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MODERATOR:

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Moderator: Ladies and Gentlemen, Good day and Welcome to the Fourth Bi-Monthly Monetary Policy Governor's Teleconference with Media. As a reminder, all participant lines are in 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 '*' then '0' on your touchtone phone. Please note that this conference is being recorded. I would now like to hand the conference over to Ms. Alpana Killawala. Thank you and over to you, Ma'am.

Alpana Killawala: Thank you very much Karuna. Good morning everybody and welcome to the post-policy conference. The Governor will make a few remarks to begin with and then we move to question and answers. Governor?

Dr. Raghuram G. Rajan: Thank you Alpana. Since our last review the bulk of our conditions for cutting interest rates have been met. The January 2016 target of 6% inflation is likely to be achieved. Therefore the focus should now shift to bringing inflation to around 5% by the end of fiscal 2016-17. With weakening global activities since our last review, commodity prices will remain contained for a while. With low industrial capacity utilization, more domestic demand is needed to substitute the weakening global demand so that the domestic investment cycle picks up.

The coming Pay Commission Report could add substantial fiscal stimulus to domestic demand, but the Government has reaffirmed its desire to respect its fiscal targets and improve the quality of its spending.

Under these circumstances the Reserve Bank intends to be accommodative to the extent possible given its inflation goals while recognising that continuing government policy implementation, structural reforms and corporate actions leading to higher productivity will be the primary impetus for sustainable growth.

Now, we do believe that investments as well as durable goods purchases are likely to respond more strongly if there is more certainty about the extent of monetary stimulus in the pipeline even if transmission is slow. Therefore the Reserve Bank has frontloaded policy action by a reduction in the policy rate by 50 basis points. Given our year ahead projections of inflation, this ensures that one year expected treasury bill real interest rates of about 1.5% to 2% which we think is appropriate for this stage of the recovery.

While the Reserve Bank's stance would continue to be accommodative, the focus of monetary action for the near-term will shift to working with the Government to ensure that impediments to banks passing on the bulk of the cumulative 125 basis points cut in the policy rate are removed. This includes, amongst other things, reviewing small savings rates. The Reserve Bank will continue to be vigilant for signs that monetary policy adjustments are needed to keep the economy on the target disinflationary path.

Now we have laid out a number of other policies today. We have a medium-term framework for foreign portfolio investment in the Government Bonds with a target of allowing FPI ownership of up to 5% by March 2018. We will also open FPI investment in the State Government Bonds with a target of 2% by March 2018. Now altogether this implies incremental space about $25 billion to $30 billion over the next 2.5 years of which $5 billion will open up immediately over the next six months. The intent here is to create more room steadily to slant towards long-term investors and to help develop domestic markets.

We have also open to “Masala Bonds”, I think that is the name they are called by, these are rupee bonds and we intend them to have a minimum maturity of five years; they can be issued abroad or they will be issued abroad. For the moment they will come under the overall corporate FPI limit. We will bring down the ceiling on SLR securities held under HTM from 22% to 21.5% with effect from the fortnight beginning January 9, 2016. Thereafter, the SLR and HTM ceiling will be brought down by 0.25% every quarter till March 31st, 2017.

Now we have announced increased participation by a variety of players in various markets in our ongoing efforts to improve participation and market depth. We will increase the limit for resident entities for hedging their foreign exchange exposures in the OTC market from US$ 250,000 to US$ one million without the production of any underlying documents subject to the submission of a simple declaration. We are also going to examine the possibility of participation by financially sophisticated investors up to certain limits in currency markets without underlying exposure.

Let me conclude these opening remarks. The global environment is looking weak for a variety of reasons. Undoubtedly this is not good news for India because no country is an island. But there is opportunity in even the worse news; we can stand out as a country which still promises strong, sustainable growth. The possibility of realising this opportunity should encourage us to re-double our efforts, to implement our past announcements and to undertake new reforms. The economy has legacy problems to deal with and there are no silver bullets as I have said repeatedly. The Government, other regulators and the RBI are turning around this economy through hard work, through pragmatic policies that are not ideological but based on what works. At the same time if we are to avoid the mistakes of the past, policy goals have to be steady and predictable so that everyone knows where we are going and can make long-term investments accordingly.

I hope these remarks help you understand the policies we have announced today. Thank you.

Alpana Killawala: Thank you Governor. Please announce your name in the mike with the organisation and then ask your question.

