

# India: Monetary Policy, Financial Stability and Other Essays

C. Rangarajan

ACADEMIC FOUNDATION

---

NEW DELHI



# Contents

Introduction .....	11
--------------------	----

## Part I: Monetary Policy and Fiscal Issues

1. Challenges for Monetary Policy .....	31
<i>Historical Evolution</i>	
<i>Issue of Concern</i>	
<i>Objective; Transmission Mechanism; Intermediate Target;</i>	
<i>Level of Interest Rate; Exchange Rate Management;</i>	
<i>Financial Stability; Autonomy of Central Banks</i>	
<i>Conclusion</i>	
2. Financial Stability: Some Analytical Issues .....	61
<i>Defining Financial Stability</i>	
<i>Instability Bias</i>	
<i>Regulating Institutions and Markets</i>	
<i>Components of Regulation</i>	
<i>Regulating Payment and Settlement Systems</i>	
<i>Macroeconomic Stability</i>	
<i>Crisis Prevention and Crisis Management</i>	
<i>Monetary Policy and Financial Stability</i>	
3. The Importance of being Earnest about Fiscal Responsibility ...	85
<i>Fiscal Responsibility—The Debate</i>	
<i>Post-Reform Trends in Deficits</i>	
<i>Impact of Deficits on Economic Prospects</i>	
<i>Fiscal Adjustment—The Contrarian View</i>	
<i>In Defence of Fiscal Adjustment</i>	
<i>Targeting Deficits—Some Issues</i>	
<i>Conclusion</i>	

4. Dynamics of Debt Accumulation in India:  
Impact of Primary Deficit, Growth and Interest Rate ..... 99
- Introduction*  
*Decomposing Accumulation of Debt*  
*Some Data Preliminaries*  
*Accumulation of Central Debt*  
*Profiles of Growth and Interest Rates*  
*Accumulation of Primary Deficit*  
*Summary and Medium-Term Prospects*
5. Fiscal Federalism: Some Current Concerns ..... 123
- Federalism—As a Form of Government*  
*Fiscal Federalism*  
*Fiscal Transfers*  
*Competitive and Cooperative Federalism*
6. Issues Before the Twelfth Finance Commission ..... 133
- Fiscal Trends*  
*Sustainability Issues*  
*Design of Fiscal Transfers*  
*Vertical Dimension*  
*Horizontal Dimension*  
*Restructuring Issues*
7. Twelfth Finance Commission Report:  
Approach and Recommendations ..... 155
- Vertical Transfers*  
*Horizontal Transfers*  
*Role of Grants*  
*Debt Restructuring*  
*Institutional Changes*  
*Restructuring Public Finance*

## **Part II: Growth and Development**

8. Indian Economy: Challenges and Opportunities ..... 163
- Challenges Ahead*  
*1991 Reforms—Genesis*  
*Economic Reforms—Break with the Past*  
*Rationale Underlying Reforms*  
*Stabilisation and Structural Adjustment*  
*Uniqueness of India's Reforms*

	<i>Post-Reform Growth Performance</i>	
	<i>Six Challenges on the Way Forward</i>	
	<i>Technology</i>	
	<i>Sustaining the High Growth</i>	
	<i>Conclusion</i>	
9.	<b>Economic Growth and Social Development</b> .....	175
	<i>Evolution of Thinking on Growth</i>	
	<i>Performance of the Indian Economy</i>	
	<i>Interaction between Growth and Human Development</i>	
	<i>Efficiency in Expenditures</i>	
	<i>Conclusion</i>	
10.	<b>Economic Growth and Issues of Governance</b> .....	185
	<i>What is Good Governance?</i>	
	<i>Nexus between Good Governance and Economic Development</i>	
	<i>State and Market</i>	
	<i>Role of the Government</i>	
	<i>Good Governance—Characteristics</i>	
	<i>Conclusion</i>	
11.	<b>Employment and Growth</b> .....	197
	<i>Employment and Unemployment Scenario</i>	
	<i>Sectoral Distribution of Employment</i>	
	<i>Occupational Status of Workforce</i>	
	<i>Elasticity of Employment</i>	
	<i>Employment Projections</i>	
	<i>Conclusion</i>	
12.	<b>Rural Employment Guarantee Scheme: Physical and Financial Planning</b> .....	215
	<i>Physical and Financial Planning</i>	
	<i>Delivery Systems and Capacity Building</i>	
	<i>Asset Creation</i>	
	<i>Monitoring and Experience Sharing</i>	
	<i>Conclusion</i>	
13.	<b>State, Market and the Economy: The Shifting Frontiers</b> .....	225
	<i>Developments in the Literature</i>	
	<i>Government Intervention and Planning</i>	
	<i>Historical Experiences: East Asia, Russia and India</i>	
	<i>Conclusion</i>	

