"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 this conference, all participants' line will be in the listen-only mode. 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. If you should need assistance during this conference call, please press '*' and '0' on your touchtone phone. At this time I would like to hand over the conference to Ms. Alpana Killawala. Thank you. And over to you Ma'am.

Alpana Killawala Thank you, Shyma, and once again welcome from Reserve Bank of India to this post policy press conference. We request the Governor to make a statement.

Dr. D. Subbarao Thank you very much. Welcome to everyone present here and all those who are listening into this post policy press conference. By now we have a shared understanding on the protocol. As you may have noted I have moved away from reading a prepared statement because you all heard me read that this morning. So I thought I will use this opportunity to go a little beyond the statement and give some appreciation of our understanding and some appreciation of the decision.

First, we reduced the repo rate by 25 basis points from 7.50% to 7.25%. And those of you who been watching, would note that this is a cumulative decline of 125 basis points from October 2011; it went up to 8.5%, now it has come to 7.25%, i.e. 125 basis points decline. This decision today was based on an assessment of the current and prospective macro situation. Growth in 3rd quarter of last year was 4.5%, lowest in 15 quarters. And the Reserve Bank's current assessment is that during this year also growth will slowly pickup and perhaps in the second part of the year, and that will depend on some conditions and those conditions are: first that investment must pick up; supply constraints, especially in the food and infrastructure sectors must be eased; monsoon should be normal as has been forecast; and the global situation should not deteriorate.

The second consideration that went into the policy was the inflation outlook. Although headline inflation eased by March 2013 and came close to the Reserve Bank's threshold limit, it is important to note that there are food price pressures and there are also supply constraints which will have implications for inflation.

On global and domestic developments, global developments are quite abundantly clear; there has been some recession of the risks to the advanced economies, but that is not transmitted to economic performance. The risks of policy implementation and uncertainty about outcomes continue to threaten the prospects for advanced economies. And that is why implications will have some influence on our macroeconomic performance.

More importantly, coming to the domestic economy, third quarter last year, as I indicated, and as you all know, growth was 4.5%. For the last year, 2012-13 we got 5%, we must in the 4th quarter have expanded at 4.7%. That number is not yet out, but we might end at 5% or slightly below that, we might have ended at 5% or slightly below that. It would be quite close to the CSO's estimate of 5%, and lower than Reserve Bank's last estimate made in January of 5.5%.

On growth for the current year, we projected 5.7%. And as I said somewhat subdued in the first half but picking up in the second half. One question is has growth bottomed out. If we just look at those numbers, close to 5% last year and 5.7% this year, you could say, we may have bottomed out**,** but not a dramatic revival. Of course, growth will depend on agriculture, especially on the monsoon. Industry, we have been told that the pipeline is dry, but the pipeline to pick up itself will take time. The CAPEX cycle is depressed; the industrial outlook Survey that the RBI did shows that the optimism levels are quite low. Capacity utilization is below the highest level. In the services sector, the PMI has slowed down. And Services sector has also been pulled down by the weak global demand, not only for service exports but other exports as well which have implications for the Services sector. The bottom line therefore is that for growth to pick up and perform as the Reserve Bank has indicated, and hopes and expects, investment revival is very, very important.

On inflation, again those of you who have been noting the numbers would note that average WPI inflation year before last 2011-12 was 8.9%. Average WPI inflation last year 2012-13 was 7.3%. In March 2013, inflation was 6%, so that is a significant decline. This year we expect inflation to be range bound, around 5.5%, slightly edging down in the first half and edging up in the second half. There are of course risks to inflation, stemming from the food situation; that's the cyclical monsoon factor as well as the structural food inflation factor that we have been talking about for some time. Then fuel is another risk factor, the global price of oil has softened in recent weeks, but one can never be sure, given the uncertainty about global demand and global supply. And we need to be concerned not only about the global price but also about the exchange rate and how that may move. Then we expect a lot of suppressed inflation to open up in the months ahead because of gradual monthly diesel price adjustment, because of expected adjustment of coal prices in the next few months, and consequent adjustment of electricity prices. Rural wage pressures, we have reported in the MMD yesterday that it is slightly moderated but it is still 17% quite high, rural wage increase. The other risk factor to inflation is the minimum support prices, which could go up, and supply constraints, especially infrastructure bottlenecks.

Once again I want to say that even as RBI communicates through the numeraire of WPI, I want to say that we look at all indicated inflation, including CPI. I hear some analysts say that RBI is blind to CPI, but we are not. If you look at CPI we reported about CPI and we take that into our policy calculation. And you all know why we cannot shift completely to CPI just now.

On liquidity conditions, we have not cut the CRR, but cumulatively from the highest level of 6% in October 2011, it has now come down by 200 basis points to 4%. Last year, we infused considerable amount of liquidity; Rs.522 billion through the CRR cuts, Rs.1.5 trillion through the OMOs last year is together about Rs.2 trillion and there were some minor FOREX operations as well. There is considerable amount of liquidity buffer with the banks. Please note that- there is excess SLR of about Rs.3.5trillion, there is unutilized export credit refinancing of about Rs.210 billion and the MSF for which banks have access that is about Rs.1.4 trillion. So there is Rs. 4-5 trillion of liquidity that banks can access. We have indicated the risk factors, I will not go into them, but the current account deficit and the financing of the current account deficit remains significant risk factors.

