"RBI Post Policy Press Conference Call"

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MODERATORS

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Moderator Ladies and gentlemen, good day and welcome to the Reserve Bank of India's Post-Policy conference call for the media. As a reminder, all participant lines will be in the listen-only mode and there will be an opportunity for you to ask questions at the end of today's presentation. Participants connected to the audio conference bridge may press '*' and '1' to ask a question. If you should need assistance during this conference call please signal an operator by pressing '*' and then '0' on your touchtone telephone. Please note that this conference is being recorded. I would now like to hand the conference over to Ms. Alpana Killawala from RBI. Thank you. And over to you, ma'am.

Alpana Killawala Thank you, Marina and welcome to this press conference after the policy announcement. I request the Governor to say a few words. Thank you.

Dr. D. Subbarao Once again from my side, a hearty welcome to this post-policy press conference. I used to have a written statement which I used to read, that is, before we innovated this practice of my giving the statement on TV now. But Alpana still says that I must make a short statement in order to get warmed up so I will go through that which is somewhat an abridged version of what you already heard and digested.

This morning we released the second quarter review of Monetary Policy for 2011-12. Based on an assessment of the current macroeconomic situation, we have decided to increase the repo rate under the liquidity adjustment facility by 25 basis points to 8.5%. Accordingly, the reverse repo rate under the LAF gets calibrated to 7.5% and the MSF rate to 9.5%. These changes have come into effect immediately after the announcement this morning.

We have also decided to deregulate the savings bank deposit interest rate with immediate effect. While the impact of past monetary policy actions is still unfolding, based on growth inflation dynamics,we considered it necessary to persist with the anti-inflationary stance. Based on the current and evolving macroeconomic situation, we have revised downwards the base line projection of GDP growth for 2011-12 to 7.6%. The base line projection of WPI inflation for March 2012 is kept unchanged at 7%. Anyway, the inflationary pressures are expected to ease from December 2011 though uncertainties about sudden adverse developments remain.

As in the past, we have also given guidance for the period forward. The projected inflation trajectory indicates that the rate will begin falling in December 2011 and then continue down a steady path to 7% by March 2012. It is expected to moderate further in the first half of 2013. This reflects a combination of commodity price movements and the cumulative impact of monetary tightening. Further, moderating inflation rates are likely to impact expectations favourably. These expected outcomes provide some room for monetary policy to address growth risks in the short-term. With this in mind, notwithstanding current rates of inflation persisting till November, the likelihood of a rate action in the December mid-quarter review is relatively low. Beyond that if the inflation trajectory conforms the projections further rate hikes may not be warranted. However, as always, actions will depend on the evolving macro economic conditions.

This review also includes developmental and regulatory policies. Some of the important measures announced today are deregulation of savings bank deposit interest rate which I referred to earlier; further liberalising branch authorisation policy; making guidelines on credit default swaps effective by end November 2011; issuing guidelines on short sale of government securities by December 2011; constituting a working group to look into principles governing proper, transparent and non-discriminatory pricing of credit; implementing the recommendations of the Damodaran Committee, on which a broad consensus has emerged.

Thank you for your attention.

That is the prepared part of a statement. I also want to brief you a couple of minutes on the issues we discussed with the banks this morning. Of course, we discussed the savings bank deposit rate and I also heard you in the Q& A session with them a short while ago. What we have both understood was that this is not going to cause any disruption to the savings bank deposit rate or in banks' management of the deposits; they had past experience when term deposit rate was deregulated.

Some of them asked why we pegged the limit for the two types of accounts at one lakh Rupees. They expressed a concern about how it might change their cost and parameters. Some of them asked, could you have not given us more time to adjust than do it immediately. Substantively, the question was that if we would standardise any parameters beyond what we said in the policy document. To all these questions our standard response was that the reason we left it open ended and giving a lot of discretion to banks was deliberate. We wanted banks to devise their own schemes and their own plans and compete and hopefully in the process do what's best for the customers and best for the country.

We discussed the issue of counterfeit notes. We keep talking about that to banks but this is the first time we talked about it in the post policy conference; mainly because as long as counterfeit currency is in the banking system, it is the responsibility of the banking system and of the Reserve Bank. When we looked at the data regarding detection of counterfeit notes, the data was quite skewed across banks. There were only one or two banks which were reporting to us, which means that a lot of other banks do not pay adequate attention to detection and reporting of counterfeit notes. Obviously, one thing discussed was about much more consumer awareness about this and also awareness in the banking system. It's not that just banks who have to be sensitised but that sensitisation must flow down to the frontline people. So it was agreed that banks will introduce training on detection and reporting of counterfeit currency; in particular, because this is an important issue. They said that in calendar year 2012 they will see that at least 20% of their frontline staff both officers and other staff will be trained in this.

