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The Role of RBI in Economic Development and Social Progress

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Abstract: The (RBI) Reserve Bank of India was established in the year 1935 under Reserve Bank of India Act 1934 and was nationalized in 1949. Initially,it was a private share holder's company. It performs very important functions from issue of currency note to maintenance of monetary stability in the country and its affairs are governed by the central Board of Directors appointed by the Government of India from time to time. Since,its inception the RBI had played an important role in the economic development, monetary stability and social progress in the country. The Royal commission in Indian currency and finance appointed on Aug 25,1925 has suggested the establishment of the central Bank in India,later the Indian central Banking Enquiry committee,1931 stressed the establishment of the central bank in India. The RBI Issued first of its currency notes Rs:5 and Rs:10 in January 1938 and later in the same year denomination of Rs:100,Rs:1000 and Rs:10000 were Issued. The primary objective of the RBI was to maintain price stability and economic growth in the country. This could be achieved by the RBI with the help of its monetary policy. With the help of its quantitative and qualitative credit control methods RBI can able to maintain supply of money in the economy and make the money available to the investors for their investment projects. The RBI has played a crucial role in shaping the Indian economy since its inception in 1935. From managing the monetary policy to regulating the financial sector, the RBI has been instrumental in laying the foundation for India's economic growth. In fact,India's GDP has grown from just $30. 6 billion in 1950 to over $3. 4 trillion in 2022,and the RBI has been a key driver of this transformation. The RBI's developmental role includes ensuring credit to productive sectors of the economy,creating institutions to build financial infrastructure and expanding access to affordable financial services to the society. It also encouraging efficient customer service throughout the banking industry.

Keywords: RBI, commercial banks, monetary policy, OMO, BRP,VRR, TReDS, UPI, BBPS, eKYC, ECLGS and AA.

Introduction

The Reserve Bank of India (RBI) was established in the year 1935 under Reserve Bank of India Act 1934 and was nationalized in 1949. The Royal commission on Indian currency and finance appointed on Aug 25,1925 has suggested the establishment of the central bank in India. Later,the Indian Central Banking Enquiry Committee,1931 stressed the establishment of the Central Bank in India. The RBI issued first of its currency notes Rs. 5 and Rs. 10 in January 1938 and later in the same year denomination of Rs. 100,Rs. 1000 and Rs. 10000 were issued. It performs very important functions from issue of currency note to maintenance of monetary stability in the country and its affairs are governed by the Central Board of Directors appointed by the Government of India from time to time. Since its inception,the RBI had played an important role in the economic development,monetary stability and social progress in the country.

Post Independence

After nationalization of RBI in1949,all shares were transferred to central government. The RBI is constituted for the management of currency and for carrying the business of banking in accordance with provisions of the Act. It is a body of corporate having perpetual succession,common seal and can be sued or sue in its name. The general supervision and direction of the affairs of the RBI is entrusted with the Central Board of Directors.

I. Monetary Policy

It was formulated and executed by RBI to achieve specific objectives. It refers to that policy by which central bank of the country controls (i) the supply of money, and (ii) cost of money or the rate of interest,with a view to achieve particular objectives. The main objectives of monetary policy are to achieve price stability,financial stability and adequate availability of credit for growth.

(i) To Regulate money supply in the economy: Money supply includes both money in circulation and credit creation by banks. Monetary policy is framed to regulate the money supply in the economy by credit expansion and credit contraction. At the time of credit expansion (giving more loans),the money supply can be expanded and at the time of credit contraction (giving less loans) money supply can be reduced or decreased. It will control the money supply in such a manner as to expand it to meet the needs of society and economic growth and at the same time to curb inflation.

(ii) To Attain price stability: Another major objective of monetary policy is to maintain price stability in the country and make the economy to grow smooth manner without much fluctuation in the price level. Price level is affected by

money supply,but monetary policy regulates money supply to maintain price stability in the economy.

(iii) To Promote economic growth: Monetary policy is helps to make available necessary supply of money and credit for the economic growth of the country. Those sectors which are quite significant for the economic growth are provided with adequate availability of credits.

