“Reserve Bank of India Post Policy Conference Call for the Media”

July 30, 2013

Participants from Reserve Bank of India:
Dr. D. Subbarao – Governor
Dr. K.C. Chakrabarty – Deputy Governor
Shri H.R. Khan – Deputy Governor
Shri Anand Sinha – Deputy Governor
Dr. Urjit Patel – Deputy Governor

Moderator:
Ms. Alpana Killawala – Chief General Manager, Department of Communication

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 ask questions at the end of today's presentation. Should you need assistance during the conference call you may signal for an operator by pressing '*' and then '0' on your touchtone telephone. Please note this conference is being recorded. Participants connected to the audio conference bridge may press '*' and '1' to ask a question. Participants present in the room are requested to use the mike while asking questions. 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: Thank you Lavina. I won't really stand between you and the Governor. So, Governor.

Dr. D. Subbarao: Thank you very much. Once again welcome to this post policy press conference. Those of you who are keeping count, as I know you all are, this is my twentieth. You have all seen the statement and read about it and analysed it already, but just so that we warm up I want to give a synopsis of the statement this morning.

We kept all rates unchanged – repo rate, reverse repo rate, CRR; the MSF rate too stays at 10.25% with effect from 15th of July. The considerations behind today's policy were two; the first was from the external sector, we wanted to be prepared for all external sector developments and to be able to respond to them. The second consideration was the balance between growth decelerating and risks to inflation remaining present.

I will come back to guidance shortly but first I will make a short comment on the global developments. Global growth has been uneven and slower than we thought it might be when we met in May. The IMF has since come out with their WEO and they have said that growth this year 2013 is going to be 3.1%, down from 3.3% earlier. So instead of a multi-speed recovery what we have is a multi-speed slowing across all segments of the global economy. At the G20 Meeting in Moscow, about 10 days ago, there was realization that global growth is slowing down, that the risks to downside growth have been contained but those risks still remain elevated.

As far as domestic economy is concerned, the silver lining is the monsoon. Both spatial and temporal distribution of rainfall so far has been very good, and rain fall has been above the long period average except for some pockets in East and the Northeast. However, other sectors of the economy, both industry and the services are a cause of concern. We expected that they would be sluggish when we came out to make statement but the performance so far has been somewhat inferior to that. So keeping all that in view, we revised the growth forecast downwards, growth projections downwards from 5.7% to 5.5% for the current fiscal year. On inflation, Wholesale Price Index inflation has come down below 5% but retail inflation remains high. WPI inflation has edged up in June, largely because of food, especially inflation in vegetables and cereals. Fuel price inflation has declined due to reduction in coal prices in March and easing of inflation in electricity because of the base effects. In the May policy we said that we will endeavour to keep inflation for the current year at 5.5%, in that range, although there will be some edging down in the first half and edging up in the second half and the performance of inflation so far has been along the trajectory. And the Reserve Bank will endeavour to maintain an environment for inflation at a level of about 5% by March 2014.

There are risks to inflation. By far the biggest risk is the depreciation of the currency because there will be pass-through from imports, there will be increased under-recoveries as a consequence of that, and there will be passing off from producers to consumers. In spite of low demands, the concern is that producers might pass on higher prices to consumers. I was quite disturbed to see the latest analysis of the Reserve Bank shows that the pass-through has increased- for every 10% depreciation, the inflation is 1.2% as against the number of 1.1% earlier.

The second risk factor is global oil prices, which has not softened as much as other commodity prices; I am talking about global prices. Although the IMF and World Bank have said that oil prices will remain soft this year, there is a concern that that projection may not come true largely because of political considerations and the situation in the Middle East.

The third risk factor is fiscal deficit. The Finance Minister has said repeatedly that he will remain committed to 4.8% as indicated in the budget, but because of GDP performance, tax revenue accruals, expenditure performance, that all estimates the risk for inflation.

We have indicated the risk factors to the macroeconomic situation. I will just list them very quickly. The first risk factor is the external situation arising from the sudden stop and reversal of capital flows as we have seen in India over the last 10 weeks starting May 22. One big uncertainty is, it is not clear if financial markets have fully factored in the full impact of the prospective tapering of QE or whether there will be at every time there is some announcement.

The second risk factor is the high current account deficit above the sustainable level of 2.5%. Most external sector vulnerability indicators have deteriorated indicating that the economy’s resilience to shocks is eroded. The current account deficit, the level at which it is reinforces the importance of a credible fiscal adjustment both in terms of quantum and quality of adjustment**.**

The third risk factor is the weak investment climate for a number of reasons that we have listed in the document.

And the fourth risk factor is supply constraints. India is very unique in the world in the sense that we are a supply constrained economy and the biggest supply constraints are food and infrastructure both of which are putting pressure on growth and on inflation and its very important that those supply constraints are addressed at the earliest.

I now want to anticipate some questions as per standard practice and answer them and it is not so much because it is a standard practice but more than ever before I feel obligated to respond to some questions even without your asking.

