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Dr. Urjit R. Patel: Good afternoon, everyone. Over the last three days the Monetary Policy Committee carefully reviewed evolving global and domestic macroeconomic developments. We noted that global economic activity and trade has continued to expand, though there has been some easing of momentum since our April meeting.

Inflation pressures have emerged in some key, advanced and emerging economies; driven in part by rising commodity prices, especially those of crude oil and petroleum. Financial markets have been driven mainly by monetary policy expectations and geopolitical developments. Emerging market currencies have by and large depreciated against the US dollar.

On the domestic front, GDP growth for 2017-2018 has been revised and estimated at 6.7%, backed by an all-time high production of food grains and horticulture, strengthening of industrial growth and resilient services sector activity. For 2018-19 the forecast of a normal southwest monsoon augurs well for our agriculture sector.

In manufacturing, capacity utilization has increased and the manufacturing PMI remained in an expansionary mode for the tenth consecutive month in May on the back of new domestic orders and exports.

In the services sector, various high frequency indicators suggest improving performance. Investment activity is expected to remain robust, even as there has been some tightening of financing conditions in recent months.

Both rural and urban consumption remain healthy and are expected to strengthen further.

Accordingly, the MPC decided to retain the projection of GDP growth for 2018-2019 at 7.4% with risks evenly balanced around this number.

Retail inflation measured by the year-on-year change in the consumer price index (CPI) rose sharply to 4.6% in April. Even excluding the estimated impact of an increase in house rent allowances (HRA) for central government employees, headline inflation was at 4.2% in April, up from 3.9% in March. In May, households reported a significant rise in inflation expectations. Manufacturing firms reported input price pressures and an increase in selling prices. The cost of farm inputs and industrial raw materials has risen sequentially.

Since the MPC's meeting in early April, the price of Indian basket of crude has surged from $66 a barrel to $74 a barrel. This, along with an increase in other global commodity prices and recent global financial market developments has resulted in a firming up of input cost pressures and persistence in the higher CPI projections for 2018-19. In the MPC's view, the price of the Indian crude basket imparts considerable uncertainty to inflation outlook, both on the upside and the downside.

Taking these effects into account, the projection of CPI inflation for 2018-19 is revised to 4.8% to 4.9% in the first half, in the first two quarters of 2018-19 and 4.7% in second half for both quarters, including the HRA impact for central government employees, with risks tilted to the upside. Excluding the impact of HRA revisions, CPI inflation is projected at 4.6% in the first half and 4.7% in the second half.

On a careful assessment of all these factors, the MPC decided to raise the policy repo rate by 25 basis points and retain the stance of Monetary Policy at neutral. The Committee reiterated its commitment to keep inflation at the target of 4% in the medium-term and to remain vigilant on how actual inflation unfolds.

Underlying the MPC's decision was a concern that headline inflation has been sharper than anticipated and that it has remained above the target of 4% for six months in succession. Over this period, the MPC maintained status quo on the Monetary Policy stance in order to carefully evaluate and monitor how the various risks to inflation have evolved.

Moreover, an abiding concern of the MPC has been that the impulses of growth were nascent and taking root. In its current assessment, domestic economic activity has exhibited revival in recent quarters and the output gap has almost closed. Investment activity in particular is recovering well and could receive a further boost from resolution of distressed factors of the economy under the insolvency and bankruptcy code.

It is in this context that the MPC decided to raise the policy rate after a prolonged pause. Going forward, we will continue to be cautious and remain vigilant in which way the balance of risks around both growth and inflation play out.

I now request Dr. Acharya to say a few words. Thank you.

Dr. Viral V. Acharya: Thank you, Governor. Good afternoon, everyone. First, I will explain briefly how the recent inflation prints have affected our projections for the year.

While the April and May prints have more or less been in line with our April projections, there has been an important compositional shift. Inflation excluding food and fuel has hardened sharply, driven by a variety of factors laid out by the Governor, such as the oil price rise and input cost pressures. This hardening has imparted persistence into higher inflation projections for the next year.

In contrast, food inflation has remained benign and the typical seasonal pickup that one sees around this time has been delayed. This has put some softening into the short-run inflation projections. Overall, however, the ex-HRA inflation projection for the second half of 2018-19 has risen by 30 basis points from 4.4% to 4.7%. And in parallel, growth indicators appear to suggest that economic revival is now on a sound footing.

