

RBI Post Policy Conference Call with Press

April 20, 2010

{Transcript}

**MODERATORS: DR. D. SUBBARAO – GOVERNOR, RESERVE BANK INDIA.
DR. SUBIR GOKARN – DEPUTY GOVERNOR, RESERVE BANK INDIA.
MRS. USHA THORAT – DEPUTY GOVERNOR, RESERVE BANK INDIA.
MRS. SHYAMALA GOPINATH – DEPUTY GOVERNOR, RESERVE BANK INDIA.
DR. KC CHAKRABARTY – DEPUTY GOVERNOR, RESERVE BANK OF INDIA
MS. ALPANA KILLAWALA – CHIEF GENERAL MANAGER, DEPARTMENT OF
COMMUNICATION, RESERVE BANK INDIA.**

Moderator Ladies and gentlemen good afternoon and welcome to the Post Policy Press Conference hosted by the Reserve Bank of India. Dr. D. Subbarao, Governor Reserve Bank of India will first make a short statement outlining the stance and measures of the monetary policy for 2010/2011 announced earlier in the day today. After this the press present in RBI Mumbai will ask questions. This is expected to go on till about 03:45 PM. Those who are connected through the telephone lines will be in listening mode at this time. Around 03.30 PM the telephone lines will open for questions. Those connected through telephone lines and want to ask a question may please press * and 1. If you should need assistance during the conference call please signal an operator by pressing * and then 0 on your touch-tone phone. Please note that this conference is being recorded. At this time I would like to hand the conference over to Ms. Alpana Killawala from RBI. Thank you and over to you.

Alpana Killawala Thank you Melissa. We have here Governor Dr. D. Subbarao, Deputy Governor Mrs. Gopinath, Mrs. Usha Thorat, Dr. Chakrabarty and Dr. Gokarn. There are other senior officials of RBI to answer your questions. I will now request Governor to make his opening remarks. Governor.

Dr. D. Subbarao Welcome from my side to yet another Post Policy Press Conference. As has become standard practice by now. I have a press statement which will take about 5 minutes to read, thereafter we will take your questions.

This morning I had a meeting with the CEOs of major banks where we announced the annual monetary policy for 2010/2011. Based on subject a wide array of stakeholders in the run after this policy I have taken their views on board. Let me first briefly summarize the main points of our discussion with the banks, before I spell out the Reserve Bank's Policy Stance.

Banks welcome the Reserve Bank's Policy Stance, they agreed that the monetary measures announced by the Reserve Bank today were appropriate given the growth inflation dynamics. Apart from monetary policy discussions centered around 3 specific measures, 1) Government market borrowing program 2) Financial inclusion and 3) Infrastructure financing. Banks indicated that the program the government borrowing may not crowd out private sector demand given the projected level of resources in the system. Banks have assured the Reserve Bank that they share their commitment to financial inclusion and indicated that they will work innovatively to promote financial inclusion. Banks are concerned about growing exposure to the infrastructure sector. Although they welcomed the measures initiated by the Reserve Bank to promote infrastructure financing by banks, they indicated that there is need to develop alternative sources for financing to supplement their efforts.

The monetary policy for 2010/2011 is set against a rather complex economic backdrop although the situation is more reassuring than it was a quarter ago, uncertainty about the shape and pace of global recovery

persists. Private spending in advanced economies continues to be constraint and inflation remains generally subdued. The emerging market economies are significantly ahead on the recovery curve, but some of them are also facing inflationary pressures.

In India economic recovery, which became around the 2nd Quarter of 2009/2010 has since shown sustained improvement. Industrial recovery has become more broad based and is expected to take further firmer hold on the back of rising domestic and external demand. After a continuous decline for nearly a year exports and imports have been expanding since October and November 2009. Flow of resources to the commercial sector from both bank and non-bank sources have picked up. Surveys by the Reserve Bank as well as others suggest that business optimism has improved. On balance under the assumption of a normal monsoon and sustained good performance of the industry and services sector for policy purposes the Reserve Bank projects real GDP growth for 2010/2011 at 8% with an upside bias.

The developments on the inflation front are worrisome. Headline Wholesale Price Index inflation accelerated from 1.5% in October 2009 to 9.9% by March 2010, what was initially a process driven by food prices has now become more generalized. Going forward 3 major uncertainties cloud the outlook for inflation i) The prospects for monsoon 2010/2011 are not yet clear. ii) Crude prices continue to volatile. iii) There is evidence of demand surge prices building up. On balance keeping in view domestic demand supply balance and the global trends in commodity prices the baseline projection for WPI inflation for March 2011 is placed at 5.5%. Consistent with the above growth and inflation projections we are looking ahead to growth in non-food credit of scheduled commercial banks of 20%.

A few words about the Government's market borrowing program, even though the fiscal deficit for 2010/2011 is programmed to be lower, fresh issuance of securities in 2010/2011 will be 36% higher than last year. Managing the borrowing program is going to be more challenging than in last year for 3 main reasons I) The option of liquidity management through OMO MSS which were used extensively last year will be limited. II) Private credit demand will pick up making crowding out a potential possibility. III) Finally inflation pressures will be stronger. Regardless the Reserve Bank will ensure that credit requirements of both the government and the private sector are met.

Let me turn to risk factors, while the indicative projections of growth and inflation for 2010/2011 may be reassuring we need to recognize the major downside risk the growth are upside risk to inflation. A) Uncertainties persist in the global macro economic environment. B) If the global recovery does gain momentum commodity and energy prices may harden further which could add to inflationary pressures. C) Any unfavorable monsoon rainfall pattern could exacerbate food inflation and dampen rural consumer and investment demand. D) Large capital flows will pose a challenge for exchange rate and monetary management.

A few comments on the exchange rate management, our exchange rate policy is not guided by effect or pre-announced target or band. Our policy has been to retain the flexibility to intervene in the market to manage excessive volatility and disruptions for the macro economic situation. Recent experiences has underscored the issue of large and often volatile capital flows influencing exchange rate movements that go against the **grain 8.06** of economic fundamentals and current account balances. There is therefore a need to be vigilant about a build up of sharp and volatile exchange rate movements and it's potentially harmful impact on the real economy.

