Monetary Policy and Impact on Indian Economy – An Empirical Study

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Abstracts:

India's monetary policy since the first plan period was one of 'controlled expansion'- that is, a policy of adequate financing of economic growth ensuring reasonable price stability. Thus, RBI helped the economy to expand via the expansion of money and credit and attempted to check the rise in prices through monetary and other control measures. ***Purpose: The objective of this paper is to*** *study the role and importance of selected monetary instruments in India to understand the importance of various monetary instruments. And also this study focuses on examining the effectiveness of the monetary policy on foreign trade* ***Scope-*** *study is confined to India's Imports and exports. And monetary instruments are considered which is used by RBI such as Bank rate, Repo rate, Reverse repo rate, CRR, and SLR. The data was collected for the period of 19 years starting from 2002-03 to 2018-21. It included the total Imports and export made by the India and Monetary rate which is used by the RBI to control money circulars in the country.* ***Design/methodology/approach-*** *this Study is mainly based on secondary data. Data are collected from secondary sources published on the RBI website and India s Export and Import website. Other required data is retrieved from the journals, Magazines, and government reports and publications for the analysis of the data researcher used the Descriptive statistics. And present the information researcher used the Graph and Charts.* ***Implications -*** *This study helps the various stakeholders to make the right decisions about International trading and also this study helps the government to chalk out the plans. This stud also helps the international traders and commission agents to frame the policy. This study also helps the new entrepreneurs to set long-term and short-term strategies.* **Findings:** *Through this study, it's found that Monetary policy indirectly influences Foreign trade. When RBI adopted the liberal Monetary policy then economic activates are raised in its country due to this international trade is also increased. It's found vice-versa result when RBI adopted restrictive monetary policy hence researcher suggested that to increase foreign exchange government should take proper steps while framing the Monetary policy.*

Keywords: *Monitory Policy, CRR, SLR, Bank rate, Repo rate, Import, Export.*

1.1 Introduction

Monetary policy is concerned with changes in the supply of money. India's monetary policy since the first plan period was one of 'controlled expansion'- that is, a policy of adequate financing of economic growth ensuring reasonable price stability Issues connected with monetary policy are: objectives or goals of the policy, instruments of monetary control, its efficacy, implementation, the intermediate target of the policy, etc. Thus, RBI helped the economy to expand via the expansion of money and credit and attempted to check the rise in prices through monetary and other control measures. A mild version of the liberalization process in the Indian economy was initiated in the mid-1980s. But, it lacked depth, coverage, and self-sustaining character. During the fag end of the 1980s the economy suffered a big jolt with the eruption of a major macro-economic crisis. It manifested initially in the form of a foreign exchange crisis, and then debt and interest payment problems. To meet the crisis India approached the World Bank and the International Monetary Fund (IMF) for a big loan. For granting the loan, World Bank and the IMF stipulated certain conditions. Since India was in a critical situation, she accepted the conditions of the World Bank and the IMF and then provided an immediate context for the realignment of the macro-economic fundamentals, through a program of economic stabilization. With this end in view. The package of economic reforms, which are expected to have a long-term impact on the economy, includes fiscal, monetary, financial, and industrial, and export-import (EXIM) sector reforms. The reforms in monetary and credit policies aimed at slowing down monetary expansion and thereby controlling inflation. The financial sector reforms were initiated on the recommendations of the Narasimham Committee Report. The first phase of reform started with a reduction of Statutory Liquidity Ratio (SLR) and Cash Reserve Ratio (CRR) and permitted a degree of flexibility to the banks in the matter of deposit interest rates. The development of the money market in India in the last few years has been facilitated by some major factors. monetary policy is often, shaped by developments in the money and the foreign exchange markets. Thus, in the post-reform period, the economy is dealing with a set of new programs and policies for its re-construction. Through the monetary policy, RBI controls the money circular in the economy. And also it affected the economic condition of the country.

On the other hand, International trade refers to the trade between two or more two countries. International trade is one of the sources of income to the country when RBI makes a variation in the Monetary instruments it also affects Foreign trade. Hence it is essential to study the impact on foreign trade. This study mainly focuses on the study the role and importance of selected monetary instruments in India to understand the importance of various monetary instruments. And also this study focuses on examining the effectiveness of the monetary policy on foreign trade

1.2 Core Concept

Monetary Policy

Monetary policy is the process by which the monetary authority of a country, generally the central bank, **controls the supply of money in the economy by its control over interest rates** to maintain price stability and achieve high economic growth.

