



“Reserve Bank of India Post Policy Conference Call”

January 25, 2010





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Alpana Killawalla

We welcome you all to this press conference, which we will be joined by the regional officers through the teleconference facility. My request is whenever you ask questions, please state your name and affiliation. So I will hand over to Governor. Thank you.

D. Subbarao

Thank you Alpana. On my own behalf, I want to welcome all of you once again to this post policy press conference. As per standard practice, I have a statement which I will read out, thereafter we will take your questions.

This morning the Reserve Bank released its third quarter review of monetary policy for 2010-11. Based on an assessment of the current macroeconomic situation, we decided to increase the repo and reverse repo rates by 25 basis points each. Accordingly, the repo rate stands at 6.5% and the reverse repo rate at 5.5%. We also decided to retain the CRR at the current level of 6% of NDTL for banks. With these increases since mid-March 2010, the Reserve Bank has cumulatively increased the repo rate by 175 basis points and the reverse repo rate by 225 basis points. Additionally, the CRR was increased by 100 basis points. Banks have responded to this calibrated tightening by raising their deposits and lending rates suggesting strong monetary transmission. In order to manage the current liquidity situation, we decided to extend the two special measures currently in operation that is the additional liquidity support to scheduled commercial banks under the LAF to the extent of up to 1% of NDTL and a daily second LAF up to April 8, 2011.

Let me start by indicating the considerations that guided our monetary policy stance for the rest of 2010-11. First and foremost inflation is clearly the dominant concern. Even as the rate itself remains unacceptably high, the reversal in the direction of inflation is striking. Primary food articles inflation has risen again sharply. Non-food articles inflation and fuel inflation are already at elevated levels. There are signs of food and fuel price increases spilling over into generalized inflation. Second there has been a sharp rise in global commodity prices which has heightened upside risks to domestic inflation. Third, growth has moved close to its pre-crisis trajectory even in the phase of an uncertain global recovery. Fourth, the uncertainty with regard to global recovery has reduced.

Let me now give you a brief overview of the global economy. Advanced economies are showing firmer signs of sustainable recovery; however, inflation has edged up in major advanced economies even as large slack persists, owing mainly to increase in food and energy prices whereas signs of inflation in advanced economies are only incipient. Many emerging market economies have been facing strong inflationary pressures. Significantly food, energy, and commodity prices are widely expected to harden during 2011 driven by a combination of supply constraints and rising global demand. This suggests that inflation could be a global concern in 2011.



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Turning to the domestic macroeconomic situation, the 8.9% of GDP growth in the first half of 2010-11 suggests that the economy is operating close to its trend growth rate. The Kharif harvest has been good and the Rabi prospects are promising. Good agricultural growth has boosted rural demand. Export performance in recent months has been encouraging. With the risks to growth in 2010-11 being mainly on the upside, we have retained the baseline projection of real GDP growth at 8.5%, but with an upside bias.

Moving on to the inflation situation, headline inflation moderated between August and November 2010 as expected by the Reserve Bank. This trend, however, reversed when WPI inflation moved up from 7.4% in November to 8.4% in December 2010 due mainly to sharp increases in the prices of vegetables, mineral oils and minerals. While the current spike in food prices is expected to be transitory, inflation stemming from structural demand-supply mismatches in several non-cereal food items is likely to persist till supply response kicks in. Non-food manufacturing inflation also remains above its medium-term trend of 4%.

Going forward, the inflation outlook will be shaped by three factors; on how food price situation both domestic and global evolves, second on how global commodity prices behave, and third the extent to which demand side pressures will manifest. We have raised the baseline projection of WPI inflation for March 2011 from 5.5% to 7%. This upward revision was based on several considerations. First the upside risk to inflation as mentioned in the mid quarter review of December 2010 has materialized as reflected in the increase in prices of metals and non-administered fuel. Second, there have been some transitory supply shocks which have triggered a sharp increase in vegetable prices. Third, petroleum and aviation turbine fuel prices went up in early January and they will add 9 basis points to WPI inflation. While the impact of transitory factors is expected to dissipate, price pressures on account of demand-supply mismatches in respect to some commodities will persist.