We talked about capital requirement of banks in the context of Basle III and those numbers are quite tentative at the moment. Public sector banks have said that government has constituted a committee and they are trying to determine what might be the number but as Anand Sinha will tell you in the course of this conference or perhaps at a later time there are some variables in this which is - what is the minimum capital requirement we are going to demand - is it going to be just Basle III or slightly below that; what is going to be the timeframe, is it going to be 2019 or are we going to accelerate it. So, how much of capital banks will have to raise will depend on those variables and of course on the credit requirements of the structurally transforming economy.

And we talked about the government borrowing programme, I was going to say discussed but there was not much to be discussed because the numbers are all in the public domain, but there was it was felt important and necessary to share understanding on how government borrowing programme might fan out over the next 3-4 months.

Thank you very much.

Alpana Killawala For a change we will start with Anup Agarwal from Bloomberg.

Anup Agarwal Is the fiscal process having a bearing on the RBI's monetary policy to the extent that it is preventing the right kind of impact on the monetary policy. I am referring to the increase in the government borrowing programme.

Dr. D. Subbarao One way from fiscal to monetary policy, your question is do we take into account the government borrowing in calibrating our monetary policy. The answer in one sense is no, which is that our monetary policy is determined independently of the government borrowing requirement. There is no sensitivity or there is no concern about the cost of government borrowing impinging on the monetary policy. However, to the extent that fiscal deficit is a variable in inflation, of course, we take that into account in estimating our inflation numbers, in projecting our inflation outlook and in calibrating our policy.

Anup Agarwal You have often said that you do not prefer using the exchange rate for having impact on inflation. Now, recently we have seen the volatility in the exchange rate. Would it be possible or would RBI look at even the cost involved or the impact being debated, would the RBI look at using it given that there has been a sudden depreciation and a big depreciation in the currency?

Dr. D. Subbarao The short answer is no. We will not use exchange rate as an instrument for inflation management. Our policy and our stance and our response remain the same and all that you heard several times before. Certainly, admittedly, depreciation of the Rupee has added to inflation pressures but this depreciation is not due to any change in our economic situation, it is due to factors outside of India and because it is factors outside of India, it might reverse in course of time when the external situation will have adjusted back. It is not clear that it will reverse completely, that might well happen but that is not a certainty, there might be some elasticity effects there. But certainly, it will adjust back. So, as always we have not used exchange rate as an instrument for inflation management.

Latha What was the trigger, what was the need to give a near commitment that you will not hike rates in December or thereafter?

Dr. D. Subbarao The two considerations as we have said in the policy, one is inflation of course, ok, the persistence of inflation and that it continues to be high as of today and the numbers that will come out in the next two months are going to be high, that is the first consideration. The second consideration as someone who would have read the policy intelligently you would have noted was growth. That the growth is moderating, although it is not broad-based, the downward pressures and downward risk to growth are greater today than they were three months ago. Therefore, even as we were committed to bringing inflation down we also have to be sensitive to the moderating growth. So we wanted to give some comfort, some sense of the way to go ahead to the market participants, particularly, investors so that they manage their expectations in the hope that they will now plan their investments on a more predictable market situation. Subir, anything else you want to add to?

Dr. Subir Gokarn I think the key as the governor said was the visibility of our projections. When we are projecting from April onwards we have been deep in this trajectory. By December now. For, in April it was difficult to say what will fan out. Lots of risks in between. As we get closer to it, it becomes a little more reliable and given that typically energy prices, of course notwithstanding depreciation, in a year-on-year terms are not going to be contributing inflation beyond December. So, apart from the base effect, the moderation in growth, we see the inflation trajectory now reasonably visible and that gives us the opportunity to start paying some attention to the growth risk. We never sort of believed that they were unimportant but as long as inflation remained high and the trajectory suggested would remain high for some time our focus was obviously predominantly on inflation but that balance is changing now.

Latha Your last policy, the statement and the press conference mentioned that the policy stance will change when there is a risk of growth falling significantly below trend. So is 7.6 significantly below trend?

Dr. Subir Gokarn 7.6 is an annual forecast, we have had 7.7 in the first quarter, and we do not yet know the second quarter numbers are. But 7.6 averaging over a period essentially given that we have been operating on the 8% as a trend that we will have now clearly five quarters below, if you take the fourth quarter of '10-11, so five quarters more or less given below trend. I think would translate into that qualitative judgment of significantly below trend.

Dr. D. Subbarao Also, on the guidance, the other thing that we said in the earlier policy was that when we see some discernible trends of inflation coming down, admittedly headline numbers are still high but they will start coming down beginning December but the momentum numbers, the seasonally adjusted quarter-on-quarter numbers, there have been some drop in that, which we have pointed out at least twice in the policy document, so that also was one of the variables that shaped our stance.