Given the MPC's commitment to maintain headline inflation at target rate of 4% on a durable basis, the time seemed right to the committee for raising the policy rate by 25 basis points.

Second, let me turn to liquidity. As expected, the redemption of market stabilisation securities in March, and the normalisation of bank balances have added to liquidity in April. However, higher than expected increase in currency in circulation during both April and May as well as the Reserve Bank's foreign exchange operations during this period have negated much of the system wide increase in liquidity. In other words, liquidity remained in neutral zone during March and April, even though it switched back between deficit and liquidity during several weeks.

In terms of magnitudes, the daily average liquidity absorption by the RBI, this is the excess liquidity that RBI mops up as surplus liquidity from the system if the net LAF operation is positive. During the month of May this was Rs. 0.12 trillion or Rs. 12,000 crores as compared to Rs. 0.5 trillion or Rs. 50,000 crores in April.

The weighted average call rate at which money market participants lend to each other overnight on an unsecured basis, and which is a good proxy for liquidity conditions in the economy, this rate has remained soft, on an average five basis points below the policy rate during April to May 2018. It was three basis points below the policy rate during January to March 2018.

At the time of last policy, we had indicated that liquidity is likely to remain moderately in surplus during the first half of fiscal year 2018. The few days of June so far have been in comfortable surplus liquidity condition of Rs. 0.9 trillion or about Rs. 90,000 crores, this has been driven by an increase in government spending.

However, the currency in circulation expansion has remained above trend. Looking ahead, advance tax outflows in mid-June would also reduce the system liquidity. So, we will watch these evolving liquidity conditions to determine our choice of instruments for both transient and durable liquidity management.

Third, I will just briefly touch upon a few developmental policies. The details are in the part B or the developmental and regulatory policies that you have. One, in the liquidity facility that RBI provides, what is called as the LAF facilities for qualifying market participants, presently RBI applies a uniform haircut of 4% against eligible central government securities collateral and 6% for the eligible state development loans. This is in contrast to international standards where the haircut typically depends upon the maturity of the collateral, because that reflects the market risk that the collateral is going to have.

So, starting 1st August, 2018, the haircut that the central bank charges at the LAF will depend upon the residual maturity of the eligible collateral. For central government securities, it will range from 0.5% to 4%, depending on five different buckets of residual maturity, and for state development loans in the range of 2.5% to 6%.

With a view to incentivising the state governments, to get public rating for state development loans, we will offer a discount of 1% on rated state development loans for similar maturity compared to unrated state development loans.

Second, we are planning to come out with a consultative draft regulation for market abuse regulations. At present, we have what are called as codes of conduct, these are sort of voluntary agreements within our market participant bodies such as FIMMDA or FEDAI.

To be in line with international practices, I would say the best global practices, we plan to implement some enforceable regulations to essentially incentivize that the code is being adhered to.

Lastly, you might recall that in October 2017 policy, a high-level task force had been put in place under Chairmanship of Mr. Deosthalee to assess if and how a public credit registry could be created for India. The task force has submitted its report on 4th April and will be released on website of RBI today. They have recommended that to foster a better access to credit and to strengthen the credit culture in the economy, the Reserve Bank should setup a public credit register.

We have decided to go ahead and constitute an implementation task force that will guide us on the logistics for the next steps. I would just stress that public credit registry is one of the important ingredients of the ease of doing business index of the World Bank. Thank you.

Dr. Urjit R. Patel: Thank you, Dr. Acharya. May I request Mr. Vishwanathan?

N.S. Vishwanathan: Thank you, Governor. I will highlight a few issues that have been indicated in part B but not all of them, but more important ones, and not exactly in the order that it appears there.

So far as the MSME exposure, in February 2018 we had allowed the banks and NBFCs to reckon a 180-day norm for classification of NPAs for the smaller MSMEs with exposure of up to 250 crores and was limited to the GST registered NBFCs. Now we have decided to extend to the non-GST registered NBFCs. But there is, as we go forward, an incentive for getting registered because there is a phase-in of going back to the normal 90-day norm in case of those which are getting registered. But for others it will come back to normal if they do not get registered under GST before December 31, 2018. This we are doing because we believe that formalization of the sector is beneficial for financial stability.

