An analysis of Impact of monetary policy in India's economic growth

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Abstract: Monetary policy helps the nation in development by monitoring pricing movements and overall economic activity especially money supply with appropriately altering the connection between the supply and demand for money. As the economy expands, so does the demand for money. The significance of monetary policy to India's economic growth is the main topic of this article. It will also assess how monetary policy has an impact on the Indian economy; effortlessly and quickly paraphrase your content. Indian economy has been growing throughout the time at a decent rate and setting an example in front of the world which can see in the data that how it tackled the rough time as well. The GDP growth and per capita income of India helping the purchasing power to grow as well which results the economics welfare too.

Keywords: Economic Growth, Monetary Policy, Indian Economy, Inflation, GDP, Per Capita.

Introduction

Monetary policy is one of the most important aspects for any economy. If we discuss about Indian economy, it has already faced many ups and downs but still surged at a decent rate but the point is where actually it was and where it is at present? Any country can't have 45 degree substantial growth curve but every economy should get inspire from this at least. If we take Indian economy into consideration it's also not an exception and had a very sluggish growth rate but fortunately by the efforts of major industries it came back on track and doing fairly good compare to others especially in pandemic times. For India the major industries includes agriculture, steel, oil and gas, telecom, metals and mining, and chemicals. After independence all mentioned industries and related sectors contributed in helping Indian economy to cover up. Let's have a look on Indian economy's performance since 1960 to present. We can see in the below graph Indian economy in 1960 was approximately 37.029 Billions of US $ and in 1990 it was

320.979 Billions of US $. The solid economic policies and great efforts by all now in 2022, the Indian economy is worth 3385.0898 Billion of US $ and we are growing at 7% rate per annum.

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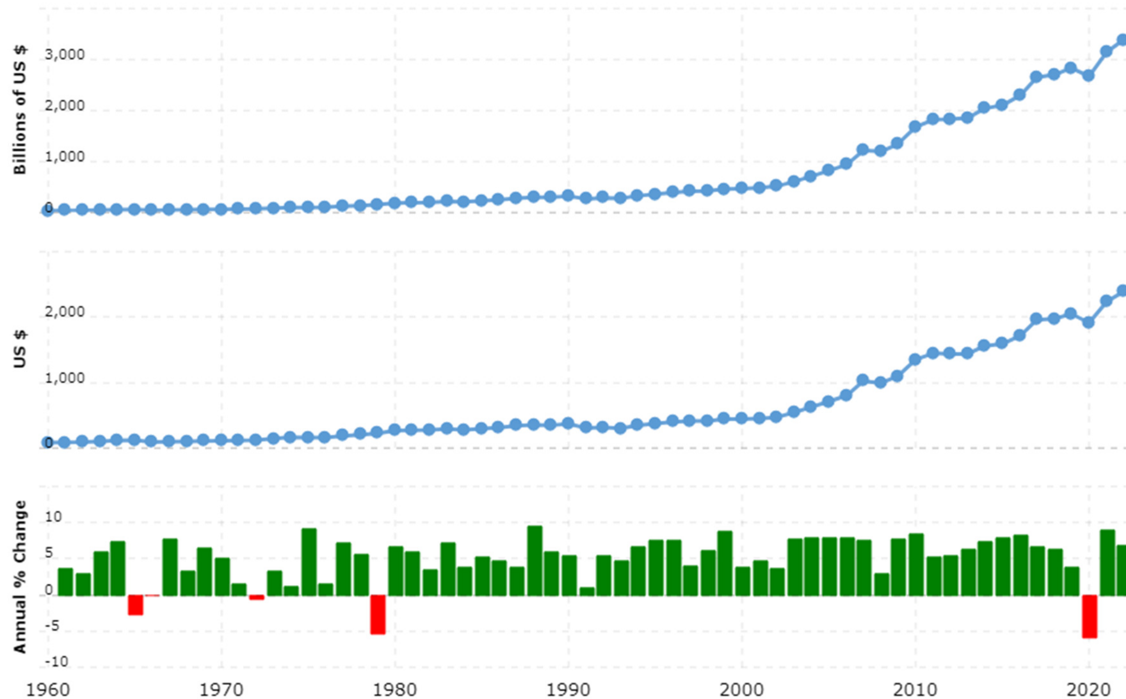

For getting the desired performance by the economy we need to have a robust cash flow and solid monetary policy to make a balance with money supply in the economy. Reserve bank of India oversees the supply of cash in financial system by the command on interest rates to produce high financial growth and sustained price steadiness. Reserve Bank of India is responsible for preserving price stability there. The following are the additional goals of monetary policy:

- Price steadiness,
- Calculated increase of bank credit,
- Encouragement of preset asset,
- constraint of inventory and stock,

[1] Data Source: World Bank

https://www.macrotrends.net/countries/IND/india/gdp-gross-domestic-product'>India GDP 1960-2023.

