Interview with Bloomberg Quint – Shri Shaktikanta Das, Governor, Reserve Bank of India on March 5, 2020

Sir I will start with the big picture question. You are back in the day before the RBI became a flexible inflation targeting central bank. Governors would often lay down their priorities in the annual statement which would give us a sense of the current context. Let me go back to that practice and ask you what your current priorities at the institution are given the economic situation:

See for the central bank, especially a central bank like the RBI and its multifarious responsibilities, if you compare it with other major central banks like the Bank of England or even the US Federal Reserve, compared to them, the RBI's domain is much wider. Therefore, every aspect of the domain is very important. But currently if you ask, while I must say that all departments of the RBI, all aspects of our domain in which we operate are important but currently the main focus of the RBI is maintaining financial stability, supporting growth, maintaining price stability which is a mandate given to us under the Reserve Bank of India Act. And also to focus on sharpening our regulation and supervisory functions so far as the regulatory entities are concerned.

Sir. Since you put financial stability right at the top, let me go into that. We are speaking on the day when there are reports that PSBs will be asked to step into support a private bank. Firstly, is this suggestion coming from the RBI with the view on financial stability?

No. First thing is that I don't go on to respond to media speculative questions. Because any reply to that this way or that way has a lot of arbitrage value and implications. But having said that I have said this earlier also that the RBI remains committed to ensure that our financial system and our banking system are strong and stable and at the moment in any case I would like to reiterate that our banking system remains safe and stable. Overall, the RBI remains committed to ensure that we have a stable and sound banking and financial system.

So we have had a lot of accidents if I can use that word. Over a few years period we had the period of asset quality review which led to the sharp rise in PSU Banks, bad loans, we had the NBFC crisis in the middle, we had a fraud or two which also caught attention. Now there are issues in some private banks. It has been a period of flux for the financial system isn't it?

Yeah right. The AQR threw up new challenges for the banking system mainly the PSBs and thanks to the capital infusion which the Government brought in and also certain regulatory measures taken by the RBI, such as, stepping of the supervision of the PSBs in terms of putting some of them under PCA and monitoring the steps being taken once they comply it. There is a certain level of compliance for taking them out of the PCA. So therefore the challenges which were thrown up by the AQR, I think they have been largely addressed and today the NPA situation is better than what it was, in 2014-15 when the so called AQR was undertaken. That is one aspect and other aspect has been governance issues in both the public and private sector and we have from time to time given guidelines to improve the governance in PSBs and private sector banks. Let us say from appointment of a chief risk officer, we extended it to the non-banking segment also. We have stepped up the level and quality of our supervision and the depth of our supervision also. We have improved on governance and we are now working on certain further measures for example for private sector banks also we have come out with guidelines for the remuneration and compensation packages of the CEOs and Whole Time Directors. We are also currently working on improving the governance structure in our banks and we do hope to come out with certain guidelines with regard to governance in banks both PSB and private sector.

What will they tackle here? What aspects?

We are working on it. It is work in progress. Based on our supervision and based on our areas which we have identified over the last 1-1.5 years certain areas still need improvement. We will come out with certain guidelines in the near future.

Will you look at the roles of boards at all? I don't know if it is in PSU banks you have limited control. I know that but it has been surprising to see how ineffective boards have proved to be in the private banks and I am not just talking about one instance. There are more than one now. Does that worry you?

I don't want. It is sort of work in progress. We are working in all the areas we feel require improvement which requires some amount of further regulation. We will come out with some guidelines.

Will it be targeted on boards or managements?

It will be targeted at improving the governance in the banks and not on the board and management because this question I can understand from where it is coming from. But, I think it is not fair for me to spill it out before we finalise everything.

Let me ask you about the NBFCs. You have publicly stated that you have seen improvements since when this NBFC crisis came up. You have steadily seen improvement in the actual underlines of these businesses. I ask that because you know we had a period of very high liquidity surplus and sometimes liquidity just buries problems rather that resolve them. Is the RBI convinced that the issues are getting resolved?