The second part is the conversion of urban cooperative banks into small finance banks because there have been demands from some quarters that we must allow them to corporatize. We believe the small finance banks are also having the same mandate of financial inclusion as part of their fundamental business model. So, we will come out with a detailed scheme on this conversion from urban cooperative banks to small finance banks. Incidentally, if you recall, the high powered committee under Mr. Gandhi, which dealt with urban cooperative banking sector had recommended that such a thing should be done.

Another is on the LCR; we have a SLR and LCR, so we have been allowing a carve out from the SLR, which can be reckoned for HQLA for LCR as well. So, we have now raised that carve out from 11% to 13%, so 200 basis points increase.

On the SDLs, the current system is to value them with a mark-up of 20 basis points above the G-Sec rate of similar maturity. With a view to improving or bringing a more realistic valuation of SDLs in the banks' balance sheet, we have decided that the non-traded state government securities will be valued based on the state specific weighted average spread over the yield of the central government securities of similar maturity as observed during the primary auctions. The traded securities will be valued at the market price.

We have also allowed the Core Investment Companies (CICs) to sponsor InvITs and reckon the investment in InvITs to the extent of minimum required as sponsor, which is 15 percent today as per SEBI regulations as part of the minimum 60 percent that they have to invest in equities of group companies. This will foster investment in infrastructure.

Thank you.

Dr. Urjit R. Patel: Request Mr. Kanungo, please.

B.P. Kanungo: I will dwell on some of the important announcements that are being made in the statement on developmental and regulatory policies, that is, part B. First, the payment systems - so far as the payment system is concerned, Reserve Bank has always batted for innovation and competition from the beginning. As a result, what we have today is a world-class payment system.

Proceeding in that direction, we feel that when it comes to the retail payment system and the provision of the platforms, there is too much of concentration risk. So, we will bring out a policy paper in three months' time with a view to fostering innovation and competition in the sector and to mitigate the concentration risk. A policy paper will be brought out, which will invite the private players to bring about pan-India payment system platforms.

On the central counter parties (CCPs) in the post global financial crises, they have emerged as very important financial market infrastructure (FMI) entities because they provide the guaranteed settlement. And so far as guaranteed settlement risk is concerned, by providing that they foster financial sector stability.

We will bring out guidelines, a framework, providing for their capital structure, governance structure and also the recognition of the foreign CCPs in India. Because there is international consensus that they should be well regulated, well capitalised and well supervised, so, we will bring out the guidelines for that.

So far as the standalone Primary Dealers (PDs) are concerned, they are an important part for development of the G-Sec market. While not diluting their role so far as the G-Sec market is concerned, our effort has always been that how their other activities can be improved. They have come to us several times saying that so far as providing a bouquet of services to their FPI clients, they are not in a position to do so because they do not have Authorised Dealer (AD) license, they are not allowed to deal in foreign exchange. So, for the purpose of providing these kind of services to their FPI clients only, we will give them a limited foreign exchange license - AD license, so those guidelines will also be issued.

Now, I will come to the When Issued (WI) market and the Short Sale market. RBI has always tried to broaden and deepen the movement in the government securities market. With that in view, in February 2006, we had allowed short sale in the government securities. So that participants can express a two-way view on the interest rates and there would be better price discovery.

Currently only scheduled commercial banks, primary dealers and very well managed urban cooperative banks are allowed to participate in that market. However, there are security-wise short sale limits and overall aggregate limits also on these eligible entities. So now we have decided that it should be relaxed, the limit will be relaxed, and the participation would be broadened and new entities would be allowed.

Similarly, in the when Issued market, that too was introduced in 2006, so that anyone who is eligible to participate in the auction, the short sale position can be taken only by the banks and PDs as of now. There also the limit remains at 5% of the issued amount. We will relax that limit and we will also allow it to other entities, so that both the segments of the market, the Short Sale and the When Issued G-Sec market improves, and the market is broadened and deepened.

Thank you.

Dr. Urjit R. Patel: Thank you, Mr. Kanungo. We will now take a few questions. Economic Times?

Govardhan Rangan
Economic Times: Good afternoon. You have raised the rates and raised the inflation forecast as well, but at the same time maintained the stance as neutral. This suggests to be a bit conflicting. Can you explain what it means for future actions?

Dr. Urjit R. Patel: Actually, it is not conflicting at all. A neutral stance leaves all options open and other central banks also do the same. So there is no contradiction, there is no difference or there is no tension between the two. The committee felt that there was enough uncertainty for us to keep to the neutral stance and yet respond to the risks to inflation target that have emerged in recent months.

