RESERVE BANK OF INDIA(RBI)

What is RBI?

- ✓ RBI is an institution of national importance and the pillar of the surging Indian economy. It is a member of the International Monetary Fund (IMF).
- ✓ The concept of Reserve Bank of India was based on the strategies formulated by Dr. Ambedkar in his book named "The Problem of the Rupee – Its origin and its solution".
- ✓ This central banking institution was established based on the suggestions of the "Royal Commission on Indian Currency & Finance" in 1926. This commission was also known as Hilton Young Commission.
- ✓ In 1949, the Reserve Bank of India was nationalized and became a member bank of the Asian Clearing Union.
- ✓ RBI regulates the credit and currency system in India.
- ✓ The chief objectives of the RBI are to sustain the confidence of the public in the system, protect the interests of the depositors, and offer cost-effective banking services like cooperative banking and commercial banking to the people.

Reserve Bank of India (RBI) – Timeline

Year	Event
1934	The British enacted the Reserve Bank of India Act
1935	Reserve Bank of India was established on 1st of April in Calcutta
1937	Reserve Bank of India was permanently moved to Mumbai
1949	Got nationalized after independence. The bank was held by private stakeholders before this.

In the year 2016, the original RBI Act of 1934 was amended and that provided the statutory basis for the implementation of the flexible inflation-targeting framework.

The Preamble of Reserve Bank of India

Another thing to know about RBI is its Preamble. It describes the basic functions of the Reserve Bank as: "…to regulate the issue of Bank Notes and keeping of reserves to secure monetary stability in India and generally to operate the currency and credit system of the country to its advantage."

Functions of Reserve Bank of India

Reserve Bank of India works as:

1. **Monetary Authority**
   - ✓ Implementation of monetary policies.
   - ✓ Monitoring the monetary policies
   - ✓ Ensuring price stability in the country considering the economic growth of the country

- ✓ Also, read about the Monetary Policy Committee (MPC) and know more about this six-member committee.

2. **Regulator and Administrator of the Financial System**
   - ✓ The RBI determines the comprehensive parameters of banking operations.
   - ✓ These methods are responsible for the functioning of the country’s banking and financial system. Methods such as:
     - License issuing
     - Liquidity of assets
     - Bank mergers
     - Branch expansion, etc.

3. **Managing Foreign Exchange**
   - ✓ RBI manages the FOREX Reserves of India.
   - ✓ It is responsible for maintaining the value of the Rupee outside the country.
   - ✓ It aids foreign trade payment.

4. **Issuer of currency**
   - ✓ The Reserve Bank of India is responsible for providing the public with a sufficient supply of currency notes and coins.
   - ✓ The quality of currency notes and coins is also taken care of by the RBI.
   - ✓ RBI is in charge of issuing and exchanging of currency and coins.
   - ✓ Also, the destruction of currency and coins that are not fit for circulation.

RBI’s Developmental role

- ✓ Promotional functions that support national objectives are organized by RBI that encourage rural and agricultural economic development.
- ✓ The RBI will regularly issue directives to the commercial banks to lend loans to small-scale industrial units.

Composition of RBI

- ❖ Reserve Bank of India is controlled by a central board of directors. The directors are appointed for a 4-year term by the Government of India in keeping with the Reserve Bank of India Act.
- ❖ The Central Board consists of:
  - ✓ Governor
  - ✓ 4 Deputy Governors
  - ✓ 2 Finance Ministry representatives
  - ✓ 4 directors to represent local boards headquartered at Mumbai, Kolkata, Chennai, and New Delhi
- ❖ The executive head of RBI is Governor.
- ❖ The Governor is accompanied by 4 deputy governors.

- ❖ The First Governor of RBI was Sir Osborne Smith and the First Indian Governor of RBI was C D Deshmukh.
- ❖ The First woman Deputy Governor of RBI was K J Udeshi.
- ❖ The only Prime Minister who had been the Governor of RBI was Manmohan Singh.
- ❖ The current governor of RBI (2021) is Shaktikanta Das.

