



## Injecting Liquidity in Economy

[Source: TOI](#)

### Why in News?

The [Reserve Bank of India \(RBI\)](#) has announced measures to inject over **Rs 1.5 lakh crore** to increase **money liquidity** in the economy.

### What are Key Points About RBI's Liquidity Measures?

- **Money Liquidity:** It refers to the **availability of cash and easily accessible funds** in the economy, influencing **spending and investment**.
  - **Liquidity** refers to how **quickly and easily** an asset can be converted into **cash** without impacting its price much.
- **Reason for Liquidity Shortfall:** The RBI's **forex sale** to stabilize the rupee amid **foreign institutional investors (FIIs) outflows** led to a liquidity deficit.
  - RBI sells US dollars in exchange for rupees, reducing the **supply of rupees** in the banking system.
  - It led to **tighter short-term interest rates** and increased borrowing costs.
- **Measures Taken by RBI:** RBI's liquidity infusion plan comprises **three measures**:
  - **Government Bond Buyback:** It means the central bank or the government **repurchases bonds** from the market **before maturity**.
    - It **injects liquidity by paying bondholders** (banks, financial institutions, or investors), increasing fund availability in the banking system.
  - **Repo Auction:** Repo auction is a **liquidity adjustment tool** used by the RBI where banks **bid for funds** at desired borrowing rates, and the **RBI accepts the lowest bids** until the required amount is allotted.
  - **US Dollar-Rupee Swap Auction:** A **swap auction** increases liquidity in the market by facilitating the **temporary exchange** of currencies or financial instruments.
    - **Borrowing dollars** stabilizes the domestic currency and prevents a liquidity drain by **avoiding rupee sales** in the forex market.
- **Potential Repo Rate Cut:** Addressing the **liquidity deficit** may be a **precursor to a possible repo rate cut** in the upcoming monetary policy review.
  - **Sufficient liquidity** will ensure that any future **repo rate cuts are effectively transmitted** to borrowers through lower interest rates.

## UPSC Civil Services Examination, Previous Year Questions (PYQs)

### Prelims

**Q. If the RBI decides to adopt an expansionist monetary policy, which of the following would it not do?(2020)**

1. Cut and optimize the Statutory Liquidity Ratio

2. Increase the Marginal Standing Facility Rate
3. Cut the Bank Rate and Repo Rate

**Select the correct answer using the code given below:**

- (a) 1 and 2 only
- (b) 2 only
- (c) 1 and 3 only
- (d) 1, 2 and 3

**Ans: (b)**

**Q. Which of the following statements is/are correct regarding the Monetary Policy Committee (MPC)?(2017)**

1. It decides the RBI's benchmark interest rates.
2. It is a 12-member body including the Governor of
3. RBI and is reconstituted every year.
4. It functions under the chairmanship of the Union Finance Minister.

**Select the correct answer using the code given below:**

- (a) 1 only
- (b) 1 and 2 only
- (c) 3 only
- (d) 2 and 3 only

**Ans: (a)**