Our Monetary Policy Stance for 2010/2011 has been guided by the following 3 considerations. a) Despite the increase in 25 basis points each in repo and reverse repo rates in mid March our real policy rates are still negative. With the recovery now firmly in place we need to move in a calibrated manner in the

direction of normalizing our policy instruments. b) The current episode of inflation which was triggered by surplus led practice is now developing into a wider inflationary process. There is therefore need to ensure that the demands led inflation does not become entrenched. c) The third consideration that informed our monetary policy stance is the need to balance the monetary policy imperative for absorbing liquidity and ensuring that credit is available to both the government and the private sector. Against this background the stance of monetary policy is intended to first anchor inflation expectations while being prepared to respond appropriately, swiftly and effectively to further buildup of inflationary pressures. Actively manage liquidity to ensure that the growth in demand for credit by both private and public sectors is satisfied in a non-disruptive way and maintain an interest rate regime consistent with price output and financial stability.

Accordingly you know our annual policy we have made the following decisions. The repo rate has been raised by 25 basis points from 5% to 5.25% immediate effect. The reverse repo rate has been raised from 3.5% to 3.75% immediate effect. And the CRR of scheduled banks has been raised by 25 basis points from 5.75% to 6% effective fortnight beginning April 24, 2010.

We expect 4 major outcomes from the above policy action. 1) Inflation will be contained and inflationary expectations will be anchored. 2) The recovery process will be sustained. 3) Government borrowing requirements and private credit demand will be met. 4) And finally policy instruments will be further aligned in a manner consistent with the evolving state of the economy.

The Reserve Bank will continue to monitor the macro economic conditions particularly the price situation closely and take further action as warranted. As is the standard practice this annual policy statement also covers development and regulatory policies. These measures aimed at carrying forward financial sector reforms, promoting financial inclusion and ensuring better customer service. Thank you very much.

Kalpana Killawala

Before I start the questions, one request, second and third row who do not have access to the mic, please wait for the mic to arrive to you. Yes.

Participant

You know we spoke to the bankers who came and talked to us after your chat with them, they seem to indicate that even after this round of hikes both in the repo and reverse repo and CRR there would not be immediate hike in lending rate this on top of the CRR hike that earlier plus that you did in March in terms of repo rate, would you then say that the measures that you have taken right now are still going to be effective in helping tame inflation and inflationary expectations or are you still in the play where you are happy with sending out a message and then later on if you need to have stronger measures on inflation you will do so, because the immediate impact on the system may not pull through.

Dr. D. Subbarao

I believe that what we have done is in accordance with a calibrated move towards normalizing policy rates. You know people talk about two ways of doing reforms for example there is the Vaclav Havel, the Velvet Revolution which says that "you cannot cross a chasm in two leaps". There is a Deng model which says that you "cross the river by filling the stones". So what model we had talked at any point of time depends on what the situation is and we believe that we must cross the river by filling the stones. We have taken into account the macro economy situation as it has evolved over the last 6 months, we have made our internal projections about liquidity, about growth, about inflation over the next 6 months and taken that into account we have calibrated the policy accordingly this morning. Yes banks have said the lending rates may not rise immediately, but that is okay because we are aware that we need the balance between growth and inflation. And we are also sensitive to the fact that growth is coming from sectors which are interest rate sensitive.

So I believe that what we have done today is along a roadmap that we have for normalizing policy rates.

Lata Venkatesh

Lata Venkatesh CNBC TV-18. Dr. Subbarao you have said that inflation problem is fairly serious, a strong statement like the balance of risks have shifted from slowdown to inflation, you have said that India is an outlier in terms of inflation being much higher than other countries and definitely as an emerging market country. And you have pointedly said that you are now even now in a negative year interest rate scenario. In spite of it the policy move is a bit small step of a 25 basis which means that we are going to remain in a negative real interest rate scenario for practically better part of the year if not the entire year. How would you justify this very small move, would it be that you think you will move many times and not just during policy.

Dr. D. Subbarao

So let me answer your second question first about whether we will move many times, at this time it looks like we have moved many times, okay. But the second part of the question is whether we will move a mid cycle. Let me explain that because this is an opportunity to explain that, we have moved mid cycle in March and that is not something we had done lightly, we had done that after considerable thought, because we thought it is advisable not to waste another 5 weeks till the scheduled policy. I will not rule out mid cycle action, because we do not know how the situation will evolve, but I want to say that that is not something that we will do lightly, we will think many times before taking mid cycle action. So while it is not ruled out it is not something that is part of, that is going to become routine. The second question, which is more substantive about whether we still in the negative territory and how do we justify being in a negative territory, I guess I have to paraphrase what I said earlier which is that yes our policy rates are negative, real policy rates are negative even after today's adjustment, but we have taken into account the inflation dynamics as we see them over the next several months. We have taken into account the liquidity in the system, we have taken into account the government borrowing requirement, we have taken into account the revival of private credit demand and taking into account all these factors we have calibrated today's policy action. And everything need not be done in one step and we believe that moving in several baby steps towards normalization is better for the economy to adjust to a pre prices growth..... Subir:

Dr. Subir Gokarn

I think people do get a little obsessed with the headline inflation number 9.9, 9.89 but to also emphasize that one of the main drivers of our calculation and our action both in the March announcement and today is the non-food manufactured inflation rate. That move from a negative 0.4 to a positive 4.3 in February that was a substantial move and in fact that was from our viewpoint the sort of unanticipated component or driver of inflation which sort of precipitated our action in March. And now it is at 4.7% so we take that as essentially reflecting the underlying demand, it is clearly not as significant an issue as a 9.9% would suggest. Given that that our actions are not normalization with the idea of comparing or reining the possibility of a demand spike, I think our actions are entirely consistent with the situation. The food price dynamics are as has already been pointed out really not within our control and the monsoons will make all the difference in terms of whether expectations of moderation over the course of the year are going to play out or not, but we do not know where that stands. So I think the shift in inflation dynamics from almost entirely food till about November of last year to now more than half coming from non-food manufacturing that has really been the big consideration and that is really what we mean by the balance of risks having shifted from slowdown to inflation that is really the underlying driver that we are picking.

