Dr. M.G.R

EDUCATIONAL AND RESEARCH INSTITUTE

(Deemed to be University with Graded Autonomy Status)

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Maduravoyal, Chennai - 600 095, Tamilnadu, INDIA

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Monetary Policies

Monetary policy refers to the credit control measures adopted by the central bank of a country.

Johnson defines monetary policy “as policy employing central bank’s control of the supply of money as an instrument for achieving the objectives of general economics policy”.

G. K. Shaw defines it as “any conscious action undertaken by the monetary authorities to change the quantity, availability or cost of money”

Objectives or Goals of Monetary Policy

1. Full Employment
2. Price Stability
3. Economic Growth
4. Balance of payments

Instruments of Monetary Policy

The Instruments of monetary policy is two types

1. Quantitative, general or indirect
2. Qualitative, selective or direct

The special credit controls aim at controlling specified types of credit. They include changing margin requirements and regulation of consumer credit. The credit control instruments are:

- **Bank Rate Policy**
- **Open Market Operations**
- **Changes in Reserve Ratios**
- **Selective Credit Controls**

Fiscal Policies

- Fiscal policy means the use of taxation and public expenditure by the government for stabilization or growth.
- **According to Culberston**, “By fiscal policy we refer governments actions affecting its receipts and expenditure which are ordinarily taken as measured by the governments’ receipts, its surplus or deficit”.
- **Arthur Smithies** defines fiscal policy as “ a policy under which the government uses its expenditure and revenue programmes to produce desirable effect and avoid undesirable effects on the national income, production and employment”

Tools of Fiscal Policy

- The **two** main **tools of fiscal policy** are

<u>taxes and spending</u>

- Taxes influence the economy by determining how much money the government has to spend in certain areas and how much money individuals should spend.

Objectives or Goals of Fiscal Policy

Some of the **key objectives of fiscal policy** are

1. Economic stability
2. Price stability
3. Full employment
4. Optimum allocation of resources
5. Accelerating the rate of economic development
6. Encouraging investment, and
7. Capital formation and growth.

Role of Fiscal Policy in India

- Capital Formation
- Increase the rate of investment
- Encourage socially optimal investment
- Increase employment opportunity
- Economic stability in face of international instability
- Counteract inflation
- Flow of investment to socially desirable channels
- Check imbalance in various sectors
- Reduce inequality of income and wealth

Difference between monetary and fiscal policy

Fiscal Policy	Monetary Policy
Change in government spending and tax rates	Change in interest rates / money supply.
Set by the Government	Set by a Central bank
No specific target	Target inflation
Side effect on government budget / borrowing	Side effect on exchange rate and housing market
Strong political dimension to changing tax rates	Mostly independent from the political process

Role of Monetary and Fiscal Policies in maintaining real economic growth with stability.

- Both monetary and fiscal policy are macroeconomic tools used to manage or stimulate the economy.

- Monetary policy addresses interest rates and the supply of money in circulation, and it is generally managed by a central bank.

- Fiscal policy addresses taxation and government spending, and it is generally determined by government legislation.

- Monetary policy and fiscal policy together have great influence over a nation's economy, its businesses, and its consumers.

Role of Monetary Policy on economic growth with stability

Economic growth can be speeded up by **accelerating the rate of saving and investment** in the economy. This requires the following steps:

- Increase in the aggregate rate of savings.
- Mobilization of these savings so that they are made for the purpose of investment and production.
- Increase in the rate of investment.
- Allocation of investment funds for productive purposes and priority sectors of the economy.

Role of Fiscal Policy on economic growth with stability

- Fiscal policy are the tools used by governments to change levels of taxation and spending to influence the economy.
- Fiscal policy can be swayed by politics and placating voters, which can lead to poor decisions that are not informed by data or economic theory
- Direct Spending To Specific Purposes
- Taxation to Discourage Negative Externalities
- Short Time Lag - The effects of fiscal policy tools can be seen much quicker than the effects of monetary tools.

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