Interview with Bloomberg on July 22, 2019 – Shri Shaktikanta Das, Governor, Reserve Bank of India

Reserve Bank of India Governor Shaktikanta Das gave his first interview with media since taking office in December. Here's an edited transcript of the topics he covered in the more than 50 minute interview.

On the economic slowdown and the RBI's response:

"The accommodative stance will depend on incoming data. How inflation numbers look how the growth numbers look. Primarily how inflation looks. With regard to the slowdown, I would not give a particular timeline and it's not possible. But overall if you see the trend, I think the fourth quarter of last year was partly a base effect and partly due to investment slowdown and demand contraction, which I had articulated in the monetary policy committee minutes. For that, so far as monetary authority is concerned, the law gives us a certain role and mandate and we have tried our best to play that role. We have reduced the policy rates by 75 basis points and we have shifted to accommodative. And shifting of the stance to accommodative itself means a rate cut of 25 basis points at least. So therefore effectively, the rate cuts has been 100 basis points if you take into account the change in stance."

On providing liquidity:

"Parallel to that we have also ensured surplus liquidity in the system. Liquidity was in deficit but at the moment for the past 1 1/2 months, the system is in liquidity surplus by more than 1 trillion rupees.

"We will ensure the banks are provided adequate funds. While the system is in surplus mode, it is possible that one or two banks may have liquidity issues. Given the role the RBI is assigned, inflation is primary target, and given due weightage to the fact that growth momentum has slowed down. For the revival, various stakeholders have to play the role."

On investment slowdown:

"There have been sectoral problems, like in the auto sector. Our survey shows that additional insurance requirements has had an impact. So every sector has had its problem. But when the world is changing you also have to change. Then there was the credit squeeze; now availability is there. The banks were unable to lend significantly, burdened with NPAs and the focus of the banks was on recovery and consolidation and not on credit. The banks are now in a better position to lend. While banks were not lending, NBFC entered their space. But for a year or so, credit flow has been affected. Another thing I would like to address the crowding out effect. It's a good thing that the fiscal deficit has been brought down and recapitalization has been announced. Every stakeholder, the government, the private sector and the RBI are playing their role and I think things are moving in the right direction. And things should improve now."

On liquidity and NBFC problems:

"We have to constantly monitor and remain alert as the regulator and as a monetary authority. We have to analyse and review the situation. Here at the RBI, we have broad medium and long-term goals. If some issue becomes critical, not a day passes without some internal high-level review. On NBFC, not a day passed in the last several months where we don't have a discussion or a review internally. Either on the sector or individual NBFCs. And we are monitoring the top 50 NBFCs which we have identified in terms of balance sheet size, volume of operation and in terms of governance practices and credit behavior. Our supervision teams are closely monitoring them. We are in constant interaction with the banks and it's our endeavor to ensure a collapse of another NBFC, especially a large one, doesn't happen. Having said that, if NBFCs have undertaken certain governance practice and certain ways of function and they have to a price for it, they will have to pay a price for it."

On banks being proactive:

"We are in constant engagement with banks. After the June 7 circular, the banks are more enabled to resolve the crisis and stress in the individual NBFCs. Now inter-credit agreement is mandatory. Earlier it wasn't. We have also given 30 days for review and another six months for restructuring and we are having constant engagement with the banks. So the banks, under the June 7 circular, have to play a proactive role. We are constantly in touch with large lenders to such NBFCs, including some housing finance, where we see some signs of fragility."

Consolidation in NBFCs:

"If somebody has diverted or there has been sort of ever-greening, there has been gold plating, if there has not been so diligent lending, so obviously they have to pay the price. Our effort is to segregate the way there have been lapses. Our focus is the overall system maintains stability. When I say system, it obviously includes all the major players. Therefore, our effort is to see that there is no repeat instances of systemically important large NBFC collapsing. And in the process some promoters have to make certain sacrifices, promoters have to accept haircut, the banks will have to deal with it appropriately within the parameters. One or two cases, the banks have signed inter-creditor agreements and they are resolving this crisis. The way I look at it, the responsibility is on the NBFCs themselves, to find market instruments to resolve their problems. Market instruments and the promoter has to bring in additional capital, he has to do a stake sale, he has to securitize his assets and mobilize liquidity, he has to meet debt obligations. And then the role of the lenders. We are in discussion with the lenders who have to protect their money also. They also have a parallel role to try and resolve this issue. That will also mean sacrifice on the part of the promoter also. The RBI will ensure adequate liquidity to banks."

On refinancing:

“This Refinance window or a liquidity window is a misnomer. We cannot lend money directly to one NBFC. Under the law, RBI is the lender of last resort, but we haven’t reached that situation where we invoke that particular legal provision. So RBI in today’s time cannot and would not be lending directly to NBFCs. We cannot give them clean money. It is up to the bank and depending on the collateral. We are backing up the banks. There is nothing called a liquidity window. Money is fungible, and when money is fungible having these windows, I think, is not relevant.”

