Edited Transcript of Reserve Bank of India's 6th Bi-Monthly Post Policy Conference Call with Media

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MR. N. S. VISHWANATHAN – DEPUTY GOVERNOR, RESERVE BANK OF INDIA
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Moderator: Good Day, Ladies and Gentlemen, and Welcome to the Teleconference with Media arranged by The Reserve Bank of India after the announcement of the Sixty Bi-Monthly Monetary Policy. As a reminder, all participant lines will be in the listen-only mode, and there will be an opportunity for you to ask questions during the teleconference. Should you need assistance during the conference call, please signal the operator by pressing '*' then '0' on your touchtone phone. Please note that this conference is being recorded. I now hand the conference over to the top management team of Reserve Bank of India. Thank you and over to you.

Dr. Urjit R. Patel: Welcome to the final Bi-monthly Monetary Policy press conference for this fiscal year. I would like to start by welcoming Deputy Governor Acharya to his first press conference. It feels good to have a full management team. Before I request other DGs to say something I will speak for a couple of minutes.

In this policy review, which you have all seen, a clear assessment of the evolving macroeconomic configuration, at least in the short-run, remains clouded by the transitory effect of demonetization. To elucidate, the CSO has stated categorically that it has used information for only the first seven months of the year while making its advance estimates for 2016 - 2017. On the inflation front, transient factors including anecdotal evidence on fire sales of perishables have discolored an objective assessment on inflation pressures. For example, if vegetables are excluded, CPI inflation would exceed the CSO's official print for the month of December, which was of 3.4%, by as much as 140 basis points. In these highly uncertain conditions, the Monetary Policy Committee exercised abundant prudence in keeping the policy rate on hold, while seeing off these transient effects and await a clearer and unbiased assessment of inflation.

Looking ahead, the Committee is dedicated to achieving the target of 4% CPI headline inflation, while keeping in mind the objective of growth as mandated by the amendment of the RBI Act and the Gazette notification. In fact, the notification states that the target has become effective since August 2016 and it is in this context that the Committee has made an explicit commitment to the target in this resolution. The Committee was fully cognizant of the lags through which Monetary Policy typically operates. It was also sensitive to the need for a calibrated approach to the target, thereby minimizing the collateral costs of achieving it. Therefore, we decided to shift the stance of Monetary Policy from accommodative to neutral, give us sufficient flexibility to move in either direction and to keep in consideration a reasonable time horizon over which inflation needs to brought closer to the target of 4% within the notified band.

In the view of the Committee, timely and effective transmission of policy rate reductions by banks is a critical part of this calibrated strategy and accordingly it has set out three guide posts to improve the efficiency of transmission:

1. Quick and efficient resolution of NPAs.
2. A speedier recapitalization of public sector banks.
3. Full implementation of the formula for determining interest rates on small savings.

I will now request Deputy Governor, Gandhi, to say a few words.

R. Gandhi: In the wake of the withdrawal of Specified Bank Notes since 9 November, 2016, the Reserve Bank had placed limits on cash withdrawals from certain types of bank accounts. On a review of the re-monetization, the Reserve Bank partially restored status quo ante effective from 1st February, 2017, by removing the restrictions on cash withdrawals from current accounts and cash credit accounts and withdrawal through ATMs. However, the limits on cash withdrawal from Savings Bank Accounts continued to be in place. In line with the pace of re-monetization it has now been decided to remove these limits in two stages as follows:

1. Effective from 20th February, 2017 the limits on cash withdrawals from the Savings Bank accounts will be enhanced to ₹ 50,000 per week from the current limit of ₹ 24,000 per week.

2. Effective from 13th March, 2017, there will be no limits prescribed by the Reserve Bank on cash withdrawals from Savings Bank Accounts.

Dr. Urjit R. Patel: Now, may I request Deputy Governor Mundra.

S. S. Mundra: I would touch upon a couple of things. As you must have seen in the 2nd part of the Policy Statement also, cybersecurity had been major area of focus of Reserve Bank of India, and to that end sometime back an expert committee was constituted headed by our Executive Director Smt. Meena Hemchandra which deliberated and gave a number of recommendations, which culminated into RBI issuing a comprehensive circular to all the banks on 2nd June, 2016, giving certain parameters to do the gap assessment of their cybersecurity preparedness and then it is a process which will be ongoing process. But having regard to continuing need to be vigilant towards the cyber security area, in existing systems as well as the emerging trend it has now been decided to constitute a Standing Committee on cybersecurity. It will be cross functional, it will also have the industry experts as well as the government representative and other details would be announced in due course.

