# RBI’s Monetary Policy

## Why in news?

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The Reserve Bank of India (RBI) is about to announce its monetary policy.

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## What is a Monetary Policy?

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- Monetary policy is the process by which the RBI controls the supply of money, often targeting an inflation rate or interest rate to ensure price stability.
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- RBI reviews its monetary policy every two months.
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- The RBI implements the monetary policy through open market operations, bank rate policy, CRR, SLR, reserve system, credit control policy, moral persuasion etc.
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- Using any of these instruments will lead to changes in the interest rate, or the money supply in the economy.
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- Increasing money supply and reducing interest rates indicate an expansionary monetary policy. The reverse of this is a contractionary monetary policy.
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## What are the key issues to be addressed?

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- **Rate cut -** The RBI has consistently kept the interest rates low in the last two monetary policy announcements.
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- The market expects the repo rate to be reduced by 25 basis points (bps) to 6%. One bps is a hundredth of a percentage point.
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- But there is also an another argument that due to demonetisation the interest rates are already low and therefore repo rate should remain unchanged to boost savings.
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- Therefore RBI's any move regarding this should be accompanied by stating the proper reasoning behind it.
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- **Inflation -** Retail inflation decelerated to a two-year low of 3.41% in December as vegetable prices continued to fall.
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- RBI is aiming to keep retail inflation under 5% in the fourth quarter and 4% within a band of 2 percentage points on either side in the medium term.
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- The RBI's assessment of the inflation situation would be crucial to understand all future rate movements.
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- **Demonetisation impact -** This is the second RBI monetary policy announcement since demonetisation.
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- In the last monetary policy announcement, RBI did not clarify the impact of demonetisation on growth in India.
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- It is crucial to find out the real consequences of removing 86% of currency notes by value from circulation. Data points about the total deposits acquired by banks during the 50-day period and the number of new currency notes pushed back into the banking system should be given out.
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- **MPC decisions -** All six members of the Monetary Policy Committee (MPC) have consistently taken an unanimous monetary policy decision.

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- Therefore it would be important to see if all six votes are in favour of a rate cut or a pause.
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- **Commentary on sectoral issues -** The banking regulator has not made any major announcements around banking sector issues such as capital and asset quality since the demonetisation announcement.
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- The former RBI governor Raghuram Rajan chose March 2017 as deadline for banking sector's bad loan trouble.
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- Therefore a decision is awaited on this issue.
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**Source: Livemint**

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