The first question is what is the rationale for our liquidity tightening measures over the last two weeks?

The current account deficit over the last three years has been above sustainable level. The rupee should have depreciated as a consequence of the high current account deficit. In other words depreciation is programmed into the rupee. That did not happen because we were able to finance the current account deficit and we were able to finance it because of extraordinary liquidity in the global system. Because of the large current account deficit and because of the way we financed it, we became vulnerable to the external outlook, we became vulnerable to global financial markets and we became vulnerable to the sudden stop and reversal of capital flows in the consequent destabilization of the exchange rate. The only unknown was when this might happen and in the event the vulnerability came sooner than everyone in the world expected. The rupee dropped from 57 to 61 in a matter of four weeks without any change in our fundamentals. There was 5.8% depreciation between May 22, the day of the first announcement effect and July 26th the last Friday. This rapid depreciation of the currency put us into a vicious spiral amplifying unidirectional movements and encouraging a herding instinct. On top of the rupee movement there was very comfortable liquidity in the system. On July 5 LAF went into a reverse repo mode briefly. The easy liquidity provided a fertile ground for speculation on the exchange rate which exacerbated vulnerability. And we were having a meeting with our technical advisory committee last week. One of the members said what is vulnerability? Vulnerability is if something goes wrong then suddenly a lot goes wrong very quickly. That’s what happened to our system. So we determined that this volatility in the exchange rate is hurtful to the economy for a number of reasons. First, there is hysteresis in exchange rate. If it overshoots it may not come back to the original levels, it stays there, so it is very important for us to see that the adjustment took place along in line with fundamentals.

Second, rapid depreciation of volatility in exchange rate would affect the balance sheets of banks, corporates and even households. And of course volatility hurts growth in a larger sense. Forex intervention is a standard tool for defending against volatility. As much as we resorted to that instrument we were also conscious that whatever we did should not fuel speculation or should not help speculators. The first line of defence against excessive exchange rate volatility is monetary policy instruments and that is what we did. Once again I want to say that we were not altering the fundamental path of the exchange rate. Our action was informed entirely by the need to curb volatility and disorderly movement. So that is the first question about why we did this.

The second question is about when and how we might roll them back. That we tried to answer in the guidance today and you have all commented on that. I want to annotate that guidance.

First very briefly, the one sentence we wrote in the guidance, I quote "The recent liquidity tightening measures by the Reserve Bank are aimed at checking undue volatility in the foreign exchange market and will be rolled back in a calibrated manner as stability is restored to the foreign exchange market, enabling monetary policy to revert to supporting growth with continuing vigil on inflation". That is a mouthful but that is what it is. We did not use the word 'temporary' advisedly because temporary would mean different things for different people and you would pressure us to define what temporary was and we were not in a position to define what temporary was. So in the event we determined that it might create more confusion than throw light. So advisedly we did not use the word 'temporary.' The roll back of the measures will be state contingent and data dependent, and linked to decline in volatility and disorderly movements in the exchange rate. Some of the indicators we will look at will be the bid ask spread, the intra-day volatility in the exchange rate, volumes of forward contracts to evaluate importers assessment of stability in the exchange rate, and open interest positions in the currency futures market, the options pricing, the forward premia, a number of other indicators, I am just giving you a sampling of indicators to give you a flavour of the nature and dimension of the problem we have which is that we are going to look at a number of indicators that determine if volatility in the exchange rate has been contained.

We will also make an assessment of the global markets. It is not just indicator, of course our indicators in part reflect global markets but we will also look at the global markets and see how vulnerable they remain to further announcement effects or indeed some action following announcements.

There has been a lot of speculation in the market about whether Reserve Bank is targeting an exchange rate. Once again I want to say that, that speculation is completely misinformed. We are not defending any exchange rate target and not altering the movement the exchange rate according to fundamentals.

Just note that the rupee depreciated from 47.4 in 2009-10 to 54.45 in 2012-13 and we did not stand in the way of rupee finding that level as it depreciated except to manage volatility. So what the Reserve Bank wants is reduced volatility and orderly adjustment of the exchange rate to its market level.

Finally, I want to say that the Reserve Bank is sensitive to the short term costs of tight liquidity measures on economic activity. And we are as anxious as everyone else to roll this back but getting locked into a timeframe is both infeasible and inadvisable. Thank you very much.

Alpana Killawala: As always, Latha.

Latha: Sir, Latha Venkatesh from CNBC. After the policy was announced it was read as dovish because you have said that but for the foreign exchange market volatility the falling inflation would have given you a chance for lowering, quite different from what you said earlier that you have little space for further monetary easing. Now because of that, it probably has had negative impact on the rupee that is now at 60.13, so it actually has weakened believing that your resolve to be too tight is not all that pronounced. Also, of course there has been concomitant fall in bond and stock prices. So has the market read you wrong, did you intend to sound dovish?

