"Edited Transcript of Reserve Bank of India's Conference Call with Researchers and Analysts"

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PARTICIPANTS FROM RBI:

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MODERATOR: **MS. ALPANA KILLAWALA – PRINCIPAL CHIEF GENERAL MANAGER,**

Moderator: Ladies and Gentlemen, Good Day and welcome to the RBI Governor's Conference Call with Researchers and Analysts. As a reminder, all participant lines will be in the listen-only mode**.** 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 '*' then '0' on your touchtone phone**.** Please note that this conference is being recorded**.** I now hand the conference over to Ms. Alpana Killawala. Thank you. And over to you, Ma'am.

Alpana Killawala: Thank you, very much, Inba, and welcome everyone for who have joined this concall at a very short notice. Hopefully, you have all seen the statement made by the Governor this morning and posted at our website. So we will start the questions straightaway.

Moderator: Thank you. Participants, we will now begin with the question-and-answer session**.** The first question is from Abhishek Panda of JP Morgan.

Abhishek Panda:
JP Morgan

Governor, in today's statement you have referred to fiscal consolidation being better than the headline numbers that have been reported in the Budget. Could you provide some more details regarding the same, as to how we could infer the same from the Budget?

Dr. Raghuram G. Rajan: The point I think we were making is that there are a number of expressed intents from the government to clean up the legacy issues of the past and ensure that what you see is what you get on the Budget. The revenue projections are in our view a little more conservative also. And also there are a number of transfers that have been made to the states which may alleviate some of the state financial constraints. So, as we have said, there are a number of intents which could result in a higher quality consolidation process than in the headline numbers and that is one reason for some confidence that was expressed in the statement.

Kumar Rajapudi:
ANZ Bank

Sir, anecdotal evidence actually indicates that the past rate cut has not been passed on where some news reports actually indicating that only 3 out of 45 banks have lowered their base rates. Are you concerned about this and is the RBI trying to take any measures? In fact if you look at the Urjit Patel Committee's recommendations, there was a specific line what said in a rate cut cycle, the transmission best works in an accommodative liquidity stance. So I just want to know your elaborated thoughts on this.

Dr. Raghuram G. Rajan: The liquidity stance has been fairly accommodative. But also I think that what happens is the process of transmission is somewhat asymmetric, that banks tend to be a little faster in raising rates rather than cutting rates. I have no doubt that the pressure of these two rate cuts over time will feed into lower rates. But, we are also examining whether there are any institutional constraints in passing on these rate cuts. We as you know have made changes to the base rate determination policy and we will be examining this very carefully to understand whether it is working as effectively as it should. So my hope is that over the span of the next few weeks, remember, March is typically a time when banks try and hold liquidity. But as we move into the new fiscal year, we will see more transmission into lower interest rates.

Devika Mendiratta:
ANZ

Just wanted to understand that last month's policy statement the inflation statement say that in January 2016, inflation is likely around 6% whereas today you indicated that at below 6%. What has led to that small increased comfort that you seem to have on inflation?

Dr. Michael D. Patra: The Central Statistics Office (CSO) has just posted on its website the granular details on the CPI and their methodological note. Together with this it is stressed that going forward inflation might trend a little lower than the headline that we have today because of methodological improvements and also coverage.

Dr. Raghuram G. Rajan: Also, remember that after our last statement we have had at least one inflation reading, which helped us make this determination.

Raghavan M J:
SBI Life Insurance

We read the documents of the previous policy quite carefully and this kind of a move was definitely factored in post the Budget. But, if I am not wrong, there was a speech which was in the public domain a couple of days ago where there was a mention that the RBI will not be very comfortable doing too many rate cuts based on inflation trajectory and that kind of put the market participants in a different tone of expectations altogether. So, I would want to know what was the intention that you were trying to tell during that particular interview or did we read it wrong?

Dr. Raghuram G. Rajan: Let me answer this first. This comes from paying attention to closed door meetings which should not have been reported outside, I apologize to the wider public, but there were no reporters supposed to be present, this was a direct interaction with students. The context was very clear. I was talking about the fact that internationally central banks especially in developed countries had brought interest rates down to zero and it was very hard for us to follow because we had higher inflation. If you read the statement fully, "we will not be able to cut rates quickly to the bone"- which means down to zero. Nowhere are we talking about cutting rates to that level. So I do not think there was any misleading of the markets, but I apologize. This was a closed door meeting; you should have seen the full context of what was discussed. Then you would have realized that I am not talking about our current inflationary path and our current monetary policy, it is more talking about the general sense in which we could not match the industrial countries. So, unfortunately, when this half-baked newspaper reports come out, it does mislead the market participants. But this was a closed door event with absolutely no reporting supposed to be done and I am afraid that when people violate the rules, these things happen.

