RBI'S REPO RATE: PAST AND PRESENT SCENARIO

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ABSTRACT

In India, the central monetary authority is the Reserve Bank of India is so formulated as to maintain the price stability in the economy. Repo Rate is the rate at which RBI lends to commercial banks generally against government securities. Reduction in Repo rates helps the commercial bank to get money at a cheaper rate and increase in Repo rate discourages the commercial bank to get money as the rate increase and becomes expensive.

The RBI governor Mr. Raghuram Rajan shocked investors by increasing Repo rate which it lends to bank by 25 basis points to fight inflation and inflationary expectations. The Repo rate has increased to 7.5% from & 7.25% with immediate effect. RBI reduced minimum daily maintenance of the CRR is not contemplated. Economic growth has weakened with continuing sluggishness in industrial activity and services, the pace of infrastructure Project completion subdued and the start of new project remains muted. Current account deficit have been mighty gated by steps taken by the government and the RBI. Steps have been taken to improve the environment for external financing turning the focuses to internal determinates of the value of the Rupee, Primarily the fiscal deficit and domestic inflation. RBI has tightened the norms for loans against gold jewellery. Market sentiments have to be improved, to stop under valuation of Rupee against major foreign currencies.

INTRODUCTION

The reserve bank of India was established on the basis of the recommendations of the Royal Commission on India Currency and Finance also known as Hilton Young the Royal Commission on India Currency and Finance also known as Hilton Young Commission. The Reserve Bank of India act, 1934 (2nd of 1934) provides the statutory basis of the functioning of the bank, which was implemented in 1935. The Reserve bank of India is the central bank of India is the Central Bank of the country. Central banks are a relatively recent innovation and most central banks were set up around the early century. Reserve bank of India was constituted to regulate the issue of bank notes, maintain reserves with a view for securing monitory stability and to operate the credit and currency system of the country for its advantage. The bank started its function by taking over from the government. The functions so far being performed by the controlled of currency from Imperial bank of India, the management of governments account and public debt. after the partition the reserve bank if India served as the central bank of Pakistan till June 1948. The bank, which was originally set up as a share holders bank was nationalized the impact of liberalization, bank focused to central banking functions like monitory policy, Bank Supervision and Regulation and overseeing the payments system and onto developing the financial markets. Mr. C.D. Deshmuk was the first Indian Governor the 13th Prime Minister of India, Dr. Manmohan Singh was the Governor of reserve bank of India from 1985-1990 i.e. for five years, 321 days and at present Mr. Raghuram Ranjan is the Governor of Reserve Bank of India.

Important Tasks of the Reserve Bank of India are:

- To maintain the population's confidence in the system, to safeguard the interests of those who have entrusted their money and to supply cost-effective banking systems to the population.
- To manage foreign currency controls: facilitating exports, imports and international payment traffic and developing and maintaining the trade in foreign currencies in India.
- Issuing money (the rupee) and adequately ensuring a high quality money supply.
- Providing loans to commercial bank in order to maintain to grow the Gross National Product (GNP).
- Acting as the Government's banker.
- Acting as the bank's banker.