Ira A question on the savings rate deregulation that everyone is very excited about. Can't understand why now? So it is just about getting done with the last bit of rupee interest regulation or do you see a specific benefit accruing from this move, from an economic perspective, firstly. Secondly bankers at least were very, very cautious in responding. Within the RBI internally is the general expectation that there would be a marginal upward move on the savings deposit rate and a scenario where there will be some drop in the savings deposits rate is now something that we are looking at right now in the current economic scenario although things can change?

Dr. D. Subbarao On timing question the answer is a standard one because whenever we do it, people will say why now. But this has been under discussion for the last one year, I think we put out a discussion paper in April 2011.,In fact, we started talking about it even before that. So bankers should not be be surprised at this and we have got all the opinion,, all the feedback , we have digested that several times. Also, since there may not be such an intense competition for deposits now we thought this might be a good time to do it. Certainly, the other factor that you mentioned that we must move forward on the reform process and this is the last remaining interest rate remains regulated that was also somewhat an issue in order to move forward on the deregulation process. On the expectation on economic benefit, yes, it will be beneficial to the economy because it will bring a lot of people into the formal financial sector and support financial inclusion, hopefully the less than no frill, let us call it a plain vanilla account of Rs. 1 lakh and below account, that will be structured in such a way certainly through low income households and that would be enormous economic pressure. On expectation about how banks might react, I think that they spoke to you. But they say, I heard SBI said that they will stay at 4% for now and other banks I don't know how they will react but our expectation is that they will take some time to internalise this and adjust to this but in the months ahead we should see this moving forward and stabilising thereafter.

Ira A quick follow-up Sir, on the operational guidelines on issues in terms of service charges, etc. would be clearly raising a lot of expectations like there would be a lot of action impact on what will be charged services that are associated with this account, Will there be regulation, a close watch on that aspect, but otherwise it could go contrary to the financial inclusion?

Dr. D. Subbarao I wanted to say that in my opening remarks. See, both banks and the public and you, media analysts could possibly think of a number of problems that might come our way. We decided that we will leave a lot of discretion to banks- - let the structure decide the sale of products and instruments as they think best. If and when they come across some problem that needs regulatory intervention, we will then come in rather than anticipating something at this time and responding to that.

Latha Just to add to that; was there any subtle expectation that given the situation chances are that there is an upward pressure on the savings rate if it is deregulated now and that will perhaps help monetary transmission coming into the effect.

Dr. D. Subbarao It was one of the pros that we mentioned in the discussion paper that it will make monetary transmission more effective. That certainly was a motivation. But I would not say that the precise timing or the calibration that was the only consideration for deregulating the savings rate. There were larger considerations.

Ritesh Sir there are two things: first when the Reserve Bank increased the interest rates in the September policy announcement. Then its transmission was not made by the banks. In today's meeting with the bankers did you give any message to the bankers that this should be passed on because an effective transmission will help contain inflation. Secondly there is more clarification needed with regard to the Damodaran Committee Report. In the policy what is being said is that in the Damodaran Committee Report, there are certain recommendations especially the consensus between the RBI and IBA on the 10 points agenda that will be implemented. I believe, in that, one of the agenda was the issue of the prepayment which banks are charging, which they should not do. Can we have a clarification on this issue?

Dr. D. Subbarao We have not given any message to the banks regarding the monetary transmission. Its something that they must do by themselves without any message from us. We believe that the signal will transmit and they will react to that and about that there was no discussion in the meeting. The 10 point formula of Damodaran Committee was discussed in the Ombudsman Conference in August 2011. In that conference IBA and Banking Codes and Standards Board were also there. IBA was asked to implement the 10 point formula. We will not give any instruction. IBA is seeing this for the last two months. Chakrabarty Saab will have a meeting with IBA and with some bank chairmen and then that implementation will be rolled out hopefully in the next one month. There will be some movement on this. Waiver of pre payment penalty was one of the points in those 10 points and on that if the IBA will not take initiative then after the Chakrabarty Saab's meeting there will be some movement on that. It is not clear nor is this necessary whether we will give an instruction to banks or they will be doing by themselves but that is one of the ten points in the programme.

Dr. K.C. Chakrabarty Banks have agreed. When we discussed once, the banks told that they are ready for that. That is the consensus that is why we have given press release and press release has been shown to them. Now they have a problem. The IBA is collective body. It is not that somebody can issue a fiat. They may have some problem, we are giving them some time, but we are very clear that these are the 10 point on which action plan is to be implemented. Other issues on which we have a consensus they will be implemented and if you see the Governor's statement, even other issues where there is no consensus; we will try to have a consensus and get this implemented. This process will continue to move ahead absolutely, there is no doubt that it is a matter of time and we want to see that implemented not as directive rather more as they also understand that it is necessary in the interest of the customers and well-being of the banks it is very important.

