Edited Transcript of Reserve Bank of India's Post Policy Conference Call with Media

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PARTICIPANTS FROM RBI:

DR. RAGHURAM G. RAJAN – GOVERNOR
SHRI HARUN R. KHAN – DEPUTY GOVERNOR
DR. URJIT R. PATEL – DEPUTY GOVERNOR
SHRI R. GANDHI – DEPUTY GOVERNOR
SHRI S.S. MUNDRA – DEPUTY GOVERNOR

MODERATOR:

MS. ALPANA KILLAWALA – PRINCIPAL ADVISER, COMMUNICATIONS

Moderator: Ladies and Gentlemen, Good Day, and Welcome to the First Bi-Monthly Monetary Policy Governor's Teleconference with Media. As a reminder, all participant lines will be in the listen-only mode and there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call, please signal an operator by pressing '*' then '0' on your touchtone phone. Please note that this conference is being recorded. Ladies and Gentlemen, with this I now hand the conference over to Alpana Killawala. Thank you and over to you Ma'am.

Alpana Killawala: Good morning to all of you and welcome to the post-policy conference. Governor will make a short statement and then we take questions.

Dr. Raghuram G. Rajan: Good Morning. After reviewing the economic outlook and prospects, the Reserve Bank of India cut the policy rate by a further 25 basis points; this means we have cut interest rates by total of 150 basis points since the beginning of the accommodative cycle. Our attention in the recent months has turned to seeing that this large quantum of rate cuts is passed through into borrowing rates. The introduction of the Marginal Cost Lending Rate (MCLR) since April 1st will help. Our first estimate from the 26 largest banks in the system accounting for about 83% of activity has been that since the last week of March, the median overnight MCLR is down by 50 basis points from the base rate and is down by 25 basis points across all tenors. This is important because it means an actual rate cut to the borrower of a further 25 to 50 basis points at least even before today's rate cut. Put differently, policy action is significantly greater today than just another 25 basis points cut. Borrowing is now significantly cheaper and will continue to get so.

To further this process, a major focus of this policy has been to address liquidity issues. After a detailed review and internal discussions, we brought in significant refinement to our framework including clearer differentiation between the durable liquidity needs of the system and short-term liquidity needs; indicated an intent to move closer to neutral on overall durable liquidity needs; reduce the MSF rate by 75 basis points and increase the rate at which banks can deposit at the RBI by 25 basis points so as to narrow the interest rate corridor; and reduce the minimum daily maintenance of CRR to 90%. All these measures along with the government's actions on small savings rates should also help continue the process of transmission. In addition to further durable liquidity provision, we have announced an open market operation- a purchase of Government securities of Rs.15,000 crore today.

The monetary policy stance remains accommodative. Going forward we will be looking for further monetary room in signs of good monsoon, further readings of low headline inflation, indications of softening in core inflation and further evidence of transmission of rate cuts.

Part-B of this policy statement also has a number of reform measures including continuing opening up of the banking sector, new market instruments such as money market futures, broadening participation in and easing access to markets such as allowing retail customers ability to trade GSECs and to undertake foreign exchange rates and strengthening financial inclusion through measures such as improving the business correspondent network.

Moreover, in the weeks to come you will see a fulfillment of our past announcements including the release of guidelines for on-tap licensing of universal banks, the start of the trading platform for priority sector lending certificates and the introduction of mobile-to-mobile transfers through the universal payment interface by NPCI.

Finally, the process of cleaning up bank balance sheets is well underway and I am happy with the progress made thus far. My colleagues and I will now take questions.

Supriya Shrinate:
ET Now

I must ask you the first question on liquidity boosting measures. A lot of people believe that you are moving through your interest rate to do your bit for boosting growth and there is a change in stance from the RBI. The RBI has always all these years talked about maintaining liquidity deficit. Is this a conscious effort to change the stance of all these years? And how worried are you about the Pay Panel Recommendations because you are talking about 100-150 basis points impact eventually when this goes through.

Dr. Raghuram G. Rajan: On the first issue which is the 'liquidity measures' a lot of our activity on the monetary policy front is driven by the Urjit Patel Committee Report which laid out both a change in the monetary framework as well as a change in how we deal with liquidity. Now, given the various measures that have been taken to fix the policy rate at close to repo rate through these overnight instruments, the need to maintain the system in liquidity deficit no longer is there. Therefore on a review of how far we had come with these overnight instruments, we decided that it was no longer necessary to maintain the significant liquidity deficit, we could move towards a more neutral position, which is what was announced today. On the issue of the 100 to 150 basis points, Urjit, would you like to comment on that?

