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Discovering the role of the monetary policy committee constituted by the reserve bank of India in 2016 in addressing the macroeconomic indicators in the economy. How effective have these instruments been in achieving meaningful macroeconomic indicators?

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ABSTRACT

Monetary policy plays a crucial role in maintaining macroeconomic stability by regulating inflation, influencing interest rates, and supporting sustainable economic growth. The establishment of the Monetary Policy Committee (MPC) by the Reserve Bank of India (RBI) in 2016 marked a significant shift in India's monetary policy framework through the adoption of Flexible Inflation Targeting (FIT). This study examines the role of the MPC in addressing key macroeconomic indicators such as inflation, GDP growth, and employment, while evaluating the effectiveness of the monetary policy instruments adopted since 2016 in achieving meaningful macroeconomic outcomes.

A comparative analysis of the pre-2016 and post-2016 monetary policy frameworks was undertaken to assess the impact of inflation targeting on macroeconomic performance. Particular emphasis was placed on evaluating the effectiveness of monetary policy instruments such as the repo rate, reverse repo rate, and open market operations in influencing inflation, liquidity, borrowing, investment, and overall economic activity under geopolitical disturbances.

The findings indicate that the establishment of the MPC improved the transparency, accountability, and credibility of monetary policy while contributing to greater inflation stability and strengthening the transmission of policy decisions. The analysis demonstrates that inflation remained within or close to the prescribed target range for most of the post-2016 period despite major external shocks, including the COVID-19 pandemic and the Russia-Ukraine conflict. However, the study also finds that monetary policy alone cannot effectively address supply-side inflation, imported inflation, geopolitical disruptions, or structural rigidities within the financial system. Overall, the research concludes that the monetary policy instruments adopted by the

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MPC have been largely effective in improving India's macroeconomic stability and have provided a more credible and predictable effect but are under stress in the current disruption of the current economic world order. Nevertheless, their long-term success continues to depend upon complementary fiscal policies, structural reforms, and a stable global economic environment.

Keywords: Monetary Policy, Geopolitical Disturbances, Repo-Rate, Open Market Operations, Structural Rigidities, Fiscal Policy.

1. Introduction

Most economies in the world today are primarily of the mixed economy model, where both public sector (managed by government) and private sector (managed by market forces) contribute towards economic activity and development. The private sector mainly works on the basis of profit motive and equilibrium of the market forces, while the public sector aims in providing social welfare and economic stability to its citizens. In the process it provides public goods and addresses market failures. To achieve these objectives, the government uses several economic policies including fiscal policy and monetary policy. Fiscal policy involves government expenditure and taxation that impacts economic activity, whereas monetary policy involves the regulation of money supply and rate of interests by the central bank .[10][11] Both policies aim to achieve macroeconomic objectives such as economic growth, full employment and price stability. They differ in the instruments used and the methods of implementation.[10] But they both need to work in the same direction so that they are in a position to make a sizable impact on the welfare of the country.

The supply of money is monitored by the central bank of a country. The instruments used have a significant influence on economic activity and thus requires careful monitoring. Monetary policy refers to the measures adopted by a central bank to regulate the money supply and influence economic conditions.Money demand can not be monitored by the central bank. They can only impact money supply. It is through the money supply that the RBI can try and influence the monetary demand.

Each economy needs a mechanism to control and balance the flow of money and maintain economic stability. Monetary policy points to the measures taken by the central bank to regulate the money supply and influence economic activity. By taking these measures into account central banks seek to affect key macroeconomic aims such as unemployment, price stability and inflation, thus making monetary policy an essential component in managing a country's economy. [1] The instruments in their control revise interest rates and attempt to control inflation and thus GDP.

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Central banks of other countries like the Federal Reserve in the United States or the Bank of England in the UK, use various instruments under their control in achieving various targets that have been set out for them. [1]

Changes in economic activity often occur due to expansion and contraction of monetary policy. This leads to fluctuations in growth, employment, and price. If left entirely to market forces the fluctuations might create economic instability and make sustained growth difficult to achieve. Therefore the Reserve Bank of India (RBI) has adopted various different stances of monetary policy over the years as a means of regulating economic activities and maintaining stability. [2] As the Indian economy is emerging, it is becoming increasingly integrated with the global market thus the need for a structured monetary policy framework is becoming more significant.[3]

Over time, this framework has evolved in response to changing macroeconomic and financial conditions, enabling the RBI to address emerging economic challenges more effectively. [3] Furthermore, in a developing economy such as India, where the banking sector serves as the primary channel of monetary transmission, monetary policy plays an important role in ensuring that policy decisions are transmitted to businesses and households, thereby contributing to sustainable economic growth and price stability. [2][3]It ensures the supply of money is regulated and adjusts the rates of interest.

