

IMPACT OF MONETARY STIMULUS PACKAGE TO COUNTER ECONOMIC CRISIS – COVID 19

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ABSTRACT

The Covid-19 outburst both supply and demand shocks. Aggressive monetary stimulus that inject liquidity and support investment can offset the effect of demand and supply shock. Policy makers in the developing economies must assess the efficiency and socioeconomic consequences of the moderation policies. In the short run the economic policy of the developing economy was dedicated on providing crisis relief to vulnerable population as in the short run it is not possible to stimulate the system. The study's goal is to examine the impact of monetary stimulus package for the Indian economy to kick-start the economy out of the stagnation trap. This paper is an exploratory research. The data used in this paper is from the reports made by an international and national organisation like WHO, IMF, Report by Reserve bank of India, articles from newspapers, interviews by the experts in the field.

INTRODUCTION

The Covid-19 outburst combines aspects of both supply and demand shocks. Aggressive monetary and fiscal stimulus that inject liquidity and support investment can offset

the effect of demand and supply shock. In the short run the economic policy of the developing economy was dedicated on providing crisis relief to vulnerable population as in the short run it is not possible to stimulate the system. The objective of the study is to analyse the influence of monetary stimulus package for the Indian economy to kick-start the economy out of the stagnation trap. This paper is an exploratory research. The data used in this paper is from the reports made by an international and national organisation like WHO, IMF, Report by Reserve bank of India, articles from newspapers, interviews by the experts in the field. "The anticipated recovery for the economy depends chiefly on the length of the outbreak and the efficiency of the policy responses. Theories related to monetary policy and growth of the economy have speedily progressed over time captured by insignificances, divergences, and inconclusiveness and cross currents" (Brunner & Meltzer, 1972). Theories associated with the Economic growth and the monetary policy precede as far back to classical QTM (quantity theory of money) (Gali J., 2008). However, in the 1930's only modern theories approached to the forefront with the theory

of Liquidity Preference of Keynes following this by Monetarism an economic theory and successively by numerous theories, like theory of Real Business Cycles, the New Keynesian Economics and the Model of New Consensus (Goodfriend and King, 1997; (P. & Sawyer, 2008). For a long time, the influence of monetary policy on different variables and explicit on output has been the centre of research indistinctly in short-run and long -run (Walsh, 2003). There exist complex and contradictory relationship between economic policy and economic soundness. A prevailing survey has made an attempt to identify these dynamics.

A crucial point that appear is that to comprehend financial instabilities, monetary policy should intervene as an instrument at the period of crunch during crisis. The Reserve bank of India has come up with a stimulus plan to condense the ill-effects of the nation-wide lockdown. Main focus of the present paper is to discover the influence of monetary stimulus package in restraining financial insecurities in a developing market like India.

The research work has been divided into four subdivisions. The initial first part is a brief review of economic policy and economic stability dynamic forces which is followed by the literature on monetary policy and its influence on economic expansion. Next section gives a brief on the methodology. Further it will be followed by the section that handles the exploratory results and its implications. And the last part of the study takes down to the conclusion.

LITERATURE REVIEW

From the existing review of literature, we observed a wide range of both empirical

and theoretical research on the prevailing association between monetary policy and economic soundness.

Monetary theory is built on the design that the alterations in the money supply is the chief influencer of the economic activities. Irving Fisher, the chief promoter of the theory states that if the economy's supply of money rises then the business activities of the economy will also upsurge and also the other way around. That means there exist a direct relationship between supply of money and the economic activities.

Keynes, rejected the classical dichotomy He asserted that the theory of money and the theory of prices can be integrated through the theory of aggregate demand or the theory of output. The apparatus of the interest rate which will increase investment will finally increase income through multiplier (Keynes, 1936).The Monetarist theory assumes that the velocity of money (V) is relatively stable, this suggests that nominal income is chiefly the function of the money supply (Friedman & Schwartz, 1963) (Friedman M. , 1968). There is extensive documentation found in the prevailing literature that supports this (among others Bullard, 1999; (Nogueira, 2009).

Selected studies have established narrow or no influence of monetary instrument. (Cyrus & Koech Elias, 2014) inspected the outcome of fiscal and monetary instrument shocks on the growth of the economy in Kenya by employing VAR methodology on the time series data discovered that monetary resources have no impact on the real output. (Kamaan, 2014) Also initiate insignificant association between monetary policy and economy's growth. (Lashkary & Kashani, 2011) Observed the

influence of monetary variables on the growth of the economy in Iran and found insignificant association between the volume of money and the economy's growth, real economic variables and the level of employment.