Dr. Urjit R. Patel: The number in the Monetary Policy Review of 100 to 150 basis points direct impact of the 7th Pay Commission on the headline inflation is of course a projection and an estimate and a mechanical exercise essentially on account of the adjustments in the HRA that will take place eventually at both the central government level and at the state government level. We will refine those projections as more details emerge. The thing to notice is that most likely the impact of the 7th Pay Commission on the headline inflation will be considerably less than in the previous Pay Commission and I think even from the 5th Pay Commission, because there are going to be no arrears. Therefore the overall impact could be most likely much less than on account of the previous Pay Commissions, but that number is essentially on account of changes in HRA and given the weight of housing in the CPI combined. It is noteworthy that in previous additions the impact was felt on the CPI industrial workers where the weight of housing was larger; it was 15.3% and now it is about 10%. So that is the background to that projection which may undergo change as we get more information on both the rollout and the timing.

Lata Venkatesh:
CNBC TV18

How quickly do you expect the system to get through with the planning for near neutrality? Also when you say near neutrality would it be habitually a minor deficit or would it be minor deficit minor substance? Therefore, would it be okay if call rate on certain days is below the repo rate? What would be the habitual behaviour of the RBI? What is the corridor? Also 150 basis points is not factored into your 5% inflation on January 2017. Is it factored into the MPR 4.2% inflation in January 2018? It is not. So if it is factored in, you are looking at a very different number. Then what happens to your word "accommodation"? How much of the 150 could be durable?

Dr. Raghuram G. Rajan: First on your question on 'liquidity', the truth is that the durable liquidity status of the economy will not affect how close the day-to-day call money rate is to the policy rate. That is determined by a short term measure, that will continue to be determined by a short term measure and we hope to hug the policy rate as far as possible, with the call money rate to hug the policy rate. Whether we go into a little bit of surplus, little bit of deficit - I think that now is actually immaterial. Point is that we are moving towards that. The period over which we move depends to some extent on market conditions, depends on the flows that come in, remember, net foreign assets is part of the liquidity move. So we have to work it out; we have to see how this move takes place. All it means an additional, moving from 1% deficit to about neutral means an additional removal of deficit by about Rs.80,000 to Rs.90,000 crore. So we have to see how much this system can take, that is something we have to figure out.

Latha Venkatesh: How much time will it take? We have no clue how is it going to work. Your deficit has been 1.5 lakh. You may argue it is not enduring or endurable it but the reality is for the banks who have been seeing this.

Dr. Raghuram G. Rajan: There are a couple of new, shall we say, 'sources of deficit' that we have to look at and see how permanent they are. One is government balances have increased on average over the year and second is most recently cash with the public has increased quite a bit, we have to figure out. It is about Rs.50,000 to 60,000 crore in excess from what we were estimating, we have to see how this plays out. So it would be I think premature to give you a sense of how long it will take us.

Latha Venkatesh: A ballpark.

Dr. Raghuram G. Rajan: Again, we are not talking quarters, we are talking a year or two. The question is whether it is a year or two years by which time we get into neutrality.

Dr. Urjit R Patel: The 150 basis points, it is correct that neither the March '17 number nor the March '18 number, and the MPR makes it very clear does not include the impact of the Pay Commission to that. To what extent this is durable? We have given an estimate of the indirect effects which are about 40 basis points. What is mechanical and just an index adjustment most likely we would look through. What is impermanent and causes externality for rest of the CPI, we will have to imbibe that in our projections. We have not done that exercise yet, in part, because there is a fair bit of uncertainty on how this is going to evolve.

Dr. Raghuram G. Rajan: First, the government has come out with what actually it is going to implement and when. Second, as DG said, it depends on what the second round effects are. If the second round effects are small, we can look through a level shift because it will return to the older levels later. If the second round effects are thought to be larger, we will have to take action. By the way on the 'liquidity move' there is a liquidity move anyway because we have to increase durable liquidity on a regular basis. So we will be injecting durable liquidity anyway. The question is not only do we have to make that up but we also have to make up the liquidity deficit. So how long we will take to make up that liquidity deficit, the additional margin, is the response I was giving to you.