Ritesh Sir what are the points on which banks have a broad consensus on the points of customer service in terms of implementation of Damodaran Committee report which is said in this policy?

Dr. K.C. Chakrabarty The press release which we have given of this 10 if you require you can look into it. There are 88 point which we cannot write in the policy. There is consensus on 88 points. There are 131 recommendations of Damodaran Committee. So it will be a gradual process. The 88 points on which consensus is there, there is no problem. That is something which banks implement on their own and we will also give some guidelines on this. It is a process. It is just the talk of stake holders but we have to see remaining 43 points. We have to take care of those points as well. May be they are more important points, on that also discussion will be ongoing. If you see the Damodaran Committee Report then you will come to know what are these 131 points. That we cannot discuss in the meeting. What are the 88 points but the major 10 points are there like prepayment penalty charges, giving statement to customers, that we have told to the press in a press release and if need be we will provide the copy of that press release to you again.

Participant Sir one more related issue is that interest rates between old and new customers. For that you talked about to form a working group. On the other hand, NHB for other finance companies they have asked to implement. You can see a regulatory arbitrage position there can be. Finance companies rules are different and banks rules are different. So don't you feel that you should be taking immediate time bound action? .

Dr. D. Subbarao We would talk to NHB also. You are right. There is one regulatory agency moving ahead on the arbitrage issues. So we would talk to NHB and see if there is some amalgamation possible so that everybody has time to adjust both the borrowers and the lending institutions.

Dr. K.C. Chakrabarty See this prepayment will be freed then automatically there will be difference. This difference between new customer and old customer...difference another bank is giving...so he has moved to another bank. So you should see these both together.Others banks will do automatically otherwise customer will move to other banks. This is the same thing but then both will not happen because there will be shifting cost as well. It will be done through competition. It is not that people will go.

Participant So then we should understand that your view is that why force banks like NHB has done in housing finance companies. If this will not be done then you would want some more time.

Dr. D. Subbarao No it's not a question of our taking time. We will pursue with the banks to do this as soon as possible. But should the system require time to adjust to this, we will be prepared to give them some time. Do you understand? If they say that we need a month or two months so that everybody is prepared to make this adjustment to the floating regime and the waiver of prepayment penalty we will consider that but I would say that is one of the possible issues on the table, I do not want you to go away from this conference thinking that we have already allowed that.

Anirudh
ET Now

You mentioned time and again in your statements the need for concerted policy action to mitigate inflation especially on the food side, the structural imbalances that we have seen. Now, given the fact that we have not seen too many things coming in from the government and there really does not seem to be much coming in from themat this point of time, how realistic it would be for us to assume that this would indeed be an end of the hike or given the fact that food inflation is still up or it may even go up further, could we really assume that this is the end of the cycle ?

Dr. D. Subbarao

I would only reiterate the same and we have also said in the policy statement, a caveat saying that exactly what you have said for inflation to ease on a sustainable basis and for growth to pick up you need a supply side response which means by way of structural food inflation constraints being eased, infrastructure bottlenecks being removed, reforms being resumed or accelerated, food supply chain issues being handled. All of those are necessary for the supply side response to manage inflation, that we rather achieve going forward.

Dr. Subir Gokarn

I think probabilities are always the qualifiers. It is not only domestic supply side forces that pose inflation risks; there are external risks as well whether this is commodity prices or anything else. So, our judgment based on our base line scenario is that this could be the last hike that's this guidance we have given but we have clearly also pointed out that there are risks which we cannot anticipate, we have to be conscious of that. The other part of that guidance that we have put in very deliberately is that these are long-term, structural kind of inflation, this is not just a one-off kind of situation, we pointed out four or five factors whether it is food, whether it is distorted prices, administered prices, whether it is the pace of fiscal adjustment itself, all of these also pose some inflation risks in the medium-term, so that has to be an input into our policy thinking as we go beyond this particular cycle and look at that what we will do further down the road. So, these risks remain, these risks are not going to disappear and that is something that will certainly impact our forward-looking assessments as we go along.

Mayur
The Times of India

Savings accounts, the banks are saying they have got a lot of standing instructions in terms of giving payments, commissions ECS etc. Whether the same number can be used across banks as per RBI rules..

Dr. K.C.
Chakrabarty

You see today it is not possible because any account relationship is a contract between the bank and the customer it cannot be transferred to another thing. Within the bank portability is possible, but from one branch to another. But across the banks we have not reached a stage, maybe where the Aadhar comes, etc., and if we can develop it,but today, it is not possible. Even we have to see the legal consequences, saving account is not only transactional, it is the contract also to provide a certain set of services and achieving that. How it can be transported to another bank we do not see that legally it is possible.