Raghavan M J: My second question is though you have an advisory committee where you release the voting of the members within that. For such inter-meeting move, can the market be made aware of if at all there was a voting or what was the majority of votes that wanted a rate cut? And going forward, if the MPC is actually implemented, what would be the conditions? Under that will there be intermeeting cut during that also or is it going to be strictly only during meeting?

Dr. Raghuram G. Rajan: So let us wait for an MPC to be created before we decide when it will meet. The Technical Advisory Committee is an advisory committee and it does give us advice before monetary policy meetings; sometimes through a physical meeting, sometimes through an e-mail discussion. At times when we feel the need to move simply because we have had substantial accumulation of data and for a variety of reasons that I have stated in the policy statement, we do not consult the Technical Advisory Committee, we move on our own at that point.

Parimal Heda:
Bajaj Allianz Life Insurance

When we read today's policy statement, it says that strong rupee is undesirable and on the other side we also see that RBI does not target a level of the exchange rate which creates confusion. Meaning, are we targeting a rupee level which creates a discretionary impulse and we are trying to go the same path like other countries to ensure a competitive depreciation of rupee?

Dr. Raghuram G. Rajan: No, we are not doing that. First, I said, an excessively strong rupee is undesirable which you will agree I am sure with. That is a statement that is very hard for anybody to disagree with. The fact that it is undesirable does not mean that we necessarily will act against that if that situation were to arise because I believe that what we can do is perhaps act against temporary undesirable volatility but it is very hard for us to act in a sustained basis to maintain a value of the rupee. So, we said time and again that our intervention which is typically both sides is to reduce volatility that we think is avoidable but not really to create or maintain a desired value for the rupee. If the rupee attains a value and I am not saying it has that value today, but if it does attain a value which is undesirable, it is not clear. I do not want to say more, that in fact we can do a whole lot against a level if that is what the market in its full wisdom with all the players participating believes is the level.

Astha Gudwani:
Birla Sun Life

Sir, two questions. You suggested that it is appropriate in the inter-meeting policy move should be read as a guidance on how would you implement the Monetary Policy Framework. If you could just explain because the operating procedure of monetary policy under the MPFA is not very clear to the general audience at large. So how do we read the inter-meeting policy as a guidance to that? The second one is since after taking into account the revision of CPI base you have a fresh trajectory of CPI in your mind, basis which you have pre-empted the monetary policy easing as mentioned in the statement today. Going forward, regarding further monetary policy accommodation, is it correct to assess that it will be based on anything which gets more weightage For example, the things that you have mentioned with respect to supply augmentation which should come on surface?

Dr. Michael D. Patra: On how we will implement new monetary policy framework? Remember, that we are moving towards has been described as flexible inflation targeting and this requires a nominal anchor. So the nominal anchors for the years 2015-16 and thereafter have been very clearly set out in this policy statement. The other thing that has been set out is that we will strive for the midpoint of that range and only over a 2-year period that will give us time to ensure a gradual disinflation while minimising the output cost. That I thought is the cornerstone of this new monetary policy framework. On the CPI, essentially, the timing of monetary policy moves will depend on these incoming data which will enable and provide headroom for monetary policy to work in its stated stance. And these are the things we will look forward to.

Venkatesh Sivaraman:
JP Morgan

My question is on the time frame for inflation targeting. Going forward the RBI will seek to bring the inflation rate to the midpoint of the band of 4% (+/-2) by the end of a 2-year period starting fiscal year 2016-17. I want clarity on that 2- year period. Does it mean 2 years after that or including that?

Dr. Raghuram G. Rajan: Two years after January 2016 effectively. So by the end of January 2018, by that time we should have reached the midpoint of the band.

Saurabh Gogri:
ICICI Bank

The question is regarding the liquidity management operations. While you continue to mention that you will continue to provide liquidity of 0.25% through LAF and 0.75% through term repo, we see that the systemic liquidity deficit has come down significantly on account of RBI actions in the Forex market. Could you throw some light on what is the targeted deficit level in the system now or RBI is open to moving system to a surplus mode and keeping the operative rate at the repo rate through variable reverse repo?

Dr. Raghuram G. Rajan: I think the way we think of it is to separate liquidity into two components – one is really what we would call “permanent Liquidity” which is the rate at which we expand the sum of our domestic bonds plus foreign assets. And that we think is more permanent assets that we are buying financed by permanent liquidity provision into the market. We want to grow that at a rate which is consistent with our inflation forecast as well as real growth of the economy. Now, the second element is temporary shortages of liquidity which emerge from things like government payments, government balances, etc., which change over time and seasonal factors, festivals, things like that. And we try and accommodate that through the short-term overnight repos, term repos and so on. So you know that in March there is usually some tightness as banks stop lending to one another, accumulate reserves and so on. And so at such times we tend to provide more short-term liquidity knowing that there will be large reversals at the end of the month. So, that is broadly our strategy. I hope I have answered your question.

