"Reserve Bank of India Post Policy Conference Call for Media"

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Moderator: Ladies and Gentlemen, good day and welcome to the Reserve Bank of India Post Policy Conference Call for Media. As a reminder all participants' line 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 an operator by pressing '*' followed by '0' on your touchtone phone. Participants connected to the audio bridge may press '*' and '1' to ask a question. Participants present in the conference room are requested to use the mike while asking a question. I now hand the conference over to Ms. Alpana Killawala. Thank you. And over to you ma'am.

Alpana Killawala: Thank you, Shyma. Once again welcome from the Reserve Bank of India to this Post Policy Press Conference. Once again to reiterate what the moderator said, those in this room please use the mike when you ask your questions. Announce your name and the organisation and then ask the question, because we put a transcript of this on the website, it helps that. Over to you Governor.

Dr. Raghuram Rajan: Thank you. Let me start with a short statement. Good Morning. Recent readings suggest that headline inflation, both retail and wholesale have increased, mainly but not exclusively on account of food prices. While core CPI and core Wholesale Price Index (WPI), that is, inflation excluding food and fuel have been stable, despite a steady and necessary increase in government administered prices towards market levels, the high level of core CPI inflation leaves no room for complacency. There is, however, reason to wait before determining the course of monetary policy. There are indications that vegetable prices may be turning down sharply, although intermediaries could impede the full pass-through into lower retail inflation. Our own current readings from the metros suggest a significant fall in vegetable prices, both at the wholesale and retail level which gives us reason to make this statement. In addition, the disinflationary impact of recent exchange rate stability should play out into prices. Finally, the negative output gap, including the recent observed slowdown in services growth, as well as the lagged effects of effective monetary tightening since July, should help contain inflation.

This policy decision, which is to stay on hold, is a close one. Current inflation is too high and I repeat, is too high. However, there are wide bands of uncertainties surrounding the short term path of inflation from its high current levels. Given the weak state of the economy, the inadvisability of overly reactive policy action, as well as the long lags with which monetary policy works, there is merit to wait for more data so that uncertainty can be reduced before we act.

There are obvious risks to waiting for more data including the possibility that tapering of quantitative easing by the US Fed may disrupt external markets and that the Reserve Bank may be perceived to be soft on inflation. Let me assure you that the Reserve Bank will be vigilant. Even though the Reserve Bank has maintained status quo today, it can help guide market expectations through a clearer description of its policy reaction function which is: if the expected softening of food inflation does not materialise and translate into a significant reduction in headline inflation in the next round of data releases, or if inflation excluding food and fuel does not fall, note that there is an "or" here, which means both conditions have to be met, the Reserve Bank will act including on off policy dates if warranted, so that inflation expectations stabilise and an environment conducive to sustainable growth takes hold. The Reserve Bank's policy action on those dates will be appropriately calibrated.

Finally, let me add that following our commitment to restore economic value to financially distressed projects and to clean up problem assets in the financial system, the Reserve Bank has put out a discussion paper for comment yesterday. After a comment period of two weeks we will issue the appropriate circulars. With that I am happy to take questions.

Alpana Killawala: Yes, Latha.

Latha: Latha Venkatesh from CNBC TV18. Governor, we were expecting a Volcker, we have got a Yellen. Your trajectory which you gave us in the October policy would indicate that your forecast would be at this moment- it should be something like below 9%, the CPI inflation if we went by your fan chart. You are 2.5 percentage points higher than where you were. What do you want your next reading to be? How should we read the RBI? Should it be like, if it came at 10.5, how should we understand? If it came at 10, what should we understand? Does it satisfy your trajectory?

Dr. Raghuram Rajan: First, to your Volcker, Yellen, etc. –how about a Raghuram Rajan? I think it is important to resist the labels of dovish, hawkish, etc. We are trying to calibrate monetary policy primarily to target inflation in an environment where the economy is weak. So when we take action we have to be convinced that the action is merited at that point, which is why we are waiting to take action. This is in some ways, I mean if you want to go into theory this is Brainard's, when there is a lot of uncertainty, you want to wait for more data to come in to get a sense of how you want to act. The precise calibration of action, remember, that any monetary policy action is determined by the variety of variables. So if I tell you, if it is X we will raise the rate by Y, I cannot tell you that, because the rate decision depends not just on a particular indicator but a variety of indicators. What we have said is that we need to see a substantial softening of both headline inflation as well as some momentum in the right direction in core inflation, that is what we will be waiting for. The precise numbers I do not think it is that clearly demarcated.