First thing. I would like to say that its not a case of surplus liquidity pushing things under the carpet. Secondly with regard to NBFCs in particular, I have also said this earlier. The top 50 NBFCs that we are monitoring. Today in our monitoring and our supervision there is a lot of deep dive also which takes place whenever we see any vulnerability or any fragility in any particular NBFC. In certain areas, we are constantly engaged and our supervisory teams are constantly engaged with managements, with the promoters of these NBFCs and working with them and monitoring very very closely and much more closely that anybody can imagine. So therefore we do see overall their health is far better than what it was one year ago. Market confidence in NBFCs is also better than what it was one year ago and we also see that the loan offtake from the NBFCs which were in difficulties earlier are also seeing improvement. So there is a greater realisation and it is also quite satisfying to know that the NBFC managements - quite a good number of them have responded to the situation and whenever, whatever steps were required they have undertaken those steps.

There are some risks though particularly wholesale NBFCs because there are still pockets of risks on some real estate companies which can have a fallout.

Real estate, particularly the housing finance companies came to our regulatory domain only after the July budget. I think from the 1st of October their supervision is with the NHB. So we are in constant touch with the NHB. Whenever the NHB finds any issues or any areas of concern they always bring them to our notice. On our side, we also monitor the overall health of the housing finance companies, particularly the big ones. And they are coming out of their difficulty, some of them need to raise more capital, some of them need to improve their current liquidity situation but that is work in progress and going forward I expect improvement there also.

Risk to the system is lower than it was?

Risk to the system is much less.

A question on RBI supervision in all of this. In the interim what is the RBI changing in terms of supervision. It cannot be denied that many things were missed from frauds to bad loans to asset liability mismatches. Why are these not caught by inspectors and people who supervised these institutions?

First thing a fraud is a fraud. We take on our best effort basis. The first layer of fraud control lies with the regulated entity bank or an NBFC whichever is the entity. It is their responsibility to check up fraud. The RBI is an external agency which goes and supervises but we are not sitting there morning to evening monitoring each and every activity and operation. So the first layer of checking the fraud lies with the entities concerned. The RBI expects managements of banks and NBFCs to have robust internal mechanisms to check frauds. To ensure these robust mechanisms exist, the RBI from time to time gives out various regulatory guidelines. For example, for NBFCs we have said that there should be a full time Chief Risk Officer because we felt that the somebody independent and directly reporting to the CEO or the board should independently evaluate the risks in an NBFC. So, we being the regulator try to create an ecosystem within the regulated entity which ensures that frauds are prevented. When we go as a part of our regulatory cycle, we go through all the numbers and we examine it and certain new things or frauds come to our notice. So when it comes to our notice, then first question we ask the management why did they miss out because it is for them to check it. Then we try to improve upon that and learn from that experience and going forward give additional safeguard measures. Then again at the same time one kind of fraud, if it happens we have to ensure that kind of that fraud does not get repeated in that organisation or elsewhere. So by way of experience we keep on fine-tuning our directions and instructions to the banks and NBFCs to prevent frauds.

Long time back you had a suggestion, may be the quantum of penalties where something is detected fraud or regulatory breach should go up, it is those kinds of penalties which have forced these financial institutions to improve their systems. The other method is used by SEBI by which they put out long detailed reports on what has gone wrong. The RBI won't want to go on any of these two directions to improve compliance?

Wherever we have had the compliance issues, Enforcement Department of the RBI has been imposing penalties. We have court cases where big amounts have been imposed as penalty. Also a penalty on a bank or NBFC particularly for an entity which is a listed entity, penalty from the regulator itself is a reputational risk. It will definitely affect the reputation of that institution and it will affect the market perception of that institution. It is a reputational risk that the regulator has found fault and regulator has imposed a penalty whether it is 25 lacs or 1 crore or 5 crores - it has its own impact.

It has been a tough period. Even though some people believe growth will be bottoming out now we have got another risk coming from the outside on the fall of coronavirus, local spread is weak right now. Numbers are low but downside risk could emerge as things stand.

