Edited Transcript of Governor's Post-Policy Press Conference Call with Media

"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 the media. As a reminder, for the duration of the conference, all participants' lines will be in the listen-only mode and there will be an opportunity for you to ask questions at the end of today's presentation. Participants connected to the audio conference bridge may press '*' and '1' to ask a question. Should you need assistance during the conference call, you may signal for an operator by pressing '*' and then '0' on your touchtone phone. Please note that the conference is being recorded. I would now like to hand the conference over to Ms. Alpana Killawala from RBI. Thank you and over to you Ma'am.

Alpana Killawala Welcome to this RBI post-Policy Press Conference. Governor will make an initial short statement and then it will be open for questions and answers. Please announce your names and your organisation's name when you ask a question and please put on the mike. Those who are sitting behind, please wait for the mike to arrive to you. Thank you. Governor please.

Dr. D. Subbarao Thank you very much and once again on my own behalf and on behalf of Reserve Bank welcome to this post-policy press conference not only to those who are present here in this conference room but everyone who is linked on account of this conference. I don't have a prepared statement, but I thought just as a bit of warm up to the Q&A session, I will make a few comments on the policy.

You all know that we have cut the CRR by 25 basis points from 4.5% to 4.25% of NDTL thereby releasing Rs. 175 billion into the liquidity system. We left the repo rate unchanged at 8%; consequently the reverse repo and the MSF rates remain where they were at 7% and 9%, respectively. We scaled down our growth projection from 6.5% to 5.8%. Let me comment on that scaling down of growth projection.

There were several factors that went into it; first the risk from the global economy had increased more than we thought in July. Rainfall deficit was expected to be much higher in July and August, but then it improved thereafter, but food grain production during *Kharif* is going to be about 10% lower than last year. IIP during April-August was practically flat at 0.4% compared to 5.6% during April-August last year. IIP was actually negative in June and July. Investment demand continues to be weak and there is some moderation in consumption spending. And net exports are weakening. So both from sectoral side as well as from demand side, there is weakening of all indicators of growth therefore we had to scale it down from 6.5% to 5.8%. One thing though is that since the first quarter growth was 5.5% and if we were to get 5.8% hopefully, or even higher than our projections of 5.8%, growth has to improve from here on.

We scaled up the inflation projection from 7% to 7.5% for March 2013 and that is again due to a number of factors. First on food, I spoke about that there is going to be a 10% lower production this *Kharif* than last *Kharif*. And even though vegetable prices have come down, prices of cereals which were not a concern earlier, they started going up. Edible oils prices are under pressure, both because of the rainfall distribution as well as global pressures. There is pressure on edible oil price from the global side.

Suppressed inflation: it is necessary and important that the government correct the suppressed inflation in diesel and in electricity. As per the numbers my staff gave me, the full impact of inflation due to electricity price revision will be 60 basis points both first round and second round of which we saw 34 basis points already until September. On diesel, the full inflation impact –both, first round and second round will be 110 basis points, of which we saw 40 in September. So the suppressed inflation coming out is the second factor for pressure on inflation. Then there is commodity prices, we saw inflation in industrial raw materials going up and input costs have gone up because of being firm in the global markets as well as the rupee depreciation. Just for the record, rupee depreciated by 7.8% in nominal terms this fiscal year and by 5.4% in real terms this fiscal year, so the depreciation in nominal terms has been higher than in real terms.

And then there is wage pressure coming from rural and urban wages, which have gone up and we noted that before, and even though there has been a little moderation, rural wages are still under pressure, so are urban wages.

So we scaled down growth projection from 6.5% to 5.8%, scaled up inflation projection from 7% to 7.5%, nominal growth remains approximately the same; 13.5% earlier, 13.3% now.

Now, we also gave guidance for the future which is that we have taken the CRR action to preempt our prospective tightening of liquidity conditions so as to keep liquidity comfortable and support growth. We anticipate that inflation will go up over the next few months before turning down in the fourth quarter of this fiscal year. There are of course risks to that trajectory which will have to be looking out for, we have to be alert, but assuming that inflation pans out as we had projected there is scope for inflation easing in the fourth quarter of this year.

As per standard practice, let me anticipate one question and answer that up front and I am going to take on more challenging questions than usual, sticking my neck out as it were, which is, why did we cut the CRR and not the repo rate? We have given the rationale in the policy document. I also gave that in my statement at the conference with the bankers this morning, but I just thought I will repeat that in my own words once again to you people who are very discerning and very incisive analysts. We have to balance growth and inflation dynamics, it has been a complex challenge. We have to restrain demand even as ensuring flow of credit to productive sectors so that supply constraints are eased. We all know that market interest rates are determined by two variables; the level of policy interest rate and liquidity conditions. We were very conscious of the fact that our rate cut will not help if liquidity is tight. Conversely, even if we have comfortable liquidity it will not help if rates are high. So we carefully calibrate both the repo rate and the CRR.