The liquidity conditions continue to be tight throughout the third quarter of 2010-11. Our deficit in overall systemic liquidity is of course consistent with the Reserve Bank's anti-inflationary stance, but the extent of tightness is beyond the comfort zone of plus minus 1% of NDTL of banks. Both frictional and structural factors have contributed to this. The frictional component is the above-normal government cash balances. The structural components are the widening difference between the credit and deposit growth rates coupled with high currency growth.

The Reserve Bank instituted a number of measures to mitigate the liquidity deficit. As I indicated earlier, we decided to extend some of these measures as part of this policy review. While the Reserve Bank will endeavor to provide liquidity to meet the productive credit requirements of a growing economy, it is important that credit growth moderates to



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confirm broadly to the indicative projections. This will prevent further build-up of demand side pressures. The Reserve Bank will constantly monitor credit growth and if necessary engage with banks which show an abnormal credit-deposit ratio.

A brief, albeit important, comment on the external sector. In the first half of 2010-11, the current account deficit expanded to 3.7% of GDP on an annualized basis from 2.2% in the corresponding period of last year. Subsequent trade data indicate that exports *have grown faster than imports* which will improve the current account deficit. For the year as a whole, we estimate that the current account deficit will be close to 3.5% of GDP.

As always there are risks to our growth inflation projections, they are the following. First, food inflation has remained at an elevated level for about 2 years and the prospect of this spilling over to the general inflation process is rapidly becoming a reality. Second, imports as a means to supplement domestic availability for many commodities will become less of an option as global growth consolidates and capacity utilization increases. This may accentuate demand side pressures. Third, the estimated current account deficit of 3.5% of GDP for 2010-11 is not sustainable. Fourth, on top of the level of CAD which is a risk, the financing of CAD is an additional risk. Should global recovery be faster than expected, it may also have implications for the financing of the current account deficit. Fifth, the recent improvement in the fiscal situation owes largely to one-off revenues generated from spectrum auctions and disinvestment proceeds; however, global commodity price developments will pose significant risks for fiscal consolidation in the year ahead. The efficacy of further fiscal adjustment will be influenced by the firming trend in commodity prices and the extent to which the government will allow this to pass through to consumers. Finally, the combined risks from inflation, current account deficit, and the fiscal situation contribute to an increase in uncertainty about economic stability that consumers and investors have to deal with.

Today's policy actions are expected to contain the spill-over from rise in food and fuel prices to generalized inflation, rein in rising inflationary expectations which may be aggravated by both the structural and transitory nature of food price increases, be moderate enough not to disrupt growth, and finally continue to provide comfort to banks in their liquidity management operations.

Let me now give you some forward guidance. Current growth and inflation trends clearly warrant that we persist with the anti-inflationary monetary stance. Looking beyond 2010-11, the Reserve Bank expects the domestic growth momentum to stabilize. Inflation is expected to moderate from the first quarter 2011-12, but several upside risks are already visible. The monetary stance will be determined by how these factors impact the overall inflationary scenario. Thank you very much.



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Anirudh, ET NOW

Now just to start with, you mentioned very clearly that you are concerned about the credit-deposit ratio and in particular the increasing credit from a lot of banks. So just wanted to understand from your point of view, is it that you want banks to lower their credit growth going forward to the rest of the year or would you rather have them increase their deposit rates or is there some kind of message that you kind of send to the banks through this?

D. Subbarao

The message is exactly as I put out. Credit growth today is 24.4% against the indicated projection of 20%. Deposit growth is 16.5% against the indicated projection of 17%. Clearly there is a wedge between the deposit growth and credit growth and that has been the structural factor, that has been responsible for the liquidity deficit. Over the last few months, we have done several things in order to ease the liquidity situation and you are all familiar with that. There is a limit to how much the Reserve Bank can do, both the structural and the frictional factors have to unwind. The frictional factor will unwind as the government stops spending or they take the additional cash balances now they have for the budget for next year. So we expect that the frictional factor will resolve in the next few months, but the structural factor the banks have to resolve. I am now coming to answering your question more directly. We told them both that they must increase their deposits and they must restrain their credit and that credit growth and deposit growth have to be aligned. Additionally, I think the banks told you in their press conference, we also said and I have just mentioned in my statement also that in the guidance, we have said we will monitor this very closely and use our supervisory responsibilities to ensure that those banks which are far out of line are brought in line.

