“Reserve Bank of India Post Policy Conference Call with Researchers and Analysts”

October 26, 2011

Participants
Dr. D. Subbarao – Governor
Dr. Subir Gokarn – Deputy Governor
Shri Anand Sinha – Deputy Governor
Shri H.R. Khan- Deputy Governor
Shri Deepak Mohanty, Executive Director
Moderator: Alpana Killawala – Chief General Manager, Department of Communication

Moderator: Ladies and gentlemen, good day and welcome to the Reserve Bank of India Post Policy Conference Call. As a reminder, for the duration of this conference, all participants' lines will be in the listen-only mode, and there will be an opportunity for you to ask questions after the Governor's address. And during the conference call, participants connected to the audio conference bridge may press '*' followed by '1' to ask a question. Should you need assistance during this conference call please signal an operator by pressing '*' and then '0' on your touchtone telephone. Please note that this conference is being recorded.

At this time, I would now like to hand the conference over to Ms. Alpana Killawala from Reserve Bank of India. Thank you. And over to you, ma'am.

Alpana Killawala: Thank you very much, Lavina and welcome to this post policy teleconference once again. I wish on behalf of Reserve Bank of India all of you a happy Diwali and request the Governor to take over. Governor?

Dr. D. Subbarao: Thank you, Alpana. Again, welcome to this post-policy press conference from my own side. I would just want to give a brief face to this conference, just 2-3 minutes. First, as most of you know we raised the repo rate yesterday by 25 basis points taking it from 8.25% to 8.50%. This is the 13th time we have hiked the rates sometimes in baby steps and sometimes in adult steps.

We have also deregulated Savings bank deposit interest rate effective yesterday. Our policy was informed by two broad considerations. First, that inflation and inflation expectations remain high and we expect this level to persist for another two months. And there was a risk to inflation expectations becoming unhinged if we had changed the policy stance prematurely.

We have also noted that reassuringly the momentum indicators especially the deseasonalized quarter-on-quarter headline core inflation measures had shown a downward trend. And this is consistent with our projection that inflation will start declining beginning December 2011.

The second consideration that weighed with us was that the growth was clearly moderating on account of the cumulative impact of our policy actions over the last 20 months and also some other factors. However, as inflation begins to decline, they will be growing room for a policy stance, give some consideration for the growth risks within of course the overall objective of maintaining low and stable inflation environment.

Admittedly, the impact of past monetary policy actions is still unfolding. Even so based on our assessment of the current growth inflation dynamics we considered it necessary to persevere with our anti-inflationary stand.

As what has now become a standard practice by now we have also given some guidance for the period forward. We expect inflation to come down starting December 2011 and to a level of 7% by March 2012. Inflation is expected to moderate further thereafter in the first half of the next fiscal year on account of the combination of commodity price movements and the cumulative impact of our monetary tightening.

With this in mind we set notwithstanding the current rates of inflation persisting till November, a likelihood of a rate action in the mid-December mid-quarter review is relatively low. Also, for the period beyond that if the inflation trajectory conformed the projections we noted that further rate hikes may not be warranted.

We did this somewhat unambiguous forward guidance mainly to create some uncertainty to remove uncertainty for potential investors about the monetary policy stance. Of course, there have been uncertainty because of a number of factors but to the extent that the interest rate regime is a factor we wanted to create more certainty about that.

There is a risk that a lot of people will interpret this guidance as a commitment indeed in the media dissemination a lot of questions were about this. So once again I want to say that what we have given is guidance and it should be read and interpreted as guidance and subject to conditions we indicated there. Importantly, there are we must emphasize several factors that are necessary to be taken into account in order to get us to a low inflation environment which is to address structural imbalances in agriculture, remove infrastructure capacity bottlenecks, correct distorted administered prices and of course get on to a credible path of fiscal consolidation.

As regards growth in the May and July quarterly statements we projected a growth of 8% but in the mid-quarter review of September we noted that the risk to growth is on the downside. So based on our assessment of the current global and domestic situation we have revised the base line projection downwards to 7.6%.

Inflation of course continues to be a concern. What is of larger concern is the fact that even with the visible moderation in growth inflation has persisted. But as I said a short while ago there is some reassurance coming from the fact that the momentum indicators from deseasonalized quarter-on-quarter numbers both for headline and WPI and for core inflation are showing some moderation. So based on this we have kept our inflation projection for March 2012 unchanged at 7%.

Finally, about the savings bank deregulation, that has been divided into two brackets; first bracket is the lower bracket where each bank will have to offer a uniform interest rate on Savings bank deposits up to Rs. 1 lakh irrespective of the amount within that limit, and second is for deposit accounts over Rs. 1 lakh where bank will provide differential rates of interest if it so chooses. However, we said that there should be no discrimination across customers on interest rates for similar amounts of deposit. There were some questions about the timing of the Savings bank deregulation, why we have to do it now. There were also some questions about whether we could allot some time for adjustment. We have given answers to those questions in the press conference yesterday and we will be happy to answer if there are related questions.