Other matter is around the asset quality of banking system. While, we are yet to receive the results from all the banks for Q3, but based on the results which are announced already and on the basis of provisional data available broad trend is while there is some elevation in gross NPA ratio in the banking system across the categories, whether it is public sector banks or private sector banks, I think for first time in few quarters this time it is seen that in few banks the ratio has come down vis-à-vis the preceding quarter. Similarly, in respect of net NPA which are consistent with the gross NPAs, while there will be an elevation, but in a large number of banks the ratio has come down, showing that the level of provisioning is quite adequate. Also, there has been some conversion of restructured assets falling into NPA category, and as a result across the industry there is a reduction in the percentage of restructured assets. Overall, the system has shown improvement in operating profit but on the back of higher provisioning I think some of the pressures on net profit would continue. And finally, on the capital adequacy, while most of the banks are well-placed to meet the regulatory norms as they are required at this point of time, but going forward quite a few banks would be required to raise additional capital**.** Thank you.

Dr. Urjit R. Patel: DG Vishwanathan please

N. S. Vishwanathan: Good afternoon. I just want to mention about a point made in the part two again, that is regarding setting up an Enforcement Department. Enforcement, of course, is an integral part of supervisory action. We do take enforcement action even now but focused attention to this we believe will improve the regulatory compliance, going forward. So we are setting up an Enforcement Department effective 1st April 2017 into which we will fold enforcement action that the bank is taking across various functionalities so that there will be complete focus. This, we believe will improve the overall regulatory framework and compliance in the country.

Dr. Urjit R. Patel: Thank you very much.

Dr. Viral Acharya: I just wanted to make two points. As you have seen we have shifted the stance from accommodative to neutral as far as the monetary policy is concerned and this is mainly driven by a concern about global inflation that is picking up essentially on fuel and metal side, I think there is also a risk that this could be coupled with strengthening of the dollar and it could feed into significant inflation for our economy. So unless you believe that the food inflation or food deflation is really here to stay, I think your expectation would be more based on the core CPI which has been very sticky.

Now, why did we hold rates though? I think it is because the only other reason to lower the rate given what I just said about the inflation outlook, would be to try and narrow the output gap that has been created by the recent events. We think that fast re-monetization that is taking place as well as the balanced budget, balanced in the sense of being more austere **,** as well as reallocating to growth focused capital expenditures should actually aid in narrowing the output gap. And in fact, the way the Monetary Policy would work is by transmitting this through banks to the lending rates or borrowing rates of corporations. But much of this has actually taken place, thanks to demonetization because of banks being flooded with easy money. So, nevertheless we await greater data to know whether the impacts of demonetization are going to be truly transient, and therefore we remain fully flexible and therefore we have kept the rates on hold.

Dr. Urjit R. Patel: Thank you very much. We will take a few questions now. May I request Aaj Tak?

Virendra Singh Gunawat
Aaj Tak:

Sir, I have two questions. Many banks have reduced their lending rates in a few days, so still is there any possibility of reducing the lending rates for the common man? And second question, one of the reasons for demonetization was to reduce flow of fake currency in the system. But in the past, two or three incidences have occurred where fake currencies have been spotted in the market, so do you think that your objective is getting fulfilled?

R. Gandhi: The new notes which have been brought on board in the denominations ₹ 2000 and ₹ 500**,** they have enhanced security and design features. So, that is not easy to copy. The recent ones which we have seen, that is a pure photocopy. So, it is not real counterfeiting. So this photocopy is easy for even a common man to not to easily identify. It will be possible for them not to be duped very easily.

Dr. Urjit R. Patel: Let me answer your first question, there is still scope for the lending rates to come down because our policy rate came down by 175 basis points and the weighted average lending rate has come down at most by about 85 basis points to 90 basis points, so I think there is scope for some more transmission. In some borrowers, the healthy borrowers, sound borrowers for housing finance, etc., they have already benefitted from it, so that is where we are on that.

May I now request Dow Jones, please?

