Edited Transcript of Reserve Bank of India's Second Bi-Monthly Monetary Policy Conference with Researchers and Analysts

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Moderator: Ladies and gentlemen, good day and welcome to the Second Bi-Monthly Monetary Policy Conference with Researchers and Analysts. As a reminder, all participants' lines will be in the listen-only mode and there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call, please signal the operator by pressing '*' then '0' on your touchtone phone. I now hand the conference over to Mr. Yogesh Dayal. Thank you, and over to you, sir.

Yogesh Dayal: Thank you, Stanford. Good afternoon. What I am going to do is there are several questions, which are similar in nature. So, I am going to read out all the questions which are similar in nature and they would be answered by the respective dignitaries.

The first question is from Mr. Utsav Adani. The question is RBI has reduced the benchmark rate to signal the banks to reduce the MCLR and other lending rates. However, now for more than eight quarters, the banks have either not reduced the rate or increased the lending rate for some instances. Going forward, how is the bank planning to resolve this transmission issue? Similar question is from Mr. Kumar Rachapudi. His question is, it is clear that past rate cuts have not been transmitted into banks deposit and lending rates as much as desired. In your conversation with banks, what factor were identified as the reason for transmission not happening? What steps the RBI is considering rectifying this? And a similar question is from Mr. Kaushik Das. His question is- should one expect one-to-one transmission from repo rate cut to lending rate cut of the banks? If the repo rate has been cut by 75 basis points so far, should one expect the lending rate of banks to eventually decline by 75 basis points or is the lending rate reduction expected to be at best 50 per cent of the cumulative repo rate cut? I will request Governor to take the questions.

Shaktikanta Das: To answer the last question first, out of the three questions, you cannot expect a one-to-one transmission because there are so many other factors which come to play. But over a period of time, full transmission is expected to happen. Now, as I have replied during the morning press conference, and you might have seen on the television that usually it takes four to six months for any rate transmission. This time the 21 basis points which we are talking about has happened faster than these four to six months average, this time it has happened at about two months or so. This is all with regard to the fresh loans. Now, with regard to the outstanding loans that are linked to benchmark, the transmission can occur only when these loans come up for resetting of the interest rate. So that naturally will take time. So far as the fresh loans are concerned, this time we expect a faster transmission to happen and we also expect a complete transmission to happen thereafter. Also, please look at the G-Sec yields. As I said, in the morning, there was 40 basis points decline between the average of April and the rate this morning for the 10-years benchmark bond yield. It was about 7 per cent or so in the morning, now the last time I saw today, it has come down to 6.9 per cent. So therefore, already the transmission there has increased by additionally 10 basis points over and above the 40 basis points which had already happened. With regard to the external benchmark, there was an earlier committee report that was placed in the public domain. Last time I had said that we are examining it internally and we have also incidentally today announced a liquidity management framework to come forward and suggest measures for enhancing the current liquidity framework and suggest a new framework. The group is expected to give its report in the middle of July. So, RBI is parallelly working on refining the interest rate structure of the banking system to ensure that there is transparency in interest rate setting and higher and faster transmission. So broadly, therefore, just to sum up what I have said, transmission of 21 basis points has happened in about two to three months' time, faster than earlier and further transmission is now expected consequent on today's rate cut faster and complete transmission is expected. RBI will continuously monitor and review the situation and if necessary, we will have an interaction with the banks, but I think the banks themselves are already doing that in their new rupee loans.

Yogesh Dayal: Thank you, Governor sir. The next question is from Mr. Sreejith Balasubramaniam. His question is- In February 2019, the RBI assessed output gap to be modestly negative, after FY17 & FY18 GDP numbers were revised upward in January 2019. Dr. Michael D. Patra had said this is set to close over the coming quarters and is factored into the RBI's growth projection, lowered to 7.4% for FY20. Doesn't this imply RBI's potential GDP estimate then was approximately 7.4%? Also, how did the assessment of 'virtually closed' not change from August 2018 till February 2019, despite GDP for two quarters coming in at 8.2% and 7.1%? This question will be taken by Dr. Patra.

Dr. Michael D. Patra: Thank you, Yogesh. You may recall that at the time of the February meeting; our assessment was that in the preceding period the output gap was virtually closed. But in the February meeting, our assessment was that it had opened up again and by the time of the April meeting it had remained negative. In the current policy, we have assessed that the negative output gap has widened. But please note and I reiterate this that the output gap is not measured in terms of growth rates but in terms of the level of output related to its potential.