Finally, people have asked us if we are going to standardize the norms further with regard to Savings bank deregulation and the answer we gave yesterday which is I want to reiterate now is that we left discretion to banks deliberately, we would expect that they would take advantage of the flexibility that we have given them to be innovative and to act in the best interests of the customers. Thank you very much.

Moderator: We will now begin the question and answer session. Anyone who wishes to ask a question may press '*' and '1' on your 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. Our first question is from the line of Amit Premchandani from UTI Mutual Funds. Please go ahead sir.

Amit Premchandani: Just a question on the savings bank deregulation, are we to assume that there will be detailed guidelines on the fees which can be charged by banks on various savings linked products and whether they will be deregulated completely, what is the definition of Rs. 1 lakh, whether it is average balance or a one-time balance? This is my first question. I have another question I will take it up later.

Dr. D. Subbarao: I will answer this question, maybe then I will pass on to Deputy Governor Anand Sinha. As I just mentioned in my opening remarks there is not intention on the part of the Reserve Bank to issue any detailed guidelines. We have left many of the details open deliberately in order to encourage banks to be innovative and we expect that the competition that will emerge as a consequence will be in the best interests of the savings bank deposit holders. Also, on the definition of what should be Rs. 1 lakh account that also I believe is open to the banks but I will defer to Anand to clarify.

Anand Sinha: We have just laid down two conditions as Governor mentioned that up to Rs. 1 lakh interest has got to be uniform and above Rs. 1 lakh there can be slabs but within those slabs the interest rate has again to be uniform across all the offices. Now, your question as to how do we determine Rs. 1 lakh or any other slab. This is completely left to the bank. To be concrete, Rs. 1 lakh could mean daily balance, Rs. 1 lakh and above could mean weekly average, it could mean any average that is completely left to the banks. As far as service charges are concerned we have not stipulated anything. There is a long standing instruction from our side that service charges should be reasonable. Now, as we go along and if some angularities are, if customer complaints increase then we will have to look, but as of now apart from these two things, banks are completely free to devise their schemes.

Amit Premchandani: Another question on the inflation, yesterday you revised repo rate at the same time government increased MSP price, so again it will have inflationary impact. So just to take your view the 7% target, there maybe deceleration in the non-food manufacturing inflation while the headline number may not go down. So what will be target say from March policy, whether you are looking at non-food manufacturing or just headline numbers?

Subir Gokarn: Interestingly, when you look at the break-up, the composition of food inflation over the last several months, cereals have not contributed significantly. Cereal prices have been rising but relatively slowly compared to many other items and that has been the focus of our articulation of concern on food inflation, the structural imbalances that we have talked about with respect to protein items with respect to food and vegetables. So, the MSP increase in wheat prices I believe are Rs. 1.25/kilo or so. May have a little bit of an impact on wheat prices but unlikely to be very significant. Of course, other factors, other risks are always there and we keep watching out for them and overall clearly food inflation whether it is coming from more of proteins or other sources but I think you have to look at this in the context of what has been the dynamic of rice and wheat prices over the last several months at a time when other food items have been really driving the food inflation process.

Amit Premchandani: And sir in terms of focus whether it will be on non-food manufacturing or will it be on headline number, just wanted to have clarity on that?

Subir Gokarn: It is both. We have been articulating our inflation projections, we do not give our projections for non-food but clearly in our headline number there is an implicit non-food manufacturing number as well. In our long-term, I would not call it a guidance but benchmark or yardstick we have been talking about 4 to 4.5% as the long-term average year of inflation non-food manufacturing. So that number clearly gives us some sense of the impact of policy on growth and pricing power and inflation. If that is moving in a particular direction and headline has then being driven somewhat differently by supply side forces, obviously, that is a scenario which we will have to apply some finer adjustment on.

Amit Premchandani: The final question, on the setting up of committee for defining the restructuring and if you look at the banking practices in the current environment will you give bank enough time to move into that kind of a scenario or I know this report is not yet out but in the current environment where banks are reporting huge NPLs increase and there is a lot of proposal on restructuring and some of the large banks who are capital-deficient, are you not concerned that suddenly if some norms are changed on restructuring a lot of banks will be capital deficient to handle ?

Dr. D. Subbarao: We have to constitute the working group. So it is perhaps premature to talk about whether we could give time for banks, it depends on what the recommendations of the working group are and whether they require time for adjustment. Should it be our judgment or they require time we will certainly give it, but I think it is bit premature to discuss that.