The importance of this policy is to promote growth, and help maintain price stability [4]. In developing economies access to capital and financial resources are limited, monetary policy plays a significant role in the provision of the availability of credit for productive activities and development expenditure. [5] Additionally, an effective monetary policy structure helps create long term investments, stable expectations and reduces uncertainty. By doing this and maintaining a balance between economic growth and inflation, monetary policy contributes towards sustainable development while ensuring transparency, credibility and accountability in economic management.[5]

The primary objective of Monetary Policy Committees (MPCs) across the countries is to make sure that monetary policy instruments and targets are being efficient and at the same time maintaining economic stability. However there are notable differences between their functioning in developed and developing economics. Since developed economies generally operate in mature and bigger financial markets, they use different monetary policy strategies. In contrast developing economies such as India usually face challenges related to financial markets, limited access to capital and greater dependence on the banking sector for the transmission of monetary policy. [6][7]

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It is important to take into account the inherent structural issues that exist in various types of economies in order to evaluate the effectiveness of monetary policy structure. These differences highlight the importance of designing monetary policy frameworks according to the needs and challenges of an economy. Since developing and developed economies operate under different economic and financial conditions it is important to note that the effectiveness of their monetary policy committees may also vary. Thus understanding these distinctions is necessary for finding the role of monetary policy targets in supporting economic stability and long term growth in India. [6][7].

2. Literature review/ background

The monetary policy framework in India has gone through various significant changes over time to respond to the evolving economic and financial conditions prevalent in the economy. The Reserve Bank of India (RBI) was established in 1935 and is responsible for formulating and implementing monetary policy in India. Throughout the years following independence. Monetary policy prioritised supporting economic development and ensuring sufficient credit availability for key sectors of the economy. As India's economy became increasingly globalised and liberalised, international trade played an important role. The framework of monetary policy and its objectives evolves to address new challenges related to inflation, financial stability, and economic growth. [3][6]

The most important development in India's monetary policy framework was the adoption of *flexible inflation targeting and the establishment of the monetary policy committee* (MPC) in 2016. The framework tries to maintain price stability while keeping the objective of growth in mind. [6][7] Inflation targeting was introduced to improve transparency, accountability, and credibility in monetary policy decision making. By maintaining stable inflation, the RBI aims to create a favourable environment for investment savings, and sustainable economic development. [4][6]

The RBI uses a variety of monetary policy instruments to achieve these objectives. Some of these are the repo rate, reserve repo rate, cash reserve ratio, statutory liquidity ratio and open market operations. Through these measures the central bank regulates liquidity, influences interest rates and manages the supply of money within the country. [1][2][4] Effective usage of these tools helps the RBI to respond to inflationary pressures, economic recessions or slowdowns and changes in financial market conditions

3. Definition and working of Repo Rate, Reverse Repo Rate and Open Market Operations-

Among the various instruments of monetary policy, the repo rate, reverse repo rate, and open market operations are the most commonly and widely used by the Reserve Bank of India to

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regulate liquidity and influence economic growth. [1][2] The repo rate is the rate at which the RBI (the central bank) lends short-term funds to commercial banks against government securities. [2][3] A decrease in the repo rate reduces the cost of borrowing for banks, encouraging them to extend more credit to businesses and households, thereby increasing investment, consumption, and thus aggregate demand. Conversely, an increase in the repo rate makes borrowing more expensive and attracts savings by individuals, helping to control inflation by reducing excess demand. [2][4] The reverse repo rate is the rate at which commercial banks deposit their excess funds with the RBI. [2][3] By increasing the reverse repo rate, the RBI encourages banks to put more funds with the central bank, thereby reducing the money supply in circulation. In contrast, a lower reverse repo rate discourages banks from depositing their excess funds with the RBI, allowing more money to circulate within the economy. [2][4] Open market operations involve the purchase and sale of government securities by the RBI. [1][3] When the RBI purchases securities, it injects liquidity into the banking system, whereas selling securities withdraws liquidity from the market. Through the coordinated use of these instruments, the RBI regulates money supply, manages inflationary pressures, and promotes sustainable economic growth while maintaining overall financial stability. [1][4]

4. Research Gap and Methodology

This paper would attempt to understand how effective "inflation targeting" has been in steering the Indian economy in controlling inflation and achieving its growth targets. Has RBI changed the emphasis on its various instruments in staying on its decided path? How effective has its policies been when the country is faced by adverse geopolitical events?

