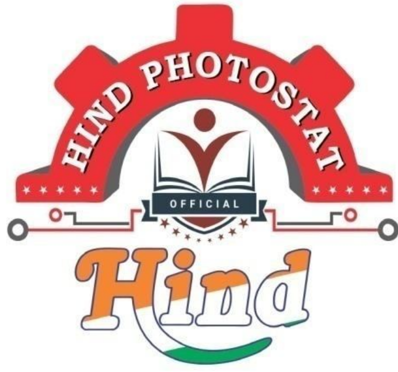

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Economics related current developments

① Concept of Monetary & Fiscal Policy

Monetary policy : Policies related to the money supply in the indian market.

→ It is managed by RBI (Reserve bank of India).
RBI is central bank of India
RBI is also called as Banker's bank.

→ The main purpose of RBI is to control the rate of inflation in indian economy

→ There are tools used by RBI to control inflation and these tools are called as monetary policy.

→ Imp. concept

① When there is more money in the market (Demand ↑), there is inflationary tendency in the market.

② When there is less money in the market (Demand ↓), there is deflationary tendency.

③ When Inflationary → Bring down the inflation.
↓
RBI applies 'contractionary policies'

④ When Deflationary → RBI brings up the inflation
↓
RBI applies 'Expansionary policies'

→ In contrationary policy, money from the market is taken out.

→ In expansionary policy, money is infused into the market.

Monetary policy tools

① Repo rate : This is the rate of interest at which RBI gives loan to commercial banks.

② Reverse reporate : This is the rate of interest at which commercial banks give loan to RBI.

③ Open market operations (OMO) : This is the purchase and sale T-bills (Teasury-bills) and govt. Securities by RBI is called as open market operations.

Note: T-Bills (Treasury Bills) :- T-bills are the instruments used by govt. of india to guarantee repayment (or) funds at a later date.

→ T-Bills are used to meet the short term requirements of the govt.
→ T-Bills are used to meet the short term fiscal deficit of the country
→ Fiscal deficit : When there is more expenditure than the income, it is called as Fiscal Deficit.
→ T-Bills are issued for a maximum tenure of 364 days.

Government securities :- Whenever there is fiscal deficit, then the govt. issues govt. securities (G-Sec). G-Sec serves as a means for the govt. to rage funds from the public to meet its expenditure needs.
For this govt. issues G-sec (or) govt. securities.
Treasury bills are a type of short-term govt. securities.
While dated securities are long term borrowing by the govt.

④ CRR (Cash Reserve Ratio) :- Every commercial bank must have to maintain some liquid cash amount. ~~The percentage of~~
This liquid cash amount is the percentage of total time and demand liability.

inflation ↑ → CRR ↑

∴ CRR ↑ → contractionary policy
CRR ↓ → Expansionary policy (Inflationary)

Saving a/c dep → demand liability
fixed dep. a/c → Time liability

Q: Contractionary or expansionary (→ Inflationary)?

1. Repo ↑ ⟶ contractionary
2. Reverse repo rate ↑ ⟶ ~~Inflationary~~ contractionary
3. T. bills purchase by RBI ⟶ contractionary
4. G.sec sell by RBI ⟶ contractionary

Fiscal Policy

Fiscal policy is the policy used by the govt. of India through finance ministry.. and these policies are related to taxation.

Fiscal policy are also called as govt. revenue collection policy.

objectives of Fiscal policy

(i) To control Fiscal deficit.

(ii) To boost economic growth.

(iii) To create employment opportunities.

Tools of fiscal policy includes :-

1. Taxation
2. Govt. spending

Taxation

Whenever govt. increases the taxation then there may be more revenue collection by the govt. but people will have less money to spend and therefore there will be reduced economic growth in the country.

Taxation ↑ → economic growth ↓

but when there is less taxation by the govt. then there will be more money in the hands of people to spend and this will lead to more economic growth but at the same time govt. will have less money to spend leading to increase in fiscal deficit.

Taxation ↓ → fiscal deficit ↑

Govt spending

Govt. spending are of 2 types—

1. **Burden** ⇒ It is related to the salary payment, subsidies expenditure etc.

→ revenue expenditure is that expenditure of govt. that has to be carried out on a regular basis by the govt.. It is also not forming any income in the long run.

Capital expenditure

This is another type of expenditure by the govt. in which formation of infrastructure is included. Infrastructure formation means buiding of dam, roadways, expressways and ports, airports etc.

Capital expenditure is considered as good for the country because It is related to long term capital formation. Such type of govt. expenditure is encouraged.

If govt. spending increases revenue expenditure then it leads to non-formation of long term assets for the country and very the govt. will fall into fiscal deficit.

e.g. on this basis only, old pension scheme (OPS) was opposed.

But if the capital expenditure by the govt. is more then it leads to long term capital formation and ultimately long term benefit. so therefore long term capital formation i.e, capital expenditure by the govt. is good for the country and it is also considered as positive expenditure.

Concept of Inflation

Inflation is the rate of change of prices of good and services.

When there is high rate of inflation then many people can not purchase the goods and services they need. while if the inflation is very low then it affects the growth of the country. Therefore there must be a balance in the inflation rate of the country

→ Inflation of 3-5% is considered as good for the country.

How to measure the inflation?

There are two ways to measure inflation.

① WPI : Wholesale price index

② CPI : Consumer price index

→ WPI is calculated on the basis of change in the prices of goods and services in the wholesale market.

→ WPI is published by the office of economic advisor, ministry of commerce and industry.

→ WPI is calculated on the basis of base year prices of goods and services.

→ Base year is the previous year in which there has not been much changes in the price of goods and services also the current base year is 2011-12.

→ The WPI is calculated on the basis of the prices of good and services in WPI in the base year. It is calculated on the basis of the basket of goods and services.

CPI :

→ This is the price of goods and services that the end consumer pays.

→ CPI is also calculated through the basket of goods and services that includes food, medical care, education, electronic products, housing, clothing etc.

→ CPI is also measured using the difference in prices of goods and services in a base year wrt to good and services in current year in terms of percentage.

→ base year of CPI is 2012.