Definitely coronavirus. So far as the global growth is concerned, coronavirus is going to pull down global growth. Even the estimates given by the IMF, OECD and other agencies are already there in the public domain. We had looked at all these assessments. We have also made our own internal assessments. It will pull down the global growth. When SARS happened in 2003, Chinese growth was pulled down by about 1 percent. That time China as a part of world GDP was about much less than what it is today. China has a bigger share of GDP. China has a bigger share of global trade. So therefore whatever dip happens in Chinese growth, IMF says it is going to be 0.4 percent but that is not the final word. I think IMF may be coming out with revised numbers. So that will definitely have the undermining effect on the global growth and the countries which are part of the supply chain will take a hit. India today is more integrated than what it was during the SARS period. But we are not really that much part of the global value chain. But certain sectors of our economy whether it is trade or manufacturing, there is a lot of interlinkage with China. So, therefore it would definitely have some impact on India's growth. We are assessing it. I think going into the next monetary policy in the first week of April, by that time we would be in a better position to estimate. We would have estimated the lightening impact on India's growth. I think the current indications based on interactions with other central bank governors, I can say that indications that the coronavirus has peaked in China and we have some port activities resuming in china in their major ports, the port activities which had really gone down seem to be resuming from 15th-20th February onwards. There is greater activity.

Since FY 18 there was a time when you were in Government and we used to talk about 8 per cent growth quite easily and now we are struggling to see whether we would make it to 6 – 6.5 in FY 21. What has gone wrong sir on the growth story?

I think the problem is global. You look at global growth also. The global growth, IMF projection for 2019 was 2.9 and for next year also IMF is talking about 3.2 or 3.3 which going forward, they will revise. That looks fairly certain now. So, therefore global growth has itself fallen and so far has India is concerned we were impacted by the problem initially of twin balance sheet problem. The corporates took time to come out of their own problems. Now many corporates are in the process of deleveraging. Then the bank balance sheets were under stress. They are also now gradually coming out of that problem. So, first it was the twin balance sheet problem, which sort of had a negative impact. Then we had the NBFC problem which happened around IL&FS. So that again sort of had a negative impact on the sentiments and in the financial sector and the credit sector. So, therefore it has been one problem after another which has encountered us. Now, as things are beginning to look up we have this Coronavirus problem which has come and that has created some amount of negative sentiment in India also. Globally the sentiment has definitely turned negative after coronavirus and on India also it is going to have some impact. But I think with the Chinese authorities saying that the Coronavirus problem is moderating and there is some evidence of revival of port activities and with the coordinated action which is being taken by all governments and all central banks, I think going forward, the problem cannot be taken lightly. The spread of the virus has to be contained and I think there is already coordinated action happening among governments. So far as India is concerned, the government has put in place several mechanisms. So, first focus has to be on preventing the spread of the virus. Parallelly the governments and the central banks will have to deal with their individual situations. G-7 has come out with a statement. IMF – yesterday there was a teleconference of the IMFC and I participated in the teleconference after which the managing director of the IMF has also issued a statement which is there in the public domain. So there is greater coordination among central banks. Each central bank depending on their country situation will take whatever action is required.

That is the global picture sir. But we can't deny that there are local elements too. People are talking about a demand problem in India after a very long time. Whether it comes from the informal sector being hit by two events – demonetization and GST or it comes from the formal sector where income growth, job growth has perhaps not been upto the mark. India being a demand constrained economy is very tough to swallow given that we have always been proud of our demographics which would mean that we would continue to grow. What about that internal problem sir?

In the sense that, that is something which the government has tried to address through the current budget. Although they had to maintain the fiscal deficit numbers with that they have taken measures not just in the budget but over the last one year, I think a series of measures the government has taken. This time the rabi crop is expected to be very good. It is expected to be a bumper crop. So, therefore that will augment and contribute to the rural incomes and also food inflation has been very low over the last years. Food inflation has also meant lower farm incomes. So some amount of food inflation would also translate into better farm incomes. So that is hopefully going to provide some support to rural demand. So we do see some improvements in some sectors. But again, as I have said elsewhere also, it is too early to say that the demand has revived. So we have to wait for some green shoots which are visible in some areas for some more months before we can conclude that things are improving. This is what I had said earlier. Now we have the new challenge of the coronavirus. So we are evaluating what impact it will have.

In the last two MPC meetings there was no change. The RBI took other measures to in some ways de-facto bring down rates. I think the question we will ask is that is there a dichotomy between the MPC's message which is more inflation focused and the RBI's message which continues to be focused on growth a little bit more than inflation?

