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MONETIZATION OF DEFICIT (Economic Times, The Hindu-GS-3)

➢ If the expenditure of the government exceeds its income, the government is said to have incurred a fiscal deficit. This deficit financing has to be done either by borrowing from the market or monetisation of deficit through RBI.

➢ In simple words, monetization of fiscal deficits involves the financing of such

extra expenses with money, instead of debt to be repaid at some future dates.

So, it is a form of “non-debt financing”. As a result, under monetization, there

is no increase in net (not gross) public debt.

It can occur only through one of two modalities:

➢ Direct Monetization (DM): Under this method, RBI prints new currency and purchases government bonds directly from the primary market (from the government) using this currency. As a result, this supports the spending needs of the government.

➢ Indirect monetization (IM): In this method, deficits are monetized as the government issues bonds in the primary market and the RBI purchases an equivalent amount of government bonds from the secondary market in the form of Open Market Operations (OMOs).

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