

# Monetary Policy

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RESERVE BANK OF INDIA



- Monetary policy refers to the policy of the central bank with regard to the use of monetary instruments under its control to achieve the goals specified in the Act.
- The Reserve Bank of India (RBI) is vested with the responsibility of conducting monetary policy. This responsibility is explicitly mandated under the Reserve Bank of India Act, 1934

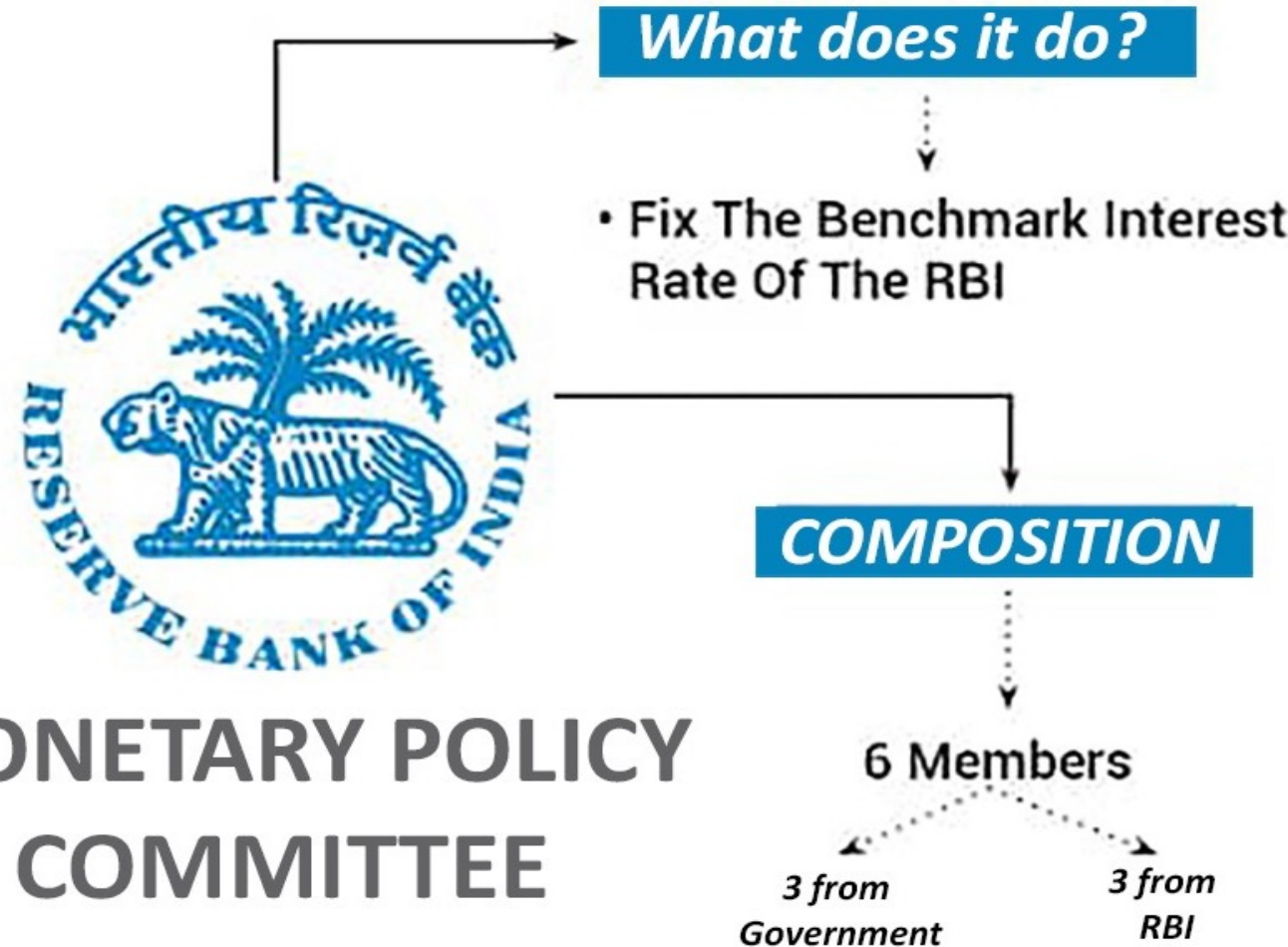
# Objectives of Monetary Policy

Inflation

Unemployment

Currency  
exchange rates

# The PROCESS



## MONETARY POLICY COMMITTEE

Which of the following statements is/are correct regarding the Monetary Policy Committee (MPC)?

- (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.

Select the correct answer using the code given below :

- (a) 1 only
- (b) 1 and 2 only
- (c) 3 only
- (d) 2 and 3 only



The Reserve Bank of India was established on April 1, 1935 in accordance with the provisions of the Reserve Bank of India Act, 1934.

Though originally privately owned, since nationalisation in 1949, the Reserve Bank is fully owned by the Government of India.

Consider the following statements:

1. The Governor of the Reserve Bank of India (RBI) is appointed by the Central Government.
2. Certain provisions in the Constitution of India give the Central Government the right to issue directions to the RBI in the public interest.
3. The Governor of the RBI draws his power from the RBI Act.

Which of the above statements are correct?