14.	National Statistical Commission: An Overview of the Recommendations .....	241
	<i>Approach of the Report</i>	
	<i>Administration of Indian Statistical System</i>	
	<i>Agricultural Statistics</i>	
	<i>Industrial Statistics</i>	
	<i>Services Sector Statistics</i>	
	<i>Infrastructure Statistics</i>	
	<i>Socio-Economic Statistics</i>	
	<i>Financial and External Sector Statistics</i>	
	<i>Price Statistics</i>	
	<i>Corporate Sector Statistics</i>	
	<i>National Accounts Statistics</i>	
	<i>Conclusion</i>	

### **Part III: Sectoral Issues: Industry, Power, Banking and Agriculture**

15.	Paradigm Shifts in Industrial Policy .....	273
	<i>Introduction</i>	
	<i>Pre-Reform Industrialisation Paradigm</i>	
	<i>New Economic Policy</i>	
	<i>Trends in Industrial Production</i>	
	<i>New Challenges</i>	
	<i>Technology Intensity</i>	
	<i>Road Map for Indian Industry</i>	
16.	Banking Sector Reforms in India .....	295
	<i>Banking in the Pre-Reform Period</i>	
	<i>Contours of Reforms</i>	
	<i>Processes of Reform</i>	
	<i>Way Ahead</i>	
17.	Financial Inclusion: Some Key Issues .....	307
	<i>Nature of Inclusion</i>	
	<i>Extent of Exclusion</i>	
	<i>Institutional Changes</i>	
	<i>Commercial Banks</i>	
	<i>Regional Rural Banks</i>	
	<i>Role of Technology</i>	
	<i>Micro Financial Institutions</i>	
	<i>National Rural Financial Inclusion Plan</i>	

18. Agricultural Credit: Reaching the Marginalised Farmers ..... 317  
*Banking Reforms and their Impact*  
*Credit to Agriculture*  
*Credit to Marginal Farmers*  
*Strategy for Enhanced Credit to Marginal Farmers*
19. Regulation of Tariffs in the Power Sector ..... 327  
*Elements in the Power Reform Process*  
*Role of Regulatory Commissions*  
*Tariff Fixation*  
*Price Discrimination*  
*Tariffs and Competition*  
*Other Issues*  
*Conclusion*
20. The Widening Scope of Insurance ..... 333  
*What is Insurance?*  
*Insurance and Growth*  
*Assessment of Risks*  
*Regulatory Framework*  
*Conclusion*
21. Reforming the Pension System ..... 339  
*Demographic Changes*  
*Existing Coverage of Pensions*  
*Issues in Pension Reform*

#### **Part IV: External Sector and Globalisation**

22. Globalisation and its Impact ..... 345  
*Introduction*  
*Historical Development*  
*Gains and Losses from Globalisation*  
*Concerns and Fears*  
*India and the External Sector*  
*Framework of Policy*  
*Conclusion*
23. Global Imbalances and Policy Responses ..... 367  
*Introduction*  
*Is it a Cause for Concern?*  
*Status of Global Imbalances*  
*Factors behind the Current Account Deficit of the US*

*Redressing Global Imbalances*  
*Fiscal Policy*  
*Monetary Policy*  
*Expanding Domestic Demand Outside the US*  
*Exchange Rate Policies*  
*Indian Response*  
*Conclusion*

24.	<b>Nature and Impact of Capital Flows</b> .....	385
	<i>Capital Flows: Magnitude and Composition</i>	
	<i>East Asian Crisis</i>	
	<i>Forms of Capital Controls</i>	
	<i>The Indian Experience</i>	
25.	<b>The Financial Crisis and its Fallout</b> .....	405
	<i>Evolution of the Crisis</i>	
	<i>Regulatory Failure</i>	
	<i>Immediate Tasks</i>	
	<i>Medium Term Concerns</i>	
	<i>Impact on India</i>	
	<i>Monetary and Fiscal Actions</i>	
	<i>Index</i> .....	411

Challenges for Monetary Policy , India: Monetary policy, financial stability and other Essays, published by Academic Foundation. Jan 2009. Rangarajan. Rangarajan (2009) " Challenges for Monetary Policy ", India: Monetary policy, financial stability and other Essays, published by Academic Foundation, New Delhi. Developing the money and securities markets in India " , Framework for Monetary stability: Policy Issues and Country Experiences. Jan 1994. Rangarajan. Rangarajan (1994) " Developing the money and securities markets in India " , Framework for Monetary stability: P... Growth with Stability. Traditionally, the monetary policy in India was focused on controlling inflation. This was done through the contraction of money supply and credit. However, this resulted in poor growth of the economy. Therefore, RBI adopted a new policy of growth with stability. Financial stability is the ability of an economy to absorb shocks and ensure that people retain confidence in the financial system of the country. Internal and External shocks can threaten the financial stability of a country and destabilize its financial system. Therefore, the RBI gives a lot of importance to maintaining confidence in the country's financial system through adequate regulation and controls. It also ensures that the objective of growth is not sacrificed.