

Money Management:

Are democracies becoming debtocracies?

Money management (and the next topic of fiscal management) is not a separate topic but a part of Gangajal Economics. It has been discussed separately to highlight its importance.

Stewardship of Economy

In the introductory part, we had mentioned about democracies becoming debtocracies due to excessive debt. A person who lives under debt all the time does no good to his persona. The excesses occur because there is no clarity about what the rational credit requirement is and how not to allow the excesses to occur.

Both monetary and fiscal policies impact each other. The stewardship of an economy should be singular. As the finance ministry/treasury of the nation has the overall responsibility, the leadership should remain with it. The central bank should not be independent. Its independence without accountability serves no purpose. The independence is also not required.

Incidentally, since both these policies impact each other, a monetary union without a fiscal union is a risk to the financial stability in the long run unless all the participating countries practice fiscal discipline.

Money Management

Money management is a broad term that includes monetary policy, banking regulation, capital market management, insurance regulation, foreign trade and forex management. Though foreign trade as such is not a part of money management, considering the forex requirement, we have included the topic under money management for the sake of convenience.

The objective of money management is to control inflation while supporting growth

and ensure financial stability. So far as the monetary policy of the central bank is concerned, it is aimed at fulfilling the first objective. The second objective is realised through the regulation of the banking industry.

It is pertinent to note how policies can go wrong. It is believed that an interest rate change impacts the asset prices and investment. Actually, it only creates temporary psychological ripples. The real investments depend upon the expectations of returns. Interest element happens to be an insignificant part in the total cost of production and is not an influential factor. But the misunderstanding continues and has been well cemented. Sometimes, even when the inflation is a result of supply side constraints, the interest rates are tinkered.

Our model steers clear of such infirmities. It does not control inflation through interest change mechanism. It applies our uniquely designed direct methodology to keep inflation under control. The solutions recommended by us would work effectively to put all the areas of the economy on the right track.

Appropriate policies to contain risks to financial stability

Securitization of debt, derivatives product, credit card systems, operations of non-banking financial institutions, lending in foreign currency and payment bank are some of the important factors that impact the financial stability. Appropriate national policies are required in this regard. Our model provides a suitable guidance in this regard.

Elements of Monetary and Banking Regulation Framework

Excessive risk taking happens from the bankers in order to increase their business. Their boards need to control such excesses but they fail to put ceilings. The central bank is concerned with the financial stability and must regulate the banking industry well. Our model provides policy guidance in respect of the following areas of banking regulation:

- Structure of interest rates
- Lending to Government
- Reserves requirements for banks
- Capital adequacy of banks & balance sheet structure
- Control over money supply
- Forex reserves and their investment by central bank
- Other financial stability issues
- Risk management by banks
- Customer care by banks
- Oversight by central bank
- Accounting by central bank and infrastructure fund

Insurance

- Principles of insurance business
- How insurance works
- What cannot be insured
- Pertinent risks in insurance business
- Guidelines for establishing an effective insurance industry
- Regulatory oversight

International Trade and Forex Management

Different aspects of international trade and forex management have been discussed in our model with specific policy guidance. These aspects have been listed below.

International Trade

- Original concept of international trade
- Perversion of the original concept
- Why absolute free trade is not desirable
- Bilateral deals; no scope for trade organisations
- Restrictions on trade and services

- Approach of Current Account surplus country
- Approach of Current Account deficit country
- Working according to one's own strengths
- Role of multi-national corporations

Forex Management

- Importance of Forex Reserves
- Capital Account Convertibility for Citizens
- Forex Markets
- Foreign Investments
- FDI and Capital/Dividend Repatriation Policy
- Foreign Currency Borrowings
- Building Reserves: Quantum
- Building Reserves: Composition of Gold
- Utilisation of Forex Reserves
- Stabilization Fund by Current Account Surplus Countries

Capital Market Management

The main objectives of the capital market are:

- Meet the capital funding requirements of corporations
- Establish trading mechanism to enable investors to enter in or exit from the investment securities
- Regulate trading to ensure reasonable brokerage, transparency and efficiency while containing speculation at acceptable level, and
- Protect the interests of the investor community

To realise the above objectives, several activities of the capital market need to be regulated. Our model provides specific guidance relating to various aspects/elements as listed below.

- Institutional set-up
- Taxation on trading
- Investor protection
- Foreign Stock Exchange listing

- Domestic Stock Markets
- Commodities trading
- Regulatory control
- Change in corporate management

Helping a nation to re-orient policies relating to money management

Our model can help assess the existing policies of a nation and take corrective measures so as to regulate the important areas of money management and ensure financial stability.