Monetary Policy Goals for Economic Stability in India

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Abstract

This paper focused on the goals of monetary policy on how to take action to reduce the inflation rate and achieve economic stability in India. The monetary policy the arm of public policy the usual goals of monetary policy are to achieve full employment, to achieve a high rate of economic growth, and to stabilize prices and wages, to maintain equilibrium the balance of payment, influencing the cost and availability of credit and increasing the repo rate by central bank and Government of India. Every country needs to achieve price stability in economic development. The inflation rate below close to 2% is low enough to allow the economy to benefit fully from price stability and avoid deflation risk and, beyond the level of inflation above 3% to 10% in any economy of the country, it's harmful to the economy. Present India's consumer price inflation rate was (CPI) 4.06% and the wholesale inflation rate of (WPI) 2.03% in the Financial Year of 2021. According to Econometric models estimated in 2021, India's inflation rate is projected around 5.5%.

In this study, we study whether inflation is an effective tool for controlling inflation and achieving economic stability in India?

Keywords: Monetary Policy, Inflation Rate, Economic Stability, Economic Growth, Repo Rate, Central Bank and Deflation Risk.

Introduction

Monetary policy in India is an adjunct to economic policy. As such, the objective of monetary policy is not different from the objectives of economic policy. The three major objectives of economic policy in India have been growth, social justice, and price stability. The Government of India tries to manipulate its monetary policy through the Reserve Bank of India, which the monetary authority in the country. The monetary policy of the Reserve Bank has been characterized as one of controlled monetary expansion. Its money to meet the requirements of different sectors of the economy to accelerate the pace of economic growth.

Meaning of Monetary Policy

Monetary Policy refers to "the credit control measures adopted by the central bank of a country".

Johnson defines monetary policy "as policy employing central bank's control of the supply of money as an instrument for achieving the objectives of general economic policy."

G.K. Show defines it as "any conscious action undertaken by the monetary authorities to change the quantity, availability or cost of money."

The History of Monetary Policy

Monetary Policy is as old as the monetary system or as money itself. It has a long and chequered history since the days of mercantilism. Evidence proves the existence of management in Greece.

But before 1914, the whole thinking about monetary policy was based upon the idea of an automatic gold exchange system. After World War I, the Gold exchange standard collapsed, and it is then the modern genesis of monetary policy that took the pace of economic growth.

The origin of monetary management in India can be traced back to time immemorial. The reference about the *Panis, the Moneylenders of Southern India, in Rig* Veda is evidence of the developed state of Banking or credit system in the Vedic Age, although the date of the coins and credit instruments is lost amid antiquity. In the Mauryan era, the system of currency, credit, and coinage was fully developed. Kautilya devotes a chapter classical the Arthashastra on rules for mining and credit.

History of money management and policy based on central banking practices in India can be traced to as far back as January 1773, when Lord Hastings, the then Governor, and later on, the first Governor-general of British of India, placed before the Board of Revenue his plan for General Bank in Bengal and Bihar. The Royal Commission on Indian Financial and are currency, also known as the Chamberlain Commission, was set in 1913 with J M Keynes as one of the members who prepared a blueprint for the establishment of an Imperial Bank of India.

The Bank came into existence in January 1921 by amalgamating the three presidency banks as a commercial bank with some of the functions of the central banks also. In August 1925, the Royal Commission on Indian Currency and Finance was appointed to represent the Hilton Young Commission.

The Commission observed that India was the only big trading country in which the currency and note issues were under direct government. It suggested several measures to reform the monetary system. The Reserve Bank of India was established by the Reserve Bank of India

Act of 1934, with the recommendations of the Young Commission and the Central Bank Inquiry Committee (1931).

Objective of the Study

1. To study the Role of Monetary Policy Goals for Economic stability in India.
2. To know the study of Is Monetary Policy's really helpful instrument of controlling Inflation and achieve economic stability in India?
3. To know the study of the Current Situation of the Inflation Rate in India.

Data Source & Methodology

This study is merely based on Secondary data, which are collected from RBI Bulletin, RBI occasional papers, RBI Annual Report, Economic Survey, Google scholars, website, www.statista.com, etc.

Scope of the Study

Thus the study examines the role of monetary policy goal for Economic stability in India. To find out the monetary policy is a helpful instrument to controlling price fluctuation and achieve Economic growth and stability in India.

