<u>Interview with The Times of India on March 8, 2021 - Shri Shaktikanta Das, Governor, Reserve Bank of India</u>

What is your assessment of the economy?

Growth impulses are gradually and steadily getting broad-based. The high-frequency indicators such as steel consumption, PMI for manufacturing and services are expanding, GST collections and e-way bills are showing improvement. Earlier, there was an impression that it was due to pent-up and festival demand. But now, it is genuine demand that is visible. The vaccination drive is giving greater confidence to consumers, so the demand is expected to sustain.

The only downside risk is the recent spike in the number of Covid cases in certain parts of the country. With daily vaccination numbers going up, we should be able to contain a further spike. But we need to be watchful. International crude and commodity price increase renders some amount of uncertainty, not just to the process of revival in India, but globally, which can have an impact. There is always a demand-supply balance that plays out in the commodity space.

Is credit flow an area of concern?

Overall credit growth has now crossed 6% after remaining low for a prolonged period.Deposit growth (YoY) is around 11.5%. Credit in the retail sector is picking up. What needs to pick up is loans to industry and manufacturing. The benign financing conditions resulting from RBI's action in reducing interest rates and making liquidity available in abundance have been utilised by corporates to raise money and deleverage their balance sheets. There was a lot of repayment of previously availed high-cost loans.

There is space in their balance sheets to invest. According to our monetary policy statement, capacity utilisation is around 63%, which is an improvement over previous months. Once capacity utilisation starts picking up and with all the positive trends on growth, and the scope for leverage, there should be more credit offtake by corporates and businesses in the months to come. There is enough credit available for any business with a good proposal and a good balance sheet.

Do higher commodity prices and hardening rates limit your ability to cut rates?

Interest rates are in the domain of the monetary policy committee (MPC). The hardening of bond yields currently is an international phenomenon. But what is important to note is that communication from almost all central banks is quite similar. Every central bank is on the same page in terms of commitment to support the process of economic revival, avoid any premature withdrawal of liquidity and avoid premature tightening of monetary policy.

What can be done to carry the process of government borrowing smoothly given the high bond yields?

The RBI remains committed to implementing the government's borrowing programme in a non-disruptive manner. Some questions have been raised about the size of borrowing. Next year (2021-22), the gross borrowing is around Rs 12 lakh crore, the net is around Rs 9 lakh crore. In the current year, we have done open market operations (OMOs) of Rs 3 lakh crore and next year also we will do Rs 3 lakh crore, or more, depending on the situation.

We have extended the held-to-maturity dispensation, which opens the space for another Rs 4 lakh crore. Against the net borrowing requirement, already Rs 7 lakh crore is on the table. As for the gap and state government borrowings, we have assured the provision of ample liquidity in the system.

One important signal in our latest Operation Twist notification is that we are injecting liquidity via OMO purchase of Rs 20,000 crore but we are taking back Rs 15,000 crore through the sale of short-term securities. This is a change from our earlier position. We are signalling that RBI will support the market with adequate liquidity at appropriate places, where required. We are injecting liquidity at the longer-end of maturity.

The actions of the central bank should be read from its communication, its actions, and its signals. The latest notification is an action plus a signal. I have already said the yield curve is a public good and there should be an orderly evolution of the yield curve because every market participant is a stakeholder. The US Fed has also recently said the yield curve cannot be disorderly. Again, you can see all central banks are almost on the same page.

Crude prices are rising and retail fuel prices are at historic highs in India. What are your views on tax cuts by the government?

The tax cut has to be a coordinated action by the Centre and the states. International crude prices have touched $67-68 per barrel, while they were around $70 just before Covid hit. It's a very dynamic sector and if prices harden further, shale should hit the market and that can have a sobering role.

Is it time to look at GST?

It is provided for in the Constitution. It is for the GST Council to take a call. It is desirable in the medium or long term, but its implementation may involve some revenue sacrifice initially by the Centre and the states.

The inflation target is up for review. Your views?

It has to be consumer price inflation. It's the pattern world over. Inflation management is very important for the common man, especially the poor. A reasonable level of inflation is good for the economy. A stable inflation framework and a stable inflation outlook and anchoring of inflationary expectations help in attracting investment, both domestic and foreign. Work done by the RBI research team shows that inflation over 6% can be negative for growth.

How does one save the savers in a falling interest rate scenario?

For savers, the first thing to be checked is inflation because if inflation goes very high, then obviously the real return for the saver gets reduced. Therefore, the first thing is to have inflation within the target range; ideally, it should be 4% but depending on exceptional situations as we had in the Covid times, the MPC decided to tolerate inflation of about 5% or a little above 5%.

That is because the situation demanded it and you could not have prematurely gone for a tightening of the rates. Inflation did go up for a certain period but has now started moderating. Second, we have reduced the policy rates from 6.5% to 4%, which in the history of RBI is one of the lowest. Therefore, when the rates have come down there is an issue for savers. It is for banks to evolve the products. With regard to small savers, I would like to say that various instruments under small savings schemes are available.

Is there a need to look at some sort of a penalty mechanism for banks for technical glitches which hurt consumers?