When will the crisis be over?

“Difficult to say when it finishes. It’s our effort to ensure there is no contagion. It is our endeavor to ensure there is no collapse of another systematically important NBFC.”

On cases of adventurism:

“There have been instances where it has happened. Some of the NBFCs have diverted. It hasn’t happened in a large scale. That is not the case. In some cases, we have noticed this has happened. A large number have encountered business failures, encountered external factors, which has impacted business models. We are coming up with a new regulatory framework. We are a work in progress. Risk management guidelines are also there for NBFCs. Now HFCs are coming under RBI, we are constantly reviewing it internally. The RBI’s endeavor is a well functioning NBFC sector and a robust regulatory framework which prevent the kind of situation we have encountered in the past year.”

On the U.S.-China trade war and what it means for India:

“India is not part of the global value chain. So, U.S.-China trade tension does not impact India as much as several other economies which are part of the global value chain. Second thing is about trade tensions, it has a lowering of global growth and contraction of demand and that would in a way have a role on oil prices. Oil prices should remain low. These are the positives. In the long run, we cannot ignore lingering and prolonged tensions. It will definitely affect countries all over the world and definitely India, which is the sixth-largest economy. In the medium term also it will affect India. If it lingers, a contraction of global demand will have impact on our exports sector. We have large exports to Europe.”

On RBI policy options:

“We have to only see our domestic demand continues to be robust and ensure that there is a domestic demand revival and that remains strong. We have to ensure that these opportunities arising out of the trade war, relocation of investment, India should utilize it. Irrespective of the trade war, India should become competitive both in the services and the manufacturing sector.”

On the risk of dollar depreciation:

“If they depreciate their currencies, it means greater inflows. When the reversal happens we have to manage spillover effect. If excess inflow comes in, it becomes a problem to absorb excess liquidity. It’s an evolving challenge. We will continue to deal with it. We have to keep in mind, in several advanced economies, bonds yields are negative, inflation is zero. In fact in my interaction with other central bankers, they are concerned about zero or low inflation. They would like to have a slightly higher inflation. Zero interest rates prevailing for far too long, it becomes unsustainable and undermines investor sentiment. In the overall context, India is much better than most other economies.”

On structural reforms:

“I don’t think the fiscal space is really the answer. If you have fiscal space any government can use. Long-term growth can be sustained by structural reforms, enhancing competitiveness, and focusing on an enabling business environment. So therefore, GST, IBC and the Niti Aayog’s committee on agriculture reforms, which will allow private investment in the farm sector and which will ensure better price to farmers for their produce, are crucial. The supply chain in the agricultural sector has to be addressed. The focus will have to be on structural reforms and improving competitiveness. Focus will have to be on continued ease of business and availability of credit at a reasonable price.”

On improving growth prospects:

The RBI’s “essential role is to maintain price stability, which is defined in terms of inflation. Along with the objective of growth. Price stability is prime. It will depend on inflation, on incoming GDP. This year we have projected 7%. There was a lot of uncertainty, but now the monsoon is catching up in Tamil Nadu and Kerala. The western part had good rains and the monsoon outlook has improved compared to what it looked about three weeks ago and oil prices are remaining in the $65 range, but then you have extraneous factors like the trade tensions, sanctions on Iran, and then you have Brexit which creates uncertain sentiments and India has a lot presence in Britain in terms of investment and exports. I would not like to specify how long it (economic slowdown) will last. India is today in a far better place than most of the major economies and India has certain inherent resilience and the signs are looking good.”

On core inflation:

“Core inflation coming down, at one level, can be seen as a positive development but at another level it is reflective of a slowdown in the demand, so therefore I don’t want to make a qualitative judgement on good or bad. Based on hard numbers, we will have to take a call.”

On global bond issuance:

“RBI is the debt manager. There is a process of consulting between RBI and the government.”

On recapitalization funds:

“The 700 billion rupees is adequate for capital requirement but also for growth. The true test of efficiency of a public sector bank is whether they are able to access capital markets to raise additional capital. Otherwise just continuous and prolonged dependence on government capital infusion — it can breed inefficiency. Banks need to access capital markets. There has to be competition in the banking sector. How many competitors are there in the field that the market will decide.”

On interest-rate transmission:

“There is a case for banks to show better monetary policy transmission. We have to keep in mind that banks have gone through a period of crisis and they are just recovering, they are just about recovering, so that aspect has also to be kept in mind. So if you drive and ask them to fix interest rates administratively, we cannot lose sight of the fact that banks will also have to recover and comeback to a level where they are out of the woods. If we see the PCA banks have fulfilled the conditions to come, they will come.”

On payments banks:

“Some are doing well. It’s a new model. It’s about two years. We are studying. We should wait a little longer how they play out.”

On financial stability:

“I would like to say our primary focus — apart from price stability and keeping the objective of growth — it is also to ensure the stability of the financial sector, which includes banks and NBFC. And in the long run, if India has to grow and show improved growth rates, it will need a well-functioning financial sector.”