

## Digital Rupee – Emergence of New Monetary Era

*Rohan Bavadekar*  
*Faculty, TMV, Pune-37*

### Abstract

On 1<sup>st</sup> November 2022, RBI launched the Pilot project of introducing the operationalization of wholesale digital rupee. The digital currency backed by the central bank of the country. It is the electronic form of money, generally today the UPI payments we are doing are nothing but the kind of online substitute to the physical form of money i.e. cash. If you don't have deposit in your banks and support of reserve bank of India; Then such kind of upi payments are useless. To liquidate or settle any transaction cash is the sole authentic mean for activity. In this article, we will look at the journey of money throughout the history pages; The need of transaction, changing nature of money, multi-characteristics of money and the new upcoming era of digital money. Initially human utilized the money in the form of barter, where people were just exchanging own commodities with other commodities. As transactions started to become more complex and diverse, then the requirement of more solid and stable medium of exchange raised. Even in this century, the money witnessed the various evolutionary changes in such short span of time. From new currencies to virtual payments to cryptocurrency; Even the financial markets developed large number of asset forms and papers, which are kind of close alternatives of money for daily transactions. In all these developments, the changing nature of monetary policy, strategies get much affected and more challenged by the social upheavals. Numerous central banks are debating whether to launch their own digital currency (CBDC). A CBDC may have a number of advantages, including the opportunity to earn interest. By introduction of pilot project wholesale digital rupee, RBI has already jumped into the sea of opportunities or challenges. The plan of full-fledged reveal of digital rupee in 2023 is dependent on the success of this pilot project, its estimated impact on the wholesale industry. The banking structure will need new restructuring and formation policies, as this is going to affect people's day to day life process. Now much kind of questions like the rates, bank rate policies, deposit categories are going to be same? Or they need special kind of conditioning? The comparative study between crypto and digital rupee is also needed for the smooth and hassle free functioning central bank digital currencies (CBDC). In the pandemic, the lockdown situation brought this new challenge of contactless world. How to carry daily financial chores, pushed this need of virtual world. The introduction of central bank digital currency got kinetic in that need of an hour. In last centuries, the changing world of globalization, international trade made the currency transaction more rich and prosper. Hence such central bank digital currencies will again made international trade more challenging with new kind of structural requirement. It is going to be interesting to see the development of new era of monetary policy regarding the introduction of central bank backed digital currencies.

**Keywords:** Monetary Policy, Trade, Banking, Digital Currency, RBI, Economy, Virtual Transactions

### Introduction

On November 1st, the Reserve Bank of India (RBI) began testing a central bank-backed digital rupee for the wholesale market. On November 1, 2022, "the first pilot in the Digital Rupee - Wholesale segment started," the big discussion about when is India going to start its own central bank backed digital currency finally rest partially. Before we move forward with in depth discussion about the applications and challenges of digital rupee. We first need to understand the meaning of central bank digital currency, its scope and nature.

**A digital currency issued by a central bank known as a CBDC is widely used by the general people.**

Money that is owed to the central bank is referred to as "central bank money." There are currently two types of central bank money in use in the United States: physical money produced by the Federal Reserve and digital balances kept at the Federal Reserve by commercial banks. Although the majority of American money has traditionally been held in digital form, such as in bank accounts, payment apps, or through online transactions, a CBDC would be distinct from other forms of digital currency currently used by the general public because it would be a liability of the Federal Reserve rather than a commercial bank.<sup>1</sup>

Fiat money is the legal tender that a nation's central bank and the government of that nation back. Fiat money in digital form is referred to as digital currency. Today, as was already indicated, we can mistake our digital wallets and UPI IDs for digital cash. There will be friction between upi payments and digital currency even in the early phases. But the Federal Reserve made everything clear in very simple terms. So, if you believe that the transaction you are conducting is supported by the RBI? So the response is no. Your money is deposited in that commercial bank right underneath the reserve. However, that commercial bank, which is supported by the Reserve Bank of India, has the same amount of money in physical form. I hope it is now crystal evident how virtual currency differs from digital payments.

### **History Of Money**

It is important to study the basic functions of money. The history will give us the glimpses of upcoming evolutions of money. As some extraordinary happenings dawn on the world, such revolutionary decisions changed the whole system of the livelihood. Digital currency is the same matter with money world. Man when used to live primitive society, his needs were very subsistence in nature, it was not the era of utilitarian mindset. Even human was behind maximum satisfaction but due to lack of invention and knowledge of technology to process the resources .human confined with survival life only. Hence the only transactions used to happen were the commodities of daily use and help to conduct daily livelihood chores.