We are constantly evaluating the technology of banks. It is very important that they should continue to invest in technology. An increase in the asset side of banks, an increase in loan books should be accompanied by simultaneous investment in technology. In fact, investment in technology should precede the expansion of the business of banks. You have to have the capacity to deal with a wider volume of operations and that is also something which we examine as part of our supervision. We have an enforcement system whereby such lapses can attract supervisory action and/or monetary penalties. These sorts of actions are already being taken. From time to time, we levy monetary penalties on individual banks for lapses, including technology failures.

Recently, we have issued guidelines for introducing a system of disincentives for banks under the ombudsman scheme. If grievance resolutions are delayed, there will be a penalty in the form of recovery from banks of the cost of handling complaints under the banking ombudsman scheme. This is expected to act as a disincentive. It is not the quantum, but it is the signal. We are giving the highest importance to technology and we will not hesitate to take any action as may be warranted to see that technology is kept robust and in tune with the requirements.

What should be the ideal path that the government should take in the proposed privatisation of two public sector banks and does it also mean that the corporate sector should be allowed?

Amendments to the Bank Nationalisation Act would be required because, under it, the government enjoys special powers, the government is not just an ordinary majority shareholder, it is a privileged shareholder with special powers. Second, which kind of banks? It is for the government as the owner of the banks to decide and from the RBI's point of view, we would be particular about two things: One, the entity (or the individual) which takes over the bank meets the RBI's fit and proper criteria, and two, what size of additional capital it is bringing to the bank.

There was an internal working group, which we had formed. If you look at the RBI's regulatory framework for scheduled commercial banks, it evolved over a period of time. Depending on when a particular bank got a licence, a different set of regulations applies to it. There was a need to synergise the regulatory framework for banks irrespective of when the licence was granted, whether it was granted 20-25 years ago, or it was granted recently, about 7-8 years ago. There was a need to bring in consistency and uniformity in the regulatory framework.

Besides, the Indian economy has grown and is expected to grow further. There is a need for greater credit penetration, improving our credit to GDP ratio. How do we ensure that it happens? Technology is also evolving, the economy is very dynamic. India is increasingly becoming globally integrated and our banking sector should keep pace. Therefore, in this background, we formed the internal working group which has given its recommendations. Our idea of putting it in the public domain was to have an informed discussion and get stakeholders' inputs. The inputs have come and are under examination. We will take a suitable decision on this in due course.

What are the concerns over cryptocurrencies?

I would like to say that there are two aspects. One is the technology that is blockchain or the distributed ledger technology (DLT). The technology needs to be harnessed. There are many positive applications that need to be exploited keeping in mind of course their high energy consumption. The other aspect is the cryptocurrencies, where some sort of digital codes are being traded. On that, we have major concerns which we have communicated to the government and now it will take a call and perhaps go to Parliament as may be required.

What are your views on the soaring stock markets?

The investor will have to take his or her own decision. But as the central bank what I have observed and said is that there is a divergence between the real fundamentals of the economy and certain segments of the financial markets which appear to be moving much ahead of the curve. In the normal course of things, both will adjust to each other. In situations like these, it is essential that every investor takes a very judicious call and not get carried away by short-term trends or developments and particularly small investors need to be very watchful and take their own decisions.

The IBC has been suspended and some banks are not keen on the freeze to be lifted. Your views?

The amendment to the IBC has a sunset date and it is expiring on March 25. I am not aware of any bank wanting an extension of that date. The RBI came out with a resolution framework for Covid-related stressed assets on August 6 last year. It would be better for borrowers to avail the benefit under that particular restructuring package and move on rather than remain static. That framework needs to be utilised.

Further, a very positive development in recent months has been that both public and private sector banks have proactively made provisions for the Covid-related stressed assets, notwithstanding the moratorium which was granted by RBI and the asset classification standstill which is operational at the moment in view of the Supreme Court orders.

RBI has talked about the possibility of a spike in NPAs and about the need for banks to be ready with capital…

In our latest financial stability report, the baseline stress scenario is 13.5% and in a severe scenario, we have given a higher number. The first thing to be noted that it is not a forecast and we have said that in very clear terms in the report. It is a projection based on certain models and the purpose of making this projection is to sensitise the financial sector players, especially the banks, to proactively take steps to protect and preserve the soundness of their balance sheets.

The banks have also responded quite positively, and this is something I have been articulating right from July last year, that is the need for additional capital by every bank, both public sector and private sector banks. Both groups of banks have raised additional capital in the last few months.

How has your experience as a civil servant helped you navigate one of the most turbulent times in history?

More than 40 years ago I did not do MA-economics, I did postgraduation in a different subject. But over the last 40 years, because I started my career in civil service in 1980, I have been a very keen observer and a keen student of the Indian economy and I was also fortunate to have worked in the economic sector both at the state and Central level for a sufficiently long period of time.

As a civil servant, what helps is that it places you in a very unique position where you take a 360-degree view of things from day one of your career. You learn how to read the nuances and the complexities of every problem and how to deal with real-life challenges. You are aware from day one that action has to be timely, it cannot be delayed and it also should not be premature. This is something civil service teaches you.