2 MONEY: DEMAND, SUPPLY & CREATION

2.1 DEMAND OF MONEY: LIQUIDITY PREFERENCE THEORY (तरलता अधिमान)

John Maynard Keynes (Book: *The General Theory of Employment, Interest and Money*) noted that people prefer to keep a part of assets in liquid form (cash money) with 3 motives:

1. **Transaction motive (संव्यवहार उद्देश्य)**: For using money as a medium of exchange e.g. for buying daily milk, veggies, fruits.
2. **Precautionary motive (एहतियाती)**: To protect against sudden / unforeseen expenditure e.g. medical emergency or impulsive purchase during a holiday trip.
3. **Speculative motive (सट्टा-उद्देश्य)**: Investors hold cash to make the best use of any investment opportunity that arises later e.g. waiting for bond/gold/land prices to fall, then "I will use my cash to buy it". Also known as "**Asset Demand of Money**".

The amount of money held in cash form vary inversely with interest rates. If higher interest available in Bonds etc, people would invest money there instead of keeping money in liquid form (cash).

2.2 SUPPLY OF MONEY (मुद्रा की पूर्ति)

Time Liabilities of a Bank (FDRD) समय / मीयादी देयताएँ	**Demand Liabilities (CASA)** मांग देयताएं
- Fixed deposits, Cumulative/ recurring deposits, Staff security deposit etc. - Bank legally not required to pay customer before maturity but can pay after deducting penalty/ interest.	- Current Account, Savings Account, Demand Draft - Overdue balance in Fixed Deposits - Unclaimed deposits
Public parks more money here, because better returns.	_ _ _ _ _ _
_ _ _ _ _	More liquid because easily convertible into cash.

*CU: Coins & Currency with Public

Measure संकुचित, व्यापक		*CU	Commercial Banks		Post Office Savings Bank		Liquidity तरलता	Qty
			Demand Deposits (CASA)	Time Deposits (FDRD)	Demand Deposits (SA)	Time Deposits (!notNSC)		
Narrow Money	M1	✓	✓	✗			☆☆☆☆	☆
	M2	✓						
_ _ _ _ Money	M3	✓						
	M4	✓					☆	☆☆☆☆

- Self-Extrapolate e.g. M3 = M1 + Time deposits with commercial banks.
- M3 is the most commonly used for measuring money supply, aka "**Aggregate Monetary Resources**" (समस्त मौद्रिक संसाधन).
- In Money supply, we are only counting the "**NET Demand / NET Time deposits**" i.e. only public deposits in bank. The interbank deposits, which a commercial bank holds in other commercial banks, not counted.

2.3 CREATION OF MONEY (मुद्रा का निर्माण)

M0 / Reserve Money / Government Money / High Powered Money (उच्च शक्ति मुद्रा) is issued under RBI Act, by RBI's ISSUE DEPARTMENT, with condition that ISSUE DEPARTMENT'S assets must match its liabilities.

Assets of Issue Department (परिसंपत्तियाँ)	Liabilities of Issue Department [M0]
1. Rupee coins [RBI circulates it as 'agent of govt'] 2. Gold coins and bullion [Min. 115 crores] 3. Foreign Securities [Earlier Min. 85 crores but Post-1995 no such requirement.] 4. Govt. Securities [through which Govt borrows money from RBI, pays interests to RBI]	Currency (& coins) in circulation: 1. Held by Public 2. Held by other Banks in "Vault cash" (i.e. amount for day to day Ops.) 3. Other Deposits in RBI (of Public, Banks & Governments)

2.3.1 Velocity of Money Circulation (मुद्रा संचालन का वेग)

It is the average number of times money passes from one hand to another, during given time period. e.g. you bought pen worth Rs.10 from shopkeeper, he uses same 10 rupee note to buy tea from another shop, then same currency note performed function of 20 Rupees. This "Velocity of money circulation" is affected by following factors:

- More quantity of money -> less velocity.
- Income distribution. Money in the hands of poor people has higher velocity than the rich.
- Booming period = more raw material purchase & hiring = higher velocity
- Low financial inclusion / low banking penetration = People tend to save more in physical assets or in cash then money doesn't change hands much= low velocity.
- If more people use loans for purchase=> higher velocity. Hence developed countries => higher velocity, because people save less and spend more because of lifestyle and confidence in Government's social-security e.g. USA.
- Higher the GDP, more transactions taking place = Higher velocity.

