NOT LETTING INFLATION GUARD DOWN

The RBI gave a robust GDP growth outlook for FY25 at 7% while expecting the inflation to align with the target only in the second quarter. It is also focusing on boosting digital payments after its recent action on Paytm Payments Bank

LIQUIDITY MANAGEMENT

Stance in terms of interest rates, transmission incomplete: Das

ANJALI KUMARI
Mumbai, 8 February

Reserve Bank of India (RBI) Governor Shaktikanta Das on Thursday said the monetary policy stance — "withdrawal of accommodation" — was in terms of interest rates, and it should be seen in the context of incomplete transmission, along with the inflation rate staying above 4 per cent.

"Our stance of withdrawal of accommodation should be seen in the context of ... our efforts to bring it back to the target on a durable basis," said Das in his monetary policy statement.

Das elaborated on liquidity conditions, ascribing them to external factors, and they were expected to rectify in the foreseeable future, bolstered by market interventions by the central bank.

The RBI, he said, is agile and adaptable in its liquidity management, employing both repo and reverse repo operations. He said the RBI would utilise a judicious mix of instruments to regulate both short-term and long-term liquidity, ensuring that money market interest rates evolved systematically while upholding financial stability.

The RBI is agile and adaptable in its liquidity management, employing both repo and reverse repo operations, the RBI Governor said

"On liquidity, Das has preferred to communicate the RBI's nimbleness to act to address both frictional and durable liquidity rather than disrupt monetary policy coordinates, thereby delinking liquidity from stance," said Aurodeep Nandi, India economist, Nomura.

Das had clarified the RBI would try to keep liquidity at a level wherein the overnight call rate, the operating target of the monetary policy, remained around the repo rate.

"On liquidity, the central bank seemed to suggest that liquidity deficits were broadly frictional and durable liquidity remained more comfortable. It did not announce any new measures and said that it would continue to manage liquidity through its fine-tuning operations including tools like the variable rate repo and reverse repo auctions," said Abheek Barua, chief economist, HDFC Bank.

The market was expecting a shift in the monetary policy committee's stance, citing continuous variable rate auctions, administered by the RBI. Ahead of the MPC's decision, market participants speculated the continuous infusion of liquidity by the RBI might prompt a transition from the current stance of "withdrawal of accommodation" to "neutral".

"The RBI's balanced stance on liquidity augurs well for the economy. It's prudent not to let go of the gains made on inflation; therefore any overhang of surplus needs to be avoided. The inflation projection of 4.5 per cent next year may be conservative and we may see some change in stance after Q2 next year. The RBI will consider easing liquidity first and then will resort to cutting rates if required," said Alok Singh, group head (treasury), CSB Bank.

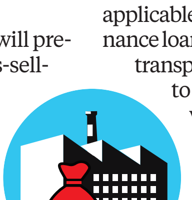
ENHANCING TRANSPARENCY

Key fact statement must for retail, MSME loans

ABHIJIT LELE
Mumbai, 8 February

The Reserve Bank of India's (RBI's) decision to mandate all regulated entities to provide the key fact statement (KFS) to borrowers for all retail and micro, small and medium enterprise (MSME) loans will enhance transparency and financial literacy.

Bankers also expect that it will prevent potential instances of mis-selling and predatory pricing.



In its statement on Developmental and Regulatory Policies, the RBI highlighted that currently, the KFS is specifically mandated for loans by scheduled commercial banks to individual borrowers, digital lending by regulated entities, and microfinance loans.

Providing critical information about the terms of the loan agreement, including the all-inclusive interest cost, will significantly benefit borrowers in making informed decisions. The RBI issued this statement alongside the Monetary Policy Review on Thursday. Dinesh Kumar Khara, chairman of State Bank of India (SBI), said that having a KFS for retail and MSME advances will empower customers to make informed decisions. Atul Kumar Goel, chairman of the Indian Banks' Association and managing director (MD) and chief executive officer of Punjab National Bank, seconded the SBI chairman's view, mentioning that it could help customers understand the total cost of loans and make informed decisions. This disclosure, already applicable to digital loans and microfinance loans of non-banks, will improve transparency and enable borrowers to make informed decisions when seeking a loan. The mandate will be particularly relevant for shorter-tenure loans with relatively higher upfront processing fees but competitive interest rates, according to Ajit Velonie, senior director at CRISIL Ratings.

H P Singh, chairman and MD of Satin Creditcare Network, highlighted that this initiative will enable borrowers to be more prudent while taking loans. It will help lenders perform due diligence on customers more effectively and understand their needs better. This will bolster financial literacy by familiarising borrowers with key loan and financial terms, thereby raising financial awareness and aiding prudent decision-making.

STREAMLINING TRANSACTIONS

New rules for verification of digital payments on cards

AATHIRA VARIER
Mumbai, 8 February

The Reserve Bank of India (RBI) on Thursday proposed to adopt a principle-based framework for authentication of digital payment transactions to promote alternative mechanisms other than the popular SMS-based One Time Passwords.

Speaking during the monetary policy statement address, RBI Governor Shaktikanta Das said although the central bank had not specified any particular Additional Factor of Authentication (AFA) mechanism, SMS-based OTP has become very popular.

However, in recent years, with technological advancements, alternative authentication mechanisms have emerged and in order to aid in their adoption, RBI has proposed to constitute a principle-based framework for the same, he said. "Therefore, to facilitate adoption of alternative authentication mechanisms for enhancing the security of digital payments, it is proposed to put in place a principle-based framework for authentication of such transactions," Das said. The RBI suggested streamlining the "onboard process" of Aadhaar Enabled Payment System (AePS) service providers and called for introduction of additional fraud risk management measures that will strengthen the security of the system while enhancing its robustness.