Lata Venkatesh Can I ask a supplementary question sir? Post you mentioned non-food manufacturing inflation as the trigger for that what you call unusual mid cycle rate hike, would that be the key parameters you will watch to take a step which you have considered not a nice step or what other parameters would you watch which would worry you?

Dr. D. Subbarao That will be not be the only parameter that we will watch, that is the short answer to your questions. If I ask my Reserve Bank colleagues, they will want me to say that we have a multiple indicator model, which takes into account a macro economic situation, the returns from various financial markets just before they start with a number of other macro economy variables to study the situation, but since I do not study the model I get informed by them, I get advised by them, but we will look at non-food manufacture inflation, we look at non-oil imports, non-coal imports we will look at IIP, we will look at credit growth, we will look at the fuel inflation, we will look at commodity prices, we will look at global prospects, so a number of variables in fact variables that you monitor that we monitor will be the same okay. So the sense I want to give you is that as much as we have been talking about non-food manufacture that will not be the only indicator we will look at.

Dr. Subir Gokarn This number itself has to be seen in a context, and the context in which we have seen it now is capacity. We have seen over the past few months, increase in capacity. We have a survey which measures this you know we are getting indications from analysts as well. And overall across the work capacity utilization is increasing. In this scenario the threat or the risks of commodity prices and food prices, energy prices spilling over into sort of sustained inflation process increase. So I think that is really one very important indicator for us and that is something we basically observe on a quarterly frequency because we, the surveys take a long time to complete. First in the context of capacity utilization pricing power, corporate performance that we look at this inflation numbers and that allows us hopefully a more sort of reassured, a more confident judgment on whether this pressure is sustainable or whether it is just temporary phenomenon.

Alpana Killawala Pradeep.

Pradeep One more, inflation that you stated in the yesterday's report as well as in today's policy that you have talked about is the asset price inflation. You have said clearly that property rates in Mumbai especially have gone over the last peak, but you have not taken any steps that you have not taken specifically and the bankers with whom we have talked after the meeting they also said that they will not increase the EMIs, so rate is not going to increase on housing loans so why it is like that you are showing so much worrying, but not taking any steps.

Dr. D. Subbarao What we have done today CRR hike and rate hike, that will have an effect on asset prices. Other than that, what you are asking that why provisioning norms, risk why you have adjusted? In the October policy we did the risk adjustment for commercial real estate taking it from 0.4% to 1%. We looked at the numbers and actually credit to commercial real estate has come down in proportion terms. So now you do not need to adjust it further. From now onwards please adjust it then we will do it, now whatever action we take in October is still working through the system and is beginning to have an impact. Usha, is there any, you have any specific numbers? No, thank you.

Namita Namita from CNBC Awaaz, I wanted to know that for inflation you have done till March 2011 projection you have given to us, is it down the line like RBI would be comfortable target, internal target if you have set it, that what is the target number we would like to know?

Dr. D. Subbarao No, our internal target for 6 months is nil, then also the trajectory we have given in document, do not read that as a trajectory actually because we have to draw a chart, it has to be continuous it could not be a broken thing, okay, but you know inflation does not move in things it just moves somewhat and a trend start you know. So you can see that there is a trend but it may not go in a straight line but it might stay at this level for a few more months and because the base effect was taken in June, will because of the base effected is set forth on after that.

Participant Sir could you give us a timeframe as to till when do you see this inflationary pressures staying firm and also you have given an estimate of 5.5% for this financial year, could you give us the reasons as to what are the factors that could be supporting that number?

Dr. D. Subbarao You know I do not want to venture trajectory from today's 9.9% to 5.5% but as if we were studying the numbers and figures we have access to the same thing. So we believe that inflation will, might stay at this level for the next few months. And after that because of the base effect, because of the supply side factors coming in the Rabi crop will come in, commodity prices might adjust, demand might pickup, a number of factors might work from both sides, they will work on the inflation trajectory. About why it has come down, you know again first on the food side there is the prospect of better Rabi crop, there is prospect of hopefully a good monsoon if the monsoon is good that should soften inflation. Commodity prices it is not clear but if global recovery is as gradual as we now believe it to be, commodity price just may not firm up. So, all those factors that have an influence on inflation. Anything I missed out Subir?

Subir Gokarn No, I think we the point I will emphasis is that we are looking at March 2011 with the 5.5% expectations as an outcome of many things but most importantly a normal monsoon. So the expectation of any softening in inflation is based on this outcome that the monsoons will not be disastrous. At this point we have very early indications which have typically been the case that a near normal monsoon is forecast but it is not the aggregate number that matters it is the way which it is distributed across the country and also across the four months period of the monsoon so both of these are unknown parameters at this point. If the monsoons are normal, if food production is normal than we will certainly see a softening of food prices, but the same time if the recovery is consolidating and capacities are getting stretched then we would see some hardening of the manufactures sector pricing. So it is a balance between these two forces that is going to drive the inflation trajectory. And our actions are aimed that softening the later which is trying to keep a check on the growth, the pressures on non-food manufacturing prices. So our forecast or projections of 5.5 is based (1) on normal monsoon (2) that the actions we are taking now we have taken today and possibly take in the future will actually have the desired impacts in terms of reining in inflationary expectations putting some sort of limits on inflation process.

Alpana Killawala Bijoy from Newswire.

Bijoy Sir Bijoy from Newswire 18, sir you have been stressing on monsoon as the key factor whereas my MET department is supposed to come out with it's forecast over the next few weeks. Do you feel that it is a time when you could probably start looking at reviewing the policy that you are looking at and the figures and the forecast that you have come out with sir, would it be possible that you would look at it in mid cycle?