Gopika CNBC My question is largely to understand what is the reasons for setting up a working group to look into the transparency in pricing of credit because couldn't the Reserve Bank have come up with a notification asking banks to ensure uniformity for old and new customers like what NHB did because if you remember right last year this was the main reason why the base rate was implemented, that was the main objective of base rate. So are we here questioning the very objective or very effectiveness of base rate in ensuring transparency?

Anand Sinha No, it is not that. Base rate is the fundamental cost of funds. On that you have to add spread. Spread may have three-four components. For example, credit risk premium, down fee premium. There could be elements of customer relationship also. So ultimately what we are saying is that interest rates which you are going to charge a customer have to be based on certain principles. That is the base rate plus the spread and whatever are the costs of fund. Now, base rate will change whenever the cost of funds changes. The spread should also change whenever these factors change but you cannot do it arbitrarily, so that is the issue. In that paragraph, we have written also that for old and new customers, if there is a discrimination and a customer complains. So what we are trying to do is to set up a set of principles rather than issuing a regulatory fiat and there are basic principles and what are the principles that should be applied for interest rate determination and that is the intention.

Gopika How would that be different from what the base rate guidelines say?

Anand Sinha No, base rate guidelines what did it say that except than the base rate most component are cost of funds and unallocatable costs, then you have spread whereas the cost of a particular product, credit risk premium and some premium have got to be added on to that. So, this is what base rate is now, how the spreads are being manipulated or being changed, are they being done in accordance with some risk or are they being done in an arbitrary manner, if it is to be changed what would be the basic principles that should carry, that is, the intention. It is not that the base rate mechanism has not delivered the goods.

Dr. D. Subbarao In fact, the inference that you must draw from this is not that base rate system has not worked, but that base rate system has worked and has settled down. So we are going to issues beyond the base rate, about the variable cost that will determine the ultimate cost of borrower.

Participant Sir if I may ask a supplementary on this. Would this working group also consider framing rules for determining spread on a variable rate? Why the base rate does not work because every individual has got a different spread and this spread is not determined on the basis ofhis credit rating but it is based on the time when you enter. Would it be possible to describe something on that?

Dr. D. Subbarao I do not want to prejudge or pre-empt what would be ambit and what route we think through that but certainly one of the issues that staff told me is that if the credit rating of a borrower has not changed, there is no reason why the spread must change. So these are some of the issues that will certainly go into it and there will be predictability and transparency and contestability built into the spread of deposit base rate.

Yogesh Is monetary policy not dependent on fiscal deficit. How big a worry is this fiscal deficit and secondly there is a thought that raising special duties lowers interest rates. So what type of health you are looking for in the fiscal deficit? Whether the monetary policy is only the way to cut the interest rate in long term.

Dr. D. Subbarao Certainly, fiscal deficit will have an impact on inflation and inflation outlook and we take that into account as I said in answer to one of the earlier questions. Your question is will the fiscal deficit overshoot the indicative target and what might be the implications for inflation and for monetary policy. We have very clearly said in this document, indeed in the earlier documents as well, that the level of fiscal deficit is going to be one of the risk factors in the inflation outlook. So if the government conforms to 4.6% that is, one level of risk, but if borrowings go beyond that and the fiscal deficit exceeds that, that will increase the risk for inflation because fiscal expansion is inflationary. To that extent, monetary policy will have to be compensated. So in calibrating our rate hike as well as the guidance we have taken into account the fiscal outlook. Beyond that I cannot really say what the fiscal deficit might be, indeed I will say in the budget session or even in the winter session, there could be definite assessment from the government.

Ben PTI Variables on inflation outlook. What is the view on the rupee in light of inflation?

Dr. D. Subbarao On the inflation outlook, 7% by March 2012 and we have given the fan chart with the probability distribution that is on page 7 on the document which you can see yourself. So that is the probability distribution in a colour code on the inflation outlook. On the risks to inflation there are several, one we just talked about which is fiscal deficit, then there is demand pressures and how they might respond to the monetary policy action that we took and be taken today both consumption demand and investment demand. Then there is the issue of commodity prices, especially in oil price how that might settle because it’s not moderated as much as it should have, given the global situation. In these last few weeks inching back up, so the gain or comfort from the oil prices has not been very much. Then there is this structural food component. There is also suppressed inflation. The electricity prices have not been adjusted because coal prices have not been adjusted. Petroleum sector prices have not been adjusted, and they do not reflect the current international price. Those are all the variables on the inflation outlook.