Latha: In the hierarchy of parameters for inflation, core CPI is the most important?

Dr. Raghuram Rajan: I did not say that. I said we will look at a number of parameters, but we do want to see softening in core inflation.

Alpana Killawala: Aniruddha.

Aniruddha: Aniruddha from ET Now. Two questions, firstly in terms of your target for growth and given the recent IIP numbers, how concerning is the slowdown in growth? You mentioned that you will be looking at the next data release as far as the inflation is concerned, would the next GDP or IIP release also be as important? And secondly, given that most of these concerns on inflation are supply driven and given that the government is expected to go a little slower on the policy action, how concerning would that aspect be from the policy side?

Dr. Raghuram Rajan: I think certainly we will look at the growth number. Our sense is growth is below potential even now, and that effect of the negative output gap should be seen in the inflation numbers. If it is not seen and that transmission is not taking place, we have to query our assumptions and that will be an important factor also.

Anirudhha: And supply side?

Dr. Raghuram Rajan: There is this argument which has often been made that the supply side is what is the constraint and clearly there are some supply side constraints. But I have said repeatedly and I will repeat once more that ultimately inflation is a mismatch between demand and supply, if the supply is not responding you cannot keep postponing decision saying it is because of the supply side. There is inflation, and that will mean we have to bring demand in closer match to supply. You mentioned very weak economy that will give us some indications of the demand side but we have to balance the two.

Alpana Killawala: Ritesh.

Ritesh: Governor, Ritesh here from Zee Business. Two quick questions; firstly in the last policy you said that second half will be better for the economy. Given the recent IIP numbers and the inflation numbers also, are you still confident or equally confident of the recovery in second half because you all are talking about it but the number does not show anywhere. And second question is about the monetary policy transmission. Last time around in the monetary policy, RBI had hiked rates but not many banks had passed it on. So that also, the lag effect which RBI talks about in this current policy cannot be seen actually. So is the RBI happy about the way monetary policy transmission has happened last time?

Dr. Raghuram Rajan: To some extent remember that when RBI cut rates, the cuts were not transmitted. So there seems to be certain amount of lag in the system, if you will, or lack of response. But, I think going forward we will have to calibrate policy to the circumstances. You talked about growth in the second half. Our sense is still that growth in second half will be stronger than growth in the first half. Of course, the factors that will play out, rather factors that have been playing out so far which is agriculture, exports and the long but delayed awaiting of the stalled projects coming back on line. We hope they will come back on line, that will help growth, that will also help sentiment. It is important however that everybody -- government, RBI be vigilant to the growth scenario.

Ritesh: Do you feel the number projection which RBI gave is happening?

Dr. Raghuram Rajan: I think give or take a few basis points, yes.

Alpana Killawala: Saloni.

Saloni: Saloni from Bloomberg. Sir, first question would be on the gloomy picture that we are seeing in terms of the macro numbers that we saw. On the fiscal deficit front we still see a lot of concerns, though CAD has receded. I would like to know your own reading as to how big a concern that would be. Because, even in the document you have mentioned that given the fact that fiscal deficit still remains high, the government would go on an expenditure cut. Your concerns regarding that. Also, just to understand your stance as far as this monetary policy is concerned, given the fact that January will be a high agriculture output season, you will wait for data as far as the food inflation and CPI numbers are concerned.

Dr. Raghuram Rajan: Yes, as far as the data goes, we will be looking at all indicators on inflation. I think the government has reiterated again and again its commitment to its fiscal deficit target. My own discussions with government officials suggest that they are very firm on achieving it, and they will achieve it March end. So that will mean given where we are certain amount of expenditure from traction in the fourth quarter. That will have some adverse growth effects of course, but that is part of I think what they need to do in order to meet the numbers they have set out. Of course, an increase in disinvestment from where we are now, greater revenues from state-owned companies will also help meet the deficit target. How much that happens? We have to wait and see. But I have been reassured time and again in private but also I think public statements by the government have been that the fiscal deficit target will be met.