I also want to paraphrase the guidance that we have given. It has been now standard practice for me to anticipate standard questions and answer that, and I think the most probable question is about giving guidance on guidance. I have been uncomfortable about doing that, because we put a lot of thought into the written form of the guidance, and my apprehension is that if I try to say it orally, I distort the nuancing of the communication. But nevertheless let me attempt that because I think it is very important that the dissemination is accurate.

We have given assessment of the macro economic situation, particularly about the inflation outlook. This year inflation will be range-bound around 5.5%. Indeed after a long time, we are within striking distance of the threshold inflation of 5%. It is critical in the Reserve Bank’s view that we consolidate and build on this effort and endeavour to condition the evolution of inflation, the threshold of 5%. Even as inflation is now below 6%, and it went down somewhat in the first half of this year, there are several risks coming from exchange rate movement because of the large CAD, because of the possibility of sudden stop and reversal of capital flows. There is the oil price, a suppressed inflation coming into the open and all other factors that I said earlier.

Keeping in view the need to consolidate on inflation gains, and the upside risks, we have said that there is little space for further monetary easing. However, and this is important, however, if inflation recedes further and faster, if current account deficit moderates more than we factored in, if the upside risks become more benign, space would open up for further monetary policy easing and we would do that. But, according to the current assessment of the macroeconomic outlook, space for further monetary policy easing is little.

On liquidity, we said that we will manage the liquidity, to reinforce monetary policy transmission. We recognize that even if we cut rates, if liquidity is not comfortable, transmission will not take place. So we remain committed to the objective of maintaining liquidity in the range of plus/minus 1% of NDTL, using all instruments available to us.

I partly heard the bankers speak to you. I do not want to go into all of that. I heard you ask them about monetary transmission and I heard some of the answers. And that is pretty much is line with what they told us. It is that monetary transmission will take place but it will not be immediate, it will take time. And cumulative transmission of not only today's cut but the cuts affected over the last 6 months is still in trail**.** They indicated a problem about inability to reduce deposit rates because of maintaining their cost, and we also appreciate that because we need to keep savings up in the economy. And some of the smaller banks said, that if the large banks take leadership in cutting rates, they will be able to follow.

By the way I just want to make a comment on gold. Again we talked about it at length in this morning's meeting with the banks, and you all heard them tell you about the three sources of demand for gold – Consumption Demand, Investment Demand and Speculative Demand. The base line, quantity of imported gold in the country is about 700 tonnes. That has been the level of volume of import in the pre-crisis years when inflation was moderate, when savings rate was going up, when the international price of gold movement was rather steady. So we take that as the base level appetite for gold. In the last two years, volume of imports have been 1,000 tonnes plus. In 2011-12 it was 1,064 tonnes; in 2012-13 last year it was 1,015 tonnes. If prices come down- and it is unclear that they have trended down in a credible and significant and sustainable way- if prices come down, the consumption demand might go up, but investment demand and speculative demand might moderate.

The Reserve Bank has concerns about gold because of the current account deficit management. It concerns about gold because of financial stability concerns. It concerns about gold for the larger consumer protection point of view. We have taken a number of measures over the last one year. We have taken, the government has taken. And there is one measure in this policy which is prohibiting banks from importing gold on a consignment basis unless that gold is meant for re-export. We have also introduced certain regulatory measures in the past against NBFCs, also the banks about being restrained both in import and sale of gold, and in lending against gold and we have reiterated that advice, that guidance and those regulations in the meeting this morning. I will stop there, I have taken slightly longer than I normally do but I thought it is important to communicate this. Thank you very much.

Alpana Killawala Thank you sir. We will start with Lata.

Lata Sir, Lata Venkatesh from CNBC**.** Sir, you have not really given us March 2014 inflation forecast. You told us that the average will be 5.5 during 2013-14 and then you have this maybe concluding statement that you will endeavour to condition the evolution of inflation to a level of 5% by March, using all instruments at your command. Now, the only known instrument to bring inflation down is to hike interest rates. So exactly what do you anticipate in year 2014, March 2014 forecast, and what will you do to reduce to 5%? If I look at your fan chart, 90% probability is 6% inflation by March 2014. So what are you going to do to bring it to 5%?

Dr. D. Subbarao You have read the statement very correctly, which is our assessment is that is the range bound around 5.5%, slightly edged up in the second half, and 90% probability at 6%. The second part of that is that we will endeavour to bring it down to 5%. But what is not correct is that the only instrument available to us is the interest rate. We have other instruments. We have said that it is important to manage liquidity as well in order for monetary transmission to take place and if that takes place growth will improve and that itself should have some benign influence on inflation. Then we have communication, and we have been using communication as an active policy tool and we will use that as well. So the belief that the Reserve Bank's armoury is limited to the policy interest rate, I think is to take somewhat narrowly. So once again, we want to bring it down to 5%. See, saying that we will bring inflation down to a mid-threshold level of 5% three years ago would not have looked credible, but today when inflation is 5.5% -6% now- but expected to come down to 5.5%, I believe that we can credibly expect to bring it down to 5%.