(iv) To Promote savings and investment: RBI through its monetary policy regulate the rate of interest and checking inflation which helps to promote savings and investment in the country. Higher rate of interest promote saving which induce the people to invest more due easy availability of credit facility in the banks.

(v) To Control business cycle: Boom and depression are two extreme cases of the business cycle. Monetary policy puts a check on boom and depression. During the period boom,credit is contracted by raising rate of interest,and money supply and inflation are reduced in the economy. During the period of depression,credit is expanded by reducing the rate of interest by RBI and increase in money supply and aggregate demand in the economy.

(vi) To Promote exports and substitute imports: By providing concessional loans to exports oriented and imports substitution industries by the RBI helps to make balance of trade of the respective countries positive and improve the position of balance of payments in the country.

(vii) To Manage aggregate demand: Monetary authority tries to keep the aggregate demand in balance with aggregate supply of goods and services. If aggregate is more then credit expanded and the interest rate is lowered down. When interest rate come down,more people take loan to buy goods and services and hence aggregate demand increases and vice-versa.

(viii) To Ensure more credit for priority sector: RBI aims at providing more funds to priority sector by lowering interest rates for these sectors. It includes agriculture,small-scale industries,weaker sections of the society etc to make balanced development of different sectors in the economy.

(ix) To Promote employment: RBI through its monetary policy providing concessional loans to productive sectors,small and medium entrepreneurs,special loan schemes for unemployed youth and creating employment opportunities in the country. This will help to solve the problems of unemployment in the economy and improve the standard of living of the people.

(x) To Develop infrastructure: RBI by providing concessional funds for various government programme or schemes helps to promote various infrastructural development in the country. It helps the country to achieve high rate of economic growth and make further economic goods in the country. It make the people to buy various goods and services for their consumption.

(xi) To Regulate and expand banking: RBI regulates the banking system of the economy. It has expanded banking to all parts of the country. Through its monetary policy,RBI issues directives to different banks for setting up rural branches for promoting agricultural credit. Besides it,government has also set up cooperative banks and regional rural banks (RRBs)

II. Instruments of Monetary Policy

The RBI in its instruments of credit influencing over the money supply in the economy. From time to time,it will change its instruments of credit and make the credit either cheap or costlier. It will help the economy to move towards the path of development without making negative impacts on the economy. The instruments of monetary policy are of two types.

(A) Quantitative or General or Indirect

The quantitative tools of credit control are designed to regulate or control the total volume of bank credit in the economy. These tools are indirect in nature and are employed for influencing the quantity of credit in the country. The general tools of credit control comprises of following instruments.

(i) Bank Rate policy (BRP): The bank rate is the minimum lending rate of the central bank at which it rediscounts first class bills of exchange and government securities held by the commercial banks. It is "the standard rate at which the bank is prepared to buy or rediscount bills of exchange or other commercial paper eligible for purchase under the RBI Act. "When the central bank finds that inflation has been increasing continuously,it raises the bank rate so borrowing from central bank becomes costly and commercial banks borrow less money from it (RBI). The commercial banks,in reaction,raise their lending rates to the business community and borrowers who further borrow less from the commercial banks. There is contraction of credit and prices are checked from rising further. On the contrary,when prices are decreased,the RBI lowers the bank rate. Now,it is cheap to borrow from the RBI on the part of commercial banks. And commercial banks also lower their lending rates. Businessmen are encouraged to borrow more and investment is increased in the economy,followed

by rise in output,employment,income and demand and the downward movement of prices is checked.

However, the efficiency of the bank rate as a tool of monetary policy depends on existing banking network,interest elasticity of investment demand,size and strength of the money market,international flow of funds etc

(ii) Open Market Operations (OMO): Open market operations refers to sale and purchase of securities in the money market by the central bank of the country. When prices start rising and there is need to control them,the central bank sells securities in the market. The reserves of commercial banks are reduced and they are not in a position to lend more to the business community or general public. Further investment is discouraged and the rise in prices is checked. Contrary, when recessionary forces start in the economy,the RBI buys securities from the market. The reserves of commercial banks are raised. So,they lend more to business community and general public. It further raises investment, output, employmeny,income and demand in the economy. Hence,the fall in price is checked.

