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RESERVE BANK OF INDIA

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Monthly Bulletin for May 2020

The Reserve Bank of India today released the [May 2020](#) issue of its monthly Bulletin. The Bulletin includes [RBI Governor's interview](#), two Articles and Current Statistics.

The two articles are: [I. Inflation Decoded Through Power of Words](#); [II. Determinants of Loan Loss Provisions: The Case of Indian Banks](#)

I. Inflation Decoded Through Power of Words

Media, as an important channel for dissemination of information, has the potential to influence public sentiment and expectations. The article explores constructing alternative indicators that could be useful to assess the state of the economy. Using high frequency unstructured information sourced from media reports and applying Big Data techniques, the article constructs a sentiment index in the context of retail inflation in India, and empirically examines their inter-linkages.

Highlights:

- Sentiment has been extracted from the unstructured news text of media reports using Support Vector Machines (SVM) classifier, deploying appropriate feature selection method.
- Timing of the arrival of news is taken into consideration in order to explore possible differences in sentiments on inflation.
- Empirical analysis suggests that the sentiment index tracks inflation very well, and its directional accuracy, is high and statistically significant.
- Causality analysis indicates that the media sentiment index may have significant explanatory power for predicting inflation.

II. Determinants of Loan Loss Provisions: The Case of Indian Banks

The global financial crisis (GFC) has drawn attention to the pro-cyclicality in banks' operations. In the aftermath of the GFC, there has been a renewed interest in the accounting practices followed by banks. One such area is the loan loss provisions, the amount which banks set aside to offset future loan losses.

Highlights:

- The study finds empirical evidence of pro-cyclicality in loan loss provisioning by Indian banks as well as existence of income smoothing via loan loss provisioning.

- Provisioning by public sector banks was found to be more pro-cyclical as compared to private sector banks.
- Recognising this cyclical pattern, an efficient loan loss provision management entails that banks should build up loan loss reserves during good times, to provide a cushion when the economy is experiencing a cyclical downturn.
- Implementation of Indian Accounting Standards (Ind-AS), which requires banks to make provisions for expected credit losses from the time a loan is originated, rather than awaiting 'trigger events' signaling imminent losses is expected to help address the pro-cyclicality issue to some extent.

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