Objectives or Goals of Monetary Policy

The main objectives of monetary policy are:

Full Employment: Full employment is standardized in the main objectives of monetary policy. This is an essential goal, not only because unemployment leads to waste of production, but also because of loss of social standing and self-esteem.

Price Stability: One of the policy objectives of monetary policy is to ensure price levels. Both economists and the downtrodden support this policy, as price fluctuations bring uncertainty and uncertainty to the economy.

Economic Growth: One of the most important objectives of monetary policy in recent years has been the rapid economic growth of an economy. Economic growth is defined as "the process whereby the real per capita income of a country increases over a long period".

Balance of Payment: Another goal of monetary policy since the 1950s is to maintain a balance in payments.

Targets and Instruments of Monetary Policy

The tools of monetary policy are of two types

A. Quantitative Credit Control Methods (General or Indirect method) and

B. Qualitative Credit Control Methods (Selective or Direct)

They affect the level of aggregate demand through the supply of money, the cost of money, and the availability of credit.

A. Quantitative Credit Control Methods

In India, the legal framework on the credit structure of the Reserve Bank is provided under the Reserve Bank Act 1934 and the Bank Regulation Act 1949. Quantitative credit control is used to maintain a proper quantity of Credit or money supply in the market. Some Important Credit Control Systems

The first category includes bank rate variation, open market operations and balance requirements.

- Bank Rate Policy
- Open Market Operations
- Cash Reserve Ratio
- Statutory Liquidity Ration
- Cash Reserve Ratio
- Repo Rate
- Reserve Ratio Rate

B. Qualitative Credit Control Methods

Under selective Credit Control is provided to selected borrowers for selected purposes.

- Ceiling on Credit
- Margin Requirements
- Discriminatory Interest Rate (DIR)
- Directives
- Direct Action

Review of Monetary Policy Since 2016

Table 1: Movements in Bank Rate (BR) during 2016- 2020

Year	Effective Since	Bank Rate (In %)
2015-2016	2016 Sep	7.00
	2016 Oct	6.25
2016-2017	2017 Sep	6.25
	2017 Oct	6.25
2017-2018	2018 Sep	6.75
	2018 Oct	6.50
2018-2019	2019 Sep	5.40
	2019 Nov	5.40
2019-2020	2020 Sep	4.25
	2020 Nov	4.25

Source: *Labour Bureau, Govt. of India, Ministry of Labour and Employment & RBI Annual Report 2016-20*

Table 2: Movements in Cash Reserve Ratio (CRR) during 2016- 2020

Year	Effective Since	Bank Rate (In %)
2015-2016	2016 Sep	4.00
	2016 Oct	4.00
2016-2017	2017 Sep	4.00
	2017 Oct	4.00
2017-2018	2018 Sep	4.00
	2018 Oct	4.00
2018-2019	2019 Sep	4.00
	2019 Nov	4.00

2019-2020	2020 Sep	3.50
	2020 Nov	3.50

Source: *Labour Bureau, Govt. of India, Ministry of Labour and Employment & RBI Annual Report 2016-20*

Table 3: Movements in Reverse Repo Rate (RRR) during 2016- 2020

Year	**Effective Since**	**Bank Rate (In %)**
2015-2016	2016 Sep	6.25
	2016 Oct	5.75
2016-2017	2017 Sep	5.75
	2017 Oct	5.75
2017-2018	2018 Sep	6.25
	2018 Oct	6.25
2018-2019	2019 Sep	4.90
	2019 Nov	4.90
2019-2020	2020 Sep	3.35
	2020 Nov	3.35

Source: *Labour Bureau, Govt. of India, Ministry of Labour and Employment & RBI Annual Report 2016-20*

Table 4: Movements in Statutory Liquidity Rate (SLR) during 2016- 2020

Year	**Effective Since**	**Bank Rate (In %)**
2015-2016	2016 Sep	20.75
	2016 Oct	20.00
2016-2017	2017 Sep	19.50
	2017 Oct	19.50
2017-2018	2018 Sep	19.50
	2018 Oct	19.50
2018-2019	2019 Sep	18.50
	2019 Nov	18.50
2019-2020	2020 Sep	18.00
	2020 Nov	18.00

