.
- Equal distribution of credit :- Monetary policy should also ensure that distribution of credit should be equitable and purposeful. The credit priority should be given to backward areas.
- Improvement in standard of living:- It is also the major objective of the monetary policy that it should improve the quality of life in the country.

These are the objectives of the monetary policy but efforts should be made to minimize the conflicts.

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4. OBJECTIVES OF MONETARY POLICY OF INDIA

The main objective of monetary policy in India is 'growth with stability'. Monetary Management regulates availability, cost and use of money and credit. It also brings institutional changes in the financial sector of the economy. Following are the main objectives of monetary policy in India.:-

- **Growth With Stability**:- Traditionally , RBI 's monetary policy was focused on controlling inflation through contraction of money supply and credit. This resulted in poor growth performance .Thus RBI have now adopted the policy of 'Growth with Stability.' This means sufficient credit will be available for growing needs of different sectors of economy and at the same time, inflation will be controlled with in a certain limit.
- **Regulation, Supervision And Development Of Financial Stability:-** Financial stability means the ability of the economy to absorb shocks and maintain confidence in financial system. Threats to financial stability can come from internal and external shocks. Such shocks can destabilize the country's financial system. Thus, greater importance is being given to RBI's role in maintaining confidence in financial system through proper regulation and controls, without sacrificing the objective of growth. Therefore, RBI is focusing on regulation, supervision and development of financial system.
- **Promotion Priority Sector** :- Priority sectors includes agriculture, export and small scale enterprises and weaker section of population. RBI with the help of bank provides timely and adequately credit at affordable cost of weaker sections and low income groups, RBI along with NABARD , is focusing on microfinance through the promotion of Self Help groups and other institutions.
- **Generation Of Employment :-** Monetary policy helps in employment generation by influencing the rate of investment and allocation of investment among various economic activities of different labour Intensities.
- **External Stability:-** With the growth of imports and exports India's linkages with global economy are getting stronger. Earlier, RBI controlled foreign exchange market by determining exchange rate. Now, RBI has only indirect control over external stability through the mechanism of ' Managed Flexibility'. Where it influences exchange rate by buying and selling foreign currencies in open market.
- **Encouraging Savings And Investments: -** RBI by offering attractive interest rates encourage savings in the economy. A high rate of saving promotes investment. Thus the monetary management by influencing rates of interest can influence saving mobilization in the country.
- **Redistribution Of Income And Wealth :-** By control of inflation and deployment of credit to weaker sectors of society the monetary policy may redistribute income and wealth favouring to weaker sections.
- **Regulation Of NBFIs :-** Non Banking Financial Institutions (NBFIs),like UTI, IDBI, IFCI, plays an important role in deployment of credit and mobilization of savings. RBI does not have any direct control on the functioning of such institutions. However it can indirectly affects the policies and functions of NBFIs through its monetary policy.

5. LIMITATIONS OF MONETARY POLICY

- **Huge Budgetary Deficits :-** RBI makes every possible attempt to control inflation and to balance money supply in the market. However Central Government's huge budgetary deficits have made monetary policy ineffective. Huge budgetary deficits have resulted in excessive monetary growth.
- **Coverage Of Only Commercial Banks :-** Instruments of monetary policy cover only commercial banks so inflationary pressures caused by banking finance can be controlled by RBI, but in India inflation also results from deficit financing and scarcity of goods on which RBI may not have any control.
- **Problem Of Management Of Banks And Financial Institutions:-** The monetary policy can succeed to control inflation and to bring overall development only when the management of banks and Financial institutions are corrupt and inefficient which leads to financial scams in this way overall economy is affected.
- **Unorganised Money Market :-** Presence of unorganised sector of money market is one of the main obstacle in effective working of the monetary policy. As RBI has no power over the unorganised sector of money market, its monetary policy becomes less effective.

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- **Less Accountability :-** At present time, the goals of monetary policy in India, are not set out in specific terms and there is insufficient freedom in the use of instruments. In such a setting, accountability tends to be weak as there is lack of clarity in the responsibility of Governments and RBI.
- **Black Money:-** There is a growing presence of black money in the economy. Black money falls beyond the purview of banking control of RBI. It means large proposition of total money supply in a country remains outside the purview of RBI 's monetary management.
- **Increase Volatility:-** The integration of domestic and foreign exchange markets could leads to increased volatility in the domestic market as the impact of exogenous factors could be transmitted to domestic market. The widening of foreign exchange market and development of rupee-foreign exchange swap would reduce risks and volatility.
- **Lack Of Transparency:-** According to S.S.Tarapore, the monetary policy formulation , in its present form in India, can not be continued indefinitely. For a more effective policy , it would be necessary to have greater transparency in the policy formulation and transmission process and the RBI would need to be clearly demarcated.

6. CONCLUSION

Thus, from above we can say that despite several problems RBI has made a good efforts for effective implementation of the monetary policy in India

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