Moderator: Thank you. Our next question is from the line of Prakash Toshniwal from India First Life Insurance. Please go ahead sir.

Prakash Toshniwal: Just on the saving and deregulation and government has also increased the 53,000 crores bowering budget. Could you just comment on the liquidity conditions, will it be remain under plus/minus 1% NDTL or will there be any change?

Dr. D. Subbarao: This plus/minus 1% of NDTL is the range that we have assessed for systematic liquidity. In other words, what we have said is that if it the systemic liquidity is within plus/minus 1% of NDTL we would think that it is within our assessed limits. So, if it goes beyond that and if it is our judgment that liquidity deficit or surplus is of systematic nature, then we will have to take some measures to offset that. So in the context of the increased government borrowing, the same formula applies. It is not automatic or inevitable that the systematic liquidity will go beyond this just because borrowing has gone up. But should we make a judgment that it is of an enduring nature then we will have to take some liquidity measures. But I also want to give a caution here, give some alert here which is that we are not going to change our stance on liquidity just because borrowing has gone up in numerical terms or yields have gone up. Our judgment is going to be based entirely on the systematic liquidity conditions.

Prakash Toshniwal: In the recent results of some of the banks, some of the banks have passed their advances book in the investment by investing CPs and bonds of companies instead giving loan to them. So what is the regulatory environment here because these bonds and CPs don’t require PSL requirement as well as standard provisioning, so what will be the regulatory stand on this.

Anand Sinha: Regulatory stance as of now you stated yourself is leading to circumventing of the loan route then we will have to take a look. As of now you have stated the regulatory stance itself.

Moderator: Our next question is from the line of Shishir Shindekar, a research student. Please go ahead.

Shishir Shindekar: Thanks and congratulations for deregulating interest rate on saving accounts. After consecutive 13th hike rate if the inflation cannot be controlled which indicates that it is beyond a scope of RBI or it is not a monetary phenomena. Rising food prices, rising government expenditure, subsidies, oil prices are the basic causes. With this backdrop as an advisor to the government why you are not strongly advocating for the reduction in the fiscal deficit or to accelerate the economic reforms in agriculture, land and energy sectors?

Dr. D. Subbarao: Very good, thank you for coming online. First of all I want to say that on the effectiveness of a monetary policy on 13 rate hikes. Your presumption that it has not had any impact is probably incorrect because you do not have the counter facts here. What would have been the inflation had we not acted? Perhaps it will be reasonable to assume that that would have been much higher. Second, you must also note that headline WPI inflation has actually come down. It was 11.4% sometime in April 2010. It has come down from the peak level. So inflation has come down in response to the monetary policy tightening. Of course, to bring inflation down on a sustainable level we need to act on the supply side and we have spoken to government in this way and constant dialogue with the government we have noted this in our policy documents including the document yesterday we noted all the things that the government needs to do to generate a supply response to bring inflation down on a sustainable level including the need to make credible and sustainable fiscal adjustment.

Moderator: Thank you. Our next question is from the line of Arjun Shetty from Deutsche Bank. Please go ahead.

Arjun Shetty: I have two questions; first, as you have pointed out in the monetary policy review, credit growth to industry in general and infrastructure in particular is decelerating sharply. You have mentioned before about the need for a stronger supply side response to accommodate demand side pressure, now given that real rates have been so low in the past few years, do you think that the government policy and regulations play a much more dominant role in driving investment growth and capacity addition? And if not, then what would be like the comfortable range for real rates that RBI would be targeting if inflation does pan out the way that you anticipate? I will ask my second question afterwards.

Dr. D. Subbarao: About the factors that influence investment you are quite right, that the interest rate is only one of the many factors. We have noted also probably not in a document but certainly in some of our other dissemination material, real interest rates today are lower than they were in 2007 or 2008. So there are obviously other factors inhibiting the investment. As far as what should be the appropriate real rates it is difficult to say but certainly they have to be positive in real terms. At the moment real policy rate is still negative but real lending rates are positive and they have been going up obviously because of our tightening and because inflation also will come down in the course of the next few months. But probably we cannot say what will be an appropriate real interest rate.

Deepak Mohanty: No, because technically, if you see that what should be a sustainable kind of a real interest rate in the economy as a whole, I am not saying that for industry or investment, it should be a fully real growth rate, so that is what is sustainable. But we do not have particular view that at what level that it should be, it depends on what stage business cycle one see and so that again and plus the inflation determine what the real rates are.

Arjun Shetty: My second question is we have had comments from multiple MoF officials on plans to raise the quota of FIIs in government debt. What are RBI's thoughts in this especially given your assessment on the risk posed by widening current account deficit in an environment where capital flows can dry up quickly and worsen fiscal situation?