Anirudhha Anirudhha here from ET Now. I just like to understand taking off from the previous question, you have said here in the policy that the risks in the current account deficit are very significant and could actually warrant a swift reversal of the policy if situation worsens from here on. Could one assume that you would not hesitate to raise rates at a juncture going forward if the situation gets worse, and also you have been critical of the government in the past. Even in this policy statement you have said that the onus for kick starting growth also lies somewhat with the government, if not completely with the government at this point in time, given the kind of policy action that the RBI has taken. So I just like to understand is there a timeline that you all have in your mind in terms of how long you can afford to wait before the current accounts deficit comes into your comfort zone and also in terms of further rate cuts, is it possible to assume that we might not see too many rate cuts until and unless the government takes any kind of concrete action?

Dr. D. Subbarao On the first part of your question, it is right that the CAD is very much on our dashboard, much more than in the past, because last year CAD, we do not have the final figure, but would be close to about 5%. And this year there is a lot of expectation that it might trend down, but our reading is that it might be lower but not substantially lower; it will be way above the economy's sustainable level of current account deficit of 2.5%. So we have to be quite careful, carefully looking at development from the CAD. And that will be one of the variables that will go in to monetary policy calculation. Precisely whether we will raise rates if CAD is higher, we will reduce rates if CAD is more benign is not clear, but I have said in the guidance, that should the CAD moderate more than we have factored in, there will be room for easing. On the second question, macroeconomic management, particularly supporting growth is joint endeavour of the government and the Reserve Bank. Policy interest rate is just one variable, the supply factors will have to come in, the supply response has to come in and that is very much within the realm of the government, not just central government but also the state governments. And there is clearly no timeline; it is not an ultimatum that we think. We will of course be watching the situation and as you know we do this every 6 weeks these days, so quite frequent intervals. So I think the opportunity and occasion for any response from the Reserve Bank is already factored in.

Lata Sir can I just add to what Anirudhha asked? Anirudhha referred to what had actually been a little out of line. You were referring to this two way movement in rates- that there could be a possibility of hiking in rate. Now, where is that exact sentence? .. could warrant a swift reversal of the policy stance. You said it today, you said it yesterday also. This is the first time we have heard you say this on two consecutive occasions. Do you really see a situation where you may have to raise rates Sir?

Dr. D. Subbarao I cannot really forecast about that now. I cannot really say how the CAD might behave and how we might respond to that. All we have done is to alert all the stakeholders that the Reserve Bank is watching the CAD and the CAD will have implications for inflation, for macroeconomics stability and should we need to respond we will not hesitate to, and that is what we intend to say.

Lata When you say it is 5, it looks like a base line scenario.

Dr. D. Subbarao Yesterday was one document, today is another document.

Lata But that exists.

Dr. D. Subbarao Yes. And I have also said in the same breath, you may have noted that should the CAD moderate further, there will of course be room for easing. Urjit would like to share your views?

Dr. Urjit R. Patel I think you have reiterated something that is in the normal armoury of macroeconomic policy makers and managers when external risks turn into left tail events. And so I think it is a reiteration of almost a text book response when matters go awry.

Dr. D. Subbarao Did you all have any doubt that we were not looking at CAD?

Lata No, I do not think anybody was prepared that you will say that you will hike rates, a situation will come when you will hike rates. Yesterday it looks like a text book statement because department was not the Monetary Policy Department. Today, it is the Monetary Policy Department itself saying and the Governor himself repeating it. So it looks like it is very much in your radar that a situation may come when you might raise rates.

Dr. D. Subbarao We completely own yesterday's document on behalf of the Reserve Bank. We have no doubts about that.

Devina Devina from NDTV Profit. Sir, you have been highlighting that you are watching CPI very closely. Right now inflation has come down, imported inflation has come down, commodity prices have cooled down, and crude oil prices have come down. Second half, the full transmission of diesel prices has not yet been passed through for consumers right now. You will see that coming in, electricity tariff to go up, that will have a negative implication on inflation and then again, crude oil prices have to go up in another case. Some say and if I may be the Devil's Advocate, the 25 basis points cut would be little premature.

Dr. D. Subbarao Yes, that is your view, certainly, but it was our considered judgment that the 25 basis points reduction this time was warranted along with the guidance that we have given. And I want to say once again that we are sensitive to all the risk factors, that I had mentioned myself more than you have mentioned, more in number than you have mentioned. We are sensitive to that.

Devina Just a follow up to that. So in that light and with that having implications, again the fiscal situation …….(inaudible) of you going ahead and hiking, right?

Dr. D. Subbarao I cannot speculate on that, about the conjecture of circumstances and how we might respond. But those are all uncertainties that we have to live with.

Ritesh This is Ritesh here from Zee Business. Governor, one question on CRR front, some parts of the markets were expecting a CRR cut, as we have seen the repo borrowings are way ahead of Rs. 60,000 comfortable limit which within RBI stays, we have seen the borrowings from the RBI is too ahead of its a limit but also you said that bank are sitting on excess liquidity, they have excess SLR and other tools like that. So one, what was the rationale in not cutting the CRR, and if RBI feels that banks are sitting on excess SLR and other liquidity tools, then why is not the RBI nudging banks to use that liquidity?

