About Monetary Policy

- Monetary policy is the process by which monetary authority of a country, generally a central bank controls the supply of money in the economy by exercising its control over interest rates in order to maintain price stability and achieve high economic growth.
- In India, the central monetary authority is the Reserve Bank of India (RBI). is so designed as to maintain the price stability in the economy.

About Monetary Policy

- The part of the economic policy which regulates the level of money in the economy in order to achieve certain objectives.

- In INDIA,RBI controls the monetary policy. It is announced twice a year, through which RBI, regulate the price stability for the economy.

1. Slack Season policy	April-September
2.Busy Season Policy	October- March

Importance of Monetary Policy

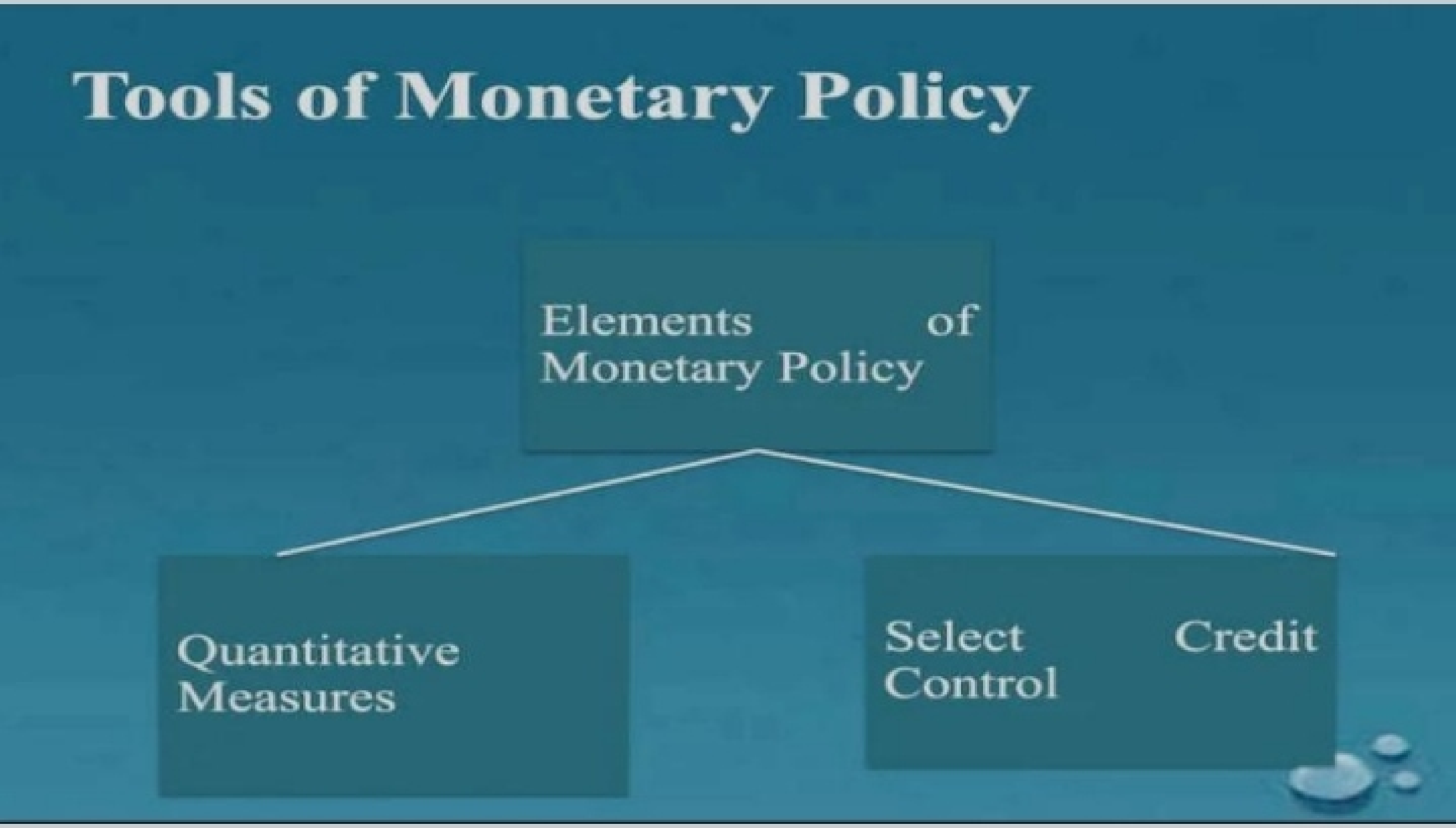
- Gross National Product (GNP) = C + I + G + X