2.4 MONEY MULTIPLIER (मुद्रा गुणक)

RBI's legal reserve system (CRR-SLR) leads to *Fractional Reserve Banking & Credit Creation* by the commercial banks, which creates money multiplier effect as following:

High Powered money (M0) = 100	Asset Side	Loaning	10% Reserve ('r')
Bank#1	100	90	10
Bank#2	90	81	9
Bank#3	81	72.9	8.1
Bank#..	..	..	..
Total Money (here M3)	1000 =	900 +	100

$$\boldsymbol{Money\ Multiplier} = \frac{Stock\ of\ Total\ Money}{Stock\ of\ High\ Powered\ money} = \frac{1000}{100} = 10.$$

- Every "R" reserve generates "1/R" new money. Here, 10% reserve generated 10x times the high-powered money. 4% reserve ratio will generate 25x times (in theory), however in reality the multiplier will be lower due to poor banking penetration, black money etc.
- In functional economy, money multiplier is always greater than 1.
  - & It directly improves with cut in legal reserve ratios (SLR, CRR)
  - & It indirectly improves as economy develops, consumption / loan demand increases, banking penetration improves etc. In 60s = less than 2x, 90s = more than 3x, At present = more than 6x.

2.5 FACTORS AFFECTING MONEY SUPPLY [M1, M3]

M1, M3 Money Supply will increase when:

- When Money multiplier and / or Velocity of money increases.
- When RBI's asset side increases e.g. Government borrowing more from RBI using G-sec or increase in RBI's Forex securities.
- With the increase in banking penetration, financial inclusion, formalization of economy, Boom period, whenever loan demand increases.
- When RBI adopts Cheap / Easy / Dovish / Expansionary monetary policy to combat deflation.

3 MONETARY POLICY (मौद्रिक नीति)

- **[Definition]** Monetary Policy is a macroeconomic policy (समष्टि आर्थिक नीति), designed by the central bank of a country, to manage money supply & interest rates. It helps shaping variables such as inflation, consumption, savings, investment, and capital formation (मुद्रास्फीति, खपत, बचत, निवेश और पूंजी निर्माण).
- **[Significance]** Monetary policy plays an important role in price stability [inflation control], economic growth, job creation and social justice in any economy.
- John Maynard Keynes: When economy is functioning at full employment, aggregate supply matches aggregate demand i.e. Consumption (C) + Investment (I) + Govt Purchase (G) + Net Export (eXport-iMport). If demand higher than supply -> inflationary gap.
- **Philip Curve**: Inflation _ = unemployment _ (and vice versa).
- Therefore, stable & moderate inflation is good for the economy. So, RBI tries to keep inflation with 2-6% CPI (All India) using its bi-monthly monetary policy made by its 6-member statutory monetary policy Committee.

3.1 MONETARY POLICY: QUANTITATIVE TOOLS (परिमाणात्मक साधन)

Also known as (aka) **General or Indirect Tools** as they affect the entire economy, and not just a particular sector.

3.1.1 Statutory Reserve Requirements: CRR, SLR (Fight inflation: _ , deflation: _)

CRR: _ (नकद कोष अनुपात)	**SLR:** _ (वैधानिक तरलता अनुपात)
Banks have to keep this much deposits with RBI. RBI doesn't pay interest on it, except in extraordinary circumstances like 1999-2000's Banking slowdown.	Banks have to keep this much deposits in liquid assets such as cash, gold, G-Sec, T-Bills, State Development Loan Bonds and other securities notified by RBI.
Bank earns no profit / interest*	Some profit*
Mandated under RBI Act, 1934 (Section 42)	Banking Regulation Act, 1949 (Section 42)
RBI can fix any amount of CRR, legally there is no minimum floor or maximum ceiling. Presently it's 4% of total DTL	Legally, SLR can't be more than 40%. Presently it's 19.5% of NDTL and will be reduced to 18% in 2019-20 in phased manner.
Counted on Total Demand and Time Liabilities (DTL) of the Bank.	On Net Demand and Time Liabilities (NDTL) (निवल मांग और समय देयताएँ)

During demonetization, RBI prescribed Incremental CRR of 100% to drain excess liquidity & prevent crashing of loan interest rates. It was a temporary measure, presently, no incremental CRR.	Associated topic: Liquidity Coverage Ratio (LCR) and High Quality Liquid Assets (HQLA): we'll study in BASEL-III lecture.
Scheduled Commercial Banks (SCBs) must maintain CRR	Same
State and Central Cooperative Banks must maintain CRR, but RBI could keep different slabs / norms for them.	Same
RRBs don't have to maintain CRR	RRBs must maintain SLR, but RBI could keep different slabs / norms for them.