- a) 1 and 2 only
- b) 2 and 3 only
- c) 1 and 3 only
- d) 1, 2 and 3

## **Monetary Authority:**

- Formulates, implements and monitors the monetary policy.
- *Objective: maintaining price stability while keeping in mind the objective of growth.*

## **Regulator and supervisor of the financial system:**

- Prescribes broad parameters of banking operations within which the country's banking and financial system functions.
- *Objective: maintain public confidence in the system, protect depositors' interest and provide cost-effective banking services to the public.*

## **Manager of Foreign Exchange**

- Manages the Foreign Exchange Management Act, 1999.
- *Objective: to facilitate external trade and payment and promote orderly development and maintenance of foreign exchange market in India.*



## **Issuer of currency:**

- Issues and exchanges or destroys currency and coins not fit for circulation.
- *Objective: to give the public adequate quantity of supplies of currency notes and coins and in good quality.*

## **Developmental role**

- Performs a wide range of promotional functions to support national objectives.

## **Regulator and Supervisor of Payment and Settlement Systems:**

- Introduces and upgrades safe and efficient modes of payment systems in the country to meet the requirements of the public at large.
- *Objective: maintain public confidence in payment and settlement system*

## **Related Functions**

- **Banker to the Government:** performs merchant banking function for the central and the state governments; also acts as their banker.
- **Banker to banks:** maintains banking accounts of all scheduled banks.

In India, the Central Bank's function as the "lender of last resort" usually refers to which of the following?

1. Lending to trade and industry bodies when they fail to borrow from other sources
2. Providing liquidity to the banks having a temporary crisis
3. Lending to governments to finance budgetary deficits

Select the correct answer using the code given below

- a) 1 and 2
- b) 2 only
- c) 2 and 3
- d) 3 only

The Reserve Bank of India regulates the commercial banks in matters of

- (1) Liquidity of assets
- (2) Branch expansion
- (3) Merger of banks
- (4) Winding-up of banks

Select the correct answer using the codes given below.

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

## Expansionary Policy

Helps in Revival of  
Economy and  
Promoting Growth  
and Investments



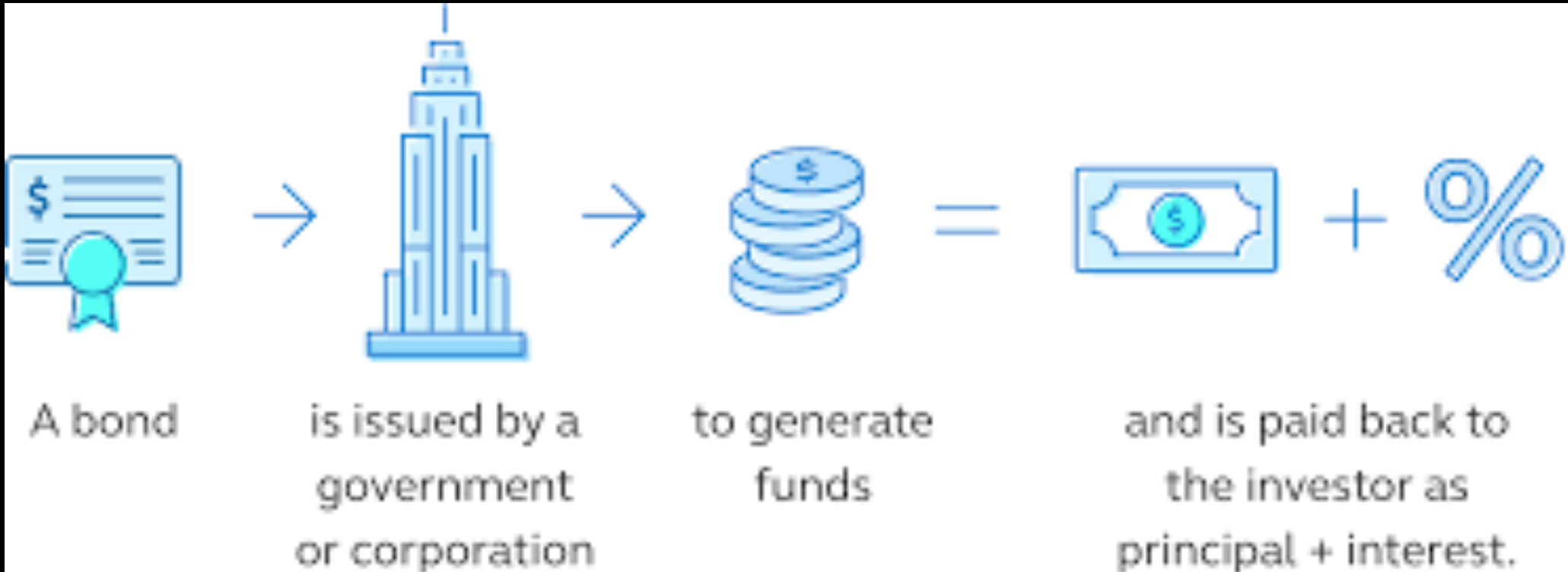
## Contractionary Policy

Helps in Fighting  
Inflation.