Gabriele Penisini
Dow Jones: The Committee mentions here the uncertainty that surrounds the direction of macro-economic US policies with potential spillovers, so could you tell us a bit more about beyond the strengthening of the dollar as already mentioned and how do you think that is going to affect India specifically?

Dr. Urjit R. Patel: So I think there are several global developments, one, continuing uncertainty on the upside over oil prices, that might be enhanced due to geopolitical reason, Iran, etc. base metal prices have gone up internationally, the global food index by the way has gone up as well. So there is more than one channel of global spillovers. And then the continuing uncertainty which of course always adds the risk premia on a full rollout of US macroeconomic policies, especially on the fiscal side where we still await clarity. And given the general tendency to roll back some of that extra accommodative monetary policies by the systemic central banks of the world, I think there is enough global uncertainty to go around.

Govardhan:
Economic Times

Govardhan from Economic Times. Sir, next fiscal second half the inflation is projected at 4.5% - 5% for which global oil prices and the financial market developments were cited. At the same time the demonetization impact is assessed to be transient, so why is there shift in stance, why couldn’t they have been accommodative if it is only transient?

Dr. Urjit R. Patel: Main reasons are the following – the Committee wanted to emphasize that in a calibrated manner and therefore to make it on a durable basis we need to move closer to 4% . Secondly, the non-food, non-fuel part of the CPI index has been stubborn at about 4.8% - 4.9% since September. And therefore, that is the kind of risk that is there. And if you combine that with all the risks we have told you about, as I said in the opening statement that is abundant precaution, the committee felt that we needed all the flexibility that we could muster.

Bijoy:
Cogencis

Sir, a couple of things. One, you mentioned the liquidity overhang from the demonetization, you said it will continue in the FY18. What does that mean for your neutral stance on liquidity? Also, because you spoke about all the global elements, what happens to the real interest rate discussion that you had raised last time and the 1.25 % that you all had moved to, these two elements coming together?

Dr. M.D. Patra: We expect liquidity to be evening out, we started already doing that because currency in circulation has gone into positive territory. There will be residual liquidity surplus in the rest of the year and a little bit in to the early part of the year but that is not so much due to demonetization as it is due to the fiscal policy being played out and all that.

On the real interest rate, I think you mean the natural rate of interest. So that does not change every time we meet. So we set out our range of 1.25% to 1.75%, we stay there. And if you make your calculations taking in risk-free rate and the forward inflation rate, you will come into that range.

Shyama Mishra
Doordarshan:

Sir, in total new notes, how many new notes of ₹ 2000 and ₹ 500 have been circulated? And we are still seeing the effect of demonetization is there, so how long for a common man to end this suffering?

R Gandhi: Notes in circulation as on 27th of January, 2017, had been ₹ 9.92 lakh crores comprising of all the denominations including the 2000s and 500s notes.

Shyama Mishra
Doordarshan: Sir, specifically 2000?

Dr. Urjit R. Patel: No, we do not usually give that information out. And Deputy Governor Gandhi has already laid out the two-step process by which we are easing the situation**.**

Simon Mundy
Financial Times:

I was interested in the remarks about the NPAs which obviously have been at quite elevated levels at several banks for some time now. I was wondering if we can get your thoughts on how big a problem this is for the economy. We speak to some people they say, well the demand for credit is not that high so perhaps it is not as big a problem as some might think, but you clearly have voices on the other side as well, so how big a problem is this NPA problem for the economy and what will it take to really draw a line under it?

Dr. Viral Acharya: I think the numbers are out there, I think the problem in an absolute sense is quite large. And I think it requires a significant recapitalization of the banking system, especially the public sector banks. But I think it also requires speedy and efficient resolution of the non-performing assets, the stressed assets. And I think it is easy to use the words demand and supply but usually they are very hard to separate out, if you have a sector where we over lent, as a banking sector as a whole and then things come crashing down, usually that leaves the sector with excess capacity and of course there will not be demand. So I think it is hard to say this is just pure supply and demand so that we can separate it out. I think if we resolve the NPAs of banks, it will probably actually help restore some of the capacity utilization in this sector by actually reducing some of the excess capacity that might actually create healthy conditions for investment in these sectors, it might create pickup. And at the same time banks, because of the resolution of the NPAs might be able to consider beginning to start lending to the same sectors again.

Simon Mundy
Financial Times: You can say to some extent it is holding back industrial activity and lending activity?