Dr. D. Subbarao Okay, first of all we have not cut CRR because we believe that the liquidity deficit to the extent that it exists is not because of structural reasons. It is because of frictional reasons, government cash balances and some wedge for much of last year between credit growth and deposits growth, although towards the end they both converged. But for March of last year there was a wedge which caused liquidity deficit. And this year too, the same factors apply in large, it is not structural deficit. So we saw no case for cutting CRR. As far as individual banks are concerned, how they manage their liquidity is their concern. I gave the numbers in order to let everyone know about the quantum of liquidity that the Reserve Bank injected last year and about the room that is available for banks to claim liquidity, at a cost of course. So this view that liquidity can only be improved by the Reserve Bank by cutting CRR I think is mistaken. You can understand banks saying it, but I think all of us should understand that liquidity is more than reducing CRR.

Devina Sir, any outlook on OMO operations?

Dr. D. Subbarao No, we will announce them as per standard practice as and when we believe that they should be done.

Kavita Kavita from CNBC Awaaz. One follow on question which Ritesh asked you. You are saying that banks have excess liquidity, you also said that not much transmission has happened in the through the previous rate cuts. The banks have given a similar indication this time that they would not be able to do too much rate cut transmission. So then how long is the RBI ready to wait for the transmission of rate cut?

Dr. D. Subbarao Kavita, this does not depend only on the RBI, we can only do so much and we expect transmission to take place. Admittedly, some transmission has taken place as we reported in the document. It is not one-to-one. So what we gathered from banks this morning is that transmission will take place in the next 3 to 6 months. It may not be as immediate as everyone expects it, but it will certainly take place and transmission will not just be of the cut this morning but of the cumulative cuts over the last 9 months. And as I said we meet every 6 weeks, so we will take stock of the situation and see what action we may have to take.

Lata Sir, in that context, how do you interpret 'yields little space for monetary easing'? In numerical terms, does 'little space' mean no space, does it mean one cut, does it mean 50 basis points cut?

Dr. D. Subbarao I cannot give a quantitative equivalent to that, nor can I take a lesson in grammar. Little is little, little is not a little; little is little.

Lata Sir, little is not nil.

Dr. D. Subbarao Well, we use that word quite advisedly. Other alternative was to say nil but we did not. But we also did not say 'a little'.

Virendra Virendra Singh Gunawat from Aaj Tak and Headlines Today. Two questions, one over the Ponzi schemes. After the Sharda Group, the Ponzi schemes headlines stories are back in the limelight. We have certain cases where Madhya Pradesh High Court and the CBI investigation report have come out last year in July 2012. They had indicated that at least 30 ponzi schemes are floating around where cattle, buffaloes, goats, floating around and the SEBI, RBI, Ministry of Finance and the Union Government of India- all the reports have been sent to them. My question is that why it takes almost a year even not to take an action on these particular companies which are still floating around and people are investing in these companies and is it that like the SEBI even RBI is looking for one single regulator to handle all these chit funds, M&M, CISF kind of a scheme? My second question, very important, is on first cobra post investigation because few minutes back we spoke to bankers and they were saving their skins and they even said that they are waiting for the RBI report. My question is that till now, what action has been taken by RBI, what has been communicated to these banks? This is very important because this is the money which is floating around, it is not just the customers' money, it is about terrorism funds, it is about money laundering and many other things.

Dr. D. Subbarao Thank you for these questions, both are very, very important. I don't know how much time I can spend on them because those two questions themselves require an entire press conference. But regardless, first on the number of illegal fraudulent quick operators who are in several parts of the country duping innocent people, in the Reserve Bank we have been concerned about that. First of all you must note that the Reserve Bank's regulatory jurisdiction on the non-bank sector is quite small. We regulate only the non-bank finance companies and only those non-bank finance companies which have assets and income of more than 50% from finance business. So that segment of non-bank financial sector that we regulate is quite small. It is quite important of course, but that is quite small. And the reason for that is because the systemically important require intense special regulation by an institution like the Reserve Bank. On the other hand across the country there are thousands of companies, thousands of unincorporated bodies of which some of them are doing legal activity, some of them are doing illegal activities and those do not come within purview of the Reserve Bank. Regardless, Reserve Bank as a public policy institution, as one of the premier regulators in the country, we have assumed responsibility for this towards educating people, towards spreading awareness, towards training a lot of people who should be involved in curbing this. In meetings with the state governments, in meeting with the state chief ministers, in meetings of the state level bankers committees, these issues invariably come up as a standard item that we have instructed our Regional Directors to invariably put on the agenda. We have trained police officers, we have trained officials, elected and nonelected at panchayat and zilla parishad levels. We have issued public awareness advertisements. So curbing all this will need investigation, will need enforcement of law, but more importantly two things as Dr. Chakrabarty said a few days ago, first of all we must provide access to the formal financial system for a large segment of the population which do not have access now. The reason these Ponzi schemes all thrive is because those people do not have access or experience barriers to accessing it. Even if there is a bank branch in the village, I may not feel free to go there because of my socioeconomic background, etc., and the second thing is we must spread awareness and both those things the Reserve Bank is doing. About why certain cases are taking long, etc., you know the general situation in this country; I don't have to say why that is taking so long because the processes are quite involved.