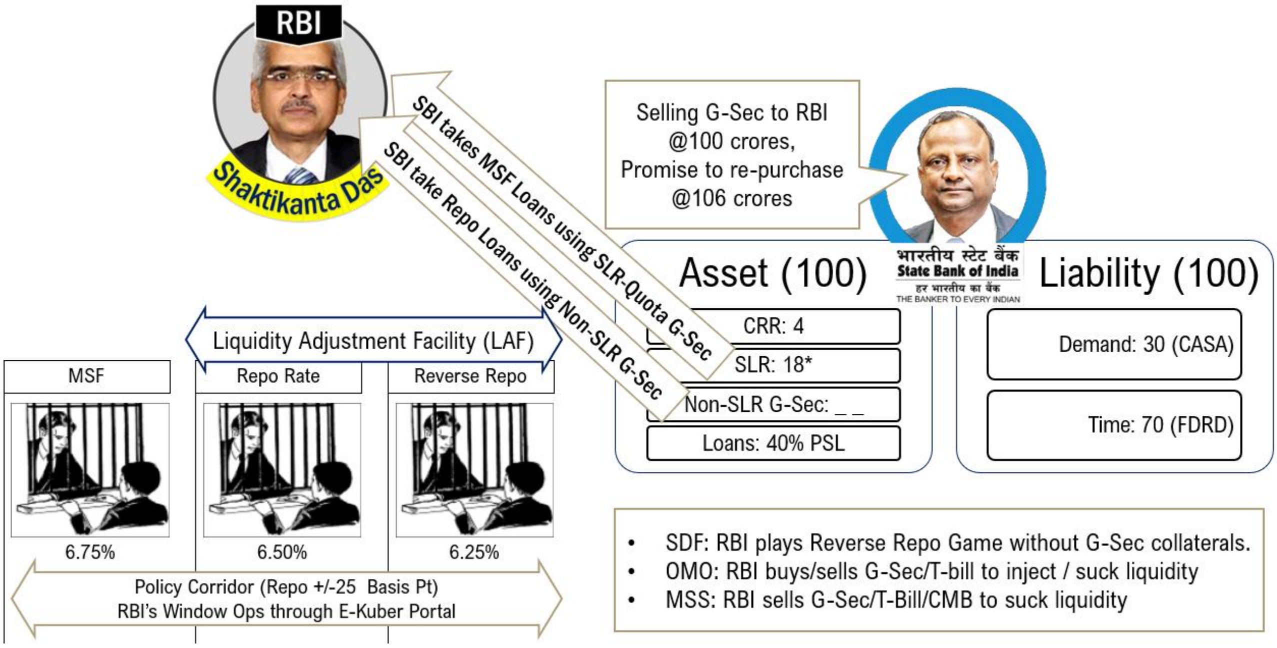
- SLR/CRR are counted on fortnightly basis. If not maintained, bank will have to pay penalty interest rate which is linked with Bank Rate.
- CRR/SLR ensure monetary stability of India through **two primary functions**
    1) They assist in money multiplier effect
    2) They create Buffer-Protection during a Bank Run i.e. an emergency when everybody wants to take money from his bank account at once, mainly due to fake news / rumors.
- While in theory CRR/SLR can be used for inflation control but RBI primarily relies on REPO Rate (=its Policy Rate) to combat inflation, and not CRR/SLR.

Asked in UPSC-CDS-2011-II	*Asked in UPSC-Pre-2015*
Q. Find correct statements about Statutory Liquidity Ratio (SLR) 1. To meet SLR, Commercial banks can keep cash only. 2. SLR is maintained by the banks with themselves. 3. SLR restricts the banks leverage in pumping more money into the economy. Answer codes: (a) 1, 2 and 3 (b) 1 and 3 (c) 2 and 3 (d) only 2	Q. When the Reserve Bank of India reduces the Statutory Liquidity Ratio by 50 basis points which of the following is likely to happen? (a) India's GDP growth rate increases drastically (b) Foreign Institutional Investors may bring more capital into our country (c) Scheduled Commercial Banks may cut their lending rates. (d) It may drastically reduce the liquidity to the banking system

3.1.2 Key Rates (Inflation -> _ _ Rates, Deflation -> _ _ Rates)

- **Bank Rate (बेंक दर):** Interest rate at which banks borrow long term loans from RBI without pledging any securities/collaterals. It's not the primary tool of monetary policy, but used in computation of penalty rates.
- **Marginal Standing Facility (MSF, 2011 - सीमांत स्थायी सुविधा):** The Interest rate at which RBI lends short-term loans to Scheduled Commercial Banks (SCB) with their _ as collaterals. MSF _ _ _ _ _ _ _ _ than Repo Rate.