On oil price and depreciation, our people have done some numbers on this. If we take August 2011, when the US debt downgrade took place and October 21 or so, the Rupee depreciated by over 10%. The international oil price has actually moved up slightly not moved down. So not only has depreciation completely off- set any positive impact of international price of oil, the international price of oil itself has moved up since August 5. So that is below comfort. In Rupee terms, oil price has moved up.

Ben from PTI Have oil prices been taken into the estimate of inflation?

Dr. D. Subbarao We have taken into account. We had to make some internal estimates of what the oil price might be of the Indian basket. We did that and arrived at this 7% projection.

Ben from PTI What about the transmission of policy rate hikes?

Dr. Subir Gokarn He is saying the banks are not keen to pass on the policy rate hikes.

Dr. D. Subbarao I have answered that question earlier to Ritesh which is that, we leave it to the banks to determine their response to our policy signals instead of telling them or instructing them.

Gayatri Economic Times My question is regarding this un-hedged foreign currency exposure part of it. What are the triggers besides the volatility in the currency market for this directive to bank?

Anand Sinha The un-hedged foreign currency exposure is a source of great risk if it is done beyond limits for the corporates and, therefore, this market risk becomes a credit risk for the financing banker. And this is an issue which is not a new one if you see the paragraph, you will find that right from 2001 we have been cautioning the banks. If you are asking what is the trigger to reiterate it, the trigger is very recently, a couple of years back, we had derivatives problems and within a few weeks Rupee has depreciated by 10%. Now what impact it is going to have on some of the corporates, we will see soon.

Gayatri Do you have any specific instances ?

Anand Sinha Not yet, but I can also tell you in one of the economic papers, I think yesterday, I saw a comment that some of the corporates are going to have problems with Forex exposure. Whether we see or not or whether we know the instance today or not, it is bound to be a problem.

Gayatri Is that a pre-emptive measure?

Anand Sinha Yes, that is pre-emptive and we have gone a little further from our previous advices, we have left it to the banks, we have not mandated but we have said that while you are financing you may also think in terms of having a limit on the open positions that you can have, but that is entirely left to the bank at this stage.

Dr. D. Subbarao On the oil price, there is a table in the document that we released yesterday - The Money Macro Statement - on page 43 about the Rupee movement as well as the oil price movement since August 2011. So that is on page 43. That shows that global price moved up in dollar, Rupee has depreciated, so on both accounts in terms of the Rupee price of oil it has been half much more.

Shamik Reuters Would just like to know with the supply of government debt, is there a chance of the RBI financing open market operations?

Dr. D. Subbarao The answer is that it is not clear. We have said, it is reiterated again in today's statement that the liquidity we will try to maintain as plus/ minus 1% of NDTL, that position remains. So it is not necessary that we will manage liquidity only through OMO, but to the best of our ability we will see that the systemic deficit is within that limit.

Aparna Newswire 18 Exactly a year ago, you had taken review of the last year's monetary policy. You had given a similar indication of not raising rates in December. And rightly so you had called for the wage hikes. After that you know what happened, inflation and inflationary expectation. What makes you feel that this time it will not happen again? And my second questions is, are we seeing any instances of pricing power of companies coming down to reduce demand and impacting on inflation?

Dr. D. Subbarao I will answer this and then I will turn to Subir. A year ago, there was no expectation that we were coming to the close of guidance. The guidance that we gave in October 2010 was with reference to the December policy only, not over a period of time. And then, of course, some one of the things happened like onion price, etc. They were not structural factors that jacked up the inflation for a short while thereafter it might be called right. So we are hoping that the trajectory this time would be more reliable, our projections would be more accurate than it happened last time around and the situation today is different from what it was in October 2010. On the pricing power, pricing power of corporates has come down but not as much as it should be in order to reduce demand. The indication for that are the PMI for inputs and PMI for outputs. I understand the PMI for inputs has come down markedly but the output PMI has not come down so much in corresponding terms it is much less which shows that even if pricing power has come down, it has not come down markedly which means there is still some pricing power to producers.