Yogesh Dayal: Thank you, Dr. Patra. Next question is from Mr. Vikas Kotha - What is your view on the fiscal situation of the government in FY'20? What would be the ballpark estimate of slippage, if any, according to the RBI? A similar question is also from Mr. Kumar Rachapudi. What is RBI's view on the government's fiscal numbers especially the fact that the food subsidy has been lower than the budgeted one due to off balance sheet funding, should we not consider this as fiscal slippage? Should this be a factor into monetary policy decision at all and this impacts the future inflation? I will request Governor sir to take this question.

Shaktikanta Das: All aspects of the overall fiscal position have been discussed by the monetary policy committee in detail. The points which you have mentioned also have been discussed. Now, for FY'20, what is likely to be the fiscal number, etc., I cannot say that because when the budget is presented on 5th of July, we will get to know the number. As I said in the morning, over the last five years, government has broadly remained on the path of fiscal prudence. There has been a glide path and my expectation is that they will adhere to the same principle of fiscal prudence, which they have done in the past.

With regard to the food subsidy budget- because of off balance sheet funding, etc., even in the previous years, there is always a rollover which used to happen earlier. Now how much is the rollover this year, I have to check. But you are probably referring to the financing of the food subsidy from the NSSF. Now, whether this amounts to a fiscal slippage? You have to take a call. But so far as the MPC is concerned, MPC has considered all aspects of the government's fiscal position including the off-budget borrowings which you are referring to.

Yogesh Dayal: Thank you, sir. Next question is from Kushal Asthana. The question is- As GDP moderated to a multi quarter low in Q4 of fiscal year 2018-19, the inflationary trend remain soft aided by recent decline in crude oil prices and the rupee appreciation. Against this backdrop, can we expect more rate cut in the next few months and also some more measures that banks actually pass on the cuts to the customers? Dr. Viral V. Acharya will take this question.

Dr. Viral V. Acharya: Thank you, Yogesh. Thank you, Governor. As you are aware, the MPC has changed the stance of monetary policy from neutral to accommodative. As Governor also explained at the press conference, an accommodative stance means that rate increases are off the table. Of course, things have been relatively volatile over the past twelve months in terms of both financial market outcomes as well as macro outcomes, domestically and globally. So future rate actions will have to depend on incoming data and MPC's assessment of the outlook for the economy, which includes both trajectories of growth and inflation. Thank you.

Yogesh Dayal: Thank you, Dr. Acharya. Next question is from Mr. Gautam Singh. The question is- Given the net liquidity in the banking system has turned into surplus of ₹ 980 billion as per latest data, is it fair to assume that the need for injecting liquidity into the system via carrying out OMO purchases or dollar swaps has come off sharply? Also, if capital inflows gain further momentum, would RBI opt for OMO sales to sterilize the excess liquidity in the system? Dr. Acharya will take this question.

Dr. Viral V. Acharya: Thank you for your question, Gautam. RBI always perseveres to assure that there is adequate liquidity available in the system for all productive purposes. The question you asked is reasonable and you can form equally reasonable inferences on when we are likely or not likely to supply durable liquidity. I would stress that sometimes it is not just an assessment based on the present liquidity conditions but also how the liquidity conditions are going to be for the rest of the year. So, there is also some time management that we have to do across different quarters. But, as in the past, our liquidity management will be based on a continuous assessment of the evolving liquidity situation, which includes the factors you have mentioned including FX flows, currency in circulation and changes, etc., and we will take appropriate steps using the available tool kit that we have. Thank you.

Yogesh Dayal: Thank you, Dr. Acharya. Next question is from Alpesh Mehta. The question is- RBI draft guidelines on ALM and LCR of NBFCs addresses the issue of near-term liquidity, i.e., less than six months; however, liquidity/solvency issue still remains a challenge say for more than six months. What is the RBI's view on this? I would request Deputy Governor Shri Vishwanathan to take this question.

N.S. Vishwanathan: Thank you, Yogesh. The liquidity guidelines relate to management of liquidity and I do not think we must mix it with solvency. The guidelines related to solvency in the form of CRAR, which the NBFCs are required to maintain, a CRAR at the rate of 15 per cent of their aggregate risk-weighted assets. The ALM policy kind of provides more granular monitoring of the asset/liability mismatches as opposed to during the past and as you are aware for the larger NBFCs the proposed liquidity coverage ratio. In fact, these are on par with what you see internationally for banks. So, we must not mix up the two. The prudential regulation of CRAR is what looks for solvency and the ALM guidelines with more liquidity management.

Yogesh Dayal: Thank you, DG Vishwanathan sir. Again, a question from Alpesh Mehta regarding NBFCs. NBFCs have completed one year of Ind-AS implementation. What is RBI's view post transition to new accounting standards – will there be a new set of guidelines by RBI to implement Ind-AS for the system? I will request DG Vishwanathan again to take this question.