Pradeep Pandya: CNBC Awaaz and CNBC Bazaar

First question the on the cut that you have made in MSF instead of CRR, or instead of doing a deep cut in repo rate and giving leeway in CRR which most people were expecting. So is it going to be that much effective or more effective according to you? How do you think that it will help because banks are not borrowing much of money from the MSF? So what you were expecting from government how much has been fulfilled? Secondly what you have said about public holding more cash according to the figures which you have seen. So what reason do you see behind it, do you see increasing black money like the Panama Papers have revealed. Are you pursuing that? In what context are you seeing this?

Dr. Raghuram G. Rajan: So on the first question "Has the rate cut been enough?" we think it is what is sensible given the uncertainties surrounding the economy right now. But I think what was important to focus on is what I started with, that because of the MCLR we actually already have a rate cut of 25 basis points to 50 basis points before the policy, and as this winds its way through, the MCLR, over the next few months, we will have more of a rate cut. So do not look at it as 25 basis points, look at the composite of measures they all add up and borrowing rates are coming down significantly in this economy. The effects of the liquidity measures will also help transmission because banks have continuously been saying it is because of liquidity tightness that we cannot transmit. Now we have given them enough liquidity, they have the ability to transmit even more. So my hope is we will see significantly more transmission in the next few months and we have to be careful therefore that we are doing what is appropriate given the state of the economy. On the 'reasons for excess cash' we are trying to understand it. Around election time cash with the public does increase, you can guess as to reasons why, we also guess. And you see some not just in the state which is going for elections but also neighboring states. So there is something there, we need to understand it better, but it is about 50,000 to 60,000 crores more than we anticipated at this time of year.

On Panama, we are obviously part of the investigative team that is going to look into these matters. It is important to note that there are legitimate reasons also to have accounts outside, the LRS scheme allows you to take money out, and we have to see what is legitimate and what is not legitimate. That is a process of investigation that will take place.

Aparna:
Mint

In the Urjit Patel Committee report there is a Phase-I and Phase-II of liquidity framework. Have we moved to the Phase-II or will we be moving towards Phase-II very quickly, do you look at the 14-day repo now? And the second question is on the banking side. In schemes like SDR, so banks invoke SDR and take over a company, but then they look for resolutions outside the SDR. Doesn't this violate the spirit of the scheme?

Dr. Raghuram G. Rajan: So let me start with the second question SDR itself that we have been reviewing the SDR and we offered some revised suggestions to the banks. What is important is that they take over a company when they think that genuinely management change can make a difference. But then when you take over there is no point leaving control in the hands of the original guys while you are looking for a buyer because that puts the company at risk during that period. So we have asked the banks to take action as soon as they invoke the SDR rather than wait and some other measures that have been suggested by a review of the SDR mechanism. We are seeing more buyers come in to the system but a full-fledged operation of an SDR I think we are yet to see. So as and when that happens we will look at that and seek more lessons from this process.

Dr. Urjit R Patel: On the issue of Phase-II, we are still in Phase-I to give you a direct answer. The changes that we have brought in today is a move towards creating the enabling conditions to move to Phase-II where the 14-day repo becomes the operating target.

Bijoy:
Cogencis When you had joined at that time the corridor was broad and at that time I had asked you about the corridor of uncertainty and now that you moved the corridor again to 100 and then again there is uncertainty and now we don't know whether the corridor can move again. So for the market itself using the corridor is a concern because the corridor itself was fixed earlier. Also on the liquidity side on the cash credit system you were internally reviewing and looking at, any update on that?

Dr. Raghuram G. Rajan: We are still looking at this cash credit system. We have to be conscious of the fact that you do not want too many changes in the system at the same time because the system has to adjust gradually. It is tied to our concern also about large exposures in the system which we are going to bring down. What I mean by that is large concentration of bank loans to particular groups and so on, that has to come down over time. There is no uncertainty about liquidity today. Today, it is going to be 100 basis points corridor. If tomorrow it narrows, it narrows. This does not affect any bank decision. I know that the corridor is 100 basis points rather than being 200 earlier. So I am not sure this creates any uncertainty whatsoever.

Bijoy: Why was it narrowed?