Dr. D. Subbarao: We do not make a determination about whether we want to sound dovish or sound hawkish. Now in the last five years that I have been in the Reserve Bank we did not start with the determination first and then fill in the language. Actually the language comes from a lot of analysis and the stance the way the analyst read it becomes a by-product of all that. Second, you said Rs.60.13 or whatever is the current level, we are not targeting a level once again. So if the rupee is adjusting gradually that is the way it should be. But I want to say that we remain committed to curbing volatility in the exchange rate. As far as the broader monetary policy stance is concerned, correct, we said in the policy that there would have been reasonable argument for further easing because growth has moderated more than we thought; inflation has ebbed, I would not say more than we thought, but the prognosis going forward is not as uncomfortable as before as much as there are risk factors. So that is the reason behind language there that there would have been a case for monetary policy easing but for the external sector concerns. In fact, I would have liked it to be having been read as the importance that the Reserve Bank is attaching to containing volatility in exchange rate.

Latha: Now that the rupee has depreciated further, should we expect that you could probably want tightening steps?

Dr. D. Subbarao: I cannot really commit to that and it is not so much depreciation per se, it is the volatility that we have been looking at. So the level is not what you should be looking at. If I say at 60.13 we are intervening or we are doing tighter measures, it means that we are targeting an exchange rate, which we are not. So we will be looking at the volatility, the two-way movement in the exchange rate and indeed the one-way movement as well.

Aniruddha: Governor, Aniruddha from ET Now I just like to understand the first thing there has been a lot of criticism of late ever since you took your actions on the 15th of July, from bankers from market participants as well. So I would just like to understand whether it did cross your mind that you could straightaway either tighten the CRR or repo rate, was that an option? And secondly, if you could give us somewhat of a timeframe as to how long the RBI would be comfortable with banks kind of passing on the impact of this kind of tightening which they are facing at this point in time?

Dr. D. Subbarao: Thank you, Aniruddha. First of all, criticism is part of the course, okay. We are a public policy institution, we make policies that affect economy and everybody is welcome and entitled to criticism and we learn from that, as I have said that many times before. But your most substantive question, yes, certainly it did cross our mind about what other measures we could be taking - CRR, repo rate hike and OMOs and whatever. Advisedly, we did not touch the repo rate or CRR and we determined that tightening liquidity by the measures we adopted by adjusting LAF and raising the MSF rate and by some open market operations is the best prescription for containing rupee volatility. The idea was to make liquidity scarcer and more costly. So we determined that modulating access to LAF would be the most efficient way of controlling volatility. And we determined that if we do this it can be calibrated more flexibly rather than distorting the CRR or the repo rate, because there are other implications attached to those measures. As far as banks responding by raising their rates, yes, they will always have correction, but transmission will take place in a way that is not advisable. But we are also aware that there is some cushion for the banks. When we reduced rates over the last one year, transmission has been less than commensurate with that and we have been saying that transmission is still in progress. So I believe there is cushion available to the banks and they can perform without raising lending rates.

Ira: Governor, Ira from Financial Express. You said your first line of defence is monetary policy. This time around you had the buffer because liquidity wash easy, credit growth was low so you could have tightened liquidity. Now do you feel that you have room on the traditional monetary policy instruments should the currency not stabilize, and then what is the second line of defence? Are we talking about capital management measures, are those even on the anvil? And there is a part B to it, you are saying you want structural measures given that you got a little temporary breather with the RBI's measures. What structural measures Sir? Export, imports, these are not things that will adjust over 3 to 6 months. Are you talking more about a sovereign bond, or something about reserves? What do you have in mind Sir?

Dr. D. Subbarao: Thank you very much. I cannot really speculate on what other measures we might take should this problem persist. All of us including you hope that this problem will be contained and the measures we have taken now are adequate for that purpose. But should this problem take a different turn we will have to diagnose that depending on the circumstances. It will be both inadvisable and difficult for me to really say what measures we will take but I want you to be assured that there is enough arsenal with the Reserve Bank to contain volatility in exchange rate. On the second question about structural measures, we were talking about structural measures to contain the current account deficit, not so much measures to finance the current account deficit. Of course that is an issue on which both the government and the Reserve Bank are in consultation, we are engaged in a discussion. But when we talked about structural measures in policy document, it is the structural measures to contain current account deficit. You are right that these measures cannot be taken overnight or even if measures are taken, they will take a long time and that they will also depend on the external situation. But I believe that signalling that the government is taking measures to encourage exports, boost exports, and containing imports by some domestic policies I think will be a very important signal to contain the volatility in exchange rate. Because what we have done is actually to find some space for a more durable adjustment and that space must be constructively used.

Ira: Just a follow up, Governor. Does the Central Bank have a formal view on the timing or the possibility of a sovereign bond? There has been so much speculation, it will be nice to know if the central bank has a view on the timing or the feasibility.

Latha: And indeed whether you like a sovereign bond?