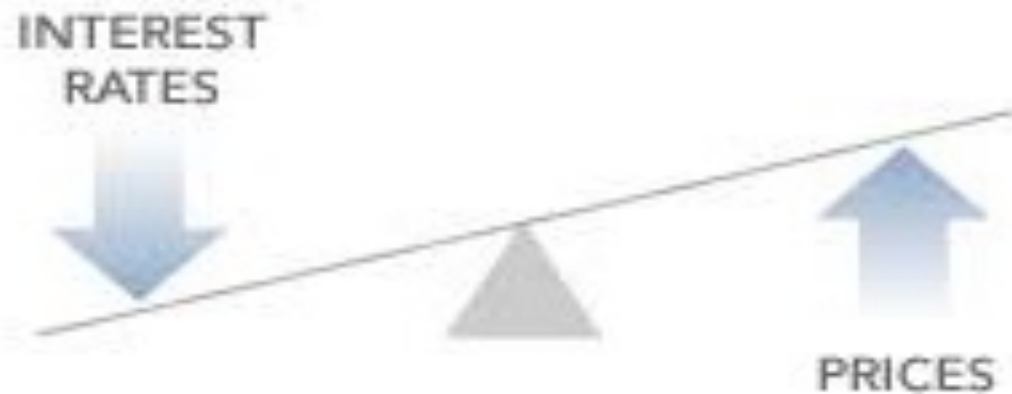
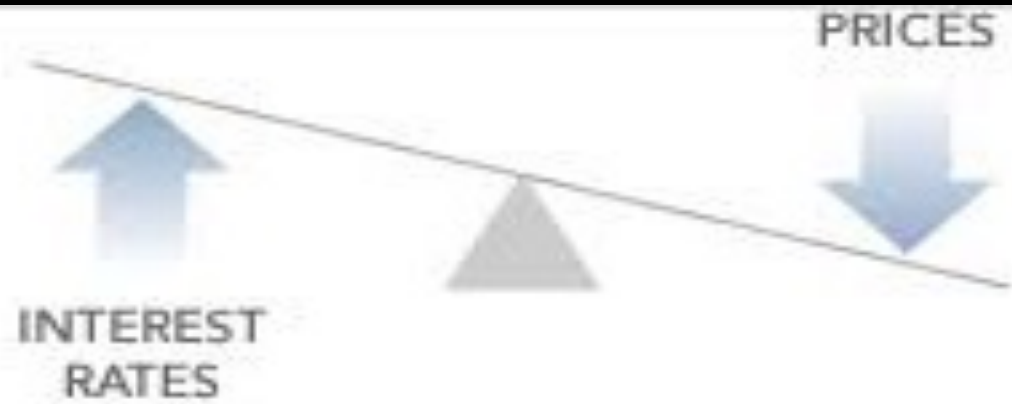