Dr. Raghuram G. Rajan: Simply because we felt that over time since our marksmanship is getting much better we can live with a narrower corridor and rather than I think impose significant cost on the banking system as they find they have excess liquidity they have got a deposit at 100 basis points less or they need liquidity desperately they got to borrow at 100 basis points more, this impact makes it cheaper to make mistakes, we do not want them to make mistakes, we would like them to improve their liquidity management which is why we have not brought down the CRR daily rate to what they wanted, but more to what we think is appropriate. But at the same time we want them to see the system as friendlier and pass on the rate cuts that have happened. So this is part of that process.

Shobhana:
Financial Express Is there a growth estimate for FY17?

Dr. Urjit R Patel: 7.6 per cent.

Shobhana: Is that under threat, with the monsoon?

Dr. Raghuram G. Rajan: No, I think it was reiterated. So obviously there are risks around that growth estimate. If the monsoon is not good, I hope not. But if it is not, then obviously that will imply some reduction.

Shobhana: And will the RBI encourage a rollover of the FCNR(B) deposits that mature in September?

Dr. Raghuram G. Rajan: There is no new scheme that is intended. So if they want to roll it over they will. Our estimate is that that scheme came with a lot of leverage; that banks were offering loans to people who invested in that scheme and we anticipate that will not be renewed because we are not going to offer the same favorable terms again. So we are actually estimating a fairly low roll over rate on the FCNR. The good news is we are fully prepared for whatever exit takes place and we will monitor market conditions. We think at this point that we do not anticipate volatility, but if there is, we will deal with it.

Govardhan:
Economic Times There is a para on this purchase of foreign assets. You have talked about ensuring durable liquidity through alternate purchases of domestic as well as foreign assets. Can you explain how that would operate?

Dr. Raghuram G. Rajan: So what we will do is estimate over the next 12-months how much durable liquidity we want to infuse into the economy. In other words, how much reserve money creation we want. Then regardless of short term liquidity conditions such as government balances, etc., we will infuse that amount of durable liquidity. So we are separating durable liquidity infusion from temporary liquidity infusion. So divide the 12-month target by 12 and that is how much we aim to infuse every month. Now that could come in two ways - either we buy foreign exchange assets because there are a lot of flows and we want to reduce volatility in the exchange rate or we buy domestic assets. Typically, what happens is we have less choice about when the foreign assets come in and so the residual becomes the domestic assets. So we will do both, sometimes we will do one. If lots of foreign assets are coming in we may even sell domestic assets to make room for the foreign assets consistent with our target growth rate of durable assets.

Govardhan: You said the liquidity shortage would get close to zero over one to two years. At the same time you mentioned banks will have more liquidity because of your measures, but they don't add up. Does that mean fall in borrowing costs would be just a trickle and over a period?

Dr. Raghuram G. Rajan: No. So one is maintaining the deficit at 1%, we would supply that incremental which is needed even to maintain, see balance sheet has to grow even to maintain the deficit at 1%. So that will supply anyway, that take for granted, we will do it on a monthly basis, could be through OMOs, could be through foreign asset purchases. Over and above that, we will try and narrow the gap by doing a little more than that. Lata asked me "How much time will you take to do that?" We will see, but we will do more than is needed on a monthly basis to get the gap closer to zero.

By the way, all of you are getting a very good education in Central Bank balance sheet. It is not something that most people understand, but this liquidity measure requires you to understand that very keenly.

Himadri:
Bloomberg TV

My question is on transmission. Your read-through of the MCLR that have been announced, transmission still is elusive and deposit growth has been the lowest over the last few decades. Is that a concern?

Dr. Raghuram G. Rajan: 25 to 50 basis points on the MCLR I think is significant. Now, we will obviously look at it, we are having our people look at it to see the formulas have been adhered to. But it is a significant change from the base rate that was in operation. Remember, this is money that people can actually go out and borrow at. So I think that is positive. On your second question, deposit growth is certainly lower than credit growth; now that is good news that the credit growth is picking up. One of the things you have to be careful about is all these things are measured at the old rates of inflation and given that inflation has come down, 15-16% increase in deposit growth rates is probably not something that you could anticipate. In the last quarter there have however been some developments which have sucked out deposits. For example, the issuance of tax free bonds, the rush to get into the small savings before those rates expire and the new rates come in. And remember the new rates are still reasonably attractive and therefore we need a continuation of this process to make them consistent with deposit rates. So my sense is this will take a little bit of time before deposit start coming back up. But I think that even with 9-9.5% growth it is nothing to be sneezed at, it is reasonable growth.