Alpana Killawala: Suvashree.

Suvashree: Suvashree from Reuters. I just wanted to clarify the RBI policy stance:, is there a change in the stance given that monetary policy will not handle vegetable price led inflation, and that is why you want to handle it through non-monetary policy related issues, that is why you did not do a rate hike, and even going ahead if inflation is driven by vegetable prices and food prices you will not tackle it through monetary policy?

Dr. Raghuram Rajan: I do not think you should read it that way, I think what we are saying is that we will not react to every spike in inflation that is temporary. Monetary policy after all operates with long lags, 3 to 4 quarters, right? So whatever we do now is about affecting things output a few quarters down the line. So we have to be sure that what we are dealing with is longer term phenomena rather than a short term spike in certain elements. Our sense from looking at the data that we have access to, not just reading the newspapers, but data that we have access to, is that at least from a sample of metros and this is not as comprehensive as the inflation data collected by the government but certainly sampling of metros suggest that vegetable inflation is coming down quite sharply. So in that sense our view is, this may be a spike. Let us look through it. And our belief is that so long as we reiterate our commitment towards tackling inflation people should not doubt our commitment to that. And what we are doing is basically looking through spikes and seeing the longer term movement which we hope will be reflected in the next round of data.

Alpana Killawala: Bijoy.

Bijoy: Bijoy from Cogencis. Two quick questions; one is has CAD clearly moved down your priority list when you are looking at prices, are local factors now clearly driving your policy decision? And on the other front, you spoke about liquidity in your policy statement. Do you think you will have to continue to maintain the curbs on liquidity so that the term repo window that you all have created becomes more accessible, to make it viable for people to borrow at term repo do you think you will have to kind of retain liquidity at those tight levels?

Dr. Raghuram Rajan: On the first issue the external environment cannot be something that we become complacent about, we are certainly focused continually on the external environment. As I said before we are in a better position to withstand the volatility stemming from tapering, our current account deficit is significantly lower, and we have shown the ability to raise money we need. If you look at FII inflows since April 1st, on net now they are negative two billion. In another words the equity inflows have offset the debt outflows by a considerable margin. If you look at debt, there were outflows till about late November, early December we started seeing inflows once again. All this suggest we are in a better situation but I do not think anybody in the world including the Federal Reserve knows the consequences of what happens when they announce tapering. I think the maximum likelihood at this point is 'tapering lite' as some people call it starting tomorrow but whether its tomorrow or next month or the month after, it has to happen, and we are better prepared to withstand it, but we cannot in anyway take our eye off the ball. So on the external environment, I think we are still focused. Current account deficit I would be much happier if we had the kind of current account deficit we have without significant curbs on anything, including gold. I think that is our aim. We should aim for having a current account deficit without any distortions, removing the incentives for smuggling, etc. That is what we will work for, but at this point I feel very comfortable with where we are on the current account deficit. On the liquidity measures let me turn to Dr. Urjit Patel.

Dr. Urjit Patel: Thank you. The term repo market has been put in place but that does not mean that we would not have normal monetary policy at the overnight tenor, and therefore while we strive to get to the normal monetary policy at the overnight tenor we find that banks find the 15-day and possibly even going forward the 1-month repo be quite suitable for that purposes, and therefore that would carry some term premia, and for the moment not only for domestic reasons but for the reasons that the Governor just outlined for that in terms of being vigilant on the external front, the curbs on the overnight repo at 0.5% of NDTL will continue to be there.

Alpana Killawala: Aparna.

Aparna: This is Aparna from The Financial Express. My question is clearly given the growth- inflation scenario, you would have seen something really that has been overwhelming on the growth side to pause today largely because you have said that a rate hike would have been overly reactve from the RBI. What I wanted to know is we have never seen CPI may be below 9% in the last 3 to 4- years and entrenched Indian food inflation history shows that food inflation is out of hand. What was it on the growth side that you saw that made you pause today? And I have one more question on transmission. You have a ceiling on the LAF repo tender borrowing and because of this the price of immediate liquidity is somewhere between the repo rate and MSF rate. In your response to the inflation going forward where will liquidity and where will this corridor feature and how would you tweak it?