Zonal Offices

- ❖ RBI has four zonal offices:
  - ✓ New Delhi for North
  - ✓ Chennai for South
  - ✓ Kolkata for East and,
  - ✓ Mumbai for West.
- ❖ The Reserve Bank of India has 19 regional offices and 11 sub-offices at present.
- ❖ The bank has two training colleges for its officers:
  - ✓ Reserve Bank Staff College at Chennai
  - ✓ College of Agricultural Banking at Pune.

What is Monetary Policy?

Monetary policy is the procedure by which the monetary authority of a nation, normally the central bank or currency board, controls either the expense of short-term borrowing or the cash supply, focusing on inflation or the loan fee to guarantee value strength and general trust in the currency. Further goals of monetary policy are:

- ✓ to contribute to the stability of the gross domestic product,
- ✓ to achieve and maintain low unemployment, and
- ✓ to maintain predictable exchange rates with other currencies.

In India, the monetary policy is developed by the Reserve Bank of India. Hence, it is also called the Monetary Policy of RBI.

Types of Monetary Policies

1. **Expansionary Monetary Policy**
   - ✓ If a country is facing a high unemployment rate especially during a crisis period such as a slowdown or a recession, the monetary authority of the country, which is usually the central bank of the country, can opt for an expansionary policy that is aimed at increasing economic growth and expanding economic activity.
   - ✓ As a part of expansionary monetary policy, the subsequent monetary authority often lowers the interest rates for consumers through various measures that make money-saving relatively unfavourable and promotes spending in the market. It leads to an increase in money supply in the market, with the hope of a boost in investment and consumer spending.

2. **Contractionary Monetary Policy**
   - ✓ Contractionary monetary policy is when a central bank uses the tools of monetary policy in order to fight inflation. Since inflation is a sign of an overheated economy, the bank must slow economic

growth in order to control the situation. So, the contradictory monetary policy may result in slowing down economic growth and an increase in unemployment but is often required to control inflation.

Monetary Policy of RBI

Developing the Monetary Policy in India is a prerogative of the Reserve Bank of India. Hence, it is also called the Monetary Policy of RBI. The RBI is vested with this responsibility under the RBI Act, 1934. The Monetary policy of RBI regulates the money supply, availability of credit and interest rates. Let us look at the main goal of monetary policy and the monetary policy instruments that the Reserve Bank of India uses to regulate the money supply to achieve the objectives of the economic plan.

Main Goal of Monetary Policy of RBI

The primary goal of monetary policy of RBI is to maintain price stability keeping in mind the objectives laid out in the economic plan. Price stability is extremely important for attaining sustainable growth. To maintain price stability, inflation must be kept in check. RBI uses various monetary policy instruments to ensure that inflation is controlled. Let us look briefly at the monetary policy instruments used by the RBI.

Monetary Policy Instruments

There are several direct and indirect monetary policy instruments that help in implementing the monetary policy in India. Let's discuss each one of them in brief:

1. **Repo Rate:** Repo rate is the rate at which RBI lends short term loans (less than 90 days) to commercial banks.
2. **Reverse Repo Rate:** Reverse repo is the rate at which the RBI keeps the extra deposit of all banks within itself.
3. **Marginal Standing Facility (MSF):** It is the rate at which banks borrow overnight loans from RBI. It can be only up to 2% of the NTDL(Net Demand and Time Liabilities). It is always 1% or 100 basis points more than the repo rate.
4. **Bank Rate:** It is the rate at which RBI offers long term loans (more than 90 days) to commercial banks.
5. **Cash Reserve Ratio (CRR):** It is the ratio of the bank's total deposit that every bank has to keep with the RBI. It has to be in cash form only. RBI does not offer any interest on this reserve money. It can be between 0 to 15%. RBI announces the CRR in its monetary policy.
6. **Statutory Liquidity Ratio (SLR):** It is the ratio of the bank's total deposit that a bank has to maintain with itself. It can either be in cash or in liquid assets including Gold, Foreign Currency, Government Bonds, etc. It can be between 0 to 40% as announced by the RBI in its monetary policy.
7. **Open Market Operations(OMO):**It refers to the buying and selling of government securities between the RBI & banks.