Shobhana Subramanian: Financial Express Sir, thank you for your Diwali Gift. But, how much do you think, even you yourself see even if the transmission is slow. You are expecting stimulus to drive the investment. So how much transmission are you looking at? What do you think would be reasonable within the next six months, seven months?

Dr. Raghuram G. Rajan: We are going to be working very hard with the Government on this. So the intent here is to not point fingers at other people but to start moving quickly on ensuring that transmission does take place. Of course there are limits to how fast it can happen, but we believe that some will take place very soon and more will take place over time. We want to create the conditions, some of which will include things like the changes in the calculation of the base rate, some which will include government actions such as reviewing the small savings interest schemes. But the intent is to work together, to move over so that transmission takes place. Now I must say here that some transmission is already taking place through markets, the short-term money markets have come down, the long-term bond markets yields have come down, so that will help, but I think other actions will also be forthcoming in the next few days.

Nisha Poddar: ET Now Governor wanted to understand, you did say that you are going to be accommodative but then transmission is slow, it should pick up. And taking off from her previous question, are the future rate cuts really dependent on the transmission? Are there any expected in this calendar year? And how much of a weightage will your decision making have on the Fed rate hike this particular year. You said that it could be there, and in fact also on the Indian debt market?

Dr. Raghuram G. Rajan: To start with the last, we clearly pay attention to what the Fed is doing as well as other Central Banks because it does affect the economy through foreign investment. So we have to pay some attention to it. But I cannot say it is the central issue that we focus on when we discuss monetary policy, it is one of the many concerns that we look at. Now as far as transmission goes, we want to encourage faster transmission and we will do what is needed. What we need to look at going forward is to see that we have greater comfort on the inflation path; some of it is predicted on positive developments for inflation stemming from the global economy. There are also risks to inflation, we pointed them out before, you know what they are, including the weak monsoon and the effect on the food prices. So all these are things we will examine as time goes on and then take a view, transmission is just one of the factors we will look at.

Latha Venkatesh: CNBC TV18 For FY17 you have forecast a growth of 8% in the last quarter and an inflation of 4.8% in the last quarter. Now that is a bit difficult when you expect growth to pick up by about 60 basis points from the current year and you still expect inflation to fall to 4.8%. So what are the bases of that expectation? Also in terms of transmission, you said you will work with the Government is it only on small savings or else, I mean in the past Governments have worked at arm-twisting the banks to pass on rate cuts. So what do you exactly mean? As well you have kept liquidity a little better in the past one quarter, will that be a policy to ensure that rates are transmitted?

Dr. Raghuram G. Rajan: Let me answer your second question first. I mean transmission, there are various impediments as we said in the policy, including our own regulations which we have to examine to make sure that banks have the ability to transmit given the regulations on things like the base rate. So what we are going to do is work on a variety of dimensions. One thing to remember is if we have lags in transmission, they add to the lags also that even when transmitted monetary policy takes time to work. So we have two sets of lags, lags from policy announcement to transmission and then from transmission to the policy actually working and it could take a long time if we are not more active. Now you should ask the Government what it intends to do, I think they are the best people to speak on it, but from our side we ensure that liquidity is plentifully supplied. We do not want excess and the natural state of this economy with slight deficit in liquidity, which we supply. So the intent is to be there, the intent is to keep rates and the money market close to the policy rate which is 6.75% going forward and the intent is to use all liquidity instruments to supply what is needed. So from our side liquidity, the base rate calculations, those are some of the things we will work on.

Latha Venkatesh: Sir the call rate has been lower than the …?

Dr. Raghuram G. Rajan: For some time because of the excess liquidity but that has reversed post the tax inflows, and we have to manage this process and we are trying to keep the weighted average call rate pretty close to the policy.

Latha Venkatesh: You are confident of 4.8%?

Dr. Raghuram G. Rajan: Let me ask Dr. Patel to speak a little on the factors.

Dr. Urjit R. Patel: The output graph is still negative, so I do not think that this is necessarily a breaking tension between the projection for output at GVA and inflation. Secondly, as we enter a period of persistently lower inflation, the opposite of what was the case for several years prior to the current disinflationary cycle the impact of those on inflation itself will I think for the first time will be felt on the downward side. Thirdly, the global commodity prices are still expected to be soft and therefore that particular beneficial factor is likely to continue even as we grow somewhat faster.

Dr. Raghuram G. Rajan: Especially on the food side, so that is something that is a source of comfort, let us see.

