SOME REFLECTIONS ON THE RATIONALE AND OBJECTIVES OF CENTRAL BANKING

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A fruitful approach to the theory and practice of central banking is to examine the very rationale of central banking. This is not such a pedestrian undertaking as it may sound if only because the intellectual appreciation of the rationale of central banking dates back only to the late nineteenth century and more particularly with the appearance of Walter Bagehot's classic monograph 'Lombard Street,' even as Thornton's treatise on paper credit served to clear the thickets of monetary controversy. Even more recent than the intellectual foundations of central banking is the fact that the accepted practice of central banking is essentially a twentieth century development. A closer examination of the rationale of central banking is even more germane to the crucial question, Is a central bank an indispensable appurtenance for an underdeveloped economy?

To answer this question, one has to analyse the 'necessary' and 'sufficient' conditions of effective central banking. The text books tell us that a central bank is necessary to act as (a) bank of issue; (b) government's banker; (c) bankers' bank; (d) as a controller of credit and (e) lender of last resort. Obviously, a central bank is not necessary merely to serve as a bank of issue. The function can as well be discharged by a Currency Board even if it were to operate with a 'partial' fiduciary issue and not with a cent per cent reserve as was the case in many of the former British colonies. Likewise, the function of being a government's banker can be as well fulfilled by a commercial bank e.g. National and Grindlays are bankers to the Government's of Zan-

This is the text of the second lecture delivered by the author in the Department of Economics, Sardar Vallabhbhai Vidyapeeth, in the year 1963-64.
zibar, Kenya, Aden, and Uganda. Even the existence of a multiplicity of commercial banks in itself does not prove the case for the creation of a central bank, as for instance in Hong Kong. Any necessary regulation and supervision of banking units could be entrusted to a functionary like a Banking Commissioner. In so far as the commercial banks are able to operate entirely on local deposits and/or their borrowings from overseas head offices, they do not need a banker’s bank or a lender of last resort. At this stage, however, one gradually begins to encounter the ‘case-for-a-central bank’ situation. It is vital to realise that money will not manage itself, and while banks, like all good oligopolists, would take into account the effects of their own and competing units behaviour on the respective profits, they would not be concerned over-much with the effects of their individual actions on the sum-total of the the monetary situation. Nor does the aggregate of their individual behaviour add up to a ‘policy’. But a policy cannot emerge unless there is a focal point for it in the form of a central bank. On the other hand, there is not much point in setting up a central bank if it cannot be effective. This in its turn postulates one or two pre-conditions, namely, the banking system must borrow from the central bank to supplement its cash base, because it is only then that a central bank can enforce a desired policy by stipulating the quantum and price of central bank credit (i.e. act as an effective lender of last resort); secondly, the banks have to vest part of their reserves with the central bank and observe the legal ratios of cash to deposits. This enables the central bank to act as a controller of credit and lender of last resort. The latter function becomes all important if for instance there is a liquidity crisis affecting the major portion of the banking system which cannot be met by inter-bank borrowing or lending. Of course, as soon as a lender of last resort is created, it is also convenient to vest in it the other functions of issue of legal tender currency, government’s banker, and custodian and controller of exchange. Therefore while these other functions are in the nature of ‘necessary’ conditions, that of a controller of credit and lender of last resort are the ‘sufficient’ conditions of effective central banking. And irrespective of the degree of development of an economy these propositions hold good. Even so, the environment of central banking determines its effectiveness.
II. THE ENVIRONMENT OF CENTRAL BANKING

( WHAT IS AN UNDERDEVELOPED MONEY MARKET? )

The Concept of financial maturity is logically quite distinct from that of the general economic development of a country. An underdeveloped or a semi-developed economy may have a comparatively sophisticated financial system, as for instance, in India where certain segments of the financial system like the call money and gilt-edged markets are comparatively well developed.