Dr. Subir Gokarn I think that the key development that happened between our guidance of November 2010 and December-January 2011 was the spurt in oil prices. When we gave that guidance, oil prices were somewhere in the $80-85 per barrel and the outlook for oil, if you went by futures market or in fact the IMF-WEO published in September had anticipated somewhere $89 per barrel average price for 2011. But as we saw, end October and early November the price spurted to over $100 eventually going up as high as $124 was the peak in this cycle. And that fundamentally changed the inflation trajectory from January onwards. So in that sense, there was an unforeseen development we cannot anticipate that shock to oil prices that happened then. Such a shock could occur even now, and obviously that could make our guidance, therefore, sort of irrelevant but the assumptions we are making, the judgments we are making about the trajectory of commodity prices based on the way they have behaved over the last few months, gives us some confidence that this is the most likely outcome and, therefore, the guidance is being shaped by that. On the issue of pricing power what we follow most closely now are EBITA margins of companies and we track them very closely, we track them across MAT samples and across the IIP and the user based classification to sort of map into the company, it is not a very tight mapping but it is pretty indicative. One thing that has been clear when you break up companies into that categorisation, i.e., intermediate goods, consumer goods, capital goods, is that the bulk of the margin compression that, of course, a lot of people are talking about, seems to have happened in the intermediate goods segments. The other segments, capital goods, consumers, non-durables, durables and basic goods, the compression has not been as…. they are coming down as compared to Q4 of 2010-2011 and also now of Q1. Just before we went to press, we had about 160 companies which we had matched, EBITDA margins for that sector was 17% in Q1, 16.6% in Q2. So slight moderation, of course, then different samples will give you different results, but it is important I think to recognise that the margin compression is not uniform and it is most severe in companies whose commodity input costs are the highest. So that is quite reasonable and consistent with the overall commodity price situation. But the pass through to products around the supply chain and eventually to the final product seems to be quite strong. It is moderating which gives us the reinforcement for our downward trajectory of inflation consistent with the seasonally adjusted Q-on-Q deceleration in prices. So it is a process that is consistent with the outlook but it is still on the downward trajectory. It has not fallen off dramatically.

Participant Are you banking too much on the high base effect to achieve the 7% target, are you banking too much on the fact that last year inflation was at a much higher level?

Dr. Subir Gokarn Firstly, the base affect gives us clearly a number that we communicate with which is the year-on-year number and there will be a base effect there. But we are also looking at momentum indicators and those momentum indicators give us added input into what's the direction of inflation is. So it is not only the base effect. That momentum effect is being driven by the deceleration in demand as well and although we have not and would not because of the risks involved, come out with projections beyond March, the direction suggests that that pattern will continue. The 7% in March is a March-end forecast but we think that trajectory in again, making certain baseline assumptions will continue. That is really what has given us a foundation for the guidance that we have given.

Participant You mean it will be a downward trajectory?

Dr. Subir Gokarn Yes.

Parnika Business Standard Bankers said that there are times when banks have enough liquidity, there is possibility that the interest rate on savings bank account could be renewed downwards from the current level. So would there be a minimum rate that a banker should give or would you leave it to competition to take care of that? And would there be any limits to how many times they can revise these rates?

Dr. D. Subbarao The answer to both questions is, no. In fact one of the suggestions made to us in de-regulating the savings bank interest rate, was that we must do it in two steps, de-regulate the savings rate with a floor and then after sometime, de-regulate it completely. But we decided that we must do it in one go rather than have a floor. And also to the second question, there will be no limit on the number of times they could change this stuff. Obviously banks themselves will not do it too often because they want to give some stability to their market.

Ruchira Economic Times The policy, of course, talks about setting up of a working group on G-Sec and interest rate derivative market. If you could just throw some light on this working group and considering products like repo, corporate bond markets and all have not taken off?

H. R. Khan The whole motivation behind this working group is as under: , we have a fairly efficient G-Sec market and we have been able to raise huge borrowing for the central and state governments and we have a yield curve going up to 30 years. So far as the market infrastructure is concerned we are comparable to world class in terms of our NDS OM; central counterparty in the form of CCIL. But still there are issues regarding the liquidity in the market particularly there are only four securities which are broadly traded and we do not have liquidity at major points of the yield curve. Then public sector banks do not participate actively in the derivative market as there is skewness in the market and some of the future products which have been launched, they have also not taken off and there is some amount of disconnect between the capital market and the derivatives market. And there are accounting issues also. So we thought to look at the whole thing in a comprehensive manner and come out with some suggestions so that we can further improve and further deepen and further broaden the Government Securities market which will provide fillip to the whole host of products which are launching whether it is the IRA, whether it is the CDS, whether it is the rupee derivative.

Participant BusinessWorld Sir, CDS (credit default swaps) was supposed to be introduced yesterday but now there has been a delay. So I just wanted to know what are the reasons? And secondly do you think , somehow I understand, that there is a lot of apprehension about participants' understanding of swaps. Do you think that is the case? Are market participants ready first of all and also the IRS what we understand but you are saying that you will introduce that for two year and five year also. What do you feel? Are market participants ready for complex products like these?

