ROLE OF MONITORY POLICY ON ECONOMIC DEVOLOPMENT

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Abstract:
A growing nation like Bangladesh's economy benefits greatly from monetary policy since it affects the cost and accessibility of credit, the ability to control inflation, and the balance of payments. Different monetary policy elements have contributed to Bangladesh's increasing current GDP growth. This essay seeks to determine how Bangladesh's monetary policy has affected the country's overall economic growth. The goal of the study is to establish a causal link between several economic elements contributing to Bangladesh's economic growth and the monetary policy. Data from the previous 20 years, from 1997 to 2017, were gathered for this study. To conduct this study, primary data from 57 respondents from various commercial banks were gathered. For this study, a variety of economic variables were employed, including the inflation rate, employment rate, loan rate, borrowing rate, export-import growth rate, broad money growth rate, and FDI rate as a percentage of GDP. The data were analyzed using both descriptive and inferential statistics. To determine the variables that affect Bangladesh's overall economic performance, multivariate analysis techniques such exploratory factor analysis were used with SPSS version 20.0. To find the link between Bangladesh's monetary policy and its economic growth, multiple regression analyses were conducted. The findings indicate that the GDP growth of Bangladesh is highly influenced by factors including consumption, investment, net government spending, and net export. The study also shows that these mediating elements are significantly impacted by Bangladesh's monetary policy. By guaranteeing appropriate monetary policy implementation, the research provides significant insight into the socioeconomic development of Bangladesh. The central bank and decision-makers in Bangladesh will soon see more robust economic growth if they concentrate on the important elements listed above.
Keywords: Monitory Policy, Goals, Policy committee and Impact.

I. INTRODUCTION:

By regulating price changes and other aspects of the economy, monetary policy is essential to the development of impoverished nations. This is accomplished by properly adjusting the relationship between the supply and demand for money. The demand for money continues to rise as the economy grows. Therefore, by striking the right balance between the demand for money and the economy's productive capacity, monetary policy can significantly contribute to the economic growth of developing nations by reducing price fluctuations and overall economic activity.

II. MONITORY POLICY:

A country's central bank can use a variety of measures known as monetary policy to encourage stable economic growth by regulating the overall amount of money that is accessible to the country's banks, consumers and enterprises. The U.S. Treasury Department can print money, but the Federal Reserve generally controls the amount of money available to the economy through open market activities (OMO). In essence, this entails purchasing financial securities during monetary policy easing and selling such securities during monetary policy tightening. U.S. Treasuries and agency mortgage-backed securities are the Fed's preferred OMO securities. The objective is to maintain a steady state of economic activity that is neither too hot nor too cool. The central bank may push down interest rates to encourage greater borrowing and spending, or it may push rates up to discourage borrowing. The nation's currency is the fundamental tool at its disposal. Rates for loans to the country's banks are determined by the central bank. All financial institutions adjust the rates they charge all of their customers, from large enterprises borrowing for ambitious projects to home buyers seeking for mortgages, when they raise or drop their rates.

The financial authority of India, i.e., the central bank, oversees the supply of cash within the economy through its control over interest rates in order to produce high economic growth and maintain price stability. The central monetary authority in India is the Reserve Bank of India (RBI), and it is responsible for preserving price stability there.

III. **THE RBI HAS LISTED THE FOLLOWING ADDITIONAL MONETARY POLICY GOALS**:

1. Price stability, first
2. Managed Growth of Bank Credit
3. Fixed investment promotion
4. Restriction of Stocks and Inventories
5. To Increase Effectiveness
6. Lessening Rigidity

1. **Cost Stability:** Maintaining reasonable price stability is the major goal of price stability in order to ensure that projects develop quickly and are supported by favorable environments.
2. **Controlled Bank Credit Expansion:** RBI primarily works to limit the increase of bank credit and the money supply, taking into account seasonal credit needs without having an impact on output.
3. **Fixed investment promotion:** Limiting non-essential fixed investment is intended to boost investment productivity.
4. **Stock & Inventory Restriction:** This policy was created to prevent overstocking and idle funds in the company. The unit was getting sick because of the additional stock that was offered there that was becoming out of date.
5. **To Increase Effectiveness:** Today's central banks are much more cautious with their systems, and as a result, a transaction including this approach boosted the effectiveness of the bank. They were able to de-restrict many bank operations through this practise, including the easing of operational controls in the credit distribution system, the introduction of new money market instruments, etc. They also attempted to make some structural changes that would benefit their company in the long run.
6. **Lessening Rigidity:** The Reserve Bank of India provides some operational flexibility to banks, enabling them to operate on their own. These options for flexibility foster competition and promote growth. Regular control-keeping aids in ensuring that the financial system's operations are conducted with the utmost caution and discipline.