On Cobra-Post, as soon as that came to light, we started a special investigation or supervision or whatever you might call it, with those three specific banks as well as thematic study against 30 banks. A number of specific transgressions of norms have come to light. We don't believe that this involves any money laundering, if you understand money laundering as money involved in crime; however, there have been transgressions of KYC norms, I have a list of them, but I don't have to go into all of them. What we have done is talked to those banks, called those CEOs for a meeting, told them about what the deficiencies are and they have gone back and implemented some of the systemic improvements. We have talked to the forensic auditors pointed by those banks, now we will of course be issuing them "Show Cause" notices and on the basis of that we will take action. On the thematic study- that is complete. We are trying to access our learning from that and very shortly based on that study, we will issue guidelines about what banks need to do, we will internalize the guidelines about what the Reserve Bank needs to do in order to improve systems and we will also see how we can improve awareness among people for a lot of this thing. Ultimately the safeguard against all these is the people themselves. It is not so much the banks, it is not so much the police, it is not the Reserve Bank, its the people's awareness to protect us from this.

Virendra One small clarification, "Show Cause" notice to only three banks or some more banks?

Dr. K.C. Chakrabarty It will be issued to all banks depending. Regarding "Show Cause" notice, first we will give them the report and ask them to explain. Now we must understand all deviations is not a wrong thing. For example, if my address is not there, in the bank books it is not KYC compliant, but that does not make the transaction illegal. You put my address properly it becomes a right transaction. Many things will be rectifiable. Only if I find that because of address is not there, somebody else has transferred money to account then that becomes an offense and then we can take action, so those are things that we ask for explanation. If we feel we are not satisfied with the explanation, then we issue the "Show Cause" notice, that look these are things that are wrong and then based on that we will take some action. It is a process. We have to send and this will happen to all the banks. If we find their compliance report is satisfactory, this is the thing but what I am saying in this thing, we must see in all this things it is an evolutionary process and KYC, anti-money laundering guidelines these are taking place for the last 10 to 15 years. We are trying to improve the system, we are trying to use the technology, so this is an ongoing process, that does not mean our banking system is that bad, but then everyday there are lakhs of transactions taking place and there will be some deviations and as and when deviations happen, banks have a system to identify that. The main point is that system is strong enough, but there are aberrations and we are trying to improve that. And if you see the policy guidelines, many of these things have been indicated, what are the systemic level corrective measures banks need to take. Wherever there are some regulatory gaps, that also we are trying to bridge.

Virendra Sir, how many banks do you plan to serve "Show Cause" notice and that includes a public sector bank as well?

Dr. K.C. Chakrabarty You see I cannot give the number at present, but even a "Show Cause" notice when we will give we will not be able to tell. But yes, definitely whomsoever we find that there are mistakes, there are transgressions, violation of the thing, we will definitely issue the "Show Cause" notice and take appropriate action.

Lata Sir, your point is the "Show Cause" notices may not necessarily be issued only to the three banks covered?

Dr. K.C. Chakrabarty Not at all, everybody is same for us.

Lata Which means you have observed transgressions across?

Dr. K.C. Chakrabarty Yes, and not that- every year we are observing, it has nothing to do with Cobra-Post.com., Every year, AFIs we are finding there are transgressions and anybody who is working, there will be mistake. But all mistakes are not critical mistakes, we can rectify many of the things, the transaction is not invalid, it is not illegal, that is what we are trying to say.

Lata Possibly, these banks would not attract the penalty also from the RBI?

Dr. K.C. Chakrabarty I cannot say. If they have not done wrong, I cannot.

Lata Since you have detected these kinds of transgressions in earlier inspections as well, have you already had to issue "Show Cause" notices for these kinds of violations?

Dr. K.C. Chakrabarty No.

Virendra Taking it forward, have you given a clean chit to these three banks specifically?

Dr. D. Subbarao No we have not and we are saying that we have to issue "Show Cause" notices, so the enquiry is still in progress.

Mayur Shetty I am Mayur Shetty from the Times of India. In the context of the new bank licenses, you are about to open the window shortly. I wanted to know if there is a number of banks that you are comfortable with in terms of regulating or are you looking at giving licenses to everyone who is fit and proper?

Dr. D. Subbarao No, we are not thinking of giving license to everybody who is fit and proper. In fact I think there is a sentence in the guidelines which actually says that not all eligible applicants may be given licenses. To your first question about how many licenses we do not have a number in our mind now, but it cannot be too many, it cannot be too few, so let us not get into numbers just now.

Diana Monteiro Diana Monteiro from Bloomberg TV. I have two questions, one from the liquidity deficit. You said that you will continue to manage the liquidity deficit in the system, but you have not cut CRR, which essentially means that over the next one and a half months you see management via OMOs. But at the same time, banks believe that easing any kind of liquidity pressure via OMO will not really help them ease their liquidity deficit, this is what they told us just before we had this meeting. So is there is a slight disconnect about between what the Reserve Bank of India considers easing and liquidity and what banks are looking forward to in terms of easing of liquidity? The second question is, is there any perceived risk associated with bringing down interest rates because of which the kind of attractiveness that we are currently getting, because of the high yield that we have in terms of capital flow might go away?