Source: *Labour Bureau, Govt. of India, Ministry of Labour and Employment & RBI Annual Report 2016-20*

Table 5: Movements in Repo Rate (RR) during 2016- 2020

Year	**Effective Since**	**Bank Rate (In %)**
2015-2016	2016 Sep	6.50
	2016 Oct	6.25
2016-2017	2017 Sep	6.00
	2017 Oct	6.00
2017-2018	2018 Sep	6.50
	2018 Oct	6.50
2018-2019	2019 Sep	5.15
	2019 Nov	5.15
2019-2020	2020 Sep	4.00
	2020 Nov	4.00

Source: *Labour Bureau, Govt. of India, Ministry of Labour and Employment & RBI Annual Report 2016-20*

Table 6: Annual Rate of Inflation of Consumer Price Index (CPI) during 2016- 2020

Year	Effective Since	Bank Rate (In %)
2015-2016	2016 Sep	4.4
	2016 Oct	4.2
2016-2017	2017 Sep	3.3
	2017 Oct	3.6
2017-2018	2018 Sep	3.4
	2018 Oct	2.3
2018-2019	2019 Sep	4.6
	2019 Nov	5.5
2019-2020	2020 Sep	5.0
	2020 Nov	6.2

Source: *Labour Bureau, Govt. of India, Ministry of Labour and Employment & RBI Annual Report 2016-20*

Table 7: Annual Rate of Inflation of Wholesale Price Index (WPI) during 2016- 2020

Year	Effective Since	Bank Rate (In %)
2015-2016	2016 Sep	3.6
	2016 Oct	3.4
2016-2017	2017 Sep	2.6
	2017 Oct	3.6
2017-2018	2018 Sep	5.5
	2018 Oct	4.5
2018-2019	2019 Sep	0.2
	2019 Nov	0.6
2019-2020	2020 Sep	2.0
	2020 Nov	2.0

Source: *Labour Bureau, Govt. of India, Ministry of Labour and Employment & RBI Annual Report 2016-20*

Table 8: Annual Rate of Inflation of Consumer Price Index (CPI) from during 2016- 2020

Year		For Industrial Workers Base 2016-2020	For Rural Employees Base 2016-2020	For Agriculture Workers Base 2016-2020
Base year		CPI	CPI	CPI
2016	Sep	277	877	873
	Oct	278	881	876
2017	Sep	284	985	893
	Oct	287	907	901
2018	Sep	300	917	910
	Oct	301	920	913
2019	Aug	320	92	965
	Sep	322	983	976
2020	Apr	332	1019	1014
	May	338	1025	1019

Source: *Labour Bureau, Govt. of India, Ministry of Labour and Employment & RBI Annual Report 2016-20*

Table 9: Movements in Key Policy Rates (in %), and CPI in India during 2016- 2020

Year	Effective Since	CPI	WPI	Reserve Repo Rate	Repo Rate	CRR
2016	Sep	4.4	3.6	6.25	6.50	4.00
	Oct	4.2	3.4	5.75	6.25	4.00
2017	Sep	3.3	2.6	5.75	6.00	4.00
	Oct	3.6	3.6	5.75	6.00	4.00
2018	Sep	3.4	5.5	6.25	6.50	4.00
	Oct	2.3	4.5	6.25	6.50	4.00
2019	Sep	4.6	0.2	4.90	5.15	4.00
	Nov	5.5	0.6	4.90	5.15	4.00
2020	Apr	5.0	2.0	3.35	4.00	3.50
	May	6.2	2.0	3.35	4.00	3.50

Source: *National Statistical Office, Ministry of Statistics and Programme Implementation, Government of India & RBI Annual Report 2016-20*

The movements in key policy rates in percentage value, WPI and CPI in India are shown in Table-9. It reveals the rate of changes in monetary activity and the corresponding response in WPI and CPI in India from 2016 to 2020. There are frequent changes in CRR, Repo rate, and Reserve Repo rates along with changes in the price level.