Latha Venkatesh: That means in 2016 you are going to be cutting rates when the Fed would be hiking, so are you okay with that?

Dr. Raghuram G. Rajan: I think we take one policy at a time. So a lot of the projections, of course medium-term projections, a lot can happen in between. A year ago none of you thought we would be even talking about achieving the 6% goal; today we are clearly within good reach of that. So my sense is these are projections, let us wait and see how things pan out. And as we have said in the policy, deviations we will adjust to.

Anupriya Nair:
Bloomberg TV India I want to drive that point forward, what causes disinflation from here on? In the policy itself the Review has viewed that WPI will have to be watched very carefully. So what causes disinflation from here on to 4.8%? It is not global commodity because the seep through is minimal in retail pricing, so what takes it to 4.8% exactly? And the second question is slightly unrelated to the first one, is how much is the worry on power discoms? In your conversations with the Government are power discoms a worry on the financials? Because a large part of the inability of banks to pass on transmission is also the large overhang from power risk exposure on banks. So if you could answer both of them.

Dr. Raghuram G. Rajan: Okay. Let me start first with the power issue. The Government of course is fully cognizant of the problem as are we and we do not intend to kick the can down the road as perhaps has been the unintended consequences of past policies. So we need to take a very careful decision here to put the power distribution companies back on track with healthy capital structures and absorb the debt that has been created over time in the right place with the right sort of interest rates. So that is the intent of what we are working on with the Government, with the States and hopefully we will get a resolution which will help the power distribution companies look ahead. Obviously there will be a lot of contingencies in the final resolution that they will have to meet, the States will have to meet, the Centre will have to be as well as actions for the RBI. Now turning to the other question.

Dr. Urjit R. Patel: It is an extension from the previous question emphasising two more factors, one is that the capacity utilisation continues to be low at around 70%-72% and so that gives us confidence that there is adequate slack to have higher growth and lower inflation. The other factor that is assumed is that the Government's programmed fiscal deficit reduction over the medium-term this year, next year and the year after is on track, so that is also an important assumption on the inflation front.

Dr. Raghuram G. Rajan: I think the biggest risks to inflation which we are watching is on the services side where capacity, it is hard to determine what capacity is in the service side and inflation in areas like healthcare, education have been high over the past few years. Now there are some signs that they are coming down but that is the place we have to be very watchful. Of course in addition to the consequences of the monsoon and whether they are contained. But food management can help a lot in keeping food prices low, where we need more capacity creation is in areas of services where we are possibly running into bottlenecks relating to human capital, availability of teachers, and availability of doctors and so on.

Amol:
Zee Business Sir you have partly answered the question about transmission. If you allow me to ask, out of 75 basis points the banks have reduced 30 basis points. Now out of 125 basis points how much do you think banks are have scope to reduce? Because banks are obviously in the argument of cost of funds, deposit rates. Do you think that we still have to listen to that argument or banks have scope to reduce the rates now?

Dr. Raghuram G. Rajan: When we look at the numbers we find that the reduction on deposit rates has been quite substantial already and therefore if you are not passing it on through lower transmission into lending rates that means it is accumulating at the bank. Now some accumulation will happen because the maturity of the deposits is different from how this translates into lending quickly. But I think overtime they should be able to pass through everything, the question is how much time will that take and whether there are measures that are preventing them from doing it either that we have put in place or the Government has put in place and we are both determined to make changes on those lines.

Neelasri:
Business Standard You have said that the limit for FPI investment in debt securities will henceforth be announced fixed in rupee terms. So what will be the rupee value which will be taken into account for this?

Shri H.R.Khan: What do you mean by rupee value?

Neelasri: How it will be calculated in rupee terms?

Shri H.R.Khan: We have outstanding in rupee terms and Governor has said that our target is 5% at the end of March 2018. So it is simple, there is no question of exchange rate coming into picture.

Neelasri: So the outstanding value will be taken…

Shri H.R.Khan: Yes, outstanding value which is in rupee and 5% is in rupee.

Dr. Raghuram G. Rajan: So you can then extrapolate from where we are and where we are going and approximately that space we will open up. The limits will be announced every six months, the additional limits and over the next six months it is about 5 billion -at current rate- going back to dollars, but spread across SBLs and government securities. You can see the numbers.

Govardhan:
Economic Times Sir you have mentioned in the past that real interest rate would be somewhere around 150 to 200 basis points, that is the repo. Now if you look at the inflation projection and the repo rate it is actually less than 100 basis points. Does that mean that those numbers are no more relevant? And what are the reasons for 50 basis points cut when everyone forecast only 25, why did you go for 50?