The Methodology adopted would be of the mixed method type where both quantitative and qualitative strategies would be adopted in understanding the nuances of various policy measures. All data used would be from authentic sources. Quantitative data would be explained through qualitative explanation.

5. Analysis of the role of inflation targeting in achieving success in macroeconomics indicators before 2016

Table 1: comparative study of GDP and Inflation under the monetary policy followed by the RBI

Year	GDP Growth (%)	Inflation (CPI, %)	RBI/Government Inflation Target
2011-12	5.2	8.9	No formal inflation target

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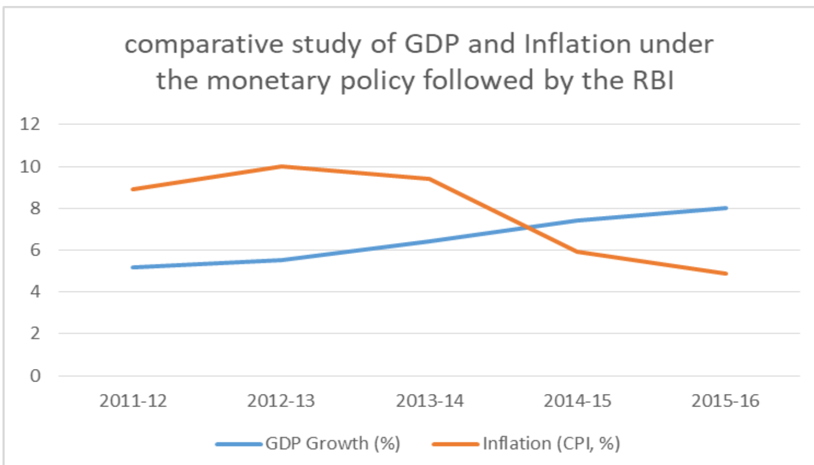
2012-13	5.5	10.0	No formal inflation target
2013-14	6.4	9.4	8% by January 2015 (Patel Committee disinflation glide path)
2014-15	7.4	5.9	8% (intermediate target)
2015-16	8.0	4.9	6% by January 2016 (before formal FIT in 2016)

Source: Reserve Bank of India, Handbook of Statistics on the Indian Economy; World Bank, World Development Indicators; World Bank, Inflation Targeting in India: An Interim Assessment; International Monetary Fund, India: Stabilizing Inflation.



The data presented in the table and graph above show that prior to the introduction of the Flexible Inflation Targeting (FIT) framework in 2016, India experienced various fluctuations in both inflation and economic growth. During 2011-12 and 2012-13, inflation remained constantly high at around 9-10%, while GDP growth remained relatively moderate, suggesting that the existing monetary policy framework faced many difficulties in simultaneously achieving price stability and sustained economic growth. [12][15] however GDP growth gradually improved between 2013-14 and 2015-16, inflation continued to remain above the desired level until the implementation of the RBI's disinflation glide path based on the recommendations of the Urjit Patel Committee. [12][14] This advice to reduce CPI inflation to 8% by January 2015 and 6% by January 2016 made an important transition towards a rule-based monetary policy framework, eventually leading to the adoption of *Flexible Inflation Targeting* in 2016. [12][15] As these measures were adopted, inflation declined significantly from 9.4% in 2013-14 to below 5% by

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2015-16, while GDP growth also strengthened over the same period. [12] This suggests that placing greater pressure on inflation management *helped to improve macroeconomic stability without significantly constraining economic growth or resulting in hyperinflation*. However, studies also indicate that the effectiveness of monetary policy during this period was constrained by weak monetary transmission, monetary policy transmission lags , and structural rigidities within the financial system, which limited the immediate impact of policy rate changes on the real economy. [5][16][17] These challenges revealed the need for a more transparent, credible, and accountable monetary policy framework, ultimately resulting in the establishment of the Monetary Policy Committee (MPC) and the formal adoption of *Flexible Inflation Targeting* in 2016. [13][14]