A financially immature economy has a large non-monetised sector and low ratios of (a) bank deposits to money supply : (b) bank finance to total finance of economic activity : (c) and near money to money supply : (d) high concentration in ownership of interest-elastic assets such as near money and Government securities, and debentures. The ratio of total liquidity to national income is, however, independent of the degree of economic development, and consequently one would expect economies at different levels of development to have similar or different ratios of money supply and liquidity to national income.

In addition to the above quantitative indices, it is also possible to identify the existence of financial immaturity with reference to some qualitative aspects of the monetary and financial system. Financially backward economies are characterised by the existence of a broker’s rather than a dealer’s market in both the money and capital markets as well as by the predominance of customer rates of interest as against competitive market rates of interest. But the common habit of judging effective rates of interest by the height of nominal money rates—for example, Lord Keynes referred to the exorbitant rates of interest in agricultural economies where it approximates sometimes to as much as the principal sums overlooks that in real terms the rate of interest cannot possibly exceed the margin between total real income of agriculturists and his minimum subsistence and other requirements (e.g. tax).

It may be worthwhile to amplify a little the significance of the various ratios mentioned above. Obviously, the greater the size of the non-monetised sector the smaller is the scope for monetary policy, but within the monetised sector the effectiveness of central banking depends
in direct proportion to the ratio of bank deposits to total money supply. In the limiting case of an economy where money supply consists exclusively of currency, there would be virtually no scope for an effective monetary policy but only for budgetary policy or physical controls. It is easier for a central bank to regulate bank deposits than currency. Similarly, the effectiveness of monetary policy is governed by the importance of banks in the finance of total activity. Extending this argument, it is also easy to see that the higher the ratio of near money assets such as time deposits, to money supply, the greater is the scope for regulating the supply of money, because near money assets are interest-bearing assets and are therefore more sensitive to variations in rates of interest. The ownership pattern of interest-bearing assets is likewise an important data, in particular, the extent of concentration or diffusion in ownership. If one may generalise, the wider the diffusion of near money and government debt*, the greater is the scope for effective monetary policy. Normally, in under-developed economics, the ownership pattern shows a higher degree of concentration relative to developed economies.

While one would be justified in giving weight to these factors, their significance should not be interpreted in a mechanistic manner.

III. NATURE AND CONSISTENCY OF POLICY OBJECTIVES OF CENTRAL BANKING

The policy objectives of a Central bank can be classified according as they are proximate or ultimate. The former refer to the monetary variables like the quantity, availability and cost of money and the Central bank may decide upon a policy of appropriately regulating these magnitudes while endeavouring to keep the financial structure of the community upon an even keel. This was considered by the Macmillan Committee to be the primary objective of a Central bank. Of course, this objective is in turn proximate to the overriding purpose of general economic policy viz. stabilisation. From this point of view the chief aim of central banking policy is to refrain from aggravating the monetary factor in economic fluctuations and to offset any deleterious effects of non-monetary factors. But in a developing

economy a central bank has to take account of 'development' as much as 'stability'. This may take the form of assisting directly or indirectly the finance of development through loan, rediscount and refinance facilities to special groups or else by participation in the share capital of other development finance agencies. Similarly, the central bank may, as part of the overall scheme of improvement of social overheads, promote the growth of banking and remittance facilities in the balance of payments, and there is no scope for monetary management by the Central bank in this case except that of adhering to the rules of the game, which then becomes the sole objective of its policy. Of course, a Central bank can, even in an automatic system, regulate credit creation by commercial banks, given the cash base determined by the balance of payments. An independent policy of maintaining domestic stability is not feasible and in fact is subordinated to the maintenance of exchange stability. Strictly, banking based on the fractional reserve system and a multiple credit creation on a cash base regulated by the Central bank is inconsistent with the pure theory of a gold standard with gold circulation. Under such a system the only logical possibility is the existence of 'free' banking somewhat on the lines envisaged by Mises. The development of national central banking and the gradual severance of the link between the domestic money supply and the foreign balance creates scope for discretionary monetary management which is the 'raison d'être' of real central banking. It is only under a fully discretionary monetary system that the real problem of conflict between different central bank policy objectives arises. These may be illustrated by the following examples.