Dr. D. Subbarao: This is an issue on which we are in dialogue with the government. You are right that the government has spoken about this. They have also spoken to us about this. In taking a decision on this we will take into account not just the government's borrowing program, a borrowing needs but also the external sector viability issues that we just mentioned. We certainly need capital flows to finance our current account deficit but we also need to pay attention to what sort of flows are coming in to finance that deficit.

Moderator: Thank you. The next question is from the line of Dr. Manvendra Singh from Devi Ahilya University. Please go ahead.

Dr. Manvendra Singh: I had a question that there had been 13 hikes in the repo and reverse repo rate from RBI side to control inflation. This had led down to fall in CapEx as you had mentioned day before yesterday in your assessment of the economy. Sir, what I want to ask is that instead of continuously concentrating on the interest rate phenomena why not RBI is using exchange rate as it to control inflation? Because Rupee from the last review that you had done had come down from 45 to 51 and at the ground level what I had surveyed is that people had raised prices of every commodity even consumer durables by 25%. And since you had posted a risk for your December interest rate scenario that low probability of rising interest rate will only depend on the exchange rate as well as global environment, so for the time being why not instead of concentrating on raising interest rate, RBI through appreciation of Rupee try to control inflation and give confidence to the industry that we had capped the borrowing cost instead we are controlling inflation that way, that way it will promote investment as well as cheap import and will lead down to fall in inflation and growth in the economy?

Dr. D. Subbarao: I answered this question yesterday which is that we do not use exchange rate as an anti-inflation instrument. We do not use it when exchange rate whichever way it moves that we need to control inflation through the standard monetary policy tools and exchange rate should be used for external sector management. Regardless of what instrument we use for inflation management somebody has to pay the cost. So, if we use exchange rate intervention certain economic agents are going to pay the costs for that. So the question is, apart from its effectiveness the question is, is it appropriate to pass the cost on to a few people who operate in the external sector? The other thing I want to say is that the pass-through from exchange rate to the domestic prices that is relatively low in our system. So exchange rate may not be terribly effective instrument for combating inflation. But I will turn to Subir if he has got any thing to add?

Subir Gokarn: I think it is important to also recognize that the exchange rate is not an entirely controllable indicator instrument. It is very easy to resist depreciation if foreign exchange is flowing into the country you just keep buying up the foreign exchange and creating reserves which prevents the domestic currency from appreciating, but when the currency is depreciating, the capacity of the system has to prevent depreciation if the volume of reserves that the central bank is holding. Now, you can of course very easily use up all your reserves and trying to protect a particular rate but if you do not succeed then the sky is the limit. There is no ability to control the currency and people realize that you do not have enough reserves they can continuously hammer away your exchange rate which means it will depreciate much more than it would have otherwise. Now, this is not of hypothetical scenario, this is a scenario that many countries have faced. In the 90s we had this happening to the UK, we had it happen to Mexico and it is very, very significant threat in a situation where money is flowing out very rapidly in an attempt to defend the currency usually ends up in failure. So an instrument of something you must have control over. If you do not have control over it then it is not a very effective instrument and that is why and we will letting the exchange rate move in response to market forces, while also preserving the credibility of our reserves, in a sense that we use them to minimize volatility in the market to give some confidence that liquidity in foreign exchange will not drive completely. That is the balance that we are trying to achieve and that is the way we will be approaching our exchange rate situation. Let us also keep in mind that for the moment what has happened to rupee in the last few weeks is the result of global factors, not the result of anything happening domestically virtually every emerging market currency has been subject to the same pressures and there is a general expectation which we will have to test as we go along that when the global financial system stabilizes after some reassuring outcome so we are waiting for that, today, in fact, on the European front that there will be some correction in currencies because money will flow back into emerging economies. So it is a temporary phenomenon then we should not be exhausting resources, try to fight it, but I think this is our judgment we will have to make as we go along and see how things are working.

Dr. Manvendra Singh: Sir, in this light I just wanted to ask that cannot RBI give us signal to the market by pumping in a few dollars for few moment? Because what I have been observing is that the dollar had been depreciating against major currency in recent one month; dollar had depreciated against Yen, Euro, Australian Dollar as well as British Pound, but against Indian currency it had appreciated quite a bit. So, with your intervention, cannot RBI signal market so that Rupee tries to move on a higher side and that way we can slightly help out on the front of inflation?

Dr. D. Subbarao: No, Prof. the answer remains the same which is that exchange rate is a different type of variable, it is not very effective for the purpose of inflation management, and it is not very effective in our system because of the limited pass-through. Also in the current situation you yourself are studying this very diligently I noticed. The movement of the Rupee has been, for reasons to do with the external sector development, nothing to do with our domestic situation, so it will be inappropriate to use exchange rate for the purpose of inflation management.

