Introduction
INTRODUCTION

The present study entitled "Role of Central Bank in Monetary Management of a Country with Special Reference to Reserve Bank of India" is an attempt to analyse the role of different Central banks, particularly, the Reserve Bank of India in managing the monetary system of the country especially after the liberalization and globalization.

Prior to the commencement of the twentieth century there had been no clearly defined concept of Central banking. Gradually, the control of currency and credit vested in one bank with the support of the State and subject to some form of State supervision and participation irrespective of the stage of economic development in the country. But the methods of monetary management vary in degree and sometimes in kind as between one Central bank and another, depending upon the particular stage of economic development of a country, the volume and variety of its material resources, the makeup of its banking and credit structure, the nature of its international financial relationship, the state of development of its capital market, the degree of organization and activity of its money market. The
methods of Central Banks also vary in kind and in degree as between one period and another in accordance with the need for adjustment to fundamental changes in economic conditions and in the trend of political thought and action. Despite all these variations there lies a large measure of agreement in practice and Central bankers are to be found all over the world with more or less the same outlook on monetary and banking matters.

Review of Literature:

_Deepak Mohanty, Amitava Sardar and Abha Prasad_ (1997); in the paper entitled "Perspectives of Monetary Developments and Policy in India", makes an attempt to capture the monetary developments, and the theoretical and empirical underpinnings of monetary policy, in particular the changing efficacy of various instruments of monetary policy in India. It delineates the evolution of the role of monetary policy from one of developmental in nature during 1950s and 1960s to that of neutralizing huge liquidity generated in the economy consequent upon weakening of fiscal balance of the Government during 1970s and 1980s. This was also followed by institutional reforms during 1990s culminating in the supplemental agreement between the practices of automatic monetisation of fiscal deficit. While analyzing these developments, the article also focuses on how
the emphasis on various monetary policy instruments have evolved from essentially one of direct and administered instruments to that of relatively indirect and market based instruments. The analysis of money, output and prices in a historical perspective shows that unbridled growth of money supply translates largely into rise in prices underscoring the need for prudence in monetary management.

Manohar Rao, M.J. (2003); the paper entitled, "Science of Monetary Policy – some perspectives on the Indian economy", exposit the monetary policies design problem within the limits of an empirical framework for the Indian economy. It first looks at a few of the theories that have been advanced to explain the stylized facts of economic fluctuations and then examines the main features of business cycles in the Indian economy over the past 50 years. Secondly, it empirically measures the threshold rate of inflation within the framework of growth-inflation trade offs and derives the optimal rate of monetary expansion needed to smooth out fluctuations and stabilize the inflation rate at its threshold level. He estimated the optimal rate of monetary expansion around 15 percent to stabilize the inflation rate at the threshold level and the corresponding optimal fiscal deficit, which maximizes the growth rate around 4 percent of GDP.
Sayers, R.S. (1967); in his book entitled, "Modern Banking" have discussed about the economic importance of Banks. According to him a full discussion of the 'monetary' influences on the country's economic activity would have to include an examination of the behaviour of a very wide range of financial intermediaries and the business of the banks. But at the same time while trying to trace the influence of the banks on the level of total demand some regard must be paid to the great web of other financial claims that serve nearly but not all the purposes of money.

Meltzer, Alan H. (1997); in his book entitled, "On Making Policy More Effective Domestically and Internationally" published from McMillan Press Limited, London have found that the conduct of monetary policy has become extremely complex in the environment of interdependent risks. In fact the choice of monetary arrangements depends more on the choices that other countries make.

Dr. Rakesh Mohan, (Deputy Governor, RBI); in his paper entitled, "Challenges to Monetary Policy in a Globalising Context" published in the Reserve Bank of India bulletin, January 2004, have discussed the recent global development and the monetary policy operations. In this paper he emphasizes that the globalisation has expanded economic interdependence and interaction of countries greatly, which
has created the need for greater coordination in terms of the design of appropriate institutional architecture as well as standardization reflected in the adoption of similar monetary policy approaches.

De Kock, M.H. (1987); in his book entitled, "Central Banking" have discussed about the evolution of Central banking as a technique of monetary management. He analysed the methods adopted by different Central banks and concluded that the methods vary in degree and sometimes in kind as between one Central bank and another, depending upon the particular stage of economic development of a country, the volume and variety of its material resources, the make-up of its banking and credit structure generally, the nature of its international financial relationship, the state of development of its capital market and the degree of organization and activity of its money market. But despite all these variations there lies a large measure of agreement in practice, and Central bankers are to be found all over the world with more or less the same outlook on monetary and banking matters.