Dr. D. Subbarao No, that alone will not trigger a mid cycle action. Mere forecast of a normal monsoon will not trigger any actions, okay we will have to study this with the number of others factors. And again let

me reiterate that we are not going to do a mid cycle action likely at the same time I do not want to rule it out.

Alpana Killawala

Aniruddh.

Aniruddh

Governor you mentioned the need for foreign banks to kind of operate a subsidiaries in India that is considered merit in foreign banks operating subsidiaries, sir could you kind of elaborate as to why you feel this way and also secondly you have mentioned the need for financial conglomerates or banking holding companies. So what exactly is the need for this and also in the kind of the backdrop of the very public spat between two other regulators IRDA and SEBI, how exactly does RBI plan to go about regulating financial conglomerates?

Dr. D. Subbarao

Okay, as I see there are three questions there, first about this proposed study on foreign banks. As you know under our current policy foreign banks can come either under the branch mode or as under the subsidiary mode. For whatever reason all foreign banks have chosen to be present in India through the branch mode, after the crisis there is a vigorous debate internationally on the advisability of having foreign banks on their performance during the crisis, how they should be regulated, how they should be supervised. We are participating in that discussion. There is no final view yet, in fact I should say that our experience with foreign banks has been less disagreeable or I would say that we had it is not bitter like many other countries have had. However, for the purposes of cross-border supervision for the purposes of ensuring that banks which operates in India, serve India's interest first. And for the purposes of having a standard model we thought we should study whether it will be advisable to have foreign banks come in only as subsidiaries. However, we believe that we must get wisdom and advised from outside of the Reserve Bank, for that purpose we are going to do a discussion on paper and put it down and we look forward to your suggestions, Usha anything else.

Mrs. Usha Thorat

Yeah this is one of the three major suggestions in this policy, actually the holding company's recommendation for having the bank holding company is a small exercise by the Committee of Financial Sectors Reform because it was observed that the absence of the holding company structures imposes the investors and the depositors and the parent company to risk in that same to the parent company's ability to fund their own core business and it could restrict the growth of subsidiary business. Very often what happens is that the bank itself would be the holding company than only subsidiaries activities in the same proven to be the risk for the banks itself. So holding company structure where there is a holding company with various activities as part of the entire conglomerate is found to be better way, but even on this issue like the **(Inaudible) 31:23** issue there is a lot of discussion, but we had asked setting up this working group which we looked into sort of a legal issues also to be examined. So we will have what is a group to actually work out the modalities by which a holding company could be setup particularly a bank holding company. And it is correct that within the bank lead financial conglomerate there are entities which are doing insurance business and which are also doing asset management business, currently there is a framework for supervising this financial conglomerates for where if the predominant for business is the banking business, the Reserve Bank is regulator and we have the other regulator also coming and sitting with us and looking at the kind of data that comes from this conglomerates and we try to look at the conglomerates as a whole.

Participate

Just a follow up on that, so should we understand that the RBI more or less is in the favor of bringing in the bank holding company is just a question of a structure being put in place if there are guidelines or which is going to get into instituted at least conglomerated in public domain.

Mrs. Usha Thorat

It would be better to do it as early as possible that obviously they will be taking a sorry we have not....report but we have just said that we are taking up....yeah because there are legal issues and amendments which will of course we cannot put a timeline on that, but we could like this working group to get at that as well.

Participant

Now you know the last policy have made give a entrepreneurial important to the fiscal consolidation a company monetary tightening so then monetary policy is effective. So I do would want to understand at this point in time do you think that fiscal consolidation if you think would a monetary policy timing in your efforts to contain inflation and secondly the high governments spending how do you see that limiting the effectiveness of monetary policy in containing the inflation?

Dr. D. Subbarao

Thank you very much, you would note that we have made a comment on fiscal consolidations because when we did the January policy that was before the budget, now the budget has come and it begins to part of fiscal consolidations from 6.8% to 5.5% fiscal deficit, 5.5% to GDP in 2010/2011 which is good. And in formulating a monetary policy stance we have taken into account the implications of that fiscal policy as you know the government borrowing programs, but it must be recognized that in reducing from 6.8% to 5.5% there were certain one off factors that it helped for example the revenues from 3G for example that it reduced commitments on 6th Pay Commission, reduced commitments on farm waiver all these issues that you people have talked about after the budget. So going from 6.8% to 5.5% was a challenge, but was lesser the challenge is then what the forward moment is going to be from 5.5% to wherever we have to go 3%. So we have taken that into account and we have also set that the government going forward must keep in view the need to make fiscal consolidation more broad-based not depend only on cash effort but also look at expenditure restructuring. We have also, we also believe that it is important for us as an economy to look at the quality of fiscal adjustment as we consolidate.

Ritesh

Governor Ritesh here from Zee Business there has been given a lot of emphasis on customer service it is being said that there have been a lot of complaints have been coming, there is a committee formed and it has also been said that RBI overall is not satisfied with the grievances mechanism so is there a trend that private sector bank or public sector banks receive more complaints, either of them all for that matter foreign banks and what kind of customer services did RBI actually not right now happy with?

Dr. D. Subbarao

I will answer this question and I turnover to my colleague Dr. Chakrabarty, for supplementing what I have said. It is not that there is a difference, you know we get a lot of complaints, I get mail every day and bulk of the mail that I get is from people from across the country writing about customer services because the Reserve Bank and the Governor Reserve Bank is the name that comes to anybody who had a bad treatment or unsatisfactory service at a bank, but I do not believe that there is a difference in trend as between a foreign banks, private sector banks and public sector banks. All banks are good, all banks are bad to the same extent. We have been concerned that customer service must increase as part of the process of financial inclusion. If you want a poorer people we want people lower income people getting to the banking sector we must make sure that the service they receive is good and they will come that is the motivation for paying great attention to customer service. And our views on where the defects are where egregious practices are is shaped by the type of complaints we get. And pensioners write to us, people who have borrowed from banks write to us, people who have taken credit cards from banks write to us and companies who have borrowed also write but that is less so. So the idea is not to replace any system but the idea is for the Reserve Bank to understand what customers _____37.27 address the systems banks have

and to see if they are efficient, to see if they are sensitive, and collectively on that basis what lessons can we draw and what lessons can the banking system draw. Dr. Chakrabarty.

