

General Studies – 2; Topic: Important aspects of governance, transparency and accountability

Autonomy of RBI

1) Introduction

- Relations between central banks and governments have never been easy anywhere. India is no exception.
- The demonetisation decision has led several observers to express concern about the autonomy and institutional integrity of the RBI
- Government directing the RBI on such matters and RBI acting accordingly is being seen as an infringement on its autonomy.

2) Role of RBI

- RBI has 3 main roles in which it acts as an autonomous body free from the interference of the government
- **Ensuring low and stable inflation**
 - a) Ensure low and stable inflation via the autonomous conduct of monetary policy.
 - b) Once the target is laid down by the central government, the central bank must ensure that it meets those targets with complete operational autonomy.
- **Debt management**
 - a) The RBI is the government's debt manager
 - b) This function has been proposed to be hived out to an independent debt management agency but resisted by the central bank.
- **Regulation of the banking system**
 - a) Government plays a separate role in the banking sector as the owner of public sector banks which control nearly 70 per cent of all lending.

3) Criticism

- United Forum of RBI Officers in a letter to RBI Governor had said employees were feeling "humiliated" by events since demonetisation
- They alleged that the government has been impinging on the central bank's autonomy by appointing an official for currency coordination.
- Three former governors -- Manmohan Singh, Bimal Jalan and Y V Reddy -- flagged concerns about the central bank's functioning.
- Former deputy governors, including Usha Thorat and K C Chakrabarty too have voiced their worries.

4) Why autonomy has not been affected?

- As per RBI Act, the Central Government may from time to time give such directions to the Bank as it may, after consultation with the Governor of the Bank, consider necessary in the public interest
- The reason behind this clause is so that any major decisions are made by the government which is elected and hence accountable to the people.
- The decision to demonetise high-denomination currency was taken by the government in public interest after consultation with the RBI
- The RBI board simply performed its duty by implementing the decision.
- The separation of debt management from the RBI is not an assault on the RBI's independence by the government.

- Instead, it is to remove the conflict of interest that exists in the RBI's functions of setting interest rates, and management of the government's debt.
- There has not been any assault on the RBI's autonomy — in the setting of interest rates or in the regulation of banks or in other operational spheres.
- As government is the owner of PSBs, government's interference is justified in case of disbursal of loans from PSBs.
- Consultations between the government and the RBI are undertaken on various matters of public importance wherever such consultation is mandated by law or has evolved as a practice.

5) Conclusion

- Government while demonetising the currency notes was acting within the norms of the law and did not assault the autonomy of the central bank.
- In a democracy, the final responsibility of all policy decisions must lie with Government
- Therefore there should be mutual cooperation and coordination between RBI and Government in large at public interests for an efficient and sustainable economy