Nivrita Ganguly
BTVi: My question is on oil prices, because of the sort of volatile moves that we have seen. At the MPR that we got at the last meeting the MPC had factored in at $68 price for oil, since then it jumped to about 80 even though it has cooled off recently and that could change based on the OPEC meet at the end of this month. What is the price now that is being factored into these forecasts by the MPC? And also, does the inflation forecast factor in a full pass through of the rise in oil prices or you expect it to be an incomplete pass through?

Dr. Urjit R. Patel: I request Dr. Acharya.

Dr. Viral V. Acharya: So, typically we tend to use the most recently available price in our projection, so that is the one we have employed. As we have flagged in the resolution that there has been a 12% increase in the crude oil price since the April policy. In terms of the pass through, I think that is the government's policy at present, so that is what we assume as well.

Nivrita Ganguly
BTVi: But what has been factored in the projection for inflation?

Dr. Viral V. Acharya: That is the full pass through.

Bijoy Idicheriah
Cogencis: You spoke about the liquidity side and you have also done SLR carve out for meeting the LCR. But on the broader side, because there is FX intervention also that you have been working on, can you give a little more clarity to the markets in terms of OMOs, because OMO purchases especially, you did one and you stopped and there has been lacklustre demand in the market for government securities. So if you can throw some light on what your view and what your strategy on that front is? Because it has a much wider implication on your overall policy too.

Dr. Urjit R. Patel: Just to make a general comment, our policy regarding liquidity is determined by anchoring the weighted average call rate to the repo rate, and we have stuck to that, both in terms of transient liquidity management and durable liquidity management, and that is what we will continue, going forward, anchoring the liquidity policy towards the weighted average call rate.

Ira Dugal
Bloomberg Quint: A number of emerging market central banks have responded to the volatility in the currency markets with the rate defense. What is the RBI's perspective, is that built into inflation projections? What does the RBI believe is the efficacy of the rate defense in the case of the Indian currency?

Dr. Urjit R. Patel: Our monetary policy is determined by the nominal anchor that has been given to us through a legislative process and which is the consumer price index.

Manojit Saha
The Hindu: After the last policy, bond yields went down when the minutes of the same policy were released bond yields went up. So, why do you think the market is misinterpreting, or do you think the market is unable to interpret what the RBI is trying to say?

Dr. Viral V. Acharya: I think minutes are important, so is the resolution. And in some ways if the minutes were not important, there would be no value to putting them out separately besides the resolution. I think I view the process as being quite open, transparent and positive in the sense that different members of the MPC often have divergent views and minutes seem the right way to convey them. But I think what is important to keep in mind is that the resolution reflects the majority view, whereas the minutes are the individual views of the members. I think that is something for the markets to keep in mind.

Debiprasad Nayak
Wall Street Journal: Sir, how much more pain is left in the bad loan resolution process and if there are more farm loan waivers later this year in the state elections? How do you see those things?

Dr. Urjit R. Patel: I will request Mr. Vishwanathan to answer the first part. The second part is that the farm loan waivers so far that have been given, have been done through the budgets of the individual state governments. And therefore, the implications on the banks' NPAs directly is not there.

N.S. Vishwanathan: See, you have taken out of the financials reported by the banks, much of it is given by better recognition of NPAs. And a notable feature of this is, if you see the PCR, i.e., the provision coverage ratio of almost all the banks have gone up substantially. And this also we have to see in the context of the kind of resolution that we have seen in the two large cases that have happened where in both the cases the banks are in the money because the provisions held by them were much higher. And we believe that some of the other cases that are in the pipeline, if they are resolved in the same manner, the banks will have some right back in terms of provisions that they have made, so we believe that going forward, things should kind of improve.

Pradeep Pandya CNBC Awaaz: Sir, the question is, you have recently seen that the outflow of foreign investors this year from January till date, is nearly of the same levels that was in 2008. So, the measures that you have taken are they taken keeping this in mind? Do you think this rate hike will help you hold back the money that is going out through the debt market? And you recently wrote an article in an international paper, do you feel that this outflow of money is because of other big central banks policies, so you are taking up this issue at present?

Dr. Urjit R. Patel: Absolutely not. The monetary policy as I just answered is determined by our inflation targeting mandate and not by anything else. To that effect, if there are international financial or crude oil or commodity price developments, then that is internalized in the inflation forecast projection and the consequent policy choice.

Thank you.