Amol:
Zee Business Sir my question is on the target you have kept to clean up the bad accounts or bad loans for FY17. As you have said you are happy with the progress which banks are making. A big issue is of Kingfisher and CBI is doing a lot of investigation. Have any of these organizations

contacted RBI specifically about these accounts because a lot of agencies are working on this. And second is paragraph no.26 where you have written about enhancing credit supply through market mechanism for the large exposure. So what is the definition of large exposure and what about the small exposure?

Dr. Raghuram G. Rajan: Let me ask about the large exposure to Mr. Gandhi. I do not want to take specific names into account, but there is cooperation amongst the investigative agencies and the RBI. It is important that this kind of investigation not be done through the press. I think when people release letters that they have issued here and there and so on, I think it does tend to create an environment which is not conducive to investigation. What we must look at in all these situations is what were the conditions under those circumstances? Were the loans given by the banks in the spirit given the information that was known then and being careful about hindsight being 20-20. I will give you an example, today, we know certain sectors in the economy are weak, but there is always a statement that they will strengthen, it is a temporary weakness. Now, if banks give loans under these circumstances, if there is some forbearance that takes place, it does not immediately imply that there was venality, there was corruption that this is a bad action. So one has to be very careful if three years from now these sectors turn out to be even worse or tend to have collapsed, the action that was taken to support the sector at that time should not be seen with the 20-20 hindsight that comes. You have to look to see whether reasonable precautions were taken, whether reasonable judgments were made that what a prudent man would do under those circumstances. So again and again both the finance minister and I have said that it is important that we investigate to see the mistakes as well as criminal activity that may have taken place, but do it based on judgments that would have had to be made at that time and do not use today's thinking and today's information to guess at that. Otherwise you will chill bank lending and you will make sure that we really do not get any risk taking in this economy by entrepreneurs or by the bankers, we need both in order to get economic growth. So that care has to be taken.

Shri R. Gandhi: Large exposure is always measured in terms of the bank's specification basically with reference to its capital. So in the discussion paper you can find more detail. It has standard principles which have evolved under the Basel, it should be related to the Tier-I capital. So it is depending upon bank's own capital, the exposure to a particular party or a group of parties.

Amol: But it will be specifically for the large exposure?

Shri R. Gandhi: Yes, this particular framework is meant for dealing with large exposure. So obviously there will be cut off beyond which we only it will affect.

Sandrine: Bloomberg My question is on the cyber theft which took place in Bangladesh. Will the RBI take any measure for this on its cyber security? And the second is on rural inflation which is quite high, what is stimulus for inflation in rural India?

Dr. Raghuram G. Rajan: First on 'cyber security', it is an important risk, it is a risk that I think across the world we still understand too little. And there are various ways of getting through cyber defenses including through people rather than through processes or through the networks. So we have to take action on all these issues. What happened in Bangladesh is certainly a source of concern for all of us and we have taken some measures and are continuing to understand better what actually happens so that we can further our measures. I should mention that we have identified now a leader for our cyber security subsidiary and we will now start recruiting people into it and the idea is that this would serve both the RBI as well as the system to improve the quality of cyber security and the strength of cyber security. On 'rural inflation' we have to remember that we have had two very severe droughts and in fact rural wages are still quite moderate. So that would suggest that rural inflation, even though it is higher than urban inflation, that is more because of perhaps some bottlenecks and some constraints in inflows and in logistics than because the rural areas are really very buoyant. In fact, rural demand is still quite weak. So as of now the fear that it might take off significantly is still relatively muted, and, of course, abundant production of food through a good monsoon would help quell any inflation.

Virendra Singh: Aaj Tak and India Today Sir on Panama you have said that a lot of agencies are already working on it. So I want to know what immediate action RBI is going to take because 500 Indians are there and you have said that we have to examine that how many are legitimate and not legitimate. So what will be further action? And second question is on Kingfisher, Enforcement Directorate has taken the statement of the former CMD of IDBI and they have come to know that the due diligence by IDBI Bank was not followed, there was some carelessness. They have found out that when banks have to do loan restructuring then they have to take permission from RBI, so in that also due diligence has not been done properly. I want to know your perspective on this. And the last one is regarding the list of the defaulters you have given to Supreme Court in a sealed cover. Why don't you want that all the names should be published and the country should know? What is the benefit and loss of that?