Ritesh, Zee Business

Sir on the inflation front I want to know that is it right to say that the hands of RBI are tied to some extent so that they will not take extra measures to control the inflation because it is a supply side problem. So interest rate will not contain inflation to some extent?

D. Subbarao

Are there any other questions on this general issue?

Lata Venkatesh

Lata Venkatesh, CNBC TV-18. Governor, you have raised the inflation forecast by 150 basis points from 5.5 to 7%. Is not then 25 basis a weak response, did you contemplate 50 basis at all?

D. Subbarao

Any other variations of this question?

Lata Venkatesh

Very similar question variation being that in terms of the commentary that is coming out, you are talking about the spill over, the pace of the spill over from food inflation to generalized inflation becoming a lot more, but then at the same time in the policy today you are talking about the fact that the monetary policy response has been limited or its efficacy is limited. Seems to be a little bit of disconnect between the message that is coming out from the words than the action?



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Diana, Bloomberg UTV I just wanted to know how do you see things changing from right now where we see inflation at 8.5 to March end. How will things change in terms of prices from now to then?

Arti Governor, Arti from Business India. You said that the inflation situation will ease by the first quarter of next fiscal, right? So does it mean that we are looking at a tough stance this year for the next 12 months, as the liquidity situation is tight and rates have gone up?

D. Subbarao Thank you. I have been expecting this question about our policy stance and whether that has been adequate for the current growth inflation dynamics and please bear with me I want to give you an extended answers.

We have calibrated our exit from the accommodative monetary stance to our unique growth inflation dynamics. We have raised repo rate 6 times and reverse repo rate 6 times and today has been the 7th time. Also our LAF window has shifted from a surplus to deficit mode. So if you take the 7 increases, last shift in the LAF corridor from surplus to deficit, the effective tightening has been of the order of 325 basis points in addition to an increase in CRR by 100 basis points. There has been some monetary transmission I have said strong the adjective that I have used in the statement and some more is yet to play. Yes, it is true that the inflation is driven by supply side factors and for that monetary policy is not always an effective response; however, we do recognize that supply side inflation will spill over into generalized inflation. We recognize that if inflation is left to persist, it will lead to inflation expectations hardening. We recognize that demand side pressures are gaining momentum and the actions that we have taken over the last one year since March 2010 have been directed at addressing this monetary policy response to evolving inflation situation, but you also have to look at the real sector. Growth next year will moderate; it may be because of some mathematical reasons, but it is also because some supply constraints will kick in. IIP has been volatile and to the extent that IIP carries any message. What the message it is carrying is that industrial growth is still not firmly in place. If you look at other indicators, business expectations have moderated. PMI is still above 50, but has moderated somewhat.

And current account deficit, government's fiscal stance, all these factors are going to create economic uncertainty and it is against this that investors and consumers have to make decisions. The dilemma for the Reserve Bank really was how to balance the concerns of growth and the concerns of inflation. This is an economy with per capita income of \$1500 and whenever there is rising income that is happening now that quickly translates to demand side pressures. So our challenge is really to restrain demand pressures in the short-term, but support supply responses. So with one monetary policy instrument, how do we do both. Restrain demand and support supply that has been the challenge. Lata I think asked whether we consider 50 basis points indeed we did and lot of you did as well so we saw that. So it was not as if it was a straightforward decision that fell out of some



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analytical model, it was not unambiguously clear. It was a judgment call and ultimately we decided that we will do 25 basis points. The last thing I want to say on this is the guidance we have given. We have said that we will need to persist with the anti inflationary monetary policy stance and we said that more clearly than before. The second thing as I said before, we will monitor the credit deposit ratio especially the incremental credit deposit ratio of banks. And in response to Diana's question on how it will go from 8.5 to 7 over the next two months? We expect the supply is transient inflation component in food inflation, that will unwind. Some other structural responses might come in and importantly the monetary policy action that we have taken will have an effect going forward. Arti's question about inflation situation how will it change in 2011-12? Again 7% by March 2011; I want to say although I'm not sure we said that very clearly in the guidance which is that we expect inflation will come down during 2011-12 but the pace of coming down will be slower than we expect. Subir you want to add anything that.