Narendra Jadhav (2003); in his paper entitled, "Central Bank Strategies, Credibility and Independence - Global Evolution and the Indian Experience" have offered a comprehensive perspective on Central banking in India. The genesis, evolution and development of
the Reserve Bank of India, the domestic compulsions and evolution of international best practices have been analysed thoroughly. Formulation and the conduct of monetary policy, financial stability and management of the changes in the payment and settlement system in the changed environment have been discussed clearly and also highlighted the challenges and the policy dilemmas faced by the Central bankers around the world. Finally, he concluded that Central banks must, at any given time, simultaneously pursue three objectives of price stability, growth and financial stability.

Thus a lot of work has been done on the monetary management of the Central banks and many more would be in the process. In fact review of these literatures helped me a lot in building the arguments and in setting up the objectives of the research work.

Objectives:

In the light of research topic, "Role of Central Bank in Monetary Management of a Country with Special Reference to Reserve Bank of India", the following objectives have been set.

(1) To examine the relationship between money, output and prices.

(2) To know the trade-off between inflation and growth.
(3) To examine the efficacy of different instruments of monetary management after the financial sector reforms.

(4) To analyse whether a single target, single instrument rule is preferable over the multiple target approach.

(5) To know whether the monetary targeting is still feasible in the changed environment or not.

Plan of Study:

Though, the conduct of monetary policy in India has transformed over the past 54 years, but the transition from a planned economy to a market economy in the 1990s, sharpened the Reserve Bank’s monetary management dilemma of providing credit to both the Government and the commercial sector at a reasonable cost, while at the same time containing inflationary pressures. The sudden external shocks require a hardening of monetary conditions in order to ensure orderly conditions in the financial markets, while the growth objective presaged a softer interest rate regime. The increasing complexities of monetary management forced the Reserve Bank of India to adopt a multiple indicator approach in which a host of macroeconomic variables are monitored for the process of monetary policy formulation. The relative efficacies of the different instruments and the environment in which they have been applied
have undergone a sea-change. The complete study has been divided into five chapters.

In the First Chapter we have primarily dealt about the evolution of Central banking as a technique of monetary management. The objectives and the operating procedures of different Central banks in the changed environment have been also dealt. The births of the Reserve Bank of India and its role in the monetary management have also been discussed.

The Second Chapter deals with general instruments of monetary management viz., Bank rate, Open market operations and Cash reserve ratio in detail. Their relative efficacies especially after the liberalization have been discussed.

The Third Chapter deals with the selective methods of monetary management. In this chapter the use of different selective methods like, margin requirements, interest rate differential and moral suasion etc have been discussed in three phases — pre-nationalisation period, post-nationalisation period and post-liberalisation period.

The Fourth Chapter deals with the impact of monetary policy on various macro-economic variables. The relationship between
inflation, growth and money supply has been established. The transmission channels have been discussed and effort have been made to find the effective transmission channel especially when the economy is affected not only due to internal factors but also due to external shocks.

Fifth and the Last Chapter is the summary and conclusion which concludes about the role of Central banks especially Reserve Bank of India in the monetary management after analyzing and testing the different parameters under different circumstances especially after the 1990.

Hypothesis:

We have formulated the null hypothesis, which has to be accepted or rejected as per the findings:

(i) $H_0$: Financial liberalization and globalisation has made the relationship between money, output and prices unstable and unpredictable.

(ii) $H_0$: There is a trade-off between growth and inflation at least in the short-run.

(iii) $H_0$: Every Central bank should pursue a single target, single instrument rule.
(iv) $H_0$: Interest rates and exchange rate has replaced the monetary targeting as an anchor of monetary management.

**Research Methodology:**

Since the Research work is evaluating in nature. We have to evaluate the performance of the Reserve Bank in monetary management especially after the liberalization. Therefore all the data are secondary in nature, collected mainly from the Publication Department of the Reserve Bank of India and the Economic surveys of the Government of India. In order to test the different hypothesis, correlation coefficient has been used which shows the interdependence of different variables like inflation, GDP growth and money supply. Moving averages and graphs have been also used to depict the relationships among inflation, output and money supply in the economy.