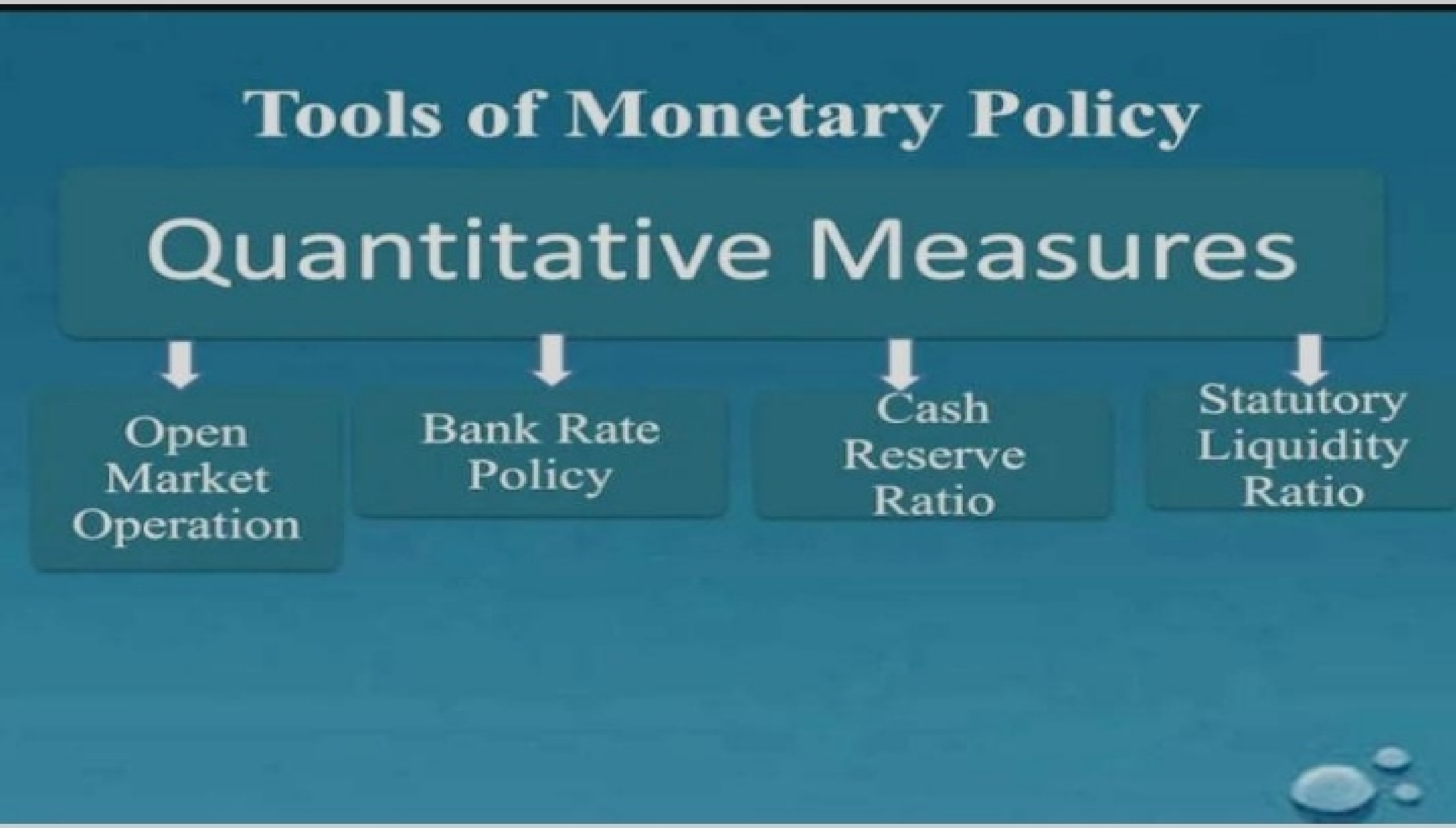
Where: C = Private Consumption expenditure
I = Private Investment Expenditure
G = Government Expenditure
X = Net Exports

- C, I, X can be influenced by the monetary policy which can also influence the private consumption and investment spending and exports and imports.

Objectives of Monetary Policy

- Price Stability
- Controlled Expansion Of Bank Credit
- Promotion of Fixed Investment
- Restriction of Inventories
- Promotion of Exports and Food Procurement Operations
- Desired Distribution of Credit
- Equitable Distribution of Credit
- To Promote Efficiency
- Reducing the Rigidity


Tools of Monetary Policy
Elements of Monetary Policy
Quantitative Measures
Select Credit Control


Tools of Monetary Policy
Quantitative Measures
Open Market Operation
Bank Rate Policy
Cash Reserve Ratio
Statutory Liquidity Ratio

Tools of Monetary Policy

ƒ Open Market Operations:

- An open market operation is an instrument of monetary policy which involves buying or selling of government securities from or to the public and banks.
- This mechanism influences the reserve position of the banks, yield on government securities and cost of bank credit.
- The RBI sells government securities to contract the flow of credit and buys government securities to increase credit flow.
- Open market operation makes bank rate policy effective and maintains stability in government securities market.