THE RESERVE BANK OF INDIA HISTORY PROJECT

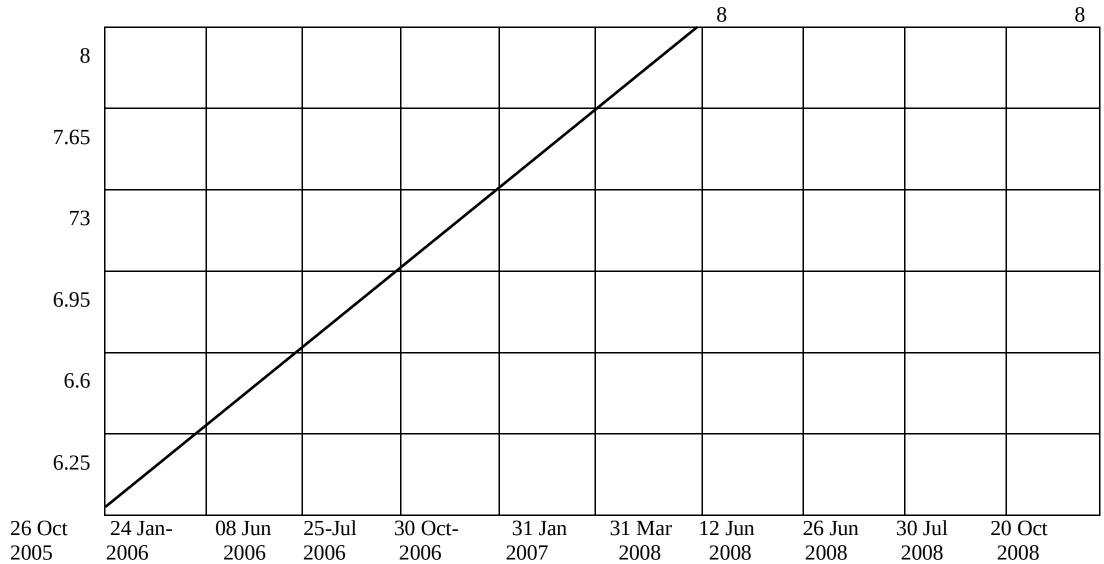
So far the reserve bank of India has published. The first volume (1935-1950) written by Mr. S.L.M. SIMHA under the guidance of the editorial committee headed by former Governor C.D. Deshmuk which was published in 1970. The second volume holds a period of 1951-1967. The third volume period was 1967-1981 and was published in March 2006. This was the period when banks were leading towards nationalization and the post nationalization era, the "growth periods" of banking which was leading to an exponential expansion in banking, bringing banks to the masses.

RBI'S REPO RATE: PAST AND PRESENT SCENARIO

Repo Rate

Period to October 29. 2004, the reverse repo rate was known as the repo rate. The rate at which the Reserve Bank of India lends money to commercial banks is called repo rate. The repo rate in India is similar to the discount rate in the US. It is an instrument of monetary policy. Whenever banks have any shortage of funds they can borrow from the reserve bank of India. A reduction in the repo rate helps banks get money at a cheaper rate and vice versa. If the Repo Rate goes up, borrowing, becomes expensive. On 29th October 2013, India raises policy repo rate to 7.75%. The reserve bank of India has raised its policy repo rate for the second consecutive month by 25 basis points to fight high inflation and rolled back an emergency measure put in place in July to support the rupee. Following an assessment of the evolving microeconomic situation the reserve bank has decided: reduce the marginal standing facility (MSF) rate by basis points from 9.0% to 8.75% with immediate effect, increase the policy repo rate under the liquidity adjustment facility (LAF) by 25 basis points from 75.% to 7.75% with immediate effect, cash reserve ratio unchanged at 4.0% of net demand and time liability (NDTL) : and increase the liquidity provided through term repos of 7 day and 14-day tenor from 0.25% of NDTL of the banking system to 0.5% with immediate effect.