Rohit Arora:
Barclays

In today's statement there was a mention that the RBI seeks to bring the CPI rate to the midpoint of 4% at the beginning of FY19. I have two questions on this: One is given the volatile components in the CPI basket, how much government support would this require? And second, what in RBI's view is a sustainable equilibrium nominal and real rate for India's economy?

Dr. Raghuram G. Rajan: I think as far as how much support will be required only time will tell, right? I cannot tell you right now, but I do think you should take comfort from the willingness of the government to go into the inflation targeting framework as a partner in some sense. The way we look at it is we get our orders on the framework from the elected representatives of the people who are represented by the government. So, in that sense, that is our framework. And the government of course has to be supportive in this process and it has been in the past. To your second question, the way we think about this 4% mid-point is really if you look at the industrial countries, they are seeking for the most part a 2% nominal interest rate. And if we say on top of that that we have a 2% productivity advantages as we catch up in growth, then a 4% inflation rate on our side would tend to keep our nominal exchange rate, that is including "Balassa-Samuelson effects" at pretty much a level vis-à-vis industrial countries. So, that is really the thinking behind why 4%, it is also something that previous committees that have gone into this in great detail, for example the Sukhamoy Chakravarty Committee have suggested 4% may be a comfortable level for India to try to reach. But also given that this is a process that is starting, we have somewhat wide bands around it. My belief is as we get more comfortable and I am talking in the 5-years to 10-years scenario these bands could tighten. But for now we think these are appropriate. As far as the level of the real rate goes, I have said repeatedly, at this point in the cycle 1.5-2 real is probably appropriate.

Sudhir Agarwal:
UTI Mutual Fund

I wanted to know the latest fiscal deficit. If you look at the consolidation has been to the extent of just 11 basis points from 4.05 to 3.94. So is it that now the RBI is looking at the quality of the consolidation rather than looking at the quantum of consolidation or is it that the CPI disinflation was so high that RBI has chosen to look at that only?

Dr. Raghuram G. Rajan: The statement that we have issued makes it clear that there is a possibility that the actual fiscal consolidation could be higher than the numbers that you just mentioned. But also, we have emphasised the quality of fiscal consolidation. The emphasis on investment rather than substantially more consumption expenditure. Of course, people will toil through the Budget and look for various aspects of it. Our point is this is a reasonable place for it to meet the conditions we had set in our earlier statement about seeing higher quality fiscal consolidation. But we also emphasise that more work needs to be done as implementation takes place and that work is not just the central government, it is also the state governments because there have been so much devolution to the states. So, this is work in progress and we will be watching the progress.

Prithviraj Dutta:
Edelweiss

In the Union Budget we saw that there was some provision for setting up of public debt management agency. So, my question is what would be its function and how would it be different from the issuance department of the RBI and what would be its objective basically?

Dr. Raghuram G. Rajan: I think this is the question you should ask the government, not us. It is an agency which has been mooted for some time by the FSLRC report. I think the government has expressed intent to bring it about. I think as of now this is just an enabling clause. We have to see what precise form the agency takes. My sense is when it finally emerges it will have a lot of RBI presence and support to avoid reinventing the wheel. But there is still a long time to go before the precise form; there is a task force which is out there, which is formulating the structure of this agency. So I think we are at least a year or two away from more details.

Shubhada Rao:
Yes Bank

There is a report that some regulatory powers over debt markets are being shifted from RBI. Do you have any comments on this? What do you think of the shift of public debt management function from the RBI?

Dr. Raghuram G. Rajan: On public debt management I just said that this is work in progress and will take some time. The notion is this agency will be independent and would not suffer from conflicts of interest. I have said in the past that these issues of conflicts of interest are probably not the most important thing now. But nevertheless, I think that the form that this will take over time we have to wait and see and as I said, there will be substantial RBI support to the eventual structure. On the shifting of regulatory powers over debt markets from the RBI, there are indeed some clauses in the Finance Bill referring to this but the Finance Minister's speech did not contain any reference to this and the Finance Minister's speech generally flags the important actions of the government. I am not worried that this will happen.

Moderator: There is a similar question on a statement of the Finance Minister in his Budget speech. Finance Minister said "Capital Account Controls is a policy, rather than a regulatory, matter. I, therefore, propose to amend, through the Finance Bill, Section-6 of FEMA to clearly provide that control on capital flows as equity will be exercised by the government, in consultation with the RBI. " What do you see RBI's role in foreign exchange in future?