Dr. KC Chakrabarty

Customer service what the Governor said is right we do not want to dictate the bank that you give good customer services, give this type of service, that is in the banks interest for customer service because it is a very competitive environment whoever will give good services that will get a good business, then also people are asking that why Reserve Bank does not focus on this, because one thing is there, banking is that one type of business like where competition is not as open as we are regulating it, everyone does not get entry in it. So that is our responsibility that minimum standard of service is given to people, we are not going to show that service is also very bad because we are showing that also we are not showing that that if customer has any complaint or not, we have around 30 Crores customers for bank, 85,000 branches are there, everyday we have around 50 lakh transaction is happening, in that there is some problem in that, we want to know that when customer is going to bank, listen to the customer and that complaint that are saying that should be solved in good manner. That system is there or not so what study we are showing to you, we are going to make committee that they will see that this factor would do in one way or not, if it is not doing the work than what type of discipline is needed in this. So we have like that that complaint is there but if customer is going to bank, their problem should be solved as early as possible and indifference attitude should not happen from staff to customer. what changes we need to make, we have offsite and onsite surveillance in this system what is the difference in that, in bank internal structure what should be the changes in that and also what Mr. Governor said that bank's board should focus on this more. We ultimately want that bank for their own interest should improve in customer services. You know by saying of the Reserve Bank the improvement is not going to happen, bank will understand that it is through the customers that our business will grow then only we will see improvement in this and board should see for that.

Participant

Thank you sir.

Alpana Killawala

From customer services we should go to market, Anup Bloomberg.

Mr. Anup

Anup from Bloomberg, I just want to know does India required founder (**Inaudible**) at next (**inaudible**) 40.0 and the other question is that if China revalues its currency what is RBI's has set of impact on the currency, the exports handling charges?

Dr. D. Subbarao

I am not going to make a specific statement on the Yuan, but I do want to say that some countries manage their exchange rate and keep them artificially low. The burden of adjustments falls on countries which do not manage their exchange rate so actively. And this happens both because their imports substituting industry gets hurt and because our exports get hurt. Whether we will take it up in the G20 or not is not an issue that I can discuss, but if and when this is discussed in the G20 Forum we will certainly give our opinion or our view on the subject. What is your second question?

Anup

If China revalues its currency on India's imports and its exports and the currency and economy of India?

Dr. D. Subbarao

Yeah, we have any specific model for that. We do not have a model just to track our prospects based on Yuan's movement. But I have seen the numbers. The trade balance between India and China has changed remarkably in the last seven, eight years. The Chinese exports to India have grown much-much faster than our exports to China. And that obviously is among other things a

reflection or a result of differences in exchange rate management. So I am sure that if China revalues the Yuan, it will have a positive impact on our external sector.

Alpana Killawala At this stage if you do not mind we will take a break and we will take if any other questions from the telephone. And if there are no questions then we will come back to you. Melissa, can we see if there are any questions there?

Moderator Sure. Ladies and gentlemen, we will now begin the question and answer session. Anyone who wishes to ask a question may press '*' and '1' on their touchtone telephone. If you wish to remove yourself from the question queue you may press '*' and '2'. Participants are requested to use handsets while asking a question. Anyone who has a question may press '*' and '1' at this time.

Alpana Killawala Maybe we should continue here for a while. And questioners who have questions on the telephone please. Oh there is one. There is one Pranav Kumar from Northeast TV, Melissa.

Pranav Kumar Question there to Mr. Governor please. May I know what steps that RBI is taking to check the inflation rate because that is going to ruin our economy **(Inaudible) 43.21**. So my only question is that.

Dr. D. Subbarao Pranav Kumar Ji, all the steps we are taking as we have said in the documents and as I have said in the conference, discussed conference is to manage the balance between growth and inflation. We want our policy to support the growth impulses, but we want to maintain price stability. As we have said our concern is shifted over the last six months from supporting growth to combating inflation and current inflation expectations. The actions we have taken in January of raising CRR by 75 basis points, the action we took in mid-March to raise the repo on reverse repo rates by 25 basis points and the action we took this morning to raise policy interest rates and the CRR are efforts to rein in inflation.

Pranav Kumar Thank you, sir.

Dr. D. Subbarao Thank you.

Alpana Killawala Maybe we will take five, ten minutes from Bombay once again and come back to you, Melissa.

Moderator Sure.

Roshni This is Roshni. I wanted to know, sir, what is your view on investment demand and secondly, sir, what is the realistic scope of huge MSS bond given that you did mention that in your report that capital goods **(Inaudible) 45.24**.

Subir Gokarn On the investment question whatever indications we are getting from the production numbers, IIB numbers that capital goods are moving quite strongly as it coming quite strongly. The two most significant drivers of the industrial recovery are consumer durables and capital goods. Within this, of course, commercial vehicles are playing a very important part. Commercial vehicles have really hit a truck in 2008-09, they are now recovering quite strongly, they are still not back to the levels of the previous year. But in terms of the cycles, this is the pretty strong rebuke. In addition to commercial vehicles, machinery equipment is also showing signs of recovery, both of these suggest that investment activity is coming back into the picture. And this assessment has drawn out by both our conversations with the financial sector and our surveys of companies. They suggest that there is more optimism about capital spending because the recovery scene has been pretty

robust and the uncertainties are abating. So we hope that the investment will play significant part in driving the recovery. And of course the long-term consequences of that are very favorable because we will get enhancement of capacity. On the infrastructure front, the policy statement does make reference to the financing on infrastructure, we are seeing a lot of activity in terms of financing, which suggest that projects are picking up, the activities picking up and this also goes very favorably to in terms of the sustainable recovery in terms of larger capacity being created to support the long-term growth process. So we do see investment as having recovered from the downturn of 2008-09 and starting to come back very strongly.

