Size of RBI’s Contingency Fund

Click here for RBI’s Surplus Halved

\n\n

Why in news?

\n\n

\n
- RBI has set aside Rs.13,140 crore for its Contingency Fund (CF) this year.
\n
- This is the part of the reason for the smaller surplus.
\n

\n\n

What is the necessity of CF?

\n\n

\n
- The RBI says the CF is meant for unforeseen contingencies.
\n
- CF exist to cushion against unforeseen fluctuations in forex and gold reserves, losses on its exchange rate operations, valuation losses on bond holdings and risks arising from its supervisory responsibilities.
\n
- Today, the RBI’s record forex reserves are vulnerable to an appreciating rupee and an NPA-ridden banking system.
\n
- Expert committees have recommended that the RBI hold a minimum 12% of its assets in contingency reserves.
\n

\n\n

What is the problem with this?

\n\n

\n
- There is a disagreement between RBI and the centre on the level of reserves that a central bank should keep to tide over extreme financial disruptions.

\n

- This is because of the differing ways in which the government and the RBI perceive the risks that a central bank anticipates.
\n
- The RBI bases its assessment on the results of a sophisticated risk analysis by RBI staff.
\n
- The government, on the other hand, considers there is nothing special about the composition of the RBI's assets.
\n
- It feels that the risk to RBI is significantly less compared to its peers.
\n

\n\n

What should be done?

\n\n

\n

- Centre should avoid treating the RBI as another money supplier like the public sector undertakings that can be tapped to balance its fiscal math.
\n
- As risk manager to the economy, RBI is tasked with managing the country's foreign exchange reserves, ensuring stability in the financial markets and acting as a lender of last resort to the banking system.
\n
- It is only fair that it gets to decide on the capital buffers it needs to cushion against these risks.
\n
- It is time the Government and the RBI planned out a mutually acceptable distribution policy as they did with the Monetary Policy Framework Agreement.
\n

\n\n

\n\n

Source: BusinessLine

\n