Dr. D. Subbarao: I will actually collapse the question into does the Reserve Bank support it or is in the Reserve Bank's view sovereign bond issue appropriate? We have reservations about that. We have done a cost benefit analysis of the sovereign bond issue. There are perceived benefits of bond issue which is that it will buffer your reserves, it will lower your interest rates, it will establish a benchmark for government borrowing and broaden the investor base. Those are standard text book arguments in favour of a sovereign bond issue, but there are costs. It will compromise our financial stability. There is a lot of value to be attached to government's borrowing in domestic markets. We have learnt that lesson during the global financial crisis; we are learning that lesson now. Those of you who have seen the latest Economist, which has talked about the great deceleration in emerging economies. One thing is that they have said that the emerging economies are not as unsafe as they would have been because their borrowing has been domestic. They said that in a different context, but we should interpret that in the correct sense to draw quite correct lessons. And when we really get a lower interest rate, the cost of sovereign bond issue is not clear if people factor in the exchange rate variation. So in the Reserve Bank's view, the costs of a sovereign bond issue, especially in the current juncture outweigh the benefits**.** We should be doing a sovereign bond issue, if at all, from a position of strength when we are much less vulnerable than at this time.

Parnika: Governor, this is Parnika from DNA. You said in the policy that these recent measures have been rupee-positive. So firstly, what kind of factors led to this conclusion, what data did you really look at? And secondly, in the past, we saw a lot of bond auctions being cancelled, the treasury bills was one of them, the OMOs volunteered did not yield good results and thirdly the weekly government borrowing was also impacted. In fact there was devolvement on primary dealers. And the next week RBI came and the T-Bill auctions that went on but you borrowed at 11%. So what kind of signals are you trying to register in the market?

Dr. D. Subbarao: On the first question, we have said volatility has been reduced, because if you just look at the volatility on a day to day basis, it has reduced, there has been some two-way movement, rupee went above, better than 58 for a short while, so that was some early indication. But I would then refer to Urjit to give you a more considered answer on that. On the second question about our management of the roll over policy, the first policy was on the evening of July 15th, the second was on the evening of July 22, how did we manage that? The intent of the policy was to raise the cost of money at the short end of the yield curve. We were conscious that we were doing it abruptly. We were conscious that we were doing it in the middle of an important fortnight. So, first we wanted to leverage on the announcement impact. Just that the Reserve Bank has a resort to monetary policy measures to contain volatility has had a tremendous announcement effect, quite independent of how we manage the roll out. Then there was a T-bill auction on July 17, and OMO sales on July 18, G-Sec auction on July 19. We determined that the adjustment to tighten rates at the short end should be non-disruptive. We found that the T-bill bids were discontinuous with the market rates and some of the bids were higher than the CD and CPs of that day. So, we determined that our adjustment would be too discrete, too discontinuous. As much as wanted the adjustment, we wanted a smooth continuous adjustment. It is true that banks had drawn Rs. 200,000 on July 16, when there was a one day window to adjust for CRR over the fortnight, but remember they had given it back to us the next day, so that accommodation was for one day. We also found that not this week, not last week, but week before last week, I am talking about July 17, 18, 19, there were some sort of uninformed reports of panic reaction in the market. So we wanted to calm the markets as much as we wanted the yield curve to move, we wanted that to move in a non-disruptive way and I believe our attempt was to navigate that non-disruptive movement. Whether we have succeeded or not is for you to write about. Urjit.

Dr. Urjit Patel: The effectiveness of the measures that we undertook this month in two or three phases was more in the way of a process rather than events, and we believe that we have achieved some success. For one, the unidirectional fall in the exchange rate has been checked, especially if you look at the data post 9th July. The intraday volatility which is the range between the high and low during the day has declined from about 90 paise on July 9th to an average of about 48 paise post July 16th. The cancellation of forward purchase contracts increased from a daily average of about $0.5 billion in the first half of July to a daily average of about $800 million since July 16th which would imply that importers cancelled forward, buying on perception of exchange rate stabilizing in the near future. And the volumes in open interest position in the currency future markets have also declined. And it is interesting that even both the domestic and offshore NDF markets have converged in terms of one month forward premia. So I think that is a fair bit of evidence in this regard. Of course there are other things happening in the world at the same time and it is almost impossible to bifurcate and decode those other events but I think this is a fair bit of hard data there. Thank you.

Govardhan: This is Govardhan from Economic Times. You had said that you would not be standing in the way of rupee depreciation; at the same time as a monetary measure you did not touch the repo rate. Does it indicate that the RBI is more for exchange rate to settle the macroeconomic imbalances than the interest rates?

Dr. D. Subbarao: No, I do not think that conclusion or inference would be appropriate. We would use all economic variables, both the interest rate and exchange rate for macroeconomic stability, economic growth, inflation management, and external sector management. Yesterday, one of our advisors was telling me that you cannot treat them independently, they are interlinked. Indeed he wrote me a long note, which I have not observed fully but the substance of that is that you cannot delink the exchange rate from the interest rate, they are both linked. Also I want to say that we have to find structural solutions to current account deficit problem, meanwhile we have to find financing for the current account deficit as much as it exists. There are sovereign bond issues, one option about which you asked me. But there are other ways of financing the current account deficit. So the Reserve Bank is interested in long term stable flows for financing the current account deficit.

