JAIPURIA INSTITUTE OF MANAGEMENT, NOIDA
PGDM / PGDM (M) / PGDM (SM)
SECOND TRIMESTER (Batch 2024-26)
END TERM EXAMINATION, JANUARY 2024

Course Name	Macroeconomics and Economic Environment of Business (MEEB)	Course Code	20402
Max. Time	2 Hours	Max. Marks	40 MM

INSTRUCTIONS:

a. Attempt all Questions
b. Be Precise in your answer

Read and answer the questions that follow.

PART I

Economic Challenges Facing the New RBI Governor

Mr. Sanjay Malhotra has recently taken charge as the Governor of the Reserve Bank of India (RBI), the apex financial institution responsible for regulating the monetary and financial systems of the country. His appointment comes at a pivotal moment in India's economic journey. The nation is ambitiously working toward its vision of becoming a developed country by 2047, a goal that demands consistent economic growth, robust financial policies, and resilience in the face of global uncertainties.

However, Mr. Malhotra's tenure begins amidst a complex economic landscape. Over the past four quarters, India's GDP growth rate has been on a declining trajectory, as shown in the table below:

Quarter	GDP Growth Rate (%)
Q3 2023-24	8.6
Q4 2023-24	7.8
Q1 2024-25	6.7
Q2 2024-25	5.4

Inflation, which had remained below the target of 4% (within the RBI's tolerance band of 2-6%), has seen a significant rise in recent months, as outlined below:

Month	Inflation Rate (%)
July 2024	3.6
August 2024	3.65
September 2024	5.49
October 2024	6.21
November 2024	5.48

This spike in inflation, particularly in September and October 2024, breached the upper limit of the RBI's tolerance range, posing additional challenges for policymakers. Rising prices erode consumer purchasing power and can lead to a reduction in demand, exacerbating the economic slowdown.

This dual challenge of decelerating GDP growth and rising inflation presents a classic policy dilemma, often referred to as 'stagflation.' To navigate this, the RBI must strike a delicate balance. Strategies to curb inflation, such as tightening monetary policy through interest rate hikes, could potentially dampen growth further. Conversely, stimulating growth might risk driving inflation even higher.

In addition to addressing these immediate challenges, Mr. Malhotra must also focus on long-term structural reforms. Building a resilient financial ecosystem, promoting financial inclusion, and fostering innovation in the banking and payment systems are critical to achieving the nation's developmental aspirations. External factors, including global oil price fluctuations, geopolitical tensions, and shifts in international trade dynamics, further complicate this landscape.

Despite these challenges, Mr. Malhotra's leadership will be pivotal in ensuring India remains on track toward its ambitious 2047 vision. Successfully navigating the present economic headwinds while laying a strong foundation for sustained growth and stability will define his tenure as the Governor of the RBI.

Questions

Q.1. Evaluate the effectiveness of various monetary policy tools available to the Reserve Bank of India, such as interest rate adjustments, open market operations, and credit control measures. **(10 Marks)**

Q.2. Analyze the possible challenges Mr. Sanjay Malhotra might face as the Governor of the Reserve Bank of India in addressing inflation and slowing economic growth simultaneously. Consider factors such as global economic trends, domestic fiscal policies, and the expectations from stakeholders like the government, businesses, and the general public. How might these factors complicate his decision-making process? **(10 Marks)**

Q.3. Propose innovative and forward-thinking measures that the Reserve Bank of India could adopt to foster sustainable economic growth while managing inflation. **(10 Marks)**

PART II

Public Debt: Do not let it eclipse the fiscal deficit

(Adapted from Livemint, 06 Jan 2025, 07:30 AM IST)

In a 2020 address to the nation soon after the outbreak of covid, Prime Minister Narendra Modi cited age-old wisdom that advised against losing control of three things: fire, debt and disease. To cushion India's economy from the pandemic's shock, though, government spending had to vastly exceed its inflows, taking its fiscal deficit to 9% plus of GDP in 2020-21. The reversal of this debt-raising fiscal expansion since then has followed a glide path with 4.5% as the fisc's aim, to be achieved by the next Union budget—for 2025-26. As no further target for it has been set, the Fiscal Responsibility and Budget Management (FRBM) Act's goal of 3% looks likely to keep gathering dust. Signalling a shift in approach, the last budget revealed an intent to target the level of public debt, rather than the annual fisc, in subsequent years as a way to keep overspending in check. This conforms with the PM's prudent advice of 2020, but what exactly does it imply? Official data on the Centre's debt burden, available till end-September, would place it about halfway between 55% and 60% of GDP, well above the FRBM ask of 40%. To North Block, the appeal of going by this metric might be its utility in keeping public debt within a safety limit, one that keeps the risk of a debt trap at bay. Now, so long as the rate of nominal GDP growth—not adjusted for inflation, i.e.—exceeds the rate of interest paid on debt, the debt-to-GDP ratio will decline (if there's no gap between revenues and non-interest spending). It's the GDP effect: In a fast-growing economy, an administration with access to affordable credit can borrow and spend that much more, although fiscal restraint is still needed to prevent the deficit from overdoing that leeway. In any case, the aim should be to reduce the public debt ratio, not just keep it from rising, given how interest payments at its current level eat up such a bulky chunk of funds, depriving the budget of money that could be spent usefully. Debt that has piled up over the years can also be inflated away by the expedient ploy of letting price levels soar, as inflation reduces the real burden of debt. But this is plainly unfair to the country. This is also a reason a hawk's eye will always need to be kept on the fiscal deficit. If there exist short-run capacity constraints, a splurge of funds by the state could overheat the economy and make prices flare up. Keynes had proposed fiscal stimulus only as a device to rescue output and jobs from a demand slump (like the pandemic's). Else, fiscal over-reach can be inflationary. Had India's recovery in demand been broader, a 4.5% gap may have been a big worry for the central bank, whose job is to retain the rupee's real value even if a fiscal pump makes rupee supply spurt. The trend of deficits also shows which way the carve-up of a country's credit pie is going.

This helps assess the relative share of the state—versus market—in the allocation of an economy's resources. A fiscal bloat involves borrowing that may crowd out loans to the private sector, an effect usually seen in rising bond yields and capital costs. Admittedly, this has not been the post-2020 case in India. Private investment has seen only a partial revival, with the state playing the role of big spender to drive GDP growth. The idea was to 'crowd in' private players, but hefty central outlays on capex now seem like the new normal. Yet, for faster growth, we still need a broad revival of 'animal spirits.' And the fiscal deficit will remain a useful economic indicator that must not get eclipsed by a focus on public debt.

Q.4. Keynes advocated fiscal stimulus as a short-term tool to address demand slumps. Critically assess whether India's current fiscal strategy aligns with Keynesian principles or deviates into long-term fiscal overreach. **(5 marks)**

Q.5. Discuss the implications of shifting fiscal policy focus from annual fiscal deficit targets to public debt levels. How might this impact economic stability and growth in the long run? (5 **marks)**

CLO distribution

Question No.	CLO	Marks
1	1	10
2	2	10
3	3	10
4	2	5
5	3	5