Dr. D. Subbarao

On the MSS question – I will answer that briefly. .Whether we would resort to MSS will depend on how the flows behave and better we intervene in the market. And balance of payments numbers for the last fiscal year are not available. They are not available in public domain; they are not available even to RBI, we only have some tentative numbers. In 2009 end our flows were just slightly above the current account deficit we expect that deficient of the surge will be there, but very marginal, very modest. Maybe about \$10-15 billion. Going forward, there are different estimates about how flows will behave and that is depend I believe on both push factors and pull factors. Global growth prospects, there is a bit of turn in the global markets and the liquidity in the global system. On the pull side, the promise of growth in India, the interest rate differentials and the risk free rates of return in our markets. Should capital flows be far in excess of our current account deficit? And should we believe that that is not consistent with our stable macroeconomic system. If the exchange rate is volatile we may then we have to intervene in the foreign exchange market. And from the liquidity side if you believe that that liquidity needs to be stabilized, we will resort to measures available to us, and if necessary, to MSS norms. It is not clear at this point of time that MSS will do any auction. First of all, it is not clear what capital flows will be. It is not clear whether we will intervene in the foreign exchange market. It is not clear whether we will need to intervene in the liquidity system and it is not clear whether we need to resort to MSS to manage liquidity.

Alpana Killawala

The next question, Melissa.

Moderator

Thank you. The next question is from the line of Bijay Shankar Patel from PTI. Please go ahead.

Joyeeta

This is Joyeeta from PTI. Sir, this is regarding the inflation projection of 5.5%. The Finance Ministry today said that it will be lower than a projection of RBI, the margin projection of 5.5%. And same for the growth projections also like in the today's growth projection is less than economic surveys growth projection. So is RBI a bit conservative on growth trends and liberal on inflation front?

Dr. D. Subbarao

For all our sake I hope the Finance Ministry is right and the RBI is wrong. I hope growth is higher and inflation is lower than our projections. But I saw the Finance Ministry statement and what the finance ministry has said that his forecasts are super imposition of intuition and judgment over statistical models. So we all know that judgments are different, intuition is different, experiences are different. And having worked in the North Block earlier I know that the perceptions from North Block can be quite different from here in the ministry. So I respect the numbers that have come out from the Finance Ministry and I hope they are right.

Moderator

The next question is from the line of Sunidhi Ahuja from Indian Express. Please go ahead.

- Sunidhi Ahuja** Good evening, sir. Wanted to know about the unbanked blocks, still in the country we have 99 unbanked blocks. And you have mentioned that the banks had to submit their financial inclusion plan by the end of last financial year March 2010. First question is have they done it? And secondly, what is your plan on the unbanked areas that are still there in the country?
- Dr. D. Subbarao** Sunidhi, thank you very much for that question. I believe we reviewed this morning with banks and I believe that most banks have submitted their board approved financial inclusion plans. And I will revert to Dr. Chakrabarty to give some details of that.
- Dr. KC Chakrabarty** Banks have submitted their financial inclusions, then there are two aspects. One is unbanked block see there are few unbanked blocks. They maybe in a very difficult terrain either in the northeast or other places. For that already along with the Government of India we have drawn up a scheme that if the state government provides a necessary infrastructure for bidding process we are allowing the banks to open the branches and the exercise has been completed in Meghalaya, we are trying this in Tripura, but most probably all these unbanked blocks will be covered during the course of the year or there is a definite kind of action is there provided some basis infrastructure is available. As regards in the financial inclusion plan not only the unbank blocks there are other villages also where the banking facilities are not available, we are trying to cover up all villages of more than 2,000 population in the first phase and second phase all the villages. I am only happy to say that primarily plan which the banks have submitted they said that 10 banks have said that they will cover more than five lakh villages in the country in the next three years, which is encouraging and we hope as and when this particular implementation of plan will start we will be able to provide the banking services to large section of population.
- Dr. D. Subbarao** I just want to supplement what Dr. Chakravarty said. Much of we are driving this number that every village for over 2,000 population as we covered with access to banking services to some model or the other, we are also concerned about the quality of their access. It is not just that we tick off as soon as the banking correspondent has been appointed for that village or a branch has been opened up, some of the accesses have been provided. We are also monitoring whether the people are opening accounts, how many people are opening accounts, whether the electronics are operational and effective in a real sense and whether they are helping poor people improve their income. And that is something that we do not have much experience in but we could study and push that.
- Sunidhi Ahuja** Okay, great, sir, thank you.
- Alpana Killawala** Gopika.
- Gopika** Gopika from CNBC. The annual report mentions that Basel Committee is undertaking the quantitative impact study and 10 large Indian banks are covered under the study. What could be the impact of the study on the Indian banks, will they necessarily have to compliant with the study? And my second question is a little more specific, which is in reference to a private sector bank called Bank of Rajasthan. What is the course of action that RBI is taking especially against the promoters as well as, if any, against the bank? And RBI is also appointed two consulting agencies the law is to work on its report. Have they submitted the report and what does the report suggests in terms of action to be taken? Thank you.
- Dr. D. Subbarao** Is it appropriate to discuss specific bank issues in this....? Perhaps we will defer that question, okay. We will answer your first question. My apologies for that.

Usha Thorat We refer to this consultative document which the Basel Committee has put out in December and the quantitative impact study which is currently going on where ten large Indian banks are participating in this. Now, as far as the members of the Basel Committee and the banking supervision and to the extent that our banks are still on the standardized approach, more or less whatever is the process we will be in convergence with the international standards, where we have certain timeframe, those timeframes is something that one can always suggest to me or in certain areas we can add on certain additional potential requirement. We do not even know only after the quantitative impact study results are analyzed will the calibration be done or what will be the implication. There is several alternative proposals made. So at this stage it is not possible to say what it would be. Because you do not even know what the ratios are going to be. So we are a part of the international process, we are taking part in the study and this will be calibrated along with the results coming from the world over in the Basel Committee.

Gopika Is the Basel Committee among.....