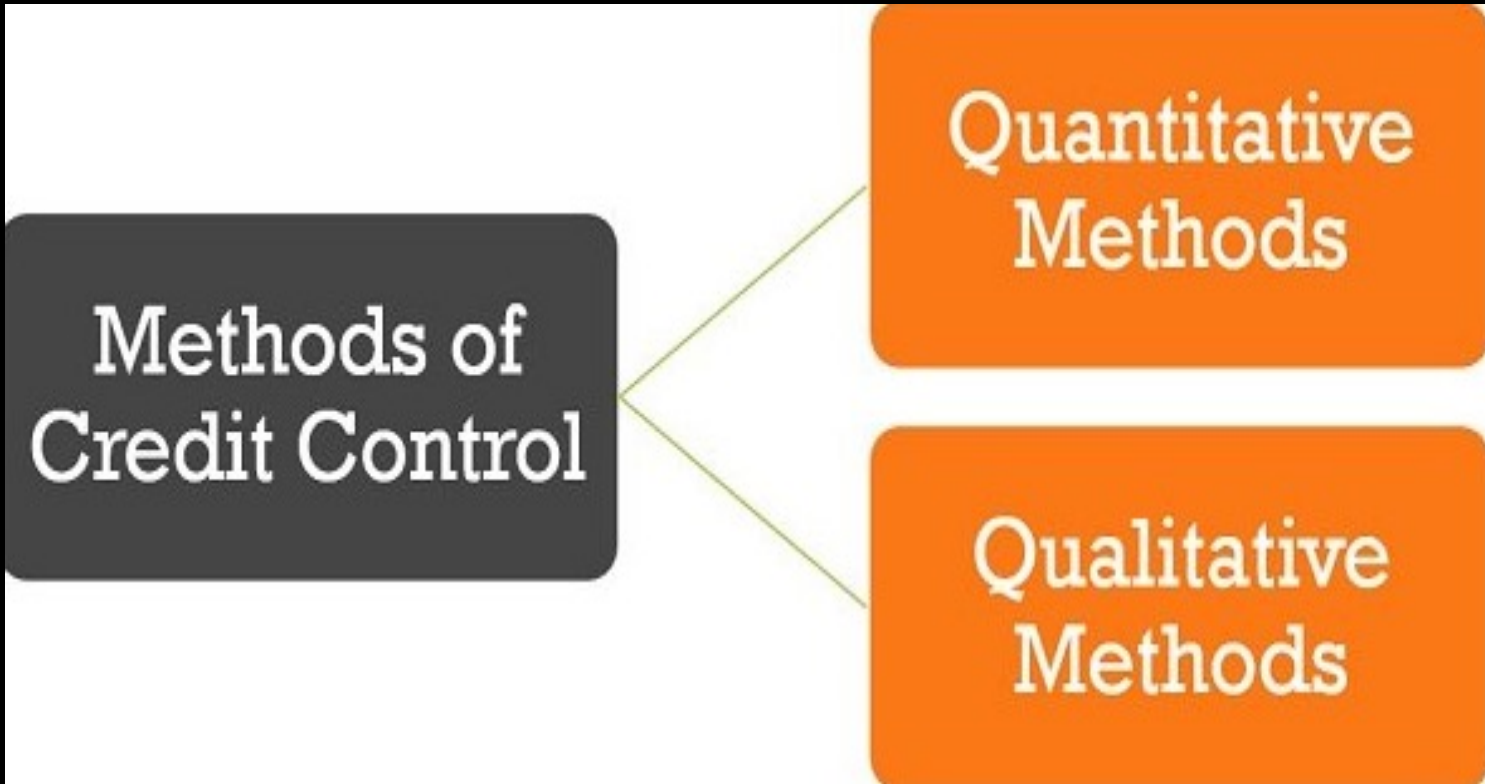
# Bonds

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# Interest Rates, Bond Prices, Bond Yield





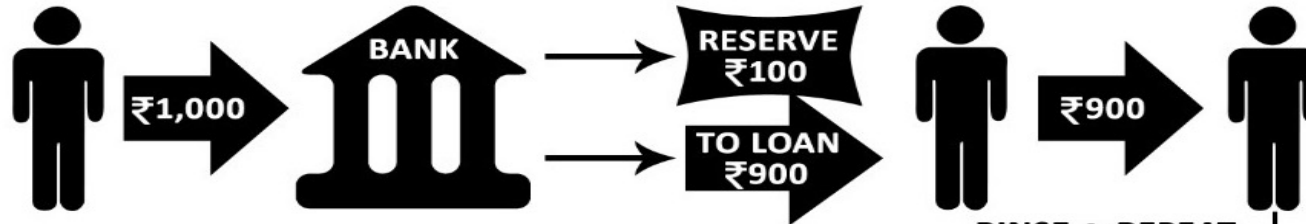


# THE BASIC FRACTIONAL RESERVE BANKING CYCLE

1. DEPOSIT

2. LOAN

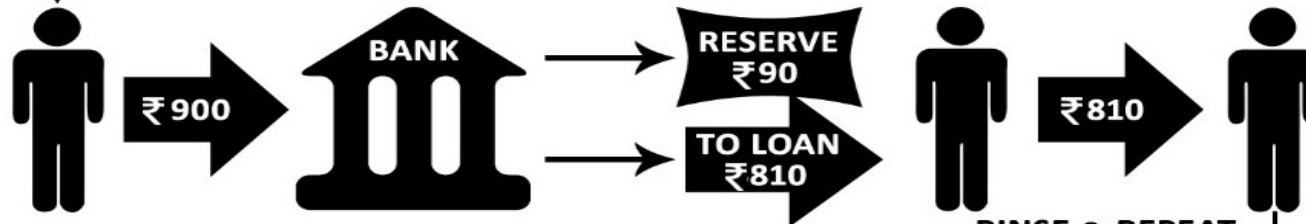
3. SPEND



AT THIS POINT THERE IS ₹1,900 IN THE SYSTEM.

THE BANK HAS ₹100.

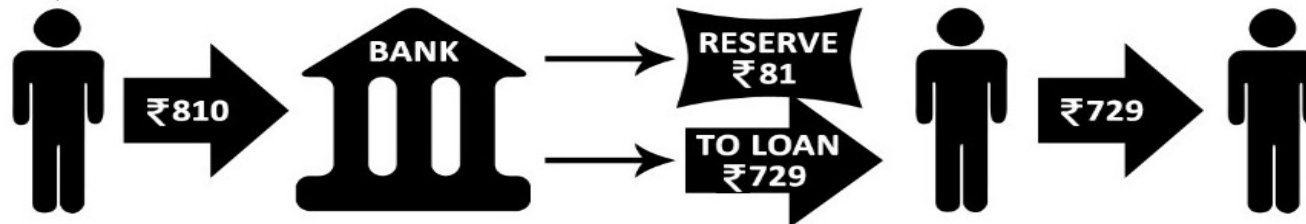
RINSE & REPEAT FROM STEP 1...



AT THIS POINT THERE IS ₹2,710 IN THE SYSTEM.

THE BANK HAS ₹190.

RINSE & REPEAT FROM STEP 1...



AT THIS POINT THERE IS ₹3,439 IN THE SYSTEM.

THE BANK HAS ₹271.

The money multiplier in an economy increases with which one of the following?

- a) Increase in the Cash Reserve Ratio in the banks.
- b) Increase in the Statutory Liquidity Ratio in the banks
- c) Increase in the banking habit of the people
- d) Increase in the population of the country

# Cash Reserve Ratio

@ 3%



Rs 10,000



Balance Rs 9700

Rs 300



# Statutory Liquidity Ratio

@ 18%





**SOVEREIGN DEBT**

**CRONY CAPITALISM**

**PUBLIC**

**BANKS**

**GOVERNMENTS**

**FINANCIAL REPRESSION**

**Your MONEY**

**Your BLOOD**

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

In the context of Indian economy; which of the following is/are the purpose/purposes of 'Statutory Reserve Requirements'?