In the beginning, barter was the primary form of transaction. When one commodity or service is exchanged for another, it is known as a barter system. For instance, someone might build a house in exchange for a bag of beans or exchange a bag of wheat for a pack of lentils. The goods were difficult to utilise and perishable. Transportation and cost were two additional concerns. Sometimes, a person in need of a particular commodity—say, let's salt—must find someone who has salt and must have something to offer the salt owner, failing which the sale is void. People invented a product called commodity money to address the problem. The basic products that were included in the commodity money were things that everyone needed and could exchange at any time. Salt, beans, seeds, cattle, tea, and tobacco were the main commodity money items. But over time, this method also led to issues like perishable and challenging-to-use goods.<sup>2</sup>

So it can be seen in above paragraph that as time changes the problem with old system of transactions started gaining ground. The introduction from any thing to only commodity money also landed in the problem of perishability of that commodity money. Even if you are transacting the commodity goods , the nature of commodities is different, their durability differs which ultimately brought the question of value of that product. In barter system , there is no measure to find the value of commodity which they transacting.

Whether in the shape of shells, barley, feathers, or whale's teeth, several helpful properties of money become obvious if it is used to encourage commerce. For instance, carrying barley makes it neither portable nor particularly durable. Whale teeth can be difficult to divide into two pieces. Shells are not very rare and can be found on any beach. Additionally, trading outside of your local community can be challenging if the currency serving as a symbol has no real worth, such as feathers. Another distinguishing characteristic of money was that it gave you power, and power could acquire you a lot of it. In order to guarantee their weight and value, kings came up with the notion of minting coins

<sup>1</sup>(Bank)

<sup>2</sup>(Dodwani, 2021)

from precious metals and stamping them with an insignia. Metal currency checked all the financial boxes. It could be traded with other groups since it had intrinsic value.

The popularity of metal money, however, brought temptation, and sovereigns soon discovered they could profit from the circulation of devalued currency by slimming down the coins or adding less expensive base metals.<sup>3</sup>

Early Chinese emperors came up with the idea of keeping their heavy money back in the palace while issuing IOU certificates on paper for long distance transactions because carrying around large amounts of coins may be hard effort. People believed the paper even though it had no intrinsic value because they knew they could always swap it for gold, silver, or the coins it represented. Paper money became popular as trade between nations expanded. However, because it was so simple to print money, traders and bankers tried to tie the value of money to the price of gold, which failed.

So the Chinese invention of issuing certificates is kind of the gold standard system of today's world. Where the central authority keep certain reserves with them and issued the representative money for the transactions .

If there seems to be a common trend in the evolution of money, it's that it usually becomes more portable, accessible, and convenient to handle. Technological advancements allowed users to carry virtual currency in their mobile devices, like smartphones, and use it at accepted stores and among peers.

Nowadays, banks have official apps that allow you to make local and international interbank transfers, globalizing the reach of money.<sup>4</sup>

So this is the brief history of evolution of money. Now what is the origin of the idea of digital currency? We all know that during covid pandemic the discussion about the digitalisation took ground. Everything which has electronic support boomed like crazy. The e-commerce business , food delivery companies were the ones to earn lot during those difficult times. But the topic of central bank digital currency is not this fresh.it has its origin in 20<sup>th</sup> century during the world was facing the volatility caused due to the gold standard system. Hence many economists come with the new form of money known as digital cash. As the silicon valley was experimenting with the new level of computer technology.

The idea of a digital form of money secured by a private key was first proposed by David Chaum in 1983, marking the beginning of the history of digital currency.

### **The Point of View of RBI**

The Reserve Bank established an Internal Working Group (WG) in October 2020 to conduct research on optimal design in light of the worldwide advances in the field of CBDC. As per these committees , RBI reached to the various conclusions and point of views before starting the pilot project on the e currency. Those are as follows-

Even the sorts of money used to make payments are changing, in addition to the payment procedure itself.

The public receives money from the central banks in the form of actual currency, and banks and other financial institutions receive it through reserve and settlement accounts. New private-sector financial goods and services, such as digital wallets, mobile payment apps, and new digital assets, have been made possible by recent technological advancements. While cash remains the preferred method of payment , innovations are forcing central banks to consider how new central bank digital currencies (CBDCs) might supplement or replace traditional money (Committee on Payments and Market Infrastructures and the Markets Committee (CPMI-MC) 2018). More than half of central banks are currently working on developing them or conducting actual experiments.