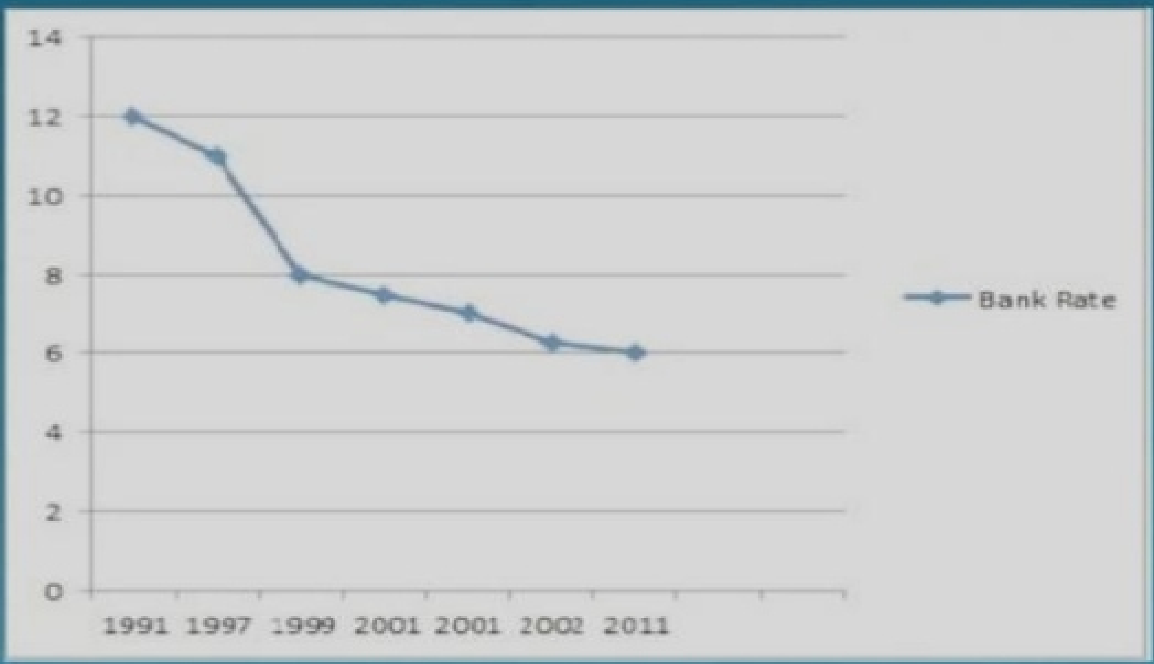
Bank Rate Policy:

- The bank rate, also known as the discount rate, is the rate of interest charged by the RBI for providing funds or loans to the banking system.
- This banking system involves commercial and co-operative banks, Industrial Development Bank of India, IFC, EXIM Bank, and other approved financial institutes.
- Funds are provided either through lending directly or rediscounting or buying money market instruments like commercial bills and treasury bills.