No. I think the MPC is also focused on growth. When the MPC resolution said that there is policy space for rate cut, obviously the MPC had growth in its mind. So there is no dichotomy between RBI's thinking and MPC's thinking and as per the law, growth is also to be kept in mind while maintaining price stability and all measures we took in the last MPC, it was mainly to ensure better transmission. It was not for any yield management or anything. It was to ensure that whatever reduction we have done in the repo rate over the last one year, that translates into the corporate bond market segment. Today, I think during February itself after our monetary policy announcement, I think totally something around 57 – 58,000 crore of corporate bonds are being raised. Ofcourse, most of it is by the way of private placement but there are signs that the corporate bond market has revived and the rates look fairly attractive. So therefore, our effort was to ensure that the MPC, the rate reduction, the transmission takes place through the corporate bond market and I think to that extent our policy seems to be working.

But it is yield management in some ways.

It depends how you look at it. I have explained to you what has been our objective. Our objective was to ensure better monetary policy transmission. In the process the yields have come down. So it is a question of perception. But our objective was not to do yield management.

LTRO, Operation Twist, etc. were not driven by bringing down borrowing rates. For the government or the individual borrowers.

LTRO you see, it was mainly to ensure better monetary policy transmission. It was also to ensure better credit flow from the banks. That was the intention and again the CRR dispensation which we gave in the last monetary policy was also to ensure better credit flow by reducing the cost of funds for the banks.

And these tools remain on the table if the MPC can't act purely on the interest rates if the interest rate scenario does not allow it to. The RBI will continue to try and do what it takes.

But we will see. Whenever the MPC will decide what MPC decides. But a central bank always has several tools at its disposal. We will use all these tools at the right time when required.

There is a perception now though that the RBI, side-stepping is not the right word, but the RBI is doing things which the MPC is not willing to do or in a position to do.

You see the MPC has a defined mandate. All the other things which we have done are not within the domain of the MPC. The MPC is to focus on price stability and the measure of price stability is the repo rate and inflation at 4 per cent through the repo rate mechanism. So therefore MPC has a defined role.

Liquidity, Yield are all directly Monetary Policy Tools

But that is within the RBI's domain. MPC does not go into the liquidity framework for example which we announced during the last MPC. That was part B of our announcement. So it was not really a decision of the MPC. MPC has a defined role. Within that defined role the MPC is supreme.

Are you more of a believer in the full service central bank theology rather than an inflation targeting central bank?

I don't know the theory or ideology of it but the RBI has been mandated to undertake several responsibilities and we cannot say that. Inflation management is one of the objectives. It is a very important objective but then the other areas which I mentioned regulation, supervision, you have things like maintaining financial stability, stability of the payment and settlement systems, it is a multifarious responsibility. Encouragement of the FinTech – that is one of the other area where we are working so I think RBI has been able to sort of produce excellent results over the years.

Infact that was my last topic Governor. On the digital economy, first a quick word on the Supreme Court's decision on the RBI's cryptocurrency circular. Looks like you will have to go back and revisit how you approach that space.

Supreme Court order has come yesterday. We are going through the order of the honorable Supreme Court. Supreme Court has very clearly upheld the regulatory powers of the RBI. It has not at all questioned. Infact it has really recognized the regulatory and other functions of the RBI and the Supreme Court has struck it down on the ground of proportionality. So we are studying the order of the Supreme Court and after we examine it thoroughly we will decide on the way forward. But talking on digital and FinTech and all, I would also like to mention that we have decided in RBI to set up exclusively a Department of FinTech to give focus on digital transactions, adoption of technology in all aspects of banking and non-banking we are working on that.

That is great to hear sir. Payments in particular. I think India is very well ahead in the payments space. Lots of payment providers. Great for the customer. But there is very very intense competition in that space. Cashbacks, payment companies making lots of large losses. Is the RBI comfortable? I know it is not the same as a bank making loss. But is the RBI watching these payment companies also from a quality perspective?

We are sort of keeping track with what is happening and mostly if you know many of them are giving discounts and other things. So I think those who are in e-commerce business Government has already come out with certain guidelines and regulations for that. So far as India is concerned it is a new area, it is a new business. So we will watch it and if required we will intervene at the appropriate time. If something new is happening, we should not kill it from day one. It is better to watch how it develops and in any case all these investors are putting their money, they should be more responsible. I expect them to be responsible and there are lenders also. There are banks also which are lending them money. They have investors which have put in their money. So there is equal amount of responsibility on their investors and the banks which are financing them to see the viability of their business model.

Regulator comes much later if required

It is a new area which is developing. So we don't want to come out with a whole lot of restrictions before the business has even taken off.