N.S. Vishwanathan: Ind-AS is a comprehensive accounting framework notified by the Ministry of Corporate Affairs. That is the framework under which the accounting statements for NBFCs have to be made. The first set of accounts under the Ind-AS are yet coming and if need arises for us to give any regulatory guidelines, we will assess based on that. As of now, we would let Ind-AS play as per the regulation that RBI has put in place.

Yogesh Dayal: Thank you, sir. Another question from Mr. Mehta is - Section of media have been reporting for on-tap banking license likely to be stopped for at least three years. Any comment by RBI on this front?

Shaktikanta Das: I am not aware of any such proposal. On-tap license for universal banking stands. That is it.

Yogesh Dayal: Thank you, Governor sir. Next question is from Mr. Jayesh Kumar. What was the rationale for 25 basis points cut and not 50 basis points when inflation is well below the target rate and the economy and unemployment is worsening? Do you think taking baby steps are the right medicine rather than front-loading of the rate cuts?

Shaktikanta Das: Monetary policy takes a judicious call based on the facts of the circumstances. Now how much should be the quantum of each rate cut, there is always considerable amount of discussion within the MPC and MPC takes these decisions. So, therefore, whatever decisions are taken on any aspect of the monetary policy, they will depend on the evolving situation, and at the current juncture it was felt that a further cut of 25 basis points would be appropriate and also please remember the fact that this 25 basis points cut is being done together with shift in stance from neutral to accommodative. That is a very big signal. So you have to see the rate cut by 25 basis points and the change in stance, you have to see both together.

Yogesh Dayal: Thank you, Governor sir. Next question is from Mr. Dhaval Gada. His question is - Can Reserve Bank change its guideline on listing of small finance banks in case of entities where holding company of the SFB is listed?

N. S. Vishwanathan: The answer is no.

Yogesh Dayal: Thank you, sir. A similar question of Mr. Gada is, has RBI contemplated the idea of opening RBI liquidity window to mutual funds or NBFCs in the last one year?

Shaktikanta Das: No, I think on this NBFC issue, I have replied in fair amount of detail and not once, but I think twice or maybe thrice during the morning press conference and I have nothing to add at this point of time.

Yogesh Dayal: Thank you, sir. Next question is from Mr. Shaunpaul Kavalakatt. His question is: There were two negative headlines in the last week which could impact food inflation going forward - a) Onion prices have already started to rise b) India received the 2nd worst pre-monsoon showers in 65 years. Monsoon onset is yet to be declared over Kerala and also Skymet prediction on monsoons are lower than IMD. Dr. Chetan Ghate has in the last MPC minutes mentioned that frequent changes in policy rates and stance runs the risk of introducing uncertainty and volatility because of our own actions. Dr. Patra had mentioned to remain watchful about the upturn in food prices that usually precedes the onset of the monsoon. Dr. Acharya had mentioned, with several uncertainties facing the economy, it is appropriate to maintain the neutral stance of monetary policy. Did MPC members consider these factors while changing the stance to accommodative in a unanimous vote instead of waiting for more clarity on monsoons and the Union Budget? I will request Dr. Patra to take the question.

Dr. Michael D. Patra: Thank you, Yogesh. On behalf of the MPC, let me say that all these factors were considered when the committee met and deliberated before arriving a decision. In fact, to quote from the resolution, the MPC had observed that the baseline inflation trajectory shape several factors and it listed the sharp sum of pick up in vegetable prices, accompanied by a correspondingly large reversal during autumn and winter. The broad based pick up in prices in several food items other than vegetables, the significant weakening of domestic and external demand conditions which have led to a decline of 60 basis points inflation excluding food and fuel in April, continuing volatility in crude prices and its impact on CPI inflation given the incomplete pass-through and the moderation in near-term inflation expectations of households. The MPC also noted that growth impulses have weakened significantly, in particular the sharp slowdown in investment and moderation consumption is a matter of concern. It is against this backdrop the MPC was of the view that given the headline inflation trajectory remaining below the target even after taking into account the expected transmission of past two cuts, there is scope for the MPC to accommodate the growth concerns by supporting efforts to boost aggregate demand and in particular to revive private investment while remaining consistent to its inflation mandate. Thank you.

Yogesh Dayal: Thank you, Dr. Patra. Now, Stanford, I request you for any other questions that you may ask.

Moderator: Sure, thank you. The first question is from the line of Kaushik Das from Deutsche Bank. Please go ahead.

Kaushik Das: Governor, I had one question. You spoke about accommodative stance, meaning no rate hikes from here on either pause or rate cut. Should we infer something on accommodative stance regarding liquidity as well at least till the committee submits the report, can we assume that liquidity will remain in a surplus mode because till now RBI's stance was to keep liquidity in a neutral state. So that is one question. And regarding transmission, has there been any discussion with the government about reducing the administered rates which are still higher and that is why probably bank deposits are losing out, so has there been any development on that front?