Looking at the current balance between growth and inflation risks, we thought it is appropriate to maintain the policy rate where it is, just a little bit above the inflation rate, also considering that inflation is going to go up over the next few months. On the other hand, liquidity has tightened for three important reasons; first, because of the wedge between deposit and credit growth; second, the build-up in government's cash balances; and third, the festival demand.

We expect that these factors of tightening liquidity will continue to play out over the next few weeks or few months.

Given that the risks to growth have increased, we do not want tight liquidity to push interest rates higher than they would be. So this CRR cut is expected it to ensure that the demand for credit at the current policy rate, at the current interest rate structure, is fully met and thereby help ease the supply constraints, help increase capacity utilisation, which will be non-inflationary. So this CRR cut is aimed at maintaining liquidity deficit which supports our policy rate projection, but a deficit which is small enough not to restrict credit flow.

Finally, we had the meeting with bankers this morning and you spoke to the bankers just before this. We talked about the policy stance and about transmission and about demand for credit. There was not a unanimous view, but large majority of them thought that the binding constraint to investment now is not the interest rate but there are other factors at play. Of course, interest rate is a factor, but that is not a binding constraint at the moment.

There were two other issues that we discussed at length. One is the state of the SME sector in the country. The concern was that all of us here, the bank chairmen as well as the Reserve Bank, whether the problems and the stress of the SME sector is sufficiently on our radar screen and we want to acknowledge that that is a big sector contributing to our economic growth and that at a time like this we should be focusing on that. It is not just about restructuring the SME sector wherever they are in trouble, it is the whole gamut of issues about timely credit, adequate credit, monitoring and nurturing them, giving additional support wherever there might be need and most importantly, doing everything in time, so that the distress is not exacerbated. SME sector is an important lobby, it is not as articulate as the other lobby and we need to pay special attention to that, especially because it is employment intensive and dispersed across the country.

So what did we decide? We decided that we will give banks a month’s time to study the SME sector financing of their own bank by consulting their own hierarchy, especially frontline managers and that both Chakrabarty and Anand Sinha will have a meeting towards the end of November or early December with bank chairmen to see what can be done to improve flow of credit to the SME sector.

We have spent a much longer time discussing the NPA. There is nothing new I can tell you, but we did share each other’s understanding and our concerns.

Two or three messages we have got from that meeting, the first is the level of NPAs and the rate of deterioration is disturbing; it is not alarming, but it is certainly disturbing. This is due to the downturn in the economy, but also due to a number of other factors. What I have been given to understand is that if banks manage their credit portfolio better, more effectively, they can manage the NPAs much better, particularly about credit appraisal, about monitoring, about detecting incipient signs of sickness, etc.

There was a question that some of you raised about restructured assets. We have taken a decision in this morning's policy raising the provisioning for restructured standard assets from 2.0% to 2.75%, that is an interim measure pending full discussion and dissemination of the Mahapatra Committee which all of you have seen. That is all I have to say. Thank you very much.

Latha Sir, Latha from CNBC TV18. One of the rosier parts of your statement, is that promise for a policy easing in the fourth quarter. To quote your own line, "the baseline scenario suggests a reasonable likelihood of further policy easing in the fourth quarter of 2012-13. The above policy guidance will, however, be conditioned by the evolving growth-inflation dynamic". Now you meet on January 29th, you will only have the December data at that time. Do you expect that inflation will give you signs of peaking off by then already or when you say fourth quarter do you mean maybe March or the April quarter?

Dr. D. Subbarao By fourth quarter, I mean the quarter starting January which runs until 31st March. We have inflation projections for the next few months until March and indeed into 2013-14, but these inflation projections by their very nature are quite I would say approximate. So I cannot precisely say where inflation will .peak, when the inflection point will be, but a little beyond January. So at this time, I cannot give guidance about what will happen in January, what will happen in March. But if we see that the inflation is likely to be coming down even in the January-March quarter, we might take some action in January, but I really cannot say anything beyond that.

Latha The data that economists are now giving us indicate that inflation will be well above 8% definitely up until December, which is the last data you will have on January 29th. I was just wondering what in terms of the level, what is the highest you see and approximately in terms of time when do you see it peaking off?

Dr. D. Subbarao It could go beyond 8%, not well beyond 8%. As I said, it is difficult to put a precise time point on that. It could happen after January, but we expect that because of the base effect, because of a number of other constraints easing, inflation will come down thereafter. But the link from the inflation trajectory and inflation numbers to policy, we will have to decide not just on inflation numbers but on growth as well and on the other indicators such as including the growth number for the second quarter.

Dr. Subir Gokarn I would refer to the chart on Page 9 of the policy which suggests the inflation peaking in December. If that trajectory plays out as we have projected here, then the downward movement after that is something that will become little more let us say clear.