- effective promotion,
- Reduction of inflexibility.

Cost steadiness

Very basic goal of price steadiness is to continue a decent level of stability in order to make sure that projects develop quickly and are supported by favorable environments.

Controlled Bank Credit Expansion

The RBI primarily works to limit the increase of bank credit and the money supply, taking into account seasonal credit needs without having an impact on output.

Restriction on Stocks and Inventories

This strategy was developed to prevent excessive stocking and wasteful spending within the company. The unit was getting sick because of the additional stock that was offered there that was becoming out of date.

To Increase Effectiveness

As a result of this approach, central banks are now much more cautious when it comes to their systems and transactions. They are now able to derestricted many of the functions of the as introducing new money market instruments, loosening up operating controls in the credit distribution system, etc. Additionally, they attempted to make some structural adjustments that would benefit their organization over the long term.

Lessening Rigidity

The Reserve Bank of India assists banks by providing some operational flexibility that enables the bank to function autonomously. These options for flexibility foster competition and promote growth. Regular control-keeping also ensures that the highest level of caution and discipline is maintained in the financial system's activities.

Financial policy board

Reserve Bank of India Act, 1934 was amended by the Finance Act, 2016 in order to give the Monetary Policy Committee legal and historical context. These modifications aimed to increase growth and maintain stable prices. The committee is tasked with achieving a particular target

level and serves as the benchmark setter for the policy rate (repo rate). RBI Act mandates that three of the six RBI members serve on MPC, with the remaining three members being assigned by the Government.

Government of India said to central bank that "Inflation Target" for the phase starting from the publishing day of the announcement and ending on March 31, 2021, will be 4 % in a Gazette of India Extraordinary dated August 5, 2016. At the same time, it was announced that the tolerance levels would only be 2% and 6%, respectively.

Tools for monetary policy

The following tools are used to manage the stream of money through the financial system:

- Open Market Operations,
- Statutory Liquidity Ratio (SLR),
- Cash Reserve Ratio (CRR),
- Credit Ceiling,
- Credit Authorization Scheme,
- Moral Suasion,
- Repo Rate and
- Reverse Repo Rate,
- Bank Rate Policy

Important indicators

As of Oct, 2023, the main indicators are:

Indicator	Current Rate
Inflation (CPI)	6.20%
MSF(Marginal Standing Facility) Rate	6.75%
CRR	4.50%
SLR	18%
Bank rate	6.75%
Reverse Repo Rate	3.35%
Repo Rate	6.5%
GDP growth rate	7%

Source: https://rbi.org.in/home.aspx, ***https://www.rbi.org.in***

Monetary policy's role in India's economic growth

Following are some ways that monetary policy has a role in a nation's economic growth:
Proper balancing of the supply and demand of money

- Prices must be stable,
- Credit must be controlled,
- Financial institutions must be established and expanded,
- An appropriate interest rate structure must be in place,
- Debt management must be done.

Appropriate balancing of the supply and demand of money

The increasing demand for money can be used to gauge economic development. When a nation's population grows and its per capita income rises, more money is needed to conduct day-to-day transactions. Additionally, if the monetary authority gives the industries more money than they need, this will impede national development and lead to inflation.

For preventing economic oscillations and create the conditions for quick growth, the financial authority must maintain a stability in the demand for and supply of wealth.

Cost stability

For a nation to have economic growth, price stability is essential. The stability of exchange rates and domestic pricing levels must be maintained at all costs. If the monetary authority does not act, it will cause inflationary pressures in developing nations.

Credit Management

Long term credits are given to companies and industrialized sectors to suit the credit demands, while short term credits are primarily given to businesspeople and dealers. By making distinctions among the expenditure and accessibility of credit in various companies and industries, specific credit system must be developed to stimulate the plan of investment and manufacturing.

Development and Growth of Financial Institutions

The Central Bank must give the issue of rural finance special attention. Rural residents' needs for credit can be met in large part by a system of cooperative credit societies. Business and industry

will be financed by the Central Bank and other financial institutions. This will contribute to accelerating the nation's economic growth rate.