RBI REPO RATE

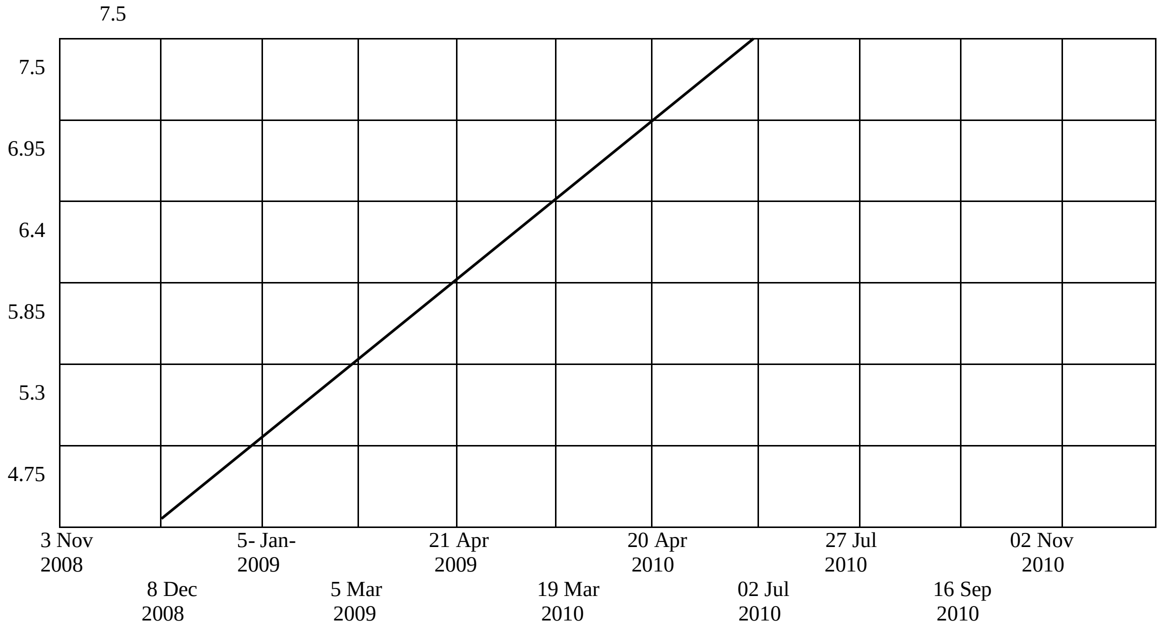


Reserve Bank of India Raises the Repo Rate to 7.5%. The reserve bank of India decided on September 20th to raise the repo rate by 25 basis points to 7.5% in an attempt to refrain inflationary pressures. At the same time, it reduced the marginal facility rate by 75 basis points to 9.5% to preserve the value of the rupee, while slacked back the minimum daily cash reserve ratio banks must keep with the central bank published on 2013-09-20. Reserve bank of India decided on July 30th to leave the repo rate unchanged at 7.25%, to support the rupee and citing increasing risks to growth outlook published on 2013-07-30.

PAST REPO RATE SCENARIO

For the past repo rate the time period is from 26th October 2005 to 2nd Nov. 2010. The graph shows that there was fluctuation in the repo rate. The minimum repo rate was 4.75% on 21 April 2009 and the maximum was 9% on 30th July 2008.

RBI'S REPO RATE



PRESENT REPO RATE SCENARIO

The minimum repo rate was 6.50% on 25th HJan. 2011 and the minimum was 8.50% on 16th September. Twice 8% rep rate was in June 2011 and April 2012. Twice it was 7.25% on 3rd may 2011 and on 3rd may 2013.

One basis point is one-hundred of the a percentage point. The rupee traded little changed at 61.48 per dollar as f 10:11 a.m. in Mumbai, compared with 61.46 on Oct 25, according to prices from local banks complied by Bloomberg. It rose and fell as much as 0.1 percent, One-month implied volatility, a measure of expected moves in the exchange rate used to price options, climbed eight basis points, or 0.08 percentage point, to 11.76 percent. The currently strengthened 1.8 percent this month after the federal reserve unexpectedly refrained from paring stimulus that's boosted demand for emerging-market assets. The Fed is likely to delay lowering its monthly bond purchases until March, according to a Blooberg News survey of economists conduced Oct. 17-18. While the repo increase was in the context of inflation management, RBI has shown greater comfort on external sector developments. One of the objectives of normalization of monetary policy has been achieved through the 25 bps cut the marginal standing facility (MSF) rate-the corridor between the repo and MSF rates has been brought to the earlier level of 100 bps. The Reserve Bank of India's ision to increase repo rate by 25 basis points in the second quarter review of monetary policy for 2013-14 was very much expected by the market. According to Bhatt" Insulate the economy of fluctuation in prices, the RBI has n other option than increase the policy rates, especially when business and consumer confidence is low. In the monetary policy review, the RBI has also decided to increase the liquidity provided through term reps of 7-day and 14-day tenor from 0.25 percent of NDTL (net demand and term liabilities) of the banking system to 0.5 percent and also to reduce the marginal standing facility (MSF) rate by 25 basis points from 9.0 percent to 8.75 percent. The extra liquidity given to the market by way of these two measures will bring down the interest rate in the near term, and will revert the interest rate curve to normal, recovering from earlier losses after a government panel recommended an immediate increase in state-subsidised diesel prices, reducing some concerns about the country's finance.