Subir Gokarn

Two things. One is we have to take into account the impact that liquidity situation is having on markets and through that on bank lending, on the transmission of interest rates keep in mind that the call rate which is in a sense an indicator of how tighter or loose the policy position has been above the corridor for much of the last quarter in fact as all of it and in a sense that is a reflection of an additional tightness or additional constraint on liquidity which from our interactions with various stakeholders, suggest that it makes a little difficult to keep the lending model, the credit flows model in place because of the uncertainty associated with the liquidity supply. So that's an added consideration when we think about rate changes, is that it is going to be disruptive to the point that it might constrain growth. The second again talking about 50 basis point versus the 25 basis point choice, last year we did make a very conscious, very considerate decision to extent the frequency of credit policy reviews, so that rather than thinking in terms of every quarter and then doing off cycle, we have clearly introduced now a schedule and I think that gives us a little more room in terms of spreading it out if necessary. So the disruptiveness of a 50 basis point hike maybe off set by the spreading out of smaller hikes on a predictable cycle. So it is no longer now it may happen, it may not happen. As we go into the next six weeks we will have more information about how inflation is behaving, you will have more information about how industrial production is behaving and we will have more information about how the global situation evolving particularly with respect to commodity price. So all of those factors help us then take a more considerate decision about the need for continuing hikes and our guidance has been that our stance as of now is clearly and unambiguously anti-inflationary.

Participant

Since you very clearly say that the current growth in inflation trends warrants consistent with anti-inflation monetary stance, should we therefore read this along with your previously mentioned position that rather than give us 50 basis you have more positioned? Should we understand that you are not done with rate hikes?



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D. Subbarao

I am not sure that I want to interpret that for you. We are not done with our monetary policy, our monetary policy stance continues to be anti inflationary and we need to persist with the anti inflationary monetary policy stance and Subir has just told you about the frequency of the occasions for reviewing this. I think interpreting beyond that may not be appropriate.

Participant

Governor just a follow-up question of the previous question. December mid quarter policy RBI did not hike rates, is there are thinking within RBI that if RBI would have hiked rates that time the situation wouldn't have been that worst that RBI would have to hike the inflation projection by 50 basis points?

D. Subbarao

No I don't think that there is a feeling like that. In December we deliberately paused in order to keep the commitment we had given and looking back I think was wise to wait for some time. And inflation development as we know between November and December was a consequence of developments that are largely unrelated to the monetary policy stance.

Subir Gokarn

Can I just extend that? If you look at the breakup of that transition from 7.5 to 8.5 which we provided in the document, the bulk of it came from price shocks that happened in December or late November--onion prices obviously but other vegetables too, but oil was also very significant So these are things that happened partly in response to domestic shocks which we did not anticipate but also in response to what is now being seen as a somewhat more robust global turnaround. So in that sense the bulk of the inflation shock from November to December, happened because of these developments and in that sense I don't think it then invalidates the decision to pause and wait for the transmission to take hold. Now keep in mind that in this period both lending and deposit rates by domestic banks have gone up substantially, that was the transmission that we were anticipating after our November policy and we saw that happening.

Ira, NDTV

It's a follow up on inflation side, we have not talked about the medium-term targets from the RBI and now we stopped talking about the 3% forecast or projection that we used to talk about, we have two years of high inflation behind us and next year is going to be another relative high inflationary year. What should we look at the medium-term comfort zone for the RBI now for the inflation will that change is that we talked about earlier?

D. Subbarao

3% we said in the medium term and 4% to 4.5% in the near medium-term depending on how you interpret the medium-term and near medium-term. Actually we did think about whether we should say that again and we decided not to say it but that still remains our goal and our aspiration. But it depends on how a number of factors will evolve both at home and around the world.

Participant

Then what you have said earlier nonfood manufacturing inflation is 4% or more than that is 5.3% is it that a new goal which you will follow in future?