Normally,during the inflation period in order to reduce the purchasing power,the RBI sells securities and during the recession or depression phase,it buys securities and make more money available in the economy through the banking system. Thus under OMO there is continuous buying and selling of securities taking place leading to changes in the availability of credit in the economy. However,there are certain limitations that affect OMO viz;under developed securities market,excess reserves with commercial banks,indebtedness of commercial banks etc.

(iii) Variation in the Reserve Ratios (VRR): Under this method,CRR and SLR are two main deposit ratios,which reduce or increases the idle cash balance of the commercial banks. Every bank is required by law to keep a certain percentage of its total deposits in the form of a reserve fund in its vaults and also a certain percentage with the RBI. The CRR refers to some percentage of commercial bank's net demand and time deposit liabilities which commercial banks have to maintain with the central bank and SLR refers to some percentage of reserves to be maintained in the form of gold or foreign securities. In India the CRR by law remains in between 3-15 percent while the SLR remains in between 25-40 percent of bank reserves with the RBI. Any change in the VRR (CRR+SLR) brings out a change in commercial banks reserves positions. Thus,by varying VRR commercial banks lending capacity can be affected.

When prices are rising, the central bank raises the reserve ratio. Banks are required to keep more with the central bank. Their reserves are reduced and they lend less. The volume of investment,output and employment are adversely affected. In the opposite case,when the reserve ratio is lowered,the reserves of commercial banks are raised. They lend more and the economic activity is favourably affected in the economy.

(B) Qualitative Instruments or Selective or Direct

Selective credit controls are used to influence specific types of credit for particular purposes. They usually take the form of changing margin requirements to control speculative activities within the economy. These tools are not directed toward the quality of credit or the use of the credit. They are used for discriminating between different uses of credit. It can be discrimination favouring export over import or essential over non-essential credit supply. This method can have influence over the lender and borrower of credit. The selective tools of credit control comprises of following instruments.

(i) Change in Margin Money: The margin refers to the "proportion of the loan amount which is not financed by the bank. "A change in a margin implies a change in the loan size. This method is used to encourage credit supply for the needy sector and discourage it for other non-necessary sectors. This can be done by increasing margin for the non-necessary sectors and by reducing it for other needy sectors. For instance,raising the margin requirement to 70% means that the pledger of securities of the value of Rs. 10000/-will be given 30% of their value, ie, Rs: 3000/- as loan. In case of recession in a particular sector,the central encourages borrowing by lowering margin requirements.

(ii) Consumer Credit Regulations: Under this method,consumer credit is regulated through hire-purchase and installment sale of consumer goods. Under it the down payment,installment amount,loan duration,etc is fixed in advance. This can help in checking the credit use and then inflation in a country.

(iii) Publicity: Under it,the central bank publishes various reports stating what is good and what is bad in the system. This published information can help commercial banks to direct credit supply in the desired sectors. Through its weekly and monthly bulletins,the information is made public and banks can use it for attaining goals of monetary policy.

(iv) Credit Rationing: RBI fixes credit amount to be granted. Credit is rationed by limiting the amount available for each commercial bank. This method controls

even bill re-discounting. For certain purpose,upper limit of credit can be fixed and banks are told to stick to this limit. This can help in lowering banks credit expousure to unwanted sectors.

(v) Moral Suasion: It is a kind of suggestion to banks. It helps in restraining credit during inflationary periods. Commercial banks are informed about the expectations of the central bank through its monetary policy. Under moral suasion central bank can issue directives,guidelines and suggestions for commercial banks regarding reducing credit supply for speculative purposes.

(vi) Control Through Directives: Under this method the RBI issue frequent directives to commercial banks. These directives guide commercial banks in framing their correct lending policy. Through a directive the central bank can influence credit structure,supply of credit to certain limit for a specific purpose. The RBI issues directives to commercial banks for not lending loans to speculative sector such as securities etc beyond a certain limit.

