IJCRT.ORG ISSN : 2320-2882

INTERNATIONAL JOURNAL OF CREATIVE RESEARCH THOUGHTS (IJCRT)
An International Open Access, Peer-reviewed, Refereed Journal

Monetary Policy And Role Of Central Bank

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ABSTRACT

monetary policy is a set of tools used by a country central bank to manage the money supply and interest rates to achieve macroeconomics goals like price stability and maximum employment. Central banking involves the oversight of a country currency and financial system to implement these policies, which can be expansionary (to stimulate the economy) or contractionary (to cool down). The primary tools for this are manipulating interest rates, reserve requirements and conducting open market operations, reserve requirements, and setting interest rates, influencing borrowing, sending and investment throughout the economy. The primary goal is to control inflation while supporting economic growth and financial stability.

- monetary policy: A set of actions a nations central bank can take to manage the money supply and credit conditions to achieve macroeconomic objectives such as price stability and sustainable economic growth.
- main objectives of monetary policy:

1. Maintain price stability, which usually means keeping inflation low and stable.
2. Promote high employment.
3. Contribute to economic stability and predictable exchange rate.

- Central banking: the management and oversight of a country currency, money supply, and interest rates by a central institution.
- Key functions of central bank: 1. Monetary policy implementation.
  2. Issuing currency.
  3. Managing foreign reserves.
- key relationship: central banks execute monetary policy to achieve their mandates, which include price stability and maximum employment. They are often given independence from the government to prevent short term political motivations from interfering with long term economic goals.

keywords: monetary policy, money supply, interest rates, financial stability, foreign reserve, macroeconomic goals.

1.1 Bank rate

- The bank rate is the rate at which the central bank lends money to commercial banks without any collateral for long term purposes.
- when the bank rate increases, borrowing becomes costlier for banks, so they lend less- this reduces money supply.
- when the bank rate decreases, borrowing becomes cheaper, and banks lends more- increasing the money supply.

1.2 Repo rate

- The repo rate (repurchase rate) is the rate at which the central bank lends short term funds to commercial banks against government securities.
- the increase in repo rate makes loan costilier, reducing lending and controlling inflation.
- the decrease in repo rate encourages more borrowing and boosts liquidity in the economy.

1.3 Reverse repo rate

- the reverse repo rate is the rate at which the central bank borrows money from commercial banks.
- when the rate increases, bank prefer to keep their money with the central bank (to earn safe interest), which reduces lending capacity.
- when it decreases, banks lend more to the public, increasing money flow.

1.4 Cash reserve ratio (CRR)

- CRR is the percentage of banks total deposits that must be kept as cash reserves with the central bank.
- A higher CRR means banks have less money to lend- reducing capacity.
- A lower CRR means banks can lend more- increasing lending capacity.

1.5 Statutory liquidity ratio (SLR)

- SLR is the percentage of a bank total deposits that must be maintained in the form of cash, gold, or government approved securities before lending.
- higher SLR means banks have less money to lend- credit tightens.
- lower SLR means banks can lend more- credit expands.

2. Open market operations

Open market operations refer to the buying and selling of government selling of government securities (like bonds or treasury bills)

by the central bank in the market. It is used to control the money supply and influence interest rates in the economy.

RATES	CURRENT VALUE	EFFECTIVE DATE
Cash reserve ratio	**4.5%**	**8september,2023**
Repo rate	**6.5%**	**8 february, 2024**
Reverse repo rate	**3.35%**	**8 february, 2024**
Bank rate	**6.75%**	**3 may, 2023**
Statutory liquidity rate	**18%**	**5 may, 2023**

Table no: 1 (Rates in 2025)

3. Conculsion:

The central bank plays a vital role in maintaining the stability and growth of a nation economy through its monetary policy. By adjusting key policy rates such as the bank rate, repo rate, reverse repo rate, cash reserve ratio, statutory liquidity ratio, the central bank regulates the supply of money, controls inflation, and ensures adequate credit flow in the economy. through open market operations, it influences liquidity and interest rates, striking a balance between economic growth and price stability. These instruments work together to promote sustainable development, maintain public confidence in the financial system, and achieve macroeconomic goals such as full employment and financial stability.

4.Reference:

1.dnpgcollege.ac.in

2. International monetary funds

3. Chatgpt