(IV) CENTRAL BANKING IN A DISCRETIONARY SYSTEM

Nowadays the possibility of conflict between profit-making and monetary policy objectives is not important as most central banks are nationalised or at least under effective control of their Governments. But historically when central banks were still private corporations the conflict between profit-making and objectives such as the maintenance of adequate liquidity in the downswing of the trade cycle was ever present. This is well exemplified by the history of the Bank of England which gradually realised that it could not attempt to maximise its
profit once it assumed the obligations of ‘lender of last resort’. One can also visualise situations wherein the objectives of monetary policy and of widening the Government securities market may conflict. For instance, if it is intended to prevent the monetisation of the public debt, this may involve restriction of central bank purchase of gilt-edged stock. Variations in interest rate may be inconsistent with a stable bond market policy.

But with an enlargement of the nature and scope of central banking more than one policy objective could be achieved. While trying to stabilise the pattern of interest rates, the Central bank may also attempt to stabilise the volume of loan if it has the power to vary stock market margins and consumer credit, as in the case of the Federal Reserve System. Nor can the possibilities of ‘moral suasion’ in an integrated and concentrated banking system as in England or India be overlooked. If controls over the volume and price of credit are supplemented by controls over the direction of lending, a Central Bank may achieve more than one policy objective. Moreover, active co-ordination between the Central bank and the Treasury means that the monetary policy of the former can be appropriately reinforced by fiscal policy and debt management.

Of course, the conflict between ‘development’ and ‘stability’ is nothing peculiar to central banking. Rather it is a reflection of the tendency of the ‘warranted’ and ‘natural’ rates of growth, in the Harrodian sense, to diverge. But this may or may not be due to monetary factors.

All in all, one can only take an eclectic view of central banking as a flexible technique and policy. A stage might well be reached when central banks might become as important as lenders of last resort to the capital market as they are to the money market.
સૌથી મેળવના સૌખી પાણી અને તેના ત્રણું ઉપર કેટલાક નિયંત્રણ

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સૌથી મેળવના સૌખાલ અને તેના ધાતનીરની સમગ્રતા માટે સૌથી મેળવના સૌખીના પાણી વિશેષ કરેલી કવરી છે. આ લાગે છે તેનું અંગ સમગ્ર કામ નથી. અદધિકાર દેશની ભાષામાં એક પ્રકાર આ બાબતમાં ઉપલબ્ધ થાય છે અને તે અદધિકાર દેશની કેટલાક અનિવાર્ય છે?

આ પણની પણા આપવા માટે સૌથી મેળવના 'કવરી' અને 'પાણી' સાથે વહે છે તે વિશે વિચાર કરવી અદધિકાર

તાલુકાના 'પાણી પાથરંગા' કામ, સરકારની વાતાવરણ આપવાનું કામ, દેશની કામગીરીનું અનિવાર્ય કરવાનું કામ પણને કામ. સામાન્ય રીતે સૌથી મેળવના કેટલાક કામો ગણાઓ આપે છે. પરંતુ આ કામી પણ અને અદધિકાર દેશની ધાતનીરની સહાય કામ છે.

અદધિકારનાં પુત્રીને પુત્રી માટે કામ કરવે છે કે અને દેશની ધાતનીરના સૌથી મેળવના કેટલાક કામ વિશે વચન આપવા લાગે. ઉલ્લેખિત દેશની ભાષામાં રસાલી વાચવાનું સમગ્ર કામ સૌથી મેળવના કેટલાક મામલો નિયંત્રણ કરવી શકે નહં.