(vii) Direct Action: Under this method the RBI can impose an action against a bank. If certain banks are not adhering to the RBI's directives,the RBI may refuse to re-discount their bills and securities. Secondly,RBI may refuse credit supply to those banks whose borrowings are in excess to their capital. Central bank penalize a bank by changing some rates. At last it can even put a ban on a particular bank if it does not follow its directives and work against the objectives of the monetary policy.

III. Role of RBI in Indian Economic Development and Social Progress

The RBI has played a significant role in shaping the Indian economy since its inception in 1935. From managing the monetary policy to regulating the financial sector and laid the foundation for India's economic growth and development. In fact,India's GDP has grown from just $30. 6 billion in 1950 to over $3. 4 trillion in 2022,and the RBI has been a key of this transformation.

(i) Nationalization of Banks-1969: Nationalization of banks was implemented under the Banking Companies (Acquisition and Transfer of Undertakings) Act of 1970. The ordinance came in to force on 19 july 1969,to serve better to the needs and development of the economy and society with national policy objectives.

This move aimed at integrating the banking system with the needs of economic policy and achieving a more equitable distribution of resources in the context of development, where banks are played a significant role. With nationalization of 14 major banks by the government under the guidance of the

RBI,the banking sector was given a significant boost towards achieving a more equitable distribution of resources and increasing financial inclusion.

(ii) Priority Sector Lending-1972: The roots of priority sector lending can be traced back to 1966 when Moraji Desai recognized the need for increased credit to agriculture and small -scale industries due to its importance in determining the GDP of the country. But, the RBI report in the National Credit Council in 1972 that the definition for priority sector was formalized. In 1974, commercial banks were given a target of 33. 33% of their ANBC, which was later increased to 40% on the recommendations of Dr. K. S. Krishnaswamy committee. After the nationalization of banks the priority sector lending also allowed the government to address important political lobbies. Later, the definition of priority sector lending has grown to cover important neglected sectors of the economy, with a focus on agriculture and small-scale industries, which includes Micro, Small and Medium enterprises (MSMEs).

(iii) Liberalization of the Indian Economy-1991: In 1991, India faced a balance of payment crisis due to the increasing pressure on foreign reserves. The government of India initiated a series of economic reforms aimed at liberalizing and opening up the Indian economy.

RBI played an important role in implementing these reforms, which included reduction in import duties, liberalization of industrial licensing, abolition of license Raj and allowing FDI in many sectors of the Indian economy. As a result of these reforms, India's international competitiveness increased in various sectors like auto components, software, biotechnology, pharmaceuticals, telecommunications, research and development and professional services. Foreign investment in the country increased from US$132 million in 1991-92 to $5. 3 billion in 1995-96. Apart from that, poverty in India decreased from 39% in 1993-94 to 26. 1% in 1999-2000.

Overall, these reforms helped India shift from a protectionist and regulated economy to a market oriented economy, leading to increased economic growth, job creation and a rise in standard of living of the people in the country.

(iv) TReDS-2014: In order to solve the problem of delayed payments and working capital inefficiencies faced by Micro, Small and Medium Enterprises (MSMEs), the RBI introduced Trade Receivables Discounting System (TReDS) in 2014. TReDS is an electronic plarform where MSMEs can sell their trade receivables at a competitive rate to financiers, including banks and non-banking financial companies (NBFCs) through an auction mechanism.

Under it, the number if invoices uploaded and financed through the TReDS has more than doubled in the financial year 2021-22 and the success rates has improved to 94. 7% from 91. 3% a year earlier. It shows that a growing acceptance of TReDS among MSMEs and financial institutions, which is expected to grow in future further.

(v) Unified Payment Interface (UPI)-2016: It was launched by the National Payments Corporation of India (NPCI) in 2016 under the guidance of the RBI. The RBI has played a significant role in conceptualizing and developing the UPI platform, which aimed to provide a seamless and instant payment experience to users across India.

Since its launch, UPI has gained massive popularity among consumers and business alike, with the volume of UPI transactions increased manifold from 0. 45 crore in January 2017 to 804 crore in January 2023. The value of UPI transactions has also increased from just Rs:1700 crore to Rs: 12. 98 lakh crore during the same period. It shows that, the UPI has produced great impact on digital payments adoption in India, promoting financial inclusion and reducing the dependency on cash transactions.