The objective of Monetary Policy

Monetary Policy is designed to maintain the price stability in the economy another objective of the monetary policy of India are as below

1. Price stability
2. Controlled expansion of Bank credit
3. Promotion of fixed investment

4. Restriction of inventories of stocks
5. Promoting Efficiency

Instrument of Monetary Policy

1. **Open market operations**

   An open market operation is an instrument of monetary policy which involves buying or selling government securities like government bonds from or to the public and banks. This mechanism influences the reserve position of the banks,

2. **Cash reserve ratio (CRR)**

   The cash reserve ratio is a certain percentage of bank deposits which banks are required to keep with RBI in the form of reserves or balances. The higher the CRR with the RBI, the lower will be the liquidity in the system and vice versa.

3. **Statutory liquidity ratio (SLR)**

   Every financial institution has to maintain a certain quantity of liquid assets with themselves at any point of time of their total time and demand liabilities. These assets have to be kept in a non-cash form such as G-secs precious metals, approved securities like bonds.

4. **Bank rate policy**

   The bank rate, also known as the discount rate, is the rate of interest charged by the RBI for providing funds or loans to the banking system. This banking system involves commercial and cooperative banks, the Industrial Development Bank of India, IFC, EXIM Bank, and other approved financial institutions.

5. **Credit ceiling**

   In this operation, RBI issues prior information or direction that loans to the commercial banks will be given up to a certain limit. In this case, the commercial bank will be tight in advancing loans to the public.

6. **Repo rate and reverse repo rate**

   Repo rate is the rate at which RBI lends to its clients generally against government securities. Reduction in repo rate helps the commercial banks to get money at a cheaper rate and an increase in repo rate discourages the commercial banks to get money as the rate increases and becomes expensive. The reverse repo rate is the rate at which RBI borrows money from commercial banks. The increase in the repo rate will increase the cost of borrowing and lending of the banks which will discourage the public to borrow money and will encourage them to deposit.

7. **Import**

   "Imports" consist of transactions in goods and services to a resident of a jurisdiction (such as a nation) from non-residents. In other words, bringing goods and services from out of National border is known as Import

8. **Export**

   Export in international trade is a good produced in one country that is sold into another country or a service provided in one country for a national or resident of another country. The seller of such goods or the service provider is an exporter; the foreign buyer is an importer.

1.3 Significance of the study

This study is an attempt to examine the impact of monetary policy on foreign trade The study is based on the analysis of monetary policy and foreign trade of 19 financial years starting from 2002-03 to 2018-21. This study helps the foreign trader to frame the strategy for foreign trade and this paper also helps the government to chalk out various financial and plans and frame EXIM policy, also this study help RBI to control the Monetary supply in the economy.

1.4 The objective of the study

- To study the role and importance of selected monetary instruments in India
- To examine the effectiveness of the monetary policy on foreign trade

1.5 Scope of Study

The study covers a period of 19 financial years starting from 2002-03 to 2018-21. Thus, the study is exclusively on the impact of monetary policy on foreign trade in the past period. This study is mainly concerned with India's Import-Export and Monetary policy of India.

1.6 Research Methodology

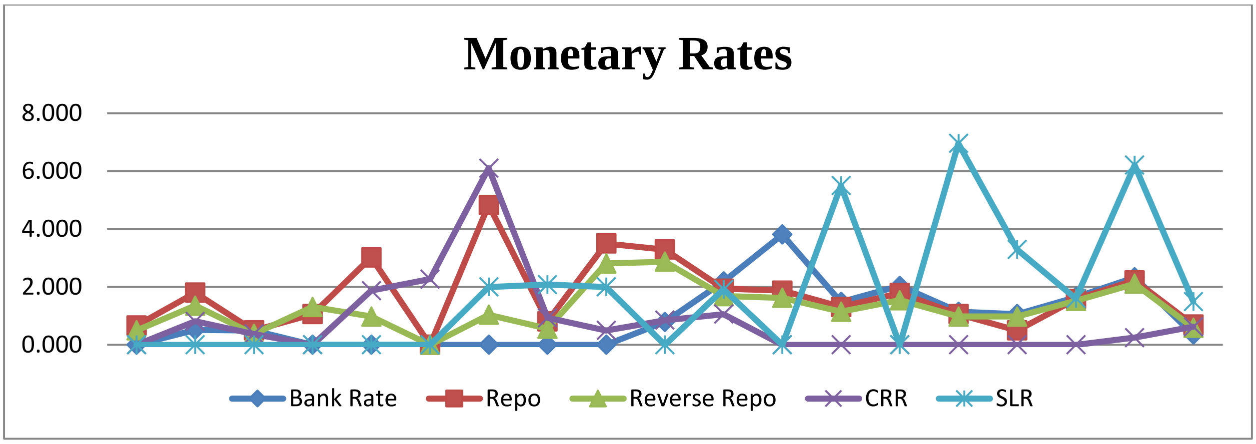
In this paper, mainly secondary data is used. Data are collected from sources such as internet websites of selected companies Balance sheet annual reports. Analysis of data is done with the help of Descriptive Statistics.