Moderator: Thank you. Our next question is from the line of Himanshu Sethia from ING Mutual Fund. Please go ahead sir.

Himanshu Sethia: Just wanted to know you said that the momentum indicators for inflation have come down and that has provided some relief to RBI. Wanted to know could you share by how much would the momentum indicators could have come down sir?

Subir Gokarn: If we take the season adjusted annualized rate quarter-on-quarter of the WPI headline and non-food manufacturing it came down in the second quarter which is the July-September quarter, the numbers are about a percentage and a half below that of the first quarter. Inflation is still positive but the rate of inflation has gone down. So for headline roughly has come down for about 7.5-8 to about 6-6.5. There are of course different methods of deseasonalizing and that always create some range but what is important if the non-food manufacturing has come down from about the 6-6.5% range to about 4.5-5% range. So both of these suggests that core inflation momentum is starting to moderate. There is of course a lot of volatility in these numbers if we go month-by-month, so we have been trying to focus on the quarter-on-quarter.

But what also striking is that the food inflation momentum. If we take the Q2 our inflation rate Vs Q1 inflation rate has actually gone up. Despite the good monsoon we still have acceleration in food inflation because of the kind of structural factors that we have been talking about. There, the number is gone up from about 7.5-8 in the first quarter to about 8-8.5 in the second quarter.

Himanshu Sethia:: As far as the increase in MSP yesterday would you be worried about anything different change in inflation ?

Subir Gokarn: I think we have already answered that question, you presumably heard our response that the main drivers of food inflation are not cereals and the MSP largely affects cereal. So, yes, it may make a contribution but when you look at the composition of food inflation there are other factors which are backlog basically resource structural supply/demand imbalance which seem to be contributing much more. So it is not to say that MSP will not contribute. Investors in the larger scheme of things contribution may not be very significant.

Moderator: Our next question is from the line of Devendra Nevgi from Delta Global Partners India. Please go ahead.

Devendra Nevgi: I have two quick questions; the first was that with RBI not intervening in the fixed market since the last November-October, the last released data, it will be right for the market participants to take that as Rupee had become a free float that is one. Secondly, on the fiscal side that large inelastic kind of expanded feature and fear of fiscal deficit being overshooted now, is the RBI worried about the impact of the same on the rates?

Dr. D. Subbarao: Answer to your first question we really cannot comment on whether we have intervened or not and therefore we cannot really comment on your presumption about free float. But I just want to reiterate our policy which is that we would of course intervene if the exchange rate movement is volatile or if the exchange rate movement is disrupting macroeconomic stability, that has always been the RBI policy, that continues to be RBI policy. Based on that you can make your own judgment that Rupee is a free float of course I would say that we have not free float yet but we should get there sometime, I do not know when. On the fiscal deficit, yes, we have noted consistently in all our quarterly policy document including the one yesterday that fiscal deficit is adding to inflationary pressures and that fiscal expansion at a time when monetary stance is tightening is clearly a suboptimal. So it is something that we need to take into account, it is something that we should be concerned about, but I also want to say that the government are sensitive to the need to make quick and credible fiscal adjustment and hopefully we will see some statement from the government in the winter session of the Parliament.

Devendra Nevgi And one last question, on the OMO RBI always taken a stance and purchase OMO would take place only when the liquidity deficit is of a durable in nature. So is it possible to give a kind of a definition to the durability of the liquidity banking decision?

Dr. D. Subbarao: I wish I could but I believe we cannot make an objective definition of what is systemic liquidity deficit of a durable nature. It depends on what is causing the deficit and how long it might persist and I would suppose that the judgment is contextual and cannot be captured in any set criteria.

Moderator: Our next question is from the line of Anindya Das Gupta from Barclays Bank. Please go ahead.

Anindya Das Gupta: I have actually a couple or maybe three questions; I just go through them one by one. The first question is what will be the instruments in order of preference to neutralize permanent or semi-permanent liquidity deficit if the RBI sees such a deficit emerging?

Dr. D. Subbarao: A menu options is available, you know them one is the OMO, the second is CRR, the third is to further liberalize the capital account, I am just reading them out as menu options not necessarily in any order of preference. So, what we will do and when we will do it, how much we will do it depends on the situation.

Anindya Das Gupta: Related but not possibly directly connected to the policy. The RBI in the recent past, post the huge increase in borrowing in the second half, has devolved bonds on the primary dealers a couple of times and two, possibly not explicit, should the market look at that as yield signals or a case of yield moving too fast too soon or being away from the secondary market levels, would you choose to comment on that?

H. R. Khan: We have clearly articulated and clarified that devolvement on primary dealer should not be read as any yield signal. If primarily dealers underwrite and we pay underwriting commission to them and if bidding is way away from the market yield, then there is a case for devolvement. That is purely if it is not in line with secondary market yield and way away from that we devolve. So in no way should be interpreted as a yield signal.

