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Date: 3 September, 2019

1. Does the payout of ₹1.76 lakh crore to the government damage the credibility of the Reserve Bank of India as an independent central bank?

- Why this year RBI has a different payout?
- What are the ways in which RBI earn money?
- What is the controversy involved?
- What could be the implications of this move?

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GS paper 3 (Indian Economy)

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In this video, you can find detailed answers for all the above questions.

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Express Web Desk . (2019, August , 14). India, China no longer 'developing nations', won't let them take WTO 'advantage': Trump. Indian Express. Retrieved from https://indianexpress.com/article/world/india-china-advantage-developing-nations-tag-wto-trump-tariffs-5904775/

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What is the context about?

- It was on August 26, when the Reserve Bank of India (RBI) central board decided that Rs. 1.76 lakh crore to be transferred to the government (which also includes a sum of Rs. 52,637 crore from its contingency reserve). This move was likely to look into the Central government's uncertain fiscal situation.

- As identified under a new Economic Capital Framework (ECF) adopted by the RBI board.The transfer amount included the dividend payment of Rs. 1.23 lakh crore, and funds from its reserves. A committee chaired by former RBI Governor Bimal Jalan was formed to review its ECF last year.

Why this year RBI has a different payout?

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Normally, RBI use to transfer that money in its balance sheet to the central government that it deems to be out of its operational and contingency needs.

But, this year the amount of funds which is transferred by the central bank (RBI) to the government is very much higher than its transfer last year (approximately 146.8% more than what it had paid out last year when it transferred Rs. 50,000 crore as dividend as compared to Rs. 1.76 lakh crore this year.)

Even the highest amount of surplus funds being transferred by the RBI in previous years (Rs. 52,683 (2013-14); Rs. 65,896 (2014-15); Rs. 65,880 (2015-16); Rs. 30,659 (2016-17) and Rs. 50,000 (2017-18)) to the central bank were lower than that of this year.

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What is the controversy involved?

- The major concern that has came up in the forefront is that the government might be confiscating money from the RBI to meet its urgent spending needs. This is what is turning the central bank into a government's piggy bank where it can store money to meet their unforeseen spending needs.

- Generally, the central banks such as the RBI, are supposed to be independent from all forms of influence from the government and its agencies. But, in reality, governments across the world try to influence decision-making by their respective central banks in multiple ways.

- When it comes to appoint members to the central bank, such as the post of Governor, the governments always tends to pick those bureaucrats who have been and will be loyal to them.

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What are the ways in which RBI earn money?

- Open market operations, in which a central bank purchases or sells bonds in the open market in order to regulate money supply in the economy and is considered as the major source of RBI's income.
- Favourable changes in bond prices may also profit the RBI, apart from the interest received from these bonds.
- Dealings in the foreign exchange market that the RBI engages in may also contribute to the profit of the central bank. For example, RBI may buy dollars cheaply and sell them in the future to make profits.

It should kept in mind, however, that the primary objective of the RBI is not to earn profits but to preserve the value of the rupee. These profit and loss are merely a side effect of its regular operations to shape the monetary policy.

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What could be the implications of this move?

- It is highly expected that the government will achieve its 3% fiscal deficit target this year with the help of these surplus funds from the RBI. Is is also expected that these fresh funds will help the government to spend more on any fiscal stimulus plan that it may decide to implement in order to check the slowdown in the economy.
- But, it should be noted that the transfer of money from the RBI to fund government spending will increase the amount of money supply in the economy, which will exert an upward pressure on prices. Thus this transfer of surplus funds from the RBI to the government could effectively turn into a monetary stimulus for the economy which has been slowing down for several consecutive quarters.

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