IV. MONITORY POLICY COMMITTEE

The Reserve Bank of India Act, 1934 (RBI Act) was amended by the Finance Act, 2016 in order to give the Monetary Policy Committee legal and historical context. These modifications aimed to increase growth and maintain stable prices. The committee is tasked with achieving a particular target level and serves as the benchmark setter for the policy rate (repo rate). The RBI Act mandates that three of the six RBI members serve on the MPC, with the remaining three members being assigned by the Central Government.

The Government of India told the RBI that the "Inflation Target" for the period starting on the publication date of the announcement and ending on March 31, 2021, is 4 percent in the Gazette of India Extraordinary dated 5th August 2016. At the same time, it was announced that the permitted tolerance levels were 2 and 6 percent, respectively.

V. MONITORY ACTIVITIES:

In order to preserve price stability, economic growth, a healthy balance of payments, a stable exchange rate, and financial stability, monetary techniques are a component of monetary operations that act on monetary magnitudes including monetary supply, interest rates, and credit limitations.

VI. INSTRUMENTS OF MONITORY POLICY:

The following tools are used to control the flow of money through the economy:

1. Open Market Transactions
2. Ratio of Cash Reserves (CRR)
3. Ratio of Statutory Liquidity (SLR)
4. Bank Rate Policy
5. Credit Limit
6. Credit Authorization Plan
7. Moral Persuasion
8. Reverse repo rate and repo rate

VII. MONITORY POLICY'S IMPACT ON ECONOMIC DEVELOPMENT:

1. **Proper balancing of the supply and demand of money**: A growing economy and a corresponding decline in the subsistence sector lead to a significant increase in the demand for money for transactions, which in turn causes the demand for money to raise. The demand for money to conduct daily transactions is also increased by the rise in per capita income and population during the development process. In order to prevent prices from rising as a result of an increase in national output, the monetary authority must expand the money supply at a pace nearly equivalent to the rate of increase in real income due to the ongoing rise in demand for money.

   By starting a vicious downward spiral of prices and output, a declining price level has a negative impact on the speed of economic growth. Similar to this, if there is more money available than what is required for trade and industry, it might be utilized for speculation, which would slow down economic growth and lead to inflation.

   The main thrust of the argument is that stabilizing the money supply will minimize economic turbulence and create the conditions for quick growth. Therefore, by limiting price volatility and overall economic activity and striking the proper balance between the need for money and the economy's productive capability, monetary policy can significantly contribute to the economic growth of developing nations.

2. **Cost Stability:** One requirement for economic growth is the preservation of domestic pricing and exchange rate stability. However, due to a number of structural rigidities and imbalances, economic progress causes inflationary pressures in underdeveloped countries. The tendency to save is negatively impacted by the inflationary rise in prices, which also directs invertible resources into speculative and unproductive investments like real estate, jewellery, gold, stockpiling of products, etc.

   The monetary authorities should consequently maintain a continual eye on price changes and control the supply and flow of credit and money in order to restrain the rate of inflation. Similar to how inflationary pricing rises cause repeated currency devaluations. Exchange rate fluctuations have a negative impact on international trade and the ability to gain foreign exchange profits, which could aid in a nation's development.

   As a result, monetary policy should focus on preventing excessive price increases and preserving currency stability at a reasonable level. In essence, volatility in internal prices and exchange rates hinders the rate of sustained economic growth. This entails the implementation of monetary measures that will limit inflation and currency volatility.

A rise in interest rates, on the other hand, will encourage saving. The Central Bank may add to it by selling government and bank securities, increasing the serve ratio, and implementing selective credit controls in order to further reduce the banks' ability to create credit.

3. **Credit Management:** The monetary authority should use its credit management tools to influence and mould the nature and pattern of investment and production in order to ensure a faster pace of economic growth. It goes without saying that this will rely on the variety of credit institutions present in the economy as well as the types of credit regulations used by the Central Bank. The banking system is still underdeveloped in the majority of developing nations. The commercial banks primarily fulfill the short-term credit needs of businesspeople and dealers, but they are hesitant to fulfill the medium- and long-term credit needs of industry and manufacturing in general. In order to induce and encourage banks to give medium and long-term loans for beneficial uses, the monetary authority should intervene and provide the necessary guarantees and rediscounting facilities. Along with cooperative lending, state-owned financial institutions and commercial banks can make significant contributions in this area. Similar to this, selective credit regulations that differentiate between the costs and availability of loans to different sectors and industries should be implemented to influence the pattern of investment and production.