Govardhan: Sir, a follow-up to that. You mentioned about current account deficit being the problem for the rupee deprecation, at the same time there was this kind of hint about the short term measures, which could be temporary. Of course, you did not use the word, calibrated, so either the assumption is that current account deficit is going to get corrected soon or these measures are going to remain for a longer time, so which was that?

Dr. D. Subbarao: I do not want to commit to an answer to that. We hope and expect that the current account deficit will adjust, but whether current account deficit will adjust first or we will find financing or we will roll back these measures first, it is difficult to say.

Bijoy: Sir, Bijoy from Cogencis here. Sir, yesterday in the Macroeconomic Report, you used the word temporary breather when you were referring to the relief that has come from your measures. Is that actually a reference to how long do you think that this relief can sustain or is it more with respect to the timeline. Also, on the corridor change that you have brought about, you have increased the MSF and Bank rate by 200 bps. Earlier there used to be fixed corridor of around 200 bps. Now that it has been increased to 400, is there now probably a corridor of uncertainty that it has opened up on the fact that the corridor itself can keep shifting?

Dr. D. Subbarao: Can you be more specific?

Bijoy: Earlier it was a fixed corridor. People knew that reverse repo would actually was 100 bps lower, and MSS and bank rate would be 100 bps higher. But now that you all have once touched the corridor is it likely that people can start to think that you can use the measure again in the future?

Dr. D. Subbarao: Okay, thank you. On the first question, 'temporary breather,' that word temporary was used like a 10th class student would use. As an adjective to qualify breather, and I do not think you should read from that any inference about whether these measures are short term, long term, whether they will be with us for months, weeks or days, etc., I do not think that would be the right direction to go. Please read temporary exactly as you would read if you were not an economic analyst. Second, about the corridor, yes, the corridor has widened to 400 points. One of the first lessons I learnt in the Reserve Bank was that the width of the corridor signifies level of certainty, right. So we reduced the corridor and sometime during my governorship we had also said that we will honour a fixed corridor of 100 basis points or 200 between the MSF and the reverse repo rate. Now that we have moved it, it certainly signifies that uncertainty has increased. Whether we will make the corridor very variable is uncertain, but we will be loath to do that. We want to respect the width of the corridor as much as possible.

Ritesh: Governor, Ritesh from Zee Business. Governor, over the last few policies you had, in most of the policies inflation dominated the policy decision, in one or two policies you were moving towards growth, now it has moved towards currency. So what will prompt RBI or give RBI the signal that now is the time to take steps because on the other hand you have also revised the growth projections and it is not likely to improve anytime soon as all other agencies have also revised. Secondly, you had said that the monsoon, in your initially remark you had said monsoon is the silver lining. But at the same time in your policy document you also said that better than expected monsoon has not yielded results on the food inflation front. So why do you think and where do think the problem is that it is not yielding results on the food inflation front?

Dr.D. Subbarao: Thank you for those questions, in fact I was looking forward to that question about growth, inflation and external sector stability. The Reserve Bank is committed to all those three objectives. Growth, price stability and financial stability, which in our context today is external stability. The challenge for us, every time we make policy is to balance between those three objectives. We are very anxious that monetary policy must revert to supporting growth, that is why we have used the phrase "enabling monetary policy stance to revert to supporting growth" We want to do that as much as anyone else, and we are hoping that certainly the situation will revert to normal so that Reserve Bank can support growth. Now that Wholesale Price Index inflation has ebbed and growth has moderated there is a reasonable case, in fact, there is quite a strong case for monetary policy to support growth. It is not just now; all along the Reserve Bank maintains a strong commitment to supporting growth. But within an environment of price stability and financial stability because those are necessary conditions for steady and accelerated growth. On the second question about monsoon being a silver lining and still food inflation being higher, we would expect that since the monsoon is good, robust and in anticipation of a bumper crop, prices would soften. I understand from our analysts that prices have not softened as much as they should have, because of some distribution problems, weather-related distribution problems, in vegetables and cereals. So, if we should take care of this, I expect that even the retail inflation can come down. In other words, at least a part of our inflation problem is not a problem of production, but a problem of distribution. I used to live in Africa, and in Africa one of the big problems is not production, it is the distribution that causes all the distress, we are experiencing part of that.

Ritesh: Do you believe food security bill can cause a problem that because a lot of this production will go to the government companies or government agencies?