An extended study on empirical research also authorizes that monetary policy is decisive for the growth of the economy. (Vinayagathan, 2013) Estimated the effect of monetary resource on the growth of the economy by using a seven-variable structural VAR for Sri-Lanka establish that rate of interest shock had a substantial effect on the output in accordance with the economic theory. (Onyeiwu, 2012) Studied the influence of monetary instrument by using the ordinary least square method for the Nigerian economy estimated a positive influence of monetary policy on the Economic (GDP) growth. (Billi & Verdin, 2014) Observed that monetary policy and the financial stability are intrinsically intertwined. As financial uncertainties can restrict economic growth and also hamper the Efficiency of monetary transmission. This shows that financial stability is important for the conduct of monetary policy. These opinions further reinforce the statement that these two variables (financial stability and monetary policy) are supportive in the long-run.

(Nair & Anand, March 2020) Enquiries about the monetary policy as an instrument to attain economic stability. The study after making comparison between rate of interest attained from the standard Taylor rule and asset price augmented Taylor rule concluded that aiming asset prices could be one of the potent ways to comprehend financial insecurities and resulting economy's slowdown. (Loayza V & pennings,

March2020). Discussed in the short run economic policy should be dedicated towards disaster relief to susceptible population and in the medium term monetary and fiscal stimulus should be used for the recovery of the economy.

METHODOLOGY

It is an exploratory research. The data used in this paper is from the reports made by an international and national organisation like WHO, IMF, Report by Reserve bank of India, articles from newspapers, interviews by the experts in the field. Nature of the paper is conclusive and suggestive to bring the attention of the readers towards the influence of monetary stimulus package at the outburst of covid-19 in restraining financial uncertainties in an emerging economy like India.

ANALYSIS AND DISCUSSION

Monetary stimulus – An Effort to elevate the Economy

The magnification of COVID-19 disturbances has conveyed urgency to comforting repayment pressures and refining access to working capital by moderating the burden of debt servicing, prevent the diffusion of financial stress to the real economy, and certify the steadiness of viable businesses and households. The Indian central bank professed a postponement of the moratorium on loan EMIs by three months .

Due to continuing disruptions of COVID-19 Developmental and Regulatory policy of the central bank publicised (on 27th march, 2020) that all commercial banks, cooperative banks and Non-bank financial companies to prolong the moratorium period for the three months

from 1st June, 2020 to 31st August, 2020 on term loan instalments. During the moratorium period the borrower is not obliged to make payment of an EMI on the loan amount. This time period may also be identified as EMI holiday as borrower is allowable to halt their loan payments. Under the usual situations, if the reimbursement of the loan has been deferred than the history of the borrower's credit and the risk classification of the loan will be unfavourably impacted. But as per the extension of the moratorium on loan EMI's given by the RBI the borrower's credit history will not be affected.

Owing to the extension of loan moratorium, the difficulties faced by individuals and businesses in making repayment of the loans due to cash flow and income interferences will

be reassured. And this delay of loan payments will not call for penal charges and also will not impact borrower's credit score. This step further going to reduce the Non-performing Assets of banks at least for certain time period.

Observing the evolving financial market and macroeconomic conditions; further the aim of the central bank of India was to inject more liquidity in the economy. Further, the central bank of India has reduced the repo rate and the reverse repo rate to confirm that banks lend credit to the productive sectors of the economic system instead of submissively park funds with the central bank (RBI). This decision of central bank continues to direct the proactive move under the monetary policy of India. These slashed rates will be supportive for the economy to revive the economy in the long run .

Figure 1: Policy Rates source: <https://rbi.org.in/>

Date	Repo Rate (%)	Reverse Repo Rate (%)	CRR (%)	SLR (%)
April 2021	4	3.35	3	18
May 2020	4	3.35	3	18
March 2020	4.4	4.4	3	18.25
February 2020	5.15	4.9	4	18.25
October 2019	5.15	4.9	4	18.75
August 2019	5.4	5.15	4	19.5

To handle the liquidity pressure of shadow banks and microfinance institutions central bank has freed up more capital (Rs 50,000 crore) that banks can lend targeted Long-term repo operation (LTRO). LTRO is a tool in which central bank offers liquidity to banks for a period of one to three years at the prevalent repo rate. In turn as a collateral to

the central bank the banks offer government securities with same or higher tenure. This measure will provide relief to the economy by preserving adequate liquid assets in the economy. It will further ease and incentivize banks to ensure the availability of credit and permitting healthy working in the financial markets.

In order to address the significant volatility in the domestic financial market and also to deliver relief to the Indian banking system, under the Marginal standing facility (MSF) banks limit to borrow funds from the Reserve bank of India in an emergency situation has been increased. This initiative will permit the Indian banking system to avail an extra additional liquidity of Rs 1, 37,000 crores under the window of liquidity adjustment facility (LAF) at the reduced MSF rate of 4.65 %.