આ માટે સૌથી મેળવના પૂર્વ આવસ્થાના કારણ છે. અદધિકાર તો જે જે પ્રકાર માટે કામ પણ અદધિકાર 

તાલુકાની દ્રાક્ષી અનાવરનની પુસ્તક કરવા માટે સૌથી મેળવના કેટલાક વાતાવરણ વિષયમાં વહે છે. તેમાં જે જે આ દેશની કામગીરીની 'પાણી' આવસ્થાના છે. પરંતુ આ જે આવસ્થાના પૂર્વ કરવા માટે આવસ્થાના પુસ્તક વાચવા વિનિમય હતું, વિશેષ કરી રાખાતા વાતાવરણ 

અદધિકારના પુલાવાના

સૌથી મેળવના કામગીરીની સામગ્રિકતા નાવાળગ્રાસની સૃષ્ટિ ઇચ્છા ધરાન લાગે છે. નિવષટ નાખું કારણ સૌથી મેળવના કામગીરીના પ્રકૃતિ આદર્શ નથી છે.

નાવાળગ્રાસ લીટરેટ અપત્રીક અદધિકારના પણ પૂર્વ વિશેષ વચન વહે મેળવી છે. આ તેમાં (એ) અને ચેટ રમણ અને નાતક પૂર્વક 'વસ્તુ' (એ) આદધિક
અધિકારીઓ બદલાવ કરવા ને આધારધાર સ્થાપના ચાલુ કરવું. આધારધાર સ્થાપના કરવા માટે આવેલી યોજનાઓ ઉપરાંત પણ આધારધાર સ્થાપના કરવી તથા આધારધાર સ્થાપના કરવી તથ્ય હોય છે. આર્થક અને વિકાસ સુધી અધિકારીઓ બદલાવ કરવા માટે આધારધાર સ્થાપના કરવી તથા આધારધાર સ્થાપના કરવી તથ્ય હોય છે.

અધિકારીઓ બદલાવ કરવા માટે આધારધાર સ્થાપના કરવી તથા આધારધાર સ્થાપના કરવી તથ્ય હોય છે. આધારધાર સ્થાપના કરવા માટે આધારધાર સ્થાપના કરવી તથા આધારધાર સ્થાપના કરવી તથ્ય હોય છે. આધારધાર સ્થાપના કરવા માટે આધારધાર સ્થાપના કરવી તથા આધારધાર સ્થાપના કરવી તથ્ય હોય છે. આધારધાર સ્થાપના કરવા માટે આધારધાર સ્થાપના કરવી તથા આધારધાર સ્થાપના કરવી તથ્ય હોય છે. આર્થક અને વિકાસ સુધી અધિકારીઓ બદલાવ કરવા માટે આધારધાર સ્થાપના કરવી તથા આધારધાર સ્થાપના કરવી તથ્ય હોય છે. આધારધાર સ્થાપના કરવા માટે આધારધાર સ્થાપના કરવી તથા આધારધાર સ્થાપના કરવી તથ્ય હોય છે. આધારધાર સ્થાપના કરવા માટે આધારધાર સ્થાપના કરવી તથા આધારધાર સ્થાપના કરવી તથ્ય હોય છે. આધારધાર સ્થાપના કરવા માટે આધારધાર સ્થાપના કરવી તથા આધારધાર સ્થાપના કરવી તથ્ય હોય છે. આધારધાર સ્થાપના કરવા માટે આધારધાર સ્થાપના કરવી તથા આધારધાર સ્થાપના કરવી તથ્ય હોય છે. આધારધાર સ્થાપના કરવા માટે આધારધાર સ્થાપના કરવી તથા આધારધાર સ્થાપના કરવી તથ્ય હોય છે. આધારધાર સ્થાપના કરવા માટે આધારધાર સ્થાપના કરવી તથા આધારધાર સ્થાપના કરવી તથ્ય હોય છે. આધારધાર સ્થાપના કરવા માટે આધારધાર સ્થાપના કરવી તથા આધારધાર સ્થાપના કરવી તથ્ય હોય છે.