Dr. Raghuram Rajan: On this issue of overly reactive, the point that what we are trying to make there is we should not react to every reading of inflation if we believe that inflation will come down. In other words if we set the level of policy consistent with 11.24 reading on CPI headline and it came down to 9 next month or 9.5, whatever the number is, would we then react to that 9.5 again by changing the policy rate. In other words we have to see through that. We are vigilant for the possibility that food inflation may be more entrenched, we are not ignoring food inflation but we would like to see through the noise, and for that we want to wait a month more, right, till the data comes in to see what those data reading suggests. So this is not in any way changing trade-offs between growth and inflation or anything of that sort. This is saying that as responsible central bankers, in an environment where there is a weak economy we have to try and see what is the underlying strength of inflation that we are trying to tackle recognising that monetary policy works with fairly long lags. So we will calibrate the level of the policy rate consistent with what we think the underlying inflation is. Our sense is the recent numbers add a lot of noise, and we want to look through them. We also want to see what has been happening because of the last couple of rate hikes, what has been happening as a result of the exchange pass-through, remember, the exchange rate has also strengthened, and we think another month's reading will not put us way behind the ball in some sense, and we will at that point set policy accordingly. So what we are trying to do is be responsible central bank.

Alpana Killawala: Govardhan.

Govardhan: This is Govardhan from Economic Times. You have maintained that the real returns for savers is likely more important than anything else for the economy to come back but with the still real negative returns for investor or for savers and inflation and your stand, is there a contradiction in what you have done today? Two is that you said that we will not react to every spike that is happening and in last 3-4 years your predecessor had taken the stance once, and he came up for criticism, and especially from Mr. Patel when he was there with RBI for a little bit of time. So what is that you are looking here?

Dr. Raghuram Rajan: I do not want to say we are risking nothing because in the policy statement we have said that any kind of sense that we are on status quo will immediately raise questions of whether we are being soft on inflation. I want to emphasise we have not been soft on inflation, we are waiting for data. I also want to emphasise that it should not be taken that we are on hold, we are waiting for data, and as the data come in we will react appropriately. Now just as an aside I should emphasise that there are actions that the government can take on some of these supply side issues and I think there has been some movement by the government for example in releasing wheat stocks but can more action be taken by both the central government and the state government in bringing down food prices that will help in the overall inflationary environment. We do want inflation to come down to a level where savers have a positive real return, where the savings rate in the economy comes back to some of the levels it has been in the past and there is no reason why it should not and especially this should come back into financial savings. So again I think the takeaway is that policy will continue to be calibrated to the incoming data. Our sense is the current data was marred by a certain amount of noise and once we see the new data we will see whether the trends are consistent with the disinflation that we want in the economy, if it is not we will act accordingly. You want to add anything, Urjit?

Dr. Urjit Patel: Just to say that the forward guidance in the last para is about the strongest I have seen from the RBI- that if the expected softening of food inflation does not materialise and translate into a significant reduction in headline next month or if inflation excluding food and fuel does not fall, the RBI will act. I think what the Governor has said that if we believe that increase in vegetable prices in the latest read is temporary, then actually it would be not good policy to have reacted to it given that everything else has stayed the same, CPI excluding food and fuel- marginal increase of just 0.1% on the non-food manufacturing on the WPI side. So reading that and the forward guidance, I think there is no doubt that we are extremely vigilant regarding inflation reads that are more than transitory, but it would not be right for us to have acted if we and I think everyone else seems to be saying that it could be transitory.

Dr. Raghuram Rajan: But let me also add to what Dr. Urjit Patel has said that we are not happy with the level of core CPI either even though it has stayed stationary, we want to see it come down which is why that second statement in the forward guidance should be also taken seriously, we want to see some softening in the core to see that the transmission that we have been awaiting actually takes place.