Anindya Das Gupta: On foreign currency liquidity in the Indian money markets, the RBI has been tracking and have got the last mechanism to adjust any surplus or deficit liquidity in the INR money markets, but not so often we see cases in the foreign currency money market liquidity debts to be pretty unhedged. Is that something the central bank is looking at pretty seriously in terms of tracking the cash norm premia and things like that and if that has treated or policy for that?

H. R. Khan: In case of extreme situation, we look at both ForEx liquidity and Rupee liquidity. Post Lehman also we had looked at ForEx liquidity issue also. But we do not think that the situation has come in respect of ForEx liquidity to that extent that we will be taking action in the post the Lehman period. But we are monitoring and getting some feedback with regard to availability of funds to Indian banks for meeting export credit as well as for trade credit. We are looking at that and if necessary we will take some action. As of now, we are closely monitoring and getting some feedback.

Moderator: Our next question is from the line of Piyush Chadda from Edelweiss. Please go ahead.

Piyush Chadda: I have two questions; the first one is that we have a target of round about 7% as the headline inflation from March. Is that a level at which the RBI would consider reducing interest rates or would the interest rate policy still be on a pause mode were to hit those kind of levels? Second question which is related is it there is a divergence between food inflation and non-food core inflation. Would we prefer to look at headline numbers or just the core inflation numbers to guide action?

Dr. D. Subbarao: On the first question, the answer is no. 7% is above the comfort zone of RBI and I believe about the comfort zone of the vast majority of people in India if not the entire population of India. So, inflation has to come down below 7% before we contemplate reversing our policy stance. I also say that if and when we decide to reverse our policy stance will depend not just on the level of inflation but also on growth and not just the headline numbers of growth and inflation but on the disaggregated numbers and what might be driving them. We have done some studies on the threshold inflation, those studies are in the public domain. Threshold inflation is currently indicated to be in the range of 4-6%. So that is the range we need to come down to before we can contemplate any reversal of the policy stance on interest rate. Your second question about when core and food inflation diverse, whether we will look at which one we look at and which one will we be guided by. We look at all of them. So, what will inform us is not just the numbers, but the trend in those numbers, and the drivers in those numbers and as we have said several times we look at not just CPIs, also the momentum indicators but host of numbers beyond the inflation too.

Moderator: Our next question is from the line of Upasna Bharadwaj from ING Vysya Bank. Please go ahead.

Upasna Bharadwaj: Just a question with respect of the deregulation of saving rates. My question is how do we ensure the symmetric impact of such a move given that only upside rates would have listed by the banks, the decline in rates could be easy passed on, so that was asymmetric to move, so how do we ensure that this is symmetric in nature?

Anand Sinha: The basic intention is that it has got to be market related. We have not taken the responsibility of making it symmetric, it is for the market forces to decide which way it will go.

Moderator: The next question is from the line of Neha Kothari from Shubhkam Capital. Please go ahead.

Neha Kothari: Sir, you have made a downward revision in the GDP growth but however, your credit growth expectations remain the same, considering the second half, are we confident of achieving 18% target? I just want to understand your outlook on the same.

Dr. D. Subbarao: The non-food credit growth is currently running at 19.3% or something like that in the third week of October as against our projection of 18%. The question is whether we are comfortable with that number. You must recognize that even as investment has moderated there are still a large number of projects under implementation and disbursements for those projects will have to continue to take place. Also, there will be credit demand from running units for their working capital and working capital requirements will be higher because of the higher prices of inputs. So taking all these factors into account we decided to stay with the projection of 18%.

Moderator: The next question is from the line of Ragvendra MJ from SBI Life Insurance. Please go ahead.

Ragvendra MJ: I have two part questions; my first question is with respect to the RBI tracking the activity of our industry, you have already mentioned your suspicion regarding the veracity of the IIP numbers going to the volatility. So does the RBI actually look at the PMI numbers that are being released globally and for India? Because once when I had spoken to Dr. Pronab Sen he says that if you are a patriot you have to look at the IIP number but then if you want to genuinely track growth in the industry you can look at PMI. So does RBI look at PMI and then the fall in PMI numbers does that pose a threat to our growth? And the second question is we do realize that the RBI's release said that global factors do tend to play a role in our own monetary policy stance. So with that in mind what are the biggest indicators that the RBI looks at globally to judge the pace of growth and fall in economic activity?