- **Liquidity Adjustment Facility (LAF, 2000- तरलता समायोजन सुविधा)**: consists of two mechanisms:
    I. **LAF-Repo Rate (पुन: क्रय-अनुबंध):** The Interest rate at which RBI lends short-term loans to its clients with their G-Sec as collaterals. Clients enter into an agreement with RBI to repurchase their G-sec at a future date at a (higher) pre-determined price. SCB _ _ _ _ _ _ pledge their SLR-quota-G-Secs. Repo Rate is our Policy Rate to control inflation. MSF & Reverse Repo tied with it.
    II. **LAF-Reverse Repo Rate (उलट पुन: क्रय-अनुबंध):** It's the interest rate that clients earn when parking their surplus funds with the RBI for short periods. Mechanism similar to Repo, RBI gives its G-Sec used as a collateral. Reverse Repo is _ _ _ _ _ than Repo Rate.



3.1.2.1 Key Rates- associated terms

- **Policy Corridor:** It's the width among MSF-Repo-RR. Presently, 25 basis points (0.25%). Previously it had been 1%, 0.50% but narrowed to 0.25% for better alignment with call money market, thus ensuring better transmission of monetary policy
- **Window Operations:** LAF-MSF "windows" are operated through RBI's _ _ _ _ _ _ CBS platform.
- **(Uncollateralized) Standing Deposit Facility (SDF, स्थायी जमा सुविधा):** Banks parks funds in RBI for short-term to earn interest. No G-sec or collateral, unlike Reverse Repo. This helps RBI absorb excess liquidity for short term in situations like demonetization when RBI may not have enough G-Secs to pledge as collaterals. Urjit Patel Committee on Monetary policy (2013) proposed this, Budget-2018 agreed to amend RBI Act for this.
- **Tri-Party Repo Rate (त्रि-पक्षीय पुन: क्रय-अनुबंध):** In ordinary repo, there are two parties- borrower vs. lender (RBI). In Tri-party Repo, there are 3 parties 1) borrowers 2) lenders 3) Tri-Party Agent (e.g. NSE) who, acts as an intermediary between the

two parties to facilitate collateral custody, payment and guaranteed settlement. RBI issued guidelines in 2017, NSE started this in 2018. This is not a tool of Monetary Policy. It helps deepening Corporate Bond market.

3.1.3 Market Operations (OMO, MSS): (Inflation -> Sell G-Sec, Deflation -> Buy)

- **Open Market Operations** (खुले बाजार की क्रियाए): RBI buys and sells G-sec, T-Bills to control money supply. RBI buying injects liquidity, RBI selling sucks liquidity.
- **Market Stabilization Scheme** (बाजार स्थिरीकरण योजना): RBI sells G-sec, T-Bill & Cash Management Bills (CMB) to suck excess liquidity. While the money thus collected is not part of Govt.'s borrowing, but Govt. pays interest on it. This mechanism was enhanced during Demonetization to counter excess liquidity and crashing of lending rates.
- **Sterilization**: <in Pillar#3: Balance of Payment>

Q. Which of the following measures would result in an increase in the money supply in the economy? (Asked in UPSC-Pre-2012)

1. Purchase of G-Sec from the public by the Central Bank
2. Deposit of currency in commercial banks by the public
3. Borrowing by the government from the Central Bank
4. Sale of government securities to the public by the Central Bank

Select the correct answer using the codes given below:

(a) 1 only
(b) 2 and 4 only
(c) 1 and 3
(d) 2, 3 and 4

3.2 Monetary Policy: Qualitative Tools (गुणात्मक साधन)

While quantitative tools (SLR, CRR, Repo etc.) control the 'volume' of loans, these qualitative tools (PSL,LTV etc.) control the "distribution" of loans to a particular sector of economy (e.g. agriculture) or particular segment of society (e.g. farmers, women, SC/ST). Hence, also known as SELECTIVE (चयनात्मक) or DIRECT Tools.