Dr. D. Subbarao: Food security bill implications, the quantitative implications of the Food Security Bill are still being analysed. In the Reserve Bank we have to analyse ourselves, we depend on a lot of studies that are coming from outside. Studies so far show that there may not be a significant increase in the amount of food to be procured even after the Food Security Bill if the coverage of 67% of the population and the quantity is a 5 kg per person per month or whatever the parameters there. However, should those calculations be taken, certainly there will be pressure on procurement, there will be pressure on subsidy, there will be pressure on fiscal deficit that will have implications for growth and for inflation. There will be implications for the surplus income that the beneficiaries of food security might have and how much they might spend that, and what implications that will have for inflation. So there is going to be lots of economic consequences of the Food Security Bill which in the Reserve Bank would study further, but after that somewhat incoherent reply let me turn to either Urjit or Deepak or anyone who has got to add anything to that.

Dr. Urjit Patel: I think it is correct to say that at the moment the fiscal consequences and therefore the macroeconomic backdrop that will change on account of the Food Security Bill is a bit premature to discuss because the numbers are still being worked out in terms of the marginal change that this will require in the system and therefore in terms of higher expenditure. And at the moment we do not have anything more to add other than what the government has said regarding the increase in cost this year or part of the year.

Pradeep Pandya: Pradeep Pandya from CNBC Awaaz. In yesterday's Macroeconomic report and today's policy statement, you have referred to Fed many times, you have referred to quantitative easing, that is unprecedented, from all the policies for the last several years that I remember. The question I want to ask you, these temporary or not so temporary measures, how long will they last? Will the answer to that actually come from Fed or Ben Bernanke? Have you ever visualised such a scenario. Say if from September the rollback of QE will actually commence, what measures will you take? Or if this is deferred till December or even further, will your job become easier?

Dr. D. Subbarao: Urjit says, that he will answer that but, I just want to tell you a story. In one of the BASEL meetings, one of the emerging economy governors asked Chairman Bernanke, that "Look, when we make our policy, we write about global economy, what is the American Fed going to do, what is the ECB going to do, what is the Bank of Japan going to do. And we analyse a lot of what you are doing, you will do, you said, you will say, and you look at our document and there is a lot about that. When you make your policy do you ever think of us?" So, this is true, that developments over the last 10 days has made have been a consequence of the announcement effect of the US Fed. It is because of the Fed we are talking about. Maybe in 3 months from now, 6 months from now, we will be talking about the ECB, or the Bank of England, or the Bank of Japan. The important thing is that what systemically important countries do have an impact on the emerging economies like India as much as we are integrating into the world. And one of the challenges for us is to be able to better understand global trends and to be able to adjust to them better.

Pradeep Pandya: But for that statement, you think things would have been completely different. I mean, you would have been talking in a very different context.

Dr. D. Subbarao: Yes, we have said that in our document. But for that statement, that is a hypothetical question, it is another world; yes, it would have been different certainly.

Dr. Urjit Patel: I think the important variable entities and an uncertain variable is that how much of the re-pricing in the international bond prices has already happened and how much is left. There has been a significant firming up of yields in the US, 60-70 basis points, that is large. So, many people, though not all, say that a fair bit of this has already been internalized by the market given the May and June guidance that was given by Chairman Bernanke. However, there is likely to be some residual effect whenever the actual taper starts and eventually shuts down. It is important to remember that everyone knows what the quantity involved is, and you now have a fair indication on the month that it may start. Of course it is a contingent guidance and you have some guidance on when it will end. So fair bit of this information is already there within the market and I would suspect that much of the bond pricing changes that were required may have happened. But I could be wrong; there are some who say this is the case, some who say it is not the case.

Pradeep Pandya: One corollary would be that probably that there will not be further selling in Indian bond market from FIIs if you think a lot of re-pricing has already happened in US?

Dr. Urjit Patel: We would have to see what happens going forward. As you know there is a news flow every month from the US, which is part of the contingent information that would determine this.

Krishna: There is a talk in hushed voices in Delhi circles that India might be in a situation to approach IMF for a loan. Do you think the BOP situation is going to that extent that the situation might actually arise?

Dr. D. Subbarao: The answer is no. I do not believe that we are in a situation where we have to go to the IMF, we are fairly resilient.

Saraswati: Sir, what I understand the bankers were telling us that they have made some suggestions in terms of dollar refinance window. Is the RBI willing to consider those measures?

Dr. D. Subbarao: The bankers have made several requests, several suggestions including resuming the dollar refinance window. We will examine that but there is no commitment as of now about whether we might reopen that.

Anup: Governor, Anup here from Mint. The market is talking about and a lot of analysts are also saying that whatever measures you took in the last two, three months there was some kind of panic reaction to it. People are saying that Reserve Bank is acting in a panicky manner. So, just one simple question: was that a panic reaction or was that a well thought out plan?

Dr. D. Subbarao: I would request you to please find an answer to that question. It will be difficult for me to answer it.

Mayur: If the intention of the measures that were taken last month were to drain out liquidity and curb speculation. Does not the statement that these measures are temporary and there will not be any transmission sort of dilute these measures and give an impression that these measures can continue for a long time thereby

Dr. D. Subbarao: I did not understand the question. What are you saying?

