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BA Economics Honours | Semester 3 | Calicut University

Monetary Policy in India

Course Code: ECO3MN202 • Module 4

Module IV: RBI's Monetary Policy Committee (MPC)

The institutional architecture of monetary policymaking in India was revolutionized in 2016 by transitioning from the personal discretion of the RBI Governor to a collegial, statutory **Monetary Policy Committee (MPC)**.

Unit 18 & 19: Formation, Purpose, and Constitution of the MPC

Prior to 2016, the RBI Governor made all interest rate decisions independently, assisted by an informal Technical Advisory Committee (TAC) whose advice was purely consultative. Following the Urjit Patel Committee recommendations, Parliament amended the RBI Act in 2016 to insert Sections 45Z to 45ZO, establishing the MPC.

The MPC is a six-member committee:

- Three internal RBI representatives: The Governor (Ex-officio Chairperson), the Deputy Governor in charge of monetary policy, and one officer nominated by the Central Board.
- Three external independent experts appointed by the Central Government on the recommendation of a Cabinet Secretary-headed search committee, serving non-renewable four-year tenures.

Decision-Making Process and Accountability

The MPC meets at least four times annually. Each member possesses one vote. In the event of a tie, the Governor exercises a casting vote. Crucially, the law mandates complete transparency: minutes containing the voting record and individual rationale of each member are published on the 14th day following the meeting. If the average inflation breaches the 2%–6% tolerance band for three consecutive quarters, the RBI must submit a formal report to Parliament explaining the failure, remedial actions, and an estimated timeframe for returning inflation to the 4% target.

Advanced Theoretical Formulations and Empirical Frameworks (Analytical Division 1)

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Empirical Methodology, Identification Strategies, and Econometric Estimation

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accordance with the Lucas Critique. Consequently, contemporary applied economics bridges micro-foundations with aggregate macroeconomic phenomena through dynamic stochastic general equilibrium (DSGE) modeling and micro-econometric panel estimations.

Comparative Institutional Analysis, Market Failures, and Policy Governance

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Behavioral Motivation	Hyper-rational agents maximizing expected utility with complete cognitive computational capacity.	Bounded rationality, behavioral heuristics, loss aversion, and institutional anchoring effects.	Choice architecture, behavioral nudges (NITI Aayog initiatives), and consumer financial protection mandates.
State Intervention	State role restricted to core public goods, contract enforcement, and national defense (minimalist state).	State acts as developmental catalyst, risk-absorber of last resort, and promoter of equitable distribution.	Strategic industrial policy (PLI schemes), counter-cyclical fiscal intervention, and universal public services.
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Comprehensive Empirical Analysis: The Kerala Model and Sub-National Development

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However, contemporary economic analysis also highlights structural challenges confronting this development paradigm: high educated unemployment, fiscal constraints stemming from escalating public debt servicing and pension obligations, and heavy reliance on external remittance inflows from migrant workers in the Persian Gulf. Sustaining this high-welfare equilibrium necessitates transitioning toward a knowledge-driven economy, incentivizing high-tech manufacturing, and mobilizing sustainable sub-national fiscal resources.

Policy Synthesis and Analytical Evaluation

Policy formulation in dynamic economic environments must therefore synthesize foundational deductive reasoning with robust inductive empirical inquiry. Economists must continuously evaluate the balance between market incentives and regulatory governance, ensuring that institutional frameworks promote both productive efficiency and distributive social justice.

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