Usha Thorat No, the selection of these banks is more for a typically in a jurisdiction to give us more important to get the real qualitative data because it is a huge amount of data. So we think it will be quite typical, it would not be fairly representative banks, especially internationally active banks to where this really applicable. So I think this would be quite a good benchmark.

Moderator Thank you. The next question is from the line of Aabhas Pandya from NewsWire18 Delhi. Please go ahead.

Aabhas Pandya Hi, good evening. The Governor mentioned in his opening remarks that managing the government borrowing this year will be a bigger challenge compared to what we saw last year. There is a kind of hope in the market that RBI will use open market operations if required to support the government's borrowing program. What are the Governor's thoughts on use of OMO for this financial year?

Dr. D. Subbarao Thank you for that question, Aabhas. See, I do not want to make any specific comment on whether we will resort to OMO or not. But what I do want to say and I want to reiterate what I said in the statement, what has been said in the printed document which is that, we will keep an eye on liquidity and we will ensure that there is enough liquidity both for the government and for the private sector as credit demand from the private sector picks up. Beyond that it will be inappropriate to speculate on any specific measure because that could send wrong signals. I want to stand by our broad assurance that we are keeping a tight monitoring vigil on the liquidity situation.

Aabhas Pandya Right, thank you.

Alpana Killawala We will take one question from Mumbai Melissa. Yogesh?

Yogesh **(Inaudible) 59.44** private consumption demand need to improve to **59.46** support the growth momentum and outset of the hovering in interest rate how you are looking for the growth in private sector should be matched, which is expected.....

Dr. KC Chakrabarty Well I think the idea there is that the recovery will be sustained, become more robust if there is a greater contribution from different components of demand. When we look at last year's numbers most of the components are sluggish, government was big contributor and net exports, which is the difference in exports and imports were a significant contributor. The fewer the drivers of recovery the more prestige is because any set of any threat can disrupt the process. So the more broad based

it becomes with consumption expenditure being close to 60% of GDP, obviously, even a small recovery impact large component will add substantially to the overall recovery. So we are really thinking in terms of its really a desire to see the drivers of growth becoming more diversified which in a sense will add greater degree of stability to the recovery.

Participant

Three questions actually two bigger issues, one is you talked about globalization moving towards normalization and your policy document is mostly focusing on concerns about inflation Is that a view seen that (inaudible) 1.1.1 between the values and that's probably led to without the inflation you would have probably moved much more slowly towards normalization process as compared to given the kind of inflation condition, that's one. How does the Reserve Bank plan to balance out the rate action with the overseas inflows that expected to come because of higher interest rates in bands attracting overseas inflows it almost looks certain that every time you move rates you move CRR also upwards to the same direction to stabilize? And the third one is in the relation to the bond market. Last year it was an exceptional situation in terms of liquidity and the expectation of the bond market you have to start the first auction of the first year with involvement and then the rates move up and in fact this year the bond markets are probably much more volatile than probably in the last couple of years you have seen? Is there some kind of stability that the Reserve Bank can provide to the bond market in terms of yield, in terms of perception, and in terms of psychology?

Dr. D. Subbarao

Thank you. Very clear questions. The first question that you asked which is whether we would have moved more slowly towards normalization if we were not confronted with an inflationary situation, the short answer is yes. I mean it is quite clear that we did not have the threat of inflation we were moving slowly because we would have supported growth much more. The second question about how do we balance rate action with possible flows from outside. As I told you we are watching the situation. It is not clear how flows will come in, in what form they will come in, and there is a short term flow, there is a long-term flow, debt flows or equity flows or whatever. But, yes, it is true that the interest rate differential between India and advanced countries will be a variable, not the only variable in determining the quantum of flows. As I said earlier there are other variables such as the amount of liquidity in the global system, the global prospect, prospects here, risk free returns here, all those considerations are there. But the interest rate differential is an important variable. To that extent our raising of rates might attract more flows and some flows are necessarily right. We do not want too much in excess of current account deficit and that is what we are hoping for and that is what we will calibrate our policy towards. And on the devolvement issue I will request Shyamala to answer.

Shyamala Gopinath

Actually, the first option there was a very small amount devolve, and in fact, I think that action did lead to a very positive influence on the bond markets and the subsequent auctions and as you know very well the subsequent auctions went off well and even in the first auction there was a good bit of cover ratio and even in the subsequent auction. So I think sometimes actually one has to look at the demand for that paper and sometimes you know, certain judgments have to be made in terms of when you have the tail so I think that was that did have a positive influence. And one, I would like to assure you that we very closely monitor the bond market developments and the sentiments in the bond market and whatever action needs to be taken.

Dr. D. Subbarao

Thank you, Alpana how are we doing on the time front?

Alpana Killawala

I need 10 minutes more sir, 10-15 minutes.

Dr. D. Subbarao

Okay.

Alpana Killawala

Yeah, Aparna, and then Rajendra and then we will take your questions from the telephone.

Aparna

Sir, I have two questions and a clarification one is through your policy stand you have mentioned that you will actually manage liquidity from the new **(inaudible) 1.6.6**, credit demand from private as well the public sector As against we are **(inaudible)** you have specifically mentioned public sector demand are there any specific reasons for you that whatever the entities you are referring to are public are you referring to all the companies..... My second question is about the exchange rate. But I feel serious in this the RBI has been more prominent towards a stronger rupee because oil prices did have inflation in price, so we are organizing a **(inaudible) 1.6.6** panel which we have underwent. What is your position on the exchange rate? Will you be more prominent towards a stronger rupee in the context of import and inflation things **(inaudible)** commodity prices **(inaudible)**. My clarification is on the Para-40 is this like fresh issuances of government securities will give a **(Inaudible)** since you are having the risk last year. And how did you **(inaudible)** is it fresh paper issue as opposed to additional....?