Latha We will know about it only after February.

Dr. Subir Gokarn We are looking at our projections, which is in a sense why we have also indicated that we believe inflation rates will go up. That was in a sense one factor in our decision not to cut the repo this time.

Dr. D. Subbarao Are there any more questions on the rosier part of the statement?

Ira Governor, Ira from NDTV. Just taking that a bit further, while explaining the CRR *versus* repo trade-off you were just talking about the fact that policy rates are just marginally higher than the current inflation rates. If you look at where inflation is expected to go, 7.5% to where you are projecting it by March, the professional forecast which was included in yesterday's document talks about 7% plus inflation until the second quarter of next year. Should we then believe that the room for policy rate action, while it may open up a bit, is still relatively limited even well into next year?

Dr. D. Subbarao I would think that would be a reasonable surmise given that inflation is going to come down, but now it is going to remain relatively high. The scope for policy action is also limited, but also I want to caution you that we look at inflation but we also look at the growth numbers. So don't be guided only by the inflation numbers.

Ira A follow-up question, because you mentioned growth. The Finance Minister in his reaction said that growth is as much of a challenge as inflation and if the government has to walk alone to face the challenge of growth, then we will walk alone. Is there a bit of disconnect of how the government is seeing the economy, where they perceive growth is a bigger challenge and the Reserve Bank is perceiving inflation as a bigger challenge?

Dr. D. Subbarao I think both the government and the Reserve Bank share concerns both about growth and inflation. We are as much concerned about growth as inflation, only our balance has been shifting. If you are asking about the nuances of the Finance Minister's statement, I think you should ask him.

Anirudh Anirudh here from ET Now. I just like to keep it with the inflation again. Like you have mentioned, the inflation numbers are expected to move up again in the next quarter and really going forward it could ease somewhere. Whether again, given the kind of projections we have seen from forecasters and multiple other agencies, there does seem to be a growing feeling that inflation at around 6 or 7% region could be the new normal going forward. Could you comment on this, given the fact that you are maintaining your medium-term inflation projection at 3% to 4%?

Dr. D. Subbarao Yes, I still stand by that standard paragraph that we have in our document. It is true that over that last two- three years inflation has been high and it is true that inflation is going to be high in 2013-14, but into the medium-term I believe that it is possible that we can still bring it down to 5% and even below that, so as to be at par with the global inflation levels. And for inflation to come down to that level, we need to ease the supply constraints and that I hope will happen over the next couple of years. So I do not think we should settle for a higher inflation as the new normal. We should still come down to 5% and below.

Ritesh Ritesh here from Zee Business. Three questions; firstly, on the NPA and the restructuring front, on an earlier occasion, most of the RBI executives have said that the NPA is a concern but it is not sending an alarming signal. So today you have taken several steps as far NPA is concerned. So should we read between the lines, that now the level has reached for NPAs where RBI is getting figures to be concerned going forward. Second question on the credit information reports which you have mentioned on Page No. 23, Para. 98. You said that banks are not actually accessing the credit reports to the extent where they are sanctioning the loans or they are considering the loans. What is the concern that RBI is getting at this point in time as far as credit information reports? Because, on earlier occasions also RBI executives have said that the credit information reports have not been used for the larger loans of mid-corporate and large corporate loans. And third question, on the RBI banking licenses front, what is the position right now because we are getting mixed signals from the government that RBI will issue banking licenses. What is the status right now?

Dr. D. Subbarao I think RBI has maintained a consistent stand on NPAs that it has moved up both in absolute and in proportional terms. I believe between March 2012 and June 2012, they have gone up from 2.9 to 3.25%, which is a rather steep increase and they are likely to go up further. So it is important that both banks, and the Reserve Bank as the regulator and supervisor is abreast and taking action on this. Now, it has been a concern, it is a concern, concern is the precise word we use as that depends on the limitations of our English. All I want to say is that it is not an alarming thing. Our banks are resilient, they can withstand NPAs of this level, but that does not mean that we remain complacent, we need to take action on this. There are a number of things, the downturn in the economy as I said earlier is one factor and as long as the economy doesn’t pick up, it is difficult for NPAs really to come down, but there are other things that banks can do.

Now on banking licenses, you all know what the current status is, which is that an amendment to the Banking Regulation Act is pending for giving us the necessary authority, power, and dispensation to deal with corporates entering the banking sector; that is where it stands. I have seen some media reports about whether something can be done to give the RBI those powers even before or even without the amendment being carried out, but we are yet to receive any formal communication about that. On your second question about credit information reports, I will turn to Anand.

