

## Monetary trends and developments

3.5 The increase of 12.6 percent in broad money ( $M_3$ ) during the current financial year (up to January 10, 2003) compared with 11.2 percent in the corresponding period last year needs a careful interpretation because of mergers. The merger itself increased  $M_3$  growth by 2.8 percentage points. On a year-on-year basis, growth of broad money, net of mergers, at 12.8 percent is lower than the growth of 14.5 percent last year.

3.6 Among the components of broad money, while currency with the public and time deposits (net of merger) registered a lower growth, demand deposits with banks registered a higher growth in the current financial year. On the sources side, growth in bank credit to the commercial sector and net foreign exchange assets of the banking sector have been significant. Net bank credit to Government registered a lower growth of 10.1 percent during the current financial year (up to January 10, 2003) as compared with 13.7 percent during the corresponding period last year mainly on account of negative growth of 21.0 percent in net RBI credit to Government. (Table 3.1)

3.7 The money multiplier-the ratio of  $M_3$  to reserve money- which had increased from 4.3 to 4.4 in the previous year, increased further to 4.8 as on January 10, 2003. Income velocity of broad money declined from 1.7 at the end of 2000-01 to 1.6 a year later. (Table 3.1)

3.8 A significant development in the current year is the lower growth of reserve money despite a substantial increase in the NFA of the RBI and primary support to the Government's borrowing programme. Reserve money grew by 2.9 percent during the current financial year (up to January 24, 2003) as compared with 4.7 percent in the corresponding period last year. While currency in circulation registered a lower growth of 9.3 percent during the current financial year as compared with 10.7 percent during the corresponding period last year, other components of reserve money registered a negative growth. Bankers' deposits with the Reserve Bank declined significantly by 15.7

percent in the current financial year as compared with a decline of 9.7 percent last year reflecting the impact of reduction in CRR. Among the sources, net RBI credit to the Government declined by 29.1 percent as compared with a decline of 0.9 percent recorded last year. In the current financial year, the amount raised by Government of India by way of gross market borrowings (long and medium term) amounted to Rs. 112,000 crore up to January 24, 2003. Out of this, an amount of Rs. 23,175 crore was in the form of private placement/devolvement on the RBI. However, the entire devolvement was subsequently liquidated by way of open market sales amounting to Rs. 53,626 crore. Thus, net RBI credit to Government remained negative during the current year. The second major source of reserve money, viz., net foreign exchange assets of the RBI increased significantly by 32.8 percent during the current year compared with 20.8 percent during the corresponding period last year. (Table 3.2)

3.9 Over the years, net foreign exchange assets of RBI have emerged as an important source of reserve money. From 9.1 percent as at end-March, 1991 the share of net foreign exchange assets in reserve money had reached 78.1 percent by the end of 2001-02. The share reached 100.7 percent on January 24, 2003. The substantial increase in the foreign exchange assets was partly neutralised by the negative growth of net RBI domestic credit.

3.10 Net RBI credit to Government has ceased to be an important source driving the growth of reserve money over the years. The share of net RBI credit in reserve money which was over 101 percent as at end-March, 1991 had come down to 45.0 percent by the end of March, 2002. The share further declined to 31.0 percent as on January 24, 2003. The declining trend in net RBI credit to Government is on account of the following two factors.

- Discontinuation of the practice of issuing ad-hoc treasury bills and automatic monetisation of budget deficit following the agreement between the RBI and the Government of India in 1997.