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- D. Subbarao** No I don't think we will follow one particular disaggregated component of inflation, we have looked at inflation, we have looked at all indicators of inflation and we have looked at dis-aggregated inflation and in less than the ideal world that we have in terms of inflation measurement, nonfood manufactured inflation becomes a measure of core inflation for us, so we look at that. We have looked at that and we will continue to look at it, but I don't want don't give the impression that that's the only thing will look at. That in a way is one of the prime indicators of demand side pressures.
- Aarti, Business India** Governor would you be looking at any constraints on the reverse repo window to push the process through? Banks and funds had a good rates on the reverse repo would you consider putting caps on it if you will be looking at the credit that basically is a mismatch, between the credit and the corporate growth.
- D. Subbarao** No we have not considered that I know that we tried that in the past to put caps on the LAF window but no we are not going to continue that.
- Subir Gokarn** We have put a cap on the reverse repo.
- D. Subbarao** Either way the question is no we have decided not to do that.
- Gopika, CNBC** You have given guidance on inflation and growth for the next year that is FY12. Can we take this guidance seriously considering that most of the guidances given so far have actually gone wrong. So how should investors or market read this guidance?
- D. Subbarao** Whether you take it seriously or not is a decision that you have to make. I would urge you that we put a lot of thought into this and there are problems or difficulties for us to be more specific. On the other hand we did not want it to be so convoluted that it doesn't give any additional message or information. A guidance is important only if it conveys something beyond what is already said, right? And I was very conscious that it must give everybody who is reading the document some additional information about what the RBI is thinking and how the RBI will react to the evolving situation. But how this situation will evolve is largely beyond our control. So we cannot be anymore specific than this. I hope you understand, but again I want to say that we are learning to give guidance and we will try to refine and improve the processes as we go forward.
- Subir Gokarn** I also want to mention that if the guidance is a conditional guidance, it has come very explicitly with the set of risks. So it is our best judgment of how we see the situation evolving. What is that maximum likelihood but clearly recognizing that it can go wrong because one or more of those risks might materialize so that's why it's a guidance and not a forecast.



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Ashwin Shukla

Ashwin Shukla from Live India. Sir I want to talk you in Hindi that within last 9 months by increasing repo rate and reverse repo rate you tried to control the inflation. It has been controlled somewhat but we could not see the full impact. Sir do you think that is there a gap between demand and supply if government keeps an eye then the inflation can be controlled? (32:36-part translated from Hindi to English)

D. Subbarao

The situation of inflation is from supply side and from demand side also, this is responsibility of government and responsibility of Reserve Bank also. As you have said that Reserve Bank has increased the rate seven times and the government is trying on supply side. Both have to make the effort. So government has to do and Reserve Bank also has to bridge the gap between the supply and demand. [Translated from Hindi to English]

Ashwin Shukla

Who is responsible for this weakness--RBI or government?

D. Subbarao

No I'm not talking about the weakness. Both are trying and state governments are trying too.

Atul, ET

This is Atul from Economic Times. In your policy document you have said that there could be capital outflows if the western countries grew, now what will be the impact on Indian economy of that?

D. Subbarao

This again is our reading of the situation. This year 2010-11 we have said that the current account deficit will be 3.5% of GDP and we don't foresee any problem in financing that. In fact for last several years we have not had a problem in financing the current account deficit. But next year we want two things, that we want our current account deficit to narrow and we want that to be financed by more stable source. This year, of course, there has been continuation of monetary easing in advanced economies and as a result financing of CADs has not been a problem. If advanced economies recover, the relative attractiveness of bringing money into emerging economies will reduce. So we said that that is a risk factor, we must keep that in mind. But I don't want to give the impression that we see a serious problem in financing the current account deficit. That will not happen. What we need to be concerned about is what type of flows is going to finance the CAD.

Subir Gokarn

Just to reinforce I think you are referring to risk factors on page #10. We are not talking about outflows, we're just talking about the possibility that the rate of inflow will decelerate because there will be a more balanced portfolio approach by investors as other economies start to show growth. So it is not really a question of money flowing out in the way that we saw in 2008 that's not the scenario we are visualizing. We have said that the money flowing in will slowdown little.