Dr. Raghuram G. Rajan: So let me start with Kingfisher. I will ask Khan saab to talk about Panama. First important thing to remember is the regulator does not make a loan. The regulator offers principles on when a loan will be termed a bad loan, an NPA or when forbearance could be exercised, it could be considered a performing loan. So the regulator does not actually make a loan. When the regulator decides whether a loan is deserving a forbearance he does it based on whether he thinks the industry or the sector will broadly recover and therefore the forbearance can be exercised. Now, I have to say that since 2015 we have ended all forbearance. That is why the AQR etc. But at a time when the economy was getting into trouble, the RBI decided to exercise forbearance based on request from a variety of parties including the banks and the government. The important thing was to judge how much forbearance was required in each circumstance for particular industries. Typically the forbearance, was obviously, based on certain signal cases, but was given broadly on principles that the RBI had agreed to. So in the Kingfisher case as well as elsewhere, it was based on estimates of whether the industry would recover or not, just like today for certain metal industries you hear people saying this is a temporary downturn, they will get back, please exercise forbearance. I get a letter a day from people saying this. Similarly, at that time there were letters from the airline industry as well as from the bankers saying, if we hand hold for a little while longer, this will get better. So whatever forbearance and in no circumstance was entire forbearance given or all the requests acceded to. There was forbearance given to some extent in 2010 and whatever investigative agencies will look at that. But I think it is important to put that in the context in which these things take place. Today, the government is helping the steel industry and is working to ensure the steel industry gets back on track. Similarly, the regulator under certain circumstances when an industry is distressed may believe a certain amount of respite might get the industry back on track because converting loans into NPA may in fact chill lending. That is sort of the judgment call that has to be taken at that time.

On the defaulters list, let me ask you. In this room, sometimes you default in a credit card bill. Would you like that credit card default to be put up in public? Many of you bank with public sector banks. Would you like that regardless, you just forgot, it is not that you are trying to make this thing. If every time you defaulted it was put up in public for everybody, your neighbors, your friends, relatives to see and no reason was given, it was just put up that you are a defaulter, you might have some concerns, right. Similarly, what we are saying is the act of default happens in business. Sometimes it is not your own fault. In fact, again I get a letter a day saying it is not our fault, demand is weak, prices are low, there is dumping going on by foreign countries, government permissions did not come through, Supreme Court ruling took away some of these assets because they said 'null and void this allocation.' Variety of reasons why a project gets into trouble. To then put the promoter up for all to see that this person defaulted without details of why they defaulted. And the details sometimes are hard for a lay person to understand because they are intricate details. Are you going to go into the business of every promoter to understand why they defaulted? So we have no problem if the intent is to publish wilful defaulter list. That is where the promoter has in the eyes of the bank taken the bank for granted. The bank has gone through a legitimate process to declare the promoter a wilful defaulter. That can be made public. In fact, some courts have prevented the banks from making those lists public. If there is a judgment along those lines we have no problem. But we believe that simply any act of default without understanding, via understanding severity, etc., if it just put out for public to consume, it make create both loss of business as well as undue anxiety and panic and therefore chill business activity. And after all if you are a promoter why would you take any risk if at the slightest chance of default, your name is put up in public for shame. I do not think we want that kind of move. That was our plea to the Supreme Court that "Please, keep this confidential." There are elements that can be disclosed but let us not disclose everything.

Shri Harun R. Khan: As Governor had earlier said, in the case of Panama Papers, a high level committee has been set up in which CBDT, FIU and ED are there, and on behalf of the Reserve Bank highest attention is been given. So in that investigation we too will help. As you must have read that the SIT which is already working on black money that too is keeping an eye on it. In this as Governor has said earlier there are two three points to note. First is that many people who have invested outside, opened accounts out of the country, under FEMA many things are permitted, many things are not permitted and many things are in grey area. All these things will be investigated and will be seen how much is legitimate and how much is not legitimate. So as it gets investigated we will come to know.

Alpana Killawala: Thank you very much for attending the conference. Thank you very much, Governor.

Dr. Raghuram G. Rajan: Thank you.

Moderator: Participants, with this we conclude today's conference call. Thank you for joining us. You may now disconnect your lines.