Shaktikanta Das: On the second part of your question, discussion with the government, as I said, we discuss various things with the government, so therefore, let me not specify which points I have discussed or which points we have not discussed. It is an important point which you are making nonetheless. Now, with regard to the liquidity, if you see we have been injecting sufficient liquidity over the last several months, even this month also on 13th, one OMO auction of ₹15,000 crore has already been lined up and government expenditures have also picked up. So, the general expectation is that liquidity position should remain very comfortable and perhaps in surplus mode for some time because of government expenditure picking up. As regards RBI stance is concerned, two points I would like to make – One, as I said in the morning, we will ensure that there is adequate liquidity made available to the system. Two - the internal working group will give its report by the middle of July, and once that report comes, then we will work on that immediately, and then we will be in a position to give greater clarity. Thank you.

Moderator: Thank you. The next question is from the line of Hemandra Bhatia from Andres Assets. Please go ahead.

Hemandra Bhatia: Sir, in March and April, the RBI conducted a couple of dollar/rupee FX swap auction and through that medium liquidity was injected into the system. So my question is regarding that (a) does the RBI intend to make it as a regular instrument for injecting liquidity and (b) if the RBI has conducted any study on this? If this external swap had any impact on the currency market and volatility in the currency market?

Shaktikanta Das: No. Swap has not really affected the volatility. For temporary period the hedging rates were sort of were impacted differently during the two auctions -- one in March, the other one is in April -- and it is a tool kit which we have tested and tried for the first time along with OMO, of course. OMO operations will continue, that continues to be a tool kit. This is a new instrument which we have introduced. How much of it we will utilize, that is, the FOREX swap in the coming months or later, that will depend again on the evolving situation. All these aspects which you are mentioning will be considered by the internal working group and then we should be able to spell out our stance. But there will be adequate liquidity made available.

Moderator: Thank you. The next question is from the line of Abhishek from Asit C Mehta. Please go ahead.

Abhishek: Thanks for taking my question. My question is regarding the quantum of rate cuts; 25 basis points and 50 basis points. Would it be possible for RBI to take a 35, 10, 15 basis points rate cut to send effective message with regard to transmission?

Shaktikanta Das: You see, I had articulated this point of view in one of the recent lectures on the margins of IMF meeting, and basically my idea was to have some debate and discussion in the public domain. There have been some discussions, some write-ups in some places about having a rate hike or rate cuts or basically rate decisions not in 25 or in multiples of 25 basis points. At this juncture as I said earlier, 25 basis points rate reduction was considered as appropriate and therefore the MPC decided to cut the rates by 25 basis points. Thank you.

Moderator: Thank you sir. We take one last question from the line of Aurodeep Nandi from Nomura. Please go ahead.

Aurodeep Nandi: The RBI just mentioned that it is a big signal that it is accommodative along with 25 basis points cut. On the other hand you are also mentioning that all what accommodative means is no further rate hikes. Aren't these not in contrast with each other? And secondly, the Governor mentioned about adequate liquidity for productive needs. How does the RBI perceive productive needs?

Yogesh Dayal: This question will be taken up by Dr. Acharya.

Dr. Viral V. Acharya: In one of the earlier responses, Governor stressed that this is effectively a 75 basis points cumulative policy rate reduction in slightly over a four months period that is quite significant in itself. Remember that in February policy, the stance was changed from calibrated tightening to neutral and now it has been changed from neutral to accommodative. So, I think these are fairly significant policy actions in a short amount of time and it is fair to conclude even though I am an MPC member that MPC has been reasonably data-dependent over this period. How do we assess there is adequate liquidity for productive purposes? You know, typically, durable liquidity needs of the economy are assessed based on the GDP growth rate that is anticipated that translates into the currency needs for the economy that also maps into some implied credit growth for banks which in turn will determine their deposit growth and therefore their reserves management. Then of course there are the somewhat unpredictable foreign exchange operations on which you get better signals as time goes by in the year and if they are stable then you are able to predict more comfortably what they might look like, if they are volatile then it is hard to know. So these are the main operations that ultimately determine the durable liquidity needs of the economy and we do our internal calculations, but as Governor highlighted earlier, the liquidity review that has been internally setup will explain some of these things and help the market interpret the data and the quantitative measures that the RBI puts out as to how some of those map into the decisions that we take.

Yogesh Dayal: Thank you Dr. Acharya. That will be all from our side, Stanford. Thank you so much for joining.

Moderator: Thank you very much. Ladies and gentlemen, with that we conclude today's conference. Thank you for joining us and you may now disconnect your lines.