3.2.1 Moral Suasion (नैतिक दबाव / सलाह)

- "Persuasion" without applying punitive measures. RBI governor tries this tactic via conferences, informal meetings, letters, seminars, convocation, panel discussion, memorial lectures.
- Example, Governor asking Banks to transmit rate cuts, open new branches in rural areas, spread financial literacy, give loans to farmers beyond PSL quota etc. Similarly, Governor asking CM/FM to control fiscal deficit & subsidy leakage to enhance the impact of RBI's monetary policy.

3.2.2 Direct Action (सीधी कार्यवाही)

- RBI can punish banks (and even non-banks) for not complying with its directives under RBI Act, Banking Regulation Act, Payment and Settlement Systems Act, Prevention of Money Laundering Act, Foreign Exchange Management Act (FEMA).

3.2.3 Margin Requirements / LTV (सीमा अनिवार्यता)

- RBI can mandate that Loan to Value (LTV) for a gold-loan, home loan, auto loan or business loan can't be more than x% of the value of the collaterals. RBI can change this x% to boost / curb demand.

3.2.4 Selective Credit Control (चयनात्मक ऋण नियंत्रण)

In a negative / restrictive direction	In a positive direction
- In erstwhile-USSR: Credit Rationing System where an individual can't get more than prescribed amount of loans for each category (housing, education, business). - 1960s: Credit Authorization Scheme (CAS) in India: all commercial banks had to obtain prior approval of the RBI before giving Rs. 1 crore/> to a single borrower. - 1970s: RBI imposed quantitative ceiling on non-food loans to boost green revolution, food inflation. But such measures failed due to lax monitoring and loopholes.	- Consumer credit control e.g. During deflation / recession, RBI can relax the downpayment / EMI installment norms for durables like Vehicles, TV, Fridge etc. to boost consumption and demand. - **Priority Sector Lending** <see below>

3.3 PRIORITY SECTOR LENDING (प्राथमिकता क्षेत्र के लिए ऋण मानक)

- 1968: First time RBI used the word "priority sector": Banks must give 40% of their loans to 3 priority sectors 1) agri 2) small industries 3) exports by 1985.
- 1971: Credit Guarantee Corporation of India Ltd. setup to facilitate bank lending to the priority sectors. [Will study more with MUDRA Bank in NBFC pillar]
- 2015: the PSL norms were updated:

Priority Sector Loans	Quota
Weaker Sections: SC, ST, Women, PH, Minorities, Manual scavengers, Artisans, NRLM/NULM beneficiaries, PMJDY Overdrafts upto Rs.10k.	_ _ %
Agriculture: Non-corporate farmers etc.	10%
Agriculture: *Marginal Farmer (upto 1ht); *Small farmer (>1 upto 2ht)	_ %
Micro Enterprises, Khadi-Village industries	7.50%
Above parties, as well as Small & Medium Enterprises, Affordable housing loans to beneficiaries under Pradhan Mantri Awas Yojana, food processing companies, Vermi compost, biofertilizer, seed production, Exporters, Student-Education loans (upto Rs.10l), Social Infrastructure (schools, health care, drinking water, sanitation facilities); Renewable Energy Projects (wind mills, biomass generators, solar street light, micro-hydel plants etc.)	4.50%
Total PSL for SCB and (Foreign Banks with 20/> branches).	_ _ _

- If foreign bank has less than 20 branches, they'll also have to give 40% PSL-Quota loans WEF 31/3/2020, but no internal loan-quotas for weaker section, small farmers, khadi enterprise etc. for such banks.
- If Regional Rural Bank (RRB) or Small Finance Bank, then above 40% quota + extra 35% quota (in any PSL-sectors) = _ _ PSL loan-quota.
- Loans given to Microfinance Agencies for above categories, are also counted in quota.
- Bank + NBFC's joint lending / co-origination loans to PSL categories are also eligible, with conditions.

3.3.1 Priority Sector Lending Certificates (PSLC) from 2016 onwards

- In this arrangement, the overachieving Banks can sell their excess PSL in form of 'certificates' to underachieving banks without transferring the loan assets or its risk.
- Four kinds of PSLCs traded through RBI's _ _ _ _ Portal, viz., Agriculture (PSLC-A); Small and Marginal Farmers (PSLCSM); Micro Enterprises (PSLC-ME); and General (PSLC-G).
- If an underachiever bank can't fulfil its PSL-quota through PSL-certificates purchase then ultimately, it'll have to deposit PSL-shortfall money to NABARD's Rural Infrastructure Development Fund (RIDF), SIDBI's Small Enterprises Development Fund (SEDF) or NHB or MUDRA Ltd. as per the norms. Under-achiever bank will earn interest from such deposited money, but it'll be linked with Bank-Rate.

