MONETARY POLICY

GHAZALA SHAHEEN
GUEST FACULTY
VANIJYA MAHAVIDYALAYA

INTRODUCTION OF MONETARY POLICY.

- Monetary policy is a powerful instrument of economic management. where government takes various steps to promote economic development. It influences supply of money credit policy, rate of interest. It also regulates the banking system so as to meet credit needs of economy. it creates favorable environment for saving and investment.

- Monetary policy is formulated and executed by Reserve Bank of India to achieve specific objectives. under monetary policy the central bank of the country makes use of instruments to regulate money supply and bank credit so as to influence the level of aggregate demand for goods and services. The availability and costs of credit are regulated to influence the level and nature of economic activities in the country. The monetary policy which affects the demand for and supply of credit is, therefore, very important for business and industry.

DEFINITION OF MONETARY POLICY.

According to Prof. Harry Johnson,

- "A policy employing the central banks control of the supply of money as an instrument for achieving the objectives of general economic policy is a monetary policy.“

According to A.G. Hart,

- "A policy which influences the public stock of money substitute of public demand for such assets of both that is policy which influences public liquidity position is known as a monetary policy."

OBJECTIVES OF MONETARY POLICY

1. Rapid Economic Growth
2. Price Stability
3. Exchange Rate Stability
4. Balance of Payments (BOP) Equilibrium
5. Full Employment
6. Neutrality of Money
7. Equal Income Distribution
8. Control business cycle
9. Promote export and substitute imports
10. Improvement in Standard of Living
11. Control of Inflation and Deflation

- **Rapid Economic Growth** : It is the most important objective of a monetary policy. The monetary policy can influence economic growth by controlling real interest rate and its resultant impact on the investment. If the RBI opts for a cheap or easy credit policy by reducing interest rates, the investment level in the economy can be encouraged. This increased investment can speed up economic growth. Faster economic growth is possible if the monetary policy succeeds in maintaining income and price stability.

- **Price Stability** : All the economics suffer from inflation and deflation. It can also be called as Price Instability. Both inflation are harmful to the economy. Thus, the monetary policy having an objective of price stability tries to keep the value of money stable. It helps in reducing the income and wealth inequalities. When the economy suffers from recession the monetary policy should be an 'easy money policy' but when there is inflationary situation there should be a 'dear money policy'.

- **Exchange Rate Stability** : Exchange rate is the price of a home currency expressed in terms of any foreign currency. If this exchange rate is very volatile leading to frequent ups and downs in the exchange rate, the international community might lose confidence in our economy. The monetary policy aims at maintaining the relative stability in the exchange rate. The RBI by altering the foreign exchange reserves tries to influence the demand for foreign exchange and tries to maintain the exchange rate stability.

- **Balance of Payments (BOP) Equilibrium** : Many developing countries like India suffers from the Disequilibrium in the BOP. The Reserve Bank of India through its monetary policy tries to maintain equilibrium in the balance of payments. The BOP has two aspects i.e. the 'BOP Surplus' and the 'BOP Deficit'. The former reflects an excess money supply in the domestic economy, while the later stands for stringency of money. If the monetary policy succeeds in maintaining monetary equilibrium, then the BOP equilibrium can be achieved.

- **Full Employment** : The concept of full employment was much discussed after Keynes's publication of the "General Theory" in 1936. It refers to absence of involuntary unemployment. In simple words 'Full Employment' stands for a situation in which everybody who wants jobs get jobs. However it does not mean that there is a Zero unemployment. In that senses the full employment is never full. Monetary policy can be used for achieving full employment. If the monetary policy is expansionary then credit supply can be encouraged.

- **Neutrality of Money** : Economist such as **Wicksted**, **Robertson** have always considered money as a passive factor. According to them, money should play only a role of medium of exchange and not more than that. Therefore, the monetary policy should regulate the supply of money. The change in money supply creates monetary disequilibrium. Thus monetary policy has to regulate the supply of money and neutralize the effect of money expansion. However this objective of a monetary policy is always criticized on the ground that if money supply is kept constant then it would be difficult to attain price stability.

opinion that the monetary policy can help
supplementary role in attainting an econo
monetary policy can make special provisions
supply such as agriculture, small-scale indu
industries, etc. and provide them with chea
longer term. This can prove fruitful for these s
up. Thus in recent period, monetary policy
reducing economic inequalities among differe
society.

- **Control business cycle:-** Boom and depression are main phases of business cycle, monetary policy puts a check on boom and depression.

- **Promote export and substitute imports:-** By providing concessional loans to export oriented and import substitution units, monetary policy encourages such industries and helps to improve the position of balance of payments.

- **Improvement in Standard of Living :-** Monetary policy is also the major objective of the monetary policy that it should improve the quality of life in the country.

- **Control of Inflation and Deflation:-** Inflation and deflation both are not suitable for the economy. If the price level is reasonable and there is an adjustment between the price and cost, rate of out put can increase. Monetary policy is used to coordinate the cost and price. So price stability is achieved through the monetary policy.