Dr. D. Subbarao

Thank you Aparna. On the first question about active liquidity management to support the growth credit demand on private and public sector what we wanted to convey was that we will look at the credit demand of the entire economy. It is not as if we were implying that there will be greater demand from the oil companies, etc., I do not think that should be interpreted that way. What we wanted to convey again is that we will look at the credit demand coming from public sector, larger public sector which is what the international institutions use public sector to include the government and the larger government sector. Second, on exchange rate management. There have been questions about whether we will use the exchange rate as an anti-inflation tool. No, we will not because if some comfort comes on the inflation side because of rupee appreciation, that is okay, but we do not look at the exchange rate as an instrument for managing inflation. There have been some studies done on the pass through, I have been told before I joined the Reserve Bank I keep being told now that the pass through from the exchange rate to inflation is uncertain. When we had an economist meeting a week ago different economists had different models. The currency and finance report of the Reserve Bank of 2004-05 has done a study, which states that if your exchange rate appreciates by 10% that will have a .0.4% impact on inflation. But that is 2004-05, I do not know whether that is still true today. So the short answer to your question is that we do not use exchange rate as an inflation management tool. On the fresh issuance of securities 36%, this is about debtor securities of the central government alone. You take the next issuance, take out from that any MSS, any OMOs and you will get the figures and the figures that I have are 251,000 crore, this is net supply of fresh securities 251,000 crore for 2009-10 and 342,000 crore for 2010-11, which is 36%

Shyamala Gopinath

Yeah, I think she talks about reissuances. What we mean is a net supply. That is what the Governor explained, so it is not like new or reissuance or anything, it is all supplies.

Participant

You have allowed banks to formulate the new policies for conversion of deposits. Does this means that they can now levy penalty when there is a conversion of deposit?

Dr. D. Subbarao

You want to explain that in little detail?

Shyamala Gopinath

Well, basically we have more or less the decision relating to premature closure of the bank deposits and what interest rates the banks will pay on such deposits will be banks and their customers. But

there was one message of regulation that will remain and that was this one. That was the situation where there is a deposit they transfer a certain period and it is before its maturity its closed and the deposit is renewed for a longer period than what the deposit had originally placed it. In such cases the bank would expect it to give the revised rate. Here we have set without any penalty so here we are saying and this was inhibiting in a sense the asset/liability management for the banking, as it could be a rash of such type of renewal, conversion at the time of interest rates going. So for this policy we feel we have left it to the bank which is now left to them to decide in what manner they want to do.

Alpana Killawala

Melissa, next to your questions.

Moderator

Sure. The next question is from the line of Vikas Singh from The Economic Times, Guwahati. Please go ahead

Vikas Singh

Yeah, sir, good afternoon. How does RBI plan to propel the credit flow of northeastern region? Would RBI like to offer bank special incentive for credit disbursement?

Dr. D. Subbarao

That is for Dr. Chakrabarty.

Dr. KC Chakrabarty

You see we are not asking, because we cannot ask the banks to give some incentive for the credit disbursement, credit has to be self stipulating in the nature, but what we are saying that it is the state government banks, they should work together to increase the flow of credit. So one, we have created the lead bank scheme, create the basic infrastructure and create a particular environment through which the demand for credit can be improved. So we can only play an intermediary role to bring the state government and together our lead bank scheme and thereby improve the flow of credit no other special incentive.

Vikas Singh

Thank you sir, thank you.

Moderator

Thank you. The next question is from the line of Sunny Verma from the Financial Express, Delhi. Please go ahead

Sunny Verma

Good evening sir. You little while ago you mentioned about the changing nature of trade balance between India and China. Exporters keep telling us that because of the currency issue in China renders them uncompetitive. Now that your voice is heard internationally, would it not be appropriate for RBI to take this issue up may be at a domestic forum or at an international forum?

Dr. D. Subbarao

Now, this is something that we discuss with the government and I am sure that government will hear you and that has indeed heard the exporters and there is a G20 meeting for Finance Ministers and Governors in Washington this weekend. So I am sure that this issue will come up. Thank you very much.

Sunny Verma

Okay, thanks sir.

Dr. D. Subbarao

I will now request Subir to sum up the discussion and give some lasting messages. Thank you.

Subir Gokarn

Well I have a lot of time to sum it up, but let me just try and highlight some key messages as far as the monetary policies in concern with the bank. One, as we have said clearly the balance of risk has shifted from growth, the growth slowdown to inflation and our response to that has been action on both rate and CRR. There have been questions asked about whether this action is too muted, too

mild to be effective. Our view on that is that while the headline inflation number is getting all the attention the underlying drivers of inflation are shifting from factors which are moderating and in fact we just got the CPI numbers for March, both agriculture labor and laborer and rural laborers, the number is almost a percentage point below the February number so that suggest that would hurt the indeed starting to moderate as expected from the estimates about the rabi crop. But non-food manufacturing which is really to us a reasonable measure of demand side pressure has accelerated not dramatically, but noticeably from a (-0.4) in November to 4.7% in March. And based on that trend we think that the actions we have taken are value appropriate. We do expect that these actions will help to reign in our expectations about runaway inflation, even as food prices are being driven by factors really outside our control, particularly, the monsoon over the next few months. An additional consideration which we have kept in mind is the need to manage liquidity and the economy non-disruptively government obviously is borrowing a lot of money this year despite the significant reduction in the deficit to GDP ratio, the absolute volume of borrowing is quite high, the private sector is expected to start showing growth in its demand for credit and together this will put a reasonable stress on the financial system, which needs liquidity to be managed carefully. So our attempt is to try and balance these objectives. We want to make sure the recovery sustains. We want to make sure that the underlying drivers of inflation are kept in check as the one that we can control and we want to make sure that the funding requirements of both the public and the private sector, government and the private sector do not cause undue disruption.

Dr. D. Subbarao

Thank you very much. You always challenge us with your questions thank you.

Alpana Killawala

Thank you sir. Just an announcement for the people who joined into the teleconferencing. We are aware that there are many questions and many questionnaires who wanted to ask questions, but we couldn't take them. Mostly, these were research and analysts. I want to tell them that please join us tomorrow between 2:00 and 3:00 because that con call is scheduled only for you, the researchers and analysts groups and you will get your chance to ask the questions. Thank you very much, thank you all.

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