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- Vijayshankar Patel. PTI** Sir what would be the impact of policy rates hike on various loan given by bank, will they become more expensive?
- D. Subbarao** Well if the monetary policy transmission works as we want it to lending rates will have to go up and loans by banks will become more expensive.
- Bijoy, Newswire 18** Last time when you had given the guidance you had indicated in the December mid-term there would not be any tightening, this time there has been seen no clear indication on what that is and what would be the effect after that indicate that there could be a phasing out continued to 25-25 kind of growth that RBI may see. So is there something that you could read into that sir?
- D. Subbarao** Again I want to say that I cannot interpret anymore clearly than what is indicated there and what we just said. We have said that we need to pursue with the anti-inflationary stance and there is a milestone, as Subir said, every six weeks. So that's what it is. I cannot really say anything beyond that.
- Bijoy** Have you ruled out the possibility of inter policy actions?
- D. Subbarao** We have never ruled that out, only we said that mid-quarter review we will think twice before taking policy action. But we never ruled that out.
- Anup, Bloomberg** Sir as the global economy recovers and since the pace of the inflows currently stabilize what is the impact you are anticipating from the currency markets and the exchange-rate, possibly because the recovery is uneven. So what is the impact you are anticipating on the currency market volatility and exchange rate and the second question is that what sort of support you are seeking from the government in terms of making the monetary policy more effective?
- D. Subbarao** The answer to your first question is fairly simple, that I don't want to speculate on currency movements. So as inflows come and go, as current account transactions takes place the exchange rate will respond to that and we will respond if there is volatility. So beyond that I don't think it is appropriate for me to say anything on the exchange rate. On the second question we have been saying it--we said that very clearly last time and we are saying that again this time, which is that for monetary policy to be effective there has to be fiscal consolidation. Because crowding out is becoming more and more of a distinct possibility. Earlier times crowding out was a theoretical construct, even as government borrowed because the private sector was not in a position to raise credit or not demanding credit, the crowding out impact did not happen. But this time round crowding out is going to happen, so fiscal consolidation is important. The second thing is about how fiscal adjustment might take place in the face of increase in commodity prices, especially oil and fertilizer prices. If the government decides to absorb that on that fisc, fiscal adjustment



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will become a problem and there will be inflationary pressures coming from the fiscal deficit. If the government decides to pass it on to consumers, there will be an inflationary impact through the price increase. So it is a difficult thing for the government. At least what I told the government is that, now that I am outside the government I can advise them, is that between the two I think it is important to focus on fiscal consolidation because that will have a long term impact.

Mayur, Times of India

There are two questions. First of all, it is related to housing. You had earlier expressed concern over housing prices, since in some pockets the prices have gone up even more. Do you feel that this is a concern or is this too isolated to reference? And the second question is on the issue of black money which the Finance Minister has announced some steps to measure. So would the Reserve Bank of India be joining the government in this?

D. Subbarao

Thank you. More generally on the asset prices, we did not make a comment in the statement this time. But the point is that on the equity markets there has been a correction. Gold has come off from its all time peak and on the real estate housing, the question that you most directly asked, I am not sure that prices have gone up across board. In fact, we have not done any surveys but anecdotal evidence suggests that the prices are stabilizing or at least the rate of increase has come down. So we continue to monitor the asset prices but there has been no movement in asset prices to warrant a specific statement in the policy review. On the second question about black money, I am afraid I have not seen the Finance Minister's press conference, I do not know what he said, but to the extent that Reserve Bank has any role, we will take action.

Shukla

Sir this question, maybe not only from my side but from the common man which I want to ask in Hindi. Today one road side gentleman asked me that why is there so much crowd here I informed him that today policy will be declared, he asked me, what would happen with that. I replied that maybe high prices will come under some control. So please reply to those lakhs of people, about this decision of yours to reduce the reverse repo rate, will this be beneficial to the common man or will things keep going on like this? [Translated from Hindi to English]

D. Subbarao

We feel that definitely there will be benefit because inflationary high prices will come down, that is what we are trying for. The common man is more affected by high prices, we know that. We are also going to villages and small towns in the "Outreach" programs and meeting and seeing people. I may not meet those many people as you do, but we do know what is happening. High prices will come down and after that whatever rates we are adjusting, the deposit rates will come down for common man. With the deposit rates coming down he will get more interest in his savings and those people who are getting credit, definitely the high prices will be there, but in the long term will get adjusted. (42:00-translated from Hindi to English)



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Swati, Reuters

This is with regards to what Sarkozy said yesterday. He spoke about wanting some kind of regulation for the commercial markets so as to reduce the volatility. And he also spoke about the possibility of some kind of a global database for commodity stocks. So what is the RBI's view on that? Any kind of comment that we can answer you on that?