Dr. Raghuram G. Rajan: So first on the real interest rate. Over time we have refined that to a one year look ahead, usually one year treasuries are about 25 basis points over the policy rates so the one year look ahead treasury would be about 7%, given policy rate of 6.75%. So 7% and we are saying it would be 150 to 200 which means the inflation would be between 5% and 5.5% one year from now, that is approximately where our projections suggest it will be. So between 5% and 5.5% inflation in one year from now and that is why we have this. Now the second question is what made us do 50? I think the policy is very clear that since our last policy statement the conditions that we had laid out for further accommodation broadly met, except perhaps monsoon we have not seen a good monsoon, but at the same time we have not seen food prices except in vegetables and pulses go up and there is some sense that Government is working to bring some of those down. But we have also seen a dramatic reduction in the external environment including the news on China which has had a tremendous effect on commodity prices including on oil and prospects for these commodity prices going forward. So if you see around the world there is a general sense that global activity is actually going to be further downgraded from what we thought in August. So that gave us a sense that we probably could look for a little more room given that that would also impinge the domestic demand, and as Dr. Patel said the capacity utilisation which really is the first factor which leads to more investment is still very tepid and that would suggest there is room for more domestic demand which will be non-inflationary and then that will eventually create more investment. Ultimately we also need investment to create the supply which holds longer term inflation in check. So we need to restart investment; corporate investment has been weak and investment intentions which is a sign of look ahead what corporations want has not picked up yet. So these are factors which suggested that we could use the maximum room that inflation forecast gave which forecast to the 50 basis points.

Govardhan: So can that also be read as that if the US Fed raises rates that you do not see much of a turmoil in the financial markets?

Dr. Raghuram G. Rajan: I will never predict what financial markets do. I think we should be prepared for anything the financial markets do but repeatedly I have said our best protection against financial market turmoil and surviving financial market turmoil is good policies and good policies that result in sustainable growth ultimately are what will protect us from what is happening in the rest of the world. Now again we want to make sure that the words sustainable and growth go together, both are important and that is why we used what room we had but I do not think we were excessively aggressive. We were not throwing out a Diwali present. But really this was about, given the state of economy, how can we move it forward.

Pradeep Pandya:
CNBC Awaaz First question, you have done a lot of analysis on how much banks have reduced deposit rates and how much transmission has not taken place. Have you also tried to analyse that if we shift from average cost formula to marginal cost formula then how much space will get created because the cut that HDFC Bank just did they said that there has been a difference of 35 basis points by only changing the formula. Will this be correct for the whole sector or do you have some other estimate? And other question was, till now all markets used to look 6% of CPI very closely, after today's policy can we say that that number is 5% now, your goal one year from now?

Shri R. Gandhi: How much room for reduction is based on reduction in the marginal cost- that is very difficult to determine upfront. Different banks have different marginal costs, that is what we have been trying to express to them that they have to work out and come out with their own policies and accordingly bring down the base rate. It will be very difficult because it depends upon each particular bank to position their own deposit structure, and various term structures in which they have acquired the liabilities and accordingly they will have to be repriced. So it will very difficult to determine.

Dr. Raghuram G. Rajan: We have said that we aim to get inflation down to 5% by the end of fiscal 2016-17, that is by March, this was the announcement. We had announced 4% by end of fiscal 2017-18 in April policy of this year, so we are refining that by saying the interim target would be filed by 2016-17 end; that means about 1.5 years to disinflate a little more. Now remember the average for this year is approximately 5% that we have had inflation. So of course we have benefitted from some good external factors, but we have also had a very difficult monsoon. So we have to do a little more to get us to the 5% over the next year. We think it is feasible, after all we came down 2 percentage points over the last year. Going further down becomes more and more difficult overtime but we think 5% is eminently feasible given where we are. Now 1.5 years is a long time, let us see.

Pradeep Pandya: Should it be read as a hawkish statement followed by a dovish policy?

Dr. Raghuram G. Rajan: I do not know what you want to call me, you want to call me a hawk, I do not know, I do not go by these decisions. My name is Raghuram Rajan and I do what I do.

Moderator: Participants on the audio bridge, if you would like to ask a question please start '*' and '1' on your touchtone telephone. We have the first question from the line of Mayur Shetty from Times of India. Please go ahead.