- (1) To enable the Central Bank to control the amount of advances the banks can create
- (2) To make the people's deposits with banks safe and liquid
- (3) To prevent the commercial banks from making excessive profits
- (4) To force the banks to have sufficient vault cash to meet their day-to-day requirements

Select the correct answer using the code given below.

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

# CRR + SLR

(When CRR rate is 6% + SLR rate is 20%)



₹1000  
Deposit



₹740 Balance

Distribute as  
Individual / Corporate  
Loan

CRR ₹60 + SLR 200





With reference to the India economy, what are the advantages of “Inflation-Indexed Bonds (IIBs)”?

1. Government can reduce the coupon rates on its borrowing by way of IIBs.
2. IIGs provide protection to the investors from uncertainty regarding inflation.
3. The interest received as well as capital gains on IIBs are not taxable.

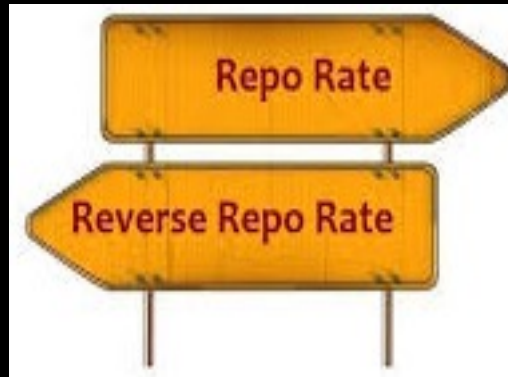
Which of the statements given above are correct?

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

# Liquidity Adjustment Facility (Repo and Reverse Repo)



# Reverse Repo Rate



# Bank Rate



An increase in the Bank Rate generally indicates that the

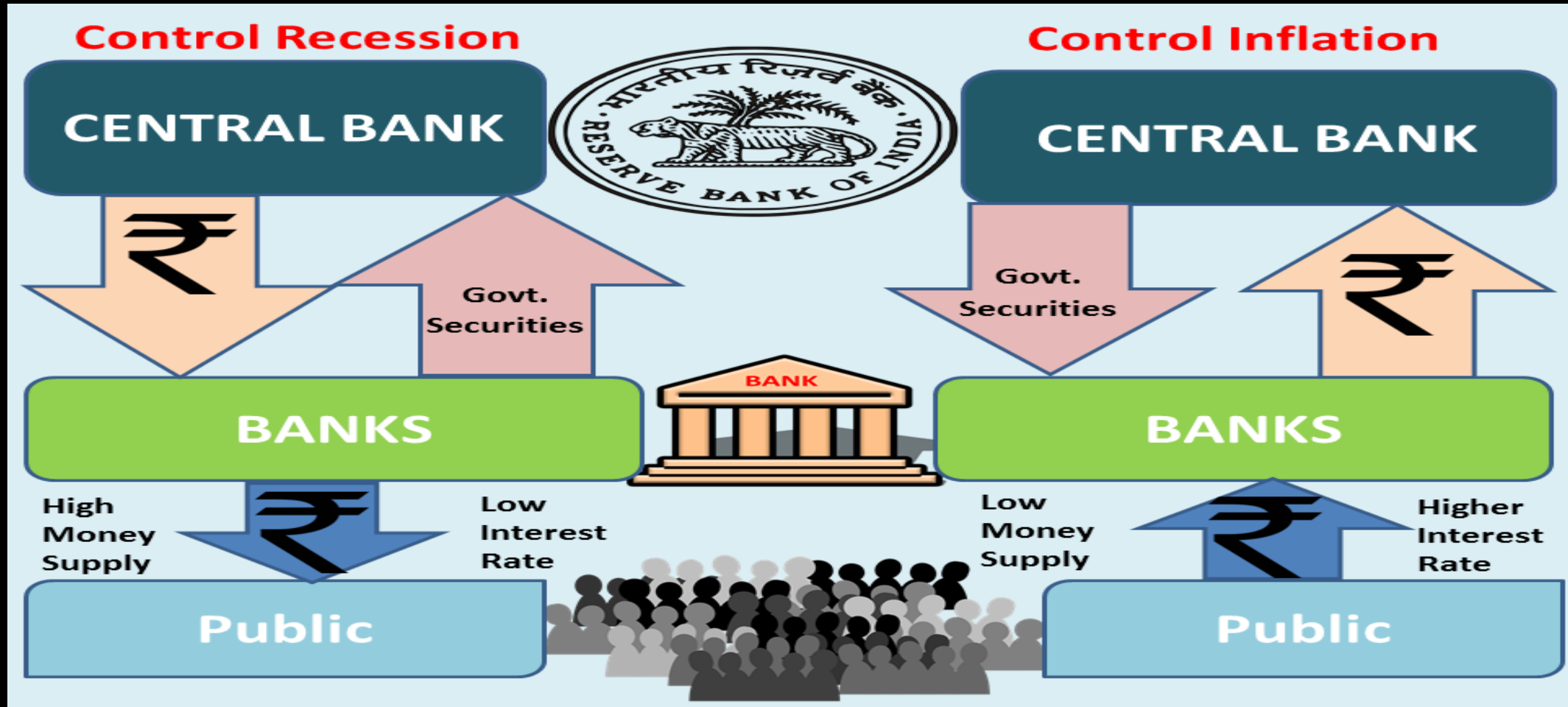
- (a) Market rate of interest is likely to fall
- (b) Central Bank is no longer making loans to commercial banks
- (c) Central Bank is following an easy money policy
- (d) Central Bank is following a tight money policy