Dr. Raghuram G. Rajan: I think that as the Finance Minister has said this is an area where we talk to each other. So precisely who has the power to issue the final regulation, the consultation does take place and my sense is that it is reasonable to say that equity areas perhaps the government should have the framing rights. But the consultation which happens on these issues between the RBI and the government will continue and I do not think we ever do anything in our regulatory framing without the full consent of the government and I presume that it will be vice versa.

Moderator: There was a question on RBI auctioning of government cash balances. The question is, "Why do you not announce it separately?"

Dr. Raghuram G. Rajan: The issue is we have to examine the concerns of the government in revealing the precise level of the cash balances. There are day-to-day concerns about whether we should make it public wherein this is a subject matter which is being discussed and let us see where we come out. We have tried to give as much transparency on this as possible right now. But if there is a possibility of giving more transparency we will discuss with the government and see how we can do it.

Abhay Modi:
Axis Bank

Direct benefit transfers are expected to reduce subsidies. But do you think that better subsidy targeting may actually have greater impact on aggregate demand and reducing subsidies. The total amount of subsidies has actually not decreased significantly except for the petroleum subsidies. So the amount is going to remain the same more or less and there will be direct benefit transfer. So in the end for the consumer there will be money at their disposal. So that means there will not be equal amount of money is going to be in more hands so aggregate demand will increase. That means there will not be substantial reduction in subsidies but there will be increase in aggregate demand.

Dr. Michael D. Patra: Do you not think with targeting subsidies it would reach the right person not get diffused to many people? And therefore the same amount of subsidy is really the same amount of aggregate demand. And at this time when there is slack in the economy I do not think there will be excess aggregate demand. It will just be a better positioning of aggregate demand in the right hands.

Kaustubh Gupta:
Birla Mutual Fund

Sir, we understand that you are deriving a lot of comfort from the conservative estimates on the revenue projections and the transfer of surplus to states as per the Finance Commission. And that is why as RBI or a country we are choosing to ignore that the fiscal deficit has moved from 3.6% to 3.9% and there is a potential it can improve further. But how on the leverage part of the infrastructure funding which the government is promising that Rs.20,000 crore will be provided as a seed equity and which can potentially maybe leverage somewhere between 5 to 7 times, 10 times. Although it is not reflecting in the main Budget, but in a way government is trying to raise that resources from the market and to fund that money for the infrastructure sector and which in itself is a large fiscal stimulus. So if that kind of a stimulus is coming our way over next 12 to 18 months, so how much RBI is looking to choose to ignore that and if such kind of a stimulus is there, what is the monetary policy stance on that kind of a stimulus?

Dr. Raghuram G. Rajan: I think if you read the policy carefully, we are not in a sense pronouncing from here forever more on the quality of fiscal consolidation. What we have said is this is a good beginning and we are going to be watchful, we are going to wait and watch over time as to how the path takes place. So, in our forward guidance, we have this element of continued high quality fiscal consolidation. We have to watch this path; there maybe positives in certain kinds of infrastructure coming up which may help in helping supply over the medium-term. So, not all additional demand is bad. It maybe supply creating in some sense down the line. But, there are lots of plans, lots of intent as we said and we are going to watch how it rolls out. So I do not want to pick each part of the Budget and say good, bad, ugly, or whatever. As a composite, it is something that we can work with. That is all that we have said in the statement and there are lots of intents expressed in the Budget. Let us see how they play out.

Saket Kapoor:
Kapoor Company

Now the Budget being behind us, how is RBI looking in the direction of "Make in India" campaign that our Prime Minister has endorsed? And how do you think the Budget has enabled more towards that because it was a point of debate whether it is "Make in India" or "Make for India?"

Dr. Raghuram G. Rajan: First, I do not think this is a real debate between "Make in India" and "Make for India." You are making in India, you will make for India and make for the outside world. So I do not think they are one against the other, they both can exist. That is a point that a very few people seem to have understood. In fact, given that exports in a country are always a small fraction of domestic production, you are going to be making for India. So the notion there is the contradiction between these two I simply do not understand. I cannot pick out places in the Budget that for "Make in India". Undoubtedly the entire thrust on medium term reforms are going to be very helpful for making in India. But if you want specific items to be singled out, I think that is a question better posed to the Chief Economic Advisor or the Minister of State, it is not something that we should respond to in great detail. But I have no doubt that the various medium-term measures proposed in this Budget will certainly help the country become more of a power house in the world. So I think this is therefore from that perspective a very good Budget.

Alpana Killawala: That is it from our side. Thank you all very much for joining in. Thank you, Governor.

Moderator: Thank you very much. Ladies and Gentlemen, on behalf of RBI that concludes this conference. Thank you for joining us and you may now disconnect your lines.