Tools of Monetary Policy

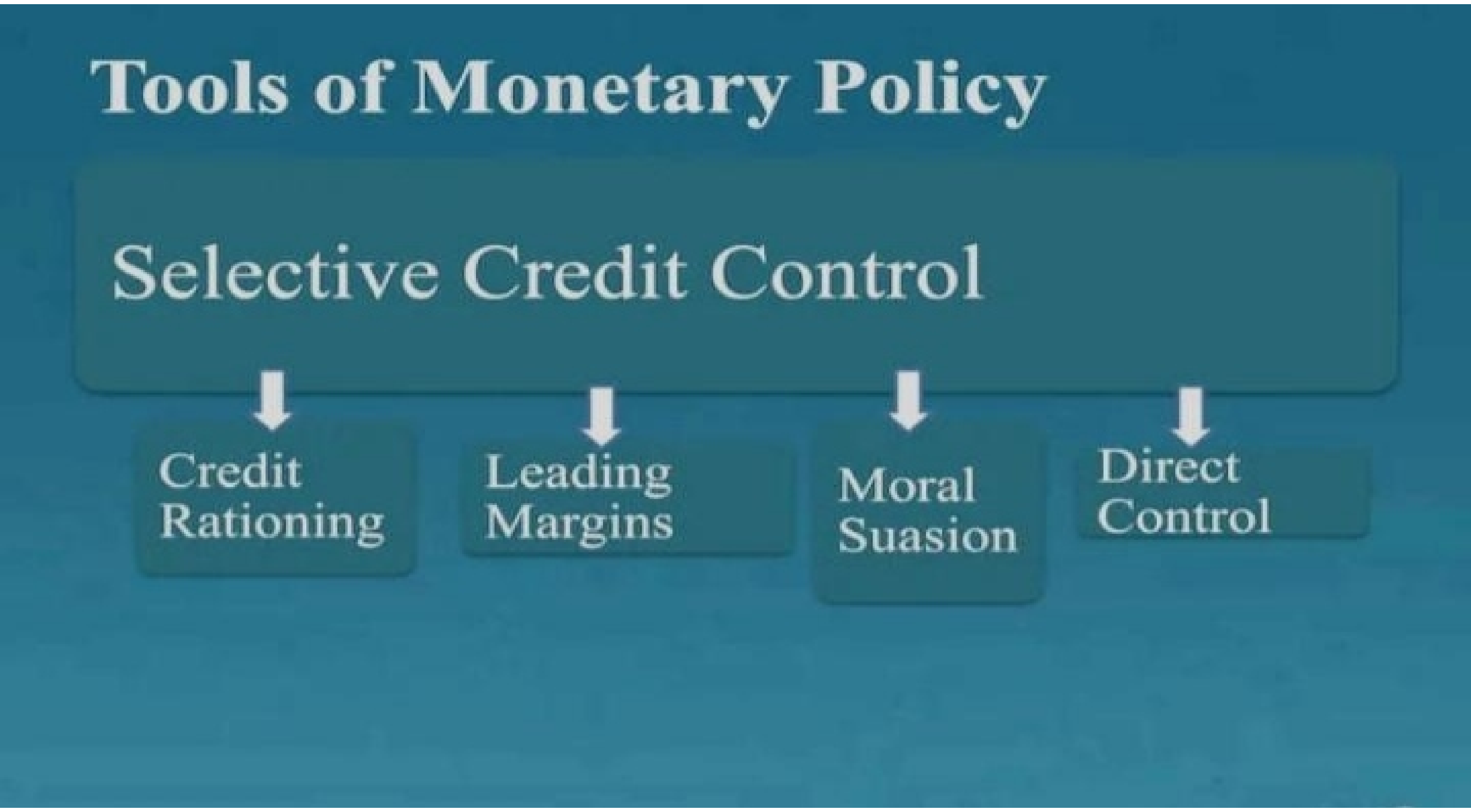
- Increase in Bank Rate increases the cost of borrowing by commercial banks which results into the reduction in credit volume to the banks and hence declines the supply of money.
- Increase in the bank rate is the symbol of tightening of RBI monetary policy.
- As of 1 January 2013, the bank rate was 8.75% and as on 29 October 2013 bank rate is 8.75%

Tools of Monetary Policy



Tools of Monetary Policy

- Cash Reserve Ratio:
  - Cash Reserve Ratio is a certain percentage of bank deposits which banks are required to keep with RBI in the form of reserves or balances .
  - Higher the CRR with the RBI lower will be the liquidity in the system and vice-versa.
  - RBI is empowered to vary CRR between 15 percent and 3 percent.


Tools of Monetary Policy
Selective Credit Control
Credit Rationing
Leading Margins
Moral Suasion
Direct Control

Tools of Monetary Policy

- Credit Rationing:
  - Under this method there is a maximum limit to loans and advances that can be made, which the commercial banks cannot exceed.
  - RBI fixes ceiling for specific categories. Such rationing is used for situations when credit flow is to be checked, particularly for speculative activities.
  - Minimum of'Capital:Total Assets" (ratio between capital and total asset) can also be prescribed by Reserve Bank of India

Tools of Monetary Policy

- Leading Margins/ Marginal Requirement:
  - Marginal Requirement of loan = current value of security offered for loan-value of loans granted.
  - The marginal requirement is increased for those business activities, the flow of whose credit is to be restricted in the economy.
  - e.g.- a person mortgages his property worth Rs. 1,00,000 against loan.

Tools of Monetary Policy

- The bank will give loan of Rs. 80,000 only.
- The marginal requirement here is 20%.
- In case the flow of credit has to be increased, the marginal requirement will be lowered.
- RBI has been using this method since 1956.

Current monetary policy of India

On October 4 during the first monetary policy committee meet Urjit Patel as a governor of RBI has announced some of the major decisions taken for the change in some instruments of monetary policy which involves the Policy **Repo rate** , **Reverse repo rate** under liquidity adjustment facility (LAF) **Marginal standing facility** (MSF) rate and the **Bank rate**

THANK YOU