Supply of money remaining the same when there is an increase in demand for money, there will be

- (a) A fall in the level of prices
- (b) An increase in the rate of interest
- (c) A decrease in the rate of interest
- (d) An increase in the level of income and employment

- Marginal Standing Facility(MSF)
- Standing Deposit Facility

# Open Market Operations





In the context of Indian economy, Open Market Operations' refers to

- (a) Borrowing by scheduled banks from the RBI
- (b) Lending by commercial banks to industry and trade
- (c) Purchase and sale of government securities by the RBI
- (d) None of the above

If the interest rate is decreased in an economy, it will

- (a) Decrease the consumption expenditure in the economy
- (b) Increase the tax collection of the Government
- (c) Increase the investment expenditure in the economy
- (d) Increase the total savings in the economy

If the RBI decides to adopt an expansionist monetary policy, which of the following would it not do?

- (1) Cut and optimize the Statutory Liquidity Ratio
- (2) Increase the Marginal Standing Facility Rate
- (3) Cut the Bank Rate and Repo Rate

Select the correct answer using the code given below:

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

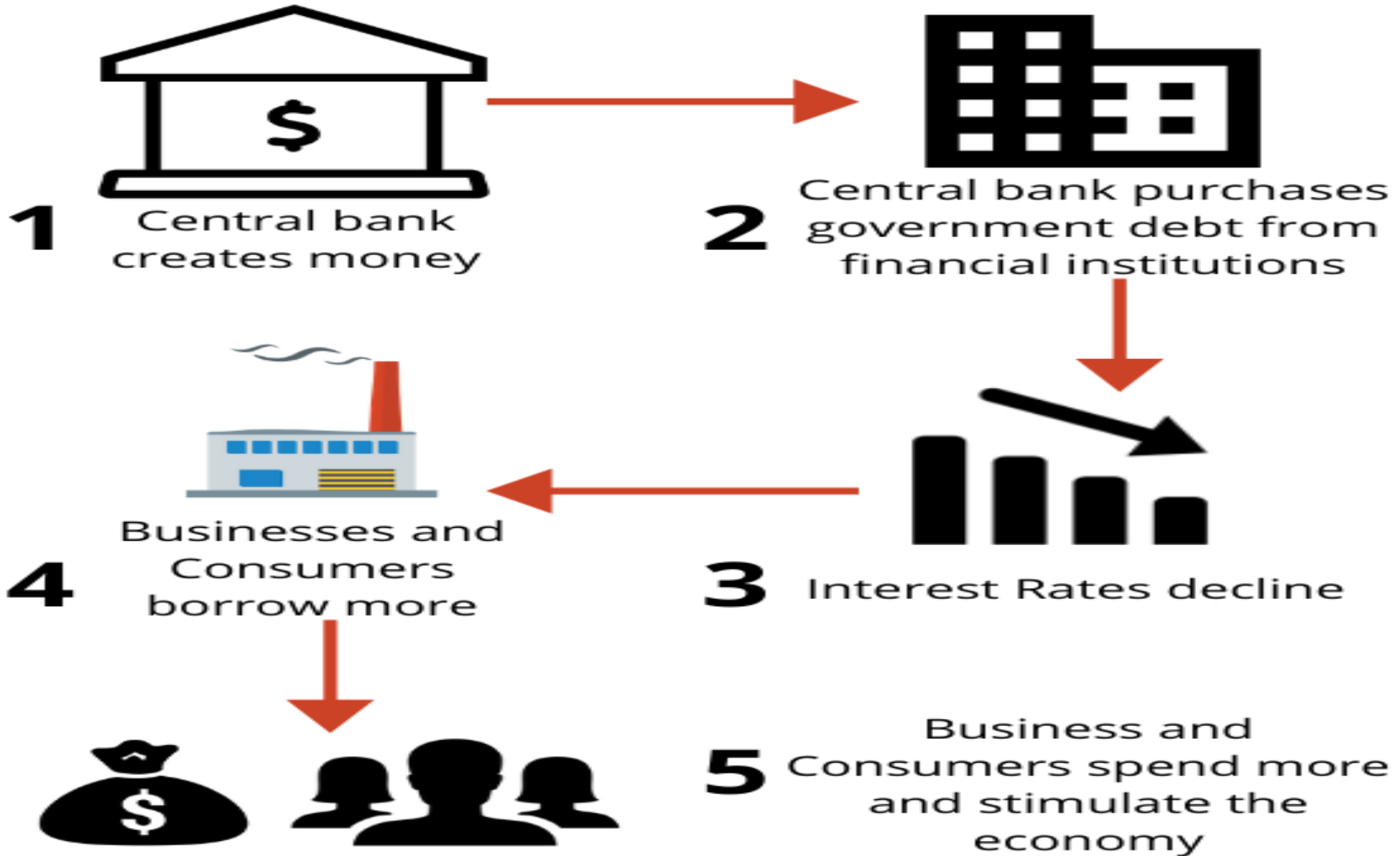
With reference to the Indian economy, consider the following