Subir Gokarn

Not really, it's a ongoing debate in the

S. Gopinath

If there is a move to get data on commodities well it will benefit everybody I am sure.

D. Subbarao

I think President Sarkozy said as the French leadership of the G-2- perhaps and I am sure that what is told in the press conference he would carry forward in the February meeting.

Gautam Chakravarthy

Good afternoon, this is Gautam Chakravarthy from Ticker Plant. One of the points that was mentioned in the macro economic review and which you also partly responded to in your statement some minutes back, was the volatility in the financial markets basically, both to the FX foreign exchange and in the liquidity front. Is there something in terms of when you talked about liquidity being above the comfort level, can it be interpreted that RBI will step-in with more such measures like OMOs and other things when the market is in excessive deficit mode? And simultaneously also intervention in the foreign exchange market wherever it is necessary, thank you.

D. Subbarao

On the liquidity question, yes we have not said anything about OMO, but we have said that Reserve Bank will endeavor to manage the liquidity to see that the credit needs of productive sectors are met. In response to an earlier question, there are limits to how much the Reserve Bank can intervene because some of these frictional and structural factors will have to resolve and not afford to do anything that runs counter to its anti inflationary stance. So we have to strike a balance and I cannot really comment on that we will do but for now we have not announced any further OMO. So I will again summarize what I have said, we want to be sure that there is liquidity enough, that it needs for productive sectors but we also want banks to understand the limits to which RBI can intervene in the liquidity market. On the exchange rate issue, the response is standard I sure it is getting quite old now, we will intervene only if there is volatility.

Abhas Pandya, Newswire 18 Sir, would you want to give any guidance as to when you see liquidity getting back to the comfort zone that you have been ascribing to?

D. Subbarao

No, I am afraid that is not possible. I am only hoping that in the next few months this easing will take place with the government spending and if the banks take in the message that we gave today about aligning their credit growth to their deposit growth. But I am



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unwilling at this point of time to put out a time frame in which the adjustment will take place.

Lata, CNBC-TV18

Sir in the previous policies up until November you have always mentioned something in terms of a medium term inflation perception that RBI wants to fashion. I am reading of a November policy, “the conduct of monetary policy will continue to condition and contain perception of inflation in the range of 4-4.5 percent, this will be in line with the medium-term objective of 3 percent inflation consistent with India’s broader integration into the global economy.” That constitutes it by its absence. Why? And secondly there is in some sense, I can read out several lines which seem to indicate a certain helplessness of RBI. We can as such contain inflation from flowing over to a generalized inflation. But the government has to do this, the government has to do that, it has to increase agriculture, it cannot go berserk on deficit. So is there a feeling that now its in the government’s court not in our court, and we are helpless. So in that context would you say even a 4.8% fiscal deficit which is next years target is too much?

D. Subbarao

On the first question, actually Ira asked a bit earlier. That message was not put in this policy and I do not think you should read too much into that. That still remains our medium term goal. But we also are aware that as income levels go up, demand-supply imbalances might accentuate further before they start adjusting. So the time to reach 4 to 4.5% might be a little longer than we had talked earlier but that still remains RBIs goal. I would urge you not to read too much into that conspicuous omission. They can speak to us as it might be.

On the second question I do not think you should read that as helplessness as more of explaining what the current inflation dynamics are. Precisely for the reason that you and many others asked about the calibration of our response, why is 25 basis points and not anything higher, we have to explain that about to what extent RBI has a role and how we are meeting that role. It is not that RBI is helpless, but combating inflation is a shared responsibility of the government and the RBI especially inflation of the dynamics that we are seeing today. So whatever we have said is by way of explaining, and not by way of apologizing or not by way of expressing any helplessness.

Subir Gokarn

I think a lot of the heightened concern about inflation has come from the reversal of the food price strength and I think we have to emphasize this fact that what we are seeing as demand side inflation pressures, yes, there is some reversal in that as we pointed out with respect to non-food manufacturing. But that is not as dramatic as has happened on the food and energy front. So I think it is also a question of managing expectations--if you have to respond to headline, there is a huge risk of completely undermining the growth process without necessarily having any impact on inflation, which is an outcome that is even less desirable than having or maintaining the balance that we are talking about. So we have to



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be fairly clear about what our instruments are able to address and to the extent that there is concern over the turnaround, however, modest it may be, in non-food manufacturing inflation. We have responded to that turnaround and we believe that this pressure is likely to persist because of the other factors that are contributing and that is really shaping our stance as to go forward.

