Interview with the Economic Times on December 14, 2020 – Shri Shaktikanta Das, Governor, Reserve Bank of India

It has been two years since you became the governor. How do you describe the challenges in this role compared to your previous role as a bureaucrat?

There have been several challenges and it is difficult to segregate one from the other. The pandemic is the biggest health crisis in a century leading to an economic one. The event by itself is once in 100 years. The level of direct accountability with the governor is very high. In RBI, the buck stops with the governor. When you are in government, you are part of a system and the accountability is on the government. That means the political executive. As a civil servant, you face challenges from day one in a subdivision where there are law and order issues to deal with. But this role in the RBI is the biggest so far. Whatever you do and whatever you don't do has implications for the economy and financial markets. You have to take the right step at the right time.

Central banks like the US Federal Reserve or the European Central Bank (ECB) have responded to keep markets functioning with liquidity. RBI also did so. How do you assess your actions?

When we went into the pandemic, there was a synchronised slowdown already across countries. The financial markets were drying up. In India, the corporate bond markets were coming to a standstill. Every central bank had to respond to the domestic situations. There was no template. In February, we announced the LTRO (long term repo operations). There was a talk about virus in China spreading to other countries. I mentioned in my February statement that we needed to be watchful. First was a generalised liquidity action. We also realised that some banks didn't have enough excess government bonds for accessing liquidity through the repo window. So, we cut CRR. (In parallel), we nudged banks to lend and not passively park surplus with the RBI. We were closely monitoring the stability of the financial system.

You transformed RBI's approach to liquidity. Financial markets are cheering, but economists are warning about the next crisis. What are the risks?

When we announce measures, we also assess the risk for every measure. We always evaluate the downside risks and how to mitigate it. The liquidity infusion has achieved its objective. Bond markets are revived. The flow of liquidity to NBFCs (non-banking finance companies), MFIs (micro finance institutions) and others got revived. Now the excess liquidity is from foreign exchange flows. If you go by the ECB and Fed's talk about keeping rates low for long and liquidity in abundance for two years, you will have inflows. Within emerging markets, India is seen as a safe and sound market by international investors. We are fully aware of the downside risks. We also analyse what kind of mitigation measures need to be taken or what safeguards need to be built into the measure itself to ensure that it does not lead to other problems. We also have to keep in mind that this crisis is the biggest the world has faced in 100 years, bigger than GFC (global financial crisis) and even bigger than the great depression. Still, uncertainty prevails though there are optimistic signs on vaccines. There's a fear that continued easy policies and rising inflation could be a potent combination that could cause the next crisis… and you have cautioned the financial markets. When you are dealing with the worst crisis in 100 years, you have to put in your best to revive growth and to contain the detrimental effects of the pandemic on the economy. We are very much aware that a premature withdrawal will be detrimental to growth. A delayed withdrawal will also have its own negative effects. We are fully aware and conscious of both the ends of the situation. Therefore, we have to take a balanced call and at the right time. It will be our endeavour to take the right call at the right time. Both premature withdrawal as well as delayed withdrawal can cause problems. We are mindful of the delicate situation. I am confident we would be able to strike the right balance. Let me reiterate that our forward guidance to markets stands and we shall adhere to it.

We had three bank blowups in less than 18 months. And that's causing some worries.

We are intensely monitoring. We were aware that there are problems. We expected them to resolve the issues through market-based mechanism. When that did not happen, RBI had to intervene to protect the depositor interest, which is paramount. The intervention in the two banks is more to do with specific situations in those banks and has nothing to do with systemic issues. It doesn't reflect on the strength of the banking system. The system continues to be robust. Banks should raise capital proactively to build up their resilience.

Is there a lapse in supervision and inspection?

In the last two years, we have substantially tightened our supervision of banks and the NBFCs. We now have early warning signals. We have an internal matrix. One of the signals, for example, is the business model of the bank and the composition of loan growth. If there are alarm bells we go deeper. During the pandemic, we have become much more specific and sharpened our examination of issues from the financial stability angle. We are also having a deeper look at small finance banks and urban cooperative banks. There's greater use of suptech (supervisory technology) for supervisory analytics and we are constantly trying to also improve our analytical systems.

Is the DBS' takeover of Lakshmi Vilas Bank (LVB) a signal toother foreign banks? There's also a feeling that there's no consistency in the way banks are bailed out.

Since the matter is in court, I won't be able to comment. There's no standard template for dealing with problems in individual banks. Each bank has a specific situation and needs to be dealt with. Therefore, the cases of Yes Bank and LVB were different. We reacted to the situation prevailing in each bank. It has to be case-specific, but the underlying theme is to protect depositors' interest.

You are doing everything to boost growth. How has the economy responded?

There are signs of growth, but it is not broad based. We are forgetting that we are in contraction. Therefore, the MPC (monetary policy committee) has given unambiguous forward guidance to support growth while remaining watchful of the emerging macroeconomic scenario.