- (1) Bank rate
- (2) Open market operations
- (3) Public debt
- (4) Public revenue

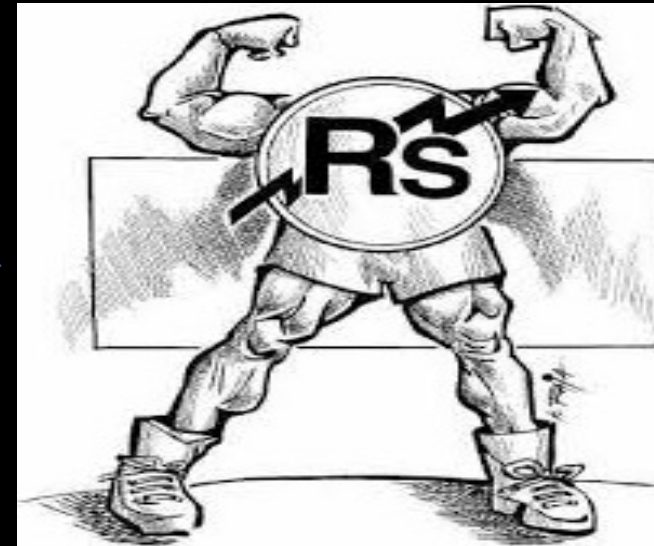
Which of the above is/are component/ components of Monetary Policy?

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

# Quantitative Easing



# When too many dollars chased too few rupees



Consequences?



# Fed Tapering



When too many dollars started leaving,



Consequences?