Shri Anand Sinha In any credit decision making, it is important that the entire exposure of a corporate or any borrower is available to the sanctioning bank. In particular, when we have moved away from the compulsory concessional lending about a certain amount and gone into multiple banking, it gives the borrowers a larger leeway, it is very important that information is available while making a decision. Now one of the mechanisms is credit information bureau. So today we have four credit information bureaus and what we have said is that we want to strengthen that mechanism so that it is for the purpose for which it has been created, that is, supplying timely and accurate data and also making use of that while taking decisions because if proper information is not factored in it will lead to obviously an inadequate decision and NPA.

Participant Just a follow-up on the banking license, when Mr. Chidambaram was in Mumbai earlier in the first week of this month, he had actually categorically said in a press conference that he has spoken to you as far as banking licenses goes and what signals he has given to you? The discussion between RBI and Government of India is that RBI can start the process while the

Banking Amendment Act can be passed in the winter session. So what kind of signals have you received from the government as far as banking licenses is concerned?

Dr. D. Subbarao We have not received any signals. It is true that the Finance Minister spoke to us when he visited us and that was on the agenda and he asked us whether it can be done without amending the Banking Regulation Act. We could not offer an informed response to that question because we believe that we need these powers to move forward. Then the Finance Minister asked whether something can be done by way of giving those powers and the authority to the Reserve Bank even before amending the Act, and then he said he will go back and study that.

Participant Just a follow-up on that, I think what was reported was that they would just bring in the powers to supersede the bank board maybe even without the amendment. I was just wondering, if that is done, in effect, I do not know how it will be done, probably if that is taken care of, does that give comfort to the RBI or is there more within that amendment?

Dr. D. Subbarao I am not in a position to offer a comment on that because there are two or three things that we wanted authorisation for, to supersede the board; to authorise acquisition of shares beyond 5% power to consolidate its supervison, so all those things are necessary, but whether we can move forward with only one issued being dispensed is something that I cannot comment on at this time.

Participant It was also mentioned in the report, may be all these requirements are only for providing a license to a corporate, and NBFC who want to convert to a bank, for them you may not require the amendment, if that is the case, if that is the position that RBI holds?

Dr. D. Subbarao No, RBI does not hold that position. Our position is that it is best to open up the process for all potential applicants at the same time.

Participant Just to complete that question which was asked on credit sharing, it is a genuine concern. After all there is lots of lending in multiple banks here, you don't have that kind of information. Are you contemplating putting in some institutional mechanism to share or you are expecting CIBIL or to some extend their data base, what is the process from here to there, to ensure the information is shared?

Shri Anand Sinha If you see the document, you will find that we have taken up both; one is strengthening credit information bureau. But maybe, three years back perhaps, when credit information bureaus- all the four were not there or were in the process; obviously the stage was much earlier than what it is today. We were concerned about sharing of information at that time also equally and we had prescribed a set of format for bankers to share information among themselves. The idea is that it should be done while credit information bureau gets strengthened. Ultimately full information should be available by whichever mechanism. So that format or template was designed three years back or something like that, but somehow it did not take off. So what we are now saying is that you must do it, and of course also strengthen the credit information bureau mechanism.

Shobhana Shobhana from Financial Express. There has been some amount of transmission ever since you started cutting the CRR. Now do you think that banks have scope to cut loan rates further? Or this time around because the provisioning requirements have gone up, some banks will be constrained by that and also the fact that the costs are going up such as that they will not be in a position to really cut the deposit rate. How much scope do you see there for banks to be able to cut rates to stimulate demand?

Dr. D. Subbarao You had given the answer yourself. You have indicated the constraints the banks will face both in terms of mobilising deposits and in terms of the additional provisioning they have to make. But we believe that there is scope given the more comfortable liquidity that we will now provide, even at the current repo rate and the current base rate; at the current repo rate to adjust the lending rates for lending to productive sectors of the economy to ease the supply constraints.

Participant Governor, I have a follow-up question to that. In the year 2012 we have seen a slew of measures from Reserve Bank in regard to bankers. You have the CRR cut 175 basis points and had an SLR cut. Even if you look at short-term lending rate, you have brought down the CP/CD rates around 100, 120 basis points. But we have not seeing a transmission of that. We are looking on most of the banks on an average cutting lending rates by around 25 to at the max 50 basis points in the entire of this year. So we are not seeing too much of a pass-through. Where do you see the problem?

Dr. D. Subbarao We have indicated the transmission in the document. Have we not?

Dr. Subir Gokarn She is referring to the base rate changes that we have reported.

Participant That indicates 25 basis points despite all the changes that have happened.