Ira, NDTV

It's a non-policy question, not directly linked to inflation or growth, but I just wanted to ask you about banking supervision in the context of for the Citibank case, firstly, whether anything has materialized in terms of reporting from them to you on that specific case. But the broader issue on the supervision especially when it comes with a time when the RBI supporting linking up foreign banks considerably.

D. Subbarao

I will first refer to Anand to answer that question that may be I will add to that.

Anand Sinha

As far as wealth management is concerned we have a set of guidelines, we do not call it wealth management, those are PMS i.e., Portfolio Management and there are extensive guidelines on that. Now in the case of Citibank the supervisory department is looking into what exactly had happened and once we know that, once we have a full picture then we will have to look into the regulatory issues and the regulatory gaps if any. Then the question of investment advisory also comes in where SEBI also has a role. So once the full picture emerges then we will be able to take whatever action is required to be taken.

Gopika, CNBC TV18

Sir it is just not seen in the Citi case, there have been other cases with lots of question the corporate governance within the banks and probably the lending standards. So what is RBI doing in terms of it enhancing the supervision and maybe regulating banks better?

Mr. Gopalkrishnan

See basically you have a three level of supervision. One, internal control, second the internal auditor, the financial auditor and finally in the bank, so each of us has to play a different role. As far as Reserve Bank is concerned, these are overall system levels whether interest in the depositing is taken care of or not. So that is the major objective of the bank. But these are the issue of course, do come across when we take up these issues with the bank during the course of annual financial inspection or other interactions with the bank. Not to say that the entire system is bad but it is correct to say that their....

D. Subbarao

But I do want to add from my level, which is that we have the board for financial supervision, where all of us, all the Deputy Governors, all the concerned EDs, and we have some very learned members of our board and outsiders on the DFS, we look at all this and we take lessons from specific cases for systemic improvement. Ira, question you asked. So whatever comes out of Citi or any other specific instance we would not treat that as an isolated incidence, but do see what lessons they might have for improving our supervision, our regulation, and as Anand said, that to see if there are any regulatory gaps. And you will see that over the last 2.5 years, nearly 2.5 years that I have been here in



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know that specific instances have led the systemic responses. For example, that the non-convertible debentures, NCDs were less than one year. We found that that was a regulatory gap and we responded to that. So it does happen that we learn our lessons.

Gopika, CNBC-TV18

Sir one question on the Malegam Committee Report. The report actually recommends that basically the regulation of NBFC-MFIs should come within the ambit of Reserve Bank. Is Reserve Bank equipped to supervise and monitor the functioning of MFIs and do you think the state government machinery should not play any role in the supervision?

D. Subbarao

No, first of all on some correction. We already regulate NBFCs which are MFIs. So that is already under our regulation. What the Malegam Committee has recommended is to carve out a special category of NBFC-MFIs because the regulation for them has to be different from other NBFCs. So that we will consider. Second, about whether the Reserve Bank has the reach, I have not read the report but I have been briefed about the report, I have read the summary. What the committee has said is that there has to be different levels of the regulation-- by the MFI itself as an organization of MFIs, by the banks, and then by the Reserve Bank and that the Reserve Bank will have to do selective regulation and supervision. I think that is eminently reasonable and that is what we will try to do. But how it might evolve, what specifics there are we have to think through. The third part of your question about state governance, now Andhra Pradesh has been the one government that passed the law, other state governments might do it but what Government of India and the Reserve Bank will want is that the regulation has to be neat, should not be overlapping and should be clear, not only to us regulators but to the general public about who is doing what and I am hoping that as we implement the Malegam Committee, this will become clear. I have requested Dr. Chakraborty that as part of the review and implementation of the Malegam Committee, we will call some state governments and Government of India and have a half day work shop to understand their perspective. But you are right Gopika that we need to resolve this with the state governments, everybody has to agree on the regulatory pattern.

Alpana Killawalla

Thank you Governor. With this we come to the close of this press conference. I am sorry if somebody did not get a chance to ask questions and thank you regional press, Melissa and everybody here. Thank you.