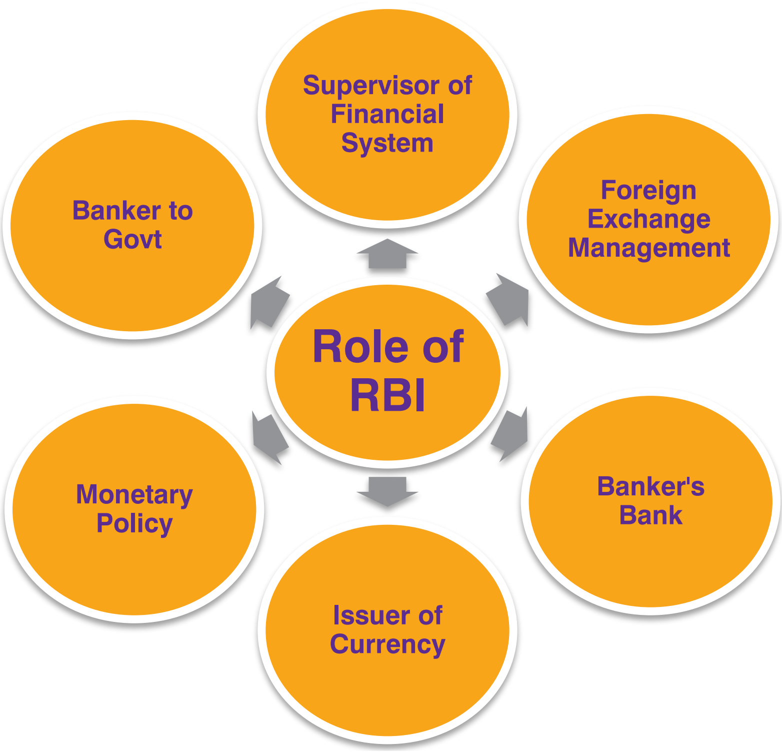
Monetary Policy

- RBI commenced its operations in 1935 in accordance with the provision of RBI Act, 1934.



- As banker to government, RBI performs merchant banking function and maintains account of central and state government.
- RBI role as banker's bank is to help maintain liquidity in the system and acts as lender of the last resort for banks facing liquidity issues.
- RBI also maintains accounts of all scheduled banks.
- RBI's role as supervisor of financial system is to set regulations for smooth functioning of banks and financial institutions including Non Banking Financial Companies (NBFC).
- RBI also needs to maintain public confidence in the financial system and protect depositor's interest.

- One of the most important functions of RBI is money supply management which is done through monetary policy.
- Monetary Policy is a process by which RBI controls money supply in the economy and influences liquidity cost in the financial system.
- RBI uses different monetary policy tools at different times based on assessment of macroeconomic and financial developments in the economy.
- Chart below gives a snap shot on monetary policy.

Monetary Policy snap shot

RBI broad Objective when announcing Monetary Policy	Monetary Policy Instruments	Factors influencing RBI stance to make changes in Monetary Policy
• Maintain Price Stability • Enhance Economic growth	• Cash Reserve Ratio (CRR) • Statutory Liquidity Ratio (SLR) • Liquidity Adjustment Facility (LAF) which includes Repo and Reverse Repo rate • Marginal Standing Facility (MSF) • Bank Rate • Open Market Operations (OMO)	• Macroeconomic Factors- GDP, Inflation, Current Account Deficit, Rupee depreciation & appreciation etc • Financial developments in the economy-Liquidity conditions, Credit Deposit growth etc

- Prevalent macroeconomic or financial situation in the economy determines RBI's direction of monetary policy.
- RBI either takes a contractionary (tighten money supply) or expansionary (loosen money supply) monetary policy measures.
- RBI takes a contractionary monetary policy measure by raising policy rates like CRR, Repo rate, MSF or conducts OMO sales thereby reducing money supply.
- RBI expands money supply by lowering the policy rates or by buying OMOs.

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