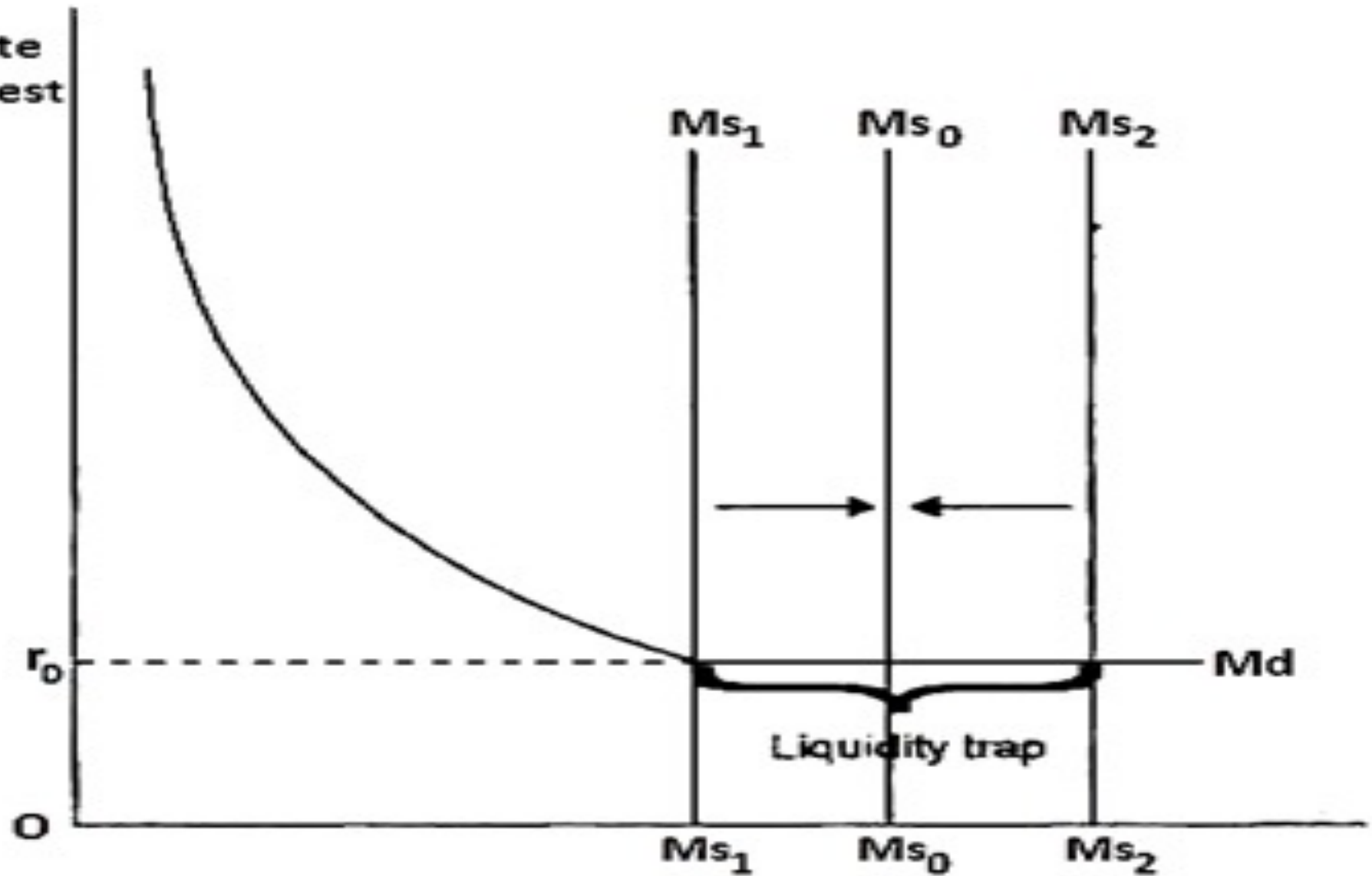




'European Stability Mechanism', sometimes seen in the news, is an

- (a) Agency created by EU to deal with the impact of millions of refugees arriving from Middle East
- (b) Agency of EU that provides financial assistance to eurozone countries
- (c) Agency of EU to deal with all the bilateral and multilateral agreements on trade
- (d) Agency of EU to deal with the conflicts arising among the member countries

The rate of interest



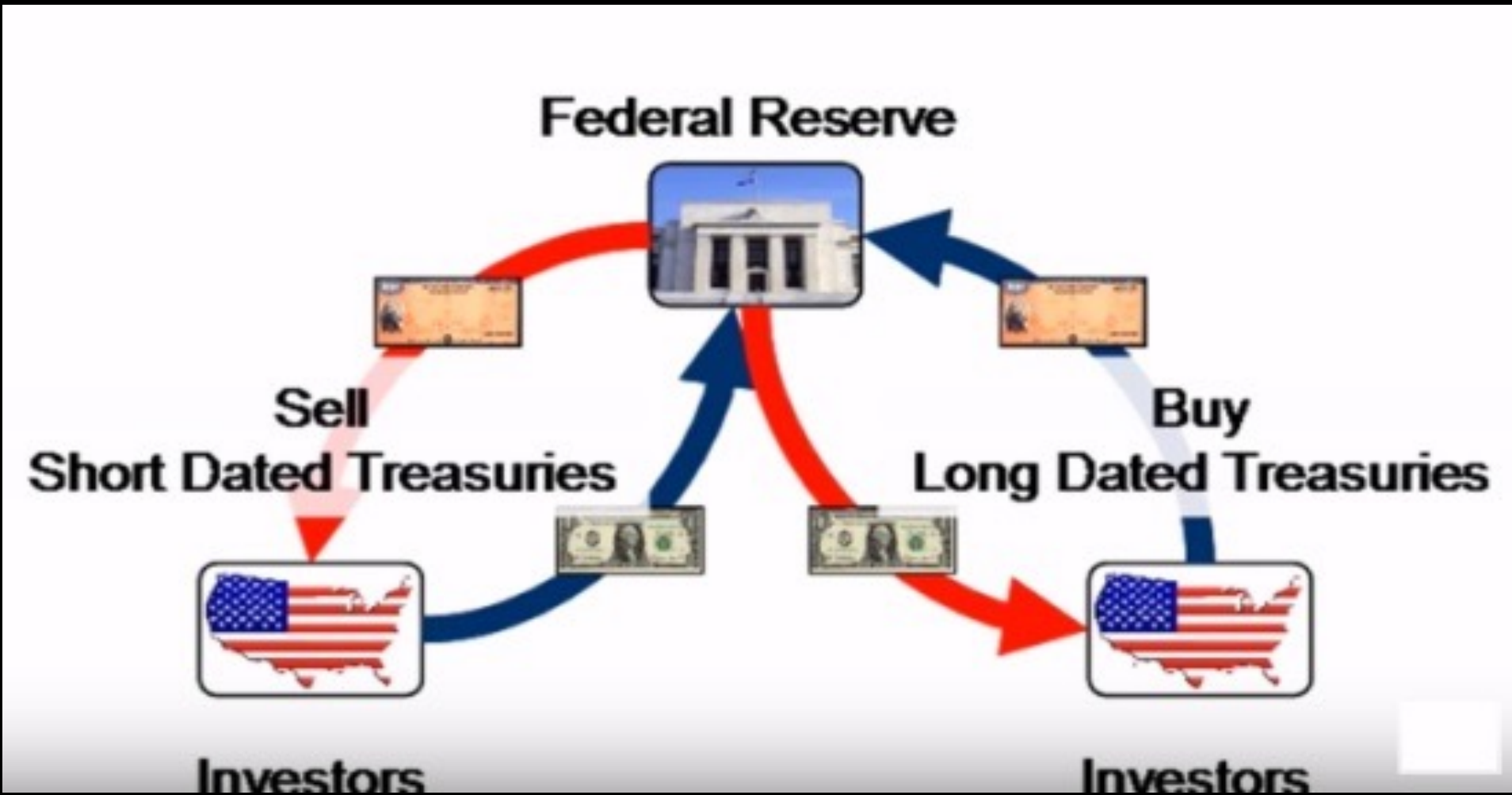


<https://t.me/econforum>

# Qualitative Tools of Monetary Policy

- Credit Rationing
- Margin Requirements
- Moral Suasion
- Regulating Consumer Credit

# Operation Twist



**Thank You**