Q. Priority Sector Lending by banks in India constitutes _ _ _ *(Asked in UPSC-Pre-2013)*

a) Agriculture
b) Micro and Small Enterprises
c) Weaker Sections
d) All of the above

3.4 MONETARY POLICY TOOLS: A READY RECKONER TABLE

<table>
<tr><td colspan="2" rowspan="2">Tools & Strategy?
- Deflation: ↑ money supply, inject liquidity=> make loans cheaper, ↑ consumption
- Inflation: Do reverse</td><td><2%CPI= Fight deflation (अपस्फीति)</td><td>>6%CPI= Fight Inflation (मुद्रास्फीति)</td></tr>
<tr><td>Easy, Cheap, Dovish, Expansionary policy.
आसान-सस्ता व्याजदरे, विस्तारवादी</td><td>Tight, <u>Dear</u>, Hawkish, Contractionary
तंग- मँहगी व्याजदरे, संकुचनवादी</td></tr>
<tr><td rowspan="3">Qualitative</td><td>Reserves: CRR, SLR</td><td></td><td>↑</td></tr>
<tr><td>Key Rates (Repo, MSF, Bank Rate)</td><td>↓</td><td></td></tr>
<tr><td>Market Ops (OMO, MSS)</td><td>OMO: RBI _ _ _ _ _ G-Sec from market
MSS: N/A</td><td>OMO: RBI _ _ _ _ G-Sec
MSS: same as OMO</td></tr>
<tr><td rowspan="3">Qualitative</td><td>Moral Suasion / Direct Action</td><td>Nudge / Force the banks to enforce Dovish Policy</td><td>To enforce the Hawkish policy</td></tr>
<tr><td>Margin Req. / LTV</td><td>Increase e.g.
Gold-LTV: 60%->90%</td><td></td></tr>
<tr><td>Selective Credit Control / PSL</td><td><think!></td><td>- ↓the loan-flow to sectors where speculative investment is leading to demand-side inflation e.g. real-estate & housing.
- ↑loan-flow to sectors where loans can ↑supply e.g. onion farmers.</td></tr>
</table>

Asked in UPSC-Pre-1995	*Asked in UPSC-Pre-2013*
Q. Which of the following is not an instrument of Selective Credit Control? a) Regulation of consumer credit b) Rationing of credit c) Margin requirements d) Cash reserve ratio	**Q. An increase in the Bank Rate generally indicates that _ _ _** A. Market rate of interest is likely to fall. B. Central Bank is no longer making loans to commercial banks. C. Central Bank is following an easy money policy. D. Central Bank is following a tight money policy.
Asked in UPSC-Pre-2015	
Q. Consider the following: 1) Bank rate 2) Open market operations 3) Public debt 4) Public Revenue Which of them is/are part of Monetary Policy? (a) 1 only (b) 2, 3 and 4 (c) 1 and 2 (d) 1, 3 and 4	

4 MONETARY POLICY IN PRESENT-DAY INDIA

There are 3 major ways of making monetary policy

1. **Exchange rate stability:** Singapore & other export-oriented economies use this.
2. **Multiple Indicators:** Central Bank tries to focus on Growth, Employment, Inflation Control and Exchange rate stabilization. India's RBI had this before 2016.
3. **Inflation targeting:** Central Bank only aims to keep inflation controlled, and other indicators (growth, employment, exchange rate) will automatically fall in line. This strategy successful in Western nations, adopted in India WEF 2016-Oct, based on Urjit Patel Committee Report (2013-14), by amending RBI Act Section 45 with following provisions:

4.1 MONETARY POLICY MAKING UNDER RBI ACT SINCE 2016

Monetary Policy to be made by a statutory Monetary Policy Committee with following composition:

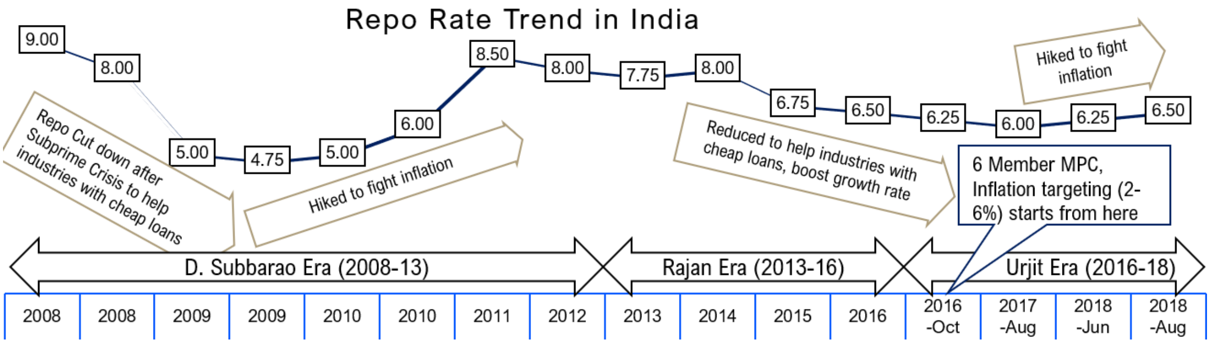
RBI side	Govt. Side
1. RBI Governor, as the Ex-officio Chairman. 2. Dy.Governor responsible for Monetary Policy: Viral Acharya 3. One person nominated by RBI Central Board: Michael Patra (Executive Director, RBI)	1. Dr. Chetan Ghate, Indian Statistical Institute 2. Dr. Pami Dua, Delhi School of Economics 3. Dr. Ravindra H. Dholakia, IIM-A
Their tenure tied with their ex-officio job tenure E.g. Shaktikanta's *shakti* (powers) will be gone after 3-year tenure as RBI-Governor expires, unless reappointed.	Tenure: 4 years, no re-appointment. They're selected by a Committee headed by cabinet Secretary (IAS)

- Meeting quorum 4 members- incl. Governor. Minimum four meetings a year. In practice, they meet every two months to decide bi-monthly monetary policy updates.
- Repo rate (=Policy rate) decided by Majority vote. If tie, then Governor has _ _ _ _ vote.

- To ensure transparency / accountability: Govt can send message only in writing. Committee must publish its minutes of the meeting on _ _ _ day, and "Monetary policy report" at every 6 months.
- Inflation target decided by Union Government in consultation with RBI.
    - **Present target**: Keep CPI (All India) within 2-6% for _ _ _ _ _ _ (ending at 31/03/2021). [alt. way of saying: 4% +/- spread of 2%]
    - **Target fail:** if inflation not kept in this 2-6% zone for 3 consecutive quarters (=9 months) then Committee must send report to Govt with reasons and remedies.

Asked in UPSC-Pre-2015	Asked in UPSC-Pre-2017
Q. With reference to inflation in India, find correct statement: a) Controlling the inflation in India is the responsibility of the Government of India only b) The Reserve Bank of India has no role in controlling the inflation c) Decreased money circulation helps in controlling the inflation d) Increased money circulation helps in controlling the inflation	**Q. Consider following statements about Monetary Policy Committee:** 1. It decides the RBI's benchmark interest rates. 2. It is a 12-member body including the Governor of RBI and is reconstituted every year. 3. It functions under the chairmanship of the Union Finance Minister. Find Correct Statements: (a)1 only (b) 1 and 2 only (c) 3 only (d) 2 and 3 only

4.2 Review of Last 1 Year's Monetary Policies



	Policy Decisions & Regulatory Announcements [we will study in appropriate pillars/sections]
Feb-2018	- **No change in Repo@6%; Neutral Stance** - Share market volatility, Advanced Economies recovery= foreign investors' outflow-> weakening of rupee + OPEC-Russia OIL production CUT = crude oil led inflation. - PSL loan caps removed for MSME. Base rates-MCLR Reforms. - ATM-Cash recycler machine subsidy removed - Ombudsman for NBFCs
April-2018	- **No change in Repo @6%; Neutral Stance** - Wait and Watch mode because Budget's pro-farmer-MSP, pro-rural approach; 7th Pay Commission's HRA hikes could generate demand-side inflation.