Dr. D. Subbarao On the first question about whether there is a disconnect between the Reserve Bank and the banks in the assessment and remedies for liquidity management, I think that is an interpretation you have to make. But our understanding is that CRR is across the board for all banks and please remember if we cut CRR by 25 basis points that is about Rs. 170 billion, not very much. Whereas OMOs as I gave you the numbers, we have actually run into trillions of rupees. So in terms of sheer volume or sheer value, OMOs have been much-much larger and also remember OMO is demand based, it helps those banks which have liquidity shortage whereas CRR is across the board and if liquidity is the problem, I think OMOs are as good as CRR, if not better. On perceived risk about the capital flows, the second question, if we reduce interest rates how will capital flows behave? There are two ways of answering that, one is that the interest rate differential between us and the advanced economies will narrow and we will become less attractive and therefore the debt flows might come down. But on the other hand some people have argued that there is this "India exceptionalism". I don't know, you or somebody was calling that phrase, that we actually reduce interest rates, we have given a signal that economic situation here is improving and therefore we might be seen as being more attractive for flows, so it depends on how people interpret the situation.

Dr. Urjit R. Patel Even after the interest rate reduction, the differential is still so large, you know the yields internationally- they are barely in basis points. So despite this India still remains attractive even from a debt perspective.

Bijoy Bijoy from Cogencis. In the past you have mentioned in a couple of speeches that banks should start living with lower net interest margin. Is that something that you may have considered when you are telling banks to do more transmission at this point of time because they constantly are saying that the deposits rates are high. Have you brought up that argument once again when you were trying to talk to the banks this time?

Dr. D. Subbarao No, we did not, not this morning, but I still remain committed to that view.

Kavita Sir, just wanted to ask you about gold. You have talked about the restriction to be imposed on gold imports. How much imports could be reduced as a result of that?

Dr. D. Subbarao It will be difficult to say, but we said that 700 tonnes is the base volume and 300 tonnes is the additional demand because of investment and speculation. As prices has come down, that demand should go down, but again I want to caution that there will not be a dramatic reduction, but we expect some moderation in the quantum of gold imports, some moderation - maybe marginal, maybe significant.

Shobhana Do we have an updated estimate of the unhedged foreign exposure with Indian companies? Mr. Khan had given us an estimate a few months back, do we have an updated estimate?

Dr. D. Subbarao I believe not, he is saying, it is around 40% is hedged.

Shobhana 60% is unhedged, do we have a quantitative update?

Dr. D. Subbarao Maybe when we do the study we will get it, when we draft the guidelines.

Shobhana Do we have an estimate of the money lying with chit funds and Ponzi schemes? Does the Reserve Bank of India have any number, rough estimate?

Dr. D. Subbarao No, remember chit funds are not illegal, Ponzi schemes are. Actually I have heard about this, one of the first things that came to me when I joined the Reserve Bank was actually this, some Ponzi Scheme in Odisha and since then in Eastern India especially and now increasing in the Northeast this is on the rise and we need to curb this.

Shobhana How much transmission has the Reserve Bank of India built in while estimating the growth for FY14 and FY15?

Dr. D. Subbarao Transmission of the policy rate?

Shobhana Because if you are saying 5.7 per cent, I am assuming that you have estimated that there will be some transmission that is taking place, how much have you built in for FY14?

Shri Deepak Mohanty Transmission should take place but there is no quantification.

Dr. D. Subbarao I don't know if there is a variable in the model about the transmission itself, I have not looked at the model, but I don't know if there is just stock variable there about how much of Reserve Bank's policy rate will transmit to the lending rate.

Shobhna How much does the Reserve Bank of India expect in terms of transmission in FY14, because it is critical.

Dr. D. Subbarao That is right. It is critical and I think we spoke about it last time. We don't know what is the cause and what is the response. Whether it is higher demand that will have banks reduce the lending rate or banks reduce the lending rate which will in turn accumulate demand. It is not clear, which way the causation runs. So I think it is difficult to build that in to a model precisely, a quantitative model.

Gopika Is that a reason why you have reduced the credit growth forecast for FY14 and keeping a marginally hiking the growth forecast. What is the misnomer here is that you have increased GDP forecast marginally but you have reduced the M3 forecast. Is that the reason why you are expecting maybe lower transmission to happen, is that a reason why growth could be lower or is it the risk aversion within the banks as you had mentioned. How do you expect this growth to happen?

Dr. D. Subbarao I have looked at the numbers for translating that 5.7% growth to M3 growth. That you must have done the arithmetic- that tallies right-13%. Credit growth is 15%. As far as I know a 2% is differential between M3 growth. M3 growth plus 1 is deposit growth and deposit growth plus 1 is credit growth. That has been the standard pattern and when I checked with our staff they said yes, structurally nothing has changed, we can go along with that, with 1% point differential between these three.