Mayur Shetty: Times of India My question is on the asset quality of banks. Recently you had unveiled new set of measures to address stressed assets giving banks more flexibility to change management and more clout to the joint lenders forum. My question is, were these measures prompted by deterioration in the asset quality situation?

Dr. Raghuram G. Rajan: Well, let me answer very quickly and turn it over to Mr. Mundra. The answer is no, it was examining our existing policies and making sure they are working, and of course policies have to be adjusted continuously to make sure that what you intended is what is actually happening and that was primarily some of the reason for change. But let me ask Mr. Mundra to comment more on it.

Shri S.S. Mundra: Exactly the same, any policy measure cannot be decoupled from the developments in the real economy. So the idea is if there are developments and I think we have been always been maintaining that the whole policy focus is that if there is a genuine problem in the sector the policy measures should be proactive because to sort out those problems but the policy measure should also be used in the right spirit, so there should not be as Governor has been mentioning earlier- no pretending and extending. So I think this is a part of supervisory process as it should be done.

Sandrine Rastello: Bloomberg You mentioned you want some degree of predictability, yet as you probably know, almost nobody expected the 50 basis points today. Going forward actually, most economists expected a prolonged pause. Reading your paragraph 16, has that changed? You still have the accommodative stance, yet you have some conditions. Should we expect some sort of a pause? And a quick question: Since commodity prices have tumbled, we've seen a big problem on the debt market developing with Glencore. Is that something, as a central bank, that you're monitoring for potential or systemic risks for India?

Dr. Raghuram G. Rajan: So note very carefully, we said predictability about goals, of course if you can also introduce predictability about what we do every time that would be a good thing. I think most people expected a rate cut, nobody expected a pause; that was good. Now the extent of the rate cut, to some extent, we were influenced by international development since last time which suggested a much weaker external environment. If you look at our exports, for the first time volumes also were a little weaker this time around, all of which suggests that we have to live in turbulent waters for a little while longer. So that was why the policy was a little different from what people expected. Going forward, I mean again we will try and ensure that people understand what we are trying to do and we make judgments on what we need to do to get there based on all the data before us, as well as some of the actions we can take. So I think I cannot tell you exactly what policy will be every time, but I hope to give you a sense of what it might be as well as once we do it even understanding of why we did it, which is reasonable.

On Glencore itself, I doubt that there is a significant risk stemming from them. Of course which way will it go, typically with large commodity traders having difficulties, I would guess the primary factor would be to depress commodity prices even more. One could argue the other way that given that there are intermediaries in the process it could elevate some commodity prices. Nevertheless I think it is one company amongst many companies that do similar activities and the fact they are in distress does not mean they stop functioning. So I do not think we worry too much about the effects of Glencore.

Shri S. S. Mundra: I will just add to what Governor is mentioning, I think if you do some analysis of the particular instances which you have mentioned, it is more from the ownership of the commodity assets rather than their trading activities, so I think that should be taken into account.

Gabriele:
Wall Street Journal Sir you mentioned last time in your remarks the role played by the Fed decision not to hike rates and one of the arguments for not raising rates this time. Could you tell us a bit more about that and could you also tell us going forward how you view the Fed decision and how that is going to influence your decision?

Dr. Raghuram G. Rajan: I think last time we had said that this was one source of uncertainty which we now know more about, and of course what happened was it continues to remain a source of uncertainty but at least it was not realized over this period. Now different central bankers have different views on this, some would have liked to get it behind us, others say you bought us sometime and it depends to some extent on the degree of preparation as well as the turmoil their markets are undergoing. It is hard to say, I think the markets have taken the Fed decision a little adversely also. But some of them are worried about what this means for what the Fed knows about global activity. So it is not clear that there is any policy that would be without problems for the Fed, they would always get blamed for something or the other. Going forward, I think number of Fed decision makers have said that they would like to do it this year- 2015 which presumably means around December. But clearly I think the single take away from what the Fed has been doing so far is its policy is very contingent on the environment when the policy makers meet and we do not know what that environment will be like in December. So from our perspective we are just continuing to try and make this economy more robust and ensuring strong sustainable growth. I think that is what we can do in this environment, we do not agonise everyday about what the Fed is going to do.

Alpana Killawala: Thanks very much participants and thank you very much Karuna on the audio bridge.

Moderator: Thank you very much Ma'am. Ladies and Gentlemen, with this we conclude today's conference call. Thank you for joining us and you may now disconnect your line.