Price Fluctuation

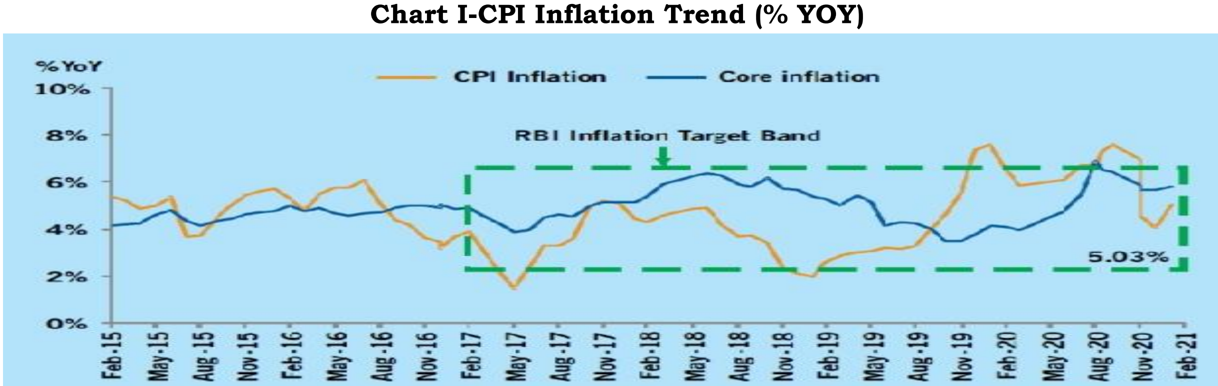
On the whole, these divergent movements caused CPI headline Inflation outcomes to manage overshoot inflation projections.

Consumer price Inflation registered from November to February 2021. Underpinned by a pickup in food inflation, particularly in Vegetables and protein-based items. Inflation excluding food and fuel has softened since March growth in organized sectors staff cots showed divergent movement. They were rising for the manufacturing sectors and remaining range-bound for the service sectors. Over the last six months, November to February 2021, CPI Inflation trailed below the target of 5.0% Averaging 3.4% over this period. The Monetary Policy Report (MPR) of February 2021 had projected CPI inflation at 5.1%.

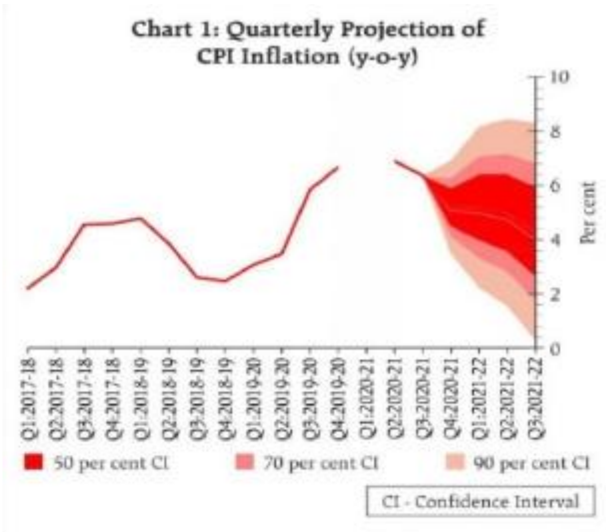
Consumer Prices

While food Prices moved out of deflation as anticipated, the summer rise in prices of vegetables this year. The Indian basket of crude oil prices eased unexpectedly from averaging of US $67 barrel from 2020 to 2021.

Chart I-CPI Inflation Trend (% YOY)



CPI Inflation is now projected at 5.0% in Q4 FY 21; 5.2% in Q1 FY 22, 5.2% in Q2 FY 22, 4.4% in Q3 FY 22 and 5.1% in Q4 FY 22, with risks broadly balanced.



The distribution of inflation across CPI shows a considerable drop in the median inflation rate from 4.3% in 2019 to 3.6% in 2020; moreover, the negative skew in inflation in 2019 and 2020 resulting from food prices was absent in 2020. Difficulties indices of month-on-month Price changes in CPI items on seasonally adjusted basis moderation during June to August 2020 across both goods and services categories.

Conclusion

The study was an attempt to analyze the role of the Monetary Policy goal for Economic stability in India. To find out their effectiveness in the Indian context, especially to achieve Economic stability and managing price stability through control Instrument of Monetary Policy. The use and Importance of Monetary weapons like Bank Rate, CRR, SLR, Repo Rate & Reserve Rate have increased over the year. Repo and Reverse Repo rate the most frequently used monetary technique in recent years. The rates are varied mainly to control inflation and absorb the excess liquidity and hence to maintain price stability in the economy.

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