(1935 - 2010)
प्लैटिनम् जयंती
PLATINUM JUBILEE

प्रेस प्रकाशनी PRESS RELEASE

भारतीय रिज़र्व बैंक
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August 03, 2009

Reserve Bank of India releases Winter 2008 Issue of its Occasional Papers

The Reserve Bank of India today released the winter 2008 issue of its Reserve Bank of India Occasional Papers. This is a research journal of the Reserve Bank and contains contributions of the Bank's staff and reflects the views of the authors. It contains articles, special notes and book reviews on issues ranging from the relevance of government deficit for stabilisation, banking penetration for financial inclusion, imported inflation and its implications and efficiency in auction of Government securities, which are some of the important areas of policy concerns.

The first paper titled 'Is the Government Deficit in India Still Relevant for Stabilisation?' by Jeevan K. Khundrakpam and Rajan Goyal revisits the causal relationships between government deficit and money, and the latter with real output and prices in India for the period 1951-52 to 2006-07 by employing the ARDL approach to cointegration analysis. The paper finds evidence of government deficit leading to reserve money creation with consequent increase in money supply. This could take place through government deficit leading to incomplete sterilisation of net foreign assets (NFA) accumulation with the intention to enable adequate market subscription to Government borrowings, replacing the erstwhile channel of net RBI credit to the Government. The paper finds that while price is caused by money and real output both in the short as well as in the long-run, money is neutral to output. The paper concludes that government deficit continues to remain relevant for stabilisation since it leads to money creation which in turn has inflationary implications.

In the second paper 'Auctions of Government Securities in India – An Analysis' by Ravi Shankar and Sanjoy Bose, the various performance parameters associated with auctions of Government of India dated securities are evaluated in view of the increasing importance of auction methodology and its practical use in a market oriented mechanism from 1990s onwards. The paper observes that G-Sec auctions in India are fairly efficient as bidding dispersion is quite low with normality in pricing behaviour. The bidding behaviour analysis of Indian government securities auctions shows that bidders' pricing strategy is negatively influenced by bid size, bid cover ratio and tenor of the security. To minimize the 'winners-curse' in the auctions, bidders are reducing their bid amount for higher priced bids. The statistical analysis in the paper also validates various standard auction features and also establishes that the auctions help in determining most commonly perceived market-clearing borrowing rates out of well behaved bid-price distributions.

Under the section on Special Notes, a paper 'Imported Inflation: the Evidence from India' by Janak Raj, Sarat Dhal and Rajeev Jain analyses the sources and commodity-wise trends in imported inflation in India during the last four decades. At the global level, the paper finds that export of inflation from oil exporting countries is significantly higher than that of industrial and non-oil developing countries, and among the latter two the export of inflation from the former is higher. The paper finds that domestic inflation in India is positively influenced by import price, capital flows and exchange rate. The paper indicates the need to strengthen absorptive capacity of capital flows in the domestic economy in future through efficient allocation of capital, which otherwise could have some stabilizing impact on domestic inflation through exchange rate appreciation and resultant reduced import prices, and may lead to asset bubbles and overheating of the economy. Lack of the absorptive capacity raises doubts not only regarding the potential gains to the domestic economy from the globalization but also the overall institutional and policy environment of the country.

The second paper in this section, titled 'Bank Penetration and SHG-Bank Linkage Programme: A Critique' by Pankaj Kumar and Ramesh Golait examines the outreach of SHG-Bank Linkage Programme (SBLP) in the backdrop of growing banking and socio-economic divide between regions in India. The paper finds that nationalisation of major commercial banks and the remarkable spread of the banking system to the unbanked and under-banked rural areas that followed has not reduced the dependence on informal sources of credit in rural areas. The distribution of SBLP, which was conceived to fill the existing gap in the formal financial network and extending the outreach of banking to the poor, is skewed against the poorer Eastern and Central Regions of the country. The paper provide several suggestions including: the need for encouraging banks to become facilitators in extending the SHG movement in the poorer regions by introducing performance-linked incentive; creation of specific funds to address the regional imbalances in the SBLP; formation of SHGs around activities of rural infrastructure such as construction and renovation of minor irrigation tanks, feeder channels, rural roads, etc., which can generate significant external economies for agricultural yields and overall rural development; and efforts to embed livelihood activities, micro-insurance and grain banks in the SHG model.

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