Latha: If you can read that paragraph further, you end that paragraph Dr. Patel with the guidance that the Reserve Bank policy action on those days will be appropriately calibrated. Should we understand that you are warning about 50 basis or are you warning that no rate will be calibrated or, how do we understand calibrate?

Dr. Raghuram Rajan: Appropriately calibrated means appropriately calibrated, it means that there is more than just one number, there are multiple numbers, and we will pick the one that is appropriate for that date. I think you can read whatever you want into that. No, we are not defining a particular number; we are saying the number will be appropriate to that particular reading.

Alpana Killawala: One last question from this room.

Alpana Killawala: Pradeep.

Pradeep: Pradeep from CNBC Awaaz. You mentioned about fiscal contraction. You said that there would be growth implication but I also assume there would be deflationary or disinflationary implication if government does cut down the expenditure, should we think that that is one of the major reforms which need to be taken today? And second, last time they did a similar exercise a lot of the expenditure cut in March quarter was actually a roll over to the first quarter of next fiscal. What is the kind of quantity and quality of expenditure cut that you are expecting?

Dr. Raghuram Rajan: First, yes, if you look at the policy statement, we are also saying that we expect expenditure reductions in the fourth quarter which will be disinflationary and that is something we are looking at also. Again, it depends on the outcomes and how the government acts. My reading is that there is always a certain amount of rollover. I do not expect the net rollover this year to be significantly greater than the net rollover from last year. But of course this is we have to wait to see policy action for that, but my discussions do not suggest that there will be an increase in that to a significant extent. That is not something we are factoring in a big way.

Simran: Governor, one last question, you spoke about improving foreign exchange reserves. So is this going to be fluidic from now or more calibrated nature in terms of building up the foreign exchange reserves that you already started off?

Dr. Raghuram Rajan: Our foreign exchange reserves have built up on the backs on the FCNR and capital window that we opened where we took the money directly into reserves. We are not in a sense targeting an exchange rate, and therefore we are not going into the market and buying reserves at this point to increase the foreign exchange reserves, we have not done that. It is basically what has come in through that window.

Simran: That is what you intend?

Dr. Raghuram Rajan: I did not say that, I said we have not done that, and the increase in reserves thus far has come from those windows.

Simran: And are you content with the kind of volatility in the currency, 61-62 where we are at right now?

Dr. Raghuram Rajan: I think we are happy with the reduction in volatility and that was our aim right through, we wanted to reduce volatility, we also wanted to reduce these unhinged expectations, there was a point where analysts were competing with each other to see how weak they could proclaim the rupee to be at the end of the year. We hope that that unhinging of expectations has come down. As I said, we are watchful for the taper. We think volatility will increase then, but we think we are better positioned to weather that volatility.

Nupur: (Nupur from Dow Jones) One question, on the bad loan report that was put out.

Dr. Raghuram Rajan: Bad loan report, I am happy to answer questions on that.

Nupur: I believe that the numbers which are there on the bad loans are not very trustable. Do you think the report is going to address the issue? And second question is you mentioned about the role of private equity players in the market, but there is not much elaboration in the discussion paper, if you could throw some light on this?

Dr. Raghuram Rajan: The discussion paper is out there for basic comments after which some of the measures will be detailed. In terms of how large the size of the loan problem is and whether we know something significantly more that we are reacting to the answer is, no. I think what you see out there is what we are reacting to. I am saying that the level of NPAs as well as restructured loans is not alarming at this point but it is something that we want to take action quickly before it gets to the point that is alarming. I have also said and I will repeat that a number of these problem assets are good assets which are stressed because of bad repayment schedules as well as delays for a variety of reasons. In the longer run they will produce revenues. And so we need to put them back on track. And so, the sort of sequence of objectives is put the assets back on track, get recovery for the banks, and be fair to entrepreneurs who have taken risks. So in that sequence put the assets back on track, get recovery for the banks and be fair to entrepreneurs who have taken risks. If we can do that quickly the economy is on a much better footing. I think that will help the growth process.

Alpana Killawala: Thank you very much for participating. Thank you very much, Shyma.

Moderator: Thank you. Ladies and gentlemen, on behalf of Reserve Bank of India that concludes this conference call. You may now disconnect your line.