Dr. Subir Gokarn I think there are two ways to look at liquidity. One is its impact on rates directly. The other is its impact on comfort which is when banks face tight liquidity situation which is based on feedback and discussion we have had with banks over the last couple of years, they tend to hold back on credit because it makes us the management of the liquidity requirements more difficult. So, to some extent rates have gone down. This follows of course also the 50 basis points reduction in April. To some extent we are seeing and this is an agenda that Mr. Sinha's Committee is looking into, which is the balance between spreads and base rates. Base rates are transparent and visible and spreads are not until we actually look at the post-facto data. The post-facto data suggests that weighted average lending rates have actually come down. The transmission is little more visible there than it is on base rate. I think more importantly from liquidity perspective the message we keep sending is to ensure that flow of credit to productive activities remain and that is really where the constraint comes in when liquidity situation turns tight. So it is an attempt to address that aspect of bank lending also.

Participant I also have another follow-up question on the restructuring loan front. On an overall basis, in the few numbers that have started trickling in from Q2, restructured loans along with gross NPAs have gone up substantially in Q2. What is the concern for the Reserve Bank of India? I know that you have gone ahead and increased the provisioning, but are there any other measures for recognising a restructured loan, that we could see any kind of norms getting tweaked over there for how really you recognise a restructured loan, how do you define a viable loan that can be restructured? And also there has been a significant amount of divergence between the private banks and the public banks. What is the reason for the divergence? I mean are public sector banks doing something wrong which the private sector banks are not?

Dr. K.C. Chakrabarty So far as NPA restructuring, we should understand we cannot blame the banks for the NPA alone. People borrow money from the bank, they do not pay or they are not able to pay, that is why it becomes NPA. Now, this is an issue, a systemic issue and it has to be tackled accordingly. But within that what we are trying to say that if it is due to systemic downturn, it would have been across all bank groups, but this is not happening and that is what Governor is indicating. Yes, we admit that there is a downturn, there is a stress on the people but within that the probability of adverse selection is not the same across all the bank groups and that is why banks need to look into those aspects also. What we are saying, that is, what we are sensitizing the bank, that you need to look into this aspect and to that extent mitigate risks. Other things are okay, if there is NPA in the system, if the growth comes down in the system, people are not paying, banks have to absorb the shock. Then what as the regulator we can do? We can only improve the capacity of the banks to absorb that. And that is why is the provisioning requirements will go up. Now, this cannot be done at one stroke, it has to be done in a phased manner, and that is what we are trying to do that. But what Governor is saying let us not be alarming, what we are saying, at present banks have enough capital and they will be able to absorb the shock, but this cannot go indefinitely.

Gopika Gopika from CNBC. Mahapatra Committee has recommended 3.5% as first phase of the increased provision. You get to the 2.75%. So could we expect that other 75 basis points coming probably in the next year?

Shri Anand Sinha The logic for 0.75 instead of 1.5 is that 1.5 they would have absorbed over a year, since half of the year is gone therefore we have kept it at 0.75. We have also said that we will take all decisions on Mahapatra Committee recommendations by end January when we will come up with the draft guidelines. So you will find our final view over there but there is no denying the fact that with NPA rising, provisioning has to be strengthened.

Participant A follow-up on NPA. Over the last three, four days markets have kind of panicked looking at the NPA numbers that have come out and then there is a new guidance on provisioning that came in today. My question is when we spoke to a number of bank chairmen, they are not really in a position to give us a clear guidance whether the worst is already behind us or the next quarter would be even bad in terms of NPAs. What is your assessment of the situation? Where do we really stand?

Dr. D. Subbarao You asked the banks, we asked the banks too and we got the same reply and I appreciate that. I have sympathy for what they said which is that one of the factors that is influencing NPA is the economic situation, on which nobody has a very definitive view how it will turn out. So that is what they said, which is that if the economy starts improving from here on we will see a reversal of the NPA situation as well. But if the economic sluggishness continues, the NPA problem will also persist. The reason they have not been able to give a definitive projection for the period forward is because of the uncertainty about the economic situation. Factors which are controllable, which are within the control, of course, they will take action and improvement that will come on the account will show in the numbers.

Shri Anand Sinha I would like to clarify one aspect regarding restructured accounts. This we have done earlier but I want you to appreciate it because a lot of panic has been spread than what actually is the situation. In the case of restructuring, the figures that you are seeing is the cumulative figure, that means every account which was restructured even four years back, today it is still called as 'restructured account.' Now, we have a rule whereby the restructured standard accounts have additional provision requirement. That is instead of 0.42% and in some cases higher capital requirement. This is withdrawn once they complete two years. So after two years they are no longer restructured assets. Now that kind of distinction is not yet available to us but we are going to take it into operation from 31st March, 2013, balance sheet. So the restructured account figure should be discounted by this factor. One of the bank's chairmen told us that in his case it will be 45%. So we will be collecting figures from all the banks and see where it is. But I want you to take note of this fact that the restructured account figure which you are seeing needs to be discounted by those which need not be considered any more restructured.