The government should raise diesel prices by about 9.5 percent or Rs. 5 ($0.08) a liter, along with other measures aimed t cutting the government's huge oil subsidy bill. The rupee also got a boost after the central bank risks excessive tightening, given the lag in monetary policy. The partially convertible rupee closed at 61.23/24 a dollar compared to 61.31/32 on Tuesday. It moved in a range of 61.23 to 61.60 during the session. The rates finished higher at 8.70 percent. It moved in a range of 8.80 and 8.50 percent. The RBI and the government have spent a fair amount of time trying to narrow the Current Account. "As of yesterday the Foreign Currency Non-Resident Account (Bank) deposits plus capital rising by the banks has reached $ 12 billion. International market are open to borrow in India. The central bank may have done enough on rate hikes, but they will need to monitor the economy. "I would not say that we have a set of rate hikes in mind and we are taking small steps towards that goal. The Indians have a very low tolerance for high sustained level of inflation. "There is some growth sacrifice already and there may be more of a growth sacrifice. We are getting calls from left, weight and center about the damage we are doing to growth. I do not think it is fair to say there is no growth sacrifice even now and we can't say that, as a result of the rate hike, there will be no additional growth sacrifice." He sad. "If we tighter signification more now, given the long lead time in monetary policy acting, we may find ourselves having over tightened and we do not want to go there with a weak economy."

CASH RESERVE RATIO (CRR)

The Cash Reserve Ratio is a tool used by the Reserve Bank of India to control the money supply ad interested. Cash reserve ratio is the amount of funds that the banks have to keep with the Reserve Bank of India. If the central bank decided to increase the Cash Reserve Bank of india, the available amount with the banks comes down. The Reserve Bank of India uses the Cash Reserve Ratio to drain out excessive money from the system. The Cash Reserve Ratio is the portion of funds that banks have to retain with the reserve bank of India. When the reserve bank of India increases this percentage, the amount actually avaibale with the commercial banks comes down. Cash Reserve Ratio checks the increase in prices.

RESERVE REPO RATE (RRR)

Reserve Repo Rate is the rate which the reserve bank of India borrows money from commercial banks. Banks are always happy to lend money to the Reserve Bank of India since their money is in the safe banks with good interests. When the reverse repo rate is increased banks find it more attractive to have their money with the reserve banks of India and hence money is drawn out of the system. If a borrower opted for a fixed rate loan, then his EMI repayment remain constant. Most fixed loans come with certain clauses that empower the lender to increase their lending rates. Monthly EMI repayments fluctuate in case of floating rates loans. If the interest rate goes up. the EMI increases. In case interest's rate go down the EMI deceases. Liquidity Adjustment Facility (LAF) is a facility that banks should be using as a resource to moderate their daily fluctuations to liquidity requirement rather than a window where they should be borrowing every day in large amounts. "By every rupee diesel prices are increases, saves about slightly less than 0.1 percent of GDP and therefore if diesel prices are brought fully to market, it would compensate for the increase in food subsidies, "said Rajan. RBI raised the repo rate by 25 basis points on Sept. 20, has said containing inflation is his top priority. Increased price pressures will prompt the RBI to raise the benchmark rate by 50 basis points this months, Taimur Baig, Singapore-based director of Asia economics at Deutsche Bank AG, wrote in a Oct. 16 report. Goldman Sachs Group Inc. sees the benchmark rising to 8.5 percent by March.

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ACRONYMS

- CRR-CASH RESERVE RATIO
- RRR-REVESRE RATE RATIO
- SLR-STATUORY LIQUIDITY RATIO
- CPI-CONSUMER PRICE INDEX
- MSF-MARGINAL STANDING FACILITY
- LAF-LIQUIDITY ADJUSTMENT FACILITY
- NDTL-NET DEMAND AND TIME LIABILITY
- WPI-WHOLESALE PRICE INDEX

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