According to RBI, in 2023, more than 37 crore users undertook AePS transactions, highlighting the importance played by the segment in financial inclusion. "To enhance the security of AePS transactions, it is proposed to streamline the onboard process, including mandatory due diligence, for AePS touchpoint operators, to be followed by banks. Additional fraud risk management requirements will be considered,"

RBI said in a statement. The banking regulator said that the instructions regarding AePS will be issued shortly. Both these measures are expected to help in controlling the frauds in the system.

"The new framework for digital payment authentication together with more stringent due diligence requirements for Aadhar Enabled Payment Systems will help curtail fraud risk," said Zarin Daruwala, Cluster CEO, India and South Asia markets (Bangladesh, Nepal and Sri Lanka), Standard Chartered Bank.

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'Have to be vigilant about incoming data and outlook'

RBI Governor Shaktikanta Das (*centre*) with Deputy Governors Swaminathan Janakiraman (*extreme left*), Michael Debabrata Patra, M Rajeshwar Rao, and T Rabi Shankar at the RBI headquarters in Mumbai on Thursday PHOTO: PTI

Reserve Bank of India (RBI) Governor **SHAKTIKANTA DAS**, along with Deputy Governors **MICHAEL DEBABRATA PATRA**, **SWAMINATHAN JANAKIRAMAN**, **T RABI SANKAR**, and **M RAJESHWAR RAO**, responds to a range of issues during a post-policy media interaction. Edited excerpts:

RBI Governor Shaktikanta Das' initial remarks highlight 9 points

1. Domestic economic activity continues to be strong. We expect real gross domestic product (GDP) growth of 7 per cent in 2024-25.
2. Consumer Price Index (CPI) inflation is moderating with intermittent interruptions and spikes. We have to remain vigilant about the incoming data and the outlook. Our endeavour to achieve 4 per cent inflation on a durable basis has to continue.
3. Global markets are front-running central banks in anticipation of policy pivots. But central banks remain apprehensive and await a more durable alignment of inflation with the targets.
4. Liquidity will be actively managed by the RBI.
5. Our multi-pronged, proactive, calibrated policies have worked well to maintain and strengthen financial stability.
6. Systemic, sectoral, and institution-specific signs of stress are being proactively monitored and acted upon wherever necessary.
7. Good governance, robust risk management, sound compliance culture, and protection of customers' interests are the hallmarks of RBI's approach to the safety and stability of the financial system and individual financial institutions. Regulated entities must accord the highest priorities to these aspects.
8. The external sector of the economy remains resilient. The current account deficit is expected to be eminently manageable.
9. The exchange rate of the rupee has remained stable.

You mentioned that the transmission of 250 basis points (bps) is continuing. Bankers say that deposit rates have already gone up by 200-250 bps, and lending rates have also gone up. What, in your mind, is the actual transmission that has not happened, and how much is that? What is the benchmark you are looking at to conclude that transmission has happened?

Swaminathan J: The rates on the deposit side reset quickly, and they are passed on even quicker, as we have seen that deposit rates have almost played out. On the lending side, rates take much more time to pass for two critical reasons in our assessment. One is that the proportions of loans that are benchmarked externally, which we call EBLR (external benchmark lending rate) loans, are still less than 50 per cent. In the case of other benchmarks like MCLR (marginal cost of funds based lending rate) base rates or fixed-rate loans, they take time to transmit. Banks' anxiety about maintaining their market share in the incremental credit also adjusts their margins, not to lose their market share in the incremental credit, which also impedes a complete transmission in terms of effective interest rate.

Next year's growth is projected at 7%, while nominal GDP by the government is projected at 10.5 per cent. Effectively, that means inflation will be 3.5 per cent next year. Are you being too optimistic about growth, or the government is being modest in its projection?

Michael Patra: My understanding of this is that what goes into nominal GDP is not CPI inflation, it's the GDP deflator, and it is always a weighted combination of CPI and Wholesale Price Index (WPI). Now WPI has been in deflation for most of this year, and it is just emerging out of deflation, so that must be the reason.

Q&A

Was RBI late in acting against Paytm Payments Bank? Why did RBI not consider appointing a director on the board of Paytm when it found out about the compliance issue?

Shaktikanta Das: We give sufficient time to every regulated entity that is supervised by the RBI to comply with the regulatory requirements. If everything had been compliant, why should we act? RBI is a responsible institution.

Swaminathan J: We make our assessment of the scale and proportion of the issue. A one-size-fits-all kind of solution may not work in such a situation.

You said your stance is with respect to the rates, and there is incomplete transmission. Are you making elbow room for liquidity operations, so that open market operation purchases won't be seen out of sync with the stance?

Shaktikanta Das: What we have attempted to do is to clarify and state that, do not read the stance of the monetary policy in terms of excess liquidity prevailing or deficit liquidity prevailing.

Liquidity plays a secondary role in supporting monetary policy transmission. We try to keep the liquidity at a level wherein the overnight call rate, the operating target of the monetary policy, remains around the repo rate.

Banks and markets take time to adjust to the evolving liquidity situation. So far as RBI is concerned, we will remain active, we will remain nimble in our liquidity management, and what instrument we will utilise will depend on the prevailing situation.

COMMENT