Participant Governor, one question on the steps which you have taken about advances against gold. If you can just explain us the rationale behind that and what is the signal which you have found in this particular segment, what kind of advances, how banks have been giving to the companies or the retail individual for the advances against loans? And secondly, on the currency chests, because this was the question- that you have mentioned clearly in your policy document that 90% of the currency chests are available with the public sector banks, but they have not been reporting. So what do you think is the problem there? Why it is happening?

Dr. D. Subbarao On gold loans, what we have said is that banks should not give loans for purchase of gold. That has I believe been in force since 1970s. So over time this has been lost track of, so we reiterated what is already a standing instruction, which is that banks should not finance gold except for jewelers for working capital. That is what you will find in the document.

Dr. K.C. Chakrabarty Yes, 90% currency chests are in the public sector banks and that is the problem. If somebody goes with a counterfeit note and presents to the counter and if the counter person identifies it is a counterfeit note - today, the law says FIR is to be lodged and that particular note is to be seized and customer loses the money. We understand what is the practical situation the banks face. The fellow says you return my note. Now he returns. In the process it goes, he pushes the note somewhere. What we are saying that these detection part should take through the machine. Even if need be we are ready to absorb that, look into that and create a system and we have also improved the reporting mechanism, we have taken up the issue with the Home Ministry and we say that up to four notes if somebody is seeing a counterfeit, no individual FIR is necessary. So why it is more in the private sector bank because their counter clerk does not identify a counterfeit note. It is processed through the machine and that is to be identified.

And then what happens? Either they absorb the risk or they have to contact the customer to look into it. That is what we are saying to the public sector banks so that we know what is the extent of counterfeit note. And that is the new system we are trying to implement but because you see, it is a change in the system and what we have instructed banks that all notes of Rs. 100, 500, 1000, it cannot go for recirculation unless it is processed in the machine. Now this is taking a little bit of time and that is the thing but the necessary background work for implementing the system has been done, including the reporting mechanism, it was a hassle because the Ministry of Home Affairs, they must issue the guidelines, it is all the state governments have to accept that particular procedure which took a little bit time everywhere, where we have gone for the meeting in the state level, Governor requested the concerned Chief Secretary, this is in the plan, but it will take some time. And the other thing is the problem is there and which we are admitting. We are saying we understand the problem and we need to address the issue.

Moderator Thank you. We have a question from the line of Poonam Saney from Times Group. Please go ahead.

Poonam Saney My question is that what is your assessment of inflation? Is this more demand pull or cost push? And if it is more of cost push inflation then does using monetary policy to arrest cost push inflation really help?

Dr. D. Subbarao In our assessment both cost push and demand pull factors are there and the cost push factors as you know are coming from food and some commodity prices including rupee depreciation. There are of course demand pressures, they have moderated somewhat but they still persist and then there is the pressure coming from rural and urban wages. So in our assessment inflation is due to both cost push and demand pull, although the demand pull factors have declined in importance in the last few months. Also, you must remember that inflation no matter what the driver, if it persists for a long time it drives up inflationary expectations for which monetary policy is responsible, so therefore we believe that there is both, need and an obligation that the Reserve Bank to be acting on the inflation front.

Vijay Vijay from Newswire Agency. A simple question. You have taken so many steps on the liquidity side saying that there needs to adequate liquidity in the system, but we can see from the banks' balance sheet, there has been increase in SLR holdings of most banks. So in that sense do you see that bank will do any transmission without policy rate cut from the RBI? And just another question not connected to the policy, but various private sector banks that have higher promoter holding and there was earlier recommendation concerning December 2012, but different banks have been given different timelines and if could there be some more clarity on that would be helpful?

Dr. D. Subbarao Different timelines for?

Participant Different banks were given more time and everything.

Dr. D. Subbarao For what purpose?

Participant For the promoter holding.

Dr. D. Subbarao First, on liquidity, you are right that banks are holding little more SLR than they are required to for liquidity management purposes. But we believe that given the CRR cut that we did today, which we thought was important because of the impending liquidity constraints that we see and because of the persistence of the liquidity constraints, it provides conditions for better transmission of the policy repo rate to the base rate and then the lending rate. So the answer to your question is yes, this CRR cut will provide liquidity which will improve the transmission of the policy rate to the lending rate. So I believe that there is a scope for further reduction by banks of lending rates, especially to sectors which will ease off the constraints in the economy.

Shri Anand Sinha As far as promoters are concerned, they all have to come down to 10% that you know but it is very difficult to have a rule of thumb or a mechanical rule. It depends on several factors, on how much they have to dilute, what is the market capitalization. So we look at it on case-to-case basis, we maintain the pressure and today I do not think there is any single bank which hasn't given us a program. But I must also say that the programs are not always adhered to in totality for various reasons. We have other methods. If we find that it is getting too much delayed we put pressure through different means, for example, maybe branch expansion or some such thing but everybody has to come down to that level and today everybody has given us a plan.

