Publication: Economic Times

Page no: 11	Date: April 07, 2017

Guest Column

RBI Has Moved to Reduce the Stress on Banks' Books

AJAY SRINIVASAN

The monetary policy committee on Thursday, in line with its neutral stance, chose to stay on hold as far as the repo rate is concerned, but narrowed the policy corridor by 50bps. The status quo on rates was widely expected. The undertone of the policy, which surprised market participants in the last meeting, was different this time.

Several factors highlighted as risks in the last policy seem to have waned, be it crude oil prices, dollar strength or concerns around core inflation. On the contrary, INR strengthening, a dovish Fed hike, under check domestic food and moderating core inflation emerging were mentioned in this policy.

The key problem that is absorbing attention for some time now is regarding the stressed bank balance sheets. The NPA levels in India are high relative to the comparable EM pack and that has inhibited banks' ability to extend credit, which has reached multi-year lows of about 3.3% growth in Feb'17, with credit to industry contracting and off late even mortgage loan growth slowing. With this in mind, the RBI has revised the Prompt corrective action for banks and also raised the minimum level of net owned funds in the asset reconstruction company.

There is some concern also around liquidity management measures. The system has been flush with liquidity and a large part of it doesn't look temporary. Both net deposit accretion (post demonetisation) and the recent large capital inflows have created a problem of plenty for the RBI. With a neutral stance around rates, allowing more money into the system and then sterilizing the inflows would have sent contradictory signals to the market. As a fall out of this, INR has appreciated 4.3% CYTD. We witnessed about $11 b of inflows in Q4FY17 and with international markets re-evaluating dollar strength, flows into India and EMs are likely to persist. To deal with this, market participants were awaiting more clarity on the standing deposit facility (SDF). RBI chose to mention other measures from its toolkit such as CMBs, MSS, longer tenor reverse repo auctions and if need be then also OMOs. Added to this, the narrowing of the corridor in effect means reverse repo rate has been raised by 25bps (and MSF rate cut by 25bps) and this would reset the interest rates along the curve marginally higher.

On domestic fundamentals, while acknowledging the loss of momentum in industrial and services sector in terms of growth (basis the latest GVA release by the CSO for FY18), the RBI expects growth to recover facilitated by increased remonetisation and improved external demand. We are witnessing modest improvement in a lot of high frequency indicators, but that still is largely consumption demand centric, while investment growth continues to remain a laggard. Addressing this would require a solution to stressed bank balance sheets. An interesting move was allowing banks to participate in REITs and INvITs. This can improve availability of funds to the RE and infra space.

ANIRBAN BORA

On inflation, the RBI continues to be watchful despite a sizable 150bps undershooting of its target. The concerns regarding food inflation seem to be under check courtesy the buffer stocks, INR appreciation will keep any exchange rate pass through led higher inflation at bay and flattish crude and other commodity prices will also help keep overall inflation under check. Apart from this, there has been a secular moderation in core CPI inflation as well. As incoming data reinforces this, RBI would probably take cognizance of this in its monetary policy stance.

With the view to encourage less cash usage and improve user experience, RBI announced 11 additional settlement batches for NEFT starting 8:30am, taking the number of half hourly settlement batches during the day to 23. This will add to user convenience and improve our payments system.

(Author is chief executive-financial services, Aditya Birla Group)