**Table 3.1 : Sources of change in money stock (M<sub>3</sub>)**

Items	Outstanding balances		Variations during										
	as on		Financial Year			Year-on-Year		Financial Year			Year-on-Year		
	March 31,	January 10,	2001-02		2002-03	2001-02	2002-03	2001-02		2002-03			
	2002	2003	Mar. 31 to Mar. 31	Mar. 31 to 11-Jan	Mar. 31 to 10-Jan	11-Jan over 12-Jan	10-Jan over 11-Jan	Mar. 31 to Mar. 31	Mar. 31 to 11-Jan	Mar. 31 to 10-Jan	11-Jan over 12-Jan	10-Jan over 11-Jan	
1	2	3	4	5	6	7	8	9	10	11	12	13	
			<i>Rs. crore</i>					<i>Percent</i>					
<b>I. M<sub>1</sub> (Narrow Money)</b>	422533	454490	43083	22719	31957	39729	52321	11.4	6.0	7.6	11.0	13.0	
<b>II. M<sub>3</sub> (Broad Money) (1+2+3+4)</b>	1500003	1689086	186782	146436	189083	185313	229429	14.2	11.2	12.6	14.5	15.7	
		[1,646,493]		[146,491]		[186,837]		[9.8]		[12.8]		[12.8]	
1. Currency with the public	241399	265687	31849	25423	24288	26601	30714	15.2	12.1	10.1	12.8	13.1	
2. Demand deposits with banks	178284	186123	12014	-1498	7839	13008	21351	7.2	-0.9	4.4	8.6	13.0	
3. Time deposits with banks	1077470	1234596	143699	123717	157126	145585	177107	15.4	13.2	14.6	16.0	16.7	
		[1,192,004]		[114,534]		[134,515]		[10.6]		[12.7]		[12.7]	
4. "Other" deposits with RBI	2850	2680	-780	-1206	-170	120	256	-21.5	-33.2	-6.0	5.2	10.6	
<b>III. Sources of change in money stock (M<sub>3</sub>)</b>													
<b>1. Net bank credit to Governemnt (A+B)</b>	586466	645684	74511	70327	59218	80864	63403	14.6	13.7	10.1	16.1	10.9	
A. RBIs' net credit to Government	152178	120210	-1699	-2119	-31968	-6637	-31547	-1.1	-1.4	-21.0	-4.2	-20.8	
( i ) Central Govt.	141384	113070	-5150	-2770	-28314	-9906	-30694	-3.5	-1.9	-20.0	-6.4	-21.4	
( ii ) State Govts.	10794	7140	3451	651	-3654	3269	-853	47.0	8.9	-33.9	69.2	-10.7	
B. Other banks credit to Government	434288	525474	76210	72446	91186	87501	94950	21.3	20.2	21.0	25.5	22.1	
<b>2. Bank credit to commercial sector (A+B)756265</b>	859250	77047	54097	102985	74864	125934		11.3	8.0	13.6	11.4	17.2	
A. RBIs' credit to commercial sector	5929	3002	-7358	-5677	-2927	-5512	-4608	-55.4	-42.7	-49.4	-42.0	-60.6	
B. Other banks' credit to commercial sector	750336	856248	84405	59774	105912	80376	130542	12.7	9.0	14.1	12.5	18.0	
<b>3. Net foreign exchange assets of the banking sector</b>	314733	388395	64913	37696	73663	51819	100880	26.0	15.1	23.4	22.0	35.1	
<b>4. Government's currency liabilities to the public</b>	6366	6851	1012	723	485	1011	774	18.9	13.5	7.6	20.0	12.7	
<b>5. Banking sector's net non-liabilities other than time deposits</b>	163828	211096	30702	16407	47268	23244	61562	23.1	12.3	28.9	18.4	41.2	
Memorandum Items													
1. Money Multiplier (M <sub>3</sub> )	4.4	4.8											
2. Velocity of Money	1.6												
<b>Note: 1.</b>	All figures are provisional. RBI data relate to March 31 after closure of Government Accounts. Variations in respect of Scheduled Commercial Banks (SCBs) are based on data for last reporting Friday of March. SCBs time deposits include Rs. 17945 crore on account of proceeds from RIBs ( Resurgent India Bonds), since August 28, 1998 and Rs. 25662 crore from India Millenium Deposits (IMDs) since November 17, 2000.												
<b>2.</b>	Monetary data are revised in line with the new accounting standards and consistent with the methodology suggested by the Working Group on Money Supply: Analytics and Methodology of Compilation ( June 1998). The revision is in respect of pension and provident funds with commercial banks are classified as other demand and time liabilities and includes those banks which have reported such changes so far.												
<b>3.</b>	Figures in bracket are net of merger of ICICI Ltd., with ICICI Bank.												