In the outlook of COVID-19 the financial institutions like National Housing Bank, Small Industries Development Bank of India and National Bank for Agriculture and Rural Development are finding difficulties to raise

finance from the market. These financial institutions play a significant role in meeting the long-term funding desires and needs of the agriculture and rural sector, small industries and the housing finance companies. In the wake of COVID-19 pandemic, under the monetary stimulus to empower these financial institutions special refinance facilities of Rs 50,000 crore have been provided to NABARD, NHB and SIDBI in order to meet credit needs of the diverse sectors.

The next initiative taken under the monetary stimulus package declared by the central bank incorporated 60 percent rise in the WMAs (Ways and Means Advances) of states and union territories with the aim of providing relaxation

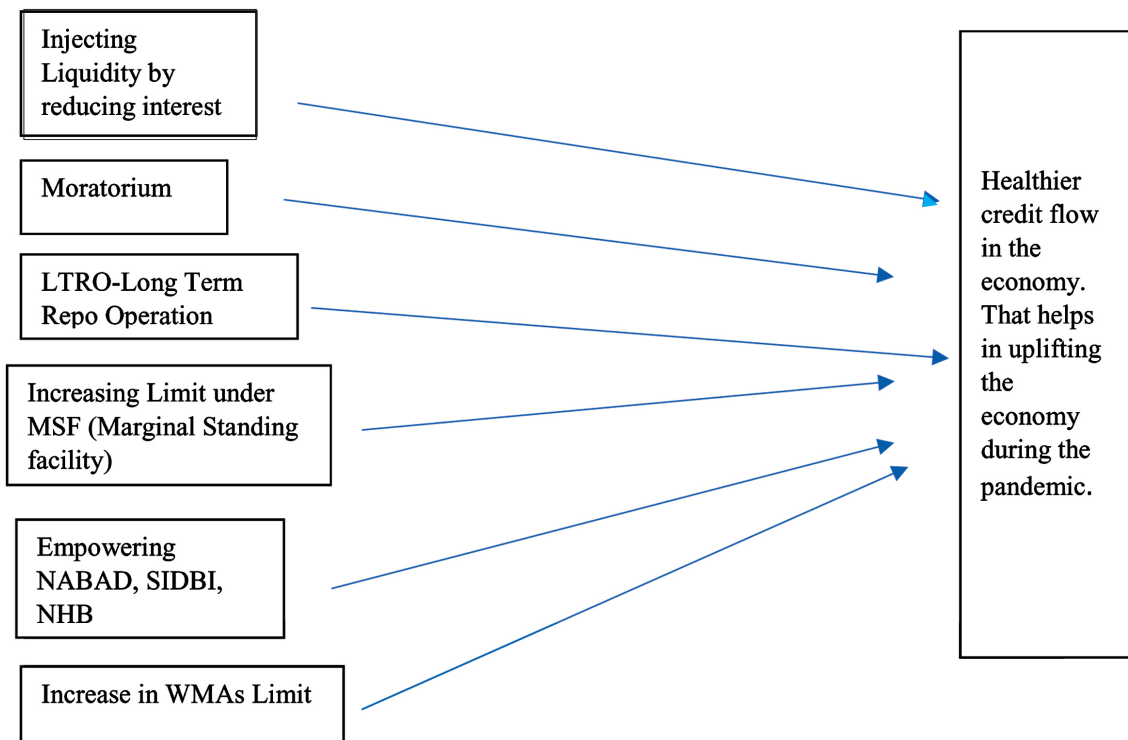


Figure 2: Model

to undertake the current pandemic suppression and the mitigation efforts. This move will also help them to plan the market borrowings better. In the outburst of COVID-19 India's exports and imports have contracted abruptly due to shrinkage in global activity and trade. The production and realisation cycles have been affected due to rescheduling of orders and deferral in realisation of bills. The decision by the regulatory body to upsurge the determined time period of the pre-shipment and the post-shipment export credit has been taken in understanding the prominence of exports in earning foreign exchange and in providing income and employment.

CONCLUSION

The Asian Development Bank (ADB) has anticipated that the GDP (Gross Domestic Product) of India will strongly recover due to constant economic retrieval improved by increased government stimulus, the ongoing vaccination drive and a flow in domestic

demand. Envisaging an optimistic picture "Asian Development outlook 2021" estimate that economic activity will continue to regularise and improve as supported by the government measures in the year 2020. The central bank of India on the monetary front reacted with a mix of Conventional monetary policy and unconventional monetary policy. Such liquidity measures have been incorporated in the monetary stimulus package to alleviate the damaging financial effect of the pandemic COVID-19. There has been significant reduction in the policy rates and around Rs.9.57 Lakh crore i.e. approx. 4.7 percent of the Gross Domestic Product has been injected in the economy since Feb 2020 to improve the availability of credit in the economic system (Ministry of Finance 2020). Central bank has taken numerous progressive and governing policy approaches to augment provision of liquidity to assist financial markets, stakeholders and also to ease the financial stress due to the pandemic COVID-19 by improving the flow of credit and firming credit discipline.

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