U.S plans to roll back QE

Why in news?

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Recently, the U.S. Federal Reserve announced its plan to gradually roll back quantitative easing (QE).

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What is quantitative easing?

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- Quantitative easing is an unconventional monetary policy to increase the money supply.
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- Central banks target the supply of money by buying or selling government bonds.
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- When the economy stalls and the central bank wants to encourage economic growth, it buys government bonds.
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- This lowers short-term interest rates and increases the money supply.
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- Central banks like the European Central Bank,U.S. Federal Reserve have adopted this policy to boost their respective economies.
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What is the significance of QE policy of US?

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- It is a nine year long program implemented as aftermath of the 2007-2008 financial crisis.
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- QE has been carried out in the hope that increased money supply would help stimulate the economy.

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- Under the programme, the central bank has been buying bonds and other debt instruments like mortgage-backed securities from the open market.
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- US also printed fresh dollars to buy these securities, it helped the nation to pump more dollars into their economy.
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What are the reasons for roll back?

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- The Fed's balance sheet currently stands at $4.5 trillion, now US has grown more confident about its economy recovery.
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- As the result of QE policy the quarter ending June grew at its fastest pace since 2015 and Inflation has shown some signs of strength.
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- U.S is clear in rolling back its QE, as modern central banks are in the business of keeping inflation and growth at manageable levels.
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How will it impact the world economy?

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- Lower demand from the Federal Reserve should cause interest rates on U.S. bonds to rise from their current, historically low levels.
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- This is likely to make these bonds more attractive to investors, as they can now be purchased at lower prices in order to earn higher yields.
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- Investors are likely to sell their other investments offering lower returns to invest in U.S. bonds, which could cause some turbulence in global financial markets.
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How this will impact India?

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- The Indian stock market has witnessed a steady outflow of foreign capital as foreign institutional investors have sold out their holdings to invest elsewhere.
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- The rupee has also shown weakness as investors pull money out of India.
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- This trend is likely to continue until the risk-adjusted returns on various investments equalise.
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Source: The Hindu

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