**Table 3.2 : Sources of change in reserve money**

Items	Outstanding balances			Variations during									
	as on		Financial Year			Year-on-Year		Financial Year			Year-on-Year		
	31-Mar-02	24-Jan-03	2001-02	2001-02	2002-03	2001-02	2002-03	2001-02	2001-02	2002-03	2001-02	2002-03	
			31-Mar	31-Mar	31-Mar	25-Jan	24-Jan	31-Mar	31-Mar	31-Mar	25-Jan	24-Jan	
		to	to	to	to	to	to	to	to	to	to		
		31-Mar	25-Jan	24-Jan	26-Jan	25-Jan	31-Mar	25-Jan	24-Jan	26-Jan	25-Jan		
1	2	3	4	5	6	7	8	9	10	11	12	13	
			<i>Rs. crore</i>					<i>Percent</i>					
A. Components of Reserve Money:													
a. Currency in circulation	250974	274329	32769	23359	23355	28371	32765	15.0	10.7	9.3	13.3	13.6	
b. Bankers deposits with RBI	84147	70920	2670	-7921	-13227	-998	-2636	3.3	-9.7	-15.7	-1.3	-3.6	
c. "Other" deposits with RBI	2850	2608	-779	-1331	-242	112	310	-21.5	-36.7	-8.5	5.1	13.5	
B. Sources of Reserve Money:													
1. Net RBI credit to Government <sup>2</sup>	152178	107823	-1699	-1418	-44355	2023	-44636	-1.1	-0.9	-29.1	1.3	-29.3	
2. RBI credit to banks <sup>3</sup>	10748	6956	-2217	-1719	-3792	-2351	-4290	-17.1	-13.3	-35.3	-17.3	-38.1	
3. RBI credit to commercial sector <sup>4</sup>	5929	2925	-7357	-5401	-3004	-5278	-4960	-55.4	-40.7	-50.7	-40.1	-62.9	
4. Net foreign exchange assets of RBI <sup>5</sup>	263969	350437	66794	40918	86468	47917	112344	33.9	20.8	32.8	25.2	47.2	
5. Government's currency liabilities to the public	6366	6851	1013	802	485	932	696	18.9	15.0	7.6	17.8	11.3	
6. Net non-monetary liabilities of RBI	101220	127135	21875	19075	25915	15758	28715	27.6	24.0	25.6	19.1	29.2	
<b>7. Reserve Money (1+2+3+4+5-6)</b>	<b>337970</b>	<b>347857</b>	<b>34659</b>	<b>14107</b>	<b>9887</b>	<b>27485</b>	<b>30439</b>	<b>11.4</b>	<b>4.7</b>	<b>2.9</b>	<b>9.5</b>	<b>9.6</b>	
<p><b>Note:</b> 1. Variations are worked out on the basis of March 31 data after closure of Governments accounts. Figures for 2001-02 and 2002-03 are provisional.</p> <p>2. Includes special securities.</p> <p>3. Includes claims on NABARD.</p> <p>4. Excludes, since the establishment of NABARD, RBI's refinance to banks.</p> <p>5. Variations are inclusive of appreciation in the value of gold following its revaluation close to the international market price since October 17, 1990. Such appreciation has a corresponding effect on RBI's net non- monetary liabilities.</p>													

- Adequate liquidity in the banking system leading to investment in Government securities far beyond the SLR stipulation of 25 percent.

3.11 With rising foreign exchange reserves, the NFA/currency ratio increased gradually from 14.4 percent as at end-March, 1991 to 105.2 percent as on March 31, 2002. The ratio stood at 127.7 percent as on January 24, 2003. The rising NFA/currency ratio has imparted flexibility to the monetary authority in the

conduct of the monetary policy. Continuous accretion to foreign exchange reserves has facilitated further liberalisation of foreign exchange restrictions on international current and capital account transactions. The Committee on Capital Account Convertibility recommended that fiscal consolidation, a mandated inflation target and strengthening of the financial system should be regarded as crucial preconditions/signposts for capital account convertibility (CAC) in India.