The Reserve Bank of India has consistently drawn attention to numerous hazards associated with cryptocurrencies in its capacity as the custodian of the monetary policy framework and with the responsibility to ensure financial stability in the nation.

<sup>3</sup>(britanniza)

<sup>4</sup>(Coingreek)

Due to their detrimental effects on the financial sector, these digital assets threaten the stability of India's finances and macroeconomic system.<sup>5</sup>

We can clearly see how the emergence of crypto world worried the financial authorities so much that it created the dire need for the introduction of the central bank digital currency. RBI made its point quite clear while proposing for the revelation of digital rupee.

Now it is quite interesting to see the implication of digital currency on the various factors of the economic system. Lets try to analyze each factor with future possibilities and risks.

The resulting reduction in financial intermediation would negatively impact the effectiveness of monetary policy. It is anticipated that the related decrease in credit availability and/or rise in credit cost will have a significant impact on the economy's overall supply and demand. Any decrease in total bank lending would likewise weaken the role that banks play in the transmission of monetary policy as a whole. However, by establishing restrictions on CBDC holdings and transactions, these problems can be resolved.<sup>6</sup>

In short, the cost of holding the cash will be less when it comes to the CBDC. As monetary policy decides the rates on the basis of the money supply scale in the market and also the situation of banking system. Such revolutionary decision may create short term confusion in monetary strategy. Banks will prefer to hold CBDC rather than cash as it would help to run banking activities with more capital in hand .

But rate decision would be in tussle. The RBI monetary council can get in conflict about which data should be used as measure to calculate and estimate the bank rates for credit creation in the market. According to a different school of thinking, interest-bearing CBDC could effectively transfer monetary policy actions to economic players, enhancing the effectiveness of monetary policy. Economic agents could switch from bank deposits to CBDC under this modality, which might cause a deposit outflow. Despite there being no increase in the policy rate, this outflow of deposits (or banks' durable liquidity) to CBDC could spur banks to compete for depositors, which in turn could raise deposit rates and consequently also retail lending rates. The central bank may need to inject more frequently and in larger amounts of durable liquidity into the banking system to prevent this risk.

As a conclusion , the impact of CBDC over the financial market is quite unclear.

For those who are thinking about establishing a central bank digital currency (CBDC), BIS has outlined three fundamental core concepts. The first of these guiding principles was "do no harm"; this does not mean "have no impact," but rather that new money supplied by the central bank should continue to support the achievement of public policy goals and should not impede and, ideally, enhance, a central bank's ability to carry out its mandate for monetary and financial stability.<sup>7</sup>

But in one of the RBI speeches, governor cautioned about the possible threats can cause due to CBDC. if legal limitations on holding will not followed then it is possible the illegal funding to the bank capital would be operationalized. That could create the problem of digital black money issues.

## Conclusion

It follows that the introduction of CBDC is an innovative step. But it will have advantages and disadvantages. It won't harm the nation's financial situation, as the RBI said, so do no harm. However, it might have an effect on the current system and cause some hazy operating waves. However, India is making a noticeable effort to adopt new monetary practises. India has never before in history made its maiden forays into the financial sector. rather than waiting to implement the decisions made by wealthy countries. India stepped immediately into the action and was prepared to investigate the opportunities in the market for digital currencies.

It unquestionably ensures that India would dominate global trade. According to analysts, this decision would stop the "Dollarization" of the economy, which was taking place as a result of the rise of

---

<sup>5</sup>(RBI)

<sup>6</sup>(RBI)

<sup>7</sup>(settlements)



cryptocurrencies, many of which were based on the dollar currency system. Digital currency will thus open up a new frontier for the virtual world. However, issues like rate setting, stock market involvement, and the current real worth of money have yet to be resolved. These different unclear doorways for the coming era of digital currency can be opened by this experimental effort.

## References

Central bank digital currencies: foundational principles and core features, bis.org  
<https://rbi.org.in/Scripts/PublicationReportDetails.aspx?UrlPage=&ID=1218#CP71>  
reports/rbi.gov.in  
<https://coingeek.com/bitcoin101/what-is-money-its-evolution-over-the-years/>  
<https://www.britannica.com/video/187664/history-money>  
<https://taxguru.in/finance/history-money-barter-cryptocurrencies.html> , Dodwani  
<https://www.federalreserve.gov/faqs/what-is-a-central-bank-digital-currency.htm>  
Arthapedia  
Finance Ministry site  
RBI speeches