4. **Establishment & Growth of Financial Institutions**: By enhancing the nation's currency and credit systems, monetary policy can hasten the process of economic development. To implement this proposal, new banks and financial institutions must be developed in order to offer more expansive lending options and to mobilize savings for useful purposes. Financial institutions are dying off in developing nations, and there are very few banking services available. Due to this, the populace's savings cannot be efficiently utilized for economic expansion, which causes the rate of growth to be exceedingly slow.
   The monetary authority can aid in the growth of financial institutions by providing new institutions with training facilities, subsidies, and special concessions in the form of free remittance and rediscounting services.
   The issue of rural loans should receive special attention from the Central
   Bank. To a large extent, the credit requirements of the royalty can be met by a network of cooperative credit organizations with apex banks financed by the Central Bank.
   In a similar manner, the Central Bank and financial institutions finance commerce and industry. It goes without saying that this will speed up economic growth. In underdeveloped economies; there is a sizable unmonitored sector that does not respond to changes in the amount of money or interest rates, among other things. This sector continues to be outside the effective authority of the Central Bank. Given this, the monetary authority must make every effort to widen the scope of the monetized sector in order to successfully implement monetary policy.

The monetary authorities of growing countries must consequently contribute positively to the establishment, operation, and growth of banking and other financial institutions as well as extend credit where necessary in order to achieve the goal of growth with stability.

5. **An appropriate interest rate structure:** massive amounts of investment are needed for economic development from both the public and private sectors. The financing of extremely ambitious programmes of economic development in all sectors of the economy requires that credit be made available to private entrepreneurs at the lowest rates possible. This is because the cheap money policy should be followed because it makes public borrowing affordable, keeps the cost of servicing public debt low and thus stimulates investment both public and private.

   Therefore, a low interest rate policy encourages investment for economic growth. Contrarily, it is noted that a policy of cheap money may encourage merchants and speculators to borrow more money from banks and use it for stockpiling, hoarding, and other speculative activities.

   However, this propensity on the side of private investors can be curbed by applying selective credit control and directing investment in the right directions.

   However, some economists recommend a high interest rate policy based on the following factors:

a) By prohibiting borrowing from banks for speculative purposes and undesired investments, it will act as an anti-inflationary measure;

b) It will encourage savings, increasing the number of investible sources available.

c) It would guarantee the distribution of limited money to the most beneficial uses and prevent resource-productive and wasteful use. These justifications, however, are weak. Direct controls and control over capital problems can better ensure the productive and efficient use of investable resources.

   Furthermore, it is possible to successfully ensure that money is flowing through the right channels by using qualitative methods of credit control. In terms of encouraging saves, it should be noted that the volume of savings is more a function of income level than of interest rate. A higher interest rate could, However, when it becomes out of hand and other measures to regulate it have failed, be employed as a shock strategy to reduce speculation in goods and securities. Therefore, emerging nations should adopt a more practical strategy and design a differentiated interest rate policy that would curb wasteful expenditure, manage inflationary pressures, encourage capital formation, and maintain investment activity at a level that won't slow down the rate of growth.

6. **Debt administration:** In developing economies, the government must borrow heavily in order to implement economic development programmes; as a result, it is the Central Bank of the nation's responsibility to manage public debt effectively and efficiently in order to meet the demands of economic growth. The main goal of debt management is to "establish circumstances that allow public borrowing to expand year after year and on a large scale without jarring the system." To keep the debt load low, this must be done at modest rates.

   A low interest rate raises the price of government bonds and so makes them more appealing to the public, ensuring the success of the public borrowing programme. Low interest rates are therefore beneficial for strengthening and stabilizing the market for government bonds.

   Additionally, a low interest rate structure reduces the weight of the national debt. Therefore, in order to hasten the process of economic development, monetary policy should focus on the effective management of public debt, which entails releasing government bonds at the right time, stabilizing their prices, and reducing the debt load.

VIII. CONCLUSION:

The investment in infrastructure, which is a key factor in determining the growth of the gross domestic product, is improved by foreign debt and credit to the private sector, it is found. Empirical evidence supports the idea that the amount of broad money and the proportion of businesses employing banks to finance their investments determine the size of lending to the private sector.

The RBI's increase in short-term interest rates may not actually result in the restriction of bank loans since the monetary transmission mechanism may be inadequate. This may occur when banks have excess liquidity (cash reserves), in which case they are less likely to adhere to a strict monetary policy and boost lending rates. As a result, banks' ability to extend credit will not be constrained. Higher offering rates may not have much of an impact on credit demand if the economy is experiencing prosperous conditions and there is a significant increase in the demand for goods as a whole. J.M. Keynes highlighted that rather than interest rate, the marginal efficiency of capital or projected rate of return is what drives investment decisions. Thirdly, given the historically low interest rates in the US, the European Union, and Japan, corporate enterprises in India are currently more able to borrow from overseas capital markets (also known as external commercial borrowing, or ECB). Therefore, RBI's monetary policy may not be effective to restrict the supply of credit to control inflation in the economy unless this debt-capital inflow (i.e., ECB) is checked.

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