Mayur: The fact that you have reduced liquidity curb speculation, but at the same time there is an impression given that these measures will be only temporary and that there will not be any transmission, thereby implying that these measures are temporary.

Latha: Can I supplement Sir? My question was similar, that is why. The charge against the Reserve Bank over the last two weeks has been that it is vacillating too much. You announce something on July 15th and then you reject so many auctions giving the impression that you are not serious and that it is also scared of repercussion. You announce again on 23rd and it looks like you are very serious and then the note of dovishness comes into the current statement; whether you intend it or not it is read as dovish and immediately the rupee reacts. The charge is that the Reserve Bank is not going all out to protect the rupee with the tightening steps, in the process it will only have to do this tightening for longer and harder.

Dr. D. Subbarao: I do not agree with those charges. As I said earlier, we have not used the word 'temporary,' very advisedly, because the Reserve Bank does not want to get locked into a timeframe on how long these measures might be necessary. We are determined to control volatility in the exchange rate. There will be consequences for this, there will be pain in the economy, somebody will have to pay a cost for this, those costs are inevitable and unavoidable. But, we will persist with these measures and implement them consistently in order to achieve the intended results. In the two weeks between 15th, 16th July and 26th of July, I explained in response to an earlier question, in response to Aniruddha's question that we wanted a non-disruptive adjustment to higher interest rates at the short end. And that has been happening and that is going to happen. Whether it will transmit to the long end is uncertain. As I said, it might well transmit, but our intention is to invert the yield curve such that short rates are higher, and the long rates stay where they are. That is good for the economy.

Mayur: The rupee today has moved again, crossed 60, it is at 60.35 right now. This appears to be sort of in response to the policy which seems to indicate that rates will come down in future.

Dr. D. Subbarao: Rates will come down in future, but not until such time as volatility in the exchange rate is contained.

Pradeep Pandya: Sir, Rs.1.60-70 paise in three days, that is the kind of volatility we have seen. Is it something you are comfortable with or you will act to it?

Dr. D. Subbarao: We are watching this, and we determine that if further measures are necessary, we will take that. It is difficult to say, when we will take them, and what measures they might be, but we are of course watching them.

Ruchira: Hello Governor, this is Ruchira from The Economic Times. We were told by the bankers that they have asked you to consider a reduction in the average daily holding of CRR from 99%, because they claim to say that all banks are holding in excess of 100% because failing to do that would lead to statutory failure. So will you be considering that, why or why not?

Dr. D. Subbarao: Let me turn to an experienced banker, our Deputy Governor Dr. Chakrabarty to answer that.

Dr. K. C. Chakrabarty: The idea of maintaining the CRR is that this has to be maintained on daily basis. If we have allowed them to maintain 70%, it is a historical perspective. Because when banks were not computerized, information was not available. Now that information is available, banks should not have any difficulty in maintaining the CRR on a daily basis. If they have a problem of outflow or inflow of the funds, they have to manage their clients. They cannot take over the job of the cash management of the clients on their own and in turn they pass on this benefit to Reserve Bank of India. That is our present thing. We feel that as of now 99% average maintenance of the CRR gives enough opportunity to the banks to meet the here and there deviations from the small customers. If the big customers are not behaving properly, then the cost has to be passed on to those customers. That is the issue, but CRR is a discipline. What we have prescribed, this must be maintained on a daily basis.

Ruchira: One follow-up question, you ruled out IMF, you have ruled out a sovereign bond issue. Then how do you think can this deficit of around $70 billion be bridged?

Dr. D. Subbarao: The entire $70 billion dollars is not a deficit, there are other avenues of capital flows and there are a number of other options that we are talking about, you know the full menu. Even sovereign bonds issue, I said the Reserve Bank has reservations because you asked me about the Reserve Bank's position. But we will be discussing with the government and all options on the table will be considered. But whatever we do should be in the best interest of long-term economic management, it should not be influenced just by a short term requirement.

Latha: Bankers mentioned that among other things that they have requested of you, if the tightness lasts for a longer period, they said that could HTM be brought back to 25% and could you give them a one-time provision for transfer cost from AFS to HTM and that too judiciously, in fact. Do you have anything to add on whether you are considering it?

Dr. D. Subbarao: They have made a number of requests as I have told you, and I have in fact a more complete list obviously of all the requests that they have made. We will be studying them, examining them, but it is not clear that we will agree to all or some of them. But over the next one month, Anand Sinha told me that we will be studying that.

Aparna: I had just had one last thing on the rupee if I can. This whole issue of speculation, what data does the RBI have to give us concrete evidence that there has been speculation. Is it on the onshore market, on the NDF market? How large was the speculation problem that you felt that you needed to actually. If it is from the NDF market, then how is the RBI going to tackle that?

Shri H. R. Khan Speculation can be existing, speculation can be potential. When there is a one-way movement people take a hedge. There are pockets where people can speculate, particularly corporates can speculate because everything they do not hedge. There is an opportunity, there is a view, then we have these days currency futures also. So there are pockets of speculation, existing and potential.