A suitable interest rate structure

Through preventing bank loans for fictitious expenditures and bad investments, interest rates act as an anti-inflationary strategy. Savings will increase as a result, expanding the pool of investable resources. It would guarantee the distribution of unusual capital to the most productive applications; prevent inefficient and inefficient use of resources. These viewpoints, however, are not very influential. Straight controls and control over capital concerns can better ensure the productive and efficient use of investable resources. The emerging nations must adopt a more pragmatic strategy and alter their differential interest rate policies to reduce unnecessary expenditure, control inflationary pressures, encourage capital creation, and maintain ventures at a point that prevents the development spurt from slowing downward.

Controlling debt

Administration is responsible for properly and efficiently managing public liabilities in order to support the demands of monetary growth since it must develop on a wide range to execute the programmers of economic development. Debt management's primary goal is to "establish conditions that will allow for significant increases in public borrowing without shocking the system." And in order to keep the responsibility burden low, this must be done at reduced rates. It is evident that encouraging economic growth can be greatly aided by a prudent monetary policy.

Research Purposes

The study's goals are as follows:

- To define the function of monetary policy in India's economic development.
- To evaluate the monetary policy's effects on Indian economy.

Methodology

Data for this study was gathered from journals, periodicals, newspapers, and based on secondary sources. Studying the effects of monetary policy requires the use of secondary data. For the study, a variety of resources from the RBI website and other journals were used to pursue a major. The factors that determine how well monetary policy achieves price stability were identified. The country's GDP growth comes first, and other factors that affect it include the

inflation rate, unemployment rate, foreign direct investment (FDI), and changes in the money supply.

Research Design:

The study examined five variables—one of which was a dependent variable, and the another four were autonomous—to examine the effect of monetary policy on the Indian economy.

Dependent variables -GDP (Gross Domestic Product)

Independent variables- Inflation, Foreign Direct Investments, Unemployment Rates, Policy Rates.

Type of Research- Empirical research is used for analyzing the data.

Methods of Data Collection- Secondary-based studies, RBI press release, RBI special Articles, RBI yearly Reports, Currency and Business Reports, Economic Surveys, Economic and Political Weekly (EPW), Finance and Growth, Economic Diary, The Hindu, ICSSR, Economic Times, IMF Report, Indian Economic Journal, Financial Express, World Bank Reports and Internet, etc. used to collect data.

Result:

This is as of data update in January 2022, data or the most recent analysis on the impact of monetary policy on India's economic growth. For the latest and most accurate information, I recommend checking recent publications, reports from reputable financial institutions, or official sources like the Reserve Bank of India (RBI) and government economic departments.

However, I can guide you on the types of data and tables you might find in such analyses. Generally, studies on the impact of monetary policy on economic growth in India may include:

GDP Growth Rates: the Gross Domestic Product (GDP) growth rates over different periods, correlated with changes in monetary policy.

Interest Rates: Data on key interest rates set by the Reserve Bank of India, such as the repo rate, reverse repo rate, and policy rates, over time.

Inflation Rates: inflation rates, as monetary policy often aims to control inflation. This might include Consumer Price Index (CPI) or Wholesale Price Index (WPI) data.

Credit and Money Supply: credit growth, money supply, and liquidity conditions, as these are key indicators of the effectiveness of monetary policy.

Exchange Rates: currency exchange rates, especially if the analysis involves the impact of monetary policy on the exchange rate.

Unemployment Rates: unemployment rates may be included to assess the impact of monetary policy on employment.

Discussion and Relevance

The use of a strict monetary strategy to curb inflation is not without drawbacks, though. First, the RBI's decision to raise immediate interest rates may not truly result in a constraint of bank credit since the monetary transmission mechanism may be inadequate. This may occur when banks have excess liquidity (cash reserves), in which case they are less likely to adhere to a strict monetary policy and boost lending rates. That's why banks' ability to extend credit will not be constrained. Higher offering rates may not have much of an impact on credit demand if the economy is experiencing prosperous conditions and there is a significant increase in the demand for goods as a whole.

J.M. Keynes highlighted that rather than interest rate, the marginal efficiency of capital—or projected rate of return—is what drives investment decisions. Thirdly, given the historically low interest rates in the US, the European Union, and Japan, corporate enterprises in India are currently more capable to borrow from overseas money market. Therefore, RBI's monetary policy may not be efficient to restrict the supply of credit to control inflation in the country unless the debt-capital inflow is checked.

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