H. R. Khan We had said that it would be launched by end October but there are some issues regarding standardisation for the market convention and the determination committee to take place there are few other infrastructural issues. So now we hope that before end of November we will be launching the whole product. Regarding the futures as I told you, we have allowed cash settled futures. Earlier we had this 10-year physical settled that did not work. So 91 days we have introduced cash settled , initially there was some momentum there, afterwards there is no momentum. Now 2-5 year we have launched we hope it will work because most of banks duration is around that time. But if there is only one way view, probably it may or may not work, that is why I had told you this working group also look at this whole gamut including the Rupee derivatives, interest rate derivatives. So far as the CDS is concerned, as I told you, we will be launching but whether there will be enthusiasm or not... not that we should not pre-judge at this stage, let us see how the things are evolving.

Ira from NDTV I am just wondering what is the RBI's assessment on the export sector right now and I am asking in the light of all these questions that have come out on the reliability of the export questions and all. There is over-invoicing, whether there is something more to be read into the data, any concern or red-flag in RBI that you are watching, sir?

Dr. D. Subbarao Yeah, we have looked at the export numbers and we have some projection for the full year numbers which is now in the public domain, of course. I have also seen some comments about the reliability of those numbers just because it is just too high.

Ira The newspaper report regarding exports to Bahamas?

Dr. D. Subbarao That is right, I saw that too and our people have also seen that. They have told me that they have matched export performance with the financial numbers, transactions, as well as the export data and they have matched roughly. So the possibility of export numbers being inflated is small. However, I saw the issue raised in one of the papers yesterday about sudden expansion of exports to Bahamas from $2 billion to $32 billion and we are investigating that. We are investigating that in the sense we are checking first of all that the data is correct and second what might explain that. But apart from the Bahamas issue, we have made a very conservative estimate of export performance for the full year. In the first half they have done reasonably well, 47% at a time when global growth is quite modest, it is quite a remarkable performance. We hope that that will be repeated in the second half much to our relief. And I have just got a note saying that export to Bahamas has not only expanded rapidly but it is largely on account of petroleum products. So we have to see what explains that. I just want to say that we are doing this not in an investigative mode but in an understanding mode just so that we report this properly.

Alpana Killawala Shall we say thank you?

Dr. D. Subbarao Okay last question.

Latha Venkatesh from CNBC TV18 I was hesitant to ask this only because it involves a little bit of the math on arriving at this 7% inflation by March. If we take the 7% inflation in March, the index would have moved to 160 because in March 2011, it stood at 149.5 and the last number we have for September is 155.8. If you take the distance from 155.8 to 160, it will increase by 0.9 every month to arrive at 160. How will that any moderation, it is 0.96 even from August to September and every month it goes by 0.9. To reach 160, which means as that gentleman pointed out, the move 7% only because of momentum otherwise the 0.9 every month on your own forecast of 7%. So are we to understand that Reserve Bank is not expecting the momentum to fall?

Dr. Subir Gokarn But the 0.9 has to be compared with something in the past, right? It is not a constant increase. If you take the seasonal adjusted Q-on-Q…

Latha Venkatesh (**Inaudible**)

Dr. Subir Gokarn No, but that is the indication of momentum, whether it is changing in relation to its previous period.

Latha Venkatesh You take the headline that actually 0.9 ….

Dr. Subir Gokarn You are taking year-on-year?

Latha Venkatesh August, September.

Dr. Subir Gokarn You are taking year-on-year there.

Latha Venkatesh This is for one month.

Dr. Subir Gokarn But the way we arrive at the end point is the headline is sort of ultimate, as I said a communication. But there is also an underlying momentum that takes us to that number. And if you compare the July to September that is the 2nd Quarter momentum number to the 1st Quarter there is a drop of roughly 3 percentage points. So from about 9 something to about 6. So that is a very sharp drop. Now that is the pattern that we expect to see. So as you get the 3rd Quarter numbers which should be the October and December we would expect to say that being somewhat lower than that 6%. So it is the momentum indicator that gives us a sense of where it is going and again, 7% is an arbitrary point, it just happens to be the month at which we are communicating. We are really looking at this trajectory continuing as I also responded to Tushar that it is not just the 7% that is giving us the foundation for our guidance, it is also the expectation that that downward momentum will continue beyond March.

Dr. D. Subbarao Just as Subir was answering your question I rechecked your number. You are right that it is 149.5 in March 2011. It is got to be around 160 in March 2012. I do not know the current index but it is 5.5 but it has got to move another 4.5 points. We will do the math again but our people have done this quite independently and they say that 7% is a reliable number. Apart from the arithmetic, the question is can we take advantage of the base effect is larger question. In fact I saw a debate some 2-3 months ago that in the US they were talking about targeting the index rather than the year-on-year inflation. So it is like saying in India we will target an index of 160 because it is not falling 9.5 last year. But there are conceptual practical policy problems in doing that but that is a good debate to have.

On that note, thank you very much. I wish you all on behalf of Reserve Bank and you and your family a wonderful and happy Diwali. Thank you very much.

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