Despite the gradual improvement in macroeconomic indicators, the monetary policy framework followed before 2016 had several limitations. Since there was no explicit inflation target, the Reserve Bank of India had to pursue multiple objectives simultaneously, including controlling inflation, supporting economic growth, maintaining exchange rate stability, and ensuring adequate liquidity within the financial system. [12][15] This often created trade-offs, making monetary policy less predictable and reducing its overall effectiveness. Furthermore, inflation during this period was largely driven by supply-side factors such as rising food prices, global crude oil prices, and supply chain bottlenecks, which could not be effectively addressed through interest rate adjustments alone. [15][18] The absence of a formal Monetary Policy Committee also meant that monetary policy decisions lacked the transparency and collective decision-making process that exists under the present framework. Combined with weak monetary policy transmission and structural rigidities within the banking sector, these limitations reduced the speed and effectiveness with which policy decisions influenced inflation and economic activity, highlighting the need for a more credible and rules-based monetary policy framework. [5][13][16]

6. Analysis of the role of inflation targeting in achieving success in macroeconomics indicators after 2016

Table 2: comparative study of GDP and Inflation under the monetary policy followed by the RBI

Year	GDP Growth (%)	Inflation (CPI, %)	RBI Inflation Target
2016–17	8.3	4.5	4% ± 2%
2017–18	7.0	3.6	4% ± 2%

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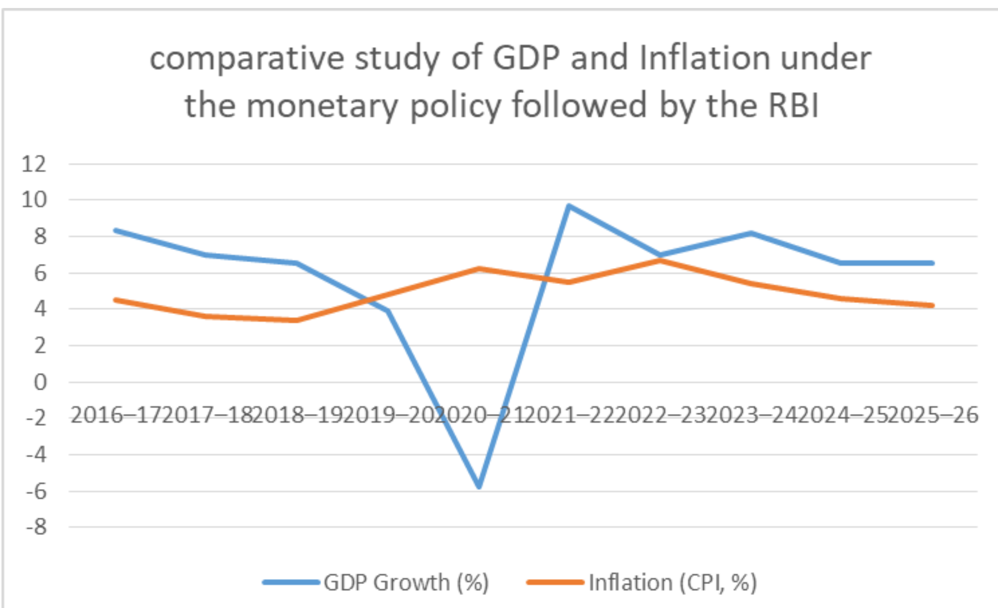
2018–19	6.5	3.4	4% ± 2%
2019–20	3.9	4.8	4% ± 2%
2020–21	-5.8	6.2	4% ± 2% *(COVID-19)*
2021–22	9.7	5.5	4% ± 2%
2022–23	7.0	6.7	4% ± 2% *(Russia-Ukraine conflict)*
2023–24	8.2	5.4	4% ± 2%
2024–25	6.5	4.6	4% ± 2%
2025–26	6.5	4.2	4% ± 2%

Source: Reserve Bank of India, Handbook of Statistics on the Indian Economy; World Bank, World Development Indicators; National Council of Applied Economic Research (NCAER), Eight Years of Inflation Targeting in India: An Assessment; Reserve Bank of India, Monetary Policy in India: Evolution, Framework and Recent Developments.



The data presented in Table 2 and the graph above indicates that the introduction of the Flexible Inflation Targeting (FIT) framework in 2016 contributed significantly towards improving India's macroeconomic stability. Throughout most of the period between 2016 and 2026, inflation remained within or close to the RBI's prescribed target range of 4% ± 2%, suggesting that the

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framework was largely successful in anchoring inflation expectations while maintaining price stability. [12][13][14] Although GDP growth experienced fluctuations during this period, particularly due to the COVID-19 pandemic in 2020–21 and the Russia-Ukraine conflict in 2022, the RBI continued to adjust monetary policy in response to changing domestic and global economic conditions. [14][15][18] The sharp contraction in GDP during the pandemic was followed by a strong economic recovery, indicating that the flexible nature of the inflation-targeting framework allowed the RBI to balance inflation control with the objective of supporting economic growth during periods of economic distress. [12][13] Furthermore, greater transparency in monetary policy decisions, regular Monetary Policy Committee (MPC) meetings, and improved communication with financial markets enhanced the credibility and predictability of monetary policy. [13][14] Studies also suggest that improvements in monetary policy transmission and greater coordination between monetary policy instruments strengthened the effectiveness of policy decisions compared to the pre-2016 framework. [16][17]