Participant What is the level that they have to have to come down to?

Shri Anand Sinha 10%. Mahapatra, every bank has given a plan?

Shri B. Mahapatra Yes, Sir.

Virender Singh Virender Singh from TV Today Network. My colleague from NDTV read the statement of Finance Minister soon after the policy. He also said sometimes he chooses to talk, sometimes he remains silent. This is the time to remain silent. My question is did RBI want the Finance Minister to remain silent and let RBI do the job? Second, you said that the recent policy announcement by the government which has positively impacted sentiment, need to be transmitted into effective actions to convert sentiments into concrete investment decision. What it is the real worry? Is it investment not coming in the country or is still the fiscal issue, the fiscal deficit or current account deficit, despite Finance Minister giving a roadmap of fiscal consolidation plan yesterday in one of those conferences.

Dr. D. Subbarao For the first question, the government is an important stakeholder in the Reserve Bank’s policy. So we understand that the Finance Minister has a position, he represents the government and we have respect for what the Finance Minister says. He says sometimes he talks and sometimes he chooses to keep silent, that is his privilege but to the extent that he communicates with us both in private and in public, we have a great regard for what the Finance Minister says. Then about policy announcements being translated into action, it is particular to mention on the fiscal, on investment, both domestic concerns; fiscal of course as the Finance Minister has said they have taken very critical and politically difficult decisions on this, on fuel price adjustment on multi-brand retail etc. But let me stay with fiscal, on the issue of price adjustment. Yesterday in his statement he also gave a roadmap for fiscal adjustment in the short-term and in the medium-term. He gave the broad contours of that roadmap. Beyond that how this will evolve is a question that Finance Minister will manage and it will also depend on a number of other factors. Having been in the government I want to say that I acknowledge the challenges of the government, especially of the Finance Minister, especially in a democratic structure like ours. So what everybody, including the Reserve Bank is looking for is a little more detail on how this fiscal roadmap will be implemented in the short-term and in the medium-term. Then on investment, we all know that the cabinet has taken decision on insurance, on pension, etc., foreign investment, raising investment limits there. But those have to be approved by the Parliament. So much will depend on when they are approved and to what extent they are approved. That is the concern that has been in the public, that is the concern we have indicated in our policy document.

Sarvesh Sir, Sarvesh Tiwari from Zee News. Sir, my problem is relating to currency if you can answer that. It is a very serious matter as all of you know and if we talk about some facts, around 1600 crore of counterfeit currency has been seized, recently. Let's take the Mumbai City, different crime branches have seized counterfeit notes of Rs. 8 lakhs in two different places. Few days back guidelines were issued by the RBI to all the banks that they are using some special paper, which paper they are using? Where has the matter reached and what are the plans to stop this fake currency?

Dr. K.C. Chakrabarty In all countries of the world there is fake currency, in our country also it is there. We cannot stop is completely but how to minimize it, we should try for that. To minimize this, first thing is very important that we should be aware that how much fake currency is in circulation. Just a minute ago I answered today that that information is not available as well. So if you ask me how much serious this is, the thing is that we don’t have proper information about it. So we want to gather all the information about it. And then our problem is different. Someone else is making it. We are improving our security features continuously and we are giving training to people. Detecting fake notes and the people who are doing it, to catch hold of them is not Reserve Bank’s job, it is a law and order situation. So we coordinate with them, we talk with them all the time. After doing so much whatever available data, according to that in 10 lakhs, only 8 notes are only fake. This is according to international standard, it is not very bad. But as we cannot be very sure how much information we have, we are trying to gather that information and we require support of all other agencies like law enforcement agency, public, media. See whatever notes Reserve Bank makes they are all genuine notes. Someone else is making the fake note. How to catch the people who make these notes we have to think about it and that people don’t use it, we only want to say that. It is present in all the countries and it will not go away completely. And the new security features like plastic etc., these are all in our plan but it will take some time. It will not be completed in one year or two years. Whole process is very lengthy but we are determined about it and we are working towards that, I want to tell that much only. And it is not as big an issue as you are saying; whatever available data is there based on that information I can tell you. But the problem is there we cannot deny that there is no problem.

Sarvesh Whenever a customer goes to the bank with such notes and I have interviewed directors of two banks, they are saying that if fake currency is detected, whether it is Rs. 1000 or 500, it has to be paid by the employee of their bank.