Gopika The GDP is higher and credit growth rate is lower.

Dr. K.C. Chakrabarty No, there is reason for that. When the economy does not do well, the many credit is for the restructuring being the receivable is accumulating, when the economy starts doing well even a lower credit growth can give the higher growth, it all depends. Credit is not always productive. So it depends, how you utilize the credit that is more important, so even with lower credit growth you can have a higher growth and higher credit growth may not give you the growth always.

Shri Deepak Mohanty Just to add, the credit growth in real terms is high because inflation is high, that is what matters.

Parnika This is Parnika from DNA. Basically how will today's rate cut actually help? What will be the practical impact? You have given us the consideration what was the reason behind the rate cut. But what will be the impact, what will be the outcome of this rate cut, because bankers' didn't really give any indication of any scope of any transmission as of now.

Dr. D. Subbarao Our expectation is that even if there is no transmission immediately, transmission will take place in the next 3 to 4 months and that will generate demand for credit and that growth will thereby improve to 5.7% at least.

Parnika Sir, this is the third rate cut in a row, you are actually expecting the cumulative effect?

Dr. D. Subbarao That is correct.

Ruchira I have two questions for you. One is the projected WPI for 2013-14 is 5.5% and you are saying RBI will do everything in its bid to bring it to the threshold level of 5%. So has RBI begun resorting to inflation targeting in any manner. The other question I have is what is the need for basically differentiated banking license policy for the foreign banks as you have mentioned in the statement today?

Dr. D. Subbarao For investment banks or for foreign banks?

Parnika For foreign banks.

Dr. D. Subbarao On the first question, on inflation targeting, no we are not inflation targeting Central Bank and I don't think we should be. I don't think even the FSLRC has said that we should be an inflation targeting central bank. In fact, pure inflation targeters are now shifting to moving away from inflation targeting. 5% is an inflation objective, that I believe is the threshold level of inflation. Deepak Mohanty and others have done a study which shows that 5% is the threshold. Above 5% inflation is decidedly inimical to growth, below 5% inflation may be positive for growth but that is not certain. So 5% is our inflation objective; that is not to say that we are an inflation targeting central bank.

Shri Anand Sinha On differentiated licensing for foreign banks, I don't know how you got that impression. We have not talked about differentiated license for foreign banks per se. What we have talked about is- today the license which is given is of one kind only that is basically it has to be a retail bank and over and above that you can build up your own niche; the banks are free to do. Now one question that we have raised is, it is time for us to think in terms of investment banks, whether they are foreign or Indian.

Anoop This is Anoop Roy from Mint. You have mentioned some risk factors that if they materialise your policy action can go either ways. At the same time you are saying that the transmission of your monetary policy will happen may be after 6 months. What if in 6 months in a dynamic situation things go awry and you actually start hiking rates. Where is the scope of transmission then and the time comes when banks are comfortable to pass on the rate?

Dr. D. Subbarao If we go in the opposite direction as you are hypothesizing, you would expect that transmission to take place. I have no substantive answer to what you are saying, but we do hope that whatever we do would transmit. That is the expectation of a central bank. And not only do we reduce the rate, but we will also do whatever necessary to hide transmission take place, like for example the liquidity management.

Dr. Urjit R. Patel Can I add? One mechanism through which you would get transmission is when inflation stays low because then banks will be confident that they can reduce their nominal deposit rates. So I think that also needs to be built on into how the transmission and when it will occur. As banks gain confidence that the inflation rate is going to stay at this level or even lower and therefore they can confidently lower their deposit rates, so you will get a transmission kick from there also.

Shagun This is Shagun from Reuters. I have two questions, one is you have done many sets of easing but that has not actually led to another transmission. So how much are you sure that this specific rate will lead to transmission and don't you think because it was time for a more radical action on that and secondly with the gold prices falling has the RBI bought gold or will the RBI buy gold if the prices are falling further?

Dr. D. Subbarao On the first question, I believe the baby steps have transmitted. So I do not agree with the premise so I cannot have an answer to your question. But to the second part of the first question about why we are not more radical, because we believe that we should not be more radical than this. On the second question, now gold purchase, foreign exchange purchase and sale and all are questions that are not in the public domain in the real time.

Dr. Urijit R. Patel For all the reasons that have been cited and risk factors in the guidance makes it amply clear why we could not be more radical.

Kavita Follow on question on gold. The policy document says that you are looking at guidelines for NBFCs, but a lot of banks also lend against gold. So will there be any guidelines that you will be prescribing for banks as well?

Shri Anand Sinha What we have done for NBFCs was in a different context. It was in the context that there were lot of consumer complaints and the expansion was too rapid, so we were worried about the health of those NBFCs. It was done in that context, not in the context of managing risk from a different perspective. That has not been there as far as banks are concerned. We are not stipulating this and now that the gold prices have come down, we certainly believe and hope that banks will take care of their own limits, whatever they be. That is why there is no regulatory prescription; the regulatory prescription is basically to cancel the imports as it were and also not to allow financing against speculative gold.

Megha Just wanted to ask about the probe report on money laundering charges, will it be made public?