(vi) Bharat Bill Payment System (BBPS)-2019: It was launched by the National Payments Corporation of India (NPCI) in 2019 under the guidance of RBI. It is an integrated bill payment system that offers interoperable and accessible bill payment services to customers through a network of agents or online channels. BBPS provides a one-stop solution for payment of various bills such as electricity, gas, municipality taxes, DTH, water, mobile postpaid, broadband, landline and more. The introduction of BBPS has helped in increasing the adoption of digital payments and has contributed towards the government's goal of creating a less-cash economy. From April to November 2023, BBPS processed Rs:1. 22-lakh crore or 689. 63 million (in volume) transactions compared to 2018's load of Rs. 9099. 3 crore (73. 39 million) transactions, this is an exponential leap.

(vii) Aadhar – Based eKYC-2019: In 2019, the RBI approved new Aadhaar EKC norms, paved the way for digital verification of identity and address. It has enables financial institutions to authenticate customers identities remotely, without the need for physical documentation.

Since its introduction, Aadhaar eKYC has significantly streamlined the customer onboarding process for banks, insurance companies and other financial institutions. Aadhaar eKYC transactions jumped 18. 53% to 84. 8 crore in the third quarter of the financial year 2022-23, indicating the increasing adoption and popularity of the digital identity verification method. In another move to promote digitalization, the RBI also allowed non-banking financial companies (NBFCs) to apply for Aadhaar eKYC authentication licenses, enabling them to perform online customer verifications.

(viii) Emergency Credit Line Guarantee Scheme (ECLGS): It (ECLGS) was launched by the Government of India in may 2020 to provide immediate credit assistance to small and medium enterprises (SMEs) affected by the COVID-19 pandemic. The RBI played a crucial role in the implementation of the scheme by providing necessary guidelines and regulatory support to banks and financial institutions.

The scheme has been successful in providing much-needed liquidity support to SMEs, as the credit to MSMEs by scheduled commercial banks in the past eight years has grown by 71% from Rs. 11. 71 lakh crore deployed during the financial year 2014-15 to Rs. 20. 11 lakh crore during the financial year 2021-22. This has helped to mitigate the financial stress faced by SMEs due to the COVID-19 pandemic and support overall economic recovery.

(ix) Account Aggregator (AA)-2021: The RBI launched the Account Aggregator (AA) framework in September 2021 to enable easier sharing of financial data across multiple financial institutions. The framework allows customers to manage their financial data from various financial entities in a secure and seamless manner through a constant-based mechanism.

After one year of its launch, India's Account Aggregator ecosystem boasts of 1. 1 billion. AA-enabled accounts and has already seen 2. 05 million users voluntarily shared their financial data with banks and financial institutions to avail loans etc. The launch of the Account Aggregator framework is expected to revolutionize the way individuals and small businesses manage their finances, making it easier and more convenient for them to access a range of financial services.

Conclusion

The RBI was established with a view to fostering the banking business and not for impeding the growth of such business. The standard for the exercise of the power have been laid down in section 22 itself. The RBI is a non-political body concerned with the finances of the country. The Reserve Bank's developmental role includes ensuring credit to productive sectors of the economy, creating institutions to build financial infrastructure and expanding access to affordable financial services. It also plays an active role in encouraging efficient customer service throughout the banking industry, as well as extension of banking service to all, through the thrust on financial inclusion. The RBI announces Monetary policy every year in the month of April. This is followed by three quarterly Reviews in July, October and January. The annual monetary policy made up of two parts viz, Part-A:Macro economic and monetary development, Part-B: Action taken and fresh policy measures.

Over the past 88 years, the RBI has played a pivotal role in shaping India's economy, and its contributions have been nothing short of remarkable. From introducing innovative policies to navigating through uncertain times, the RBI has always risen to the occasion and has served as the guardian of India's well-being. We can be sure that the RBI will continue to be at the forefront of India's growth story and laying the foundations for a self-reliant nation.

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