1.7The below table shows the Summary of Research Design and Research Methodology

Type of study	Descriptive cum analytical research design
Sources of Data	Secondary sources
Data Collected from	RBI websites, RBI Journal, and publications
Periods of Data collection	19 years from the (2002-03 to 2018-21)
Statistical tools used	Mean and standard deviation Minimum, Maximum.
Analysis of the data	The data analysis has done with the help of Microsoft Excel.

1.8 Data Discussion

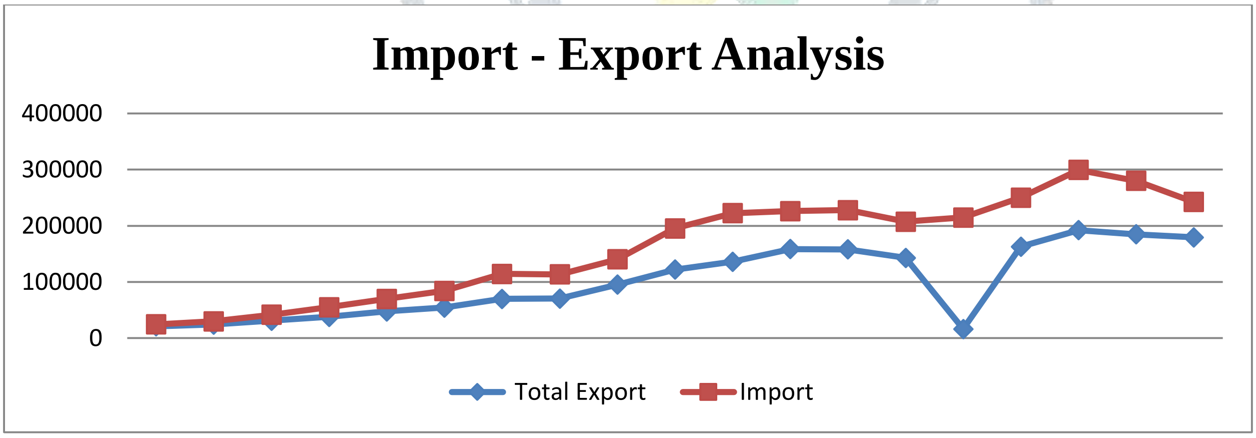
Chart No:1 Shows the result of Monetary Policy Rates over the period



Interpretation:

The above chart shows the result of monetary policy rate which includes the Bank rate, Repo rate, Reverse repo rate, and CRR rate. it was found that RBI was maintained the consistency in Bank rate from 2002-03 to 2010-11 hereafter it can be found that variation in the Bank rate. Repo rate is showing the result of the variation. However, in recent years from 2012-13 to 2017-18 RBI Maintained consistency in the rate. Reverse Repo rate showing the result of high consistency over year comparatively other monetary tools. Cash Reserve is the minimum amount that all commercial banks need to deposit in the RBI the rate of reserving amount indicated through CRR rate. it was found in increasing trend from the year 2005-06 to 2008-09 after it reached the bottom of the line in the year 2009-10 it shows the consistency result. SLR is showing the result of less variation from 2002-03 to 2013-14 but letter it shows the high variation from 2013-14 to till 2018-21.

Chart No 2 Shows the result of Import-Export result analysis over the period



Interpretation:

The above char No 2 shows the result of Import-Export result over years. In the last 20 years period, India's import has been inconsistently increasing trend without much fluctuation. And the blue line in the above chart indicates the Indi's Export which shows the result of an increasing trend but in the year 2016-17, it fell almost nil due to due to fragile global demand and low commodity prices. After this again it recovered main tied consistency in India's Export.

1.9 Conclusion and Recommendation

Researchers have attempted the above to study the role and importance of selected monetary instruments in India. And also researcher examine the effectiveness of the monetary policy on foreign trade on India's foreign trade during 2002-03 to 2018 The analysis of the foregoing pages shows that the role of monetary policy during the period of our study has been affected on the foreign trade when there is found fluctuation in the Monetary rates at the same time there fluctuation found on the foreign trade. When banks are adopted the liberal policy towards the availability of loans then economic activates are increased due to this International trades also increased but when banks are adopted the restrictive policy towards the availability of loans then economic activities are decreased in the country this leads to decreases in the International trade its concluded that Monetary policy directly impacts on the International trade. Hence government should make an effective monetary policy to earn foreign exchange and also increase International trade. The Reserve Bank of India endeavored to moderate the expansion of credit and money supply in such a way as to ensure the legitimate requirements of industry and trade and curb the use of credit for speculative and inflationary activities. In the sphere of monetary control, the Reserve Bank of India has used both quantitative and qualitative techniques.

1.10 Reference

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