Subir Gokarn: In trying to get a sense of what is happening in the real economy we have all range of indicators; some of which are data-driven or the system data-driven is in the case of IIP. The PMI is a survey of set of companies, so in that sense it does reflect a segment of the real sector, would you have manufacturing services, that is clearly an indication that a lot of input, a lot of weight on and it impacts on decisions also. But in addition to this, we track corporate numbers very closely, looking at quarterly sales and profitability numbers to get a sense of whether the aggregate numbers are being validated by company level numbers and we have a sample of about 2500 companies which gives us a pretty long and balanced kind of panel to track corporate performance. We have our own surveys; we have actually an industrial outlook survey and we have an order book, inventory and capacity utilization survey, these typically are quarterly surveys of about 1500-2000 companies which ask questions relating to current levels of performance and financial environment and also expected levels of performance and then financial factors. So there are some very elaborate dashboard that we have when we go into our monetary policy decision-making. So we are not really dependent on any one indicator at all and I think the larger context in which the statement about IIP was made is that even though that is proving to sort of giving us a sense particularly in the second half of '10-11, it was giving us a sense of things slowing down. Other indicators are actually pointing out is the direction. As it turned out when the IIP series are revised the second half of '10-11 proved to be a very, very robust growth period. So, that is where we see that if we rely on any one indicator it is always going to give us where pose some risk in terms of reaching the right conclusion, but when we have this pretty elaborate dashboard I think minimizing the risk of making the wrong judgment.

Ragvendra MJ: There was another question I had asked about, what global particular indicators that you look at to judge the slowdown or strengthen global economy before we decide on our own monetary stance?

Subir Gokarn: We have the regular forecast update from the IMF, which an important source. But every central bank puts out an assessment of its own region and global factors so that is being aggregated and we have sort of dashboard of central bank assessments and actions that we use to supplement our information. And of course, there is a whole archive of views on the global economy, partly commercial, partly public domain which all of its feeds into our overall assessment.

Moderator: Our next question is from the line of Jyoti Kumar from Spark Capital. Please go ahead.

Jyoti Kumar: My question is on the potential guidelines towards movement to Basel-II IRB related migration. Given the context where most of the banks were even grappling with identification of MPS in the right sense. Do you not think it is premature to move into IRB migration? Secondly, in our developing environment, let us say we see the reports that power sector which is a case in example being power sector which was probably considered 'AAA' or a 'AA' kind of a loan way back in 2007 or 2008 now getting almost into a default mode. Do you think the banks would be in a position to make a judgment with respect to the rating? Any comments on that ?

Anand Sinha: As far as IRB is concerned basically the issue which we are using is whether the Indian banking systems is ready for that. You cannot go waiting for eternity. Because ultimately what has IRB achieved, it raises the risk management systems. Prior to the present crisis, there was another attraction that it will reduce the capital requirements but now the view on capital has changed completely. Now, reducing capital is no longer a virtue. So, while that angle is no longer there, but the fact that it will raise the standards of risk management and that will precisely the same issue which you are mentioning, that is a better recognition of NPAs and better methods to tackle it, so that is the motivation. And as far as we are concerned we have given a timeline but it is not mandatory for banks to move on to this. So, it is for the banks to decide, but at the same time, we feel that the larger banks, the internationally active banks should move to this because first of all as I said upgrading risk management is a huge motivation and the second thing is you cannot go out into the world and say that "You are working on a very elementary level if you are international bank or if you profess to be an international bank." So, these are the two things keeping that in mind we do observe the banks, the larger banks to try and move to IRB but we have not put any compulsion on that. And the other thing which you must remember is that IRB application does not mean that we are going to approve it, there are a whole set of conditions which the bank must fulfill before the IRB approval can be given. So, I do not see it happening in the immediate future but certainly it is desirable.

Jyoti Kumar And some of the data which probably require about five years of data, will there be an extension with respect to that because considering that we are still a developing economy and there are a lot of structural issues other than cyclical issues?

Anand Sinha: No, on data requirement you are absolutely, right. In fact, if you are looking at the PD and LGD data, now they need a necessary window of 5 years and 7 years. So that data is an absolute must before anybody can move on to IRB. But at the same time what you are saying is correct in a sense that supposing we are looking at LGD data, now prior to Sarfaesi which was implemented in early 2000, our LGD data would be on a very high side. So obviously, that data cannot be used for the current situation if we are going to move on to advanced approaches, but now after Sarfaesi the data has better quality, it reflected a reasonable position. Similarly, as far as probability of default is concerned we are looking into the late 90s when interest rates were very high, when economy was not doing very well at that point of time if you are going to rely exclusively on that PD and that again will not be correct. So that is why the best thing is to take data pertaining to a complete cycle. From that perspective, PD data we have enough time series data now, even though I am also sure that banks have not had the system to capture the earlier data, but at least last 5, 7 years data they would have captured. And as I said post Sarfaesi LGD data would be reliable and in my view we can go ahead with that.

Moderator: Our next question is from the line of Siddhartha Sanyal from Barclays Bank. Please go ahead.