Dr. K.C. Chakrabarty No, none of the Reserve Bank report will be made public, in fact it is not for public discussion. Yes, if based on that we take action against banks, once the action is taken it will be declared on the website of the Reserve Bank of India and corrective measures, policy measures whichever comes through the policy other thing, that will be disseminated.

Dr. D. Subbarao You have to wait for *Memoirs of Dr. Chakrabarty*.

Participant We have been hearing that Cobra-post is issuing another.. (Inaudible).. on Monday. Has the Reserve Bank heard about it, have they contacted you, are you aware of it. Apparently it is a bigger sting as compared to what they have done last time?

Dr. K.C. Chakrabarty See our action is not based on Cobra-Post our action is based on our investigation. Other things whatever happened we see as you say whatever happens in the media, we are not insensitive to that and this is a thing, but our action has to be based on our investigation and what the conclusion we arrive at.

Dhruv When will the government finalize the mechanism for inflation indexed bonds? Government officials said that they are going to issue sometime this month.

Shri H..R. Khan We expect it soon.

Dr. D. Subbarao I know the government says RBI is working on it and RBI says it is discussing with the government. This has been going on for some time, but I think we worked on it with great sense of purpose this time and the greater determination than in the past and as Mr. Khan have told you we tried to fix the problems of last time. Hopefully we will launch it soon. Now that the inflation has come down and is trending down, government should be more confident about this. Because there was some concern about the wedge between the yields of the G-Sec and IIBs and that has to be corrected and they were some concerns about how we will manage that and how the market might interpret it. So at that point of time when we do the IIBs, all of you analysts and journalists have to do a lot of homework for interpreting that carefully and disseminating that carefully.

Participant Inflation indexed bonds was first mentioned in the early nineties.

Dr. D. Subbarao I know, but I think we did that after that and learnt some lessons from that experience. Yes I remember that we were talking about that even here. In the last 5 years I have been here, first the crisis then the inflation has been high which was not seen as an opportune time for IIBs. We may link to WPI.

Aparna Sometime back in an answer to Lata you said that interest rates are not the only tool that you will use if you have to bring down the inflation, communication is one of them. Over the last several policy statements, you have cut the repo rate but the accompanying statement is considered very hawkish by the market. Is it not that you are already using the communication tool?

Dr. D. Subbarao One of the things that we pay attention to and I particularly pay attention to is how the market is interpreting our stance. When we write something in English, how do they interpret that as hawkish and dovish and it is a matter of judgment. But since you people are influential and you command a vast audience, what you say becomes very influential. But we try to manage our communication in such a way as to be consistent and to get the results that they want. If in the past, we found that there were some inconsistencies between our expectations and our language, if there were some inconsistency between two documents that we release at the time of the policy, that is unintended and we will try to fix that.

Saraswati Just wanted to check with you, in the statement you have talked about how in terms of banks acting as agents for products like mutual fund and insurance. So you said that there will be guidelines which will be coming in by June... Bancassurance….(inaudible) You have expressed concerns about banks being exposed to reputational risks if they sell insurance products. Will this be a combination of all the guidelines or will that be a separate thing?

Dr. K.C. Chakrabarty We have concerns about the banks selling insurance product, where they are giving incentives. That is the first concern, that should not be there. That will distort pricing. Other guidelines will happen, that what is the risk on the bank, other things that we have to discuss with other regulators, alone we will not be able to decide. If you see that incentive part we are trying to see, if there is mis-selling we are trying to see that, and the third one is the KYC. That up till now what was happening, if he is not a customer of the bank and is purchasing insurance product, we are not applying the same KYC standard. Now today we are saying that if you are purchasing an insurance product or mutual fund product or any other product, same standard of KYCs should be applicable. So we are only at present trying to do what is within our regulatory purview. Then we have to discuss it with other people and see the broader perspective. Bancassurance, in fact many people are not aware what is bancassurance. Banks selling the insurance product in the agency model does not become bancassurance. If the banks are selling these products as an additional product to their customer in a normal way of business, then only it becomes bancassurance. So we have to correct those definitions, those things which is a much broader perspective, in the FSDC those need to be discussed. We are making a study on that and they will come, but it is only which is within our regulatory purview.

Lata You have not stopped them from taking cash to sell gold or wealth management products?

Dr. K.C. Chakrabarty I am again telling you cash getting is no problem, you report it. Problem is that they must understand, it is no problem in making the cash, cash you have report it. Why the person is breaking it into less than 50000, he will be caught. You have to report it to a suspicious activity if someone is putting so much cash, you can write to economic intelligence agency, but if it is normal money, then it is nothing wrong.

Lata What are your objections to making all cash in investment products? You are not thinking on those lines?

Shri Anand Sinha On gold let me clarify there is a limit of Rs. 50,000 for cash transaction. On KYC also let me clarify, all these products which banks are selling, they are selling as agents. Now principals are somebody else and therefore as agents in a very legalistic sense, they are not really responsible for KYC. What they have to do is to collect the documents and send it to the principal. But what now we are saying is that banks being a large conduit for this kind of transaction and have severe reputation risk. So we are saying that even if you are an agent you have to do the KYC.

Dr. D. Subbarao Thank you. I also want to say that you keep us on our toes.

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