Dr. K.C. Chakrabarty This is the regulation of the bank. See when the fake currency is detected, and then its value becomes zero. Whoever gets this note, its value becomes zero. If you have got one currency of Rs.1000 it is as good as paper. So whoever will have this, he has to pay for that. If the employee of the bank does not recognize the fake currency, he has to pay for it, it is the internal rule of the bank. We are trying to change this rule. I have already told this, we want this to be detected through machine. In this, whether employee pays or bank pays or Reserve Bank pays, one thing we should understand that through that fake currency whatever loss is to be done to the country it has already been done. So who will pay for this we can decide amongst us afterwards. But for bank, it is a rule otherwise the person who could not detect on the counter, if it is found from them then they have to pay for that. We are trying to change a bit and I already told you that we are talking with the banks that we should take this detection in machine. For the law we are not that much worried, but how to detect this is the most worrisome matter for us.

Participant Chakrabarty Sahib I will ask you one more question, one reason being given is that the employees have to pay money out of their pocket so perhaps they report only 10% to the government.

Dr. K.C. Chakrabarty No, it is not like that. Customer fights with them saying, it is not fake, you just give me back. The rule is that if it gets detected then they should keep the note with them. But the customer fights for that. So the staff of the branch they don't want to fight with them, so they give it back to the customer that is why it is not getting reported. If he would detect then it will not harm the officer. If officer does not detect and if it is getting detected in the next phase then it harms the officer.

Ruchira This is Ruchira from the Economic Times. My question is will the CRR cut be enough to manage liquidity tightening in the near-term or can the RBI resort to OMOs in the near future. Is there a scope for OMOs in the near future?

Dr. D. Subbarao We believe that this liquidity infusion that we have done through the CRR will see us through the next few weeks, but should it be necessary to manage liquidity through OMO we will do that. I cannot at this time say that there will be OMOs or there will be no OMOs but OMOs have always been on the table. But we believe that with what we have done, it should see the liquidity situation being comfortable over the next few weeks if not the next few months.

Parnika Just a follow-up here. Parnika from Business Standard. Did you see the government overshooting market borrowings plan this year because you said that there could be likelihood of fiscal slippage.

Dr. D. Subbarao We all heard the Finance Minister yesterday in his statement that it will be 5.3% to GDP. Also, that there will be no additional borrowing this year. That is the statement we are going by at this moment.

Anup Anup from Bloomberg News. What is the status on allowing Shariah bonds? Will that meet the nature of amendment to the Banking Act and how soon will the RBI introduce it in India?

Dr. D. Subbarao This question of Shariah bonds or the larger insurance Islamic banking has been asked to us for several years now. The Reserve Bank's position has been that the current Banking Regulation Act does not permit Islamic banking because interest rate is an important component of banking in India. If a bank operates it costs to LAF operations with the Reserve Bank which involves taking and giving of interest. Also, we do not permit banks to take risk positions in business if they finance. They must only get the return by way of interest whereas Islamic banking requires that banks take a position on the risk of the business. Also, there is regulation by the Shariah Board, they cannot do a regulation. There are a number of issues which are coming in the way of permitting Islamic banking in India. Government have also asked us and we have written to them that should the government intend to carry forward Islamic banking they have got to have a new law for this and I believe that it is under the examination of the government.

Neha I have a question for Mr. Sinha. In one of the recent events there were some inputs given in terms of using a proportion of SLR securities for calculating liquidity coverage ratio the Basel III norms are concerned. Could you throw a little more light on that, and what is the RBI sentiment as to what proportion of the SLR bond will qualify for?

Shri Anand Sinha Liquidity regulation is in the form of SLR been there for ages in India and this concept of maintaining a liquidity buffer used to be there in the west. But in the last year many years it has not been dealt. After the crisis they have realised that there must be a buffer. So we have the buffer. But the problem comes that that buffer should be usable. As per Basel III that buffer should be usable, whereas our SLR is not usable in that sense. But we cannot add more liquidity over 24%, go on adding liquidity. So we will have to have a caveat that under certain situation, part of this should be usable so we are working out on a mechanism. That we are working on. That is all I can say.

Parnika Also your committee on provisioning, new commission norms, when is that expected?

Dr. D. Subbarao Dynamic provisioning.

Shri Anand Sinha Dynamic provisioning we have already put out the discussion paper as you are aware. Mahapatra, what is the timeline here?

Shri B. Mahapatra Actually we are depending on some data from the bank and the quality of the data from the bank is not good enough to come through some kind of results, so we have called for data further and maybe by March end we will be able to come up with the final paper.

Shri Anand Sinha In fact, even the discussions paper took a very long time because banks simply are not geared so far for that kind of data. So now we have gone in for a round of calibration. Conceptually, it is very simple. The trick lies in proper calibration. So we are struggling with the data, but we certainly want to come up with it as quickly as possible. Mahapatra feels that by March we should be able to come out with that.

Shri B. Mahapatra We want to implement it by March.

Alpana Killawala Thank you very much. Thank you, Laveena. Thank you for attending.

Dr. D. Subbarao Thank you very much.

Moderator On behalf of Reserve Bank of India that concludes this conference. Thank you for joining us and you may now disconnect your lines.