Siddhartha Sanyal: If I understand correctly an answer to a previous question in that till the time inflation comes to sizably below 7% kind of markets very difficult for the RBI to change its interest rate stance. Now, in the context of liquidity management do you think in that kind of a situation RBI will have headroom to address the liquidity issues through the CRR route or that option is also quite ruled out in that kind of a situation? And in that case, are we left with only choice of OMO or anything else in that case if we need adversely liquidity situation in the meantime?

Dr. D. Subbarao: I do not want to make a judgment now on what instrument we might use, indeed when I answered the earlier question I said that I am reading out the items in the menu not necessarily indicating our preference or our choice about which instrument we might use. About whether we will use CRR or not, I cannot really tell you now. But certainly, if inflation continues to be high, they will be that much of an additional constraint in using CRR for liquidity management purposes. Beyond this I am afraid I cannot enlighten you any further.

Moderator: Our next question is from the line of Jyoti Khatri from Systematic Shares. Please go ahead.

Jyoti Khatri: I just want to understand what is the call on the commodity prices? Considering the global economy now flowing down till the commodity prices have hold on and your yesterday policy document highlighted the fact that one of the triggers of the inflation to come down in the future is softening of commodity prices. Just wanted to understand what will be the drivers that will bring down the commodity prices going ahead?

Subir Gokarn: I think base line scenario for commodity prices is that they will remain roughly at the levels they are. Some of them are of course coming down but the most important for us is oil and our projections are not based on any optimistic assumptions about actual decline in oil prices. But given the fact that in October-November of last year oil prices went up by 30% or so, 30, 34, 35% that kind of kick is not expected. So the contribution to inflation after December is going to be significant. So essentially what we are saying is that there is a very powerful base effect coming in to play in December of the year-on-year. But that is being supported by the momentum that we are seeing as a result of the growth moderation. So even though we may not see commodity prices fall dramatically since the contribution inflation is not expected to persist beyond December that is a favorable outcome. Now, of course, the situation may evolve in way which pushes them up further but that is something we will have to wait and respond to as it happens.

Jyoti Khatri: My second question is not directly related to policy, but related to bank. Entire power sector is facing problems right now. So RBI will consider in future the restructuring of power loans, any such idea is there?

Anand Sinha: RBI comes into restructuring from a very limited perspective. It is a myth that RBI allows or does not allow. The bank is fully entitled to restructure whenever they want. It is basically for them. Where RBI comes into picture is that we give asset classification benefits under certain situations, so that is the issue. Now, we have very well laid down guidelines and any restructuring from the perspective of asset classification benefit will have to comply with those, so that is the position.

Moderator: The last question is from the line of Arvind Chari from Quantum Asset Management. Please go ahead.

Arvind Chari: I am sorry to say again my question is on the exchange rate management. Of course, you answered very clearly about your policy. But do you still believe that hiking rates on the domestic side and leaving the exchange rate open in terms of policy option, is it running counterproductive to overall objective of getting inflation to a reasonable extent?

Dr. D. Subbarao: You are right, in a sense that the depreciation that is taking place in the last couple of months has actually amounted to monetary easing. But given that we will live in the real world that we do, it is difficult to control for everything. So, we just do not want to deviate from our announced exchange rate policy because of inflation concerns. I believe we have enough instruments that come on to manage inflation and external sectors to be managed through the exchange rate instrument.

Subir Gokarn: If I can just supplement, two factors that we need to take into account; one is that interest rate increase through whatever interest rate arbitrage of this exist and actually also help to appreciate the exchange rate so there is one linkage there from the financial channel. Two, that as we said in response to earlier questions at this point of its not very clear that this is the structural change in exchange rate. But some global instability which may correct and we may see a reversal if you go back to the exchange rate dynamics of second half of 2008-09, there is a very, very sharp depreciation and this was followed by a very sharp of appreciation. Overall period of correction was very short and even not the kind of horizon where you saw a structural change in policy it was warranted. So I think we are in a similar situation now. Of course, things may turn out to be different at which point we will have to obviously review the whole framework. But for the moment these are the two factors I think we have to keep in mind while resisting the sort of the temptation to start doing something which may end up costing us in the long-term.

Well, we come to end of this teleconference. I just on behalf of my colleagues like to express our thanks to you because this is a holiday and I think you are joining into the conference, I do not know but many of you are doing it from home perhaps but it is still a commitment of time and it just shows your enthusiasm and your seriousness which you take our policy statements. We are very grateful for your participation and of course on behalf of all my colleagues I like to wish all of you a very Happy Diwali and the New Year that follows. Thank you very much.

Moderator: Thank you ladies and gentlemen. With that we conclude this conference. Thank you for joining us. You may disconnect your lines.