Despite these achievements, the *Flexible Inflation Targeting* framework continues to face several challenges. Inflation has not remained within the target range in every year, particularly during periods of severe external shocks such as the COVID-19 pandemic and the Russia-Ukraine conflict, when supply-side disruptions, rising food prices, and higher global energy prices placed significant upward pressure on inflation. [13][15][18] These factors were largely beyond the direct control of monetary policy as they were due to global disruptions and would be considered as "*imported inflation*". This limited the effectiveness of interest rate adjustments alone. Furthermore, although monetary policy transmission has improved since the establishment of the MPC, studies indicate that transmission lags, imperfections in the banking channel, and structural rigidities continue to delay the full impact of policy decisions on borrowing, investment, and economic activity. [5][16][17] Therefore, while the post-2016 monetary policy framework has been considerably more transparent, credible, and effective than its predecessor, achieving the inflation target consistently remains dependent on both domestic economic conditions and external global developments. [13][14][18]

Except in exceptional circumstances like the pandemic, the Russia-Ukraine war and the current US-Iran war, the MPC and the RBI have limited tools at its disposal to address runaway inflation. The best policies available for the RBI is to use its own resources to control the inflationary impact and stem the depreciation of the Rupee.One way is to implement conditions within the Indian Banking System that would attract foreign direct investment (FDI). The current MPC in its latest meeting of June 5, 2026 has decided to keep the repo rate unchanged at 5.25% and a status quo on interest rates. The RBI has also launched a temporary dollar-rupee swap facility and has removed interest rate ceilings on Foreign Currency Non-Resident (FCNR) deposits to attract foreign currency inflows and strengthen the rupee. These measures are

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applicable only to fresh or renewed deposits booked before September 30, 2026.The inflows would depend upon the manner in which other countries fix their interest rates. India would become an attractive proposition if it ensures adequate returns to foreign investments. Given the geopolitical crisis controlling inflation and stabilizing the Rupee becomes an uphill task. *Basic limitations of the study were in collection of data and measuring the lag in terms of policy measures adopted by the MPC and its subsequent impact on the economy.*

7. Conclusion

The findings of this research indicate that the establishment of the Monetary Policy Committee (MPC) in 2016 marked a significant milestone in the evolution of India's monetary policy framework. The introduction of Flexible Inflation Targeting (FIT) shifted monetary policy towards a more transparent, accountable, and rule-based approach, enabling the Reserve Bank of India (RBI) to pursue price stability while simultaneously supporting sustainable economic growth. Compared to the pre-2016 framework, the post-2016 period has been characterised by greater policy credibility, improved communication, and a clearer inflation objective, which has strengthened public confidence in monetary policy.

The analysis further suggests that the monetary policy instruments adopted by the MPC, particularly the repo rate, reverse repo rate, and open market operations, have been effective in influencing liquidity, interest rates, borrowing, investment, and aggregate demand. These instruments have contributed towards maintaining inflation within or close to the prescribed target range for most of the period after 2016, while also supporting economic recovery during periods of financial stress. Although GDP growth experienced temporary setbacks due to exceptional events such as the COVID-19 pandemic and geopolitical conflicts, the flexibility of the inflation-targeting framework enabled the RBI to respond appropriately to changing domestic and international economic conditions.

However, the study also establishes that monetary policy is not capable of addressing every macroeconomic challenge independently. The effectiveness of the MPC continues to be constrained by factors such as supply-side inflation, imported inflation, transmission lags, structural rigidities within the banking sector, and global economic uncertainties. Consequently, monetary policy alone cannot guarantee macroeconomic stability unless it is complemented by appropriate fiscal policies, structural reforms, and a stable external economic environment.

Overall, the evidence presented in this research suggests that the Monetary Policy Committee has played a significant role in improving the management of India's macroeconomic indicators since its establishment in 2016. While the existing framework is not without limitations, it has proved to be considerably more effective than the earlier monetary policy regime in controlling

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inflation, improving policy credibility, and supporting long-term economic stability. Therefore, it can be concluded that the monetary policy instruments adopted by the MPC have largely achieved their intended objectives and have become an essential component of India's macroeconomic management framework.

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