S. S. Mundra: As Dr. Acharya already mentioned, these are the known figures that the level of stress assets in the industry is slightly above 20%, if we put GNPAs, restructured and all those things. So, it would not be fair to say that there is no concern, there is concern but as generally it is referred to as the twin balance sheet problem. So focusing only on the banks' balance sheet and talking about the gross NPA ratio, that is the one part of it which as you are aware RBI has been focused on this for quite some time. And as a result of that continuously provisioning, I think that has to some extent equipped the banks to deal with those accounts. But obviously, this concern would be completely addressed with the other side of the twin balance sheet problem that while it is good that the weaknesses have been recognized, provisions have been built but I think key would be the resolution. For resolution, a number of tools have already been given by RBI in past year, year and half and under each of these mechanisms quite a few number of cases have been taken up by the banking industry where they are working. The other important development in this will be around the bankruptcy code, which I think it will be very important that it becomes operationalized soon. Our sense is that the combined use of these tools which used to be very case specific and specific to individual entities is something we will continue to monitor.

Anurag:
Zee Business

Sir, when we see the news mostly what is said about the old currency post-demonetization, is that 98% old currency has been returned, some say that more than that also has been returned. So can you say that, and during last policy also you had said that how much of old notes had been collected. So if you could tell the exact number till now, I mean, the way there have been issues between banks and bank officials, this has affected the trust of the common man with the banking system. So would you like to give a message to them, for the common people that the banking system that we have is very transparent and in good hands?

S. S. Mundra: I will take the second question first. One, I want to assure you on behalf of Reserve Bank that the banking system of India is in good hands. And if one or two incidents that have happened here or there, then taking only those into consideration and saying that the whole banking process has been shattered is not the right way to think. What you said, even if we see that you will see that there are so many branches in the banking system, how many people are working in it. I am not saying that no such cases have occurred, handful of cases have happened but if you look at it on the country-wide basis then I think the percentage of such incidents is negligible, it is not significant. And in all those cases investigation has been done, many people have also been suspended. And generally if you see the banking service that is there for the common people, the way they have worked in the period of these two months, when people have gone beyond their call of duty; I think that it your responsibility, that the bankers they have gone out of way and worked, you must appreciate them so that is one thing on your first question. On your first question on the numbers, the work is going on. And you must understand in whole country there are 4000 currency chests and apart from that Reserve Bank keeps currency in 19 places. There is an exchange of currency between these chests and Reserve Bank. After 30th December on a net basis we asked banks to calculate their cash receipts. After that Reserve Bank's team did sample checking on the calculations furnished by banks. The reconciliation of physical cash and receipt of cash as per data from bank accounts is going on so we hope that in the coming times this will be completed. Apart from that, there are few things which are open-ended because in the beginning, Cooperative banks have collected cash, on that Supreme Court has given their direction, so NABARD will work on that. That number we have to take into our account. Under our arrangement with Nepal and Bhutan, some amount of currency is in Nepal and Bhutan that also we have to take into account and apart from that, till 31st March and 30th June this window is open, so that people can deposit cash. So cumulatively all these things we will tell you the numbers definitely but after the final verification on a piece-to-piece baisis, you must understand that such big amount of currency has been withdrawn on such a large scale, it will take some time, but that we will tell you in due course.

Gopika:
Mint

You spoke about resolution of NPAs, the Economic Survey this time mentioned setting up of a bad bank. Is the Reserve Bank considering this, Dr. Acharya also had recommended such a move earlier?

Dr. Viral Acharya: I think we have to remain open to all solutions at this point, because I think the problem is quite large. I do not think a bad bank just by itself will necessarily work, I think it has to be designed right. The big piece of the problem is can you get the bank to sell the assets at the right price to ARCs and private investors who want to come in, how to get that right price to come in and using a portfolio or a bad bank kind of approach, I think that is going to be key. We are going to be thinking about what kind of design issues might help with that, but we think it is something if designed properly could help.

N. S. Vishwanathan: As Dr. Acharya said, all options are open. Fundamentally, it is a question of structuring the whole thing and again, finding the right price so we will have to take a call on the whole thing, there is no dogmatic view on this.

Thank you very much.

Moderator: Thank you. Ladies and Gentlemen, with that we conclude today's conference call. Thank you for joining us and you may now disconnect your lines.