Dr. D. Subbarao: I want to add, speculation is a legitimate economic activity, and it adds value. It is undue speculation that we are against. It is speculation triggered by very comfortable liquidity that has been damaging in the short term. That is what we are trying to curb. It is not that the Reserve Bank is against speculation per se.

Ruchira: But does the RBI monitor the NDF market as a part of the exchange rate monitoring at all. And considering that the RBI does not have a direct control on the NDF market, in the off-shore, will it dilute or endanger the impact of your measures eventually on the exchange rate?

Dr. D. Subbarao: Well, we monitor the NDF market. Not I, but there are lots of people in the Reserve Bank who monitor the NDF market and the existence of the NDF market has influenced our foreign exchange market, but has influenced much more in times of volatility such as this. It will be a better world for us if there is no NDF market, but we cannot wish it away.

Shri H. R. Khan Just to add, one thing which we are trying to do is, is in currency futures markets a lot of position taking was taking place, which we have curtailed, and month end there is going to be further reduction hopefully, if not, further measures could be taken. So, there is a connect between NDF market and futures market. If this market goes down, automatically the propensity to arbitrage between the two markets where there is no requirement of underlying will also go down.

Ruchira: But the easier way is to allow the FIIs hedge in the onshore currency futures market, so they don't have to go to the offshore market at all.

Shri H. R. Khan: All people do not go to offshore only for hedging. Most people do go not for hedging purpose, but for punting**.**

Gopika: Governor this is Gopika from CNBC. With your permission may I shift your attention a little bit to a boardroom battle going on, which is in one of the small private sector banks? Now this gains relevance because RBI is set to give licenses to new private sector banks and any sort of boardroom battle of such kind can cause reputation risk and also sort of put pressure on the stability of the banking system. So in this context are you looking into this particular case? I know it is a specific case, but are you looking into the boardroom battle that is going on in Yes Bank?

Anita: There is a supplementary question to that. You are also considering to give licenses to new banks. In all probability that could be that you will consider giving that to industrial houses as and when you do, whatever the decision. Would you look at segregating or not giving promoters or promoters holding executive roles on bank boards, like being the CEO or being the MD wherein there could be a conflict like it is there in the current scenario?

Shri Anand Sinha: As of now there is no prohibition on promoters taking executive jobs. As far as promoters are concerned you are also aware that in a bank ultimately the holding is brought down to a very low level. Today it is 10% barring some exceptional cases and in the case of new banking license 15%. Now this board room battle which is going on we are studying it and if we think that some measure needs to be taken on the issue as you have mentioned we will look into that.

Anita: In this context have you sought any information so far from the bank in terms of the progress of the case because it has gone to court and there have been many corporate governance issues been raised in the affidavit that has been filed and the courtroom process that has gone so far.

Shri Anand Sinha: It is not necessary for us to call for information. In any case we get all the information.

Pradeep Pandya: Sir the point being contested if the qualification of the director, would Reserve Bank be looking at kind of specifying what qualification a director should have to be appointed on a bank board.

Shri Anand Sinha: As far as BR Act is concerned it does specify certain qualification and then there are shareholder directors, so the norms are there, what qualification do you have in mind?

Gopika: In this case specifically one of the directors who was appointed was beyond that age limit.

Shri Anand Sinha: That is not correct. There is an age limit of 70 but it is not a very hard limit but it is generally observed. Now when he was appointed he was well short of 70. Some part of his term may go beyond 70 but it is not the same thing as being over 70 and he has been given approval only for 1 year.

Simran: Follow up on what just Gopika asked. Like she just said that as far as the qualification is concerned what I really meant was educational qualification or the work experience and a bit like that because that is the main crux of the fight here. Because one of the reasons as to why she is not been qualified to be on the board is maybe they are not very happy with the work experience or the years or work experience or qualification, so is that it?

Shri Anand Sinha: As I said as far as we are concerned the qualifications are laid down in the BR Act, that is related to specialization. Here from what I can make out from the newspaper report is that the board seems to be feel that the candidate is not of the same level as others and that is their perception we don't come into play.

Virendra S. Rawat: This is Virendra Singh Rawat from Aaj Tak, two questions; one on Wal-Mart. Enforcement Directorate is investigating the case and I think they have requested RBI to send their clarification on this, or notify FDI rules and all.

Dr. D. Subbarao: Virendra, before you further, we do not discuss specific companies, specific issues.

Virendra S Rawat: The second thing is that some days back Intelligence agencies have found some exporters and importers overpricing and underpricing and they are stashing dollars abroad. So just need RBI perspective because it has impacted dollar also.

Shri H. R. Khan: There was a news item in one of the newspapers two days back on this. We have seen that. As of now we do not think it is a major issue, but we will further study it.

Alpana Killawala: Thank you very much, thank you Lavina.

Moderator: Thank you Ma'am. Participants, on behalf of the RBI that concludes this conference. Thank you for joining us, you may now disconnect your lines. Thank you.