	- IndAS accounting norms for Indian Banks deferred till 1/4/2019 - BASEL-III CCCB not necessary for this FY. - Payment System data must be stored in India within next 6 months. - Reiterated that cryptocurrencies / VC are dangerous WRT consumer protection, market integrity and money laundering. No entity regulated by RBI shall deal with VC companies, else be ready to "Face Direct Action". - RBI's inter-departmental group to check desirability and feasibility to introduce a central bank digital currency. - RBI data science lab for big-data analytics will be setup by 2018-Dec. - Regulatory norms for Cash-in-Transit (CIT) companies and Cash Replenishment Agencies (CRAs) - Financial literacy: new booklets for five target groups: Farmers, Small entrepreneurs, School children, Self Help Groups and Senior Citizens. Will review Lead-Bank Scheme.
June-2018	- **Repo hike 25 bps= @6.25%; Neutral Stance** - There has been a 12% increase in the crude oil price since the April policy. Crude Oil price rise are 'passed through' because Governments not reducing custom / excise /state VAT. So, had to fight inflation by raising Repo. - Will implement Deosthalee Committee's Public Credit Registry report. - Will allow Voluntary Transition of Urban Cooperative Banks into Small Finance Banks. - PSL home-loan guidelines revised to sync with Pradhan Mantri Awas Yojana. - Will develop a suitable rechargeable device or offline-software/app mechanism for visually challenged to identify Indian banknotes.
Aug-2018	- **Rate hike 25 bps= @6.50%; Neutral Stance (meaning next time, either hold, hike or cut).** - Rupee weakening against dollar, Government's MSP-hike = more inflation likely. Had to fight inflation by raising Repo. - Norms for Co-origination of loans for Bank-NBFC. - Banks' Internal Ombudsman trial successful. Now applicable to all SCB. - Extension of MSF-LAF facilities to certain cooperative banks.
Oct-2018	- **No change in Repo but Stance changed to: Calibrated Tightening (meaning next time either rate hold or rate hike but no chance of ratecut)** - RBI still apprehensive of oil prices, rupee strength and inflation, but did not increase Repo, just wait and watch for now.
Dec-2018	- **No change in Repo; Stance: Calibrated Tightening** - While Crude oil prices have declined by ~30% since October, so higher inflation is unlikely. But RBI wants to keep inflation @4 per cent on a durable basis. So, "calibrated tightening" stance continued. - Loan rate external benchmarks WEF 1/1/2019. - RBI to reduce SLR, from 19.5% to 18% at the rate of 25 basis points in each quarter for BASEL-LCR-HQLA compliance. (will learn in Pill#1:BASEL) - India and Japan have agreed to enter into a bilateral swap arrangement of $75 billion (will learn in Pill#3) - Urban Cooperative Banks to have board of management under RBI. - Told Banks to keep special facilities for the senior citizen customers since 2017, if not done then be ready for "DIRECT ACTION" via Banking Ombudsman.

	- RBI's own Ombudsman for digital transactions- he'll look into not just banks but all payment service providers. - Framework for Limiting Customer Liability in Unauthorized E-Transactions in Prepaid Payment Instruments. - RBI to setup Ex-SEBI Chairman U K Sinha’s Committee on long-term solutions for the economic and financial sustainability of MSME.
Feb-2019	<stay tuned>

4.3 LIMITATIONS OF MONETARY POLICY IN INDIA

Even though the monetary policy is updated every 2 months, its efficacy in controlling inflation or boosting growth is restricted by following factors:

- Repo is not major source of funds for banks, unlike the Advanced Economies, where households don’t save that much in Banks.
- Indian Banks don’t immediately pass on the rate cuts to customers, citing NPA problems.
- Supply side issues: El-Nino/Poor monsoon hurting crop production, geopolitical issues increasing global crude oil & raw material prices.
- Government side issues: Fiscal repression, Fiscal slippage, Fiscal deficit, Subsidy leakage, Populist Loan-waivers etc.
- Structural Issues in Economy: lack of electricity-road infrastructure, Ease of Doing Biz, Presence of Informal moneylenders in rural areas who circulate black money at exorbitant interest rates. Poor penetration of banking sector and financial inclusion etc.

Because of these reasons, RBI can’t greatly reduce the Repo/CRR/SLR, and then its criticised for not making cheap loans available to industries.

4.3.1 Mock Questions for UPSC Mains/GSM3 (150-250 words)

1. "Monetary policy is both a catalyst and an impediment to India's growth story." Examine critically. “भारत की विकास-गाथा में मौद्रिक नीति एक उद्दीपक भी है और एक अवरोधक भी है।" गंभीररूप से विश्लेष्ण करे.
2. “Monetary policy is a useful medicine, but NOT panacea for economic growth”. Comment in context of India. “आर्थिक विकास के लिए, मौद्रिक नीति एक उपयोगी दवा है, लेकिन रामबाण नहीं”. टिप्पणी करे.
3. Discuss the significance of Monetary policy in India's economic growth and human development. भारत की आर्थिक वृद्धि और मानव विकास में मौद्रिक नीति के महत्व पर चर्चा करें.